

**Manual of Accounting and Financial Reporting for
Pennsylvania Public Schools**

CHAPTER 14
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Chapter 14

The Budgeting Process

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The annual general fund budget is one of the most important legal documents at your school. The Board-approved budget presents expenditure appropriations, which may not be exceeded without an amendment.

The general fund fiscal year budget must be adopted before expenditures may be made from that fiscal year. Without a Board-approved budget, the school has no new spending authority for that fiscal year. Adoption of the budget should also be done prior to setting the tax rate for the budget year.

This Chapter presents the budget process for schools and discusses such important concepts as:

- ❖ Objectives Of Budgeting,
- ❖ Legal Requirements,
- ❖ Encumbrances,
- ❖ The Budget Cycle,
- ❖ Estimates,
- ❖ Budgetary Transfers, And
- ❖ Commonly Asked Questions

❖ Purpose And Procedure

The Pennsylvania Public School Code requires all Local Educational Agencies (LEA) to prepare, present, and adopt an annual General Fund Budget. The budget is a financial plan prepared to estimate the revenue and expenditures required to achieve the educational programs of the school entity for the next fiscal year. Each school entity may also adopt other budget documents to govern all special revenue funds, proprietary funds; such as, cafeteria operations, and capital facilities. The capital budget will encompass not only the next fiscal year but also several future fiscal years. The budget document is essential to ensure the raising of revenues and expenditures of resources consistent with provisions of the constitutions, federal and state laws, statutes, court decisions, board decisions and administrative actions. The budget, when adopted, is also the basis upon which tax rates are set. It is the legal document that places restrictions on amounts spent for stated purposes; it serves as an important management tool; and it can be an excellent public relations tool.

A budget is an outline of educational programs and services with costs affixed to specific purposes to effectively direct the administration in achieving the LEA's goals and objectives. Formal budgets play a far more important role in the planning, control and evaluation of an LEA's operations than in those of the private sector. In schools, the adoption of a budget implies that a set of decisions have been made by school board members and administrators which culminate in matching a school's resources with its' operational needs. The budget also provides an important tool for the control and evaluation of a school district's sources and uses of resources. With the assistance of the accounting system, administrators are able to execute and control the activities that have been authorized by the budget and evaluate performance based upon comparisons between budgeted and actual operations.

In the educational context, budgeting is a valuable tool in both planning and evaluation processes. Budgeting provides a vehicle for translating educational goals and programs into financial resource plans. Thus, planning to meet student educational requirements and goals should be the basis for determining budgetary allocations. This link between instruction and financial planning is critical to effective budgeting. In addition, such a budgeting practice will enhance the evaluation of budgetary and educational performance since resource allocations are closely associated with instructional plans. In this way, the annual general fund budget is not only the financial plan, but also the educational plan expressed in dollars.

GASB Codification 1700.107 states, "The *annual* budget authorizes, and provides the basis for control of, financial operations during the fiscal year. This is the type of budget recommended, whether or not required by law, and that should be appropriately controlled through the accounting system to assure effective budgetary control and accountability." The preparation and Board review process for an annual budget must be conducted and completed prior to the commencement of each new fiscal year. Section 687 of the Public School Code of 1949 requires the adoption of the budget and the necessary appropriation measures required to put it into effect. Section 687 also requires proposed budgets to be prepared at least 30 days prior to the adoption of the annual budget.

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Budgets should be prepared on a basis consistent with the basis of accounting used by the LEA. Without a Board-approved annual budget, the school has no new spending authority for that fiscal year.

OBJECTIVES OF BUDGETING

The purpose of budgeting is to provide the best possible educational opportunities for every student in an educational institution. Budgets should also reflect the administration's ability to manage the financial affairs of the school. Budgets are required to:

- ◆ Be balanced so that current revenues are sufficient to pay for current services;
- ◆ Be prepared in accordance with all applicable federal, state and local legal mandates and requirements; and
- ◆ Provide a basis for the evaluation of the school's service efforts, costs and accomplishments.

BUDGET PROCESS OVERVIEW

The budgeting process is comprised of three (3) major phases: planning, preparation and evaluation. The budgetary process begins with sound planning. Planning defines goals and objectives for the LEA's administration and support services and develops programs to attain those goals and objectives. Once these programs and plans have been established, budgetary resource allocations are made to support them. Budgetary resource allocations are the preparation phase of budgeting. The allocations cannot be made, however, until plans and programs have been established.

Finally, the budget is evaluated, after the close of the year, for its effectiveness in attaining the LEA's goals and objectives. Evaluation typically involves an examination of how funds were expended, what outcomes resulted from the expenditure of these funds, and to what degree the outcomes achieved the objectives stated during the planning phase. This evaluation phase is important in determining the following year's budgetary allocations. In summary, budget preparation is not a one-time exercise to determine how a school entity will allocate funds. A school entity's budget preparation is part of a continuous cycle of planning and evaluation to achieve the school's goals.

❖ **Legal Requirements For Budgets**

The Pennsylvania Public School Code of 1949, as amended, is published in *Pennsylvania School Laws and Rules*, edited by Michael I. Levin, to assist all individuals responsible for the proper administration of the Commonwealth of Pennsylvania's public school system. At least five (5) sections of the School Code address the requirements of various Local Educational Agencies (LEAs) to prepare annual budgets. These Sections include:

Pennsylvania Public

School Code

LEA

Section 687	School Districts 2 nd , 3 rd , and 4 th Class
Section 918-A	Intermediate Units, Summary and Program Budgets
Section 1850.1	Area Vocational Technical Schools
Section 2128	School Districts, 1 st Class
Section 2509.1	Intermediate Unit Special Education Transportation

Title 50, Mental Health, P.S. 4201(5) of the Pennsylvania Public School Code requires an annual budget from intermediate units for State-Funded Early Intervention Programs.

