

BUDGET THEORY

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BUDGET THEORY

I. PURPOSE OF CHAPTER 8

The purpose of this chapter of *The Guide* is to explain the definition and purpose of budgets, describe the budget cycle, discuss budgeting concepts and practices by fund, and to identify and understand budget information on financial reports.

II. OVERVIEW

A budget is a financial plan that sets forth the resources necessary to meet a set of goals, (departmental, college, campus) for a certain period of time. The budget records, in monetary terms, realistic goals for programs, staffing, and operations. The revenue portion of the budget identifies the means for financing the plan, and the expense portion of the budget estimates the cost of the plan. Typically, the time period covered by the budget is a fiscal year. For the college, the fiscal year runs from July 1st through June 30th. When working with capital construction projects or sponsored programs, the time period covered by the budget spans the duration of the project rather than the fiscal year.

III. BUDGET RELATED TERMS AND DEFINITIONS

Account is a four-digit number used to identify specific revenue, revenue deduction, expense, and transfer items.

Base Budget is the original budget amounts recorded for a ORG. UNIT at the beginning of the fiscal year. The term *base budget* is used primarily in the General Fund.

Budget is a plan of financial operation for a given period embodying an estimate of proposed expenditures and the proposed means of financing them. Used without any modifier, the term *budget* usually refers to a financial plan for a single fiscal year.

Budget Cycle describes a process of budget planning and control which includes the actions of developing a financial plan, comparing the financial plan to actual performance, and taking corrective action to bring substandard performance into line with the plan or adjusting the plan to reflect changing financial conditions.

Budget Journal Entry (BJE) is an online process within the Finance System used for making budget adjustments to a ORG. UNIT.

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Continuing and Temporary Budgets: Understanding the concept of continuing budget and temporary budget is essential to doing budget work, particularly in the General Fund.

A **continuing budget** is a permanent resource allocation or budget adjustment that remains recorded in the respective ORG. UNIT from one year to the next.

A **temporary budget** stays in place only for the duration of the fiscal year in which it was recorded. These temporary budget transactions are not included during the process of rolling budgets forward from one fiscal year to the next.

