

# Multi-year Budgeting: A Primer for Finance Officers

*This article presents the concept of multi-year budgeting and its benefits and drawbacks. The authors also discuss findings from a recent GFOA survey on how multi-year budgeting is practiced among local governments.*

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Over the past several years, the GFOA Research Center has received a considerable number of inquiries from state and local governments regarding multi-year budgeting (MYB). Inquiries have focused on the following questions: 1) What is MYB? 2) What are its advantages and disadvantages vis-a-vis annual budgeting?, and 3) Which jurisdictions have adopted it? In addition to these inquiries, GFOA's continuing work to disseminate newly established recommended budget practices issued by the National Advisory Council on State and Local Budgeting also has led to a resurgence of interest in ways to embed a long-term perspective to budgetary decision making. This article describes the different approaches to MYB and presents results from a recent survey on this subject.

## The MYB Concept

For purposes of this article, multi-year budgeting refers to both a process and a document. The document outlines appropriations (i.e., anticipated expenditures) and anticipated revenue for two or more consecutive budget years. Multi-year budgets exist in many forms, such as a biennial budget, a three-year budget, or a five-year budget. A multi-year budget also may consist of a biennial budget with one or more financial plans serving as tentative spending plans for the next biennial budget.

The most common types of multi-year budgets used by local governments are biennial budgets. Historically, local governments have implemented one of three types of biennial budgets: an annual budget with a financial plan, a rolling

biennial budget, or a classic/traditional biennial budget which are defined as follows.

1) Biennial Financial Plan refers to a government's spending document consisting of an annual budget with an appended financial plan that serves as a tentative spending plan for the following year. Under this budget method, the

annual budget is formally adopted and sets the spending authority for the government, while the financial plan is not enforceable and can be changed in the subsequent year.

2) "Classic" (or Traditional) Biennial Budget refers to a government's spending document consisting of appropriations and anticipated revenues for two

## NACSLB RECOMMENDED BUDGET PRACTICES

Multi-year budgeting is consistent with the recently issued National Advisory Council on State and Local Budget (NACSLB) Recommended Budget Practices. Multi-year budgeting requires governments to take a long-term perspective when making decisions to undertake new initiatives and fund existing programs and services over multiple years. In so doing, the multi-year budget process lends itself to meeting numerous NACSLB recommended practices (RP), such as the following.

- **Identify Broad Goals:** A government should identify broad goals based on its assessment of the community it serves and its operating environment (RP 3.1);
- **Develop Programs and Evaluate Delivery Mechanisms:** A government should develop programs and services that are consistent with policies and plans and should evaluate alternative delivery mechanisms (RP 6.1);
- **Develop Budget Guidelines and Instructions:** A government should prepare general policy guidelines and budget preparation instructions for each budget cycle (RP 8.2);
- **Develop Mechanisms for Coordinating Budget Preparation and Review:** A government should develop mechanisms and assign responsibilities to provide for overall coordination of the preparation and review of the budget (RP 8.3);
- **Develop Procedures to Facilitate Budget Review, Discussion, Modification, and Adoption:** A government should develop and implement a set of procedures that facilitate the review, discussion, modification, and adoption of a proposed budget (RP 8.4);
- **Conduct Long-range Financial Planning:** A government should have a financial planning process that assesses the long-term financial implications of current and proposed policies, programs, and assumptions and that develops appropriate strategies to achieve its goals (RP 9.1);
- **Prepare Revenue Projections:** A government should prepare multi-year projections of revenues and other resources (RP 9.2);
- **Prepare Expenditure Projections:** A government should prepare multi-year projections of expenditures for each fund and for existing and proposed new programs (RP 9.4); and,
- **Monitor, Measure, and Evaluate Program Performance:** A government should periodically evaluate the performance of the programs and services it provides (RP 11.1).

A complete set of the NACSLB's Recommended Practices is available in the council's 1998 publication *Recommended Budget Practices: A Framework for Improved State and Local Government Budgeting*, available from the Government Finance Officers Association in Chicago, Illinois (\$10). Call GFOA at 312/977-9700 to order.