Each Section of the Pennsylvania Public School Code listed above mandates specific procedures in completing budgets for each type of school entity.

Section 687 requires:

- annual budgets from 2nd, 3rd, and 4th class school districts;
- a proposed ensuing year budget at least 30 days prior to adoption of the annual budget on a form provided by the PDE. This budget presents estimates at the service area, major object category, however, many school entities budget to a much greater detail level and may choose to present a more detailed budget to the school board and public;
- public notice must be given at least ten (10) days before any final action is taken on the ensuing year's budget;
- a proposed budget must be made available to the public for inspection at least twenty (20) days before the school board plans to meet and vote on adopting the budget; and
- a final adopted budget must be filed with the PDE within fifteen (15) days of board adoption on PDE prescribed forms.

Section 687 also:

- ◆ **Prohibits** deficit financing; that is, the total amount of the budget may not exceed the amount of funds available for school purposes, including the proposed annual tax levy and State appropriations. Appropriations and reserves must be equal to or less than the fund balance and all estimated revenues available for the budget year.
- ◆ **Allows** unencumbered balances to be transferred from one budget category to another during the last nine (9) months of the fiscal year while prohibiting transfers during the first three (3) months.
- ◆ Funds not appropriated in the budget will be unavailable throughout the year unless placed in budgetary reserve in the original budget.

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- ◆ **Allows** the board to change the budget to accommodate emergencies such as epidemics, floods, fire or other catastrophes. The funds, therefore, shall be provided from unexpended balances in existing appropriations, from unappropriated revenue, if any, or from temporary loans. When temporary loans are made, they have to be approved by a two-thirds vote of the board of school directors.

Section 918-A requires intermediate units to submit annual budgets on or before May 1st, which estimate the cost of operating and administering the intermediate unit programs and services for the subsequent school year.

Section 1850.1 subsection (19) requires the area vocational-technical school board to prepare and submit a budget of proposed expenditures for the subsequent year to the PDE for approval on or before the first day of July of each year.

Section 2128 identifies specific procedures for estimates of expenses by first class school districts. It requires the school board secretary to certify an annual estimate of expenses made by the board to the school controller of the district at or before the time of assessing and levying the annual school tax. The school controller must then keep an account of each item of expenditure as noted in the estimate of expenses or thereafter changed by the board. Each item of estimate should be charged up against all school orders drawn against the same at the time they are approved. None of these estimates are permitted to be overdrawn. The controller must also furnish to the board a monthly statement showing the original amount of each item of estimate, the amount paid out thereon, and the balance, if any, on hand. If any item is exhausted, the board must be promptly notified.

Section 2509.1 contains several detailed procedures for payment on account of transportation for exceptional and institutionalized children. Each year before July 1, every intermediate unit must submit an estimate of the cost of transportation for pupils attending classes and schools for exceptional children, whether or not conducted by the intermediate unit.

Section 609 provides that districts may receive and expend **state and federal** funds for their intended purposes whether or not they were included in the budget. This allows school boards to augment the original budget and authorize the administration to expend these funds without re-opening the budget.

In addition to the Public School Code of 1949, LEAs are expected to abide by statements and interpretations of the Governmental Accounting Standards Board (GASB). In GASB Statement #1, NCGA Statement 1, Principal 9 was adopted, which addresses the budget and budgetary accounting for all governmental entities, including special-purpose governments. Principal 9, found in Budgeting, Budgetary Control, and Budgetary Reporting Codification, Section 1100.109, includes the following three (3) provisions:

- ◆ Every LEA should adopt an annual budget(s).

- ◆ The accounting system should provide the basis for appropriate budgetary control.
- ◆ Budgetary comparisons should be included in the appropriate financial statements and schedules for governmental funds for which an annual budget has been adopted.

❖ Basic Elements

BUDGETS AND BUDGETARY ACCOUNTS

Budget adoption is one of the most significant functions of the school board. Therefore, it should be prepared in conformity with Generally Accepted Accounting Principles (GAAP). *GASB Codification, Section 1900, Financial Reporting*, requires a budget to actual comparative presentation in the basic financial statements of a Combined Statement of Revenues, Expenditures, and Changes in Fund Balances. All General and Special Revenue Fund types, as well as all other governmental fund types should show a comparative statement if an annual budget is legally adopted. Monthly comparative reports are also recommended. The school's budget is presented at a school entity level yet often developed and controlled at the campus level. This is known as site-based budgeting.

Budgetary accounting systems are required if a budget is required for the fund. These systems should include all budgetary accounts to allow the management of your school to control expenditures at the levels budgeted and adopted by the school board. Budgetary accounting also facilitates the preparation of budget to actual comparisons and management decisions.

Your budgetary accounting systems should include budgetary accounts for Estimated Revenues and Other Financing Sources (Accounts 0300), Appropriations, Expenditure Control, Encumbrance Control, and Other Financing Uses (Accounts 0600), along with the subsidiary ledger detail and Budgetary Fund Balance (Account 0780) and reserves. These accounts enable the management of your school to provide appropriate budgetary control measures.

BUDGETING FOR REVENUES

Revenue estimates are based upon a variety of demographic and tax information, as well as projected state and federal subsidy amounts. Estimating revenue from state funding, local property taxes, federal grants and "other financing sources" such as capital leases, long-term debt proceeds, interfund transfers and incoming transfers are critical to the budget estimate.

