Basics of Revenue and Expenditure Forecasting

Presented by:
Christopher J. Ketchen
Town Manager
Town of Lenox... in the Berkshires!
Major themes:

- Forecasting is about seeing the “big picture” (i.e. developing strategy, as opposed to tactics)

- Fiscal turbulence impacts all communities (large/small; wealthy/not-so-wealthy)

- Incremental vs. multi-year approach (structural deficits, managing expectations)
Why is structural balance so elusive?

- Uncontrollable costs
- Constraints of Proposition 2½
- Variable state aid
- Lack of financial planning
The traditional approach to budgeting:

- Focused only on *next* year
- Line items in budget are changed incrementally year-after-year
- Often results in level service, level funded, or funding cuts
The case against the traditional approach

• Revenue and expenditures: no consideration for ongoing relationship

• This year’s surplus – or balanced budget – can very quickly spiral into next year’s deficit
Multi-year budget planning

• Addresses future shortfalls (structural deficit) identified through forecasting

• Focuses on departments/programs (not line items)

• Calculates approximate funding for planned service levels
Why forecast?

• To manage expectations and gain consensus around assumptions

• To help enhance fiscal stability/enable corrective action

• To quantify financial impact of policy decisions
Key points to understand about forecasting before you start...

• In the beginning, forecasts almost always involve deficits

• Multi-year forecasts help identify trends

• Integrating timing of capital spending is crucial
The anatomy of a forecast...

- The revenue side
- The expenditure side (and, don’t forget about capital!)
- Plan for monitoring/adjustments
The revenue side: taxes, state aid and local receipts

- Develop revenue inventory
- Analyze impact of rate changes or changes in economic conditions
- Craft reasonable assumptions for out-years
The revenue side (continued): use of available funds

- (Ordinarily) avoid using one-time revenue for ongoing expenses

- What are one-time revenues?
  - Stabilization: yes
  - Overlay Surplus: yes
  - Free Cash: depends
The expenditure side: personnel

• Quantify year-over-year salary obligations
  – Use contractual agreements for relevant employees
  – Make assumptions on non-contract employees
  – Estimate ongoing program/staffing needs
The expenditure side (continued): expenses and capital

- Estimate non-salary departmental expenses

- Make realistic assumptions on healthcare, other benefits and shared costs (some historical data available through DLS)

- Insert estimated costs of capital plan
“Forecasting” and “planning” are not the same thing

- Forecasting is an ongoing part of planning
- For planning purposes, simply projecting revenue and expenses for multiple years is insufficient
- Deficits are an inevitable part of your forecast, but they should not be part of your financial plan
Lenox FY2016 Budget Priorities

• Maintain Core Services
• Tax Impact below 1.5%
• Maintain reserves between 7%-13% of budget
• Emphasis on capital
• Succession Planning
  – Loss of institutional knowledge is expensive
  – Take advantage of opportunities to partner with others
Financial Reserves (FY10 – FY16*)

- **Stabilization Fund**
- **GF Free Cash**

<table>
<thead>
<tr>
<th>Year</th>
<th>Stabilization Fund</th>
<th>GF Free Cash</th>
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<tbody>
<tr>
<td>FY10</td>
<td>$2,452,007</td>
<td>$354,521</td>
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<tr>
<td>FY11</td>
<td>$1,735,871</td>
<td>$359,072</td>
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<tr>
<td>FY12</td>
<td>$1,995,140</td>
<td>$361,238</td>
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<tr>
<td>FY13</td>
<td>$2,836,744</td>
<td>$362,658</td>
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<tr>
<td>FY14</td>
<td>$3,096,154</td>
<td>$363,578</td>
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<tr>
<td>FY15</td>
<td>$3,000,000</td>
<td>$514,834</td>
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<tr>
<td>FY16*</td>
<td>$664,578</td>
<td>$3,000,000</td>
</tr>
</tbody>
</table>

**Green Line** = 10% of Total Budget
**Shaded Area** = 7-13% Range
Pay-as-you-go (PAYG) Capital Plan
FY13-FY20
<table>
<thead>
<tr>
<th>TAX LEVY DASHBOARD</th>
<th>CERTIFIED (FY2015)</th>
<th>ESTIMATED (FY2016)</th>
<th>PROJECTED (FY2017)</th>
<th>PROJECTED (FY2018)</th>
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</thead>
<tbody>
<tr>
<td>MAXIMUM ALLOWABLE LEVY</td>
<td>14,671,371</td>
<td>15,215,003</td>
<td>15,745,282</td>
<td>16,670,718</td>
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<tr>
<td>ACTUAL TAX LEVY</td>
<td>14,275,612</td>
<td>14,487,916</td>
<td>14,799,318</td>
<td>15,671,494</td>
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<td>EXCESS CAPACITY</td>
<td>395,758</td>
<td>727,087</td>
<td>945,964</td>
<td>999,224</td>
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<tr>
<td>PERCENTAGE CHANGE</td>
<td>1.87%</td>
<td>1.49%</td>
<td>2.15%</td>
<td>5.89%</td>
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</tbody>
</table>
Wellesley’s “Planning Maxims”

(From Hans Larsen’s “Best Practices: Financial Planning” in City & Town, August 2008)

1. Focus on environmental changes; set priorities based on level of financial risk
2. Gain buy-in for your strategy
3. Simplify
4. Create a dashboard
5. Emphasize the need for accountability
Helpful resources:

- MMA and other organizations (ICMA, GFOA, etc.)
- Department of Revenue – Division of Local Services
- Your professional staff
Questions?

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