

## Section 4: Finance

# Chapter 17: Budgeting

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### **The Budget: A Financial Plan**

The annual budget is the most significant of all policy-making opportunities available to local officials. Used wisely, the budget process can achieve the goals and objectives of the city or village and assure the delivery of the services expected by the citizens.

Focusing on the budget as a policy document allows elected officials to avoid the temptation to deal only with those items with which they may feel most comfortable—line-item details of office supplies, for example—and concentrate instead on basic policy issues.

Budgeting often takes two forms. The first is the operating budget dealing with short-term, year-after-year matters. The second is the capital budget for long-term, non-recurring expenses.

### **Budgets Requirements**

Budgets must:

- present revenues and expenditures for the previous fiscal year, those estimated for the current fiscal year and those estimated for the next fiscal year, which is the subject of the proposed budget;
- display the amount of surplus or deficit existing at the end of the previous fiscal year and that estimated for the current year;
- present proposed capital outlays and sources of financing for them;

- be balanced (expenditures cannot exceed revenues); and
- follow other requirements of the Uniform Budgeting and Accounting Act (1968 PA 2) and the GLV Act.

### **The Operating Budget – A Plan for Day-to-Day Operations**

In general, a budget is a plan of financial operation for a given period of time, including an estimate of all proposed expenditures from the funds of a local unit and the proposed means of financing the expenditures (definition from 1968 PA 2, as amended).

The Act, however, does not specify the format of the budget for either the general fund (operating budget) or any special revenue funds your community may use. Local governments are also required to set the millage rate required to cover the anticipated expenditures for the year, as well as to establish the necessary fees and charges for various services.

### **Types of Operating Budgets:**

**The line-item budget** divides expenditures into administrative categories such as salaries, fringe benefits, contractual services, office supplies, postage, etc. This type of budget is easy to prepare, but it is not goal- or program-oriented.

**The program budget** presents expenditures by program along with a narrative description of the services to be provided. Each program budget is composed of line-item amounts.

This type is more complex to prepare than the line-item type, but it is more goal-oriented for policy making purposes.

**The performance budget** shows the relationship between the dollars spent and units of service performed to determine a cost per unit (e.g., cost per mile of street swept). This is the most complex of all types of budgets to prepare and unit costs for some services are difficult to measure (e.g., cost per crime prevented by a crime prevention bureau). This type of budget is most useful in assessing the relative success of each program. Once again, line-item allocations of the costs must be made.

**The zero based budget** require each department to examine its programs by requiring justification for every dollar requested. This type usually follows the program or performance format. Because of its somewhat complicated nature, it is very time consuming and costly to prepare.

**The priority-based budget** allocates resources according to how effectively a program or service achieves goals and objectives that are the greatest value to the organization. In a priority-driven approach, a community identifies its most important strategic priorities, and then, through a collaborative, evidence-based process, ranks programs or services according to how well they align with the priorities. This type of budget is most helpful when aligning to strategic priorities.

Of the foregoing types of budgets, the program budget is the most useful and practical for local officials. It permits understanding of the purposes for which funds are being proposed and it encourages a policy-making approach

to budgeting. Many local governments will use parts of all the budgeting types, adapting each to the needs of the community. Regardless of the overall budget format used, it is necessary to prepare line-item detail for each section.

### **Revenue Sources**

An important step in the budget process is to determine, as accurately as possible, the amount of revenue available for the upcoming fiscal year. Special items of income vary among local units of government. Revenue sources for general operating budget purposes include:

- property taxes (controlled by law and charter);
- licenses and permits (building, plumbing, heating, electrical, air conditioning, occupancy, amusements, etc., controlled by ordinance);
- intergovernmental (state shared revenues, Act 51 monies, grants such as CBDG, Clean Michigan, etc.);
- charges for sales and services (engineering review fees, plan review fees, etc.);
- fines and forfeitures (drug forfeiture proceeds, library book fines, and penal fines);
- interest income; and
- miscellaneous.

Of those revenue sources on the list, local elected officials have much discretionary authority in all except property taxes and intergovernmental revenue sources.

## **Expenditures**

Expenditures provide for the day-to-day services to support the residents and businesses of the city or village. Under state law, all public expenditures are to be only for public purposes. Generally, allowable expenditures fall into the following categories:

- general government (council, manager, finance, clerk, etc.);
- public safety (police, fire, code enforcement and inspections);
- public works (streets, drains, walks, engineering); and
- leisure services (parks and recreation, library, museum, etc.).

