

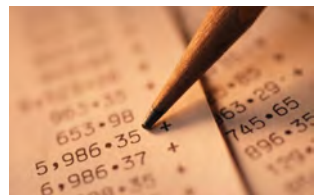


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GOVERNOR'S CENTER FOR  
LOCAL GOVERNMENT SERVICES

# Financial Monitoring Workbook

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# Financial Monitoring Workbook

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# I. Financial Monitoring System

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## Introduction

Although most municipal elected and appointed officials are aware of the numbers that make up a local government's annual operating budget, the numbers are only closely examined when the budget is being reviewed in anticipation of its adoption and with consideration typically focused on the current and next year. As demands for services increase and funding resources become more limited, local officials working to insure a community's continuing viability should develop a comprehensive, long-term understanding of the municipality's financial condition. To do this, five to ten years of data should be evaluated through the use of a financial monitoring system to create an “early warning” process which calls attention to problem areas *as they emerge and before problems get out of hand*. Information and understanding derived from such a system then can be used by local officials in their short and long-range priority setting and decision making.

The financial monitoring system presented in this workbook consists of a series of financial factors. The factors are calculated, graphed, interpreted and evaluated against previous results and projections. Once the system is initially established, the operator need only enter current year data to extend and update prior years' results.

Information generated through a financial monitoring system allows local officials to determine whether their municipality has the potential to independently support services and capital programs on a continuing basis. The municipality's capacity for self-sufficiency can be determined by assessing its short and long-term financial condition in four areas:

- **Cash Solvency** - Will the municipality consistently, on a 30-to-60 day basis, generate sufficient cash to pay its bills?
- **Budgetary Solvency** - Will the municipality generate sufficient revenue over the twelve-month fiscal year to meet its current expenditure responsibilities and avoid a deficit?
- **Long-run Solvency** - Will the municipality over the long term pay all of its current expenses as well as provide funding for future expenses incurred today but payable in the future? Examples of long-run obligations include pensions, post retirement benefits, accrued vacation and sick leave and replacement or maintenance of the capital infrastructure.
- **Service Level Solvency** - Will the municipality over time be able to provide basic public services at levels adequate to meet the health, safety and welfare needs of its citizens? In addition, to assure service level solvency assumes that a municipality is able to attain and sustain cash, budgetary and long-term solvency.

Analyzing the financial factors to determine whether a municipality can meet the four types of solvency is recommended for local governments in danger of sliding towards fiscal distress, as well as directed to communities which:

1. have previously recognized that problems exist and need to create a better understanding of those difficulties;
2. believe problems may exist but don't know what the exact nature of the problems are; or
3. are currently in good financial condition but want to create a way to review and evaluate circumstances that could give rise to future problems.

In 1984, the Intergovernmental Cooperation Program (ICP) of the Allegheny League of Municipalities created

a financial monitoring system based on factors relevant to smaller local governments. A number of comprehensive and sophisticated systems, including those developed by the Government Finance Officers Association (GFOA) and the International City/County Management Association (ICMA) as well as several developed for specific municipalities, were reviewed. Over one thousand individual factors were examined. Ultimately, 24 factors plus the trend analysis technique were incorporated into ICP's system. The primary focus of ICP's approach was to "keep it simple" in order to facilitate wider use and understanding of the system. Another objective was to make it "flexible" to allow factors to be added or deleted depending on individual municipal characteristics and preferences.

This *Workbook* is a revision of ICP's initial effort. Two factors have been added to the system, while others have been refined. The factor commentaries and recommended remedial actions have also been expanded.

## Description of the System

The financial monitoring system presented here contains 26 factors. The factors cover revenue and expenditure trends, operating position, unfunded liabilities, debt structure and investment and maintenance of capital facilities.

Not all factors will apply to every community and the relevance of some factors for a community may change from time to time. While the factors can be analyzed over as few as three years, using at least five or up to ten years of data to initially establish the system is strongly recommended. This *Workbook* includes suggestions about where to locate the information required to calculate each factor. A consistent source of data should be used for the analysis. For instance, if the accounting system has changed from cash to modified accrual, the factors should be calculated beginning with the first year of the accounting system change to avoid inaccurate interpretations.

After calculating the factors, trends should be examined in either chart or graph formats and evaluated as "unfavorable," "stable" or "favorable." No single trend should be used to indicate a good, stable, or bad financial condition. Rather, each trend should be viewed as a circumstance within the system that may warrant further examination to determine why it exists.

Once an assessment of the factors is completed, a color-coded Factor Summary Chart of all factors should be created to provide an overview of the results. Finally, the system suggests that, where appropriate, an "action agenda" be developed to address unfavorable results. The proposed action strategies include changes in current legislative policies and management practices as well as recognition of uncontrollable external influences. It is suggested that the local political culture, community resources and any intergovernmental constraints be considered as the factors are analyzed and corrective actions are identified.

Overall, the best way to effectively use a financial monitoring system once it has been established is to update it each year and present the results for review by the governing body. Two of the most appropriate times for this review are after the annual audit report is received or prior to preparation of the annual budget.

## How to Use the System

The financial monitoring system for small communities provides a way to organize and understand important information that already exists within municipal records. The system can be implemented by existing staff or become a student internship project. While it does not require the use of complex analytical tools or a computer, a personal computer with spreadsheet and graphics software makes calculation and graphing much easier. The system combines financial and non-financial data and uses nationally recognized credit rating agency criteria to assess some of the trends.

## Steps in the Process

1. **Secure a commitment** from local officials to examine the municipality's financial and operational performance on an annual basis, identify problems, develop solutions and implement changes where possible.
2. **Individuals should be assigned** to gather information and work through the financial monitoring system. If in-house staff resources are limited, college interns are a good alternative to assist with the data gathering, calculation and graphing tasks.
3. **Select the factors to be analyzed.** Each factor has a separate work sheet providing a description of the factor, instructions about how it is calculated, data sources and guidelines on the interpretation of trends and suggested remedial actions. Eliminate only factors that are clearly inapplicable. For instance, if the municipality has no debt or unfunded pension liabilities, do not include them. All other factors should be calculated to present as broad a perspective as possible.
4. **Compile the data.** After selecting the factors for analysis, the factor work sheets should be reviewed and a list of required data compiled.
5. **Complete the calculations.** As previously noted, when initially working with the factors, a minimum of five years, four prior years plus the most recent year for which information is available, should be calculated.
6. **Graph the trends.** Once the calculations are completed, graph the trends. The factor work sheet includes a grid for the graph if the work is being done by hand.
7. **Assess the trends.** The assessment of each trend should start with determining whether it is favorable, stable or unfavorable. If unfavorable or inconsistent trends exist, further examination to identify the magnitude of the problem and reason for the inconsistency or difficulty is warranted.
8. **Factor Summary Sheets.** Once all factors have been evaluated as favorable, stable or unfavorable, the ratings should be coded as green, yellow or red respectively and transferred to the Factor Summary Sheets.
9. **Action Planning.** Factors receiving unfavorable ratings should be reviewed by the municipality's chief administrator or finance officer in relation to the action items included with each factor. Consider any mitigating circumstances possibly causing a temporary problem or any ongoing factors affecting the trend long term. Each trend should also be compared to regional or national circumstances, as appropriate. Further evaluation should be undertaken to gain a better understanding of any trend that causes concern. Results of the analysis and recommended solutions and actions should be reviewed with local officials. Strategies for change and the person responsible for implementing solutions should be indicated on an Action Agenda.
10. **Monitor the Action Agenda.** Periodically, the legislative body should review the progress on action agenda items.
11. **Maintain the Financial Monitoring System.** Each year, the factors, graphs, trend analysis, interpretations, and the action agendas should be updated.



## Illustration: Revenue Per Capita

An illustration based on **Factor 1: Revenue Per Capita** is provided to demonstrate how the financial monitoring system works.

### FACTOR 1: REVENUE PER CAPITA

**Description:** This factor shows how a municipality's revenues are affected by changes in population. It suggests two questions. If revenue per capita is increasing, is it due to growth of the tax base or an increase in tax rates and/or types of revenue resources? If revenue per capita is decreasing, has the population increased without corresponding growth in the tax base or has the tax base stabilized or decreased? If the trend presented by this factor is negative (slopes downward) and revenue per capita is decreasing, a municipality might not be able to maintain service levels unless new sources of revenue are found. It may be useful to substitute the number of households for the population value in this calculation, especially if the total population is constant or decreasing. In such circumstances, the total number of households may be stable or increasing, while the household size actually may be decreasing. This factor should be examined in conjunction with expenditures per capita.

**Formula:** 
$$\frac{\text{Total Operating Revenue}}{\text{Population}}$$

#### Data Sources:

- **Total Operating Revenue** - Annual Audit and Financial Report including General Fund, Liquid Fuels Fund, Special Revenue funds and any other funds with operating revenues such as enterprise funds.
- **Population** - Most recently available population estimate. Use the same source each year.
- **Households** - Most recently available data from utility or solid waste collection billing records. Use the same source each year.

**Warning Signal:** Decreasing operating revenue per capita over time.

**Constant Dollar Comparisons:** Revenue and expenditure data should be adjusted to offset the effects of inflation by translating “current” dollar values into “constant” dollar values. This allows a comparison between two years based on real dollars, that is, without consideration for changes due to inflation.

FACTOR 1: REVENUE PER CAPITA					
Formula: $\frac{\text{Total Operating Revenues}}{\text{Population}}$					
	2005	2006	2007	2008	2009
Total Operating Revenues	\$755,000	\$784,000	\$765,000	\$756,000	\$763,000
Population	1,400	1,400	1,400	1,400	1,400
Revenue Per Capita	\$539	\$560	\$546	\$540	\$545

The effects of inflation are then discounted by adjusting all dollar amounts to the dollar value for a base year. Adjustments to constant dollars are made using the Consumer Price Index (CPI). Whenever values have been adjusted for inflation, it should always be noted on the table or graph to avoid misinterpretation of results. The adjustment process takes five steps. The chart displaying the data for the example, Factor 1: Revenue Per Capita is presented below. The April CPI data for the years, 2005 – 2009 was used to make the adjustments.