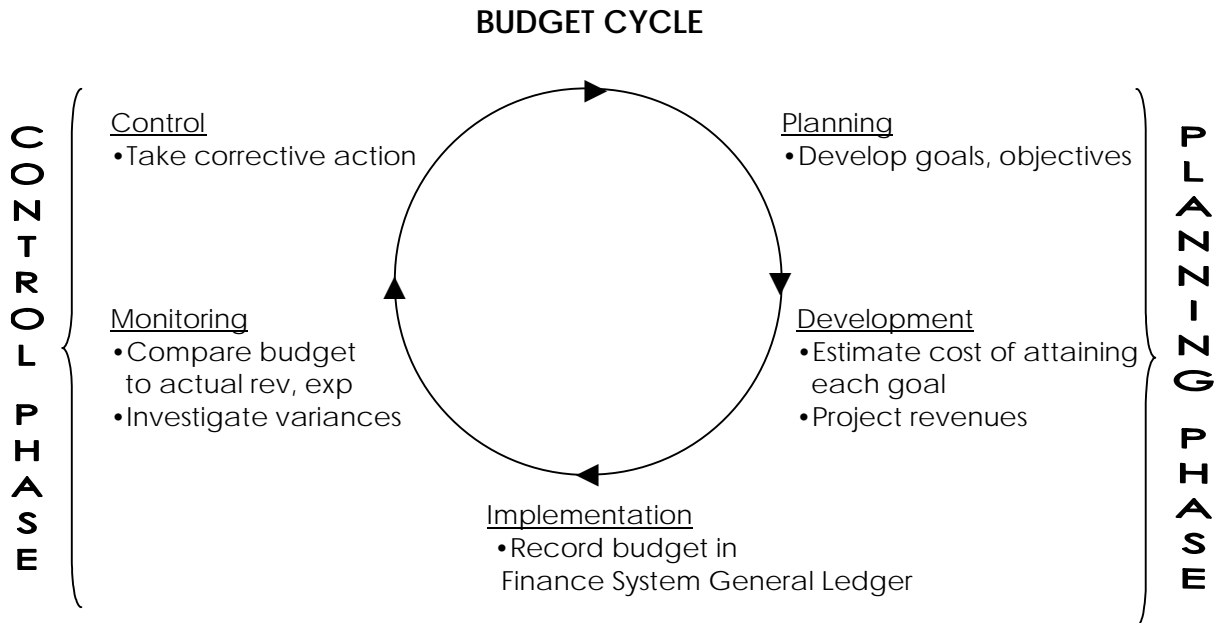
IV. THE BUDGET CYCLE

A. Overview

The budgeting process is a cycle comprised of two main phases: the planning phase and the control phase. The planning phase identifies the goals to be attained during the fiscal year, and the financial plan (budget) necessary to achieve them. The control phase focuses on actual performance towards achieving the plan. It involves implementation, monitoring and control functions. The control phase emphasizes a comparison between the budget and the actual revenue and expense activity as recorded in the financial system and displayed on the monthly statements. When actual revenue and expense varies from the plan articulated by the budget, the control phase will then include corrective action. Corrective action might involve adjusting the budget to reflect the actual financial activity, adjusting revenue projections and collections, or adjusting expenditures.

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The exhibit below provides a diagram of the budget cycle.



B. Working With the Budget Throughout the Budget Cycle

In your role as the departmental finance person, you are likely to be involved in each and every step of the budget cycle.

1. Planning and Development

The budget must be well conceived and based upon combination of historical data and future financial projections. During this step of the budget cycle, employees who handle the day-to-day finances for a department are often asked to provide information to management about past revenues, expenses and transfers, and anticipated revenues, expenses and transfers.

2. Implementation

It is essential to verify that the budgets recorded in the Finance System at the beginning of each fiscal year are correct.

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a) **Monthly Banner Budget Report or Web For Finance Period Report**

For ORG. UNIT in all funds, the Monthly Banner Budget Report or Web For Finance Period Report must be reconciled on a monthly basis.

1. Source documents for transactions must be compared to the revenue, expense and transfer transactions on the statement.
2. Errors must be researched and corrected in a timely fashion.

b) **Monthly Banner Budget Report or Web For Finance Period Report**

The Monthly Banner Budget Report or Web For Finance Period Report must be reviewed monthly to determine whether or not an organization is in control of its operations.

1. The budget in the ORG. UNIT must be compared to the actual expenditures.
2. For an auxiliary fund, the budget in the fund's ORG. UNITs must be compared to both the actual revenues and the actual expenditures.
3. For a sponsored program ORG. UNIT the budget in the ORG. UNIT must be compared to the actual expenditures. When doing budget-to-actual comparisons for the ORG. UNIT in a sponsored program, it is important to remember that the time period covered by the statement is often the duration of the program and not the fiscal year.

c) **Balance Sheet Transaction Statement/Statement of Net Assets Transactions**

The Balance Sheet Transaction Statement/Statement of Net Assets must be reconciled and reviewed each month to ensure that both the cash and fund balance account balances are favorable.

Note: More instructive and detailed information about working with monthly reports is available in *The Guide* Chapter 16, *Monthly Statements*.

3. **Control**

Departmental management must be informed when the "budget to actual" comparison indicates a significant deviation, or when the balance sheet indicates an unfavorable balance, so that appropriate corrective actions can be initiated.

With the inception of the new online Web For Finance Reporting Tool, reports will be made available to all who possess a fiscal role within a

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ORG. UNIT—no longer just one paper copy sent to departments. However, if you notice a problem or a potential problem developing in budget, it's best to err on the side of caution and inform management rather than assume they noticed it during their review. This makes for good interactive teamwork in the department.

