



# **Budgeting as a Tool for Fiscal Sustainability**



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# *Session Agenda*



- Asset Management
- Capital Facility plans
- Budgeting for Operations & Maintenance



**Infrastructure Matters**

# Asset Management as the Tool to developing the CFP



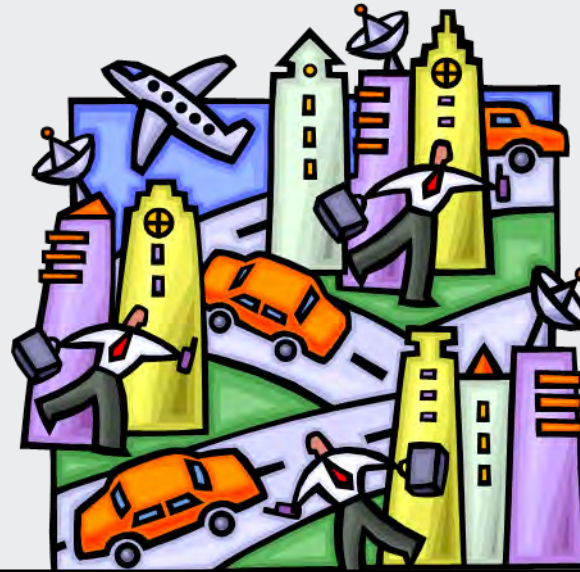
- What is Asset Management ?
  - It is maintaining a desired level of service for what you want your assets to provide at the lowest life cycle cost.
- What is Lowest life cycle cost?
  - Refers to the best appropriate cost for rehabilitating, repairing or replacing an asset
- Managing your assets
  - What do I own?
  - Where is it?
  - What is its condition?
  - **What is its useful life?**
  - **What is its value?**



