A Suggested Budget Measure for Local Units of Government in Michigan

CITIZENS RESEARCH COUNCIL OF MICHIGAN

625 Shelby Street (Lower Level)
Detroit, Michigan 48226

909 Michigan National Tower
Lansing, Michigan 48933

Report No. 259

November, 1979

This report has been made possible by a grant from the Relm Foundation established by Harry B. Earhart. Mr. Earhart served as a Trustee of the Detroit Bureau of Governmental Research from 1936 to 1944. The Detroit Bureau was the predecessor organization to the Citizens Research Council of Michigan.

TABLE OF CONTENTS

A SUGGESTED BUDGET MEASURE
FOR LOCAL UNITS OF GOVERNMENT
IN MICHIGAN

INRODUCTION

Governmental budgets can be intimidating documents. They can intimidate the local public official because the budget is the fiscal embodiment of local policies, plans, and potential debacles, as well as achievements. The numbers in the budget have a way of standing on their own, apart from the verbal gloss that surrounds them. They are the unforgiving reminders that, at some point, the public pronouncements, murky as they may be, must be converted into the hard currency of a spending plan.

They can intimidate the taxpayer because he recognizes that somewhere in the budget of his school district, township, city, village, or county, he should be able to find out what is happening to the tax dollars with which he so reluctantly parts company each year. Yet the budget is filled with unfamiliar arrangements of dollars and arcane jargon that often frustrate not only his attempts to get answers to his questions, but even to figure out which questions to ask.

Although local budgeting is not really such an old process (it is almost without exception a twentieth century phenomenon), it is no longer seriously disputed that the annual budget is the single most important document produced by a local unit. The trained observer can find in a well-prepared and presented budget information that exceeds all of the rules, regulations, council minutes, resolutions, and other documents as a source of knowledge about the direction his local government is taking.

If budgets are so important, they must always be carefully prepared and executed according to sound principles, must they not? Regrettably, the answer is no. In its research during the last several years, the Citizens Research Council has identified numerous shortcomings in local budgeting in Michigan that hinder that process in achieving its important purposes.[1] The widespread adoption by local units of sound budgetary practices needs to be encouraged.

The purpose of this document is to present a sample budget ordinance, resolution, or charter provision that may be adopted by local units of government in Michigan. This measure, if adopted, will help to institutionalize budgeting procedures that will result in accountable allocation of local public resources and retention of fiscal stability. It should also enable local units to adopt provisions consistent with the new local budgeting provisions of the Uniform Budgeting and Accounting Act, P. A. 621 of 1973. The sample budget measure is presented in Section IV.

This document would not be nearly as long as it is, however, if only the suggested ordinance were included. A general problem with governments at all levels, thought is that laws are often adopted without a sense of

---

[1] These were documented in Proposed Local Government Uniform Budgeting System, Report No. 251, April, 1977, available from the Citizens Research Council of Michigan.

the intent and “spirit” behind them. Those close to the ordinance at the time it is passed may have a good idea of the reasoning behind each provision but legislative members and citizens are usually faced with little more than the law itself, the purposes of which may not be evident from the language itself. The first two sections of this document attempt to supply a context and rationale for the ordinances in Section IV. In short, these sections attempt to give the “whys” behind the provisions in the sample ordinance. After all, state law has a reason for requiring local units to balance their budgets that is more fundamental than a penchant for tidiness on the part of accountants. And the requirement for city council approval of spending plans amounts to more than just presenting a stumbling block to the mayor. Reasons for these and the other provisions should become clearer after reading Sections I and II. Section III presents a summary of the provisions of Public Act 621 of 1978, the new state Uniform Budgeting and Accounting Act.

Finally, a word about what this document is not intended to be. It is not intended to be a budget manual, replete with detailed forms and procedures. These are required, under Act 621, to be produced by the Michigan Department of Education for local and intermediate school districts and by tile Michigan Department of Treasury for other units of local government.

It is also not a guide to accounting, financial reporting, auditing, program evaluation, or revenue forecasting. All of these are important to budgeting, but go well beyond the scope of the suggested ordinances.

Certainly no two units of government are identical and variations on the suggested ordinance undoubtedly will be desirable, Some small local units with relatively simple budgets may wish to dispense with the allotment provisions. Others may wish to require a position control system. Still others may wish to include a requirement for program evaluation. The proposed ordinance is adaptable to whatever type of budgeting the local unit finds best meets its needs—line-item, object of expenditure, program-activity, zero-based, etc. The Research Council intends this suggested ordinance to be a guide, not an inflexible measure that a local government must take or leave as is.

It is, nevertheless, to be preferred that the basic spirit be retained when alterations in the ordinance are being adopted. The spirit consists very simply of three main points.

> First, someone must be responsible for budget preparation and execution;
>
> Second, the legislative body must sanction the spending plans of the local unit and must sanction, in advance, any deviation from that plan during the fiscal year;
>
> Third, the local unit must not spend more than it takes in.

No unit that follows these basic principles is likely to go far wrong in assuring that its services are adequately financed both now and in the future.

I. THE PURPOSES OF BUDGETING

The traditional definition of a governmental budget is that it is:

> A plan of financial operation embodying an estimate of proposed expenditures for a given period and the proposed means of financing them. (Municipal Finance Officers Association, Governmental Accounting, Auditing, and Financial Reporting, 1968, p. 155)

Hardly anyone reading such a definition could envision the passion engendered by budgeting. The budgetary process is the focal point of all the hopes, plans, designs, and schemes for the use of public funds. Perhaps a hint at the reason for the significance of governmental budgeting can be gained by a quick review of the three purposes served by governmental budgets.

Basic Purposes of the Budget

Budgeting for local units of Government serves exactly the same purposes that it does for any other level of government:

- Allocation of public resources over time and among public purposes.
- Accountability to the public for the expenditure of public funds.
- Maintenance of financial stability of the governmental unit.

Allocation of Public Resources

If the financial resources of a governmental unit were limitless, budgets would be unnecessary. Budgets are the result of the fact that those resources are scarce. Individuals may differ about whether they should be even scarcer than they are, but the point is that some method must be used to parcel out the funds available to a governmental unit.

Allocation Over Time. It would, of course, be possible to simply spend the available money until it runs out and then shut down government until a new batch of tax payments comes in. This procedure is unlikely, however, to catch the fancy of the taxpaying public which expects that governmental services will be available continuously. Thus, budgets are constructed and carried out along the lines of fiscal years in order to apportion government spending over time and assure that governmental services do not come and go according to the cycle of tax collections.

Allocation Among Public Purposes. The more complicated aspect of resource allocation is that of cutting up the revenue pie and deciding how big a slice should go toward the provision of each public service. It has, in fact, been suggested that the fundamental unsolved problem of budgeting is the development of a basis on which public resources may be allocated to one function as opposed to another. Again in the extreme, it would be possible to allocate all of the resources of a governmental unit to one public function such as police protection. Clearly, this would not be popular, for while the streets might be free of crime, they would also be impassable. Budgets are the tools used by government to make sure that even if no public purpose is served completely, none will be completely ignored either.

At bottom, these are political decisions flowing from compromises among the various segments of society that wish to have problems solved or services performed by government. At some point, there is a need to translate these political choices into the spending pattern of the local unit. This translation is accomplished by the budgetary process.

Accountability

Government has the power to take the citizen's money away from him legally. In return, it promises to use that money in a manner which will, it is hoped, benefit the public in some way even if it does not benefit him directly. Budgets, as the plans of government spending, must be constructed so that, after the money is spent, the citizen can go back and obtain an accounting of the expenditure of his tax money.

Accountability is of two kinds. First, and simplest, is the kind that assures that the public's money was spent honestly for public purposes approved by representatives elected to make such decisions. Violation of this standard of accountability is what ordinarily is viewed by the public as fraud or, at best, bureaucratic bungling.

A second kind of accountability is forcing itself into the consciousness of public officials and citizens alike. This kind assures that not only was the money spent on a valid public purpose but also that that public purpose was achieved in an efficient and effective manner. In some instances, it is obvious. If a road is to be built, the actual construction of the road may be enough to answer the question. But, more often, the answer is ambiguous. If crime is to be reduced, how will we know? And if it does go down, which of any number of public or private efforts, including the police, mental health programs, and TV advertising are the cause or causes? Budgeting in recent years has tended more and more to address such issues. Successes have been modest to say the least, but pursuit of this kind of accountability continues.

Maintenance of Financial Stability

Government, like a family, buys some things that it expects to pay for later – sometimes much later. These are sewers, police stations, streets, fire trucks, and a long list of other things that are expected to last and be enjoyed by residents years from now. Because these things are frequently expensive and, more importantly, because they will be consumed bit-by-bit by taxpayers many as yet unborn, it is considered fair to shift a portion of the burden of payment forward to those future taxpayers.

Unfortunately, the practice of allowing our children to pay for our current governmental services is seductive and has a strong tendency to creep into the financing of services which will be totally consumed during the present. Such practice can ultimately jeopardize the provision of governmental services by requiring a unit of government to use a large portion of its current revenues to pay for past services.[1]

[1] The failure to "fund" pension benefits as they accrue can create the same problem in the same way.

Budgets can aid in the prevention of the accumulation of debt by requiring public officials to be continually aware of the relationship between the cost of providing public services and the capacity of the local unit's revenue base to pay for those services.

Conclusion

Budgets are convenient indicators of the managerial performance of local governments as well as of their stewardship of public funds. The budget, while it is definitely a financial instrument, is first of all a planning and management tool and only secondarily an accounting device. When it is handled mainly as a mechanism to set up accounts, it loses much of its utility. Budgets should be informative. They should answer for the taxpayer the following questions:

- How much is spent for each function (or toward each purpose) of the local unit?
- What is being purchased by these expenditures?
- Do the expenditures actually result in the accomplishment of the public purpose they presumably are intended to address?
- Where does the money come from and in what amounts is it available to finance the various local functions?
- What is the fiscal position of the local unit? (i.e., does it have a surplus or deficit?)

The answers to these questions may, in some instances, be imprecise and may also be other than those desired by the taxpayer. Yet, to the extent that the budget falls short of enabling the citizen to gain such information without undertaking a major quest, it falls short of one of its major purposes – accountability.

For most citizens "the" budget is a document that appears annually, occasionally accompanied by commentary in the local press. The budget document, however, is only one part of a much larger continuous process. No real understanding of how budgets perform the purposes noted above can be had without an understanding of the process of budgeting. The next section is intended to supply at least a little of that understanding.

II. THE BUDGETARY PROCESS

As is the case with most administrative procedures, budgeting is fully effective only when reduced to a routine. Routinization, however necessary it may be, has a major drawback – the routine frequently becomes an end in itself. In the great rush to fill out forms, make sure the columns add, and otherwise complete the paperwork, attention is often not given to the reasons for putting together a budget in the first place.

In this section, the bare bones of the budgetary process will be described, but an attempt will be made to point out the ways in which each stage of the process relates to the substance of budgeting namely resource allocation, accountability, and maintenance of fiscal stability.

The Executive Budget

Before proceeding, it should be explained that the budget may originate in either of two places: The legislative body (the board of county commissioners or the township board, for example) or the executive (the mayor or superintendent of schools, for instance). Most experts in governmental budgeting prefer the "executive" budget for several reasons:

1. The executive budget concentrates budget preparation in the branch that collects fiscal information, operates the programs, and ordinarily initiates new policies.

2. The executive budget involves both branches in budgetary decisions rather than allowing the legislative branch to unilaterally determine spending priorities.

3. The executive budget lays the groundwork for fiscal cooperation between the executive and legislative branches after the budget is developed.

4. The executive budget provides for greater accountability through checks and balances that it provides.

In many instances, governmental structures call for legislative development of the budget. In Michigan, county governments typically do not have an executive[2] that can be readily held accountable by the taxpayers for budget preparation.

In school districts, the superintendent is usually responsible for budget preparation but the superintendent is not separately elected thereby removing much of his independence in the budgetary process. City managers are in a similar position.

---

[2] As of this writing, only Oak-land and Bay Counties had county executives (and their powers are limited).

The Budget Cycle

Anyone who follows government or who works in or with government becomes aware of the budgetary cycle. The demands of the process condition much governmental activity. Operating agencies frequently know budgetary deadlines as well as do the finance officers.