## **Questions village officials should ask for compliance with appropriate budget requirements:**

- Does the person responsible for your accounting function use the state mandated uniform chart of accounts?
- Who is your chief administrative officer for budget purposes? 1968 PA 2 mandates a chief administrative officer to prepare and present the budget to the legislative body.
- Who is your fiscal officer for budget purposes? Per 1968 PA 2, this person is the official who prepares and administers the budget.
- Do you have an annual audit performed by a certified public accountant and file a copy with the state treasurer? NOTE: You have the option of a biannual audit if your population is less than 4,000 (MCL 141.425). However, the biannual audit will cover two years. If you plan to issue bonds, you will need an audit for the most recently completed fiscal year on file with the Michigan Department of Treasury. Most villages find it more efficient to have audits conducted annually.
- Does your chief administrative officer prepare and present a budget to the council according to an appropriate time schedule, with adequate time for review, discussion and public input before the beginning of the new fiscal year?
- Do department heads provide necessary information to the chief administrative officer?
- Does the council get the information necessary for proper consideration of the recommended budget?
- Are three years of figures included: the most recent complete fiscal year, the current fiscal year estimates and the upcoming fiscal year?
- Is the budget balanced? (Total estimated expenditures shall not exceed total estimated revenues. (MCL 141.435))
- Do you hold a public hearing before budget adoption as required by 1963 PA 43, as amended (MCL 141.411 to 141.415)? Do you include millage information, so you don't need to hold a separate truth in taxation hearing?
- Do you adopt the budget by indicating general appropriations by program, rather than by line item? Does the appropriations resolution or ordinance provide sufficient guidelines for the chief administrative officer and/or fiscal officer in administration of the budget?
- Do you adopt the budget prior to the start of the new fiscal year? If

- not, you have no authority for spending in the new fiscal year.
- Have you determined the millage you need to meet the liabilities for the coming fiscal year?

For samples of budgets, budget ordinances, investment policies, fund balance policies, purchasing ordinances and/or policies and other specific and general information on budgeting, contact the League’s Inquiry Service at [info@mml.org](mailto:info@mml.org). Much of this information is also available on the League’s website at [mml.org](http://mml.org). A sample budget ordinance is included in Appendix 9 of this handbook.

### **The Capital Budget—A Longer View**

The capital budget provides funding for non-recurring expenditures such as construction and acquisition of buildings, infrastructure, facilities, and equipment. These expenditures are “lumpy,” non-repetitive, and may span several years for project completion or acquisition.

The capital budget is another annual plan of revenues and appropriations. It is a document adopted by the local legislative body and having the force of law as a legally binding allocation of funds. It often represents the first year of a multi-year capital improvement program.

### **Revenue Sources for the Capital Budget**

Revenue sources for the capital budget may include any of those for the operating budget plus other sources for long-term capital improvements:

- special assessments;
- fees charged for construction;
- major road funds, Act 51—gas and weight taxes,
- local road funds, Act 51—gas and weight taxes;

- enterprise fund allocations from water, sewer, and other utilities;
- bond proceeds from issues by the local governing body and any of the authorities created by it (e.g., building authorities, downtown development authorities, housing authorities); and
- installment sales contracts for periods not exceeding 15 years for acquisitions of land, equipment, or property (PA 99 of 1933).

### **Capital Budget Expenditures**

Capital budget expenditures for property acquisition, construction and equipment usually include allocations to provide facilities for the operating departments of the local unit. Most of these are easily recognizable:

- general public works (streets, drains, water, sewer, sidewalks, lighting, motor equipment pool);
- police (equipment, vehicles, facilities),
- fire (equipment, apparatus, station houses);
- parks (land acquisition, recreation centers, play fields, athletic equipment, nature trails, etc.); and
- library and museum (buildings, furnishings, and equipment).

When considering capital expenditures for new facilities, budget makers must keep in mind the need for operating funds to place the new building or facility into operation. The need for additional employees, costs for heat, lighting, water, telephones and so on are appropriate concerns of those with budget-making authority. Additionally, consideration should be given to set aside resources in subsequent budgets

for the eventual repairs and maintenance of the facilities.