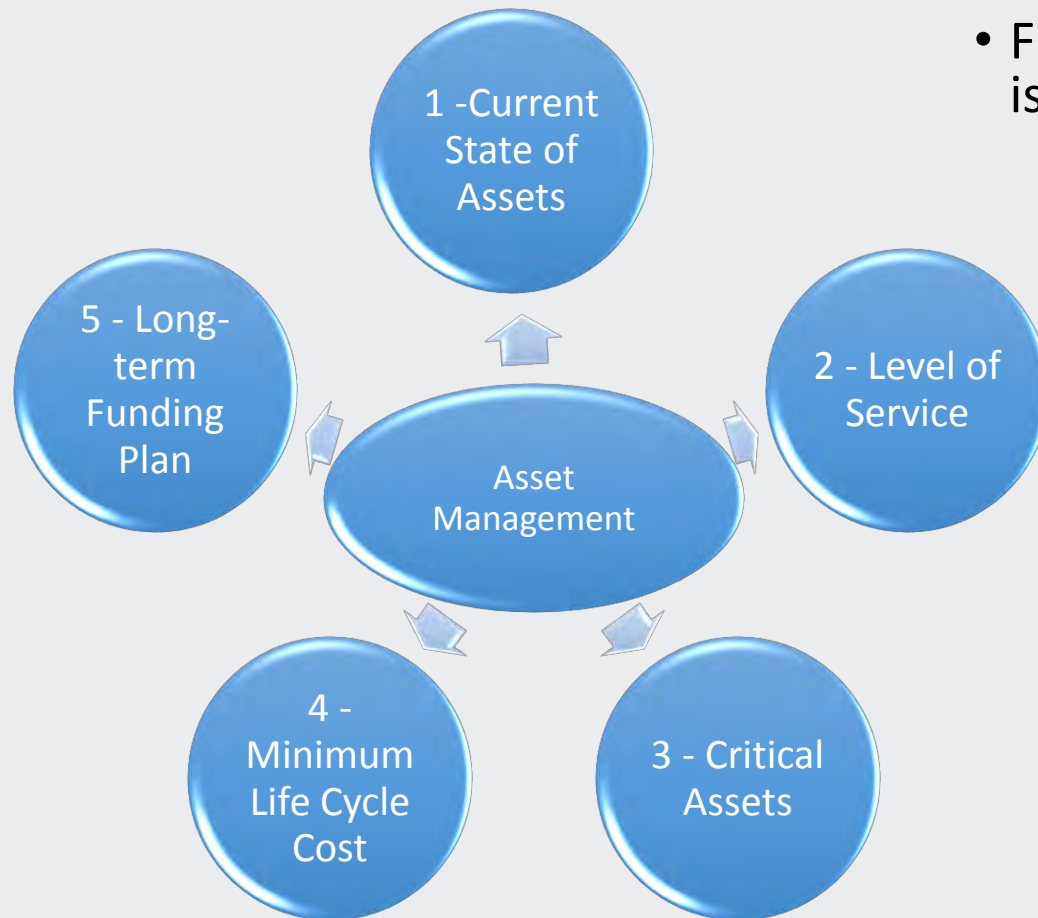
# Asset Management



- Useful Life?
  - A structure, improvement, piece of equipment, or other major asset having a useful life greater than 2 – 5 years.
- Cost – What is the Capital Asset thresholds?
  - A value set on anything that has a life cycle cost. Typically set between \$500 - \$25,000.
    - Recommend a minimum of \$1,000 - \$5,000
- Assessing current state of system's assets
  - Asset Inventory
  - Rating system for condition of asset
  - Assessing remaining useful life
  - Determining values and replacement costs



# Flow Chart: Asset Management Framework



- Five core questions framework is a starting point for:
  - Planning - provides opportunity to develop both a short term and long term asset management program
  - Implementation – gives opportunity to optimize the work of O&M crews.
    - Develops the right project, at the right time
  - Monitoring – to evaluate progress, changing factors and new best practices
  - Action – based upon the results of planning, implementation and monitoring

# *Capital Facilities Plan (CFP)*



- The Capital Facilities Plan (CFP) is an element of the “Comprehensive Land Use plan”
- Required by those entities fully planning under the Growth Management Act (GMA) or those that have opted in.
- It is a strategy for defining :
  - Public facilities needed
  - Where they will be provided
  - When the project will occur
  - How they will be financed
- The CFP is a 6 – 20 year plan of capital projects with estimated costs and proposed methods of financing.
  - Minimum of a six-year plan that clearly identifies sources of public money for such purposes

# RCW 36.70A. Growth Management Planning

- RCW 36.70A.070 (3) – Comprehensive Plan – Mandatory elements – Capital Facilities Plan
  - (3) A capital facilities plan element consisting of:
    - (a) An inventory of existing capital facilities owned by public entities, showing the locations and capacities of the capital facilities;
    - (b) a forecast of the future needs for such capital facilities;
    - (c) the proposed locations and capacities of expanded or new capital facilities;
    - (d) at least a six-year plan that will finance such capital facilities within projected funding capacities and clearly identifies sources of public money for such purposes; and
    - (e) a requirement to reassess the land use element if probable funding falls short of meeting existing needs and to ensure that the land use element, capital facilities plan element, and financing plan within the capital facilities plan element are coordinated and consistent. Park and recreation facilities shall be included in the capital facilities plan element.

# Incorporating the CFP into the Budget process



- The CFP provides:
  - A framework for decision makers about what and when to buy and how to pay for it.
  - Prioritizes and matches capital projects with the local budget and funding options.
  - Gives transparency to decisions and their incorporation into the budget process
  - The CFP - 6-year financing plan is often referred to as the “Capital Improvement Plan or CIP” - that is used to incorporate into budget process.