Since the process is a "cycle," there is no real beginning or end to it and a description could start with almost any point. At any one time, a governmental unit is dealing with three budget years the current year, the most recently completed year, and the year for which the new budget is being prepared. The cycle is probably easiest to follow and understand, however, if the description begins with the initial development of the budget request for the next fiscal year.

Budget Preparation

The preparation of the estimates for the budget is, in a sense, a continuous task. Estimates of program expenditures and revenue collections usually are made throughout the fiscal year and those that appear in the budget document are frequently not much more than extensions of currently available estimates plus the estimates of costs of new programs or of the revenues from proposed new revenue sources.

Budgetary Policy by Chief Administrative Officer. The executive budget, as presented to the legislative body, is ordinarily the result of some compromise between the chief administrative officer and the executive departments. Typically, the chief administrative officer brings to budgetary considerations a broader view than do the departments. He must take into account not only the competing demands of the various agencies, but also the likely availability of revenue with which to support the programs of the governmental unit.

The chief administrative officer normally will submit an executive budget policy statement to the agencies in order to aid the agencies in developing their expenditure estimates, to place limits on them in making their budget requests, to set the tone for the upcoming discussions with them, and often to indicate underlying budgetary policy to the legislative body. The statement is based on a budget forecast of conditions that will affect the budget either in its total size or in the relative emphasis to be accorded individual programs. (See section 4 of the suggested budget measure.)

Budget Requests by The Agencies. The requests by the agencies will reflect a generally narrower view; than that of the chief administrative officer. On the other hand, the agencies are the repositories of greater expertise in the specific activities of local government and must be expected to be aware in finer detail of the reasons for the size of the budget requests they make.

In larger jurisdictions, an individual department may have a budget office responsible for preparing agency budget estimates. In this event, the agency budget officer may well participate in the budget presentation to the legislative body. This is not common in local government, however. More frequently, the budget estimates of the agency are prepared by an employee who has other responsibilities and thus will ordinarily receive technical help from the fiscal officer of the local unit, who will then represent the executive proposals to the legislative body.

Role of the Fiscal Officer. Especially in larger units, but in smaller ones as well, it is both customary and desirable to have someone responsible for the day-to-day management of budget preparation and execution. In most local units, responsibility for the budget is combined with responsibility for other financial administration. In other jurisdictions there is a budget officer whose sole concern is for the budget.

The fiscal officer has the responsibility of finding the appropriate level of proposed spending in each area that will best accommodate the agency request with the budget policy of the chief administrative officer. He then recommends the resulting budget to the chief administrative officer. Preparation of the budget by the fiscal officer requires that he maintain access to departmental information and that he be able to acquire similar kinds of data from each department. This, unfortunately, necessitates the use of forms to organize and display the data for analytical purposes. Budget forms are frequently viewed as bureaucratic red tape. They are required, however, in order to assure that budgetary data become available at least in consistent formats for comparative purposes, and also to assure that the fiscal officer receives all of the information he requires for preparation of the budget. Agencies tend to be somewhat selective in the data they give to central budget officers and a prescribed format will help to elicit information that an agency might not otherwise have chosen to provide. (See section 6 of suggested budget measure.)

The fiscal officer, in addition to his responsibility for balancing the agency requests with executive policy, must be aware of the needs and demands of the legislative body for information since, in most cases, it is this body which must confer its sanction upon the proposed spending plan before it can be acted upon.

Role of the Chief Administrative Officer

The last section described the role of the fiscal officer in the preparation of the budget. In most jurisdictions, while the actual preparation of the document may be delegated to the fiscal officer, the chief administrative officer is responsible for setting basic budgetary policy and then assuring that the decisions made in preparing the budget actually reflect that policy.

The chief administrative officer also has the key responsibility for transmitting the budget to the legislative body (see next section). Although budget transmittal in itself is not a demanding or time-consuming act, it is important for two reasons. First, it is the formal acknowledgement by the chief administrative officer that this document represents the spending plan that he is prepared to defend, both in total amount and in distribution among the various public purposes detailed in the budget. Second, it is the official beginning of the debate in the legislative body (and among the citizens) that will lead, some weeks later, to passage of an appropriations measure by the legislative body that will sanction expenditures during the next fiscal year.

The transmittal of the budget, therefore, is the mechanism by which the chief administrative officer assumes accountability for the budget.

Consideration of the Budget by the Legislative Body

Approval of the spending plan of the local unit and authorization of actual expenditures based on that plan by the legislative body is fundamental to representative local government in the United States. According to the Michigan Attorney General:

> The authority of each local unit to expend the funds of that unit must be found in the budget and in the appropriations therefrom. Except for funds budgeted and appropriated in accordance with governing law, there is no basis for levying or collecting taxes or otherwise making available or disbursing public monies.[3]

In addition, the procedures developed by the Michigan Department of Treasury under the Uniform Accounting Act or 1968 note that:

> The power of the purse is vested in the legislative body. The law applying to local units provides that no money shall be disbursed from the treasury except pursuant to an appropriation of the legislative body. It is the appropriation measure which serves as the legislative control document.[4]

Finally, Act No. 621, P.A. 1978, the Uniform Local Budgeting Act, requires procedures to assure not only that the legislative body give its initial approval to the spending plan in the form of an appropriation, but also that approval be obtained each time that plan is altered during the year.

In Michigan, the process of supplying legislative sanction to the spending plans of the local unit has been known traditionally as "adopting the budget." The implication is that the budget as prepared by the city manager or superintendent of schools is simply embraced by the city commission or school board and that the legislative body brings little of its own policies or concerns to the approval of the spending plan. There is, nevertheless, more to this important phase of budgeting than is indicated by the phrase "adopting the budget." The importance of the appropriation will be discussed shortly.

1. Presentation of the budget to the legislative body. The form of the budget developed for presentation to the legislative body will depend, in part, upon the degree of independence enjoyed by the chief administrative officer as well as upon the kind of information wanted by the legislative body. However, the chief administrative officer ordinarily supplies a context to the figures in the budget through a budget message to the legislative body (and, incidentally, to the public). The budget message summarizes the budget and emphasizes those items important to the chief administrative officer. (See section 10 of the suggested budget measure.)

   There are ways other than the budget message available to the chief administrative officer to assure the clarity and usefulness of the budget document. Perhaps the most important of these is the level of budgetary detail presented to the legislative body. The quality of legislative consideration and the subsequent appropriation can be enhanced by careful choice of the appropriate amount of information to be considered by the legislative body. A budget

---

[3] Letter opinion, Attorney General Frank J. Kelley to Honorable Allison Green, State Treasurer, January 13, 1970.

[4] Michigan Department of Treasury, Uniform Accounting Procedures Manual for Local Units of Government in Michigan (prepared pursuant to Act No. 2, P.A. 1968), page 4.

that contains only gross totals by department, for example, will provide insufficient information for reasoned decisions to be made by board members, council members, and so on, to say nothing of the interested taxpayer, who may wish to form his own judgment.

Equally self-defeating is the budget, which contains mountains of unaggregated detail describing each proposed purchase of typing paper, pencils, and tires for the police cars. It may be possible after lengthy analysis to put such masses of numbers into a form in which they can be reasonably used for decision-making by the legislative body. Most school boards and city councils, however, are composed of public-spirited individuals who make their livings doing something else and do not have either the time or staffs available to perform such analytical tasks. Thus, the presentation of the budget in fine detail tends to force the focal point of discussion of budgetary issues to a level at which important decisions are either not made or, if they are, are based upon trivial or irrelevant data.

The best interest of the local unit is served when the chief administrative officer seeks that level of detail in the budget presented to the legislative body which is most conducive to informed decision-making. This level may be much different than that in the budget developed for operating purposes during the year.[5] There is no reason, then, why the appropriations of the legislative body need to extend to each tiny item in an operating budget and there are several reasons why they should not:

1. Decisions made by the legislative body based on massive detail are likely to focus on trivial or irrelevant items;

2. Appropriations which involve small items of expenditure that could be included within other items will necessitate excessive numbers of transfers among appropriation accounts as the fiscal year progresses.

3. Taxpayers wishing to understand the uses to which their money is being put, may find a mass of detail without value in helping them to come to grips with the spending patterns of their local unit.

2. Appropriations. Despite its long history in representative government, the appropriation remains the victim of misunderstanding. It is a simple concept and, perhaps because of its simplicity, its importance is frequently understated. It will not be understated here.

The Municipal Finance Officers Association's National Committee on Governmental Accounting (ZICGA) defines "appropriation" as

> An authorization granted by a legislative body to make expenditures and to incur obligations for specific purposes.[6]

---

[5] Different in form, but not different in total or an allocation among purposes or departments.

[6] NCGA, Governmental Accounting, Auditing, and Financial Reporting (MFOA, Chicago), 1968, page 153.

It goes on to note that appropriations are ordinarily made for a specific period of time, although they may be for indefinite periods.

The NCGA definition points up several concepts involved in the idea of an appropriation.

a. It is a legislative function. The executive may not appropriate funds. This is particularly necessary in those units (such as school districts and council manager cities) in which the chief executive is appointed.[7]

   The reason for this can be summed up in one word – accountability. No appointed official is truly accountable to the voters and in those units with elected chief executives, the checks and balances flowing from legislative appropriations are generally considered to provide for sounder, more responsive, and more open financial management, than would be possible under some other system.

b. It is an authorization, not a mandate, to spend. Various legislative bodies may interpret this in different ways, depending to some extent on the kind of program authorized, and may cause the appropriation to be both a floor and a ceiling, or just a ceiling. If the service can be provided more efficiently than originally contemplated when the appropriation was made or if the problem addressed by the program is of lesser magnitude than originally expected, expenditures substantially less than the appropriation will be likely to meet with legislative approval. On the other hand, if the problem is not easily solved or if the amount of money appropriated is intended in part to represent some legislative commitment, the amount appropriated may be viewed as a minimum expenditure. The legislative body may, in such a case, take a dim view of an executive decision to spend less than the appropriated amount.

   In either case, if situations such as a revenue shortfall arise which make it impossible to spend up to the amount of the appropriation, Michigan law for both state and local units calls for a cutback in expenditures to whatever level may be required.

c. It is an authorization to make expenditures or incur obligations. Local appropriations are almost always “fixed” appropriations, that is, they specify a dollar amount which may not be exceeded during the fiscal

---

[7] A few cities in Michigan do, however, have charter provisions which, under certain conditions, permit an approximation of executive appropriation. In these cities, if the city council does not act on the budget before the fiscal year begins, the budget as proposed by the city manager becomes the authorization to spend. With Act No. 621, P.A. 1978, cities may no longer adopt this kind of provision, although existing provisions of this kind may be retained.

year. (State governments and the federal government occasionally use "open-ended" appropriations primarily in grant programs. These kinds of appropriations, which ordinarily depend on a distribution formula, are seldom suitable for use by local units.)

d. An appropriation is for specific purposes. Just how specific those purposes are depends on the size of the unit's budget and the degree of control the legislative body chooses to attempt to exert. A small unit may have a very detailed appropriations measure and find that control by the legislative body is still possible. As the unit's budget grows larger, the legislative body will find it necessary to exercise its budgetary control over increasingly gross aggregations of expenditures if it does not want to be swamped by a sea of trivia.

   The purposes for which appropriations are made may be characterized in either of two ways (or both). The first is the traditional "object of expenditure" classification in which items to be purchased (personal services, equipment, supplies, and so on) form the basis for the structure of the budget. The second is any of several kinds of budgeting methods that have developed, principally since World liar II, to place emphasis on the outcome of public expenditures, rather than upon the "inputs." Program budgeting, performance budgeting, and zero-base budgeting all emphasize this aspect of the process.

   Although students of budgeting often debate the merits of each approach, there is less conflict between the two methods than is commonly supposed. Clearly, even the most program-oriented budget must ultimately provide for personal services and equipment. Equally clearly, those personal services and equipment must be directed at the accomplishment of some public purpose or the solution of some public problem. Thus, the budgets of most value to local officials and taxpayers alike contain elements of each approach and the appropriations that reflect this blend will usually provide for the most effective control and authority to spend.

e. An appropriation is usually (although not always) for a specified period of time, usually the fiscal year. Occasionally, legislative bodies will make continuing appropriations that expire only when (1) the project is completed (such as a capital construction project); or (2) when the legislative body acts to terminate or modify the appropriation. An appropriation may be both open-ended and continuing.