### **The Capital Improvement Program (CIP)**

**The capital improvement plan** is among the most important policy planning tools available to local budget makers.

The CIP provides a longer-range schedule for the community's major capital projects year-by-year. The Michigan Planning Enabling Act of 2008 (MPEA) requires that the CIP must project at least six years into the future: the first year of the CIP should be the upcoming budget year for capital budget allocations. Each operating department is expected to be represented in the CIP, and the task of the budget makers is to make sure the year-to-year estimated costs are within the financial capacity of the local unit.

Used properly, the CIP provides a systematic approach to financial planning so that budget makers can weigh the relative priority of these projects, build up funds for plan ahead for major investments, or undertake multi-year projects. This planning may include:

- increases in operating costs for new facilities;
- acquisition of rights-of-way;
- contributions to other authorities;
- special assessment projects; and
- bond issuance planning.

The CIP can also provide opportunity for a systematic approach to preventive maintenance and the rebuilding of facilities and infrastructure. Scheduling of heavy preventive maintenance and rebuilding will often extend beyond the required 6-year CIP time span, making a

### **Michigan Planning Enabling Act (ACT 33 of 2008) CIP requirements:**

The capital improvements program shall show those public structures and improvements, in the general order of priority, that in the planning commission's judgment will be needed or desirable and can be undertaken within the ensuing 6-year period. The capital improvements program shall be based upon the requirements of the local unit of government for all types of public structures and improvements. Consequently, each agency or department of the local unit of government with authority for public structures or improvements shall upon request furnish the planning commission with lists, plans, and estimates of time and cost of those public structures and improvements. The planning commission, after adoption of a master plan, shall annually prepare a capital improvements program of public structures and improvements, (unless the planning commission is exempted from this requirement by charter or otherwise). If the planning commission is exempted, the legislative body shall either prepare and adopt a capital improvements program, separate from or as a part of the annual budget, or delegate it to the chief elected official or a nonelected administrative official, subject to final approval by the legislative body. (MCL 125.3865)

longer planning horizon appropriate for some projects. For example:

- concrete streets—joint grouting and resealing plus selective slab replacement—seven-year cycle;

- concrete sidewalks—leveling and flag replacement—five-year cycle;
- water distribution system—system replacement—20-to-30-year cycle; or
- public buildings—plumbing, heating, electrical system updates—20-to-30-year cycle.


Under the MPEA, the planning commission is responsible for preparing the CIP annually and submitting it to the legislative body for final approval, unless exempted by charter or otherwise. The planning commission should coordinate with the chief executive official (e.g., village president or manager) to compile projects from each department or operating unit within the village into the CIP. Each year, the CIP should be updated to maintain the minimum 6-year planning horizon, and to review and adjust the planned projects for each year based on changing budgetary conditions. This process provides an opportunity for the planning commission to consider projects against the adopted master plan for the village, ensuring that major investments best support the village’s long-range goals.

Capital improvement programming is essential for the long-term wellbeing of the community. The importance of this part of municipal finance cannot be overstated.

**For More Information**

To request sample budgets, budget policies, and ordinances, email [info@mml.org](mailto:info@mml.org).

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**Rehmann**

At Rehmann, our professionals leverage years of experience to help you provide the best value to your communities with the resources you have. We are the trusted advisor team for government entities, K-12 education, higher education, and not-for-profit entities. We provide audit and financial reporting, federal and state compliance, organizational development and operations consulting, pension and retirement plan services, technology and cybersecurity solutions, CFO and accounting solutions, human resource solutions, investment advisory services, internal audit, and internal controls.

## **A suggested schedule for the budgeting process**

(assuming that your fiscal year begins March 1. If yours is different, adjust the schedule accordingly)

On or about	Step in the budget process
November 1	Chief administrative officer or fiscal officer asks department heads to compile budget requests for the coming fiscal year
December 1	Department heads submit budget requests for the coming fiscal year
January 1	Chief administrative officer presents the proposed budget to the legislative body
February 1	Council review completed; revisions made; union negotiations completed, etc.
February 7	If necessary, council adopts a resolution on the proposed additional millage rate for the coming fiscal year
February 16 (Optional)	Public hearing on the millage rate if you take advantage of increased SEV or want to increase the millage rate (Note: If you hold this separate hearing for the millage rate, the notice must include requirements set forth in MCL 211.24(e).)
February 28	Public hearing on budget (at least 6 days' notice), which may also include the millage rate information. Budget adopted
May	Millage set after final SEV figures are received. Cannot be more than proposed in public hearing.