| <b>Cost/Funding Sources</b>   | <b>2012</b> | <b>2013</b> | <b>2014</b> | <b>2015</b> | <b>2016</b> | <b>2017</b> | <b>6 Year Total</b> | <b>20 Year Total</b> |
|-------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|---------------------|----------------------|
| <b>Cost (in thousands)</b>    |             |             |             |             |             |             |                     |                      |
| North Bay Park                |             | \$ 1,129    |             |             |             |             | \$ 1,129            | \$ 1,129             |
| Damon Point Access Area       |             |             |             |             |             | \$ 140      | \$ 140              | \$ 140               |
| Chinook Park                  |             |             |             | \$ 206      |             |             | \$ 206              | \$ 206               |
| Milo Schneider Park           |             |             |             |             | \$ 85       |             | \$ 85               | \$ 85                |
| Wastewater Trtmt Plant Access |             |             | \$ 400      |             |             |             | \$ 400              | \$ 400               |
| S. End Beach Access           |             |             |             |             |             |             | \$ -                | \$ -                 |
| Emerson Park                  |             |             |             |             |             |             | \$ -                | \$ -                 |
| No. End Grand Canal Park      |             |             | \$ 33       |             |             |             | \$ 33               | \$ 33                |
| So. End Grand Canal Park      |             |             |             |             |             | \$ 25       | \$ 25               | \$ 25                |
| <b>Funding Sources</b>        |             |             |             |             |             |             |                     |                      |
| GF General Fund (C)           | \$ 125      | \$ 126      | \$ 103      | \$ 100      | \$ 130      | \$ 151      | \$ 735              | \$ 735               |
| Capital Fund -REET (C)        | \$ 50       | \$ 50       | \$ 79       | \$ 57       | \$ 27       | \$ 30       | \$ 293              | \$ 293               |



# *CFP and Asset Management programs incorporated into Budget*



- Operations and maintenance (O&M), personnel and the capital budget account for an estimated 85 percent of a utility system's expenses.
- Adoption of a Asset Management Plan and CFP meets these best practices:
  - Moving from reactive maintenance to predictive maintenance
  - Consideration for rehabilitation versus replacement
  - Develop specific response plans for asset failure
  - Evaluating lifecycle costs for critical assets
  - Identify what capital facilities will be needed in the future.



# *Budgeting – bring plans into the budget documents*



The Budget is an **economic plan** that focuses the entity's **financial & human resources** on the **accomplishment of specific goals & objectives** established by the **policy makers**.

The budget establishes the annual (or biennial) expenditure levels for “all “departments & funds.

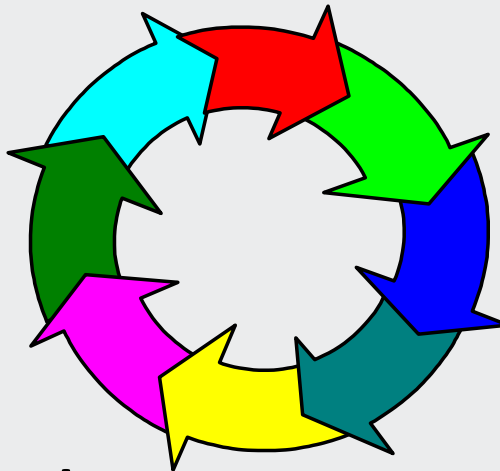
- These expenditure levels are called **appropriations**, and they represent spending limits.

# *Budget definition continued.....*



- The mission of the budget process is to help decision makers make informed choices about the **provision of services and capital assets** and to **promote stakeholder participation** in the process.

## **National Advisory Council on State and Local Budgeting**



**Pre-budget steps such as Asset Management and Capital Projects planning will assist elected with making “informed choices”.**

# *Functions of a utility budget*



- It's more than a way to authorize expenditures.
- More than just a management tool
- The budget is a political and managerial process that has financial and technical dimensions.
- Provides financial viability that generates sufficient funds to develop, construct, operate, maintain and manage utility in full compliance with local, state and federal requirements on a continuous basis.
  - **Develop the budget to operate your utility system like a business!!**