Although local property tax and state subsidies account for the majority of school revenues, other sources must be considered in completing a district's overall annual revenue estimate. Federal funds and donations from private sources (e.g., private foundations, businesses, etc.) must be forecasted also. In addition, schools must

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examine delinquent tax collection experiences, miscellaneous revenues, rentals, fees charged to patrons, and co-curricular school-sponsored revenue sources.

In evaluating the budget throughout the year, sizable differences between estimated and actual revenues should be investigated by management. Differences may indicate that estimates were made on assumptions that were realistic when the budget was prepared but are no longer feasible or that action needs to be taken so that revenues that were estimated with reasonable accuracy are actually realized. If estimates are no longer realistic, the budget must be adjusted so administrators have a more accurate view of projected revenues for the remainder of the fiscal year.

You should use the modified accrual basis of accounting to estimate revenues of the general fund and all governmental fund types. GASB Statement #33, Accounting and Financial Reporting for Non-Exchange Transactions should be followed when measuring property taxes, income taxes, state and federal subsidies and grants and all other non-exchange transactions with the exception of on-behalf payments received by the school.

GASB Statement #33 states:

Derived tax revenues such as imposed income taxes, should be recognized when the underlying transaction takes place. This requires timely reports from local tax collectors.

Imposed non-exchange transactions such as property tax revenues, licenses, permits and other fees should be recognized when the enforceable claim occurs and time requirements are met. For property taxes, this generally is the date of tax levy, not the date of attachment. Property Tax Revenues are recognized when they become available. Available means ... collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Such time thereafter shall not exceed 60 days. If, because of unusual circumstances, the facts justify a period greater than 60 days, the governmental unit should disclose the period being used and the facts that justify it.

There are four (4) elements comprising the budgetary estimate of the revenue from real estate tax levies:

- ◆ Tax levies for budget year real estate taxes;
- ◆ Delinquent tax levies for budget year real estate taxes;
- ◆ Discounts to be taken on budget year real estate taxes levied; and
- ◆ Penalties and interest to be realized on tax levies for budget year real estate taxes recognized as estimated.

To calculate estimated revenues from state sources, it is necessary to determine the amount of revenues due and payable from state sources during the budget year. The PDE projects your school's share of major state subsidies and posts

these estimates to their web page. We recommend including these projections in your final budget package, if available at the time you develop your budget. GASB Statement #33 states that all government-mandated program revenues, such as state and federal subsidies, grants and contracts be recognized when the eligibility criteria have been met. For instance, when the time period for eligibility has begun and / or when expenditures have been incurred for the required program or services. For example: Basic Subsidy is calculated on prior year data; however, eligibility does not occur until the school year begins and the entitlement is payable to the LEA. The eligibility criteria for most federal grants is the occurrence of eligible grant expenditures. Therefore, most grant revenues will be earned and recognized when the expenditure is incurred. Estimates of other financing sources vary for a school from year to year because of the sporadic or uncertain nature of these transactions. Revenue estimates should be made using the criteria established under the modified accrual basis of accounting.

❖ *Budgetary Accounting For Encumbrances And Expenditures*

ENCUMBRANCES

Encumbrance accounts allow for the recording of legal commitments issued against the appropriation of a fund. Legal commitments include items such as purchase orders for books, supplies, food, etc. and contracts with suppliers, food management companies, transportation providers, contractors, etc. Recording encumbrances is essential to keeping expenditures within the approved budget. An encumbrance reserves a part of the appropriation at the time of commitment to ensure that resources will be available to cover the expenditure when the goods are delivered or the services rendered to the school. It is essential for good management and budgetary control to record expenditure commitments that will be paid later from fund resources. The accounting entry to record a commitment is debit Encumbrances and credit Reserve for Encumbrances.

The encumbrance account does not represent an expenditure for the period, only a commitment to expend resources. Likewise, the account *reserve for encumbrances* is not synonymous with a liability account since the liability is recognized only when goods are received or the services are actually performed.

When the invoice is received and is approved, the budgetary accounts are eliminated and the actual expenditure and related liability are recorded. Any difference between the encumbrance and the expenditure is reflected as an adjustment to the remaining encumbrance balance. The original encumbrance entry is based on the estimated costs of goods and services and may, as illustrated above, differ from the eventual cost of the item.

During the budgetary period, an LEA can determine the remaining amount of the new commitments that can be signed by comparing the amount of appropriations to the sum of expenditures recognized and encumbrances outstanding.

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EXPENDITURES

While the responsibility for developing revenue estimates lies primarily with administrators, expenditure estimates are the shared responsibility of business administrators, support personnel and individual school building principals and administrators. Budget guidelines may provide substantial guidance for the estimation of expenditures through the use of standard cost allocations, per pupil estimates, building allocations or allotments and other board-approved guidelines. Expenditure estimates are critical to the development of budgets whether expenditures are estimated at the building or district level; however, building level is recommended.

LEA administrators should estimate expenditures using Generally Accepted Accounting Principles. Although estimated expenditures are required to the subfunction and major object level only by the PDE, schools should build their budget from their lowest functional level of cost accumulation and then summarize the estimates up to the required levels for reporting to the PDE. LEA administrators should estimate other financing uses, such as debt service payments, authority rentals, and transfers of money from one fund to another using Generally Accepted Accounting Principles.