1. **Select a base year.** If a series of years is being compared, the first year is generally used. For this example, the first year is 2005.

2. **Find the CPI for the years to be analyzed.** CPI information eastern (Philadelphia) and western (Pittsburgh) Pennsylvania is available at most public or university libraries or on the Internet at [www.stats.bls.gov/ro3home](http://www.stats.bls.gov/ro3home).
3. **Identify the CPI for the base year and for the year to be adjusted.** For example, the CPI for 2002 is 144.5 and the figure for 2003 is 148.2.
4. **Compute the adjustment factor.** Divide the CPI for the base year by the CPI for the year to be adjusted. For example, the adjustment factor to convert 2004 is:

$$\frac{\text{CPI for the Base Year (2005)}}{\text{CPI for the Year to be Adjusted (2006)}} = \frac{195.3}{201.6} = .969$$

5. **Multiply the figures to be adjusted by the adjustment factor.** In the above example, the 1994 actual revenue is converted into 2002 dollars by:

$$\$755,000 \times .969 = \$731,595$$

6. **Repeat steps 2 – 5 for each year to be adjusted.**

EXAMPLE: FACTOR 1 – REVENUE PER CAPITA CONSTANT DOLLAR COMPARISONS						
Year	Operating Revenue	Revenue Per Capita	CPI Index*	Conversion Factor	Operating Revenue in 2005 Dollars	Adjusted Revenue Per Capita
2005	\$755,000	\$539	195.3	1.00	\$755,000	\$539
2006	\$784,000	\$560	201.6	.969	\$759,696	\$543
2007	\$765,000	\$546	207.3	.973	\$744,345	\$531
2008	\$756,000	\$540	215.3	.963	\$728,028	\$520
2009	\$763,000	\$545	214.5	1.00	\$763,000	\$545

\*CPI Index is from U.S. Bureau of Labor Statistics; All Urban Consumers, all items.

**Interpretation:** In this example, total operating revenue increased modestly over the five-year period from \$755,000 to \$763,000, or 1.1%.

## A Suggestion about Using Population Numbers

Many of the factors call for population data as part of the formula. Because official population counts are only available for the U.S. Census Bureau every ten years, you may want to find alternative sources of population data for the later years in the decade to give you a more accurate picture of per capita comparisons. Intercensal population estimates may be available from regional or county planning agencies or from the Pennsylvania State Data Center at 717-948-6336 or [www.psdh.hbg.psu.edu](http://www.psdh.hbg.psu.edu).

## Compatibility with Other Local Government Assessment Tools

In 1989, the Southwestern Pennsylvania Commission (SPC) published Standards for Effective Local Government, a self-assessment workbook, which identifies minimum municipal service standards for local governments. A financial management component with standards for budgeting, capital improvements planning, revenue collection, accounting, cash management and investment processes was included as one of twelve service areas. A commentary outlining the rationale for each standard is also presented.

The principles and procedures which form the foundation for SPC's financial management standards essentially reinforce or reflect actions a community should take to achieve either stable or favorable trends for factors contained in the financial monitoring system. (See Appendix A for a listing of the minimum standards that support factors related to the financial monitoring system.)

For example: Standard No. 7 under Revenue Collection states: "Where fees and service charges have been established, they are adequate to recoup all direct and indirect costs of providing the service." This is consistent with the interpretation of a stable trend line for Factor 15 - User Charges/Fees where the quotient of total fees and user charge revenues when divided by the total cost of providing the service is 1 or 100%.

To further support local efforts to improve municipal operating procedures and practices, the SPC, in conjunction with the PA Department of Community and Economic Development, is publishing a series of resource manuals illustrating how local governments throughout Pennsylvania have achieved the minimum standards for the twelve service areas. One of the resource manuals addresses sound financial management practices. The materials in the manual can be utilized as models for change. For example, in response to negative trend for Factor 13 – Budget Overruns, a community working to avoid a year-end deficit may decide to implement a monthly financial report which compares actual expenditures to budgeted amounts as a way to identify expense-related problems. A format consistent with nationally recognized criteria for an interim financial report is part of the financial management resource manual.

Municipal officials may obtain copies of Standards for Effective Local Government workbook or the financial management resource manual, by contacting SPC at 412-391-5590.

## Summary

While a financial monitoring system is designed to provide basic and important information, it will be a useful tool only if action is taken to deal with problem areas. Some areas, of course, are not under the control of local officials. However, others can be controlled or at best influenced, and therefore, it is important that the community develop an action agenda which lists the unfavorable factors and assigns specific responsibility for addressing those factors to a group or individual. The main ingredient for effectiveness is a commitment within a municipality to keep track of its fiscal health.

Municipalities interested in learning more about financial condition assessment are encouraged to seek further assistance, publications and information from:

Government Finance Officers Association (GFOA)  
180 N. Michigan Avenue  
Chicago, IL 60601  
312-977-9700  
[www.gfoa.org](http://www.gfoa.org)

International City/County Management Association (ICMA)  
777 North Capitol Street, N.E., Suite 500  
Washington, DC 20002-4201  
202-289-4262  
[www.icma.org](http://www.icma.org)

Governor's Center for Local Government Services  
Commonwealth Keystone Building, 400 North Street, 4th Floor  
Harrisburg, PA 17120-0225  
888-223-6837  
[www.newPA.com](http://www.newPA.com)

## Computer Spreadsheet: A Tool for Financial Condition Assessment

In the 1984 financial monitoring system workbook for small communities, the instructions indicated that all you needed to calculate the factors was a pencil and calculator. Personal computers were not commonplace and spreadsheet programs, although available, were not particularly user-friendly. Today, wide spread access to personal computers with word processing, spreadsheet and graphing capabilities should act as an incentive to those who undertake financial condition assessment for the first time. The spreadsheet can be used to create a database for the factors, perform the calculations, convert data to permit constant dollar comparisons and create graphs and charts to analyze trends. Basically, once the data file for each factor and the factor formulas and conversion calculations have been established, only new data need be added to the spreadsheets each subsequent year to keep the financial monitoring system current. In addition, most word processing software has an import utility for spreadsheet files that can be used to prepare a report to summarize the results of the financial condition assessment.

The following section illustrates how a spreadsheet program is used to implement the financial monitoring system. Two factors, Revenue Per Capita and Expenditures Per Capita, are analyzed separately as well as together. Both have been adjusted for inflation. The spreadsheet and graphs for each factor are presented as exhibits.

### FACTOR 1: REVENUE PER CAPITA

**Step 1:** The following data should be placed in the spreadsheet's first three columns shown in Exhibit 1 for the years 1996 through 2009. (Note: For exhibits 1 and 3, data entry begins in row 6.)

- Column A - Year
- Column B - Total Operating Revenue
- Column C – Population

#### EXHIBIT 1

FACTOR 1 – REVENUE PER CAPITA							
Year A	Operating Revenue B	Population C	Revenue Per Capita D	CPI E	Conversion Factor F	Adjusted Revenue G	Adjusted Revenue Per Capita H
1996	\$2,694,799	9233	\$292	156.9	100.00%	\$2,694,799	\$292
1997	\$2,875,422	9233	\$311	160.5	97.76%	\$2,811,013	\$304
1998	\$2,981,411	9250	\$322	163.0	98.47%	\$2,935,795	\$317
1999	\$3,051,716	9250	\$330	166.6	97.84%	\$2,985,799	\$323
2000	\$5,795,187	9250	\$627	172.2	96.75%	\$5,606,843	\$606
2001	\$4,168,700	9250	\$451	177.1	97.23%	\$4,053,227	\$438
2002	\$4,604,262	9250	\$498	179.9	98.44%	\$4,532,436	\$490
2003	\$4,716,627	9096	\$519	184.0	97.77%	\$4,611,446	\$507
2004	\$4,854,352	9096	\$534	188.9	97.41%	\$4,728,624	\$520
2005	\$5,103,277	9096	\$561	195.3	96.72%	\$4,935,890	\$543
2006	\$5,223,000	9096	\$574	201.6	96.88%	\$5,060,042	\$556
2007	\$5,175,000	9096	\$569	207.3	97.25%	\$5,032,688	\$553
2008	\$5,137,000	9096	\$565	215.3	96.28%	\$4,945,904	\$544
2009	\$5,266,000	9096	\$579	214.5	100.0%	\$5,266,000	\$579
2010*	\$5,110,000	9096	\$562	217.5	98.44%	\$5,030,284	\$553

\*CPI - January - June 2010

## Formulas

- Revenue Per Capita:  $=B6/C6$
- Conversion Factor (Base Year 1983 divided by Year to be adjusted):  $=99.6/E6$
- Adjusted Revenue:  $=B6*F6$
- Adjusted Revenue Per Capita:  $=G6/C6$

**Step 2:** The formula to calculate Revenue Per Capita is:

$$\frac{\text{Total Operating Revenue}}{\text{Population}}$$

This formula is shown on Exhibit 1 as  $=B6/C6$  and would be placed in cell **D6**. It refers to Operating Revenue, \$2,694,799, for 1996 located in cell **B6** and the 1996 Population, 9233, in cell **C6**. As a result, \$292 appears in cell **D6**, Revenue Per Capita. The formula may be copied from cell **D6** into the rest of the cells in column D for the years 1997 through 2010 to calculate the respective factors.

**Step 3:** The fifth column contains the CPI for the years 1996 through 2010. To create the conversion factor for each year, the following formula should be used:

$$\frac{\text{Base Year}}{\text{Year to be Adjusted}}$$

The formula is shown on Exhibit 1 as  $=156.9/E6$  for 1996 and would be placed in cell **F6**. For 1996, the base year is 156.9 (cell **E6**) and, in this step is divided by itself to create the conversion factor in cell F6. The conversion factor then is 100.0%. For 1997 and subsequent years, the formula should be copied for the rest of the cells in column F.