# *Utility systems are a business*

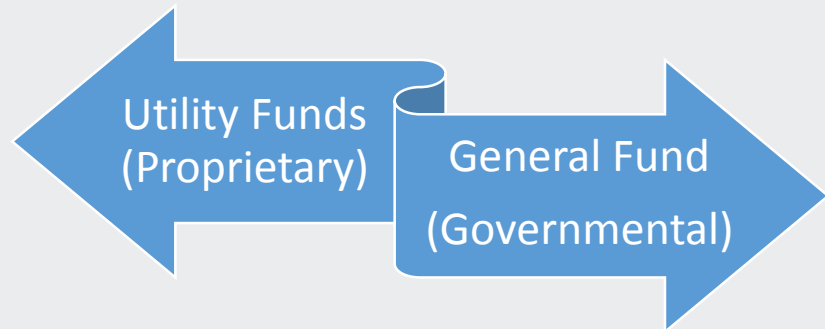


- Proprietary funds – function like a business entity.
  - Utilities are considered to be proprietary due to the fact that primary source of revenue is charges for service.

VS.

General Funds are governmental

- Primary source of revenues is taxes



# *Incorporate financial policies to add structure to the budget process*



- Financial policies that will address:
  - Balanced budget – provide definition
  - Use of one time revenues (hookup fees, connections fees, consumption beyond projection)
  - Use of reserves – when and why
  - Fund balance – cash flow considerations
  - Sustainable revenues
  - Sustainable expenses
  - Are current citizens paying the costs for current services?

# *Budget Priority Setting*



- Inherent step of the budget process:
  - Demand for services always exceeds resources
- Use the information gathered from:
  - Capital Facilities Plan
  - Asset Management Plan
  - Financial Policies for Reserves and Contingencies
- Results will assist in determining those functions/programs considered the most important to the attainment of service goals and objectives
- Evaluate the level of service to be provided
  - If needed - use a matrix for ranking services
    - Essential
    - Discretionary
    - Mandated

# *Steps to financial sustainability*



- Develop an Operating Budget
  - Take a long range look
  - 6 year forecast
- Review rates
  - Are they sufficient to meet forecast
- Create and fund an operating reserve
  - Cash flow needs
- Create and fund an emergency reserve
  - Tie to emergency management plan
- Create and fund a capital improvements and equipment replacement
  - Tie to CFP
- Do we need to go back to Step #2 and evaluate rates?







- “More with less” a short term solution
  - Need for long term solution in essential service areas
- “Less with less”
  - not sustainable unless repeatedly applied
- Sustainable budgeting requires:
  - Level of service evaluation
  - Evaluate supporting revenues in conjunction with service
  - Long term planning and evaluation
  - Contingencies
  - Reserves

