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# MEMORANDUM

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Date: December 10, 2013

To: The Honorable Chairman and Members  
Pima County Board of Supervisors

From: C.H. Huckelberry  
County Administrator

A handwritten signature in black ink, appearing to be "CHH", is written over the printed name "C.H. Huckelberry".

Re: **Budget Monitoring and Reporting**

On October 1, 2013, I asked our Finance and Risk Management Director and Budget Manager to evaluate and review the various policies, procedures and laws relating to budget monitoring and reporting. The purpose of my request was to emphasize clear, accurate and timely budget monitoring and reporting; particularly as our budget position becomes more critical in the near future due to:

- a) continuing shrinkage of the tax base;
- b) significant budget exceedance by certain County departments and agencies last year that will shrink the projected ending fund balance; and
- c) the continuing slow and sluggish economic recovery, which simply means increases in state-shared revenues will continue to lag behind other normal economic recoveries.

These factors all combine to stress the County's fiscal position; hence, requiring substantially improved, timely and accurate budget monitoring and reporting.

For your information, I have attached a memorandum dated October 24, 2013 from the Finance and Risk Management Director and Budget Manager.

CHH/mjk

Attachment

- c: The Honorable Sarah Simmons, Presiding Judge, Superior Courts  
Elected Officials  
Appointing Authorities



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# MEMORANDUM

## DEPARTMENT OF FINANCE AND RISK MANAGEMENT

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To: C. H. Huckelberry  
County Administrator

Date: October 24, 2013

From: Tom Burke  
Director

Robert W. Johnson  
Budget Manager

Handwritten signatures in blue ink. The signature for Tom Burke is written over the printed name "Tom Burke" and extends upwards and to the right. The signature for Robert W. Johnson is written over the printed name "Robert W. Johnson" and extends downwards and to the right.

Re: **Budget Monitoring and Reporting**

This is in response to your memo of October 1, 2013 regarding Budget Monitoring and Reporting (Attachment 1).

The budget monitoring process has evolved significantly over the past two decades. During that period, a series of tools have been developed to track departmental budgets and report the results of that tracking to County management. A brief discussion of these tools follows:

### **Board of Supervisors Policy Number D 22.2 – Budget Accountability (Attachment 2)**

Section A of the Policy sets forth the County Administrator's responsibility for setting up budgetary controls to identify revenues, expenditures and variances associated with the current year's budget. This policy drives our monthly analyses of budget variances and the associated reports provided to County management.

Section B of the Policy, regarding Budget Exceedance, requires that a monthly report be provided to each department comparing the budget to actual expenses and revenues through that month. Each department is provided separate Line Item Forecast Detail reports for each department fund it administers. Departments provide forecasted year-end estimates of expenditures and revenues along with explanations of significant forecasted variances for each of the individual department funds that report to them. The department is also given the opportunity to explain the "big picture" in relation to its budget and what is actually occurring in the department's budget during the fiscal year.

The second part of Section B requires that, if a department fund's fiscal year to date report for the month of December and beyond results in a ten percent or more negative net fund impact than the expected budgeted straight-line estimate to date, the department shall immediately develop and implement a budget remediation plan to assure that the department fund's forecasted year-end net fund impact does not exceed the budgeted amount. The department is required to submit this remediation plan or an alternate forecast to the Board of Supervisors via the County Administrator within ten days of the issuance of the monthly report showing a net fund impact of ten percent or more. This provision has been used sparingly in the past and will be discussed more in the Issues section below.

The final paragraph of Section B also requires that, if a department fund's actual year-end net fund impact is more negative than authorized in the adopted budget, the elected official or department director must submit a report to the Board of Supervisors prior to September 1 describing the remedial actions that were taken to avoid the budget exceedance and why such actions were inadequate.

**Board of Supervisors' Policy Number D 22.3 - Performance Audits of County Departments (Attachment 3)**

The Board of Supervisors must adopt a budget that balances funding sources with funding uses. Arizona statutes require that elected officials and department directors spend budgeted funds for their budgeted purposes and not expend monies in excess of the amounts appropriated by the Board. A.R.S. § 42-17106 states:

42-17106. Expenditures limited to budgeted purposes; transfer of monies

A. Except as provided in subsection B, a county, city or town shall not:

1. Spend money for a purpose that is not included in its budget.
2. Spend money or incur or create a debt, obligation or liability in a fiscal year in excess of the amount stated for each purpose in the finally adopted budget for that year, except as provided by law, regardless of whether the county, city or town has received at any time, or has on hand, monies or revenue in excess of the amount required to meet expenditures, debts, obligations and liabilities that are incurred under the budget.

