

By abandoning the traditional annual budget in favor of a biennial budget framework, one small city has saved staff time, improved its strategic planning capabilities, and enhanced its overall financial condition.

Taking the Plunge: The Conversion to Multi-year Budgeting

By Andrea Jackson

Multi-year budgeting offers a number of potential advantages over annual budgeting, including decreased staff time, enhanced long-range planning, and improved program evaluation. Multi-year budgeting facilitates the integration of financial and strategic planning, replacing incrementalism with a more strategic approach to resource allocation. As more and more governments have become aware of these and other benefits, many jurisdictions have converted to multi-year budgeting, usually on a biennial basis. Like many management reforms, however, implementation of multi-year budgeting requires careful planning in order to realize the desired benefits. This article describes one city's conversion from an annual budget to a biennial budget, emphasizing the most important considerations for governments pondering similar initiatives.

The Case for Change

The City of Auburn, Alabama, is a council-manager government with a population of 43,000 and a general fund budget of \$35 million. The city has a well-established history of innovation, long-range planning and goal-oriented stewardship of public resources. As a result, launching a multi-year budgeting effort was a logical extension of Auburn's approach to government. Auburn is believed to be the only local government in Alabama engaged in multi-year budgeting.

In the spring of 2000, the city manager asked the finance director to consider preparing a biennial budget with the intention of reducing the amount of staff time devoted to budget preparation and publication and to the mid-year review process. Because Auburn does not have a separate budget office or even one staff position dedicated to budget administration, finance staff were perpetually involved in some aspect of the budget. The budget also consumed a great deal of time for line department staff. A reduction in the number of staff hours devoted to the budget represented significant savings that could be channeled into other important activities.

The city manager's other motivation for investigating biennial budgeting was to extend the staff's planning and management horizon. The city's annual budget process had been goal-oriented since the institution of the annual citizen survey, the results of which were used by the City Council to establish priorities for the upcoming budget period. These priorities then served as the basis for the preparation of departmental goals and budget requests. Despite its success in linking goals and priorities to resource allocation, Auburn's annual budget appropriation and subsequent mid-year

review did little to facilitate long-term financial planning.

The improved long-range planning potential of multi-year budgeting offered another important benefit to city officials: enhanced fund balance position and bond rating. In the early 1990s, Auburn's general fund balance had dipped to precariously low levels, having been tapped for a series of capital improvement projects. By the end of the decade, the general fund balance had been significantly improved thanks to a renewed emphasis on careful budgeting and close monitoring. Both the city manager and the finance director included fund balance maintenance as a strategic goal of biennial budgeting.

Of Form and Function

Local governments that budget on a multi-year basis typically employ one of the following variations of biennial budgeting: biennial financial plan, rolling biennial budget, or classic biennial budget. The biennial financial plan is characterized by an annual appropriation linked to a tentative, unenforceable spending plan for the following year. The rolling biennial budget is a two-year spending plan comprised of two one-year appropriations that are adjusted annually. The classic, or traditional, biennial budget is a two-year spending plan in which 24 months worth of expenditures are approved simultaneously. The distribution of these three types of biennial budgets has been almost even among governments that practice multi-year budgeting.¹

In deciding which type of biennial budget to use, governments need to consider applicable state laws, as well as the characteristics of the various types of budgets. For Auburn, the classic biennial budget made the most sense. The Alabama State Code requires municipalities to adopt an annual budget and to have an annual financial audit. However, there is no apparent legal prohibition against adopting two annual budgets at one time. In the city's view, the rolling biennial budget did not offer the time savings of the classic biennial budget, and the biennial financial plan did not facilitate long-term planning as well as the classic biennial budget. Given state legal requirements and the city's major objectives in converting to multi-year budgeting, Auburn opted in favor of the classic biennial budget.

Winning Organizational Support

Introducing change is never easy in the public sector, especially when it involves something as fundamental as the budget process. To be successful, the conversion to multi-year budgeting must have

the support of the governing body, the chief executive, and department directors. Winning the support of these key stakeholders requires that finance officers be able to clearly explain the rationale behind multi-year budgeting and to identify the benefits thereof.

The process of implementing biennial budgeting in Auburn began with a meeting between the finance director and her staff about the city manager's proposal and the goals of biennial budgeting. The response from finance staff was positive and supportive, which encouraged the city manager to take his idea to the other department directors. The potential of biennial budgeting to reduce the amount of staff time required for budget preparation earned the immediate support of these important stakeholders. The department directors had ample experience in implementing innovative improvements, so they enthusiastically accepted the challenge of preparing a two-year budget despite the increased workload that was inevitable during the conversion.