ENCUMBRANCE LIQUIDATION

An encumbrance may be liquidated in whole or in part or canceled when any of the following situations occur:

- ❖ Satisfactory receipt or legal acceptance of a partial or complete shipment of goods or services;
- ❖ Notice from or failure of the vendor to fulfill terms of the order or contract;
- ❖ Cancellation of the order; and
- ❖ If funds are not available due to lack of funds.

Since many purchase orders are based on catalog prices or quotes subject to change, amounts of encumbrances may vary from the amounts of the expenditures. In any case, the total encumbrance is liquidated at the same amount as originally booked.

APPROPRIATIONS

An appropriation is an authorization for administrators to incur liabilities in the amounts specified in the appropriation during the budget period. An appropriation is considered expended when the authorized liabilities have been incurred. When determining the uncommitted balance of appropriations, simply determining unrealized budgetary revenue is not sufficient. It is not enough to compare budgeted expenditures or appropriations against actual expenditures, encumbrances must be considered also. GASB Codification 1700.129 states “Encumbrances – commitments related to unperformed (executory) contracts for goods or services –

often should be recorded for budgetary control purposes, especially in general and special revenue funds.” Penalties are imposed by law on an administrator who incurs liabilities for any amount in excess of that appropriated, or for any purpose not covered by an appropriation, or who incurs liabilities after the authority to do so has expired. Prudence dictates that each purchase order and each contract be reviewed before it is signed to determine that a valid and sufficient appropriation exists to which the expenditure can be charged when goods or services are received and that funds are still available to cover the commitment. If a review indicates that a valid appropriation exists and it has an available balance in excess of the amount of the purchase order or contract being reviewed, the purchase order or contract legally may be issued without violating the approved budget. It is imperative to record the encumbrance against the appropriation before releasing a contract or purchase order to a vendor. This ensures available funds prior to incurring a liability on behalf of the school.

Notice that the issuance of purchase orders and/or contracts has two effects: (1) the encumbrance of the appropriation that gave the governmental unit the authority to order goods and services, and (2) the starting of a chain of events that will result in the LEA incurring a liability when the purchase orders are filled and the contracts executed. Both effects should be recorded in order to assist administrators in avoiding overexpended appropriations and to plan for the payment of liabilities on a timely basis.

When goods or services for which encumbrances have been recorded are received and the supplier’s invoices are approved for payment, the accountant should record the actual expenditure and actual liability. The encumbrance and encumbrance reserve should then be liquidated. The amount set aside in the Encumbrance control account and the Reserve for Encumbrances account for the purchase order will be cancelled when the expenditure is recognized. For example, a purchase order is written for \$20,000 and later the actual invoice is received with the delivery in the amount of \$18,250. The entry to record this transaction is:

Reserve For Encumbrances	\$	20,000.00	
Expenditure Control / Subsidiary Accounts		18,250	
Encumbrances			\$ 20,000.00
Vouchers Payable			18,250

Do not cancel the encumbrance until the expenditure is recorded. Canceling the encumbrance before the invoice is processed and recorded could result in the cancellation being transacted in one (1) accounting period and the recording of the invoice in another. If this should happen, the available balance at the end of the initial accounting period would be overstated.

Expenditures and the liability account must both be recorded in the actual amount due the supplier. The fact that estimated and actual amounts differ causes no accounting difficulties as long as goods or services are received in the same fiscal period.

YEAR-END TREATMENT OF ENCUMBRANCES

At the end of the fiscal year, all remaining encumbrances are considered reservation of fund balance not liabilities. They will become a liability when the goods and / or services are received in the following fiscal year. The budgetary estimate should include an estimated Reservation of Fund Balance as part of the funds available in the following fiscal year. This is recorded on the General Fund Budget Form, PDE-2028, in the “Estimated Beginning Fund Balance Available for Appropriation.” This estimated fund balance reservation is offset by an “Appropriation of Prior Year Encumbrances” line item in the same amount, which represents the appropriation for prior year encumbrances. Encumbrances budgeted in the prior year and carried forward must be shown in the subsequent year budget; however, these amounts do not need to be budgeted for a second time. If the LEA allows encumbrances to lapse, even though it plans to honor the encumbrances, the appropriation authority expires and the items represented by the encumbrances are re-appropriated in the following year’s budget. When outstanding encumbrances are allowed to lapse at year-end, but the LEA intends to honor the encumbrance, the commitment should be disclosed as a reservation of fund balance and in a note to the financial statements. Authorization for the eventual expenditures would be part of the following fiscal year budget.

LEA administrators should estimate expenditures using Generally Accepted Accounting Principles. Although estimated expenditures are required to the subfunction and major object level only by the PDE, schools should build their budget from their lowest functional level of cost accumulation and then summarize the estimates up to the required levels for reporting to the PDE.

FUND BALANCE

The difference between governmental fund assets and liabilities is referred to as the fund balance. For LEAs, the fund balance is the difference between total assets and total liabilities as shown on the Balance Sheet or the Statement of Revenues, Expenditures, and Changes in Fund Balance in the Annual Financial Report. A school’s fund balance is between five (5) and ten (10) percent of the school’s general operating budget. However, there is no industry standard or state-mandated fund balance ceiling or floor.

To estimate fund balances that will be available to carryover into the next budget year, the amount of revenues to be received and accrued through 06/30/XX must be estimated. Then, a projection of expenditures, fund transfers, and possible budget savings must be deducted from this amount. Because this information must be available several months before the end of the fiscal year, it is important to conservatively project all adjustments and accruals so not to inflate the amount of funds available for appropriation in the subsequent year. This can be done best by running monthly budget to actual comparisons and year-to-year actual comparisons at various points throughout the year. Based on this information, projected revenues and appropriations can be adjusted and various fund balances projected through 06/30 of the current year.