**Exhibit 1  
TYPES OF BIENNIAL BUDGETS AND UNDERLYING ASSUMPTIONS**

<b>Biennial Budget Type</b>	<b>Budget Characteristics</b>	<b>Expenditure Assumptions</b>	<b>Revenue Assumptions</b>
<b>Biennial Financial Plan</b>	<ul style="list-style-type: none"> <li>• A separate document is created each year</li> <li>• Annual adoption of the budget document</li> <li>• One-year appropriation (i.e., annual budget) with a second year serving as a tentative spending plan</li> </ul>	<ul style="list-style-type: none"> <li>• Difficult to control because of unclear organizational and departmental goals, objectives, and priorities</li> <li>• Expenditures increase at a different rate annually</li> </ul>	<ul style="list-style-type: none"> <li>• Actual to projected revenue variance is large</li> <li>• Revenue fluctuates erratically from year to year</li> <li>• Revenue is difficult to predict over a two-year time horizon</li> <li>• Unstable economic conditions</li> </ul>
<b>Rolling Biennial Budget</b>	<ul style="list-style-type: none"> <li>• A single two-year spending document with two one-year appropriations with each year being formally adopted annually</li> <li>• Budget adjustment process between years one and two</li> <li>• Long-term time horizon</li> </ul>	<ul style="list-style-type: none"> <li>• Expenditures are fairly easy to control because of clear organizational and departmental goals, objectives, and priorities</li> <li>• Expenditures are fairly predictable from year to year</li> <li>• Expenditures increase incrementally from year to year</li> </ul>	<ul style="list-style-type: none"> <li>• Actual to projected revenue variance to small</li> <li>• Reasonably stable economic conditions</li> <li>• Revenue is fairly stable from year to year</li> <li>• Revenue is predicatble over a two-year time horizon</li> </ul>
<b>“Classic” (Traditional) Biennial Budget</b>	<ul style="list-style-type: none"> <li>• A 24-month budget with appropriations allocated for two separate years, with each year’s appropriations being adopted at the same time</li> <li>• Budget adjustment process between years one and two</li> <li>• Long-term time horizon</li> </ul>	<ul style="list-style-type: none"> <li>• Expenditures are predictable from year to year</li> <li>• Expenditures increase incrementally from year to year</li> <li>• Expenditures are easy to control because of clear organizational and departmental goals, objectives, and priorities</li> </ul>	<ul style="list-style-type: none"> <li>• Actual to projected revenue variance is small</li> <li>• Revenue is stable from year to year</li> <li>• Stable economic conditions</li> </ul>

consecutive years where both budget year appropriations are adopted at the same time.

3) Rolling Biennial Budget refers to a government’s spending document consisting of appropriations and anticipated revenues for two consecutive years where each budget year appropriations are adopted separately (i.e., the first budget year appropriations are formally adopted in the first year and the second budget year appropriations are adopted in the following year).

**Biennial Budget Characteristics and Assumptions.** Exhibit 1 provides a brief description of the characteristics and underlying expenditure and revenue assumptions of biennial budgets. As Exhibit 1 illustrates, each type of biennial budget is based on different expenditure and revenue assumptions. Based on these budgetary assumptions, governments desiring to change from an annual budget to a multi-year budget should examine their expenditures and structures thoroughly to determine whether it is feasible to implement a multi-year budget. Put differently, multi-year budgets have a

greater probability of success when expenditures are easily controlled and revenue sources produce consistent yields from year to year.

**Benefits of MYB**

Governments abandon annual budgeting for MYB based on the rationale that 1) they will improve their long-term planning and priority setting process, 2) better manage financial resources, and 3) reduce budget staff time dedicated to developing an operating budget. With respect to biennial budgeting, the National Conference of State Legislatures (NCSL) observes that some biennial budgeting is probably more conducive to long-term planning, program review, and evaluation vis-a-vis annual budgeting because more time is available.

According to the current literature on MYB, governments with multi-year budgets have found that their budgets have several advantages over annual budgets. Those advantages include the following.

- **Improve Long-range and Strategic**

**Planning.** Because policymakers and department personnel have to allocate financial resources and forecast revenues for multiple years at one time, they consider resource and program planning for a longer time horizon than their counterparts with annual budget appropriations.

- **Produce a More Policy-oriented Budget Process.** The multi-year budgeting process allows policymakers and department personnel to move away from a detailed, line-item approach and focus instead on programmatic policies, goals and objectives vis-a-vis micromanaging financial resources.
- **Reduce Reliance on Short-term Grants and/or One-time Revenue Sources.** Because grants and revenue sources are viewed within a multi-year budgeting framework, finance and program officers have the opportunity to seek alternative funding to replace expiring grants and one-time revenue sources.
- **Reduce Staff Hours Dedicated to the Budget Process.** Although developing a multi-year budget requires an increase of budget staff time dedicated to formulating the document during the first year,

the second year reduces staff effort. During the second year, the budget staff dedicates its time to making minor budget adjustments and revisions. In essence, the cost of producing a budget document is reduced by producing a spending plan that spans two or more years.