B. A governing body may transfer monies between budget items if all of the following apply:

1. The monies are available.
2. The transfer is in the public interest and based on a demonstrated need.
3. The transfer does not result in a violation of the limitations prescribed in article IX, sections 19 and 20, Constitution of Arizona.
4. A majority of the members of the governing body votes affirmatively on the transfer at a public meeting.

Policy D 22.3 was adopted by the Board to address situations where departments overspend their adopted budgets. Basically, this policy requires that those individual departments that exceed their budgeted net fund impact for the previous year by more than \$250,000 be subject to a performance audit covering specific audit objectives covered in section D of the Policy. The County Administrator has discretion in the scope of audit.

Other Board of Supervisors' Policies, such as D 22.5 – Periodic Review of Departmental Base Budgets and D 22.6 – Policy for Administering Grants, also reinforce the need and requirements for budget monitoring and oversight.

**Financial System Budget Control**

The County's Financial System is configured to stop financial transactions within a particular department and fund if the transaction will cause the actual dollars spent or encumbered within one of the three standard budget appropriation units to exceed the overall adopted budget for that appropriation unit. There are three standard appropriation units for most departments: (i) employee compensation, (ii)

supplies and services, and (iii) capital equipment. Some departments also have a Capital Improvement Program appropriation unit. If a department's action causes any of these areas to exceed budget, the department must then identify available budget authority within one of its other appropriation units to make budget adjustments within its total adopted budget before any further financial transactions are permitted by the system.

### **Issues Associated with the Budget Monitoring and Reporting Process**

In its ideal form, the budget is an accounting tool and an opportunity for departments to develop useful benchmarks to which actual results can be compared to goals and objectives developed by the departments during the budget process. Budget monitoring is the departments' and the County's opportunity to review individual departments and funds progress in meeting these benchmarks.

The adopted budget is a plan. As with any plan, it is subject to change from the first day of the fiscal year onward. Budget monitoring by both the departments and Central Finance attempts to manage this plan and mitigate any negative issues such as possible budget exceedances that may arise.

Over the years, the County has instituted best practices regarding budgeting and budget monitoring that has improved our overall ability to identify and address budgetary issues during the implementation phase of the budget during the fiscal year. However, there are issues that need to be addressed and processes that can be improved:

The current budget monitoring process is quite good at identifying individual departments and funds that may exceed their budgeted expenditures or may not make their budgeted revenues. However, in some situations, departments may be hesitant to report to the Budget Division times where they will come in under their budgeted expenditures or revenues. This may be due, in part, to concerns that the budget authority may be needed by the department for some unanticipated use in the latter part of the fiscal year or that future or existing budgets may be reduced by the amount of the anticipated savings. An example of this issue manifesting itself is in the General Fund where the actual year-ending fund balance unexpectedly comes in significantly above the forecasted amount in period 11 of the fiscal year. A portion of this additional fund balance is cost savings by departments that were not previously reported.

Some departments believe that they are justified in exceeding their expenditure budgets if unexpected, unforeseen, or perceived unfair costs occur during the fiscal year. The explanation is often simply that they cannot absorb the unanticipated costs.

Some departments maintain large banks of budgeted but vacant positions with large offsetting attrition amounts which tend to cloud forecasting of actual position related salaries and benefits costs. The large numbers of budgeted vacant positions cause forecasting issues and tend to overstate reports regarding total County-wide salaries and benefits.

Departments with large adopted budgets are not necessarily subject to developing the mandatory budget remediation report required in Policy B of BOS Policy D 22.2 even if they have significant budget variances due to the ten percent exceedance requirement. For example, the Health Department, which has a \$9.7 million net fund impact would not be subject unless it was more than \$970,000 over budget, whereas the Recorder, which has only an \$80,200 net fund impact, would have to comply if she was only \$8,020 over budget.

While situations change during the course of the fiscal year that may impact the department, a department cannot unilaterally decide to exceed its adopted budget authority or net fund impact. Except

under limited circumstances detailed in A.R.S. § 42-17106, any change in a budget cannot exceed the existing overall County adopted budget. That means that an increase in expenditure in one department must be offset by a reduction to another department's expenditure authority.

