



Where is that crystal ball?

The basics of revenue and expenditure forecasting

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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, and why it matters)



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?

- Uncontrollable costs
- Constraints of Proposition 2½
- Variable state aid
- Lack of financial planning



The 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

- Revenue and expenditures: no consideration for on-going 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 are the only way to 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: it depends – let's discuss...



Where does free cash come from?

START WITH: Undesignated/Unreserved Fund Balance

MINUS: Accounts Receivable

PLUS: Credit balance in Deferred Revenue

MINUS: Debit balances in other funds

MINUS: Overspent appropriations

MINUS: Prepaid Items

MINUS: Amounts appropriated from free cash

PLUS: 60 day collections from date of mailing, net refunds, if tax bills issued after May 1st

PLUS: Late Payments



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In other words...

- **START WITH:** Last year's free cash
- **MINUS:** Appropriations from free cash
- **PLUS:** Excess revenue (or minus for deficit)
- **PLUS:** Budget turn-backs
(or minus overspending X2)



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 reasonable assumptions on healthcare, other benefits and shared costs (some historical data available through DLS)
- Insert estimated costs of capital plan



How quarterly projections tie into multiyear planning...

- Quarterly projections help to identify financial opportunities (same process as multi-year planning on a smaller scale, giving you the best possible data)
- Quarterly projections are not the same thing as year-to-date budget reports



“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



Wellesley's "Planning Maxims"

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