# Utility Budget Forecasts

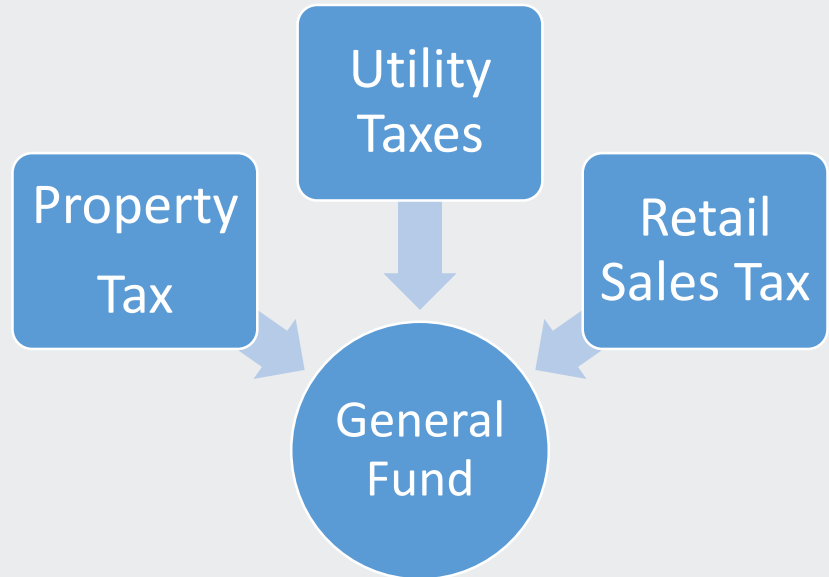


- Start with what you know ( or think you know)
  - Utility revenues (current rates)
  - Salaries
  - Debt Service
  - Contracts
  - Fixed Costs
  - Debt Obligations
  - Capital Items from CIP
- Add assumptions for more volatile items
  - Consumption (water usage)
  - Expenses / Fuel Costs
- Create parameters for new impacts such as
  - State and Federal requirements
  - Tax changes for city and/or state utility/excise tax

