Adopt/Reaffirm Budget Principles & Policies to Guide the Budgeting Process

**SUMMARY**

**Key Points**

- A college should collaboratively develop budget principles and policies with those who have executive authority to propose a budget and those who have legislative authority to approve it, in conjunction with strategic planning and the finance department.

- Budget principles are general guidelines that a college intends to honor through its budgeting process. Principles are not designed to be technical so they can be understood and appreciated by all members of the organization and the public. By adopting budget principles, a college’s decision makers can create overarching values to help frame and guide budget deliberations.

- Budget principles create overarching values for prioritization and resource allocation. Key principles to consider include defining goals for student achievement, using data to drive decision making, allocating dollars optimally to create the most benefit given the cost, reviewing past spending decisions, developing and adhering to a multiyear funding plan, and accounting for and reporting the true cost of serving students and the corresponding outcomes.

- Budget policies help a college to identify its financial action and provide a standard against which its fiscal performance can be judged. These policies could address establishing a general fund reserve, long-term forecasting, capital asset maintenance and replacement, monitoring of revenues and expenditures, diversification of revenue, pension and other post-employment benefits, and grant funding.

**Related Award Program Criteria**

- **Criterion 1.A.1: Budget Principles.** A set of principles should be formally adopted by the applicant and submitted as supplementary materials. The principles should address, at a minimum, the concepts outlined in the best practice.

- **Criterion 1.A.2: Budget Policies (Mandatory).** The applicant should formally adopt a set of budget policies and submit them as supplementary materials. At a minimum, the policies should address the topics recommended by the best practice.
Introduction

Developing a budget that optimally aligns resources with goal achievement may, for many community colleges ("colleges"), entail making changes in how resources are spent. Many long-standing assumptions about how best to develop a budget may need adjustment. A set of budget principles and policies, agreed to by those with executive authority to propose a budget and those with legislative authority to approve them before the budgeting process begins, can provide a touchstone for what matters most in the budgeting process — creating the best outcomes for students and the community with the money available, while also maintaining financial sustainability.

Budget principles and policies should be developed collaboratively between those with executive authority to propose a budget and those with legislative authority to approve the principles and policies, with the support of strategic planning and the finance department. A college should develop a process that allows governing board members, strategic planning, and financial staff to collaboratively participate in development of the principles and policies to ensure broad understanding and support for the concepts the principles and policies outline.

This best practice addresses:
I. Budget principles to consider.
II. Budget policies to consider.

I. Budget Principles to Consider

Background. Budget principles set forth the ideals that a college’s decision makers will adhere to as they develop the budget. Principles are important for creating a shared understanding of the overarching values that underpin budget development.

Recommendation. Colleges adopt, in some form, the principles below to help frame and guide budget deliberations. Colleges also may consider other principles that support the goal of optimizing student achievement.

• Use goals to drive the budgeting process. A college’s explicit goals drive how resources are allocated or reallocated and are used to guide how potential new investments are evaluated in light of their alignment with the college’s strategic direction.

• Use data to make decisions. Collecting and tracking performance measures and other data can help a college recognize where changes in its environment or services are occurring that require reallocation of funds or an infusion of new resources. For example, a college might adopt a policy stating that budget requests should be supported by data (e.g., longitudinal studies, labor market data) that illustrate a real need and/or the proven effectiveness of the proposed change.

Such requests will be looked upon more favorably than those without supporting documentation.

• Consider both the inputs and outcomes of proposed budget decisions. The budgeting process should seek to allocate available dollars optimally, in a way that will achieve the best value. This means that a college should consider both the cost of programs along with the benefits they provide.

• Regularly re-examine patterns of spending and change them when they no longer make sense. College budgeting processes are often “incremental,” where last year’s spending becomes the basis for the next year’s budget, with incremental changes made around the margin. However, past patterns of spending may no longer be the best use of scarce resources given changing needs of students and the community. Consequently, the budgeting process should undertake a critical review of past spending decisions and a college should be willing to discontinue programs that are not achieving their objectives. To support these deliberations, a college should regularly review its programs and evaluate their impact relative to its strategic goals.

• Take a long-term perspective. Many colleges will not be able to make large changes to their educational strategy and resource allocation patterns within a single year. Further, a consistent
application of proven strategies over a multiyear period will deliver better results. Therefore, to the degree possible, a college should provide a multiyear funding plan for its strategies to optimize student achievement, with the goal of full funding and realigning resources where necessary to fund high-priority elements of the plan.