• **Strengthen Performance Evaluation.**

Because less staff time is dedicated to budget development, the budget staff can reallocate its efforts and time to monitoring the accomplishment of programmatic goals and objectives. Additional staff time also can be allocated to capital improvement programming and/or policy development.

### Drawbacks of MYB

Although MYB has its advantages over annual budgeting, multi-year budgeting has some potential drawback, such as the following.

- **Lack of Flexibility.** Depending on the type of multi-year budget implemented, the budgeting process may be less responsive to drastic economic, political, and programmatic changes.
- **Potential for Increased Workload.** Again, depending on the type of multi-year budget in place, the budget staff may experience an increase in workload during the development and review stages of the multi-year budget. This is particularly true for the first year of the budget when the budget staff needs to coordinate their efforts with other departments to develop the budget document.
- **Significantly Increased Initial Workload Stress.** During the transition phase from an annual budget to a multi-year budget, the governmentwide budget staff most likely will experience an increase in workload stress as it implements budget process changes and gathers a vast amount of budget data to produce the budget document.
- **Software Limitations.** Because of the data requirements of multi-year budgeting, some financial software may need to be replaced or modified. This is particularly the case for smaller governments that have financial software that cannot accommodate multi-year budgeting.
- **Uncertainty.** When local economic conditions become unstable, producing a multi-year may become more difficult, increasing the level of uncertainty.

Additionally, when the local economy is in flux, forecasting revenues for a longer time horizon becomes more tenuous. The advent of increased government expenditures also increases the level of uncertainty across governmental departments.

Although addressing each of these drawbacks is beyond the scope of this article, multi-year budgets can establish policies to mitigate these potential drawbacks, such as developing the multi-year budget during odd years to avoid elections, establishing policies to restrict the type of budget adjustments made during the review phase, and using reserves to deal with unexpected expenditures.

### MYB Survey

In July 1999, the GFOA Research Center developed a multi-year budgeting survey consisting of 15 questions. Because of its contract with governments that participate in the GFOA Distinguished Budget Presentation Awards Program, GFOA only mailed surveys to 49 governments with award winning multi-year budgets. A follow-up mailing was sent in September 1999 to those governments that did not respond to the initial mailing. GFOA obtained an overall response rate of 61 percent.

The main objective of the survey was to answer the following research questions.

- What are the major advantages and disadvantages of multi-year budgeting?
- What type of multi-year budget was implemented by the government?
- Who initiated the change to multi-year budgeting?
- Why did the governments convert from annual budgeting to multi-year budgeting?

This section summarizes some of the general findings of the GFOA survey, and provides answers to the research questions identified above.

**Type of Multi-year Budget Implemented.** The survey results show an even distribution of local governments with financial plans, rolling budgets, and a “classic” biennial budget. Specifically, 34 percent of the respondents indicated their government had an annual budget with the second year serving as a financial plan. Similarly, 34 percent indicated they had a rolling biennial budget, while 31 percent reported using a “classical” biennial budget.

#### Implementation of Multi-year Budgets.

When asked to identify the individual (or individuals) responsible for initiating the change from an annual budget to a multi-year budget, 41 percent of the respondents indicated that the chief executive officer was responsible for the change (Exhibit 2). Another 10 percent indicated that the finance director initiated the change. Similarly, 10 percent said that the budget director was responsible for adopting the multi-year budget. In 13 percent of the cases, the respondents indicated that the change to a multi-year budget was initiated by the chief executive officer in conjunction with the budget director, chief financial officer, or finance director.

**Reasons for Adoption of Multi-year Budgets.** Exhibit 3 summarizes the reasons for adopting a multi-year budget. Based on the survey, 86 percent of the respondents indicated that their multi-year budget was adopted to enable departments to take a long-term view in decision making. Additionally, 86 percent indicated that their government also adopted multi-year budgeting to improve the linkage between their long-term priorities and the budget process. Eighty-three percent of respondents also stated that reducing staff hours dedicated to budget development was another reason for abandoning their annual budget. Finally, 45 percent said multi-year budgeting was adopted to improve the linkage between the operating and capital budgets.

To examine whether governments had multiple reasons for adopting a multi-year budget across the types of biennial budgets adopted by the local governments, a cross-table was created. Exhibit 4 summarizes the reasons for adopting multi-year budgeting by type of multi-year budget adopted.

