Cash Basis Forecasting

OHIO AUDITOR OF STATE
KEITH FABER

Cash Basis Forecasting

Presented by:
Local Government Services

Efficient • Effective • Transparent

Financial Forecasts

What is a financial forecast?

- A financial forecast is prospective financial statements that present, to the best of management's knowledge and belief, the government's expected revenues, expenditures and fund balances.

- It is based on **management's assumptions reflecting conditions it expects to exist and the course of action it expects to take**.

Efficient • Effective • Transparent

What can you afford?

- Do you want to give your employee's raises? Elimination of positions? Layoffs? Furlough Days?
- If you offer insurance, how much will your premiums increase? Can you continue to afford this benefit? Employee share?
- Can you afford a new or currently existing service?
- Can you buy new equipment or make repairs to facilities?
- Do you have reserves for an emergency or downturn in the economy?
- **What are the long-term effects of the decisions that are made today**?

Efficient • Effective • Transparent

Is this really necessary?

Why do you need a forecast?

- Identify programs, activities and service levels that you **CAN** provide compared to what you **WANT** to provide.
- Identify costs associated with providing services and the funding sources used to provide them.
- Identify capital needs and establishes a plan for fulfilling those needs.
- Allows management to set priorities and document plans.
- Determine the effect of decisions on the community
- **Are the decisions being made/discussed leading you toward financial difficulties?**
  - **IF** you are declared in Fiscal Watch or Fiscal Emergency by the Auditor of State, a five year forecast is required.

Who should be involved in the process?

- The Governing Body – Council, Trustees, School Board, etc.
- Chief Operating Officer(s) – Mayor, Administrator, Manager
- Finance Committee (if one exists)
- Chief Financial Officer - Fiscal Officer, Auditor, Treasurer
- Department heads, group leaders, etc.
- **Process should be all inclusive so that all parties are aware of the financial situation and priorities can be set.**

Long-Term Planning

- What should a forecast include?
  - An Operating Plan
  - A Capital Plan
- Does it matter which comes first?

Long-Term Planning

Operating Plan
- Based on historical trends, new laws or regulations, upcoming or expiring revenues / expenditures, other factors.
  - Unless changed, it assumes existing programs will continue at the same level of service, both now and in the future.

Long-Term Planning

Operating Plan - Where do you Start?
- **ALWAYS start with revenue estimates**! What revenues do you know are going to continue into future years (i.e. taxes) and what revenues may expire (i.e. grants, certain tax levies). New revenues?
- If these estimates are not truthful and as realistic as possible, then the entire plan is useless.
- What expenditures **must** you pay for (i.e. debt or lease payments, salaries, utilities)? **ITEMS YOU CANNOT CUT!**
- What expenditures do you really need, but can live without if absolutely necessary (at least for a time)?
- Wish list

I Might Have an Issue!

Total Expenses	$10,000 per month
Job # 1 net pay	$4,000 per month
Job # 2 net pay	$1,000 per month
Job # 3 net pay	$3,000 per month
Net Effect	($2,000) per month

Long-Term Planning

Capital Plans

- Plan for capital expenditures over a period of years

- Sets forth each project or purchase in which the local government is to have a part

- Identifies the resources to be available to finance the project / purchase

Long-Term Planning

Capital Plan - Where do you Start?

- Develop a list of projects & purchases - **no limit**
- Include roads, bridges, buildings, parks and recreation facilities, land purchases, etc.
- Identify replacement of existing vehicles and equipment, etc.
- **Set priorities based on**……
- Identify resources to finance the expenditures
- Are there any alternatives (i.e. shared services, shared grants)

Long-Term Planning

How can I pay for Capital Expenditures?

- Reducing expenditures each year to build up a balance in a fund.
- Reserve Balance Accounts
- Note or Bond Issuances
- Loans – OPWC/OWDA/EPA/USDA/ODOT, etc.
- Special Capital levies
- Grants
- Special assessments
- ORC 5705.13 Capital Projects Fund

Long-Term Planning

Special Revenue Fund (ORC 5705.13)

- Accumulates resources for the payment of sick leave and vacation leave, and for payments in lieu of taking compensatory time off, upon the termination of employment or the retirement of employees/officers.

- May also accumulate resources for payment of salaries during any fiscal year when the number of pay periods exceeds the usual and customary number of pay periods.

Long-Term Planning

Capital Projects Fund (5705.13)

- Accumulates resources for the acquisition, construction, or improvement of capital assets, including motor vehicles

- More than one capital project fund may be established and may exist at any time

Long-Term Planning

For Operating and Capital Plans, what type of Legislative approval should there be?

- Long-Term Operating Plan
  - Choice of the Legislative Body
  - Commitment is the current year Appropriation Measure
- Capital Plans
  - Choice of the Legislative Body
  - Commitment to a project takes place when appropriated and bids are authorized

Financial Forecasts

- **Management** – Those persons who are expected to direct the operations of the entity during the prospective period. Management typically refers to those persons at the highest level of authority within the entity.