   In summary, an appropriation provides authority, not cash. It simply indicates that, if the money is there, it may be spent in a certain way.

Budgeting Revenues

The budgeting of revenues involves four principal considerations: (1) Amount, (2) Timing, (3) Certainty, and (4) Restrictions. In other words, a unit must know not only how much money it may expect to have available during the fiscal year, but also when it will be received, how certain it is to be received, and whether it will arrive with strings attached.

1. Amount. Depending on the dates of its fiscal year, a local unit may know, with reasonable confidence, how much it may expect to receive from at least certain revenue sources, such as the property tax. If it is operating at rates below established millage limits, it may have fairly direct control over the amount of property tax revenue to be received because the millage rate may be adjusted upward as well as downward in order to produce the desired yield. If the unit is at the millage limit, it is dependent upon growth in its property tax base for increases in the amount of revenue from that service.

   The property tax, as important as it is to local government, is not the only source of revenue. Revenues from other sources tend to be less easily estimated for several reasons. First, the level of activity of firms and individuals determine the base and yield of the tax. For example, income tax revenues depend on the level of economic activity in the city. If that cannot be predicted, estimates of income tax revenue are likely to be off the mark. Further, no unit can foresee exactly how many marriage licenses, dog tags, building permits, or other items which form the sources of fees or charges will be required during a year.

   Second, revenue from other governmental units may depend not only on economic activity (such as the earmarking of state sales tax revenue for local units), but also upon the action of state or federal entities. An adjustment in the school aid formula may have a large impact upon a school district's budget. (See "Certainty" below)

   Finally, since local units are "creatures of the state," action by state government can reduce or expand the revenue from the unit's own sources. A recent significant example of this was the exemption of inventories from the property tax at the time of adoption of the Michigan single business tax in 1975.

2. Timing. It would probably be helpful to a local unit if it received one-twelfth of its revenue each month. Unfortunately, revenue collections are lumpy. State school aid payments are made bimonthly, state revenue sharing payments are made quarterly, property tax collections are received basically once or twice a year, and city income tax revenues fluctuate depending upon the time of year. Fees and charges also show fluctuation depending on such things as building activity (building permits), romantic activity (marriage licenses), or criminal activity (court fees).

   The local unit, then, may have "cash flow" problems attributable to a lack of synchronization between the disbursement of cash and the receipt of revenues. This may be ameliorated, if not completely cured, by a variety of devices including the timing of expenditures, by revenue anticipation borrowing, by the use of any available surplus that may be drawn upon during the year, or, if possible, by attempting to even out the flow of revenues, through administrative or other means.

3. Certainty. Taxes, generally, may be certain, but particular revenues, from both tax and non-tax sources, may be subject to chance. Tax payments may be delinquent, budgetary crises in "banker" governments may cause delays in payment of intergovernmental revenue, or those who are responsible for devising the school aid or revenue sharing formulas may simply not have gotten around to enacting them.

   The budgetary anxiety caused by such problems is especially acute in local government which often is charged with delivering a service (such as education) but has no way of knowing the extent of its permissible commitments at the time the budget is prepared or the appropriations made. There is no easy way out of such a predicament. If the unit commits itself to greater expenditure levels than are ultimately capable of being financed by the actual revenue amounts forthcoming the program may need to be cut back. Conversely, if the unit commits itself to less than actually becomes available, it may subject its citizens to an unnecessarily low level of service. The sage fiscal officer will stay in touch with his revenue sources and attempt to remove as much uncertainty as possible from the estimates of revenue.

4. Restrictions. There are two kinds of revenue: Restricted (or "dedicated") and unrestricted, depending on the use that may be made of them. Such revenues are accounted for by use of a fund structure which is an accounting device established in order to segregate revenues available for particular purposes. There may be any number of funds depending upon how many services receive revenues dedicated to those purposes. There is always a general fund," however, which receives unrestricted revenues. These revenues may be appropriated by the legislative body to any legal public purpose it chooses. It may not exercise such latitude with restricted revenues.

   Ordinarily, revenues are restricted for one of two reasons: First, at some point the legislative body or the state may have concluded that a particular service is so important that future legislative bodies or taxpayers should, not be permitted to allow the level of spending for that service to sink below a certain level, that level being represented by the revenues available from a particular tax, portion of tax, or other source. Federal and state categorical grant programs limit use of the funds to specific programs or activities. So long as there is inadequate motivation to remove this restriction, the revenues will continue to be unavailable for other purposes.

   Second, some governmental services have certain of the characteristics of the market, namely, their costs may be charged back to those who use them and who presumably benefit from them. These are frequently known as user charges. Perhaps the most prominent user charges in Michigan government are the gasoline and motor vehicle weight taxes that help to finance our streets and highways, but there are a great many more including recreation charges and special property tax assessments against property that has benefited from public improvements, among others.

   The existence of dedicated revenues is highly significant to the making of a budget. For one thing, restrictions on the use of revenues tend to condition the spending priorities of the local unit. It is unlikely that unhindered use of revenues would result in exactly the same distribution among purposes as that which occurs with the restrictions. For another, it results, in effect, in a series of separate budgets rather than a single encompassing plan.

The debate over the value of restricted revenues ebbs and flows but never really goes away. Prior restriction on the use of revenues probably has a tendency to distort the spending plan of a jurisdiction and may cause either more or less money to be spent on particular services than is justified by the value of those services. The amount of revenue raised by a tax that would ordinarily provide general fund revenue but which has been dedicated probably bears no relation to the amount required to provide an adequate level of the service it is financing. Moreover, if the service truly is so important, few city councils or township boards will risk the political retribution involved in significantly underfunding the service.

The disposition of user charges is quite a different matter. The provision of certain services such as municipal golf courses, building inspections, and adult "leisure-time" education, in which the benefits are consumed completely or mostly by the user tend to be more equitably financed if they receive little or no general fund revenue. Dedication of user charges serves the dual purpose of assuring that those charges do, in fact, support the services for which the user is paying and, equally importantly, helps to minimize the subsidization by the general taxpayer of services from which he does not benefit.

<u>A Note on Capital Budgeting</u>. Capital budgeting differs substantially from budgeting for current operations.

First, most additions to the capital of a local unit occur over a substantial period of time. By the time plans are made, land purchased, contracts let, construction begun and finished, more than a year is likely to have elapsed. Thus, capital budgeting is multi-year budgeting.

Second, the financing of many capital projects will be spread over a long period of time in recognition of (1) the long life of the building, street, or sewer and (2) the fact that it will be used by future generations of taxpayers. Typically, bonds are issued by the local unit to be repaid over a long period of time, such as thirty years. Thus, the budget must recognize the debt service costs which will recur each year until the debt is amortized. Although it is uncommon in Michigan, it is not unheard of that operational expenditures become financed by the long-term bonds issued to build the project. This is an unwise use of bonding for many reasons not the least of which is its illegality. It forces future generations of taxpayers to pay twice for the operation of a facility – once for the service they receive and once more for the service provided twenty years earlier. The accumulation of such debt can severely limit the future capacity of local Government to provide service. (For a dramatic example, New York City's financial debacle resulted in part from long-term use of capital borrowing to finance operational expenditures.)

Third, the construction of new buildings, bridges, sewers, and other facilities will create expenses over and above the cost of building the facilities themselves. If a new school is built, it must be staffed with teachers, administrators, and custodians; it must be heated, lighted, and provided with water; it must be maintained and insured; and it may occasion other costs to the community that are not so obvious, such as extra police or fire protection, road maintenance, or street lighting. It is, therefore, necessary to take these costs into account in making a capital decision in order that the true cost of the project is within the total financial capacity of the unit.

Finally, the schedule of construction of a capital project seldom conforms to the fiscal year of the local unit and will frequently straddle two or more fiscal years. A budgetary problem is then created in which the local unit must decide whether to appropriate on a continuing basis or whether to appropriate a sum each year that will permit that year's work to be completed. A strong argument exists for making one single appropriation and then, basically, ignoring the fiscal year as far as multi-year projects are concerned. In the first place, many large projects are bond-financed and the proceeds from the sale of the bonds are limited to financing that particular project. Thus, reappropriation of those funds each year is wasted motion. (However, the status of each project should be reviewed as part of the annual budget process.) Second, a single appropriation tends to assure that the total project can be completed since future payments to contractors are already authorized. A structure partly completed and never finished is not only a waste of taxpayers' money, but also a monument to poor financial planning.

The Balanced Budget

A "balanced budget" seemingly is viewed by some as the ultimate objective of the budgetary process. It is unquestionably important, but some explanation of the concept may help to put its importance in perspective. That perspective should show that a balanced budget is not the ultimate end of the process but is, in the long run, vital to it.

What's Wrong With Deficits?

A deficit interferes with the ability of the budget to perform each of its three basic tasks.

Allocation of Resources. The most basic budgetary task of all, the allocation of the local unit's resources among competing purposes, is hindered by a deficit. To the extent that expenditures must be made to pay for prior years' services, the latitude of the unit to respond to current needs is reduced.

Accountability. The budget as presented to the legislative body and the appropriations measure passed by the legislative body must be balanced. Moreover, when a deficit appears likely, steps must be taken to reduce expenditures or increase revenues. Despite these requirements of Michigan law, it is no secret that expenditures may be deliberately underestimated, revenues deliberately overestimated, and actual expenditures and revenues incompletely reported. This gives rise to the comment that it is possible to "outlaw deficit budgets, but not budget deficits." Unfortunately, deficits tend to occur as a result of spending decisions that take place out of public view. Often, by the time it is clear that a deficit has been incurred, the causes and responsibility have become blurred and accountability suffers.

Second, even when a local government is in a deficit position it must still pay its employees, its contractors, and its creditors. To do this it must borrow from some institution or it must go to the state or federal government for a grant to cover its deficit and permit it to remain solvent. In either case, the local unit runs a strong risk of losing a part of its independence and with it a degree of local accountability. The private creditors or "banker" government may exact from the local unit agreements to use its money in certain ways, to organize itself differently, or to submit to closer scrutiny in exchange for the loan or grant. Thus, the latitude of action and the ability to respond to the needs of local citizens may be restricted in favor of carrying out the mandates of other institutions.

Fiscal Stability. While a deficit may represent a short-term, non-recurring problem, a deficit that is the result of the gradual divergence of the fiscal capacity of the local unit from the level of services it has chosen to provide represents a serious long-term problem. The divergence may be the result of a deteriorating or slowly growing revenue base or it may be the result of high levels of services or excessive unit costs brought on by such things as high personnel expenditures. In either case (low revenues or high expenditures), the level or cost of services and the capacity to finance those services must be made compatible.

Finally, as a matter of simple equity, the notion of shifting the burden of paying for governmental services that are provided today forward to future taxpayers is difficult to support unless it can somehow be shown that they Hill have a great enough share of benefits to justify this sort of arrangement. It is plainly not easy to defend double payment for the same service – one payment for service rendered in the present and one payment for the same service provided in the vast.

Budget Stabilization Funds

It is possible, under Act No. 30, Public Acts of 1978 for Michigan cities, villages, and townships to create budget stabilization funds (or, as they are commonly called, “rainy-day” funds) which may be used to accumulate revenues to cover deficits, maintain services in the face of a revenue shortfall, and pay for emergency expenditures. Such funds cannot exceed 15 percent of the unit’s “most recent general fund budget, as adopted, or 15 percent of the average of the municipality’s most recent general fund budgets, as amended, whichever is less.”

Conclusion: The Balanced Budget. Although a balanced budget is not the end of the budget process, a unit of government that expects to exist as an independent, vigorous entity for any length of time must take firm steps to retain a condition in which the operating expenditures do not exceed revenue available to finance those expenditures. For this reason, it is illegal for units of government to budget a deficit or to appropriate more than can be supported by anticipated total revenues.

Execution of the Budget

The term “execution” has overtones of precision and finality that tend to misrepresent the actual process of administration of the spending of a local ‘unit. Basic execution of the budget consists generally of three functions (allocation, allotment, and adjustment). These functions depend upon the development of a suitable financial accounting and reporting system which will not be discussed here.