**Step 4:** The sixth column, G, is Adjusted Revenue for each year. To calculate Adjusted Revenue, multiply Total Operating Revenue (Column B) by the Conversion Factor in Column F. The formula  $=B6*F6$  is placed in cell **G6** to obtain this result. Again, this formula should be copied into the rest of the cells in column G for the years 1996 through 2010.

**Step 5:** The last calculation is Adjusted Revenue Per Capita. Again, the formula in step 2 is utilized;  $=G6/C6$  is placed in cell **H6** to produce \$292 as the result. The formula is then copied from cell **H6** for the rest of the cells in column H for 1997 through 2010.

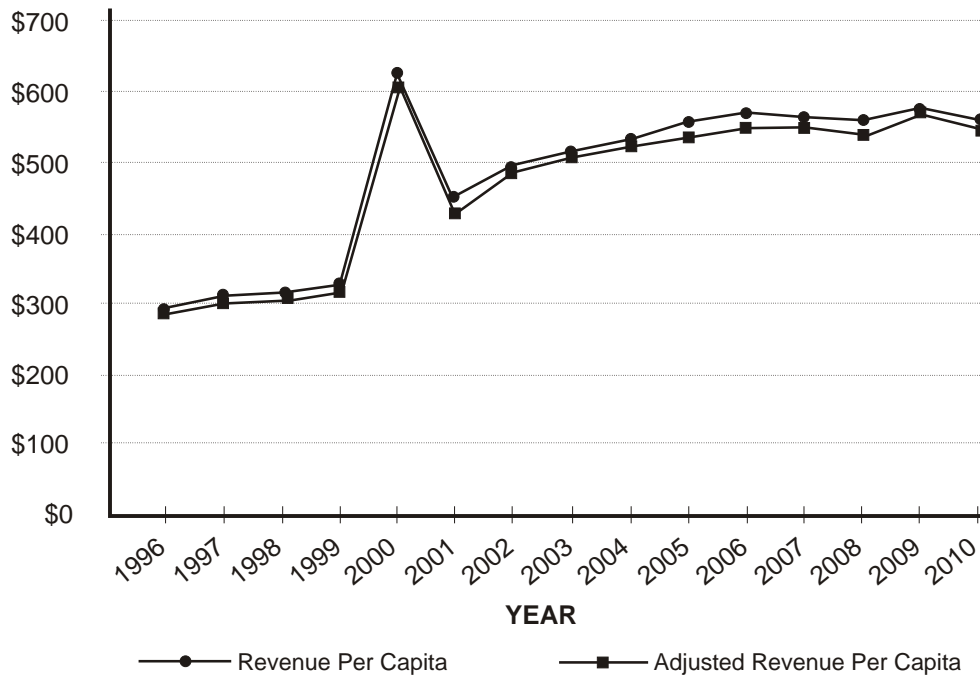
**Step 6:** The spreadsheet's graph function uses the data from columns A, D and H to create the graph in Exhibit 2. Please refer to your spreadsheet user manual for specific instructions about graphing options.

**Interpretation of Factor.** The trend for Revenue Per Capita, as graphed in Exhibit 2, appears to be favorable for years 1996 – 2010, if 2000 is excluded, but begins to show a decline beginning in 2007 for three of four years. This factor ranges from \$292 in 1996 to \$562 in 2010 in unadjusted dollars. The significant increase in 2000 was a result of a tax rate increases for real estate, earned income and deed transfer taxes. In addition, a \$2 million capital improvements bond issue was also issued in 2000, inflating total revenues.

When the effects of inflation are taken into consideration, the increases in Revenue Per Capita appear negligible. The values for this factor range from \$292 in 1996 to \$579 in 2009. The Adjusted Revenue Per Capita slightly increases for the years 1996 – 1999, increases more so in 2000, declines in 2001, increases in 2002 – 2006, is relatively stable for 2007 – 2008, and then increases again in 2009.

## EXHIBIT 2

### Revenue Per Capita versus Adjusted Revenue Per Capita 1996-2010



#### FACTOR 4: EXPENDITURES PER CAPITA

Refer to Exhibit 3 - Expenditures Per Capita to review steps 1 through 5.

**Step 1:** The following data should be placed in the spreadsheet's first three columns for the years 1996 through 2010:

- Column A - Year
- Column B - Total Operating Expenditures
- Column C - Population

**Step 2:** The formula for Expenditures Per Capita is:

$$\frac{\text{Total Operating Expenditures}}{\text{Population}}$$

This formula is shown on Exhibit 3 as =B6/C6 and would be placed in cell D6. This formula refers to Operating Expenditures, \$2,768,141, for 1992 which resides in cell B6 and the 1992 Population, 9233, in cell C6. The result, \$300, appears in cell D6, Expenditures Per Capita. The formula may be copied from D6 into column D cells for the years 1997 through 2010 to calculate the factor.

**EXHIBIT 3**

<b>FACTOR 4 – EXPENDITURES PER CAPITA</b>							
<b>Year A</b>	<b>Operating Expenditures B</b>	<b>Population C</b>	<b>Expenditures Per Capita D</b>	<b>CPI E</b>	<b>Conversion Factor F</b>	<b>Adjusted Expenditures G</b>	<b>Adjusted Expenditures Per Capita H</b>
1996	\$2,768,141	9233	\$300	156.9	100.00%	\$2,768,141	\$300
1997	\$3,086,867	9233	\$334	160.5	97.76%	\$3,017,721	\$327
1998	\$3,464,113	9250	\$374	163.0	98.47%	\$3,411,112	\$369
1999	\$3,288,996	9250	\$356	166.6	97.84%	\$3,217,954	\$348
2000	\$3,739,538	9250	\$404	172.2	96.75%	\$3,618,003	\$391
2001	\$4,876,662	9250	\$527	177.1	97.23%	\$4,741,578	\$513
2002	\$4,522,514	9250	\$489	179.9	98.44%	\$4,451,963	\$481
2003	\$4,679,982	9096	\$515	184.0	97.76%	\$4,575,618	\$503
2004	\$4,937,706	9096	\$543	188.9	97.41%	\$4,809,819	\$529
2005	\$4,506,328	9096	\$495	195.3	96.72%	\$4,358,520	\$479
2006	\$6,229,487	9096	\$685	201.6	96.88%	\$6,035,127	\$663
2007	\$5,421,836	9096	\$596	207.3	97.25%	\$5,272,736	\$580
2008	\$6,514,023	9096	\$716	215.3	96.28%	\$6,271,701	\$690
2009	\$5,451,570	9096	\$599	214.5	100.00%	\$5,451,570	\$599
2010*	\$5,885,422	9096	\$647	217.9	98.44%	\$5,793,609	\$637

**Formulas**

- Expenditures Per Capita: =B6/C6
- Conversion Factor (Base Year 1996 divided by Year to be adjusted): =156.9/E6
- Adjusted Expenditures: =B6\*F6
- Adjusted Expenditures Per Capita: =G6/C6

**Step 3:** The fifth column contains the CPI for the years 1996 through 2010. To create the conversion factor for each year, the following formula should be used:

$$\frac{\text{Base Year}}{\text{Year to be Adjusted}}$$

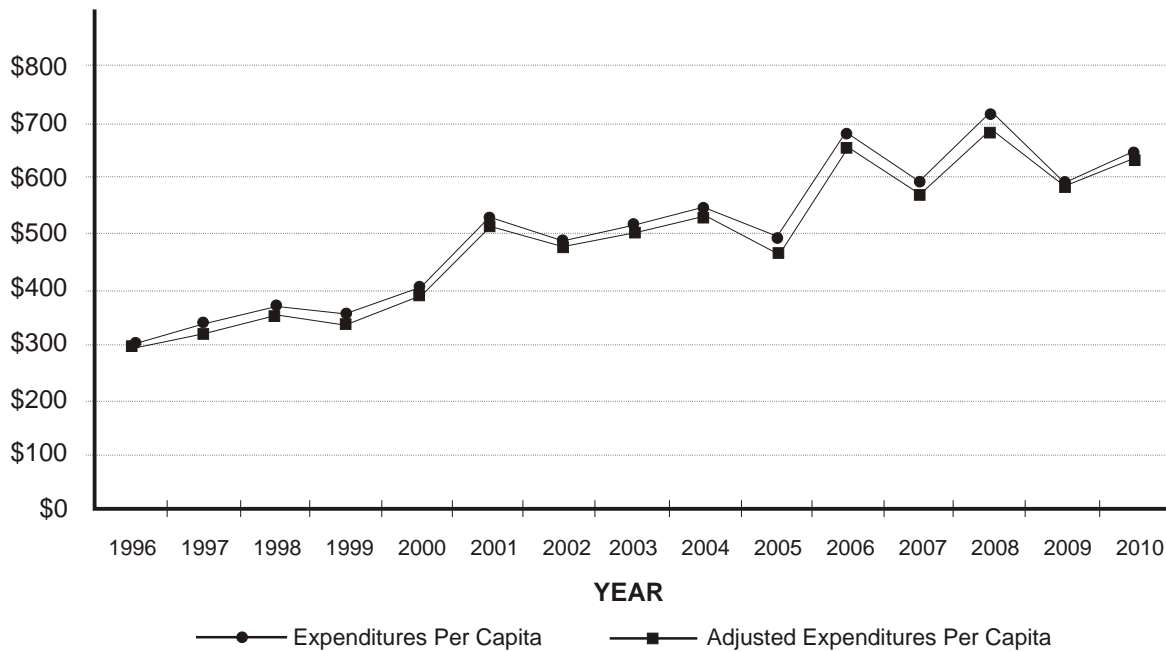
The formula is shown on Exhibit 3 as =156.9/E6 for 1996 and would be placed in cell F6. For 1996, the base year is 156.9 (cell E6) and in this case is divided by itself to create the conversion factor in cell F6. The conversion factor then is 100.0%. For 1997 and subsequent years, the formula should be copied for the rest of the cells in column F.