Budgeting for and maintaining adequate fund balances allow school boards and superintendents to maintain their educational programs and services with level tax adjustments. They also provide financial stability in emergency situations so that it is certain that employees and vendors are paid on time. Fund balances reduce interest expense on interim borrowings. In addition, stable fund balance history appeals more to underwriters and other creditors when construction projects are undertaken and the school must enter the bond market.

THE BUDGET CYCLE

❖ Preparation



The beginning of the budget cycle should be started early in the year preceding the budget year. The organizational structure of a school, the size and complexity of its administrative structure, and the level of centralization in budget development will affect the budget development process and the time required to adopt the final budget document. Beyond the budgetary requirements for federal and state programs, an LEA's preparation process and the related budget responsibilities largely will be determined by the school board and the chief school administrator.

Preparing the budget is not synonymous with preparing a cash flow statement. The budget projects the amount of resources available to meet the prospective financial obligations of an LEA. A cash flow statement, on the other hand, is prepared to ensure sufficient cash is available to pay the obligations of the LEA as they become due. A cash flow statement is a projection of cash only and is not integrated into the accounting system as is a school's budget.

An effective budget system must be conducted on a year-round basis. Preparations should include an assessment of the past to see if actual and estimated revenue resulted in favorable or unfavorable results. There should also be projections based on past experiences as well as future expectations such as new program needs, taxable property projects, new businesses and industry, anticipated enrollment trends, inflation, etc. This analysis may require personnel officers, transportation coordinators, food service managers, plant managers, federal program coordinators and at times assistance from outside consultants.

The budget preparation and analysis are followed by board review and adoption of the budget. The remainder of the year is devoted to budget control, which is comprised of comparing estimated revenues and appropriations with actual transactions and evaluating budget adjustment requests. This process is called the operating budget cycle.

Budget preparation and administration are important aspects of overall district operations. Providing adequate resources for programs within the constraints of available funding presents administrators with a significant challenge. The budgeting process is the beginning of the financial cycle of the LEA.

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BUDGET ESTIMATES

The two categories of financial resources that will be available for the upcoming budget year are beginning fund balances available for appropriation and projected revenues for the upcoming year. Both estimates are critical and accuracy is of extreme importance to the entire budget process.

Business managers should be extremely careful when appropriating amounts from the fund balance. Fund balance amounts may result from a one-time funding source, e.g. sale of assets and therefore will not be available to fund ongoing programs. If there is any uncertainty that the resources will materialize we recommend placing the estimated fund balance amount as of July 1 in the budgetary reserve account when adopting the budget. Fund balance should be appropriated for one-time expenditures only and should be placed in the estimated ending fund balance on the proposed budget if the LEA's fund balance policy requires this amount to be reserved for future year's projects.

Because a larger proportion of the total financial resources of an LEA is acquired from revenue, the revenue estimate has a more critical impact on the overall budget. However, there are normally many different categories of revenue: a shortage of receipts in one (1) category can often be completely offset by greater than expected receipts in another. There can be significant differences between actual revenue and estimated revenue in individual categories, but total receipts must come very close to the total estimate or adjustments must be made to appropriated amounts.

The three (3) basic resources used in developing revenue estimates are: (1) historical trends; (2) national, state and regional economic conditions; and (3) identifiable local events that will materially affect the LEA's income.

Analysis of historical trends in growth or decline of revenue by category is an easy and reliable method to begin the projections. Actual fiscal year receipts, as well as quarterly receipts of recent years, should be compared, and the original budget estimates should be compared against the actual revenues. Unusual increases or decreases that cannot be explained should alert the analyst that additional research is probably justified to determine that incorrect data has not been used.

National, state and regional economic indicators should be examined based on current points of reference and cyclical trends. Since the 1980s, changes in the global economy have had wide-ranging ramifications for even the smallest LEAs. Because of this, finance and budget directors must be aware of the developments in their own localities, as well as of events occurring in Washington, on Wall Street, in Harrisburg, and in various points around the world.

Locally, new businesses and residential development plans opening in the upcoming year will produce real estate taxes that will affect projected revenues. At the same time, plant closing and trends in property values must also be considered. State and federal funding may also be adjusted to reflect changes in economic conditions.

Other important factors are changes in tax rates, fees, interest rate yields, projected balances available for investment, and the enactment of state laws and / or federal provisions that may hinder or enhance the LEA's revenue-raising capabilities.

A staff budget committee is often formed to handle the consideration of these and many other factors in projecting revenue for the upcoming year and trends in longer-term income estimates. This committee should consist of key management and the professional staff who are closest to the various factors affecting the most important revenue sources. In turn, the committee members should seek feedback from the various departments concerning the conditions and trends that may affect the upcoming revenues. The budget committee should be activated early in the school year so they can play a part in formulating the mid-year budget report. The committee should then meet throughout the budget year in order to adjust the estimates as new information is received. Though projections may not always be perfect, detailed analysis, identification of economic trends and local developments, and continual monitoring by a competent review team will produce the best possible results.

The same basic methods used to project revenues are used to estimate expenditures. The first step is usually the analysis of historical trends. Second is a detailed analysis, which includes identifying past expenditure patterns at each activity level over several years and projecting the need for new programs, program enhancements, salary adjustments, position adjustments, program cuts, and debt service needs, and any other unusual cost adjustments expected in the coming year.

