

BUDGETING BASICS

For Small Businesses

Presented By:
LaTaunya D. Howard, CGFM
Assure Budget Solutions

WELCOME & INTRODUCTIONS

INDUSTRIES REPRESENTED

- Finance/Insurance/Real Estate
- Transportation/Construction
- Human Resources/Staffing & Recruitment
- Information Technology/Communications
- Retail/Manufacturing
- Other Industries?

WHAT WE WILL COVER

- An introduction to the basic principles of budgeting, including:
 - What a budget is and why it is important for your business
 - Some considerations when building a budget
 - Approaches for forecasting income and expenses
 - The relationship between budgeting and other key business functions

BUDGET PLANNING AND DEVELOPMENT

WHAT IS A BUDGET?

- A summary of all *planned* income and expenses for a specific period of time
 - May require trade-offs if income is not sufficient to cover all desired expenses
- Forward-looking, but often in consideration of historical patterns
- Iterative and on-going

WHAT ARE THE BASIC COMPONENTS OF A BUDGET?

- **INCOME** (money coming in)
 - Sales
 - Services
 - Interest
 - Other
- **EXPENSES** (money going out)
 - Personnel Costs
 - Non-personnel
 - Direct vs. indirect (overhead) costs
- Income must exceed expenses in order for the business to be profitable

WHO BUDGETS?

- **The Government**

- Federal: The U.S. Constitution Article I, Section 9 states that “No money shall be drawn from the Treasury, but in consequence of appropriations [budget authority] made by law...”
- State: The Maryland Constitution Article III, Section 52, Paragraph 3 states that “Each budget shall contain a complete plan of proposed expenditures and estimated revenues for said fiscal year...”
- Prince George’s County: The Prince George’s County Charter, Article VIII Section 803 states that the budget “...shall represent a complete financial plan for the County, including all estimated revenues from all sources, [and] all planned expenditures...”

WHO BUDGETS? (cont'd)

- **Corporations**

- A study by The Institute of Management and Administration revealed the importance of budgeting to corporations, as shown in the table below ("Change Of Budgeting And Forecasting Trend In Companies", 2010)

Financial Activity	Less Than 250 Employees	More Than 250 Employees
Annual Planning & Budgeting	57%	63%
Monitor Spending	51%	38%

- **The Wealthy**

- According to business author Angie Mohr, money mistakes of the rich and famous include “having more money going out than coming in” and “not naming every dollar” (Mohr, 2011)

- **YOUR SMALL BUSINESS!**

Key Roles Of The Budget



A Financial Plan



A Control Device



A Performance Evaluation Tool

BUDGET = FINANCIAL PLAN

- Helps to identify and prioritize the business's future expense needs
- Helps to identify whether there will be sufficient income to meet future expense needs
- Provides a statement of the business's priorities to stakeholders (e.g., customers, staff, potential investors, etc.)