V. BUDGET PLANNING SCHEDULE AT ASC

The budget process spans a 15 month time frame. In addition, each process involves a number of steps that are repeated on an annual basis at approximately the same time each year. The following exhibit, located on the next page, provides a table describing the important elements of the budget planning schedule for the College.

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BUDGET PLANNING, DEVELOPMENT and IMPLEMENTATION CALENDAR

Month	Task	Responsible Party at ASC
JUL	<ul style="list-style-type: none"> • Implement the budget for the new fiscal year • Book adjustments approved during the budget process • Audit the budget for the new fiscal year and make corrections • Set up standard journal entries for the new fiscal year • Review departmental goals, objectives and budget requests for the upcoming fiscal year 	Budget Director Accounting Dept Dept Heads / Budget Comm. / Cabinet
AUG	<ul style="list-style-type: none"> • State issues initial classified staff salary survey for new fiscal year 	State Dept of Personnel
SEP		
OCT	Complete 1 st Quarter current fiscal year budget vs. actual variance analysis and projections Budget Committee and Cabinet review and prioritize departmental budget change requests for upcoming fiscal year	Dept Heads / Budget Comm. / Cabinet
NOV	<ul style="list-style-type: none"> • Governor and CCHE submit statewide budget request to JBC for the upcoming fiscal year • CDC holds hearings on capital projects (Sometimes these have a cash-funded component). 	VP of Finance
DEC	<ul style="list-style-type: none"> • Budget Office prepares the first draft of upcoming fiscal year budget, incorporating Governor's request, revenue projections, and departmental budget change requests approved by the President 	Budget Director
JAN	<ul style="list-style-type: none"> • Complete 2nd Quarter budget vs. actual variance analysis and projections via Budget Summit with Budget Committee, Cabinet, and Campus Community. 	Dept Heads / Budget Comm. / Cabinet
FEB	<ul style="list-style-type: none"> • Current year budget rewrite submitted to Board of Trustees as action item 	Budget Director
MAR	<ul style="list-style-type: none"> • JBC revenue figure setting 	President, VP of Finance
APR	<ul style="list-style-type: none"> • Complete 3rd Quarter budget vs. actual variance analysis • Draft budget for upcoming fiscal year submitted to Board of Trustees as information item • Long bill introduction and debate • Capital projects introduced in bill form • Department heads prepare goals, objectives, and budget change request for out fiscal year that begins 15 months hence 	Dept Heads / Budget Comm. / Cabinet Budget Director VP of Finance Dept. Heads
MAY	<ul style="list-style-type: none"> • Governor signs long bill 	
JUN	<ul style="list-style-type: none"> • Budget for upcoming year submitted for final Board approval • Issue current fiscal year end closing instructions 	Budget Director Controller

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VI. METHODS OF BUDGETING

In general, the College uses two methods of budget development: *incremental budgeting* and *zero-base budgeting*. The incremental method is used to modify the existing base budget to account for incremental changes. This adjusted budget is often referred to as the “continuation budget”. Zero-base budgeting (ZBB) employs a “bottom-up” approach. It involves a re-evaluation of all programs, a review of their associated revenues and expenses, and a projection of how much it will cost to run each program during the upcoming fiscal year.

A. Incremental Budgeting

The incremental budgeting process begins with last year’s continuing budget figures as the base budget. These numbers are then adjusted to reflect inflation, growth, changing conditions and other information gathered from financial forecasts for the upcoming fiscal year. The advantage to using the incremental method of budgeting is that the work is greatly simplified, since this approach starts with a budget that is already in place. The disadvantage to incremental budgeting is that the inefficiencies and inadequacies of the prior year’s budget are automatically built into the budget for the upcoming fiscal year.

B. Zero-Base Budgeting

Zero-Base budgeting (ZBB) employs a “bottom-up” approach. This method starts with a base budget of zero and calculates the costs of running each program from scratch. On an annual basis, each cost associated with running a program must be justified before it can be included in the budget. The advantage of the ZBB method resides in the extensive review it gives each program. While the ZBB approach can uncover operating inefficiencies and identify weaker programs, it also can highlight those programs that are most vital to the organization. The effort and time requirements of ZBB are its principal disadvantages.