Once the city manager had secured departmental support for biennial budgeting, he took the recommendation to the City Council for approval. Given the city's generally favorable disposition toward innovation and change, the Council was not surprised by the proposal and threw its support behind the effort to convert to biennial budgeting. Although multi-year budgeting is sometimes viewed as a threat to the governing body's budgetary oversight, the City Council did not express any concerns to this effect. The city manager partially mitigated the potential for concern by assuring council members that they would continue to receive monthly budget reports and that any increases would require City Council approval via ordinance.

As envisioned by the city manager, biennial budgeting would reduce the City Council's workload with respect to the budget. Midway through the first biennium, the administration would compare actual to projected revenues. As long as actual revenue collections to date and projected revenues through the end of the fiscal year were sufficient to support appropriations and maintain desired fund balance levels, no additional mid-year review would be required.

Conversion Challenges

Having secured the support of the key stakeholders in city government, the Finance Department turned its attention to the logistics of developing the proposed biennial budget for fiscal years 2001 and 2002. The City Council did not approve the conversion to biennial budgeting until late April. Under the previous budget calendar, finance staff already would have begun assembling the spreadsheets, forms, and instructions to be used by the departments in submitting their budget requests. Already behind schedule, staff decided to use essentially the same spreadsheets and forms as before, using color coding to differentiate materials for the second year of the biennium. This section describes three major challenges of Auburn's conversion to biennial budgeting: estimating personnel needs, forecasting revenues, and balancing the budget.

Estimating Personnel Needs

Multi-year budgeting forces governments to assess future staffing levels and their effect on the operating budget. In Auburn, the Human Resource Department is responsible for preparing personnel budget spreadsheets for each department. These spreadsheets provide detailed information for each authorized position, including the name of the employee occupying the position, the employee's salary grade and steps, and the employee's salary for the next budget period. Auburn has more than 300 regular full-time employees, a dozen regular part-time employees, and approximately 150 temporary employees, which increases significantly on a seasonal basis. Calculating salary information for all of these employees and estimating future personnel needs for two years instead of one posed what seemed like a monumental obstacle for the Human Resources Department.

Adding to Human Resource's burden, Finance proposed and the city manager approved an additional change to the personnel budget spreadsheets. It was decided to calculate salaries so as to include the amount of the cost-of-living salary increase to be proposed to the City Council. In the past, cost-of-living increases were not included in the proposed budget. Rather, the money required to fund these raises was included separately, as one of the Council's "key decisions." This approach presented a disadvantage in that the effect of the cost-of-living increases on fund balance was not represented in the proposed budget numbers. To maintain the desired level of the general fund balance, the city determined that the effect of any proposed cost-of-living increase would be included in the proposed budget document.

Given that salaries and benefits comprise the largest single component of the city's budget, the accuracy of the personnel budget spreadsheets is always critical to the overall budget process. Because of the increased workload necessitated by the conversion process, the Finance Department was unable to include the personnel spreadsheets in the department budget packets distributed at the budget kickoff meeting. Thanks to a significant overtime effort by the Human Resources Department, however, the personnel spreadsheets for both years—including the proposed cost-of-living increase—were distributed to the departments shortly thereafter.

Forecasting Revenues

Multi-year budgeting complicates revenue forecasting by extending the time horizon from one year to two or more years. The further projections are extended, the less accurate they become. Fundamental changes in a government's revenue mix or significant deviations from expected revenues following the adoption of a multi-year budget may require revisions to revenue estimates or adjustments to appropriations.

Through the years, the Finance Department has endeavored to produce realistically conservative revenue projections for the city manager's consideration. For each major revenue source, and for most of the minor ones, Finance maintains a month-by-month revenue history going back 15 years or more. Staff carefully monitors national, state, and local economic conditions, and analyzes the revenue implications of annexations, population growth, building permit data, and developments at Auburn University. Because the city collects its own sales taxes, Auburn has a valuable source of information about the vitality of the local economy. However, the city's revenue forecasts are complicated by the fact that it relies on several state-shared revenues that cannot be reliably projected.