### **Recommendations**

Given the increasing fiscal constraints facing the County, it is increasingly necessary for all County departments to adhere to their adopted budgets. The following are proposals to improve the budget compliance, monitoring, reporting and remediation processes:

1. All departments, including those managed by elected County Officials, should complete monthly forecasts of revenues and expenditures. Although many of the County's elected officials do provide Central Finance with those forecasts, departments managed by several elected officials historically refuse to do so. We recommend that a report be submitted to the Board of Supervisors on a monthly basis reporting which departments have failed to provide forecasts of revenues and expenditures. For those that fail to do so, Finance should provide, at a minimum, the anticipated expenditures and revenues using a straight-line basis of forecasting and provide any other relevant information available to help the County Administrator monitor the revenues and expenditures for the current fiscal year.
2. Departments should continue to be allowed to shift expenditure authority between budgeted appropriation units within a particular fund. To transfer budget authority between funds, however, even if the funds are within the same department, should require approval by the County Administrator or the Board of Supervisors as required by Board of Supervisors Policy No. D22.8 relating to unbudgeted operating transfers.
3. Because of the budget authorization restrictions of A.R.S. § 42-17106, if a department forecasts to be over its adopted budget in expenditures or forecasts to be under budget in revenues, the department should clearly explain within its forecast reports the individual impact and reasons for the overage or underage by type of expense as well as an explanation of the overage or underage from an overall departmental and fund standpoint. As part of the department's monthly budget report, the department should include the reasons why the department cannot manage other costs to absorb the variances.
4. If a department forecasts to be over budget during a fiscal year (regardless of the amount), it should meet with the Central Finance Department to take actions to bring the department and fund back in line with its adopted budget. A listing of proposed actions that may be taken by the department or the County Administrator for budget remediation are listed in Attachment 4.
5. Section B of Board of Supervisors Policy Number D 22.2 should be amended to have it require budget analysis beginning with the reporting for Period 4 (October) of each year. This will allow additional time to work with particular departments to remediate budget overages by fiscal year-end. In addition, departments should be required to submit a budget remediation plan to the County Administrator for submission to the Board of Supervisors at lower thresholds than what currently is contained in the policy. We recommend requiring a remediation plan if:
  - The negative net fund impact for a particular department fund is five percent more than the budgeted net fund impact, or
  - \$500,000 or greater than the budgeted net fund impact, or
  - If the difference in net fund impact is deemed significant by the County Administrator.

6. The second reporting requirement contained in Section B of the Board of Supervisors Policy Number D 22.2 states:

If at the end of any fiscal year a department's net fund impact was more negative than that authorized by the adopted budget, then the director or officer of that department shall submit a report to the Board of Supervisors prior to September 1 describing what remedial actions were taken to avoid the budget exceedance and why such actions were inadequate.

The Budget Division will be asking departments to explain actual year-end variances from the FY 2012/13 adopted budget and submit a report to you. We recommend, however, that the reporting date discussing the unsuccessful remediation actions taken by a department should be changed from September 1 to November 1 to allow time for any changes resulting from the year-end audit.

7. As part of the creation of the FY 2014/15 requested budget, the dollar amount of vacant budgeted positions should be limited to no more than two percent of the total requested salaries and benefits. The department should be required to submit to the Budget Division details of its plan and schedule for filling any budgeted vacant positions in the requested budget. It is unnecessary to budget for vacant positions with offsets of vacancy savings. If, during the course of a fiscal year, a department requires a new position that is unbudgeted and funding is identified within its existing budget to cover the cost of that position, a new position can be created under Administrative Procedure 22-81.

8. Finance should provide the County Administrator a list of those departments whose audited net fund impact for the previous year exceeds the \$250,000 threshold for consideration of a performance audit under Board of Supervisors Policy D 22.3.

The budget monitoring process relies to a significant extent on the self-reporting of forecasted revenues and expenditures by department directors and by elected officials. Most County departments are more than willing to discuss budget issues and work with Central Finance on their resolution. Continuation of those efforts, together with more transparent reporting of budget exceedances, should improve the County's ability to monitor and manage budget variances as they develop during a fiscal year and enable management to react to mitigate any events or conditions adversely affecting the budget.

c: Martin Willett, Chief Deputy County Administrator  
Hank Atha, Deputy County Administrator for Community and Economic Development  
John Bernal, Deputy County Administrator for Public Works  
Jan Leshar, Deputy County Administrator for Medical and Health Services

Attachments