**Long-term View.** Among local governments with multi-year financial plans, 90 percent of the respondents indicated that multi-year budgeting was implemented to enable departments to take a long-term view in their decision making process. Similarly, 80 percent of the respondents with rolling biennial budgets indicated the same reason for implementing a multi-year budget. Eighty-nine percent of the respondents with a “classic” biennial budget also indicated that enabling departments to have a long-term view in their decision making process was a reason for instituting multi-year budgeting.

**Improve the Linkage between the Operating and Capital Budgets.** According to the results, 50 percent of the respondents

**Exhibit 2  
GOVERNMENT OFFICIAL RESPONSIBLE FOR  
ADOPTING THE MULTI-YEAR BUDGET**

Who in your jurisdiction initiated the transition from an annual budget to a multi-year budget?

Response	Frequency	Percent
1. Chief Executive Officer (CEO)	12	41%
2. County Commissioners	1	3%
3. Chief Finance Officer (CFO)	2	7%
4. Finance Director	3	10%
5. Budget Director	3	10%
6. CEO and Budget director	1	3%
7. CEO and CFO	1	3%
8. CEO and Finance Director	2	7%
9. Chief Administrative Officer (CAO) and Budget Director	1	3%
10. CAO and CFO	1	3%
11. CFO and Finance Director	1	3%
(No Answer)	(1)	(3%)
<b>Total</b>	<b>29</b>	<b>100%</b>

with multi-year financial plans indicated that they had implemented multi-year budgeting to improve the linkage between their operating and capital budgets (Exhibit 4). Similar results were obtained from respondents with a rolling biennial budget. Among governments with a “classic” biennial budget, improving the linkage between the operating and capital budgets was less of an issue.

**Improve the Linkage between Priorities and the Budget Process.** Based on the survey results, improving the linkage between long-term priorities and the budgeting process was an important issue for all governments (Exhibit 4). Ninety percent of the respondents with multi-year financial plans indicated that improving the linkage between long-term priorities and the budget process was another reason for implementing multi-year budgeting. Similar results were obtained for governments with rolling biennial budgets and “classic” biennial budgets.

**Reduce Staff Time.** Finally, Exhibit 4 shows that reducing staff hours dedicated to budget development was important for all governments, but was more important for governments implementing a “classic” biennial budget. Specifically, all of the respondents from governments with a “classic” biennial budget indicated that reducing staff hours dedicated to budget development was a reason for implementing a multi-year budget. In contrast, 70 percent of the respondents with multi-year financial plans and 80 percent of those with rolling biennial budgets responded similarly.

**Unanticipated Consequences of MYB.**

When asked if they had experienced any unanticipated consequences after implementing MYB, 82 percent of the respondents reported experiencing no unanticipated budgeting or financial policy issues. However, five governments indicated experiencing unanticipated consequences, such as needing to coordinate the budget cycle with city council’s term in office, addressing personnel needs in light of uncertain revenue levels, and coordinating leasing arrangements with the budget period. Difficulty determining what to include in a budget given the need to adopt an annual budget under local budget law, and dealing with uncertainty over whether a state ballot initiative would impact the budget also were mentioned.

**Advantages of MYB**

Anecdotal evidence states that multi-year budgeting offers several advantages over annual budgeting. The survey results of the GFOA survey are consistent with the current literature on multi-year budgeting. The respondents cited decreased staff time allocated to budget development, depoliticization of the budget process, and improved long-term planning as advantages of multi-year budgeting.

**Reduction of Staff Dedicated to Budget Development.** Seventy percent of the respondents stated that savings in staff time was a major advantage of multi-year budgeting. One respondent indicated that due to the tremendous savings in time, multi-year budgeting allowed “staff to take on other special projects as well as

time to review program activity.” Similarly, another budget director indicated that a two-year budget allowed time to undertake other major projects in off budget years.

**Long-term Planning.** Long-term planning was listed as another major advantage by 61 percent of the respondents. One budget director stated that its multi-year budget process forces city council to take a long-term view of the operating budget and mitigates decisions that satisfy only immediate needs. Another respondent echoed this sentiment by stating that multi-year budgeting expands the timeframe in which to react to changing conditions and mandates.

**Depoliticization of the Budget Process.** Other advantages mentioned by the respondents was the depoliticization of the budget and elected officials’ focus on major budget issues rather than on line item detail. One respondent indicated that city councils focus on major budget issues in year two, not on line item detail. Another budget director said that they adopt the budget during off election years to reduce the politicization of budget development.

**Disadvantages of MYB**

Despite the advantages of multi-year budgeting, some governments noted some disadvantages. Commonly cited drawbacks to multi-year budgeting include difficulties forecasting revenue, difficulties converting from an annual budget to a multi-year budget, and increased staff time during the first year of the multi-year budget. Although these are commonly cited drawbacks to multi-year budgeting, not all governments with multi-year budgets experience these difficulties.