BUDGET = CONTROL DEVICE

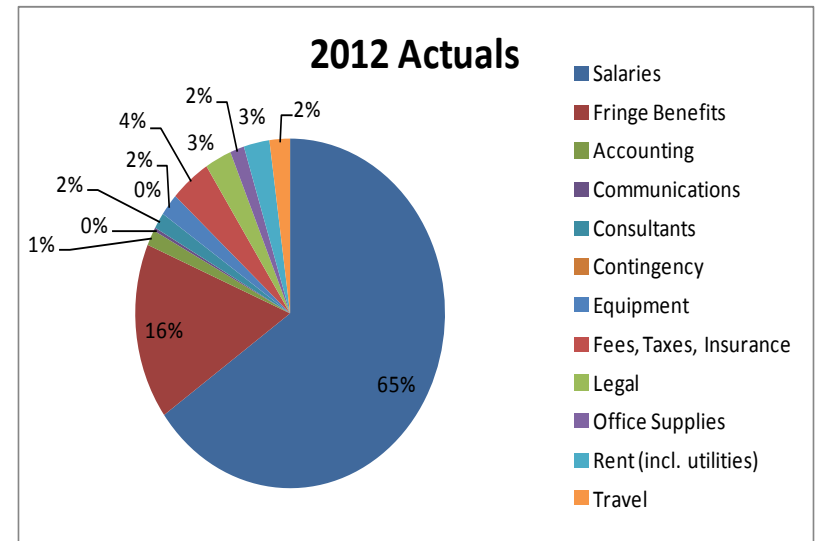
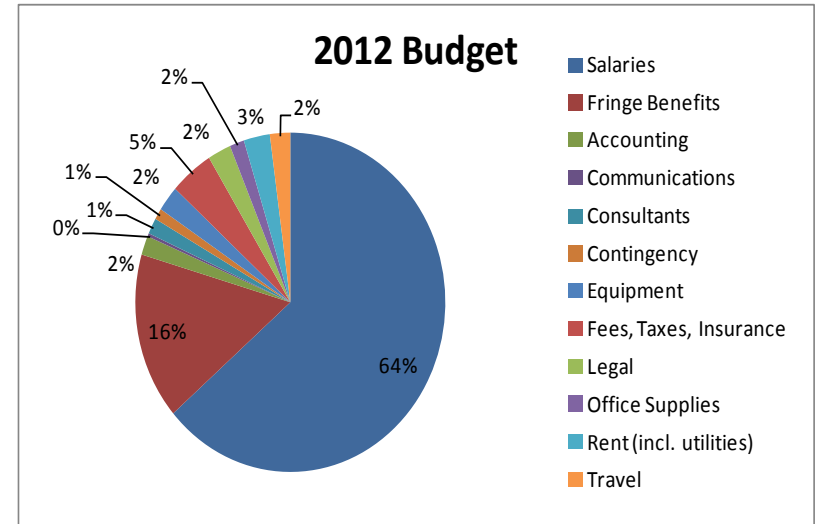
- Sets internal spending limits (esp. line item budgeting)
- Helps to contain costs and optimize profit margins
- Helps to foresee and mitigate potential financial challenges before they can threaten the business
- Enables more confident business decision-making

BUDGET = PERF. EVALUATION TOOL

- Identifies variances between planned and actual income and expenses, and where adjustments may be needed for future planning
- Monitors whether operational goals and objectives planned in the budget have been achieved
- Assesses the business's current performance to its own historical patterns, and to that of its competitors and industry standards

EXERCISE #1 – WHAT DO YOU THINK?

	2012 BUDGET	2012 ACTUALS	ACT vs. BUD \$	ACT vs. BUD %
Income				
Sales	\$ 350,000	\$ 339,593	\$ (10,407)	-3.0%
TOTAL INCOME	\$ 350,000	\$ 339,593	\$ (10,407)	-3.0%
Expenses				
Salaries	\$ 210,000	\$ 217,727	\$ 7,727	3.7%
Fringe Benefits	\$ 52,500	\$ 54,432	\$ 1,932	3.7%
Personnel	\$ 262,500	\$ 272,159	\$ 9,659	3.7%
# of Staff	4.5	4.5	0.0	0.0%
Accounting	\$ 6,000	\$ 4,840	\$ (1,160)	-19.3%
Communications	\$ 1,000	\$ 985	\$ (15)	-1.5%
Consultants	\$ 5,000	\$ 5,000	\$ -	0.0%
Contingency	\$ 3,500	\$ -	\$ (3,500)	-100.0%
Equipment	\$ 8,000	\$ 6,892	\$ (1,108)	-13.8%
Fees, Taxes, Insurance	\$ 15,000	\$ 14,067	\$ (933)	-6.2%
Legal	\$ 8,000	\$ 9,291	\$ 1,291	16.1%
Office Supplies	\$ 5,000	\$ 4,926	\$ (74)	-1.5%
Rent (incl. utilities)	\$ 9,000	\$ 9,000	\$ -	0.0%
Travel	\$ 7,000	\$ 7,139	\$ 139	2.0%
Non-Personnel	\$ 67,500	\$ 62,140	\$ (5,360)	-7.9%
TOTAL EXPENSES	\$ 330,000	\$ 334,299	\$ 4,299	1.3%
BALANCE	\$ 20,000	\$ 5,294	\$ (14,706)	-73.5%