- **Be transparent.** Effective budgeting requires valid information about the true costs of serving students and the outcomes produced. Examples of more specific principles or policies to consider include:
  - **Make performance data readily available.** The budgeting process should be informed by valid and reliable data on fiscal and academic performance.
  - **Consider all costs in evaluating the cost of educating students.** A full cost accounting approach is necessary to evaluate the classroom and non-classroom costs of educating students. In setting, reallocating, or reducing budgets, the full cost of educating students should be considered.
  - **Use a consolidated “all funds” budget.** The budgeting process should consider all available funds in order to make the greatest impact with available dollars, while also acknowledging constraints on spending.
  - **Budget for programs.** The budget should identify programs, particularly individually defined certificate or degree programs. Programs are a set of activities designed to produce a defined result for a defined set of constituents.
  - **Communicate the principles.** Make the budget principles available to stakeholders. One method would be to post them on the college’s website.

### II. Budget Policies to Consider

**Background.** Budget policies clarify and crystalize the intent behind how the college will manage its financial resources. Policies identify acceptable and unacceptable courses of financial action, establish parameters in which the college can operate, and provide a standard against which the college’s fiscal performance can be judged.

**Recommendation.** A college should develop and adopt policies in the areas indicated below.

- **General Fund Reserve**
  A college should adopt a policy to establish a formal level of unrestricted fund balance that should be maintained in the general fund as a reserve to hedge against risk. The policy should address, at a minimum: the target level of fund balance to maintain; the conditions under which fund balances may be spent; who can authorize the use of fund balance; and guidance on how the fund balance will be replenished to target levels after it has been used.

- **Long-term Forecasting**
  A policy should direct staff to develop long-term revenue and expenditure forecasts (typically covering three to five years) as part of the budgeting process and to consider these forecasts during budget development in order to address the future financial position of the college. The policy should also direct the development of long-term enrollment forecasts in order to support financial decision making, including, where practical, trend analysis for students in categories that cost more to educate, such as health care and technical career programs.

- **Funding New Programs**
  As a college looks for new ways to improve student learning, it will need to fund new programs and initiatives. Given that new programs are often at a natural disadvantage when competing with existing programs for funding, a college should develop policies that describe how it will fund and manage new programs. These policies could encourage practices that support budgeting decisions that best align resource allocation with optimizing student achievement, such as establishing a preference for “pilot” or “experimental” periods for new programs and up-front estimation of cost and benefits, followed by rigorous evaluation of actual results after a defined period.

- **Asset Maintenance & Replacement**
  A college should adopt policies that govern maintenance and replacement for its facilities as well as its shorter-lived assets such as technology. As a basic rule, the policy should direct that all assets will be maintained at a level that protects capital investment and minimizes future maintenance and replacement costs. The policy should commit the college to maintaining an inventory of its maintenance/replacement needs and define the funding mechanisms for staying current with those needs.
Estimating the Operating and Maintenance Costs of Capital Assets

Capital assets, especially facilities, are generally a significant part of a college’s total spending and the impact on the operating budget is significant because facilities must be operated and maintained. A policy should, foremost, direct that the estimated operating and maintenance costs of a potential new asset be taken into account when assessing the feasibility of acquiring the asset, including the affordability of those costs within the operating budget.

Regular Monitoring of Key Revenues and Expenditures

A college should develop a policy that establishes regular monitoring and reporting of key revenues and expenditures. The policy should describe which specific revenues and expenditures are to be monitored, identify who is responsible for monitoring, and specify the frequency of reports.

Revenue Diversification and Stabilization

A college should adopt a policy to encourage diversification and stabilization of the revenue base in order to prevent fluctuations in revenue yield. It is possible to elaborate on this basic goal in several ways. A policy could direct a college to develop sources of revenue that are under its own control in order to make the college less vulnerable to changes in state funding. A policy could also encourage the college to actively seek out new revenue sources to diversify its revenue base, including offering guidance on how fees and charges should be used, the level of cost recovery expected for fees (including for college enterprises), and parameters for pursuing grants, partnerships, gifts, and endowments. Finally, because tuition and fees are where a college generally has the most local control over its revenues (at least for colleges that have the legal ability to set their own tuition and fees), a policy should direct that tuition and fees are regularly reviewed and updated in order to ensure that they are appropriate.

Funding Pensions and Other Post-Employment Benefits (OPEB)

A pension and other post-employment benefits (OPEB) policy establishes the strategic approach on funding pension and OPEB liabilities. A college should adopt a policy that calls for it to contribute the full amount of its actuarially determined annual required contribution (ARC) each year and to target a 100 percent or more funded ratio (full funding). A policy should also address OPEB, such as health care coverage provided to retirees. GFOA recommends that a college finances these benefits as they are earned (i.e., prefund), rather than pay for benefits only as they become due. Unlike pensions, however, GFOA recognizes that in some cases, less than full actuarial funding is appropriate, perhaps because benefit levels will be adjusted over time to compensate for the effects of health care inflation.

Grant

Grant funding provides support for college programs, activities, and student scholarships. Some grants have special requirements in terms of how funds are spent, monitored, and reported or may require ongoing funding to maintain a program or asset beyond a grant’s life. A college should adopt a policy that establishes not only how it will identify grants and parties responsible for meeting its requirements, but also conducting a formal evaluation of the programming the grant funded as its conclusion.