# Utility Costs – City imposed utility tax



- Cities have the ability to impose a B&O tax in the form of a utility tax
  - Tax is on the Utility not the customer
  - Tax may be imposed upon all utilities operating within the city's jurisdiction including utilities owned by the city.
- Utility should treat this tax as an expense
  - Treat the same as state excise tax



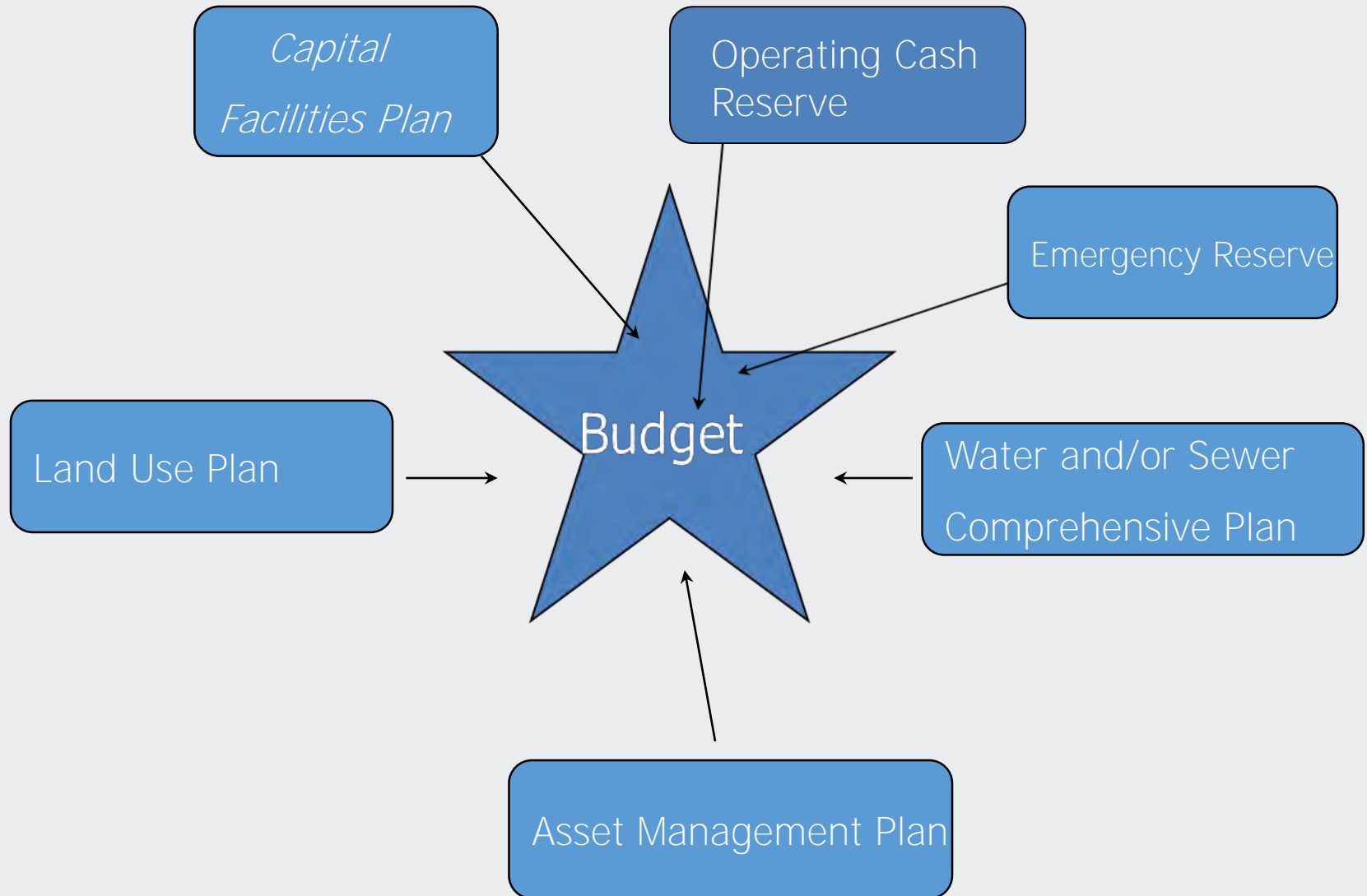
# *Debt Service requirements and rate setting*