BUILDING THE BUDGET

INCOME

Some Considerations:

- How many “units” of your product/service can you realistically sell during the budget period?
- Is there seasonality to the timing of your business’s income (e.g., high and low months)?
- What is the lag between service completion and receipt of payment?
- Are there any new, expanding or expiring income sources?

INCOME (cont'd)

	UNITS SOLD	UNIT PRICE	TOTAL INCOME
Sales - Product/Service A	2,150	\$ 100	\$ 215,000
Sales - Product/Service B	1,800	\$ 75	\$ 135,000
TOTAL - All Income			\$ 350,000

BUILDING THE BUDGET

INCOME

\$350,000

EXPENSES

Personnel Costs

- Some considerations:
 - How many employees does your business have?
 - What are the employees' salaries?
 - What payroll taxes and fringe benefits will be paid by the business?

EXPENSES (cont'd)

Personnel Costs

- At a minimum, personnel detail should include:
 - Employee Name
 - Position Title
 - Department/Group ID
 - Full-Time Equivalent
 - Salary (beginning and ending for the year)

EXPENSES (cont'd)

EMPLOYEE NAME	EMPLOYEE ID	POSITION TITLE	GROUP ID	FULL-TIME EQUIVALENT	BEGINNING SALARY	3% MERIT INCREASES	ENDING SALARY
Brown, Janet	85002	Manager	Prod/Srvc	1.0	\$ 58,252	\$ 1,748	\$ 60,000
Jones, David	45001	Assistant Manager	Prod/Srvc	1.0	\$ 53,398	\$ 1,602	\$ 55,000
McDaniel, Steven	15800	File Clerk	Gen Admin	1.0	\$ 24,272	\$ 728	\$ 25,000
Parker, Mary	10233	Secretary	Gen Admin	1.0	\$ 43,689	\$ 1,311	\$ 45,000
Taylor, Eric	52001	Computer Technician	IT Admin	0.5	\$ 24,272	\$ 728	\$ 25,000
TOTAL SALARIES				4.5	\$ 203,883	\$ 6,117	\$ 210,000

EXPENSES (cont'd)

DESCRIPTION	AMOUNT
Child Care Subsidy	\$ 5,000
Health Insurance	\$ 23,500
Life Insurance	\$ 7,000
Payroll Taxes	\$ 10,000
Retirement/401k	\$ 7,000
TOTAL FRINGE BENEFITS	\$ 52,500

Fringe Benefit Percentage = Total Fringe Benefits/Total Salaries
 $\$52,500/\$210,000 = 25\%$

BUILDING THE BUDGET

INCOME	\$350,000
EXPENSES	
SALARIES	\$210,000
FRINGE BENEFITS	\$52,500

EXPENSES (cont'd)

Non-Personnel Costs

- Some Considerations:
 - Past and current spending patterns
 - New goals and priorities
 - Inflation and/or contractual escalation increases
 - One-time costs (in current or future year)
 - Annualization of costs

EXPENSES (cont'd)

Non-Personnel Costs

Examples Include (but are not limited to):

- Rent/Lease
- Equipment
- Accounting
- Fees (e.g., bank, licenses, permits, etc.)
- Marketing
- Supplies and Materials
- Legal
- Communications (e.g., telephone, internet, etc.)
- Contingency Fund

BUILDING THE BUDGET

INCOME	\$350,000
EXPENSES	\$330,000
SALARIES	\$210,000
FRINGES	\$52,500
NON-PERSONNEL	\$67,500
BALANCE	\$20,000

EXPENSES (cont'd)

Direct vs. Indirect (Overhead) Costs

- Direct costs can be specifically associated with a particular project or activity
 - Examples *generally* include salaries, materials and equipment, consultant services, etc.
- Indirect costs are those not directly attributable to a particular project or activity, but are necessary to sustain the business as a whole
 - Examples *generally* include rent, financial and accounting services, general office supplies, etc.