1. Allocation. The first step in administering the budget is that of dividing the appropriations among the various objects of expenditure and establishing accounts that will enable subsequent expenditures to be attributed or “charged” to the proper purpose (appropriation) clearly a fundamental step in maintaining accountability. There may be a significant difference between the amount of detail contained in the legislative appropriation and that needed by the executive to properly execute and control the budget. For example, the legislative

body may choose to appropriate lump sum amounts for specific programs or activities. The executive may find it necessary for budgetary control purposes to break these lump sums down into specific budgetary accounts by object or sub-object of expenditure.

The budgetary metals must agree with the appropriation accounts, and although the executive is free to make transfers among items <u>within</u> appropriation accounts, approval of the legislative body must be obtained before transfers may be made <u>between</u> appropriation accounts. If the legislative body has passed an appropriation measure chat simply "adopts the budget," perhaps with some amendments, the establishment of accounts based on the appropriation will be a reasonably mechanical process (providing that the budget was properly constructed in the first place). The local unit in Michigan has a readily available guide in the form of the <u>Uniform Accounting Procedures Manual for Local Units of Government in Michigan</u>, prepared by the Michigan Department of Treasury.

If the legislative body has, on the other hand, passed an appropriation measure which contains categories too broad to be used for administration, an additional effort will be necessary in order to assure that the appropriated monies are properly allocated and follow the intent of the legislative body (to the extent that intent can be determined). In cases such as this, the flexibility of the executive may be enhanced (it may be up to the executive, for instance, to determine whether two police cars or a new computer would best serve the interests of the city).

2. <u>Allotment</u>. Allocation is the spreading of appropriations among objects and activities; <u>allotment</u> is the spreading of appropriations over time.

   Allotments are useful in assuring that money is available when it is needed. Emergencies aside, two spending patterns may cause an account to be exhausted prematurely. First, recurring expenditures may be made at a higher rate than planned, thus exhausting the account. Second, the expenditure may be planned for late in the fiscal year, thus leaving the account with large balances during most of the year. Without an allotment schedule, it might be wrongly assumed that those balances are available to be transferred to other accounts. Allotments are intended to prevent premature exhaustion of an account, but it is not necessary to adhere slavishly to them since it is only required that the accounts not be overspent in total rather than at given points during the year.

   Allotments are put into effect by means of an allotment schedule which is nothing more than a matrix created by listing the accounts down one side and time periods across the top of a table. Completing the allotment schedule frequently requires nearly as much analysis and foresight as the development of the budget. As a result many local units simply do not engage in this exercise. Nevertheless, a large unit with many active accounts will find it indispensable.

   Allotment of appropriations for personnel costs has a way of taking care of itself. Most employees are paid biweekly or semi-monthly so that the "pay period" forms a reasonably natural basis for allotting personnel costs over a fiscal year. Certain other costs, such as equipment or contractual services, may not fall into this cycle as neatly, but since salaries, wages, and fringe benefits absorb three-fourths of most governmental expenditures a good share of the allotting of appropriations can be approached in this way.

In preparing an allotment schedule, however, a fiscal officer may at times be tempted to seek the services of a fortuneteller. There must be an awareness of when certain expenses are likely to be incurred. As a simple example, allotting funds for snow removal in June would evidence a lack of thought about the process. But most problems are not that obvious. The fiscal officer is asked to peer through the mist of the next twelve months and create an allotment schedule that will take into account seasonal hiring patterns, a projected increase in health care insurance premiums, severance pay for three highly paid employees who are retiring, and other likely expenditures that may occur in an irregular fashion.

Allotments are also useful in assuring that the local unit makes the most of its "cash flow." If, for example, allotments of expenditures and revenues indicate that the unit will have a sizable cash balance for a period of time, investment of that cash may be planned appropriately. Conversely, if the allotment schedule indicates that the unit will be short of cash for a period, steps may be taken well in advance either to deter expenditures, accelerate the collection of revenue, or to assure that borrowed money is available when needed.

Ideally, the allotment schedule will provide for the expenditure of the last dime of each account at exactly the proper time. Reality tends to destroy even the most carefully planned allotment schedule. Unplanned expenditures, unexpected efficiencies, and any of a number of other factors will cause actual expenditures to vary from the plan as the fiscal year wears on. The next section indicates what can be done.

3. <u>Adjustments</u>. Assuming that the total expenditures of the local unit are not outpacing the revenues available to finance them, two principal alternatives are available to the local unit in order to assure that expenditures are not made from exhausted accounts. <u>Both alternatives involve the legislative body and both are performed better if the allotment process and financial reporting system operate effectively.</u>

    a. <u>Transfers</u>. Ordinarily, the disbursements from some accounts occur at a faster rate than expected. A number of reasons for this exist – planning may have been inadequate, an emergency may have arisen, unexpected price or wage increases may have occurred, or (although it is seldom discussed in polite circles) there may have been bureaucratic inattention to the budget and the allotment schedule.

    At the same time, other accounts may be developing substantial balances. Efficiencies may have been discovered, a new program may have experienced delays in becoming operational, or anticipated demand for a service may not have materialized.

    Whatever the reasons, some accounts may have been drawn down to a point at which they are 60 percent gone with 50 percent of the fiscal year remaining. Transferring the authority from one or more accounts that are underspent to one or more that are overspent is a way of curing this problem. Under Michigan law, unless the legislative body has given its prior approval in the general appropriations measure for transfers between appropriations, the executive must seek approval by the legislative body for all transfers.

The quality of financial reporting is important to the success of the transfer of money from one account to another before the account that is running low is exhausted. Under the Michigan Uniform Budgeting and Accounting Act, expenditures may not be incurred against an appropriation account in excess of the amount appropriated by the legislative body.

b. Supplemental Appropriations. The supplemental appropriation is much like the transfer except that no program is required to give up spending authority in order to provide more authority for another. Supplementals may be financed when current year revenue exceeds original estimates in amounts great enough to finance increased appropriations.

   Unlike transfers, supplemental appropriations enlarge the entire budgetary authority of the local unit. Transfers simply rearrange it.

For obvious reasons, adjustments to the budget become substantially more difficult if they take place in anticipation of a budgetary deficit. While neither a diminution of public services nor an increase in taxes is popular with most public officials, adjustments become progressively more difficult as time passes. Although the size of the required increase in revenues or reduction in expenditures may not change, it becomes a larger and larger proportion of remaining expenditures or revenues during the fiscal year. Thus, a would-be-minor adjustment in the first quarter becomes, if neglected, fiscal disaster in the fourth.

a. Expenditure reductions. Numerous considerations eater into any decision to cut back expenditures. At this point, only three will be discussed.

   First, a politically popular (or, perhaps, less unpopular) method is to simply make an across-the-board percentage reduction in every account, or in every account except certain sacred ones. This creates an image of evenhandedness and does, at least, retain the same expenditure pattern that was originally adopted by the legislative body in its appropriations act.

   Second, less popular, but probably more rational, is a selective reduction in appropriations based on changing needs and on the relative effectiveness of each program. Services could be reduced according to expected need for them based upon evidence more recent than that available at the time the appropriations were made. In addition, an opportunity is created to eliminate or reduce programs not living up to expectations, either because of excessive costs or inadequate performance. Many observers, in and out of government, view this as the silver lining to budgetary clouds.

   Third, reductions in certain services may entail corresponding reductions in revenue. This is particularly evident in those programs funded in part by other “banker” governments. If fifty percent of a service is funded by the state government under a so-called “matching formula,” for example, for every one dollar reduction in local revenue applied to that service there will be a two dollar reduction in total revenue available to finance that service. It is, therefore, frequently to the advantage of the local unit to trim those programs financed wholly or largely from local sources. It should be recognized, of course, that this may mean a distortion in the spending priorities of the local unit if important locally-financed services are cut in order to preserve inter-governmental revenue available for low priority services.

b. Increased income. Generally, there are three ways to solve a budget crunch by increasing income.

First, and by far easiest, is to simply raise the estimate of available revenues. This has an obvious surface attraction and is certainly appropriate if the estimate proves accurate. If it does not, the unit will have done nothing more than to trade a short-term problem for an even more severe long-term problem and, if a deficit occurs, it will have drifted into legal tangles as well.

Second, the unit may be able to increase its revenues from taxes, non-tax sources (such as fees and charges), or from other governmental units, provided they are willing to cooperate. Tax revenue can be increased either (1) by raising the tax rate (or, similarly, by increasing the base in some way) or (2) by accelerating the flow of tax revenues to the unit by changing due dates or by similar methods.

Third, the local unit may borrow money. This approach, of course, does not increase revenue (financial capacity) but does increase income and can therefore be useful for short periods. Ordinarily, this is accomplished by the use of tax anticipation notes authorized by Chapter IV of the Municipal Finance Act[8] which states, in part, that:

> Any municipality (virtually any local unit in Michigan – ed.] may, by resolution of its governing body, and without a vote of the electors, but subject to the prior permission of the [Municipal Finance] commission, borrow money and issue its notes in anticipation of the collection of the taxes and other revenues prescribed by this chapter for its then next succeeding fiscal year, or the taxes or other revenues f or a current fiscal year . . . [9]
>
> Where the money so borrowed is for operating it shall be used only for the purpose of paying such necessary operating expenses of the municipality as could not reasonably have been foreseen and adequately provided for in the tax levy for the then current fiscal year. The amount permitted to be so borrowed for this purpose shall not exceed 50 percentum of the operating tax levy for the current fiscal

[8] Act No. 202, Public Acts of 1943.

[9] This same general provision applies to revenue sharing as well, except the amount borrowed may not exceed 50% of the total payments received in the last preceding fiscal year.

> year, or if the operating tax levy for the next succeeding fiscal year shall have been determined, then 50 percentum of such levy.

Thus, a mechanism has been provided to permit a local unit to meet fiscal emergencies or to deal with temporary budget imbalances.

Borrowing, naturally, has its costs. It requires time to prepare the necessary legal documents, gain the approval of the Municipal Finance Commission, and "go to market." More importantly, there are interest costs to be paid and the reality that a portion of next year's revenues will have to go for this year's services with the problems that is likely to create.

If it costs so much, why not just run a deficit and forget about tax anticipation notes? From the point of view of many government officials, the answer is that a deficit should be run, especially if there is an "emergency" (i.e., ice storms, civil insurrection, and the like). From the point of view of both the taxpayer and the state, the answer is perhaps a little different. First, it is illegal. Beyond this basic consideration, although a deficit may, in fact, represent only a temporary condition, it often indicates problems that run deeper than broken water mains. The necessity of borrowing and gaining the required Municipal Finance Commission approval for doing so is a means of assuring a review of the local unit's financial affairs in order to ascertain the nature of the problem that engendered the need for borrowing, If the problem really is solely the result of an unexpected event that is unlikely to recur, this can be determined. It is possible, however, that the unit has drifted into a situation in which the revenue structure is simply inadequate to support the cost of services provided. In such an event, the unit can be advised as to appropriate means to restore balance, or may actually be forced to do so.

Sanction of Changes in Spending Plans by the Legislative Body. The original spending plan must be approved by the legislative body; it follows that changes in that plan must be similarly approved before deviations from the original may be carried out. The executive should not be in a position of being able to use the original grant of authority as license to make whatever changes appear necessary.

Specifically, prior legislative authorization of deviations should be required in the following situations:

- When authority to spend is to be transferred from one appropriation account to another.
- When authority is to be increased in an appropriation account.
- When authority is to be reduced in an appropriation account.
- When the purpose of an appropriation is to be altered.

Emergencies. A serious question arises in the case of "emergencies." Emergency expenditures in the ordinary understanding of the term, are considered to be unplanned, unavoidable expenditures arising from a required public response to natural disasters, civil insurrection, accidental destruction of vital public property (e.g., water mains or streets), epidemic diseases, and other immediate threats to public safety, health, or welfare. There is, in such instances, little question that government must act, must incur the expenditures that permit such action, and should not be overly concerned with the niceties of established budgetary practice. Some carry the argument further, however, to the point of using an emergency as justification for abandoning, at least temporarily, the requirement that the legislative body give its prior approval to changes in appropriated spending limits.