Personnel appropriation requests must include the expenditures needed for salaries and fringe benefits, as well as the authorization to fill a specific number of positions in designated classifications. These requests become the foundation for position control plans during the year to ensure that departments do not hire more than the authorized number of employees. They also ensure that personnel adjustments, such as reclassification of positions, are not included as part of the budgetary process but rather reviewed during the year as required.

Materials, supplies, and equipment needs based on cost standards developed by the purchasing department should be included in the budget document. Requests for equipment other than the standard types should be evaluated by determining availability of funds for the equipment, assessing similar equipment already in use, examining its maintenance and replacement data, and checking its ability to meet the needs of the LEA. Acquisition requests for any equipment, especially the more expensive and less frequently used, should be analyzed to determine whether a purchase or rental decision would be more economical.

A thorough review for completeness and accuracy should be performed after an LEA's proposed budget has been drafted. The review should include a check that:

- ◆ The required summaries, schedules, and detailed information forms are included;
- ◆ A recalculation of figures to verify accuracy;

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- ◆ An in-depth analysis of the reported number and classification of employees and their salaries and fringe benefits has been completed;
- ◆ A check that the figures in other appropriation categories, such as supplies, materials, and equipment, following standard guidelines has been completed;
- ◆ The appropriation requests have been analyzed against appropriations and actual expenditures of previous years and program revisions planned; and
- ◆ Unusual growth trends or requests for increases in appropriations for services have been closely examined to determine whether they are justified under the existing budget policy.

The business manager should project the non-departmental expenditures to complete formation of the LEA's draft budget. These expenditures typically include:

- ◆ interest and retirement of debt;
- ◆ pension fund costs;
- ◆ premiums for liability and property insurance;
- ◆ workers' compensation claims; and
- ◆ general charges for rent, utilities, and other costs applicable to the agency as a whole.

A budgetary reserve is usually set aside to cover unexpected expenditures, to provide for sufficient cash flow, and to cover potential increases in employee salaries or benefits.

The business manager then determines whether the budget balances by comparing the available resources for the upcoming year with the requested appropriations and required reserves. If there are any amounts budgeted in excess of available funds, the business manager can assign various department guidelines for reduction of requested appropriations or propose new revenues to resolve the imbalance.

A budget that is balanced and reflects the priorities of the administration, i.e., the LEA's board of directors, and the general constituency, should be produced by the end of the business manager's review.

❖ ***Financial Forecasting And Planning***

Financial forecasting is the practice of projecting the quantitative impact of trends and changes in a school district's operating environment on its future operations. It uses current and historical data to predict changes that could impact a school's status in the future. It is, therefore, an integral part of a school district's ongoing planning efforts.

Financial forecasting is important for several reasons.

- ◆ First, forecasting facilitates planning efforts by quantifying the future costs / benefits of strategic decisions. Thus, budgetary priorities may be evaluated based upon their long-term impacts.
- ◆ Second, forecasting makes clear trends, need, and issues that must be addressed and evaluated in the preparation of budgets.
- ◆ Finally, forecasts provide valuable insight into future issues that may affect the LEA allowing administrators to deal with them proactively, rather than reactively.

Although financial forecasting is an ongoing process, it is most important as a component of budget development. The reasons for this importance are two-fold. First, forecasting for both financial and related items (e.g. enrollment projections), creates a basis for assumptions made in the preparation of budgets. Forecasts of projected enrollments, property tax base and revenues, costs associated with salary adjustments, etc. are important elements in setting baseline budgetary guidelines for the school district. Second, forecasting provides fiscal impact analysis that may be integrated into the budget development process. Thus, current budgetary decisions may be evaluated for their long-term results.

A variety of financial and related forecasts are prepared during the budget development process. These forecasts include, but are not limited to:

- ◆ *Student enrollment projections* (can help project state aid, classroom size, number of classrooms and buildings needed, number of faculty and staff needed, *types and numbers* of students to be educated).
- ◆ *Revenue projections* (projects future local, state, and federal resources). During the budget development process, revenues and expenditures should be forecasted for the subsequent three (3) to five (5) fiscal years. This forecasting period captures the long-term impact of budgetary decisions necessary for evaluation.
- ◆ *Expenditure projections* (capital costs, operating costs, and state mandates). Forecasts of capital improvement costs should be based upon a maintenance planning process that is a component of overall district planning, rather than ad hoc estimates. Expenditure forecasts should project costs for the following major expenditure categories: (1) payroll, (2) professional and contracted services, (3) supplies and materials, (4) other operating costs, (5) debt service, and (6) capital outlay. Student enrollment projections are critical in estimating many of these expenditures since salaries and benefits are based partly on enrollment projections and state mandates concerning class size, minimum salaries, etc. Other expenditures such as supplies and materials also may be based upon student enrollments. Costs not related to enrollment levels such as utilities, insurance and maintenance costs are based upon historical data incorporating anticipated volume / rate changes.

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In preparing revenue and expenditure forecasts, some basic assumptions must be made. These may include assumptions concerning levels of state and federal funding, inflation rates, growth rates, class size, fund balance levels, etc. Historical data and using a number of data sources may be used to aid in the development of these assumptions. These assumptions should be developed and reviewed by district administrators. When the budget process is reviewed by the board, such base assumptions should be made explicit. This information allows the board to understand those forecast areas that may be revised at some future date due to changes in their base assumptions.