Forecasting revenues for Auburn's first biennial budget was a real challenge. Although the city used the same methodology it had used to project revenues for the annual budget, it was somewhat more conservative with the second year's revenues because of the extended timeframe. The fact that 60 percent of the city's four major sources of general fund revenue are received by mid-year helps alleviate some of the uncertainty. It is also helpful in identifying any significant deviations from expected revenues so that the city manager can make any necessary adjustments sooner rather than later.

Reviewing Departmental Budget Requests

Following the submission of the departmental budget requests for the first biennium, the city manager and Finance staff faced the ever-daunting task of balancing the budget requests to the projected revenues while maintaining appropriate fund balance levels. Although the city adhered to the same procedures it had used to balance the annual budget, the process was complicated by the additional year. The city manager reviewed all capital outlay items and capital projects, making cuts and deferrals as he deemed necessary. All departments were given a target budget amount for each budget year that was a specific percentage less than their original budget requests. Department heads were allowed to change line

COMPARISON OF BIENNIAL BUDGET CALENDAR TO ANNUAL BUDGET CALENDAR

Biennial Budget		Annual Budget	
Jun 1	Departments' goals due Budget forms issued	Jun 1	Departments' goals due Budget forms issued
Jun 30	Revenue projections due Departments' budget requests due	Jun 30	Revenue projections due Departments' budget requests due
Jul 1-30	Review and analysis Publish proposed budget	Jul 1-30	Review and analysis Publish proposed budget
Aug 1	Budget hearings	Aug 1	Budget hearings
Aug 15	Key decisions	Aug 15	Key decisions
Sep 10	Budget adoption	Sep 10	Budget adoption
Sep 20	Current year's end of year budget adjustment adoption	Sep 20	Current year's end of year budget adjustment adoption
Sep 30	Working document due	Sep 30	Working document due
Dec 30	GFOA document due	Dec 30	GFOA document due
Second year		Second year	
May 15	Mid-year review of revenue Expenditure budget cuts, if needed	May 1	Mid-year budget forms issued
		May 15	Mid-year revenue revisions due Departments' budget revisions due
		May 15-30	Mid-year review and analysis Publish mid-year budget
Jun 1	Departments' goal revisions due Mid-biennium budget forms issued	Jun 1	Departments' goals due Budget forms issued
		Jun 5	Mid-year review
		Jun 10	Mid-year budget amendment adopted
Jun 30	Revenue projections due Departments' budget requests due	Jun 30	Revenue projections due Departments' budget requests due
Jul 1-30	Review and analysis Publish proposed budget	Jul 1-30	Review and analysis Publish proposed budget
Aug 1	Budget hearings	Aug 1	Budget hearings
Aug 15	Key decisions	Aug 15	Key decisions
Sep 10	Budget amendment adopted	Sep 10	Budget adopted
Sep 20	Current year's end of year budget adjustment adoption	Sep 20	Current year's end of year budget adjustment adoption
Sep 30	Working document due	Sep 30	Working document due
		Dec 30	GFOA document due

item amounts as long as the target budget amount was achieved. The city made provisions to borrow money for capital projects that could not be accommodated by the projected available resources and that could not be cut or deferred because of Council priorities.

Results

As Auburn geared up for the preparation of its second biennial budget, the citywide consensus was that multi-year budgeting had lived up to its promises. The management and staff of all city departments agreed that biennial budgeting had reduced the amount of staff time devoted to budget preparation, shifting resources toward the achievement of other goals. During the first biennium, the mid-year review required only the limited involve-

ment of the Office of the City Manager and the Finance Department. Department heads and their staffs did not participate as they had in previous years. And as the end of the first fiscal year approached, staff had only to review and revise the second year's numbers instead of building a new budget from scratch. This saved substantial time for the City Council and all of the city employees involved in the budget process.

City officials scheduled preparation of the second biennium to begin two months earlier than the last time. This allowed the city to incorporate the mid-year review for the second year of the first biennium into the preparation of the proposed budget for the second biennium. Another factor in the early scheduling was that City Council election activities were to begin in July for the August elec-

tion. As such, the mayor and City Council members, all of whom were up for election, could devote appropriate attention to the proposed budget before the campaign hit full stride.

Auburn also achieved its other goal with respect to biennial budgeting—to extend the city’s planning horizon. Since the conversion to biennial budgeting, the city manager and finance director have witnessed a paradigm shift in both the department heads and middle management. The notion of “fixing things at mid-year” is now obsolete, having been replaced by a forward-facing perspective that takes into consideration the long-term financial and operating impacts of spending recommendations. The mid-year review is now just a mechanism for assessing the adequacy of revenues.