This argument involves a *non sequitur.* The fact that an emergency forces a governmental response does not mean that the executive should be given a blank check by the legislative body. It is difficult to conceive of an emergency so vast that the legislative body cannot be convened, persuaded of the seriousness of the situation, and, finally convinced that more spending authority is necessary in certain accounts. If the situation is truly an emergency, it is almost certain that the legislative body will act to provide the authority. If the legislative body cannot be persuaded, perhaps the situation is not quite as critical as that portrayed by the executive.

The problem is compounded when resources are employed to quell an emergency, thereby incurring an <u>obligation</u> that must be satisfied later. If the police have worked overtime during an emergency, the expenditure will have to be made, if not immediately, certainly at some point during the fiscal year. Thus, the latitude of the city may be narrow, but the latitude that exists should belong to that body, not the executive. In any event, <u>before</u> the account is exhausted the necessary transfers or supplemental appropriations should be made. If the emergency is so great that a budgetary deficit is imminent, borrowing authorized by the Municipal Finance Commission is available.

A Note on Budgetary Control

A budget, as a financial and program plan, is without much value if means are not employed to assure that the plan is adhered to. The basic requirements for adjusting the budget as the year progresses are noted above. However, those adjustments actually represent a failure of the plan in either of two respects:

1. The original estimates of revenues or required expenditures were wrong; or
2. The estimates were accurate, but because of lack of control over expenditures, more was spent than planned (appropriated).

The first problem (inaccurate estimates) is a “failure” only in the sense that things do not work out exactly as predicted. There are always adjustments required during the year. But, these adjustments can be kept to a minimum by eliminating unnecessary account overruns by means of internal procedures to ensure “budgetary control,” or the enforcement of appropriation (and allotment) limits.

The existence of budgetary controls recognized the general role of the governmental budget as a substitute for the profit motive that disciplines private firms. Budgetary controls are intended to counter the apparent tendency of governmental agencies to exceed their appropriations limits.

The necessity for controls would be greatly reduced if:

1. There were a "memory" that "remembered" not only actual expenditures, but also <u>commitments</u> to make expenditures at some point in the future;

2. All those with the authority to incur obligations knew what others with similar authority were doing.

In fact, of course, devices have been developed to substitute for the absence of the above virtues. These controls, if employed seriously, should remove much of the need for adjustments in the appropriations of the local unit and limit those to the adjustments required to remedy the lack of 20/20 foresight.

Two methods of control that have been developed are:

1. <u>Encumbrances</u> Very simply, an expenditure account is "encumbered" if the spending authority in that account is reduced at the time an obligation is incurred rather than when the expenditure is made. Let us suppose that a city intends to purchase a fire truck that costs $60,000. It may place the order for the truck in August for delivery the following February. If there is no way of noting the obligation to spend the money on that fire truck, many months may go by during which the appropriated spending authority in the equipment account for the fire department is artificially high but still may legally be drawn upon. The opportunity for overspending the account obviously exists. Most units of government should not simply rely upon the memory of the purchasing officer or the finance director to assure that the authority in that account is available when the shiny new pumper is delivered.

   If encumbrances are used by the governmental unit, the authority in the appropriation account would be reduced by $60,000 at the time the fire truck was ordered. When the city actually agrees to accept the truck and pays for it, the encumbrance is removed ("liquidated") and the account is charged with an expenditure.

   In a similar manner, salaries and wages accounts and contractual services accounts may be encumbered in order to prevent over-expenditure. The projected salaries of current employees may be deducted from the appropriation authority in a salaries account at the beginning of the year and as new employees are hired the projected salary for each new hire to the end of the year is deducted. Likewise, as old employees leave, their remaining salaries may be added back to the "unencumbered" appropriation (assuming that their departures were unplanned).

   (Accountants will notice that this procedure differs from accrual accounting in which "accounts payable" and "accounts receivable" are established to recognize the "accrual" of liabilities and assets. So-called "encumbrance accounting" is basically a control device, not an accounting approach.)

2. <u>Internal Budget Reports</u>. Reports prepared monthly or quarterly on the status of either budget or appropriation accounts may be used to anticipate shortages in those accounts or to identify accounts that are developing balances that may indicate that either policies are not being carried out or that there may be appropriation authority available for transfer in later months.

These reports, since they are not intended as financial statements, may be produced in as much or as little detail as is useful and need not relate to every account. Certain very active, very large, or very unpredictable accounts may be highlighted. Generally, however, such reports should contain at least the following:

(1) Original appropriation (or allocation)

(2) Allotment for period covered by report

(3) Allotments year-to-date

(4) Any adjustments to 1, 2, or 3 (supplementals, transfers)

(5) Expenditures and encumbrances for period

(6) Expenditures and encumbrances year-to-date

(7) Differences (+ or -) between allotments and actual expenditures plus encumbrances

(8) Unobligated balance in account

(9) Estimated expenditures during remainder of year

(10) Difference (+ or -) between unobligated balance and estimated expenditures during remainder of year.

A few words of warning about internal budget reports are necessary. First, they are only as good as the information that goes into them. If department heads, personnel officers, or purchasing officers are not reporting transactions on a timely basis, the information in the reports will be misleading and they will quickly lose their usefulness and credibility. And, it must be observed that department heads, particularly in larger jurisdictions, frequently perceive advantage in submitting data for use by central budget authorities on a "selective" basis during the year saving some real, and often unpleasant, surprises for the last month or two of the fiscal year.

Second, the reports are only informative and are not self-executing. Experience has shown that those Governmental units in which finance officers use them in discussions with department heads and others who either have authority to spend the unit's money or who make decisions affecting expenditures, have the most success with internal budget reports.

Finally, internal budget reports can appear too often. For example, there may be little to be gained from producing them during the first quarter of the fiscal year. Further, the changes from month to month may be so slight that trends go unnoticed. Quarterly reports may show in greater relief the changes that may result in problems at the end of the year. One solution might be to provide only quarterly reports for the first half of the year and monthly reports for the last half.

Other Controls. Other methods of controlling expenditures exist. Position Control systems may be established in which procedures are set up to account for each position, to indicate whether it is filled or vacant, and to ensure that employment commitments do not exceed the amounts budgeted by position or class of positions. Purchase and requisition approval by a purchasing officer or the finance officer is a method by which proposed purchases are funneled through a central point in order to ensure that the proper account is being charged and that there is an unencumbered balance in the account sufficient to support the proposed purchase.

Auditing

The circle is complete when, after the end of the fiscal year, the books are "closed" (i.e., revenues and expenditures are no longer attributed to that fiscal year) and an audit is made. There are numerous forms of auditing and it is beyond the scope of this report to describe them. Auditing is, nevertheless, important to the budgetary process:

1. Auditing assures that future budgets can rely upon accurate data and that the financial position of the community is as it is portrayed by the financial reporting system.
2. Auditors' recommendations can assist budget officials in substantive areas by indicating inefficiencies or mismanagement of funds or programs.
3. Auditing can promote an objective view of financial and program operations that may provide information useful in forming the budget.
4. Finally, to the extent that auditing includes "performance" auditing to determine the degree to which each service or program was successful in meeting its objectives, such information can assist in the determination of spending priorities for future years.

The Cycle Begins Again

Long before the fiscal year has ended and the books have been closed, the budget is being prepared again for the next fiscal year. In large measure, the quality of the new budget will depend upon the quality of the old, since budgets tend to be incremental, even in jurisdictions that profess to have adopted "zero-base budgeting." Abrupt changes are seldom visible in the budget of any governmental unit. Such inertia may frustrate those who wish to rearrange the spending pattern of their local government but, at the same time, it contributes to the stability and continuity of local government.

III. SUMMARY OF THE MICHIGAN UNIFORM LOCAL BBDGETING ACT

(Act No. 621, Public Acts of 1973)

Until 1978, Michigan law relating to local government budgeting consisted primarily of scattered statutory provisions and a number of court decisions and rulings by the attorney general. Most dealt with property taxation rather than budgeting in particular. The exceptions to this were specific statutory budgeting provisions related to charter townships and fourth-class cities. These units together constitute less than 2 percent of the total number of governmental units in the state. Thus, for nearly all local governments there were no state-wide rules for budget preparation and execution, the result of which was an array of procedures that would confuse the most diligent student of local government budgeting.

Moreover, the basic principles of budgeting discussed in Sections I and II were frequently not observed either in local legal provisions or in actual procedures. During the past several years this wide variety of procedures, at times inadequate, has come to the attention of the state. First, a large number of laws has been enacted providing for special financial assistance for local governmental units (usually school districts). These laws may have given aid directly to one or a few units; or they may aid all units in order to provide relief to a few; or they may provide increased taxing power for one or more local units.

Second, the uninformative character of many local budgets has led many taxpayers and legislators alike to the conclusion that accountability of local units was not being served by their budgeting processes.

The culmination of these concerns was the passage of Act No. 621, Public Acts of 1978. This act amends the Uniform Accounting Act (the new title of which is now the Uniform Budgeting and Accounting Act) to provide for a system of uniform procedures to guide the preparation and execution of budgets in all local units of government in Michigan.

General Concepts

The basic concepts embodied in the act are:

1. Someone must be responsible for preparation of the budget.

2. The budget must be balanced when presented to the legislative body and the legislative body must pass a balanced appropriations act. Expenditures and revenues must be adjusted, if necessary, during the fiscal year to assure that expenditures do not exceed revenues.

3. No expenditure may be made without the authority of an appropriation nor may expenditures from an appropriation account exceed the amount appropriated.

4. The chief administrative officer or fiscal officer may not execute transfers between departments or funds without approval of the legislative body. The legislative body may, if it chooses, permit transfers within limits it sets in the general appropriations act without prior approval.

Specific Provisions

The specific provisions of the act may be described under three main headings:

1. Coverage. The act applies to all units of local government in Michigan. It includes units (such as counties) which are not covered by the other provisions of the Uniform Accounting Act. Specifically "local unit" is defined as:

   "(a) A village
   (b) A city
   (c) A local school district
   (d) An intermediate school district
   (e) A township
   (f) A county
   (g) An authority or organization of government which may issue obligations pursuant to the Municipal Finance Act and which either may levy a property tax or may expend funds of the authority or organization."

2. Procedures to assure accountability. Accountability in local government budgeting is required in three basic ways. First, the chief administrative officer is given responsibility for preparing the budget, presenting it to the legislative body, and controlling expenditures under the appropriations act. (Clearly, the activities involved in budget preparation may be delegated to a fiscal officer, but the chief administrative officer retains final responsibility.) If the local unit has not elected or designated a chief administrative officer, the fiscal officer is to perform these functional.[10] Department heads and other administrative officers must comply with requests of the fiscal officer for budgetary information.

   Second, there are minimum informational requirements established for local budgets. The data required include:

   (1) From prior fiscal years
   - the amount of accumulated surplus or deficit

   (2) For the most recently completed fiscal year
   - expenditure and revenue data

   (3) For the current fiscal year
   - estimated expenditure and revenue data

   (4) For the ensuing fiscal year

---

[10] If the local unit has, by law, charter, ordinance or resolution, designated someone else to be responsible for budget preparation and execution, the act allows for such variations.

- estimate of required expenditure amounts, including those for budgetary centers[11]
- estimate of revenues, by source
- estimate of amounts needed for deficiency, contingent or emergency purposes
- estimate of amounts needed for debt service
- amount of proposed capital outlay expenditures (except those financed from funds noted in (5) below), including for each project:

    (a) Total cost
    (b) Proposed method of financing
    (c) Projected annual operating costs*
    (d) Method of financing operating costs*

(*Required for three years beyond budget year as well.)

(5) Informational summary for capital improvement funds which are not required to be covered by the appropriations measure.

Third, approval of planned expenditures by the legislative body must be obtained by means of a general appropriations act that is consistent with the uniform chart of accounts prescribed by the Department of Treasury or the Department of Education. Equally as important, deviations from the original appropriations act may not be made without first amending the act. This means that:

(1) Transfers between funds or departments must receive specific prior approval by the legislative body. The legislative body may, however, in the general appropriations act, give blanket prior approval to transfers within stated limits.

(2) Either a transfer or a supplemental appropriation by the legislative body is required to permit expenditures to be incurred against an appropriation account in excess of the amount of the original appropriation.