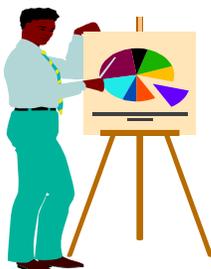
❖ *Review And Approval Of The Budget*



The final review of the budget before it is presented to the school board is made by the chief school administrator who may consult with the business manager and others involved with preparation of the budget. In addition to its value as a review of budgetary allocations, this review familiarizes the superintendent with all aspects of the preliminary budget for his / her presentation of it to the school board.

During the review process the school should review the budget data for the following characteristics:

- ◆ The reported amounts are for the current fiscal year only.
- ◆ All applicable funds are reported.
- ◆ For each reported fund, revenues, expenditures, other resources, other uses and fund balances are reported, if applicable.
- ◆ Reported budget amounts are consistent with amounts reported in prior years or, if amounts are inconsistent, the school can identify a valid reason for the inconsistency.
- ◆ Budgeted fund balances are the balances estimated as of July 1 of the current fiscal year. This amount should be the same as or close to the closing fund balances on June 30 of the fiscal year immediately preceding the budget year.
- ◆ If the audit for the prior fiscal year is complete, the budgeted fund balances should be audited figures; if the audit is not complete, the budgeted fund balances are the unaudited or projected amounts.
- ◆ In addition, schools should analyze certain budget amounts for account codes with special significance, such as taxes.



The presentation of the preliminary district budget to the school board may take the form of budget workshops or retreats. These working sessions familiarize board members with the budget process,

preliminary budget and significant budgetary issues (e.g. state or local revenue shortages). At this stage of budget review, it is important for the school board to reach consensus on the objectives and priorities of the budget and to provide feedback to district staff on proposed revisions. The school board also should consider the long-term implications of resource allocations, expenditure trends and tax rates. When a tentative budget has been established, the LEA should investigate funding options. Funding for a program may come from multiple sources, such as local taxes and one or more federal grants. As funding options are evaluated, the initial budget plan may have to be adjusted to reflect more realistic funding levels.

ADVERTISING, PUBLIC HEARINGS AND ADOPTION OF THE BUDGET

Advertising the budget and public hearings are the final steps in the budget development process. These actions are legally mandated by the Pennsylvania Public School Code of 1949, as amended. The hearings serve as the final opportunity for public review of the proposed budget. They typically include a presentation of a summarized version of the proposed budget by the board president, the chief school administrator or the business manager. Significant budgetary issues such as tax rate changes and student enrollment trends may be similarly reviewed before the board hears public testimony.

- ◇ **For 1st Class school districts**, the board of directors must, on an annual basis, at or before the time of levying the annual school taxes, prepare an appropriate estimate of the amount of funds that will be required by the school in its departments for the following fiscal year. This annual estimate should be distributed to the respective classes of expenditures of the districts as the board of public education may determine. The total amount of this estimate cannot be greater than the amount of funds, including the proposed annual tax levy and state appropriation available for school purposes in the district. The board secretary must properly certify the annual estimates to the school district's financial officer.

In addition, the school board must publish a notice that the budget has been prepared and is open to public inspection at the office of the board. This notice must appear at least once in two (2) newspapers of general circulation printed in the municipality in which the school district is located. The advertisement must also include a notice of public hearing on the proposed budget, scheduled for at least ten (10) days before final action is taken upon any budget.

- ◇ **For 2nd, 3rd and 4th Class school districts**, the school board shall prepare a proposed budget at least 30 days prior to the adoption of the annual budget. Final action shall not be taken on any proposed budget until after ten days public notice.

The proposed budget must be printed, or otherwise made available for public inspection to all persons who may interest themselves; at least 20 days prior to the date set for the adoption of the budget. School districts of the 2nd, 3rd

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and 4th class should follow the advertisement guidelines previously listed for 1st class districts, above.

NOTE: GASB Codification 2400.105, specifies, “Where financial statements prepared in conformity with GAAP do not demonstrate finance-related legal and contractual compliance, the governmental unit should present such additional schedules and narrative explanations in the comprehensive annual financial report as may be necessary to report its legal compliance responsibilities and accountabilities. In extreme cases, preparation of a separate legal-basis special report may be necessary.”

Following these presentations, individuals and interest groups are given the opportunity to present their testimony / feedback on the proposed budget. Following the completion of the public hearings, the school board may legally adopt the budget. Once the budget is legally adopted, funds are then considered available for expenditure.

BOARD ADOPTION OF THE BUDGET

The board of school directors will adopt the budget and the necessary appropriation measures required to implement it after making any necessary revisions and changes. The total amount of the budget cannot exceed the amount of funds available.

A majority of the members of the board of school directors, also known as a quorum, must vote in favor of the budget in order to approve it. Section 508 of the School Code stipulates that the affirmative vote of a majority of the members of the board of school directors in every district, duly recorded (roll call), showing how each member voted, shall be required in order to take action on a number of subjects including adopting the annual budget and levying and assessing taxes.

Failure to have five (5) affirmative votes renders action of the board void and unenforceable. Failing to adopt a budget by July 1st causes the district to lose authority to expend funds.¹

SUBMISSION OF THE BUDGET

Schools must file a copy of the budget with the PDE on Form-2028 **within 15 days after adoption.**

NOTE: The Pennsylvania Public School Code of 1949 requires Intermediate Unit Annual Budgets to be filed no later than May 1st.

School districts must also file a copy of their budget annually with both the House and Senate Education Committees. Charter schools, vocational-technical schools, special jointures and intermediate units are exempt from this requirement. Intermediate units

¹ Understanding School Finance, 1987 Revision, Pennsylvania School Boards Association, New Cumberland, Pennsylvania, Page 98.

must file their General Budget, PDE-2054, with the PDE Bureau of Budget and Fiscal Management. These filing procedures are available on the PDE web site.