**Step 4:** The sixth column, G, is Adjusted Expenditures for each year. To calculate the Adjusted Expenditures requires that the Total Operating Expenditures (Column B) be multiplied by the Conversion Factor (Column F). The formula =B6\*F6 is placed in cell G6 to obtain this result. Again, this formula should be copied for the rest of the cells in column G for the years 1997 through 2010.

- Step 5:** The last calculation is Adjusted Expenditures Per Capita. Again, the formula in step 2 is utilized; =G6/C6 is placed in cell H6 to produce \$300 as the result. The formula would then be copied from cell H6 for the rest of the cells in column H for 1997 through 2010.
- Step 6:** The spreadsheet's graph function using the data from columns A, D and H is used to create the graph in Exhibit 4. Please refer to your spreadsheet user manual for specific instructions about graphing options.

**EXHIBIT 4**

**Expenditures Per Capita versus Adjusted Expenditures Per Capita 1996-2010**



**Interpretation of Factor.** The trend lines for Expenditures Per Capita and Adjusted Expenditures Per Capita, Exhibit 4, show parallel signs of stability, growth and decline. The value of the factor ranges from \$300 in 1996 to \$647 in 2010 without adjustment for inflation and from \$300 to \$637 over the same period when the factor is adjusted for inflation. There appears to be an inconsistency in decision-making from year to year, especially from 2005 to 2010. The significant expenditure increase in 2001 was a result of a major capital improvements program that was funded by a bond issue. The key is to compare the Expenditures Per Capita with the Revenues Per Capita shown in the next step.

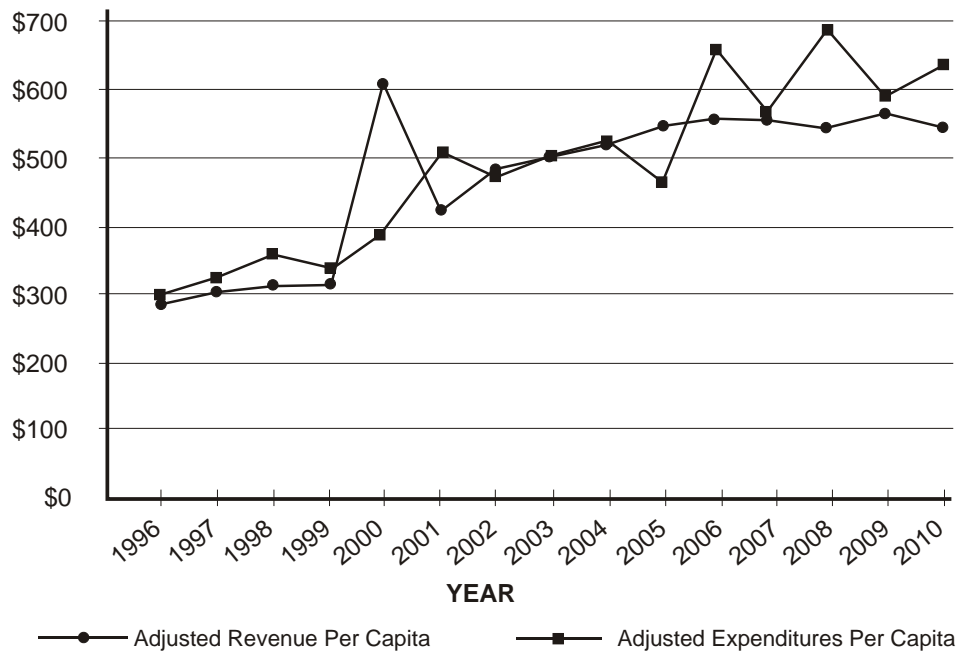
**Combined Factors: Revenue versus Expenditures**

A graphic comparison of revenue and expenditures on a per capita basis with the values adjusted for inflation is presented in Exhibit 5. The trend lines show that revenue and expenditures per capita were essentially the same in only three years, 2002 –2004, revenue exceeded expenditures in two years, 2000 and 2005, and expenditures were in excess of revenue per capita during the remaining years except 2001. While both revenue and expenditures essentially increased over the fifteen-year period, the expenditures per capita increased at a greater rate than revenues per capita in six out of the eleven years. In those six years, the budget was balanced by using prior years' surpluses—an action that is unfavorable. The budget was technically balanced from 2002-2004, the only three years when current revenues pretty much equaled current expenses. In 2005, revenues outdistanced expenditures due to policy changes made by the legislative body. In 2006 and 2008, the difference between revenue and expenditures per capita was the greatest. This difference in revenue in resulted from real estate and earned income tax rate cuts and a significant use of prior year's fund balances.



**EXHIBIT 5**

**Revenue versus Expenditures Per Capita (Adjusted for Inflation)**



**Action Items:**

The municipal legislative body should consider the following prior to the next budget year.

1. The municipality should carefully examine past patterns of funding current expenses with prior year fund balances. At some point, the fund balances will be exhausted and either services will have to be cut back or eliminated or a significant tax increase will be necessary to maintain the existing array of services. The municipality does not meet the budgetary solvency criteria, and, at some point, may not be able to maintain service level solvency.
2. Determine the reason for increased costs. Distinguish between greater expenses for existing services and increases associated with enhanced or additional services. Examining the major expenditure areas on a per capita or per household basis may help identify the changes and indicate whether they are fixed or discretionary in nature.

## Factor Summary Sheet

No.	Factor	Year	Year	Year	Year	Year	Year	Year	Year	Year	Year
		_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
1	Revenue Per Capita										
2	Intergovernmental Revenue										
3	Property Tax Resources										
4	Expenditures Per Capita										
5A	Employee Benefits: Total Cost										
5B	Employee Benefits: Per Hour Worked										
6	Cash Position										
7	Debt Service										
8	Long-Term Debt										
9	Debt Per Capita										
10	Operating Position										
11	Unfunded Pensions										
12	Revenue Shortfalls										
13	Budget Overruns										
14	Uncollected Property Tax										

## Factor Summary Sheet

No.	Factor	Year	Year	Year	Year	Year	Year	Year	Year	Year	Year
		_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
15	User Charges/Fees										
16	Employees Per Capita										
17	Property Value										
18	Fiscal Capacity										
19	Employment Base										
20	Community Jobs										
21	Construction Activity										
22	Municipal Demographics Population										
23	Municipal Demographics Personal Income										
24	Municipal Demographics Pop > 65										
25	Capital Outlay										
26	Fund Balance										

Factor Number	Factor and Trend	Action Agenda	Assigned Person

Factor Number	Factor and Trend	Action Agenda	Assigned Person

Factor Number	Factor and Trend	Action Agenda	Assigned Person

Factor Number	Factor and Trend	Action Agenda	Assigned Person

## II. Financial Monitoring System Factors

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### Factor 1: Revenue Per Capita

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#### DESCRIPTION

This factor relates municipal revenues to changes in population. It suggests two questions. If revenue per capita is increasing, is it due to growth of the tax base or an increase in tax and fee rates and/or a shift to other revenue resources? If revenue per capita is decreasing, has the population increased without corresponding growth in the tax base, or has the tax base stabilized or decreased? If the trend for this factor is negative (slopes downward) and revenue per capita is decreasing, the municipality will find it increasingly difficult to maintain service levels unless new sources of revenue are found.

In municipalities where the population is constant or decreasing, the total number of households may be stable or increasing because household size is decreasing. Consequently, it may be useful to substitute the number of households for the population value in this calculation. Revenue per capita should also be compared to changes in expenditures per capita.

#### Formula:

$$\frac{\text{Total Operating Revenue}}{\text{Population}}$$

or

$$\frac{\text{Total Operating Revenue}}{\text{Households}}$$

#### Data Sources:

- **Total Operating Revenue:** Annual Audit and Financial Report including revenues of the General Fund, State Liquid Fuels Fund plus all other funds with operating revenues such as special revenue or enterprise funds.
- **Population:** Most recently available population estimate. Use same source for each year.
- **Households:** Most recently available data per utility and solid waste collection billing records.

**Warning Signal:** Decreasing Operating Revenue Per Capita

#### FACTOR 1 - REVENUE PER CAPITA CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Revenue					
2. Current Population					
3. Revenue Per Capita (Line 1 divided by Line 2)					




ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Revenue					
2. Current Population					
3. Revenue Per Capita <i>(Line 1 divided by Line 2)</i>					


**FACTOR 1 - REVENUE PER CAPITA TRENDS AND ANALYSIS**

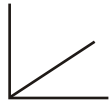
**Instructions:** List the years to be examined across the bottom of the graph. Plot the revenue per capita against the vertical axis.

**Dollars**


<- Years ->

**Unfavorable Trend** (*Color Code = Red*)  

 If the trend line resembles the one on the left, it may be difficult to maintain services unless new revenues are found or unless expenditures per capita are declining.

**Stable Trend** (*Color Code = Yellow*)  

 No immediate problem unless the expenditures per capita trend is climbing.

**Favorable Trend** (*Color Code = Green*)  

 If the trend line resembles the one to the left, no problem is apparent unless the expenditure trend is rising faster.