(3) Expenditures may not be inconsistent with the purposes specified by the legislative body in the appropriations act.

3. Procedures to assure fiscal stability. Fiscal stability, as evidenced by a balanced budget, is encouraged by the act through three separate provisions.

First, in the budget as submitted to the legislative body, expenditures, including an accrued deficit, may not exceed expected revenues, including an available unappropriated surplus.

---

[11] Budgetary center is defined by the act as “a general operating department of a local unit or any other department, institution, board, commission, agency, office, program, activity or function to which money is appropriated by the local unit.”

Second, the legislative body may pass a general act or a subsequent amendment to that act which causes estimated total expenditures, including an accrued deficit, to exceed total estimated revenues, including an available surplus.

Third, the legislative body must take steps to amend the general appropriations act, as necessary, to assure that expenditures do not exceed available revenues. If it becomes apparent to the chief administrative officer or fiscal officer or to the legislative body "that actual and probable revenues from taxes and other sources in a fund are less than the estimated revenues, including an available surplus upon which appropriations from the fund were based, the chief administrative officer or fiscal officer shall present to the legislative body recommendations which, if adopted, would prevent expenditures from exceeding available revenues for that current fiscal year." These recommendations are to include reductions in appropriations, increases in revenues, or both.

Implementation and Enforcement

The Departments of Treasury and Education are instructed to publish suggested (not required) manuals, forms, and operating procedures designed to take into account the varying sizes and kinds of local units. The Department of Education is to provide this service for local and intermediate school districts, while the Department of Treasury is to provide them to all other units of government.

These departments, together with the Attorney General, are responsible for enforcement of the act. Violations disclosed by audits are to be reported by the Department of Treasury or, in the case of school districts, by the Department of Education to the Attorney General who is to "initiate appropriate action against the chief administrative officer, fiscal officer, administrative officer, employee, or member of the legislative body."

During 1979, the Departments of Treasury and Education will prepare and distribute suggested manuals, forms, and operating procedures. The remainder of the act becomes effective on April 1, 1980, and applies to any local fiscal year beginning after December 31, 1980.

IV. SUGGESTED BUDGET MEASURE WITH ANNOTATIONS

This section includes a suggested budget measure. It may be adopted with appropriate modifications by a city, village, township, county, or school district. It can be an ordinance if the unit has authority to adopt ordinances or it may be a resolution. In the case of home rule cities or counties it could be employed as the basis for the budget provision of a charter.

The Research Council has taken care to assure that the measure suggested in this section is consistent with state law, but due care should be taken by any unit of government adopting this measure or a modification of it to assure itself that it meets all applicable legal standards and is consistent with other local laws and charter provisions.

The measure assumes that the unit has a chief administrative officer (mayor, city manager, superintendent of schools, and so on). Some units, principally counties that have not adopted either a charter or the optional unified plan, do not have a readily identifiable chief administrative officer. For these units, the fiscal officer should assume the budgetary responsibilities outlined in the measure as required by state *law* an the effective date of Act 621, P.A. 1978 (April 1, 1980).

In writing this measure, an attempt has been made to note those places in which local units are likely to vary from each other. These are indicated by (_________) and the appropriate general entry such as "chief administrative officer" (mayor, county executive, etc.) or "legislative body" (city council, board of county commissioners, etc.). Also, required deadlines for each stage of the process will vary depending on the complexity and size of the unit's budget as well as upon the date of the first day of the fiscal year. These points are indicated as well.

Moreover, the measure would, if adopted, establish basic budgeting provisions. A unit may wish to adopt other financial management procedures related to budgeting such as position control systems or sophisticated financial reporting systems. These may be more a matter of necessity than of choice as the local budget grows. The measure suggested here, however, is, with the exception of the section on allotments, to be considered as a minimum and one that could be adopted by any unit, large or small.

BUDGET ORDINANCE (RESOLUTION)[12]

AN ORDINANCE (RESOLUTION) to establish a budget system for (Name of local unit); to define the powers and duties of the (city, township, village, county, school district[13]) officers in relation to that system; to provide that the fiscal officer shall be furnished with information by the departments, boards, commissions, and offices relating to their financial needs, receipts and expenditures, and general affairs; to provide for an annual appropriation measure; to prescribe a disbursement procedure; to provide for an allotment system; and to provide remedies for refusal or neglect to comply with the requirements of this ordinance.

THE (Legislative body, Name of local unit) ORDAINS (RESOLVES):

SECTION 1. Title.

This ordinance shall be known as the (Name of local unit) Budget Ordinance (resolution).

SECTION 2. Fiscal Year.

The fiscal year of the (local unit) shall begin on (January 1, April 1, July 1, October 1) in each year and close on the following (December 31, March 31, June 30, September 30).[14]

SECTION 3. Fiscal Officer.

The (Title of designated official) shall be the (local unit) fiscal officer[15] and shall perform

---

[12] For units of government that may adopt ordinances, it is preferable that this measure be passed as an ordinance rather than as a resolution since it contains a penalty provision and it is intended to be a permanent part of the procedures of the governmental unit.

[13] For home rule cities and charter counties, this measure could be the basis for charter budgeting provisions.

[14] State law in Michigan establishes fiscal years for certain local units:

	Fiscal Year to Begin:
Cities:	
Fourth Class	1st Monday in March or 1st Monday in October
Townships:	
General law	April 1 or July 1
Charter	January 1
Counties:	
General law (under 1.5 million)	January 1

(Wayne County is December 1)

School Districts:

2nd class	July 1

State law does not set fiscal years for other local units.

[15] Act 621, P.A. 1978 defines "fiscal officer" as

> the controller, finance director, business manager, or other elected or appointed official who prepares and administers the budget of a local unit.

the duties of the fiscal officer enumerated in this ordinance (resolution).

[For units with chief administrative officer: The fiscal officer shall be responsible to the (title of chief administrative officer) for the performance of his duties.][16]

SECTION 4. Budget Policy Statement.[17]

No later than (date) of each year,[18] the (chief administrative officer) shall send to each officer, department, commission, and board of the (local unit) a budget policy statement for the use of those agencies in preparing their estimates of budgetary requirements for the ensuing fiscal year.[19]

This statement shall include information that the (chief administrative officer) determines to be useful and necessary to assure that the budgetary estimates of the agencies are pre-

---

[16] Act 621 (above) requires the chief administrative officer, if there is one, to prepare the budget and submit it to the legislative body. It is assumed that the chief administrative officer may delegate these duties to a fiscal officer while retaining the responsibility.

The act provides also that:

> The responsibilities and duties imposed by this section upon the chief administrative officer shall be discharged by the fiscal officer in a local unit which has not elected or designated a chief administrative officer.

(This provision applies primarily to counties, except those with a county executive or manager.)

[17] The policy statement might be dispensed with in very small local units.

[18] Date. The date of distribution of a budget policy statement should probably vary according to the size and complexity of the unit's budget, but it probably should occur no later than six months before the beginning of the fiscal year.

[19] Content of Statement. The budget policy statement can contain anything deemed significant by the chief administrative officer or the fiscal officer in budget preparation. Generally, however, it should include:

1. Economic review. Factors in the economy that condition the availability of revenues or the pattern of expenditures. Changing requirements by state and Federal agencies. Strikes, employment conditions are examples.

2. Revenue forecasts by source and fund.

3. Factors to be used in computing budgetary items. Such factors as social security rates, pension contribution percentages, health insurance rates, and other personnel costs; travel expense rates and limits; utility rates; interest rates; and other cost-of-living figures are examples.

4. Limits on budget requests. The chief administrative officer may indicate that increases in agency budgets above a certain level will not be entertained.

5. Policy direction. The chief administrative officer may indicate the budgetary requests he will favor or may direct the agencies to prepare estimates for certain proposals.

pared in a consistent manner. It shall also indicate limits on budgetary estimates, items that are to receive emphasis, and other policy direction deemed necessary by the (chief administrative officer).

This statement shall be available to the legislative body and the general public.

SECTION 5. Budget Estimates Required.

Any officers, departments, commissions, and boards of the (local unit) financed in whole or in part by the (local unit) shall, on or before (date) of each year,[20] transmit to the fiscal officer their estimates of the amounts of money required for each activity in their agencies for the ensuing fiscal year. They shall also submit any other information deemed relevant by the fiscal officer[21] on such forms and at such times as he may direct.[22]

SECTION 6. Budget Forms.

The fiscal officer shall prescribe forms to be used by the officers, departments, commissions, and boards of the (local unit) in submitting their budget estimates and shall prescribe the rules and regulations he deems necessary for the guidance of officials in preparing such budget estimates.

The budget forms shall, at a minimum, require:

(a) the display of actual expenditures for all purposes for the last completed fiscal year;[23]

(b) appropriations and estimated expenditures for those purposes for the current fiscal year;[24]

(c) estimates of required expenditures for the ensuing fiscal year.[25]

---

[20] Date. The date of submission of budget estimates (requests) from the agencies should probably be set at least four months in advance of the beginning of the fiscal year. State law mandates August 1 for charter townships.

[21] Relevance of information and the necessity of submitting a requested piece of information should be determined by the fiscal officer.

[22] Forms. The format of submission of budget estimates should be determined by the fiscal officer. See next section for details.

[23] Actual expenditures for last fiscal year. This is included because the last fiscal year is usually the most recent year for which solid figures upon which to base estimates are available. Current year data may be incomplete and, therefore, if used alone, may be misleading.

[24] Appropriations and estimated expenditures for current fiscal year. Current year expenditures should be the best available estimates of full-year expenditures. These estimates, in addition to their usefulness in preparing the next budget, may also form the basis for adjustments (transfers or supplementals) to the current budget.

[25] Budget year estimates. The agency requests do not ordinarily include revenue estimates which are prepared by the fiscal officer. Certain revenues, however, may best be estimated by the agencies. Fees and charges, for example, may be more accurately estimated by the agency collecting them.

The fiscal officer may require that the estimates for the ensuing fiscal year be calculated on the basis of various assumptions regarding level of service.[26]

Any agency request for the proposed purchase of land, buildings, or capital equipment shall be accompanied by a statement which:[27]

(a) describes the intended use of land, buildings, or equipment;

(b) states the order of priority of the purchase;

(c) provides a plan of financing for the purchase;

(d) provides an estimate of any operating costs associated with the purchase for the ensuing fiscal year and for the following three years.[28]

The fiscal officer may also require a statement of the purposes of any proposed expenditure and a justification of the services financed by any expenditure.[29]

The fiscal officer shall prepare estimates of revenue for each fund for the ensuing fiscal year, classified in order to show in detail the amount expected to be received from each source.

Such estimates of expenditures and revenues shall also be classified by character, object, function, and activity consistent with the accounting system classifications required by law.[30]

SECTION 7. Agency Budget Review.[31]

The fiscal officer shall review the agency estimates with a representative from each agency of the (local unit) that has submitted such estimates. The purpose of the review shall be to clarify the estimates, ensure their accuracy, and to determine their adherence to the policies enumerated by the (chief administrative officer) pursuant to Section 4.

---

[26] Calculation based on various levels of service. The fiscal officer may wish to determine the effect on services of various levels of funding. This approach can be useful in deciding the optimum combination of services to be recommended to the legislative body.

[27] Capital budget. Frequently, capital projects are financed outside of the regular budget by use of bonds. This requires a different budgetary treatment noted in this section.

[28] Three-year estimate operating costs. This requirement assures consideration of the cost of operating a building or other capital acquisition. Operating costs may ultimately outweigh the cost of acquiring the building or equipment.

[29] Purpose and justification statements help to assure that unproductive programs are not simply approved as a matter of routine.

[30] The Michigan Department of Treasury can supply the local unit with accounting requirements (except in the case of school districts for which the Michigan Department of Education has supplied such requirements).

[31] The agency budget review affords the agencies an opportunity to explain their requests and the fiscal officer an opportunity to assure himself that he understands the reasons for each figure in the budget.

SECTION 8. The Budget Document.

The fiscal officer shall consolidate the estimates received from the various agencies together with the amounts of expected revenues and shall make recommendations[32] relating to those estimates which shall assure consonance with the budget policy statement and which shall assure that the total of estimated expenditures including an accrued deficit in any fund does not exceed the total of expected revenues including an unappropriated surplus.[33] The budget shall consist of the following parts:

[32] Fiscal officer recommendations. The recommendations of the fiscal officer form the substance of his communication to the chief administrative officer regarding the proposals of the various agencies. If there is no chief administrative officer this document, as approved by the fiscal officer, will go to the legislative body.