EXERCISE # 2 – BUDGET FOR 2013

- Refer back to the budget on slide 13, and prepare a proposed master budget for 2013 that improves upon the issues we discussed earlier.
- Also consider these factors in your budget planning:
 - The business is anticipating a 3% increase in income over what was actually achieved in 2012
 - There will be a mandatory 10% rent increase in February 2013
 - The owner would like to give all existing staff a 5% increase in March 2013
 - The owner wants to hire another full-time employee at an annual salary of \$40,000
 - The owner would like to retain a contingency fund, preferably at least 2% of estimated income
 - Other factors that you believe should be taken into consideration
- We will discuss each group's 2013 proposed budget

EXERCISE # 2 – BUDGET FOR 2013

	2013 BUDGET
Income	
Sales	\$ -
	\$ -
	\$ -
TOTAL INCOME	\$ -
Expenses	
Salaries	\$ -
Fringe Benefits	\$ -
Personnel	\$ -
# of Staff	
Accounting	\$ -
Communications	\$ -
Consultants	\$ -
Contingency	\$ -
Equipment	\$ -
Fees, Taxes, Insurance	\$ -
Legal	\$ -
Office Supplies	\$ -
Rent (incl. utilities)	\$ -
Travel	\$ -
	\$ -
	\$ -
Non-Personnel	\$ -
TOTAL EXPENSES	\$ -
BALANCE	\$ -

BUDGET MANAGEMENT AND MONITORING

GENERAL BUDGET MANAGEMENT PROCESS

- Begin planning for next year's budget at least one to three months prior to the start of that year
- Prepare and review budget forecasts regularly (e.g., monthly, quarterly)
- Include others in the budget process if possible
- Remember the Pareto Principle: 80% of the issues exist in 20% of the budget

WAYS TO PRESENT THE BUDGET

- Master Budget: Compiles all of the business's income and expenditures into a single budget
- Project Budget: Delineates income and expenses for each project and/or line of business
- **NOTE**: When submitting a budget as part of a response to a solicitation, grant application, or the like, **ALWAYS FOLLOW THE GUIDELINES!**

WAYS TO PRESENT THE BUDGET

MASTER BUDGET

Income		
Sales	\$	350,000
TOTAL INCOME	\$	350,000
Expenses		
Salaries	\$	210,000
Fringe Benefits	\$	52,500
Personnel	\$	262,500
# of Staff		4.5
Accounting	\$	6,000
Communications	\$	1,000
Consultants	\$	5,000
Contingency	\$	3,500
Equipment	\$	8,000
Fees, Taxes, Insurance	\$	15,000
Legal	\$	8,000
Office Supplies	\$	5,000
Rent (incl. utilities)	\$	9,000
Travel	\$	7,000
Non-Personnel	\$	67,500
TOTAL EXPENSES	\$	330,000
BALANCE	\$	20,000