- **Assumptions** – The building blocks for the forecast developed from the key factors. They identify significant matters that are expected to occur, based on an entity's plans.

Financial Forecasts

- **Key Factors** – The significant matters on which a government's future results are expected to depend. Such factors are basic to the government's operations and thus encompass matters that affect, among other things, the government's financial activities. **Key factors serve as a foundation for prospective financial information and are the basis for the assumptions**.

Financial Forecasts

What are management's responsibilities?

- Preparation of the forecast

- Reasonableness of the assumptions

- Accuracy of the presented figures

Forecast Preparation Guidelines

AICPA "Guide for Prospective Financial Information" provides **general guidelines** to the responsible party for preparing financial forecasts. These are:

- Forecasts should be prepared in good faith

- Forecasts should be prepared with appropriate care by qualified personnel

- Forecasts should be prepared using appropriate accounting principals

Forecast Preparation Guidelines

- Assumptions used in preparing forecasts should be appropriate

- Key factors should be identified as a basis for the assumptions

- Information used in preparing forecasts should be consistent with the plans of the entity

Forecast Preparation Guidelines

- Process used to develop forecasts should provide a means to determine the relative effect of variations in the major assumptions (raises, insurance / utility increases)

- Process used should provide adequate documentation of the forecast and the process used to develop it (supporting your assumptions)

- Process used to develop forecasts should provide for seeking out the best information that is available at the time (historical information, contracts, debt schedules, calculations, etc.)

Forecast Preparation Guidelines

- Process used to develop forecasts should include the regular comparisons of the forecast with the actual results.

- Process used to prepare forecasts should include adequate review and approval by the responsible party at the appropriate levels of authority.

Assumptions and Key Factors

Property Taxes

- The type of levies, rate or dollar amount, year of approval, first and last year of collection
- Full and effective rates (real and commercial)
- Assessed valuations
- Triennial and sexennial updates
- Delinquent taxes and collections
- New and expiring levies
- Current amended certificate

Assumptions and Key Factors

Municipal Income Taxes

- Levy rate and effective period
- Department of Taxation estimates
- Income trends for area
- Unemployment trends for area
- New businesses for area? Any business leaving the area?

Assumptions and Key Factors

Predicting these revenues can be difficult:

- Local government revenues - provided by the State of Ohio. Included as part of the State's biennium budget every two years.
- Sales Tax for Counties
- Grants – some years you receive them, others you may not
- Fines and Fees
- Licenses and Permits
- Interest
- Rentals
  - For revenues such as rentals, are you charging enough? Are you charging too much?
- Miscellaneous Revenues, such as insurance or BWC reimbursements, donations from citizens

Assumptions and Key Factors

Personal Services
- Bargaining unit contract dates
- Salary schedules
- Staff positions
- Severance pay
- Retirement incentives
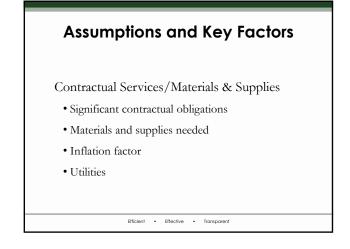- Computation of salaries (old/new rates)
- Employee vs. Contract Service?

Assumptions and Key Factors

Fringe Benefits
- Pension and Medicare payments (% of salaries) and the method of payment
- Health Care Benefits
- Purchase of service credit
- Workers' compensation premiums/rates/rebates
- Other benefits

Assumptions and Key Factors

Contractual Services/Materials & Supplies
- Significant contractual obligations
- Materials and supplies needed
- Inflation factor
- Utilities

Assumptions and Key Factors

Capital Outlay items to be purchased or constructed
- Capital Assets to be constructed
  - Infrastructure: In-Kind Contributions?
- Capital Assets to be acquired
  - Local share of contributed assets?

Assumptions and Key Factors

Debt Service
- Principal and Interest on debt payments
  - Example: Street truck, fire truck, new/renovated building, water and sewer improvement loans

We DID NOT plan for this!
Example: COVID-19

- Unpredictable – was anyone prepared?
- Additional expenditures with no anticipation of reimbursement or, if so, how much.
- CARES Act funding. Some used for prior expenditures, some for current needs.
- Will CARES Act funding continue? If so, for how long and for what may it be used?
- Will the expenditures incurred to combat the virus continue? Will costs increase?
- Loss of revenues – Will revenues recover? If they recover, how long could it take?

Efficient • Effective • Transparent

Successful Planning

- Be **REALISTIC** and **HONEST** about your situation: good, bad or ugly.
- Be willing to make and explain decisions, even tough ones.
- Maintain all documentation and materials supporting the values and the assumptions
- *****Continue to update both operating and capital plans as additional information becomes available or plans/goals change**.
  - Grant Awards
  - Construction Contracts
  - Debt Issuance
  - Unplanned Emergency Situations

Efficient • Effective • Transparent

OHIO AUDITOR OF STATE
KEITH FABER

Local Government Services
800-345-2519
ContactLGS@ohioauditor.gov

Efficient • Effective • Transparent   33