## FACTOR 1 - REVENUE PER CAPITA ACTION ITEMS

If your revenue per capita (or per household) is *decreasing*, you may want to consider the following:

- Attempt to determine why the decrease has occurred. An evaluation of the major sources of revenue may be helpful. Which particular revenue items are decreasing relative to the population or number of households? Can the change be linked to a specific short-term circumstance or has the local economy undergone a fundamental adjustment? Has a component of the revenue base changed? Has an unusual portion of the high-wage earning population recently left the labor force? Evaluating each of the municipality's principal revenue sources may indicate where the changes are occurring.
- A decrease in the revenue per capita may also result from reaching the legal maximum millage rate. The municipal codes authorize a range of special purpose millages in addition to the general purpose rate. Action by the county to undertake a countywide reassessment or change the existing predetermined assessment ratio will result in each mill being worth substantially more in revenues.
- Take action to maximize currently available local revenues by undertaking programs such as the following:
  1. Aggressively pursue collection of delinquent taxes and fees.
  2. Accelerate the due dates for property tax collections by issuing the duplicate to the tax collector earlier in the year.
  3. Cooperate with neighboring units to form a multi-jurisdictional tax collection system to minimize the cost and maximize effectiveness of earned income tax collection.
  4. Examine the current service fee structures to ensure existing user charges are supporting the entire cost of providing the service.
  5. Develop and implement a cash management and investment plan to earn maximum interest on the municipality's fund balances.
  6. Sell surplus property and equipment.
  7. Set fines and penalties at the maximum permissible rate.
  8. Review tax-exempt parcels to ensure they continue to qualify for exemption.

If your revenue per capita or per household is *increasing*, you may want to consider the following:

- Given your knowledge of the community, will increases in revenue levels continue to be available to support future services? Again, an examination of each of the primary sources of local revenue may be instructive. For instance, if the increase is related to new development or redevelopment, is there continued growth potential, or will the municipality soon become fully developed and its growth effectively stopped? If the increase in revenues will stop at some point, how will the community pay for increased costs in the future?
- An increase in revenue per capita might indicate a decrease in population without a corresponding decrease in households. If so, future difficulties could arise where services are paid for on a per household basis.
- Is the increase in revenues per capita associated with increases in tax and fee rates? In effect, has the local tax burden (proportion of personal income paid in taxes and fees) created higher revenue per capita? Has an increase in revenue per capita caused a competitive disadvantage for the community that could result in its becoming a less attractive or affordable place to live or do business?

Regardless of the direction of change, inflation can alter the interpretation of this factor. If a decrease or increase occurs, you may want to recalculate the factor using constant dollars, with figures adjusted for inflation.

For future consideration, the governing body, after reviewing this factor, may want to establish a policy to annually consider the composition of the community's revenue structure and its continuing capacity to support local services with the long-term objective of creating a diverse and consistent revenue base.

## Factor 2: Intergovernmental Revenue

### DESCRIPTION

This factor reveals whether a municipality is becoming or has become heavily dependent on revenue from other levels of government. Over-dependence can be dangerous since outside funding sources may withdraw their funding or reduce their level of support.

The effect on the community's ability to maintain basic services when general operating grants are cut can be serious. In the mid-1980's when the federal government eliminated General Revenue Sharing some small communities ultimately had to reduce or eliminate paid police and fire services.

Intergovernmental revenues received by most Pennsylvania local governments include liquid fuels/highway aid, general municipal pension state aid and public utility tax rebates. All are subject to changes on an annual basis due to the activity upon which they are based: gasoline tax collections, premiums paid to non-Pennsylvania based fire and casualty insurance companies, and the value of tax exempt public utility property. Consequently, the changing role of these funds over time should be considered versus the community's commitments to maintain roads, support volunteer fire companies and fund municipal pension obligations. For instance, deregulation of electric generating utilities has reduced the available funds for PURTA allocation.

The reliance of a community on outside assistance to create or maintain the local infrastructure is also a key consideration. Grants are often sought to address emergency recovery or expensive capital infrastructure projects. Is the community considering its own capacity to fund such expenditures in the event intergovernmental grants are not forthcoming? With cutbacks in federal domestic spending and the generally static nature of state intergovernmental funding, building and maintaining basic infrastructure systems, such as sewer, water and roads, has become an essentially local responsibility.

The factor compares the percentage of intergovernmental operating revenue to total operating revenues.

### Formula:

$$\frac{\text{Intergovernmental Operating Revenue}}{\text{Total Operating Revenue}}$$

### Data Source:

- **Intergovernmental Revenue:** Accounts 351-359 from the Annual Audit and Financial Report.
- **Total Operating Revenue:** See Factor 1.

**Warning Signal:** Intergovernmental Operating Revenue Increasing as a Percentage of Total Operating Revenue

### FACTOR 2 - INTERGOVERNMENTAL REVENUE CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Intergovernmental Operating Revenue					
2. Total Operating Revenue					
3. Intergovernmental Revenue as Percent of Total Revenue (Line 1 divided by Line 2)					



## **FACTOR 2 - INTERGOVERNMENTAL REVENUE ACTION ITEMS**

If you are experiencing an *increasing* dependence on intergovernmental operating revenue, then consider the following:

- Make sure the governing body is aware of the source and nature of these funds when adopting the annual budget, particularly if the funds are subject to annual appropriations by a higher level of government.
- Make sure the use of intergovernmental revenues is consistent with their purpose. Attempt to allocate one-time revenue to capital programs rather than for general operating purposes. Only seek grant assistance for major projects that are reflected in the municipality's capital improvements plan.
- If grant funds underwrite the development of a new program, make sure that the governing body considers the community's capacity to allocate local funds to continue the program in the future as well as the difficulty and impact of terminating the program when the grant runs out. Undertake grant-funded capital projects only if the general operating budget can adequately support and maintain the asset over the long term.
- Maintain close contact with funding agencies in your area (county and state) to determine whether you are aware and have taken advantage of all available grant programs. When preparing grant applications, include all eligible direct and indirect costs in the estimate of project costs.

Be certain to generate estimates of ongoing annual operational costs associated with grant-funded additions to the municipality's infrastructure. When such projects are approved, to avoid later funding difficulties, the legislative body also ought to commit future local resources to the ongoing operating and maintenance costs.

## Factor 3: Property Tax Resources

### DESCRIPTION

This factor shows how much additional revenue is potentially available from the property tax. The ability to raise additional property tax revenue is an important part of fiscal health for all local governments. This factor must be examined with consideration for current real estate tax rate limits set by municipal codes and charters and the potential for changes in the assessed valuation of local real estate.

**Formula:** (Maximum General Purpose Property Tax Millage Rate) *minus* (Current General Purpose Property Tax Millage Rate) *times* (Net Value of One Mill Of Property Tax)

### Data Sources:

- **Maximum General Purpose Property Tax Millage Rate:** See municipal code or charter.
- **Current General Purpose Property Tax Millage Rate:** Current budget.
- **Net Value of One Mill:** Divide total property tax revenue for last year by the number of mills levied for general purposes.

**Warning Signal:** Decreasing Amount of Property Tax Resources

### FACTOR 3 - PROPERTY TAX RESOURCES CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Maximum Property Tax Limit					
2. Current Millage Rate					
3. Mills Available (Subtract Line 2 from Line 1)					
4. Value of One Mill					
Property Tax Resources Available (Multiply Line 3 by Line 4)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Maximum Property Tax Limit					
2. Current Millage Rate					
3. Mills Available (Subtract Line 2 from Line 1)					
4. Value of One Mill					
Property Tax Resources Available (Multiply Line 3 by Line 4)					

### FACTOR 3 - PROPERTY TAX RESOURCES TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom of the graph. Plot the value of available property tax resources along the side axis

**Dollars**


**0**

**Years ->**



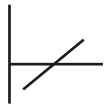
**Unfavorable Trend** (*Color Code = Red*)

The municipality's remaining property tax resources are decreasing. Unless you have the ability to raise other local revenues, this is a serious warning signal and should receive high priority for an action agenda.



**Stable Trend** (*Color Code = Yellow*)

While stability is good in many factors, a stable property tax resource should be viewed with caution since it indicates little growth in property values.



**Favorable Trend** (*Color Code = Green*)

This shows an increase in the amount of money that legally can be obtained from the property tax and is a healthy sign.

### **FACTOR 3 - PROPERTY TAX RESOURCES ACTION ITEMS**

If an *unfavorable or stable* trend is experienced in this area, you may want to consider the following:

- Have assessments kept up with general changes in real estate market values? Are all newly constructed buildings and additions or improvements to existing buildings added to the assessment rolls on a timely basis? Has your community suffered a decline in residential, commercial and/or commercial property values due to adverse economic conditions? To answer this second question, look at the proportion of the assessed value each type of real estate represents. Are the changes related to a segment of the real estate base? Why have the changes occurred?
- Has there been an increase in tax-exempt properties within your community? If the local government has become the owner of tax delinquent properties, should a program to place the properties back on the tax rolls be initiated?
- Are your municipal zoning and land development ordinances up to date and conducive to current development options?
- Is there a need to cooperate with regional public and nonprofit economic or community development agencies to rebuild the tax base by encouraging business activity and housing rehabilitation.
- Is there a need to advocate change in the county's assessment ratio? Should this option be explored in conjunction with neighboring local governments or through your county-level municipal association?
- If property tax resources are exhausted or severely limited, an analysis of alternative revenue sources should be undertaken to provide additional revenues. The study would include consideration of special purpose real estate millages, unused tax sources available under the Local Tax Enabling Act and the imposition of user fees and charges for services.

If the trend is *favorable*, attempt to determine the basis for it. Has the existing real estate base increased in value due to positive market conditions and aggressive action by the county to keep the assessed values consistent with increasing market values? Has residential and/or commercial development boosted the municipality's added new properties to the assessment rolls? Or, is the increase attributable to both?



## Factor 4: Expenditures Per Capita

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### DESCRIPTION

This factor displays the cost of operating the municipal government on a per person basis and reveals the effect of adding or deleting services or changing service levels.

Increases in expenditures per capita are particularly troublesome if revenue per capita is stable. Also, if expenditures per capita are increasing and no services have been added, then inflation or decreasing productivity may be a problem. If the trend for this factor is unfavorable, an examination of each major expenditure area—personnel services, contractual services, debt service, and materials and supplies—should be made to determine the reason for the increase. Alternatively, specific services and programs should be examined to determine where significant expenditure increases have occurred.