VII. BUDGETING PRACTICES

A. Developing and Recording the Budget for the New Fiscal Year

The Budget Office records initial fiscal year budgets for each ORG. UNIT in the General Fund, Auxiliary Funds, and Plant Funds (Renewal and Replacement ORG. UNIT). These budgets are made available to the user after July 1st and appear on the Finance System month-end statements for July. The Controller of Sponsored Programs maintains the budgets for grant and

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contracts ORG. UNITS. These budgets are available to the user from the inception of a program through the program's end-date.

B. Budget Management and Adjustment Throughout the Fiscal Year

After the Budget Office records the initial fiscal-year budgets in each ORG. UNIT, the responsibility for ongoing budget management rests with each department. It is important to keep in mind that the role of the budget, and the practices associated with doing budget adjustments, will vary according to fund.

1. General Fund

Although many departments have individual General Fund ORG. UNITS, the overall budget for the General Fund is managed as one unit at the campus level. The sum of the budgets within the individual General Fund ORG. UNITS located in departments all across campus must always equal the total campus budget approved by the Board of Trustees and the college's administration. Thus, once Budget Office records the initial budget in each General Fund ORG. UNIT, all dollar amounts in all subsequent budget transactions must be balanced so that the bottom line of the budget, in its entirety, does not change. Increases or decreases to the overall General Fund budget for the campus can be made only in accordance with revisions approved by administration. Therefore, budget change transactions must offset one another and all BJE's done in a General Fund ORG. UNIT must balance (debits = credits). If a budget is increased in one ORG. UNIT-account combination, it must have an equal decrease in other ORG. UNIT-account combinations. General Fund ORG. UNITS are budgeted on a fiscal year basis.

2. Auxiliary/Self-Funded Fund

The budgets for these funds are managed on a fund-by-fund basis. Therefore, BJE's typically record increases and decreases in the revenue and expense general budgets and accounts within one fund without having identical offsets in a different fund. In fact, budgets should not be transferred from one fund to another fund. In the Auxiliary Funds, it is appropriate to budget revenue in an amount different from the budgeted for expense within the same ORG. UNIT if it is management's intent that the ORG. UNIT generate a surplus for the period. Budgeted losses in the Auxiliary Funds are not allowed. Auxiliary Fund ORG. UNITS are budgeted on a fiscal year basis.

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3. Grant and Contract Fund

The budgets for these ORG. UNIT are managed on a ORG. UNIT-by-ORG. UNIT basis according to the budget approved in the sponsor's program document plus any subsequent amendments. These ORG. UNIT are budgeted on a program basis that may continue past the end of the fiscal year. The Controller of Sponsored Programs maintains these budgets.

4. Gift Fund

The College does not budget in gift funds, as these are deposits held in trust for others. The balance of these funds is not allowed to go negative.

5. Plant Fund – Construction

The budgets for these ORG. UNITS are based on an approved construction project budget plus any subsequent changes. Budgets in one ORG. UNIT do not affect budgets in a different ORG. UNIT and budgets should not be transferred from one ORG. UNIT to another. BJE's typically record increases and decreases in the revenue and expense general budgets and accounts within ORG. UNIT, without having identical offsets in other ORG. UNIT. Construction ORG. UNIT are budgeted on a project basis and therefore may continue past the end of the fiscal year. Facilities Management maintains and administers most construction project budgets.

6. Plant Fund – Retirement of Indebtedness

The cash in these ORG. UNITS is used for debt service payments of principal and associated handling charges or fees, or to retire indebtedness incurred in acquisition or construction of fixed assets. This fund is not budgeted in the Finance System. However, it is shown in the Board approved all funds budget and shown in the monthly budget report to the Board of Trustees.