- What is our debt ratio?
- Are current utility rates sufficient to meet:
  - O&M Costs
  - Debt Service Requirements
  - Current Asset needs
  - Future capital needs



# *Fold your plans into the Budget Process*



# *Reserves & Contingencies*



- How much is enough?
  - GFOA recommended best practice
    - Utility funds – no less than 45 days of working capital
- Differences between reserves and fund balance
  - External demands and/or fiscal policies to set the definitions of “reserved” fund balances
- Contingencies – what are they and why do we need them?
  - Historically, economic cycles will continue to occur
  - Contingencies are considered a best practice to handle the unknowns.

# *Evaluating the Budget Numbers*



- Do we have any of the known fiscal stress indicators?
  - Declining fund balances
  - Ending and beginning fund balance of 5% or less?
  - Debt service ratio to operating revenues
  - Current revenues no longer meet the demands of service delivery
  - Cost of service cannot be sustained at current levels

# *Financial Condition-Evaluation*

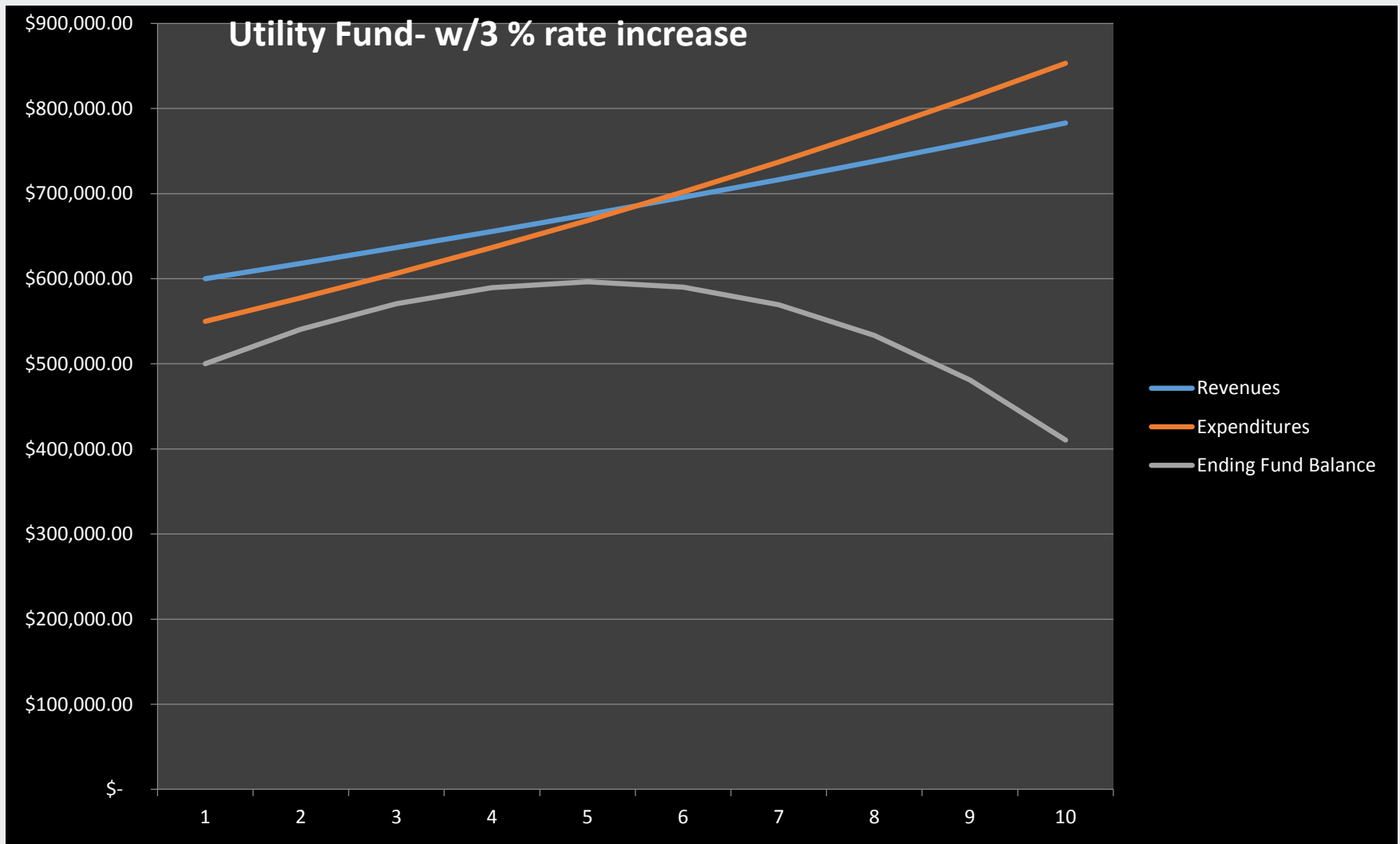


- Red Flags
  - Provides a starting point for further discussions
- Evaluation of fiscal signs will assist with developing the budget strategy.
- Fiscal review should include the question:
  - is this short term or long term?
  - What is the strategy to stop the bleeding?