Substituting number of households for the population in this calculation may be useful in communities where the total population is constant or decreasing. Under such circumstances, the total number of households may remain stable or even increase, because the household size is decreasing,

### Formula:

$$\frac{\text{Total Operating Expenditures}}{\text{Population}}$$

*or*

$$\frac{\text{Total Operating Expenditures}}{\text{Households}}$$

### Data Sources:

- **Total Operating Expenditures:** Annual Audit and Financial Report including the General Fund plus all other funds with operating expenditures such as the State Liquid Fuels Fund, special revenue and enterprise funds.
- **Population:** Most recently available population estimate. Use same source for each year.
- **Households:** Most recently available data per utility or solid waste collection billing records.

**Warning Signal:** Increasing Operating Expenditures Per Capita

### FACTOR 4 - EXPENDITURES PER CAPITA CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Expenditures					
2. Population					
3. Expenditures Per Capita (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Expenditures					
2. Population					
3. Expenditures Per Capita <i>(Line 1 divided by Line 2)</i>					

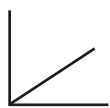
**FACTOR 4 - EXPENDITURES PER CAPITA TRENDS AND ANALYSIS**

**Instructions:** List the years to be examined across the bottom of the graph. Plot the expenditures per capita against the vertical axis.

**Dollars**

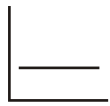

0

Years ->



**Unfavorable Trend** *(Color Code = Red)*

Most municipalities should see an upward trend due to inflation. Once that has been taken into consideration, examine the Revenue Per Capita (Factor 1) and consider options to reduce overall expenditures.



**Stable Trend** *(Color Code = Yellow)*

This trend indicates minor changes and that no immediate problem is apparent. It is most likely to appear after expenditure figures are adjusted for inflation.



**Favorable Trend** *(Color Code = Green)*

Check your numbers and calculations! Once you verify the accuracy of this trend, it would appear you are holding down costs. Check this factor against Revenue Per Capita to make sure revenues are not decreasing at a faster rate.

## **FACTOR 4 - EXPENDITURES PER CAPITA ACTION ITEMS**

If your expenditures per capita or per household are increasing, you may want to consider the following:

- Find out where the increased costs are—new services, wage increases, employee benefits, debt or contractual services, materials and supplies. You may want to examine each of the major program areas of expense on a per capita or household basis. Depending on the reasons for the increase and whether the costs are fixed or discretionary, changes in service levels or the array of services offered or the manner in which they are provided may be considerations, if expenditures must be reduced.
- Compare the expenditure trend to the revenue per capita or per household results. If revenues and expenditures are experiencing the same rate of increase, there may not be a problem.
- If revenues per capita or per household are stable, increasing at a slower rate than expenditures or even decreasing, then the municipality may need to explore alternative ways of providing basic services through cooperative or shared services arrangements or by contracting with the private sector to provide the services.
- Regardless of the type of change, inflation can alter the interpretation of this factor. If a decrease or increase occurs, you may want to recalculate the factor using constant dollars, dollars adjusted for inflation, to more fully understand any change and to facilitate comparing revenues and expenditures on a per capita or per household basis.
- When the ability to meet expenditure obligations on an annual basis becomes a critical concern for the municipality, more careful management is necessary. Reports comparing actual to budgeted amounts for both revenues and expenditures must be prepared and reviewed on a monthly basis. From an operational perspective, it may be beneficial to incorporate performance measures into the budget to establish a link between the cost of providing services and the quality and quantity of service being rendered.

## Factor 5a: Employee Benefits Total Cost

### DESCRIPTION

This factor demonstrates the impact that employee benefit costs have on a municipality's finances. At one time, fringe benefits were considered a low-cost item and given freely in contract negotiations. Employer costs for existing pension, health care, social security, vacation, holiday and other benefits have risen steadily over the past decade, becoming one of the fastest growing cost centers for municipal governments.

Often government officials and employees fail to take into account the real cost and budgetary impact of employee benefits. Twenty-five to 30 years ago, employee benefits were equivalent to about 10% - 15% of the total wage and salary cost. Today, it is not unusual for such benefits to represent 30% or more of the total cost of wages and salaries.

### Formula:

$$\frac{\text{Total Budgeted Employee Benefits Cost}}{\text{Total Salary and Wage Costs}}$$

### Data Sources:

- **Employee Benefit Costs:** Annual Operating Budget
- **Salary and Wage Costs:** Annual Operating Budget

**Warning Signal:** Increases in Employee Fringe Benefit Costs Are Proportionately Higher When Compared to Increases in Total Salary and Wage Costs.

### FACTOR 5A - EMPLOYEE BENEFITS TOTAL COST CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Total Fringe Benefit Costs					
2. Total Salaries and Wages					
3. Fringe Benefits as % of Salaries and Wages (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Total Fringe Benefit Costs					
2. Total Salaries and Wages					
3. Fringe Benefits as % of Salaries and Wages (Line 1 divided by Line 2)					



## **FACTOR 5A- EMPLOYEE BENEFITS TOTAL COST ACTION ITEMS**

If you are experiencing an increase in the ratio of employee benefit costs to total wage and salary costs, you may want to consider the following:

- Have employee benefit costs increased due to the addition of new benefits, increases in the cost of existing benefits, or enhancements to existing benefit? If increases are related to new benefits or enhancements to existing benefits, was the total budgetary impact of the increases known before they were granted? Were benefit changes made instead of, rather than in addition to, wage or salary increases during contract negotiations? If not, the municipality should consider basing future negotiating strategies on the total cost of employee compensation including wages/salaries and the employer's share of employee benefits costs. Proposing benefit cutbacks in negotiations can offset employee demands for wage increases.
- Have all employee benefit programs been evaluated to determine whether the municipality is getting the best value for the dollars spent? If you do not have a practice of routinely evaluating the costs of insurance benefits, then the use of a consultant to review this expense area may be worthwhile, especially if the municipality has flexibility to independently select the provider for the benefit.

Is the municipality, on an annual basis, keeping track of *all* employee benefits costs—including accrued vacation and sick time and any unfunded pension liabilities? As an employer, do you annually disclose each individual employee's total compensation and benefit cost to them? By doing so, you will be able to more effectively demonstrate to employees the total cost of their compensation.

## Factor 5b: Employee Benefits Cost Per Hour Worked

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### DESCRIPTION

Another method of analyzing the cost of employee benefits is to relate them to actual number of hours worked by an employee. This factor becomes an extension of Factor 5 - Employee Benefits. Three steps are involved in the process. For each job/position analyzed, specific payroll data must be collected. To start, using a few typical positions such as road worker or police officer may simplify your efforts.

### Formula:

$$\frac{\text{Total Benefit Cost}}{\text{Number of Hours Actually Worked}}$$

### Data Sources:

- **Total Fringe Benefit Cost:** Annual Budget
- **Number of Hours Actually Worked:** Payroll Records

**Warning Signal:** Increase in Total Benefit Cost Exceeds Increase in Wages/Salaries

### FACTOR 5B - EMPLOYEE BENEFITS COST PER HOUR WORKED CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Employer's Share: - Health Insurance - Social Security / Medicare - Pension - Workers Compensation - Unemployment Compensation - Uniform, Tuition, Other -					
2. 2080* Hours - Hours Paid but not Worked					
3. Fringe Benefits Cost per Hour Worked (Line 1 divided by Line 2)					

\*52 weeks X 40 hours per week = 2080 Hours

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Employer's Share: - Health Insurance - Social Security / Medicare - Pension - Workers Compensation - Unemployment Compensation - Uniform, Tuition, Other -					
2. 2080* Hours - Hours Paid but not Worked					
3. Fringe Benefits Cost per Hour Worked (Line 1 divided by Line 2)					

\*52 weeks X 40 hours per week = 2080 Hours

### FACTOR 5B - EMPLOYEE BENEFITS COST PER HOUR WORKED TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom. Plot the dollar cost per hour worked above the years indicated.

Dollars


0

Years ->



**Unfavorable Trend** (Color Code = Red)

A trend like this indicates an increase in the annual cost of employee benefits relative to the total hours worked on an annual basis.





**Stable Trend** (*Color Code = Yellow*)

This type of trend indicates that cost of employee benefits is changing proportionately to the number of hours actually worked.



**Favorable Trend** (*Color Code = Green*)

This trend indicates that employee benefit costs are decreasing relative to the total hours worked on an annual basis.

**FACTOR 5B - EMPLOYEE BENEFITS: COST PER HOUR WORKED ACTION ITEMS**

If employee benefit costs are significantly increasing relative to the number of hours worked on an annual basis, you may want to consider the following:

- How do your costs compare to other local governments in the area? Are they comparable, greater, less? Has the municipality been overly generous with the award of benefits in the areas of vacation, personal leave and sick time?
- Could costs be reduced if the municipality had discretion in selecting insurance benefit providers? Are the providers of employee insurance benefits stipulated in employee contracts? If so, obtaining greater flexibility in terms of selecting providers may be an item for future labor negotiations.

## Factor 6: Cash Position

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### DESCRIPTION

Any business operation must have sufficient cash on hand to pay bills due in the immediate future. Often municipalities accounting for their funds on a cash basis will show a misleading cash surplus without recognizing expenditures obligated, but not yet been billed and/or paid.

The cash position factor is designed to give municipal officials an idea of exactly how they stand at a given point in time by comparing available cash (bank accounts and short-term investments) with current liabilities. This factor becomes a healthy sign of the ability of the community to meet its current obligations.

### Formula:

$$\frac{\text{Cash and Short-Term Investments}}{\text{Current Liabilities}}$$

### Data Sources:

This information can be taken from the Annual Audit and Financial Report, if December 31 is the point in time being examined and compared. Current liabilities may not be completely listed and this information may have to be gathered from municipal accounting records.