MONITORING THE BUDGET

As budgeted funds are expended, periodic monitoring of the budget should be conducted. The school's accounting system normally generates expenditure and encumbrance information at least on a monthly basis. To review budget performance, this information is compared with spending plans. Annualized budget summaries which project the impact of current expenditures on year-end results are useful in this effort.

In most schools, reviews of budget-to-actual comparisons are done monthly. Reporting periodic budget / actual results to the school board is customary in most districts. This reporting relationship should not be interpreted to mean that the board manages budget implementation. That responsibility is ultimately the chief school administrative officer's; however, school board members should be given periodic updates on budget results and be informed of significant budgetary issues.

❖ Budgetary Transfers

Unforeseen events or changes in priorities, which occur during the year often require a redirection of budgeted funds. The budget is not intended to hinder these changes. Section 687 (d) of the Pennsylvania Public School Code permits school boards to approve budgetary transfers during the last nine (9) months of the fiscal year. Transfers may not be made after the end of the budgeted fiscal year. At the LEA level, any amendment that would change the budget requires formal board approval.

Budgetary transfers reallocate budgeted funds from appropriation / subfunction or service area and purpose / object level to another. These budget changes are usually the result of unexpected levels of expenditures in certain categories requiring an amended budget for legal compliance. All necessary budget amendments must be formally adopted by the school board and recorded in the minutes to the board meeting.

To provide an adequate audit trail for budget amendments, the minutes should include the original budget amount by subfunction and major object; the amount of the amendment by subfunction and major object; and the amended budget amount by subfunction and major object.

The LECS Comptroller's Office and Auditor General's staff have agreed that budgetary transfers require the following board approvals.

- ◆ **For transfers between subfunctions** (i.e., subfunction 1100 to 1200) **prior** board approval is required. For example, a transfer from 1100-100 to 1200-100.
- ◆ **For transfers between major objects within the same subfunction** (i.e., object 300 to 400) **subsequent** board approval is required. For example, a transfer from 1100-100 to 1100-200.

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❖ Augmenting the Budget

Section 609 of the Pennsylvania School Code allows schools to expend unbudgeted State and Federal funds without reopening their budget. Whenever Federal or State funds are made available to school districts, the board of school directors may use those funds for the purposes for which they were made available even though provisions were not made prior to closing the annual budget. However, this Section of the Code does not justify or support a school not budgeting any state or federal funds within their general fund budget. Federal funds must be accounted for within the general fund. This estimate should be included as part of the school's general fund budget.

Section 609 also provides that if the General Assembly establishes a law providing for the levy of taxes within a school district, the school board may use those funds for general school purposes despite the fact that no provisions were made in the annual budget.

If additional local funds or other financing sources become available after the budget has been closed, the school board **must** reopen the budget for public inspection. When reopening the budget, a school must follow all advertising, public inspection and adoption requirements as done when adopting the original budget.

❖ Commonly Asked Budget Questions

1. Should federal funds be included in the general fund budget?

School districts, area vocational-technical schools, special program jointures, and charter schools must include their federal funds within their general fund budget, PDE-2028. Although you may not know the exact amount of the federal grants your school will receive, you should estimate to the best of your ability the federal grants you expect to receive. You should not wait for confirmation of federal grant awards from the PDE before including them as part of your general fund budget.

2. What basis of accounting should be used to prepare the budget?

You should use Generally Accepted Accounting Principles (GAAP) and the modified accrual basis of accounting to prepare the budget. Do not use the cash basis to prepare the budget.

3. Would accounting for a debt refinancing through the general fund, without appropriation authority, result in a violation of the School Code?

Yes, accounting for debt refinancing without appropriation authority violates the School Code requirement to budget all funds required to operate the school.

4. Should a school reopen its budget to reflect the proper accounting to record a capital lease?

Yes, a school must reopen its budget to properly account for a capital lease. GAAP requires that accounting for a capital lease be reported as an “other financing source,” and the defeasance of the old debt be reported as an “other financing use” in the district’s budget. It would be necessary for the district to reopen its budget to show these items correctly.

5. How should a school handle the spending of any additional state or federal dollars that were received during the year and not budgeted for?

Section 609 of the Pennsylvania Public School Code provides authority to spend state and federal dollars received during the fiscal year, even if not budgeted for originally. A board resolution is necessary to authorize spending of such funds. However, only a simple majority is necessary. The need for a vote of two-thirds of the board is not necessary.

6. Should a school reopen its budget to include additional unanticipated “other financing sources” that have become available during the fiscal year?

Yes, a school must reopen its budget to include additional unanticipated “other financing sources” such as proceeds from notes and loans that have become available during the fiscal year to establish authority for expenditure of the funds.

7. What procedures should schools follow when reopening their budget?

When reopening the budget, the school must follow the same requirements used in adopting the original budget. This includes advertising and holding public hearings. Schools may not reopen a budget after the end of the corresponding fiscal year (June 30).

8. If a school receives additional unanticipated local funds, must they reopen the budget to gain spending authority?

If local funds become available during the fiscal year that were not originally budgeted for in the adopted budget, there is no authority to spend these new funds. Therefore, a school must reopen their budget to establish proper appropriation and expenditure authority for these funds.

10. Are schools limited as to when they can make budgetary transfers?

Section 687 of the School Code restricts budgetary transfers to the last nine (9) months of the fiscal year (October through June). School administrators are not authorized to make amendments or budgetary transfers after the end of the fiscal year.