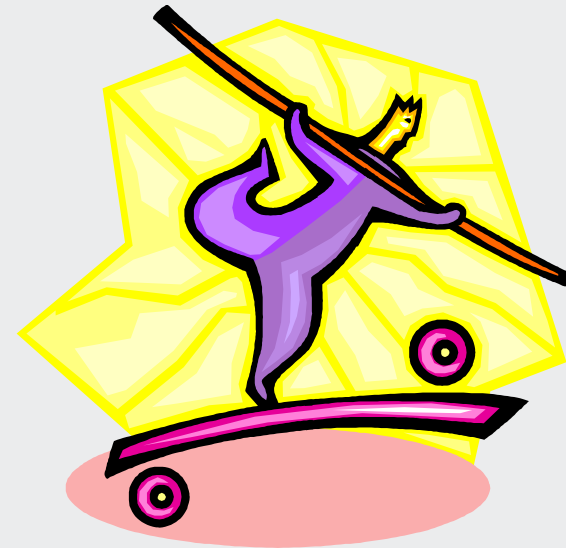
# Utility Fund Example



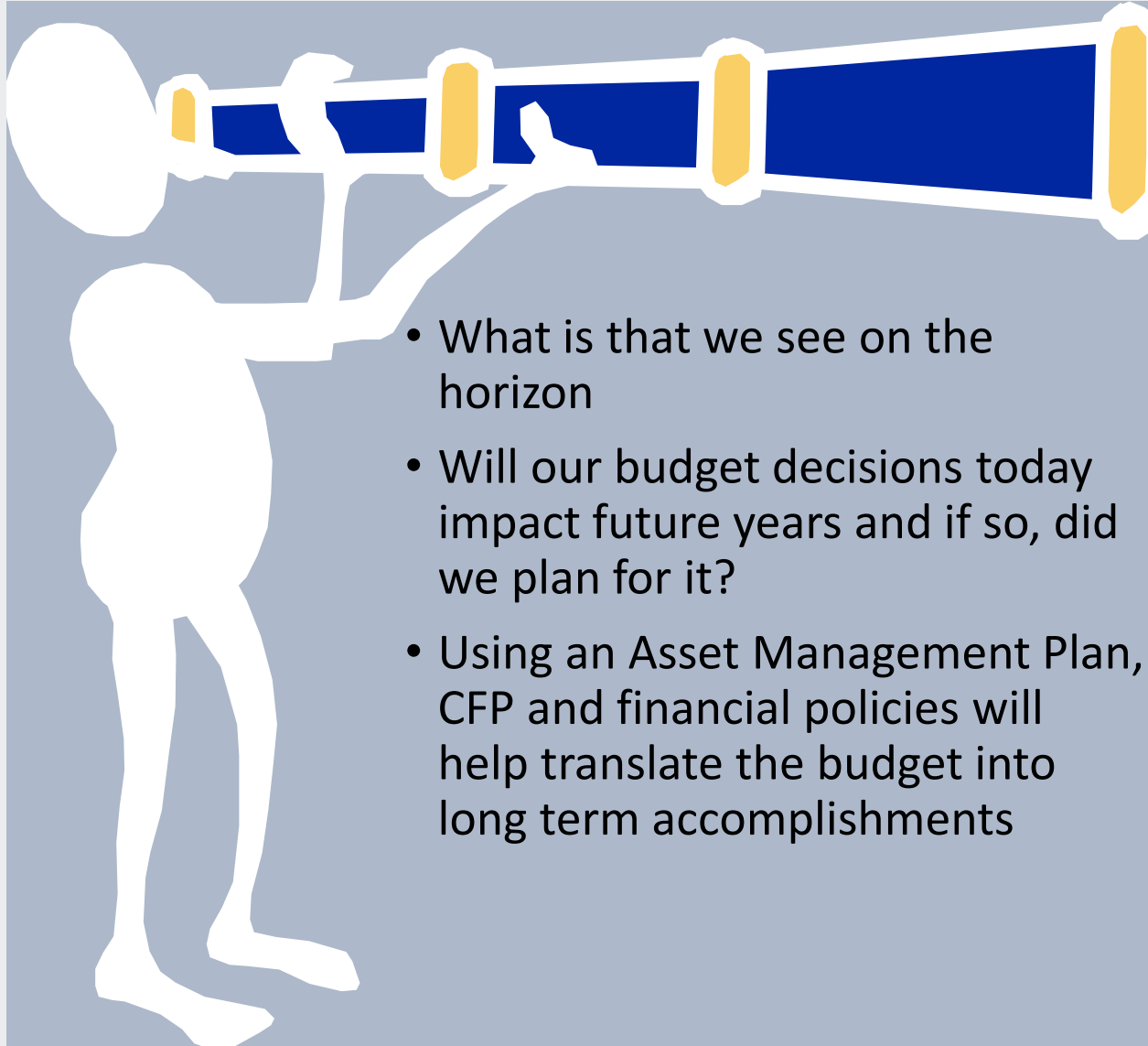
# *Budgeting Best Practices*



- Reserves
  - Utility Funds
- Contingencies
  - Plan for the unexpected
- Long Term planning
  - Capital Replacement
  - Infrastructure enhancements
- Evaluate results
  - Performance measures
  - Outcomes rather than budget compliance



# *It's a long time horizon....*



- What is that we see on the horizon
- Will our budget decisions today impact future years and if so, did we plan for it?
- Using an Asset Management Plan, CFP and financial policies will help translate the budget into long term accomplishments