**Warning Signal:** Decreasing Cash and Short-Term Investments as a Percentage of Current Liabilities

### FACTOR 6 - CASH POSITION CALCULATION

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Cash and Short-Term Investments					
2. Current Liabilities					
3. Ratio of Cash to Current Liabilities <i>(Line 1 divided by Line 2)</i>					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Cash and Short-Term Investments					
2. Current Liabilities					
3. Ratio of Cash to Current Liabilities <i>(Line 1 divided by Line 2)</i>					

## FACTOR 6 - CASH POSITION TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom. Plot the ratio determined from the calculation on the side. *The highlighted line indicates, 1.0, a perfect match between cash and short-term liabilities.*

2.0


0

Years ->



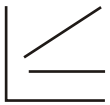
**Unfavorable Trend** (*Color Code = Red*)

A trend like the one on the left indicates that the municipality's current liabilities are increasing relative to available cash. When all cash resources are being expended, a trend like this represents a clear potential for a deficit.



**Stable Trend** (*Color Code = Yellow*)

This trend indicates that your cash remains about even with current liabilities over time. Stability in this factor is good but a sudden decrease in collections or an unexpected increase in bills might present problems.



**Favorable Trend** (*Color Code = Green*)

This trend indicates a good relationship between cash and current liabilities. It reflects a growing cushion of available cash over current liabilities for the time period being calculated.

## **FACTOR 6 - CASH POSITION ACTION ITEMS**

If you are seeing your cash position diminish over a period of time, you might want to consider the following:

- Are your revenue collection systems efficient and effective? Do you have an aggressive delinquent revenue collection system? Are you collecting and recording all revenues received during the budget year for which they were anticipated? Are all revenues deposited in a timely manner?
- Do you have large amounts of revenue due shortly after the close of the current fiscal year that should actually be attributed to the current year?
- Do you prepare a cash flow projection on an annual basis to depict the anticipated flow of revenues and expenditures during the course of the year? Is the actual cash flow compared to the projected cash flow on a routine basis? Are major expenditures timed to occur when cash will be available to pay bills? Do you familiar with the process for obtaining short-term loans in anticipation of taxes and other revenues so you are prepared to act quickly to borrow funds if the need arises?
- Do you have an aggressive policy for the investment of fund balances?

## Factor 7: Debt Service

### DESCRIPTION

This factor shows the proportion of general operating revenue devoted to paying off outstanding debt—loans, bonds, vendor leases and lease rental payments to authorities—each year. Like borrowing money by a household or business, excessive municipal debt can lead to problems, particularly when the tax base is declining or stable.

This factor compares debt service to general operating revenues. Generally, debt analysts believe that a ratio of up to 10% debt to operating revenues is acceptable. Debt service in excess of 15% - 20% of operating revenues is considered a potential problem.

Some communities have self-supporting debt, revenue debt tied to specific user fees such as water and sewer systems. For purposes of this factor, totally self-supporting debt may be excluded if the operating revenue supporting it is also excluded. Principal payments on short-term debt (tax/revenue anticipation notes) are excluded but interest on short-term debt is included. Receipts from short-term borrowings must be also excluded from total revenues.

### Formula:

$$\frac{\text{Debt Service (Not Including Self-Supporting Debt)}}{\text{Total Operating Revenue}}$$

### Data Sources:

- **Debt Service:** Sum of accounts 471, 472, 474 and 475 in Annual Audit and Financial Report. It must include lease rental payments to municipal authorities.
- **Total Operating Revenue:** See Factor 1.

**Warning Signal:** Increasing Amount of Debt Service as a Percentage of Total Operating Revenues

### FACTOR 7 - DEBT SERVICE CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Debt Service					
2. Total Operating Revenue					
3. Debt Service as % of Total Operating Revenue ( <i>Line 1 divided by Line 2</i> )					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Debt Service					
2. Total Operating Revenue					
3. Debt Service as % of Total Operating Revenue ( <i>Line 1 divided by Line 2</i> )					

## FACTOR 7 - DEBT SERVICE TRENDS AND ANALYSIS

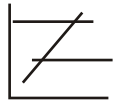
**Instructions:** List the years to be examined across the bottom. The percentages resulting from the calculations are plotted against the scale on the side. The highlighted line represents 10%. A trend remaining at or below the 10% line is considered within the acceptable range.

**Percent**

40


0

Years ->



**Unfavorable Trend** (*Color Code = Red*)

A result like one to the left indicates debt service costs in excess of the generally accepted range. Increases in revenues are not keeping up with the annual costs to service the debt being incurred.



**Stable Trend** (*Color Code = Yellow*)

If the graph looks like the one to the left, it indicates that your revenue base is increasing in proportion with your debt service.



**Favorable Trend** (*Color Code = Green*)

If you are able to keep your debt below 10% of revenue, a favorable trend will develop. Every effort should be made to sustain this level while meeting the capital requirements of the community.

## **FACTOR 7 - DEBT SERVICE ACTION ITEMS**

If you are experiencing an *increase* in debt service as compared to total revenues, you may want to consider the following:

- Is the increase due to an increase in short or long-term debt? Is the increase due to a decrease in total revenues rather than an increase in debt service? If revenues are decreasing, the community may not be able to borrow funds at attractive interest rates until previously borrowed funds have been repaid.
- Some communities have delayed capital projects and then sporadically undertaken major borrowings. In order for a community to remain healthy, capital investments are essential, but efforts should be made to develop a capital plan that evenly schedules improvements on a regular basis. The plan should encompass all available funding options—grants, low interest loan programs and long-term bonded debt.
- If a community has a significant amount of outstanding debt with higher interest rates than are available today, refinancing the debt can decrease interest costs. Independent advice should be sought to assist with this evaluation process.
- High interest rates may be the result of unfavorable credit ratings. Local officials should review the ratings with their financial advisors to determine which factors in the credit rating report might be improved.
- It is not appropriate or legal to use long-term debt to fund operating expenses unless authorized by the Court of Common Pleas in an action for approval of unfunded debt. No community should attempt to issue long-term debt to fund current expenses.

## Factor 8: Long-Term Debt

### DESCRIPTION

This factor compares the municipality's long-term debt as a percentage of its assessed valuation. This is particularly relevant in Pennsylvania where municipalities have unlimited real estate taxing power to meet debt service payments.

In a business sense, assessed valuation is the asset or the collateral being pledged against loans being taken. This factor will show if the growth of the underlying asset, real property, is keeping up with any accumulation of long-term debt.

The credit rating agencies tend to look at the following as warning signs on long-term debt.

- Long-term debt exceeds 10% of assessed valuation.
- Long-term debt exceeds 90% of the total borrowing capacity under state law. In Pennsylvania, the Local Government Unit Debt Act sets the non-electoral debt limit for municipalities.

### Formula:

$$\frac{\text{Long-Term Debt}}{\text{Assessed Valuation}}$$

### Data Sources:

- **Long-Term Debt:** Annual Audit and Financial Report.
- **Assessed Valuation:** Annual Audit and Financial Report.

**Warning Signal:** Increasing Amount of Long-Term Debt as a Percentage of Assessed Valuation

### FACTOR 8 - LONG-TERM DEBT CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Long-Term Debt					
2. Assessed Valuation					
3. Long-Term Debt as % of Assessed Value (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Long-Term Debt					
2. Assessed Valuation					
3. Long-Term Debt as % of Assessed Value (Line 1 divided by Line 2)					



## FACTOR 8 - LONG-TERM DEBT TRENDS AND ANALYSIS

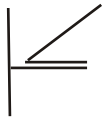
**Instructions:** List the years to be examined across the bottom. Plot long-term debt against the vertical axis. The highlighted line represents 10%. A ratio of 10% or less represents an acceptable level for long-term debt.

**Percent**

**40**


**0**

**Years ->**



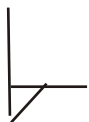
**Unfavorable Trend** (*Color Code = Red*)

The municipality's long-term debt is growing faster than its property tax base. Effort must be made to limit future borrowing only to essential purposes.



**Stable Trend** (*Color Code = Yellow*)

A good sign. Attempt to keep the value of long-term debt below the 10% line.



**Favorable Trend** (*Color Code = Green*)

The municipality is in good shape and is able to borrow when necessary to fund capital improvements.

## **FACTOR 8 - LONG-TERM DEBT ACTION ITEMS**

If you have an *increasing* percentage of long-term debt as compared to assessed valuation, you may want to consider the following.

- An increase of a municipality's capacity for incurring further debt may require a diversification of revenue sources. More reliance on service fees and user charges to fund operations may enhance a community's ability to increase debt for capital purposes.
- If the county has not recently undertaken a comprehensive reassessment, municipal property values may be significantly under-assessed. A countywide reassessment reflecting up-to-date and accurate property values may provide future debt capacity.
- A capital improvements program should extend from five to ten years into the future. A capital improvements planning process scheduling projects and funding at relatively consistent levels from year to year may keep debt levels more stable. The payback period for long term debt must not exceed the estimated useful life of the capital project it is used to finance.
- Grant funding for capital projects should be sought whenever possible to offset the need to borrow long term. Contact should be made with appropriate county, regional, state and federal agencies to determine whether your projects are eligible for funding.

## Factor 9: Debt Per Capita

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### DESCRIPTION

Another measure of the impact of long-term debt is debt per capita. This factor is designed to demonstrate the debt burden associated with each municipal resident, thereby taking into consideration the ability of the citizens to repay loans rather than the underlying value of the collateral (real estate) pledged as indicated in Factor 8 - Long Term Debt.

### Formula:

$$\frac{\text{Long-Term Debt}}{\text{Population}}$$

*NOTE: You may want to consider adjusting the debt value from year to year by discounting for inflation. See the Introduction for instructions.*

### Data Sources:

- **Long-Term Debt:** Annual Audit and Financial Report.
- **Population:** Most recently available population estimate. Use the same source for all years.