**Revenue Forecasting.** A major disadvantage, listed by 34 percent of respondents, was the difficulty in projecting revenues and changing conditions for the second year. One budget director explained that the major disadvantage of multi-year budgeting is not knowing how revenue fluctuations of certain revenue sources will impact the budget. Another budget director indicated that if revenue projections are overly inaccurate it may require a complete overhaul of the budget.

**Adopting a Multi-year Budget.** The survey results also revealed that the difficulty of the conversion from an annual to a multi-year budget was a disadvantage of multi-year budgets, according to 10 percent

of the respondents. One budget director stated that the initial staff time required to establish policies and procedures when implementing the multi-year budget process was considerable. Similarly, another respondent advised that computer capabilities and report format of off-the-shelf software does not readily accommodate multi-year budgeting.

**Increased Staff Time Dedicated to Budget Development.** Seven percent of the respondents felt that the increase in staff time required at the beginning of the each budget period was a disadvantage of multi-year budgeting. One budget director noted that creating the budget requires more preparation time than in a given one-year cycle.

Although multi-year budgeting presents minor difficulties to some governments, 17 percent indicated that they saw no disadvantages to multi-year budgeting. One plausible explanation is that these governments were better prepared to adopt multi-year budgeting.

## Conclusions

This study described the concept of MYB and summarized the results of GFOA's survey. The findings found in this study are consistent with the current literature on multi-year budgeting. Specifically, the results show that chief executive officers play a major role as change agents for implementing a multi-year budget in local governments. To a lesser degree, chief financial officers, budget managers, and finance officers are responsible for initiating the transition from annual budgeting to multi-year budgeting. What is clear, however, is that the adoption of a multi-year budget requires the support of senior government officials.

The survey results also revealed that governments have multiple reasons for abandoning annual budgeting, such as:

- enabling departments to take a long-term view in their decision making process;
- improving the linkage between long-term priorities and the budget process;
- improving the linkage between the operating and capital budgets; and,
- reducing staff hours dedicated to budget development.

These reasons are consistent for local governments with multi-year financial plans, rolling biennial budgets, and "classic" biennial budgets.

### Exhibit 3 REASONS FOR ADOPTING MULTI-YEAR BUDGETING

What were the means for adopting a multi-year budget?

Response	Frequency	Percent
1. Enable department to take a long-term view in their decision making process	25	86%
2. Improve the linkage between the operating budget and the capital budget	13	45%
3. Improve the linkage between long-term priorities and the budgeting process	25	86%
4. Reduce staff hours dedicated to budget development	24	83%
5. Other	4	14%

### Exhibit 4 REASONS FOR ADOPTING MULTI-YEAR BUDGETING BY BUDGET TYPE

What were the reasons for adopting a multi-year budget?

	Multi-year Financial Plan	Rolling Biennial Budget	Classic Biennial Budget
1. Enable departments to take a long-term view in their decision making process	9 90%	8 80%	8 89%
2. Improve the linkage between the operating budget and the capital budget	5 50%	5 50%	3 33%
3. Improve the linkage between long-term priorities and the budgeting process	9 90%	8 80%	8 89%
4. Reduce staff hours dedicated to budget development	7 79%	8 80%	9 100%
5. Other	1 10%	1 10%	2 22%
<b>Total</b>	<b>10</b>	<b>10</b>	<b>9</b>

Once implemented, governments have found that multi-year budgeting offers several advantages over annual budgeting, such as:

- depoliticizing the budget process;
- enabling departments to take a long-term view;
- enhancing long-term financial and program planning;
- improving the linkage between the operating and capital budgets;
- improving the linkage between long-term priorities and the budget process; and,
- reducing staff time dedicated to budget development.

These advantages also are consistent across the various types of biennial budgets (i.e., financial plan, rolling biennial budget, and "classic" biennial budget).

Some local governments have experienced some drawbacks to multi-year budgeting, such as difficulties forecasting

revenue and increased workload during the first year of the multi-year budget.

To assist local governments desiring to adopt a multi-year budget, the GFOA Research Center recently has completed consulting projects and several publications related to multi-year budgeting. The first publication is *An Elected Official's Guide to Multi-Year Budgeting*, and the second is *An Elected Officials Guide to Revenue Forecasting*. Available from GFOA for \$10 member/\$15 nonmember (call for quantity discounts). Contact GFOA at 312/977-9700 or [Publications@gfoa.org](mailto:Publications@gfoa.org) for more information. □

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