Budgeting...Where Do I Start?

by Sue Nelson, CCAM®

One of the most important duties that we have as managers or board members/finance committee members is to develop next year's budget, which is as accurate a forecast as possible of the association's upcoming financial needs. The thought of budgeting can send panic through the most seasoned of us and cause an extreme case of procrastination. However, with some thoughtful planning and research, it will all fall into place. The process, like many, is part art and part science.

A basic budget has three main components: the income, the operating expenses and the reserve transfer. The operating expenses plus the reserve transfer equals the income you need to support them. You can't figure out the income needed (HOA fees) until you figure out the projected operating expenses and reserve transfer.

WHEN SHOULD I START? Since the reserve study takes time, it is wise to start the process early. Get bids for your reserve study or reserve update in Month 5 of your fiscal year (e.g. May if you are on a calendar year) and approve a bid and start the study in Month 6. You will then have plenty of time to revise it, if needed. Some reserve providers will give you a discount if you give them more time. If you wait until the last minute when they are the busiest, you will often pay extra.

In Month 8, after your Month 7 financial report and (hopefully) the reserve study are completed, compile Draft #1 of the budget. If the reserve study has not yet been completed, use the forecast from the last reserve study, with the notation that it will be revised when the new reserve study is completed. This gives plenty of time to research numbers, re-draft and approve the final budget. After the board approves the budget, your reserve provider needs time to complete the "Assessment and Reserve Funding Disclosure." The budget needs to be mailed to the membership within Month 11.

WHERE DO I START—RESERVES? Your reserve provider will want you to estimate how much money will be in reserves at the beginning of the new year. To do so, take the amount of money in reserves now, estimate the transfers scheduled for the rest of the year,

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and subtract scheduled reserve expenditures for the rest of the year. Caution: if operating cash is low and you cannot make all of your reserve transfers for the rest of the year, give a realistic estimate of what you actually will transfer.

Your reserve provider will need information on recent reserve projects completed and upcoming scheduled reserve projects. Give them all of the reserve expenditures from the past year and the current year, as well as upcoming scheduled projects. Also, if you borrow money from reserves for insurance, for instance, or if you have loan payments that are coming from reserves, you need to alert your reserve provider.

WHERE DO I START—OPERATING? Set up an Excel spreadsheet that has rows for all of the categories from your income statement. Set up a column for the new budget and three columns for the actual income and expenses for the current year and the prior two years, and then a column for the current budget. I prefer working with monthly figures as they make more sense to me. For the current year actual figures, take the Month 7 year-to-date figures from your income statement and divide by seven. Exceptions: if you have bi-monthly costs like utilities or quarterly costs or annual costs like CPAs, divide by the appropriate number of months. So the annual CPA cost would be divided by 12, and 6 months of utilities paid in 7 months would be divided by 6, and if you paid the guards for 7 ½ months, divide by 7 ½ to get a realistic amount for each expense on a monthly basis. Divide all of last year's and the previous year's expenses by 12. Now for any line item, you have the current monthly cost and the monthly cost for the prior two years.

Now that you have finished your preparation, you are ready to work on next year's numbers. In addition to what you expect will happen—for instance, that insurance will go down (knock on wood) and health care will go up (it's a given)—take a look at your past history for each line to help guide you to where your budget should be for next year. If your plumbing costs have averaged $7,000 per month this year, $6,000 last year and $5,500 the year before, unless there is some reason to change, you can expect that your costs will be $7,000 or more the next year. Plug in the reserve transfer from your new reserve study, and from that total you have the amount of income needed to support anticipated expenses. *Voila!*

(Watch for Part II of this series in the next issue.)

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