[33] Balanced budget requirement. This is the first of several points in consideration of the budget in which this requirement appears. Although it may be argued that only the appropriation and the final actual expenditure and revenue totals really count, it should be assumed at this point that this is the level of spending and revenue desired by the fiscal officer and that, had he the authority, the budget would be executed accordingly. Further, it prevents the fiscal officer from shifting difficult decisions forward to the chief administrative officer or the legislative body.

Part 1. Statement of Assets and Liabilities.[34]

Part I shall contain a summary statement of all assets and current and long-term liabilities at the close of the last completed fiscal year.

The assets shall exclude fixed assets (land, buildings, equipment) but shall include for each fund the surplus or unencumbered and unreserved balances, reserves by purpose, monies receivable, and investments.

The liabilities shall include accounts payable, contracts payable, amounts due to other funds and agencies, bonds and interest payable, court orders payable, taxes or revenues collected in advance, and long-term or contingent liabilities.

Part II. Revenues.

Part II shall contain detailed estimates of all anticipated revenues applicable to proposed expenditures; summary statements of anticipated revenues classified by fund and source; comparisons between revenues actually received during the last completed fiscal year, those received and anticipated for the current fiscal year, and those anticipated for the ensuing fiscal year; the estimated surplus

[34] Statement of Assets and Liabilities. This is the statement of the financial condition of the local unit and is necessary, among other things, for complying with the provisions of Act 621, P.A. 1973 which defines surplus as "an excess of the assets of a fund over its liabilities and reserves" and deficit as loan excess of liabilities and reserves of a fund over its assets." The act also requires any surplus or deficit that has accumulated from prior years, together with an estimate of surplus or deficit expected in the current fiscal year to be stated in the budget.

or unobligated balance of the current fiscal year, and any additional information required by the (legislative body).[35]

Part III. Expenditures.

Part III shall contain detailed estimates of all operating and capital outlay expenditures for the ensuing fiscal year. It shall include a statement of proposed expenditures from, all funds classified by organizational unit, character, object, and function and activity. It shall show, in the same classification of expenditure, the expenditures of the last completed fiscal year, those anticipated for the current fiscal year, and shall include as separate items any deficit from the preceding fiscal year[36] that was not included in the budget for the current year and any anticipated deficit resulting from operations of the current year.

---

[35] Additional information required by the legislative body anticipates the transmittal to the legislative body by the executive. These requirements should be determined in advance by the legislative body.

[36] Deficit from the preceding fiscal year that was not included in the budget for the current year. An audit prepared after the passage of the current year's appropriation measure may disclose an operating deficit for the prior year for which no provision was made. This should be noted as well as an operating deficit for the current year if one is expected.

Part IV. Capital Outlay.[37]

Part IV shall consist of any recommendations for capital projects. These recommendations shall be accompanied by a statement indicating recommended priorities for projects and shall set forth for each project:

(1) The total estimated cost at completion;

(2) appropriations and expenditures made to date;

---

[37] Act 621, P.A. 197S treats capital outlay budgeting requirements differently depending on -he source of revenue:

For general fund capital outlay the requirement is:

> "The amount of proposed capital outlay expenditures . . . including the estimated total cost and proposed method of financing of each capital construction project and the projected additional annual operating cost and the method of financing the operating costs of each capital construction project for 3 years beyond the fiscal year covered by the budget."

For special assessment funds, public improvement or building and site funds, intragovernmental service funds, or enterprise funds the requirement is:

> "An informational summary of projected revenues and expenditures . . . including the estimated total cost and proposed method of financing each capital construction project, and the projected additional annual operating cost and the method of financing the operating costs of each capital construction project for 3 years beyond the fiscal year covered by the budget."

(3) expenditures and encumbrances at the close of the last completed fiscal year;

(4) estimated expenditures and encumbrances for the current fiscal year;

(5) estimates of the amounts of money necessary for the ensuing fiscal year;

(6) estimated annual operating costs, if any, and the method of financing those costs, for each of the three years following the budget year.

SECTION 9. Consideration of Budget by (Chief Administrative Officer).[38]

The fiscal officer shall transmit the budget to the (chief administrative officer)[39] who may revise or alter it, but not so as to exceed the aggregate amount authorized by law to be raised by taxation and other methods; provided that the (chief administrative officer) may not, unless error in computation is discovered, revise or alter the amounts required to be approved to provide a sinking fund for the payment of bonds at maturity, to pay serial bonds at maturity, or the interest on bonds.

SECTION 10. Transmittal of Budget to (Legislative Body).

No later than (date)[40] of each year, the (chief administrative officer)[41] shall transmit the budget to the (legislative body). The budget shall be accompanied by:

(a) A proposed general appropriations measure, consistent with the budget,[42] which shall set forth the anticipated revenue and requested expenditure authority for the ensuing fiscal year in such form and in such detail deemed appropriate by the (chief administrative officer), provided that it is consistent With the uniform chart of accounts prescribed by the State of Michigan. No

---

[38] In units with no chief administrative officer this section may be eliminated.

[39] In order to meet the other deadlines in the measure, the consideration of the budget by the chief administrative officer should be completed no later than two months before the beginning of the fiscal year. More time than that should be allotted in larger units.

[40] Date. The date of transmittal should be set so as to allow ample time for consideration of the budget by the legislative body and the public. In small jurisdictions this might be as little as 6-8 weeks before the start of the new fiscal year. In larger ones, 3-6 months might be necessary. State law mandates September 1 for charter townships.

[41] Transmittal by chief administrative officer. This is a key function of the chief administrative officer.

[42] Appropriation measure consistent with the budget. The appropriations measure need not be identical with the budget, but it must be consistent with it. That is, the spending authority created by passage of the appropriations measure should be identical both in amount and distribution among agencies and purposes, but it need not be in the same amount of detail or in the same format. It is only necessary that the appropriations be stated in such a way that expenditures can be made according to the appropriation measure.

appropriations measure shall be submitted to the (legislative body) in which estimated total expenditures, including an accrued deficit, exceed estimated total revenues, including an available surplus.[43]

(b) A budget message[44] which shall explain the reasons for increases or decreases in budgeted items compared with the current fiscal year, the policy of the (chief administrative officer) as it relates to important budgetary items, and any other information that the (chief administrative officer) determines to be useful to the (legislative body) in its consideration of proposed appropriations.

SECTIOII 11. Consideration of Budget by (Legislative Body).

The (legislative body) shall fix the time and place of a public hearing[45] to be held on the budget and proposed appropriations measure.

The (designated official)[46] shall then have published, in a newspaper of general circulation within the (local unit), notice of the hearing and an indication of the place at which the budget and proposed appropriations measure may be inspected by the public. This notice must be published at least seven days before the date of the hearing.

The (legislative body) may direct the (chief administrative officer) to submit any additional information it deems relevant in its consideration of the budget and proposed appropriations measure. The (legislative body) may conduct budgetary reviews with the (chief administrative officer) for the purpose of clarification or justification of proposed budgetary items.[47]

The (legislative body) may revise, alter, or substitute for[48] the proposed general appropriations measure in any way, except that it may not change it in a way that would cause total appropriations, including an accrued deficit, to exceed total estimated revenues, including an unappropriated surplus. An accrued deficit shall be the first item of ex-

---

43 Balanced budget requirement. See comment under Section 8.

44 Budget message. This is the formal opportunity for the chief administrative officer to explain and defend the choices made in preparing the budget. Although addressed to the legislative body, it is a public justification as well.

45 Time and place. The hearing must occur by October 24 in charter townships.

46 Designated official. This should be an employee of the legislative body, such as a city clerk.

47 Legislative review of the budget. This serves the same purpose for the legislative body that the agency review (Section 7) served for the chief administrative officer. This step should be carried out in public meetings.

48 Substitute for the general appropriations measure. This emphasizes the notion that the appropriations measure is a creature of the legislative body, and if the legislative body does not like the measure suggested by the chief administrative officer, it is free to draft and adopt its own. It may not, of course, alter the budget in a way that would jeopardize the payment of interest on bonds, the provision of a sinking fund for the payment of bonds at maturity, or the payment of serial bonds at maturity.

penditure in the general appropriations measure.

SECTION 12. Passage of the General Appropriations Measure.

No later than (date),[49] the (legislative body) shall pass a general appropriations measure providing the authority to make expenditures and incur obligations on behalf of the (local unit).

The (legislative body) may authorize transfers between appropriation items by the fiscal officer or the (chief administrative officer) within limits stated in the appropriations measure. In no case, however, may such limits exceed those provided for in Section 21 of this ordinance (resolution).[50]

The (legislative body) shall cause to be levied and collected the general property tax in an amount set forth by the Tax Allocation Board or the (local unit's) fixed portion as voted on by the electorate.[51]

SECTION 13. Failure to Enact a General Appropriations Measure.

In the event that the (legislative body) fails to pass a general appropriations measure by (date - first day of fiscal year), the fiscal officer shall notify all officers, departments, boards, and commissions that they may, in the new fiscal year, make expenditures and incur obligations under the provisions of the general appropriations measure effective for the fiscal year just completed; except that the authority for any item of appropriation in any mouth shall be limited to an amount not to exceed one-twelfth of the annual appropriation amount for that item. Expenditures shall continue in this manner each mouth until the effective date of a general appropriations measure for the new fiscal year.[52]

The (legislative body) shall not pass any amendment to the general appropriations measure for the last completed fiscal year nor make any supplemental appropriation

---

[49] Date. Passage of the general appropriations measure should occur at least two weeks, and preferably more than that, before the beginning of the fiscal year. If the local unit uses a system of allotments, the measure should be adopted 4-6 weeks in advance of the first day of the fiscal year to allow ample time for the preparation of allotment schedules. State law mandates November 1 for charter townships.

[50] See Sections 14 and 21.

[51] As noted in Act 621, P.A. 1978 (sec. 16)

> (5) The legislative body shall determine the amount of money to be raised by taxation necessary to defray the expenditures and meet the liabilities of the local unit for the ensuing fiscal year, shall order that money to be raised by taxation, within statutory and charter limitations, and shall cause the money raised by taxation to be paid into the funds of the local unit.

[52] Effective date of new appropriations measure. This provision requires that no spending occur without the sanction of the legislative body even if it has been more than a year since the last vote.

based on that measure after the beginning of a new fiscal year.[53]

[For units with independently elected chief administrative officer who has a general grant of veto power.]

SECTION __ Veto Power of (Chief Administrative Officer).

No later than (___) days[54] after the enactment by the (legislative body) of the general appropriations measure, the (chief administrative officer) may file with the (designated legislative official) written notification that he has suspended the authority of the general. appropriations measure or any portion thereof.[55] This notification must be accompanied by written justification for taking such an action.

This action may be overriden by the (legislative body) by a two-thirds vote of the members elected and serving. Unless overriden by the (legislative body), the action of the (chief administrative officer) shall remain in effect and no expenditure may be made nor obligation incurred under those items affected by his action unless and until he submits to the (designated legislative officia1) written notification that he has reversed the original

SECTION 14. Amendment of the General Appropriations Measure.

A deviation from the original general appropriations measure shall not be made without first amending the general appropriations measure.[56] Amendment shall follow the

[53] No amendment after completion of fiscal year. This requirement prevents amending an appropriations measure after its authority has expired. The purpose of an appropriation is to provide authority to the executive to make expenditures. There certainly is no point in amending the act after a new one has taken effect. (The status of the appropriation accounts on the last day of the fiscal year should be made known without further amendment.) Further, if an appropriations measure for the new fiscal year is not passed, the legislative body should not amend an outdated measure thereby postponing consideration of the appropriations measure for the new year.

[54] Days. This should be a reasonably short period, probably 10 days.

[55] . . . or any portion thereof. This provides authority f or a “line-item” veto so that the chief executive does not have to veto the entire appropriation measure in order to veto one or two items.

