



Knowing What You Can Spend

The Importance of Multi-Year Financial Forecasting in Cities and Towns

Presented by:

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What I hope you learn...

- How to get help with forecasting through the Division of Local Services
- The need to manage expectations in an environment of “structural deficits”
- The implications of which approach you take toward budgeting



What is “structural balance/deficit”

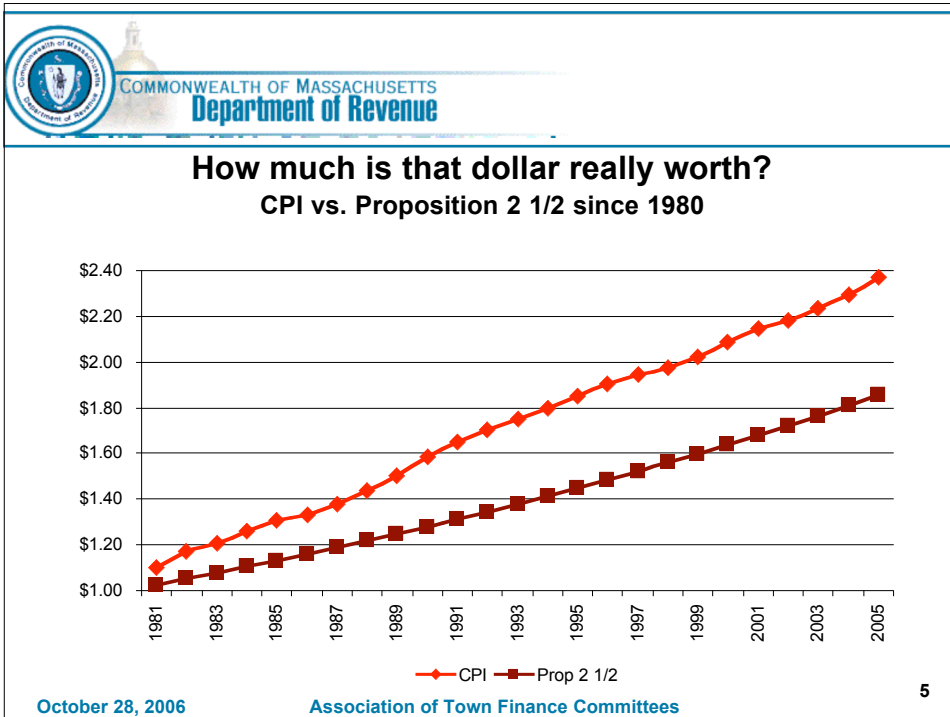
Structural balance – program cost growth equals revenue growth

Structural deficit – Currently in balance but recurring revenues do not cover recurring expenses



Why is structural balance so elusive?

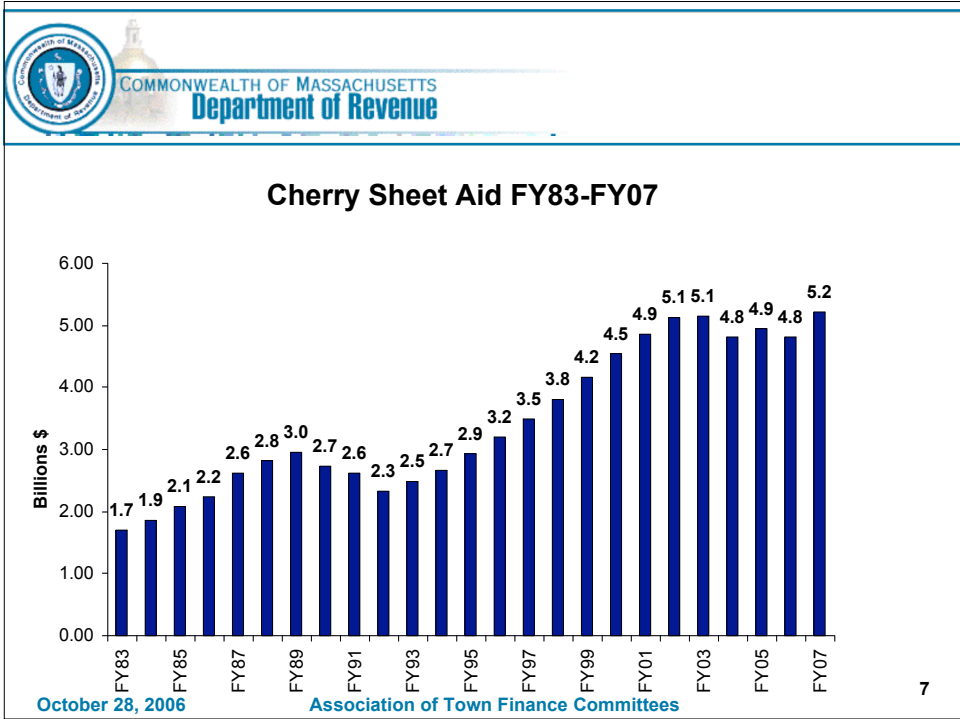
- Environment created by Prop 2_ works against structural balance
- The Commonwealth has worked both toward and against structural balance
- Cities/towns have worked against structural balance (often without even knowing it)