WAYS TO PRESENT THE BUDGET

PROJECT/LINE OF BUSINESS

Product/Service A		Product/Service B	
Income		Income	
Sales	\$ 215,000	Sales	\$ 135,000
TOTAL INCOME	\$ 215,000	TOTAL INCOME	\$ 135,000
Expenses		Expenses	
Manager (.60 FTE)	\$ 36,000	Manager (.40 FTE)	\$ 24,000
Assistant Manager (.60 FTE)	\$ 33,000	Assistant Manager (.40 FTE)	\$ 22,000
File Clerk (.75 FTE)	\$ 18,750	File Clerk (.25 FTE)	\$ 6,250
Secretary (.80 FTE)	\$ 36,000	Secretary (.20 FTE)	\$ 9,000
Computer Technician (.25 FTE)	\$ 12,500	Computer Technician (.25 FTE)	\$ 12,500
<i>Salaries</i>	<i>\$ 136,250</i>	<i>Salaries</i>	<i>\$ 73,750</i>
<i>Fringe Benefits</i>	<i>\$ 34,062</i>	<i>Fringe Benefits</i>	<i>\$ 18,438</i>
Personnel	\$ 170,312	Personnel	\$ 92,188
# of Staff	3.0	# of Staff	1.5
Accounting	\$ 3,000	Accounting	\$ 3,000
Communications	\$ 500	Communications	\$ 500
Consultants	\$ 3,000	Consultants	\$ 2,000
Contingency	\$ 1,750	Contingency	\$ 1,750
Equipment	\$ 4,000	Equipment	\$ 4,000
Fees, Taxes, Insurance	\$ 7,500	Fees, Taxes, Insurance	\$ 7,500
Legal	\$ 4,000	Legal	\$ 4,000
Office Supplies	\$ 3,000	Office Supplies	\$ 2,000
Rent (incl. utilities)	\$ 4,500	Rent (incl. utilities)	\$ 4,500
Travel	\$ 2,500	Travel	\$ 4,500
Non-Personnel	\$ 33,750	Non-Personnel	\$ 33,750
TOTAL EXPENSES	\$ 204,062	TOTAL EXPENSES	\$ 125,938
Balance	\$ 10,938	Balance	\$ 9,062

FORECASTING

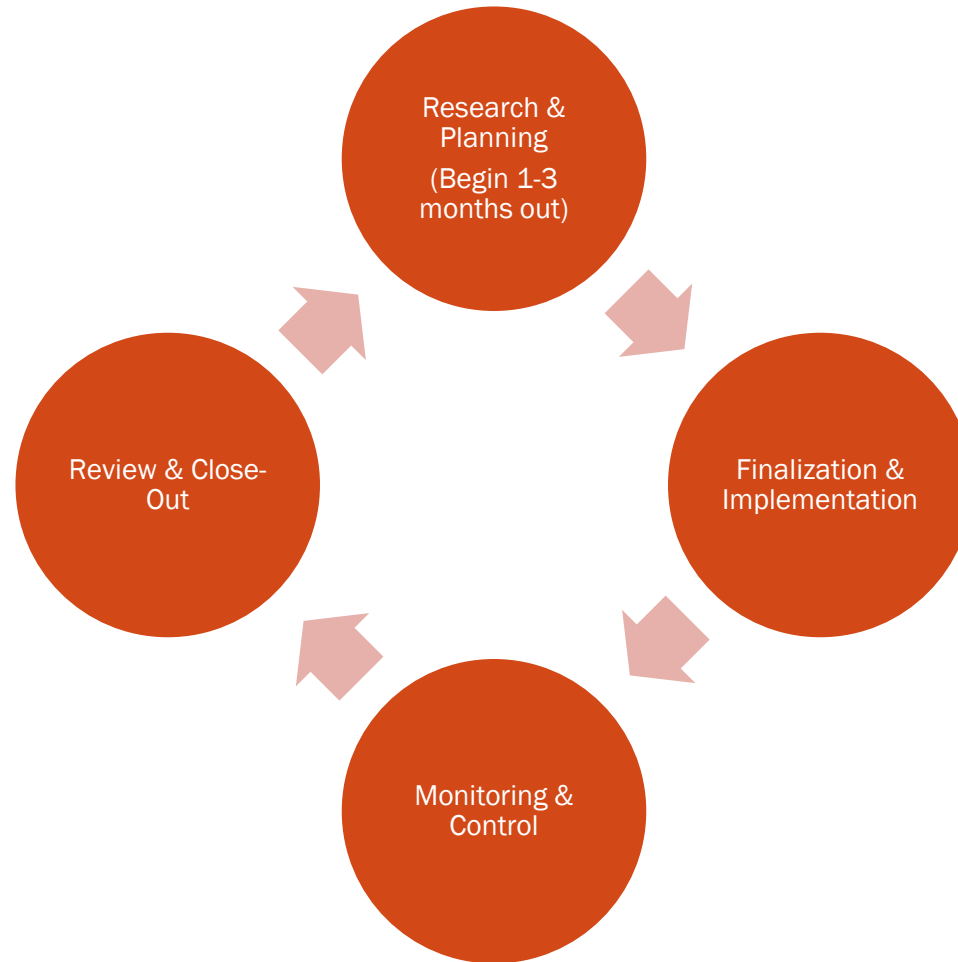
- While budgeting is *planning* for the future, forecasting is *predicting* what will occur in the future
- Forecasting has inherent uncertainties, but researching issues such as economic and industry conditions, and supplier/customer needs can help to manage the uncertainty
- Forecasting techniques can also be employed; two examples are:
 - **Moving Average**
 - Typically averages the past 3-6 months to project future months' activity
 - Better approach when income and/or expenses are relatively stable throughout the business cycle
 - **Month over Month**
 - Assumes that changes between two points in the past will occur in the future
 - Better approach when there are cyclical changes in income and/or expenses in the business cycle
- Test multiple scenarios and approaches to determine best “fit” for your business