[56] No deviation without first amending original measure. If spending authority flowed originally from the legislative appropriations measure, it follows that no changes in amount for either the total budget or any appropriation account should be permitted without the express approval of the legislative body. No situation should be permitted in which the executive makes transfers and then informs the legislative body that it must amend the general appropriations measure to conform.

Act 621, P.A. 1978 provides some flexibility in this regard in that it permits the legislative body to make blanket prior approval to transfers among appropriations accounts within limits stated in the appropriations measure. If the legislative body chooses to permit the executive to exercise such latitude, a reasonable limit would be $10,000 (or more in larger units) or 5 percent of the same procedure used for the original consideration of the budget and proposed appropriations measure and passage of the general appropriations measure pursuant to Sections 11 and 12 of this ordinance (resolution).

[For units with independently elected chief administrative officer who has a general grant of veto power.

The (chief administrative officer) shall retain the same veto power as regards amendments that is reserved to him under Section ___ of this ordinance.]

SECTION 15. Appropriation Not a Mandate to Spend.[57]

Appropriations will be deemed maximum authorization to incur expenditures. The fiscal officer[58] shall exercise supervision and control in order to ensure that program or work objectives are realized within these limits and shall not approve any expenditure beyond that necessary to accomplish those objectives.

SECTION 16. Appropriation Ledger Accounts.

The fiscal officer shall maintain appropriation ledger accounts[59] in which are to be recorded such expenditure encumbrances and obligations[60] for the future payment of appropriated funds as he may approve.[61]

---

amount of the appropriation from which the transfer is made, veto whichever is lower. (See also Sections 12 and 21.)

[57] Appropriation not a mandate to spend. An appropriation is an upper limit on expenditures. It is also an estimate of requirements that is made as much as 14 months in advance of the actual final expenditures.

As such it should not be assumed that simply because the authorization exists, it is necessary to spend the unit's funds until the account is exhausted. If efficiencies can be achieved in one area the savings can be transferred to another, returned to surplus, or returned to the taxpayers.

[58] Fiscal officer. It is necessary to establish a procedure for approving expenditures. The fiscal officer must certify that the funds are available before an expenditure can be made. See also Section 16.

[59] Appropriation ledger accounts. The requirement here is to maintain a system of accounts on which expenditures may be charged against appropriations. If the legislative body has appropriated in the same format and detail as the budget, the appropriation ledger accounts will be all that is necessary to record expenditures. If the operating budget is in greater detail than the appropriations measure, however, it will be necessary to establish sub-accounts to assure that expenditures are properly charged. These are executive items and transfers among sub-accounts within an appropriation account do not need legislative body approval.

[60] Encumbrances and obligations. A common system of Governmental accounting is the "modified accrual" basis in which expenditures are recorded at the time liabilities are incurred (such as when a person is hired or a contract signed) and revenues are not recorded until received in cash.

[61] Approval by fiscal officer. See comment in Section 15.

SECTION 17. Allotment of Appropriations.[62]

No later than (the first day of the fiscal year),[63] each office, department, board, and commission of the (local unit) shall submit to the fiscal officer, on forms provided by him, a statement of proposed allotments of appropriations[64] based upon expected periodic requirements.[65] The fiscal officer will review the requested allotments in light of the plan of work of each unit and the expected timing of those requirements, and he may revise or alter the proposed allotment of any unit. The decision of the fiscal officer as to the amount of any allotment for any fiscal period or the extent to which an allotment is consistent with the purpose for which it is intended, as expressed in the general appropriations measure, shall be final and conclusive, provided that the fiscal officer, upon the approval of the (chief administrative officer), shall have the authority at any time to modify any allotment previously made, upon application of, or upon notice to, the office, department, board of commission concerned.[66]

SECTION 18. Procedure for Disbursements.

No money shall be drawn from the (local unit) treasury except in pursuance of an appropriation of the part upon common understanding of the (legislative body).[67]

Each warrant, draft, or contract of the (local unit) shall specify the fund and appropriation designated by number assigned in the accounting system classification established pursuant to law from which it is payable and shall be paid from no other fund or appropriation.[68]

---

[62] Allotments. Units of government with relatively simple budgets may find it unnecessary to employ a system of allotments. For such units, this section may be dropped.

[63] First day of the fiscal year. It may be desirable to set the due date for allotments earlier than the first day of the fiscal year, but, in fact, there is seldom much use for an allotment schedule until a month or two of the fiscal year have elapsed.

[64] Appropriations. If the budget is more detailed than the appropriations measure, the budget items should be allotted as well, consistent with the appropriation amounts.

[65] Expected periodic requirements. The period may vary according to the needs of the unit. Quarterly allotments are common. They have the advantages of covering sufficient time for expenditure trends to become evident and reducing the amount of review time required. Monthly allotments may be appropriate for some units but they are useful primarily for large, active accounts.

[66] Determination of allotments. Although an allotment schedule is principally an informational device, its use in budgetary control depends in the amounts involved. This section provides a procedure for resolving disputes over the amounts in an allotment schedule, either their placement or timing.

[67] Pursuance of an appropriation. This means either in amount or purpose.

[68] Warrant, draft, or contract. In order for the expenditure to be properly charged to an appropriation account, it is necessary that any authorization to spend the local unit's funds contain the appropriation account (and any sub-account) number.

Expenditures shall not be charged directly to any contingent or general account.[69] Instead, the necessary amount of the appropriation from such account shall be transferred pursuant to the provisions of this ordinance to the appropriate general appropriation account and the expenditure then charged thereto.

SECTION 19. Limit on Obligations and Payments.[70]

No obligation shall be incurred against, and no payment shall be made from,[71] any appropriation account unless there is a sufficient unencumbered balance in the appropriation and sufficient funds are or will be available to meet the obligation.

Any obligation incurred or payment authorized in violation of this ordinance (resolution) shall be void and any payment so made illegal.

SECTION 20. Monthly (Quarterly) Finance Reports.

The fiscal officer, within the days after the end of each month[72] (quarter), shall transmit to the (legislative body) a report of financial operations, including, but not limited to:[73]

---

[69] Contingent or general account. A contingent account (not to be confused with a contingent fund, such as a "rainy-day fund") is an account with no purpose assigned to it. It should be used, if it is necessary to establish such an account, to cover unexpected expenditures as they arise or to finance items that originally were deemed of sufficiently low priority to fail being appropriated for. In any event, it should not turn into a "slush fund" to be used at the discretion of the chief administrative officer. Authority from such an account should be transferred to operating accounts first before expenditures are made.

[70] Limit on obligations and payments. An appropriation is authority to spend. The level of that authority is represented by the dollar amount appropriated. As charges are made against an appropriation account, that authority is diminished until the charges equal the appropriation amount, at which point the authority is exhausted. The simple existence of an account does not mean that the authority is still available and no charges should be permitted against an exhausted appropriation

[71] No obligation . . . no payment. This recognizes that there are two steps to an expenditure, both of which are necessary in order to result in a charge against an appropriation account. The expenditure can be prevented at either point. Obviously, it is preferable not to create the obligation in the first place but, if it should be, and if the account is exhausted, payment may be withheld at least until a transfer can be arranged or a supplemental appropriation made.

[72] Monthly finance reports. State law mandates quarterly reports for charter townships. Monthly reports would not be inconsistent with this requirement.

[73] The fiscal officer should feel free to provide and the legislative body should feel free to request more than is noted here. This listing of requirements enables the legislative body to assess:

1) whether the unit is likely to retain a balanced budget to the end of the fiscal year;

(a) a summary statement of the actual financial condition of the general fund at the account end of the previous month;

(b) a summary statement showing the receipts and expenditures and encumbrances for the previous month and for the then current fiscal year to the end of previous month;

(c) a detailed listing of:

(1) expected revenues by major source as estimated in the budget; actual receipts to date for the current fiscal year compared with actual receipts for the same period in the prior fiscal year; the balance of estimated revenues to be collected in the then current fiscal year; and any revisions in revenue estimates occasioned by collection experience to date.

(2) for each organizational unit and activity: the amount appropriated; the amount charged to each appropriation in the previous month and for the current fiscal year and as compared with the same period in the prior fiscal year; the unencumbered balance of appropriations; and any revisions in the estimate of expenditures.

SECTION 21. Transfers.

Transfers of any unencumbered balance, or any portion thereof, in any appropriation account to any other appropriation account may not be made without amendment of the appropriations measure as provided in Section 14 of this ordinance, except that transfers within a fund and department may be made by the fiscal officer if the amount to be transferred does not exceed ($___) or (____%)[74] of the appropriation item from which the transfer is to be made, whichever is less.[75]

[For units with an independently elected chief administrative officer with a general grant of veto power:

Transfers approved by the (legislative body) may be disallowed by the (chief administrative officer) according to the veto provisions of Section ___ of this ordinance.]

SECTION 22. Supplemental Appropriations.

The (legislative body) may make supplemental appropriations by amending the

---

2) whether revenue estimates were accurate;

3) whether legislative body mandates for expenditures are being followed;

4) whether funds will become available for transfer;

5) whether certain accounts will require transfer or supplementation.

[74] A possible limit might be $10,000 or 5%. Smaller units may wish the limit to be lower than $10,000; larger units may wish a higher limit.

[75] For commentary on transfers, see notes on Sections 12 and 14.

original general appropriations measure as provided by Section 14 of this ordinance (re solution), provided that revenues in excess[76] of those anticipated in the original general appropriations measure become available due to:

(a) an unobligated surplus from prior years becoming available;

(b) current year revenue exceeding original estimates in amounts great enough to finance increased appropriations.

The (legislative body) may make a supplemental appropriation by increasing the dollar amount of an appropriation item in the original general appropriations measure or by adding additional items.

At the same time, the estimated amount from the source of revenue to which the increase in revenue may be attributed shall be increased, or a new source and amount added, in a sum sufficient to equal the supplemented expenditure amount. In no case may such appropriations cause total estimated expenditures, including an accrued deficit, to exceed total estimated revenues, including an unappropriated surplus.

[For units with an independently-elected chief administrative officer with a general grant of veto power:

Supplemental appropriations approved by the (legislative body) may be disallowed by the (chief administrative officer) according to the veto provisions of Section ___ of this ordinance.]

SECTION 23. Appropriation Adjustment Required.[77]

Whenever it appears to the (chief administrative officer) or the (legislative body) that actual and probable revenues in any fund

[76] Revenues in excess of those anticipated. The essence of a supplemental appropriation is the expansion of the budgetary authority of the local unit. This can come only from the addition of revenue. This is different from a transfer from one account to another in which there is not actually an increase in total appropriations.

[77] Act 621, P.A. 1978, Section 17, requires that:

> If, during a fiscal ear, it appears to the chief administrative officer or fiscal officer in units which have not elected or designated a chief administrative officer, or to the legislative body that the actual and probable revenues from taxes and other sources in a fund are less than the estimated revenues, including an available surplus upon which appropriations from the fund were based, the chief administrative officer or fiscal officer shall present to the legislative body recommendations which, if adopted, would prevent expenditures from exceeding available revenues for that current fiscal year. The recommendations shall include proposals for reducing appropriations from the fund for budgetary centers in a manner that would cause the total of appropriations to not be greater than the total of revised estimated revenues of the fund, or proposals for measures necessary to provide revenues sufficient to meet expenditures of the fund, or both. The recommendations shall recognize the requirements of state law and the provisions of collective bargaining agreements.

will be less than the estimated revenues upon which appropriations from such fund were based, the (chief administrative officer) shall present to the (legislative body) recommendations which, if adopted, will prevent expenditures from exceeding available revenues for the current fiscal year. Such recommendations shall include proposals for reducing appropriations, increasing revenues, or both.

Within 15 days of receiving the recommendations of the (chief administrative officer) for bringing appropriations into balance with estimated revenues, the (legislative body) shall amend the general appropriations measure to reduce appropriations or shall approve such measures necessary to provide revenues sufficient to equal appropriations, or both. If the (legislative body) does not make effective such appropriation reductions or measures to increase anticipated revenues within this time, the (chief administrative officer) shall within the next five days make adjustments in appropriations in order to equalize appropriations and estimated revenues.

SECTION 24. Penalties.

Any violation of Sections, 14, 16, 18, 19, 20, 21, 22, or 23 shall be cause for removal of any elected or appointed officer or employee in the manner prescribed by law for the removal of such officer or employee.