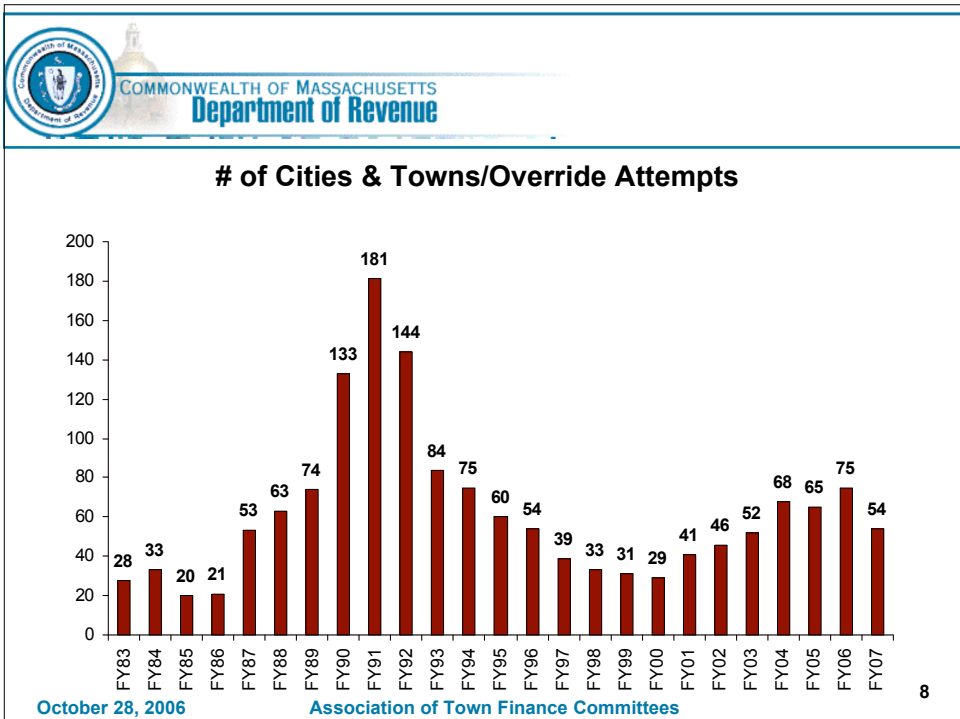
State aid and structural balance

- Increases in State aid that outpace cost increases can help balance the budget
- Level funding/cuts can lead to deficits

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Sometimes communities work against structural balance

- By not understanding financial impact of future events
- By not considering full future costs of expenses
- By spending one-time funds for on-going costs



Budgeting:

Traditional approach

vs

Forecasting approach



Traditional approach to budgeting

- Balanced only for one 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

- Income & Expenses: No consideration for on-going relationship
- This year's surplus can very quickly spiral into next year's deficit



Forecasting approach to budgeting

- Identifies future shortfalls (structural deficit)
- Focus on departments/programs
- Calculates approximate funding for planned service levels



Why forecast?

- To manage expectations
- To enhance fiscal stability/enable corrective action
- To quantify financial impact of policy decisions



What you need to understand first...

- In the beginning, projections almost always involve deficits
- Multi-year projections are the only way to identify trends
- Integrating timing of capital spending is crucial



Critical considerations in forecasting

- Consensus around assumptions
- Identifying trends vs spikes/depressions
- Creating realistic expectations



The revenue side

- Develop revenue inventory
- Analyze impact of rate changes or changes in economic conditions
- Craft reasonable assumptions for out-years



The expenditure side

- Quantify year-over-year salary obligations
 - Easy for contract employees (just read the contract)
 - Make assumptions on non-contract employees
 - Estimate ongoing program/staffing needs



The expenditure side (continued)

- Estimate non-salary departmental expenses
- Make reasonable assumptions on healthcare, other benefits and shared costs
- Insert costs of capital plan estimates



*Our new Revenue and Expenditure
Forecasting Tool is here to help:*

<http://www.dls.state.ma.us>

click on “Financial Management Assistance”