During the initial biennium, Auburn experienced firsthand the increased uncertainty that accompanies multi-year revenue forecasting. In July 2001, sales tax revenue decreased from the prior year for the first time in more than a year. Sales tax revenue is the single largest component of the city’s general fund budget, so negative fluctuations have serious budgetary implications. During the mid-biennium review, Auburn had to reduce its original revenue projections for the biennium by a net amount of approximately \$500,000 (although projected sales tax revenue was off by more than \$1 million for the biennium, other revenue sources combined to make up for half of this amount). To offset the decrease in budgetary resources, the city opted to finance a property purchase of approximately \$1 million, thereby maintaining the desired ending general fund balance.

The economic uncertainties of projecting revenues for a longer time horizon provided the impetus for a recommendation to establish a “permanent” reserve of a portion of general fund net assets. As part of the mid-biennium review, the city manager recommended establishing a \$4 million permanent reserve in the general fund. This amount represented approximately 13 percent of the budgeted general fund expenditures. The City Council approved this recommendation, and included a provision in the mid-biennium amending ordinance to establish this reserve for use only in times of natural disaster or economic downturn.

Process Improvements

The Finance and Human Resources departments learned a great deal from Auburn’s first biennial budget experience. As a result, the city has introduced several improvements to its budget process that will save additional time and money and enhance overall financial management. These improvements are discussed below.

- Maintaining separate spreadsheets for each year of the biennium proved to be too confusing for city departments and finance staff. The simplest process improvement was to include both years of the biennium on the same spreadsheet. This seemingly minor adjustment greatly facilitated the analysis of departmental budget requests and the preparation of the budget document.
- Given the critical importance of an accurate personnel budget, the city improved its accounting for salaries and benefits by establishing separate salary accounts for the various classes of employees (regular full-time, regular part-time, temporary part-time, etc.). This enhanced level of detail facilitates the analysis of departmental budget requests, providing better information on the fiscal impact of proposed increases in personnel costs.
- Heading into the city’s second biennium, the human resources director questioned the wisdom of preparing detailed personnel budget spreadsheets for the second year of the biennium. Instead, it was suggested that the amounts budgeted for salaries and benefits the first year be increased by a flat percentage accommodating both merit pay increases and proposed cost-of-living increases. The second-year amounts would then be updated position by position during the mid-biennium review to ensure their accuracy. This change made it possible to include personnel figures in the

budget packets distributed to the departments for preparation of their budget requests.

- Budgeting for the salaries and wages of temporary employees has been a perennial problem for the city. Auburn has never been able to precisely budget the personnel costs of temporary employees whose pay fluctuates by season and whose work schedules are unpredictable. Departments like Parks and Recreation that employ many such employees have traditionally budgeted for these employees as a group, using a single lump sum amount. However, the annual audited financial statements always showed significant budget balances for these departments because of over budgeting for temporary employees. Thanks to the accounting change describe above, the city determined that the actual expenditures for these employees was approximately \$500,000 less than what had been budgeted.
- Capital outlay and debt service expenditures are budgeted by department. Although this approach does not yield a GAAP-based budget, it does facilitate accountability for and comparability of departmental operating costs. For the second biennium, Finance entered the debt service amounts directly into the departmental budget spreadsheets instead of generating a separate list of debt service requirements by department. This change is intended to prevent math errors and omissions for departmental debt service expenditures.

Conclusion

The consensus opinion among Auburn’s senior management team is that the city’s first biennial budgeting experience was an unqualified success. Auburn reduced the staff required to prepare and review the budget, extended its planning and management horizon, and maintained major fund balances. The city also introduced a number of process improvements that have further simplified budget preparation and resulted in additional time savings. Although the conversion to biennial budgeting was not without challenges, the benefits realized so far have been well worth the initial effort. By thinking through the conversion issues identified in this article, other governments can successfully transition to multi-year budgeting and enhance their financial and strategic management. ■■

NOTE

- ¹ B. Blom and S. Guajardo, “Multi-Year Budgeting: A Primer for Finance Officers,” *Government Finance Review* 16 (2000): 39-43.

ANDREA JACKSON, CPA, CGFM, is finance director for the City of Auburn, Alabama. She has more than 17 years of experience in governmental accounting and auditing, and holds an MBA from Auburn University.