USING THE BUDGET FOR BUSINESS DECISIONS

- Determine root cause of significant variances between actuals, budget, and forecasts and take appropriate action(s)
- Assess current and historical trends to determine progress on business goals, and extent to which new goals and/or priorities are warranted
- Evaluate the success of individual projects/lines of business
- Plan recruitment strategies

INTERRELATIONSHIP WITH OTHER BUSINESS FUNCTIONS

THE BUDGET CYCLE



RELATIONSHIP BETWEEN BUDGETING AND OTHER BUSINESS FUNCTIONS

- **Accounting**
 - Reports provide a retrospective view of financial activities that can be compared against the current budget and forecasts, and help to prepare future budgets and forecasts
- **Business Planning**
 - Budget section and forecasts included in business plan provide prospective lenders/investors a sense of the business's viability
- **Grant & Procurement Applications**
 - A sound budget is often a central requirement for responding to a grant or solicitation (e.g., helps to show whether the business has the resources to handle the project)
- **Human Resource Management**
 - Salary benchmarking and staffing issues
 - Fringe benefits (i.e., changes in tax rates, health benefits, etc.)

EXERCISE #3 – BUDGETING ACTION PLAN

Current Budgeting Challenge (as of 1/30/13)	3-Month Progress Goal (By 4/30/13)	6-Month Progress Goal (By 7/31/13)

RECAP

- Budgeting is a management tool that can help to gauge your business's performance as a whole and by project/line of business
- Budget preparation and forecasts should not be managed in a vacuum; consider historical patterns, competitors' performance, customer input, and industry changes
- Income and expense forecasts should be prepared and reviewed regularly, and adjustments made accordingly, to maximize the budget's planning power and control capabilities
- To increase its benefits, budgeting should be integrated into your day-to-day operations, and managed in coordination with other key business functions

Q & A

REFERENCES

- Mohr, A. (2011). *First Person: Money Mistakes of the Rich and Famous*. Retrieved from <http://finance.yahoo.com/news/first-person-money-mistakes-rich-famous-20110106-110400-459.html>
- Change of Budgeting and Forecasting Trend in Companies. (2010). Retrieved from <http://budgetingforecastingprocess.com/change-of-budgeting-and-forecasting-trend-in-companies.php>

CONTACT INFORMATION

LaTaunya D. Howard, CGFM
Assure Budget Solutions
(202) 360-2009

Email:

info@assurebudgetsolutions.com

Web:

www.assurebudgetsolutions.com