**Warning Signal:** Increasing Long-Term Debt Per Capita

### FACTOR 9 - DEBT PER CAPITA CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Long-Term Debt					
2. Population					
3. Per Capita Debt (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Long-Term Debt					
2. Population					
3. Per Capita Debt (Line 1 divided by Line 2)					

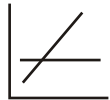
**FACTOR 9 - DEBT PER CAPITA TRENDS AND ANALYSIS**

**Instructions:** List the years to be examined across the bottom. Plot the debt per capita against the vertical axis. *Debt Per Capita at or below \$1,200 represents an acceptable level.* The highlighted line indicates the \$1200 level of debt per capita.

**Dollars**  
**4,000**


**0**

**Years ->**



**Unfavorable Trend** (*Color Code = Red*)

This trend represents an increasing burden on residents. Compare it with Factors 7 and 8 to get complete picture.



**Stable Trend** (*Color Code = Yellow*)

Your debt burden is proportionately increasing and/or decreasing in relation to changes in the population.



**Favorable Trend** (*Color Code = Green*)

Debt burden is being kept low. Borrowing may be undertaken as necessary for capital improvements.

**FACTOR 9 - DEBT PER CAPITA ACTION ITEMS**

If you are experiencing an *increase* in debt per capita, you should consider the items listed under the Action Items for Factors 7 - Debt Service and Factor 8 - Long Term Debt.

## Factor 10: Operating Position

### DESCRIPTION

Operating position is essentially defined as the local government's ability to (1) balance its budget on an annual basis, (2) maintain reserves to cover emergency situations—natural disasters, unexpected and generally expensive infrastructure repairs, and (3) have sufficient cash available for timely payment of bills, especially in times when cash flow is not even. This factor is designed to indicate whether a municipality is operating on a break-even basis or is spending down fund balances from previous years to fund current operations.

For this calculation, a number more than 1.0 means the community operated during the year at a deficit with its current expenses exceeding its revenues. A result of 1.0 means you broke even or expenses were equal to revenues received. And where the factor's value is less than 1.0, the municipality's current revenues exceeded its expenditures resulting in an operating surplus.

### Formula:

$$\frac{\text{General Fund Operating Expenditures}}{\text{General Operating Revenue}}$$

### Data Source:

- **Operating Expenditures and Operating Revenue:** See Factors 1 and 4.

**Warning Signal:** Amount of General Fund Operating Deficit as a Percentage of Total Operating Revenues Increases

### FACTOR 10 - OPERATING POSITION CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Expenditures					
2. Operating Revenue					
3. Operating Position (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Operating Expenditures					
2. Operating Revenue					
3. Operating Position (Line 1 divided by Line 2)					

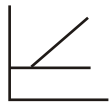
## FACTOR 10 - OPERATING POSITION TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom. Plot the result for operating position against the vertical axis. *The highlighted line represents 1.0, the point where operating revenue and operating expenditures are equivalent.*

1.4

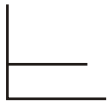

.1

Years ->



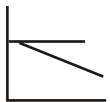
**Unfavorable Trend** (*Color Code = Red*)

If the municipality is operating on previous year's fund balances for two or more of the past five years, immediate corrective actions are warranted.



**Stable Trend** (*Color Code = Yellow*)

The municipality is operating in a break-even situation. There should be some effort to keep fund balances at a healthy level.



**Favorable Trend** (*Color Code = Green*)

Fund balances are being built up for emergencies.

## **FACTOR 10 - OPERATING POSITION ACTION ITEMS**

If the municipality's operating position is unfavorable, you may want to consider the following:

- The technical definition for a balanced budget is that current revenues are equivalent to current expenses. Taxes, fees, grants and the proceeds of long-term debt for capital improvements received during the fiscal year should meet or exceed the anticipated current year expenses for personnel, contractual services, materials and supplies, debt service and capital projects. If the municipality is not generating sufficient revenues to pay for all current expenses, it is either borrowing from another fund, using loans to pay for current expenses or living off prior years' surpluses. While many municipalities use these strategies to postpone tax increases, at some moment such practices will catch up with you.
- Financial analysts warn a municipality developing patterns of negative (less than 1.0) operating positions will be considered as financially weak. Such patterns include: two successive years of an operating deficit, a current year deficit greater than that of the prior year, operating deficits in two of the past five years, and a deficit greater than 5 - 10% of the annual operating budget. Operating at a deficit could be costly to the community in terms of paying higher interest rates in the event the municipality needs to borrow for major capital projects.
- Financial analysts also advocate maintaining an unreserved fund balance equivalent to at least 5% of the general operating budget. Surpluses in excess of 5% - 10% should be utilized for one-time expenses or be used to fund capital improvements rather than be used to artificially balance next year's budget. When the surpluses run out, the municipality usually faces the very difficult decision of not only raising taxes to meet the next year's typical expenditure increases, but also raising additional revenues to make up for the operating costs previously covered by the surplus funds. Or, at times, the municipality must face the prospect of significantly curtailing basic services when tax increases are not feasible. Moderate fund balances, though sometimes difficult to achieve, are good insurance.
- If the municipality did not consciously act as described in item 1, then time should be taken to determine why a negative position might have occurred. Were actual expenditures in excess of those budgeted? Were revenues received short of those estimated? Were the differences due to poor budgetary practices or unforeseen, emergency circumstances? If current financial management practices are the cause of the problem, perhaps the municipality should revise its procedures for budget preparation or monitoring of the budget throughout the fiscal year. If the situation arose as a result of an emergency, then consider developing a reserve to finance emergency expenses or projects to alleviate their potential future impact.
- One practice that should strictly be avoided is borrowing for a period greater than one year to fund operating expenses and rolling over short-term debt to fund operating expenses. Both mechanisms principally enable municipal officials to put off facing the reality of either cutting services or raising sufficient revenues to pay for current services.

## Factor 11: Unfunded Pensions

### DESCRIPTION

One of the most significant problems for many Pennsylvania's local governments is unfunded employee pension liabilities. These liabilities essentially represent the municipality's long-term obligations (debts) to past and current employees. The liability generally mounts over time as the municipality fails to make employer contributions or when benefit increases are granted without providing additional funding to cover their cost.

The crisis created by unfunded pensions was addressed by the Pennsylvania legislature by enacting Act 205 of 1984, the Municipal Pension Plan Funding Standard and Recovery Act. Consequently, local governments must now ascertain their employee pension liabilities on an annual or a biennial basis depending on the severity of their unfunded liability. Municipalities with unfunded obligations must annually make contributions to retire the unfunded amount. And prior to implementing benefit changes, municipal employers must identify how the costs will be funded through either employee or employer contributions. The objective of Act 205 is to achieve financial stability for unfunded pension systems over a period of twenty years.

Today, when this factor is evaluated, most municipalities should see stable or improving trends if they are in compliance with Act 205. This factor compares the total unfunded pension liability against assessed valuation as an indication of a community's ability to raise money to meet those obligations.

### Formula:

$$\frac{\text{Unfunded Pension Liabilities}}{\text{Assessed Valuation}}$$

### Data Sources:

- **Unfunded Pension Liabilities:** Municipal Pension Plan Actuarial Study Reports.
- **Assessed Valuation:** Annual Audit and Financial Report. Use the same source for each year.

**Warning Signal:** Increasing Amount of Unfunded Pension Liabilities as a Percentage of Assessed Valuation

### FACTOR 11 - UNFUNDED PENSIONS CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Unfunded Pension Liabilities					
2. Assessed Valuation					
3. Unfunded Pension Ratio (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Unfunded Pension Liabilities					
2. Assessed Valuation					
3. Unfunded Pension Ratio (Line 1 divided by Line 2)					



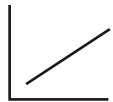
## FACTOR 11 - UNFUNDED PENSIONS TRENDS AND ANALYSIS

**Instructions:** List the years being examined across the bottom axis. Plot the factor against the vertical axis.

Percent  
100


0

Years ->



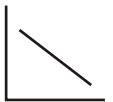
**Unfavorable Trend** (*Color Code = Red*)

Unfunded pension liabilities are increasing faster than the value of the community's major asset, real property.



**Stable Trend** (*Color Code = Yellow*)

Liabilities and property values are changing consistently. However, any unfunded liabilities are a problem.



**Favorable Trend** (*Color Code = Green*)

Unfunded pension liabilities are decreasing in relation to property values. If pensions are not fully funded, supplemental contributions should be considered.

## **FACTOR 11 - UNFUNDED PENSIONS ACTION ITEMS**

If you are experiencing problems in the area of unfunded pension liabilities, you may want to consider the following:

- Does the legislative body know the extent to which its pension system(s) are funded or under-funded? Has the municipality contracted to have an actuarial study of its pension plans completed at least every two years?
- Has the municipality made its required minimum municipal obligation contribution on an annual basis in accordance with Act 205? Has the contribution been made on a timely basis to avoid incurring interest costs?
- Are you careful to consider increased pension cost liabilities when negotiating with employee bargaining units? If you are considering increasing pension benefits, have you relied on Act 205's provisions related to employee versus employer contributions in determining how the additions to the benefits will be funded?

## Factor 12: Revenue Shortfalls

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### DESCRIPTION

Some factors are helpful in examining both fiscal condition and the performance of municipal officials in controlling budgets. While estimating revenues often seems to require a crystal ball, some municipalities regularly overestimate revenues as a way to make budgets balance. If expenditures are kept below budget during the year, this practice may not cause a problem. If expenditures equal or exceed estimates, there may not be sufficient revenues to meet the year's expenditures.

This formula is designed to compare estimated revenue with actual revenues. A result of 1.0 indicates a break-even situation; a result of less than 1.0 indicates revenues were budgeted in excess of actual revenues received; and a ratio of more than 1.0 indicates actual revenues received were in excess of those budgeted.

### Formula:

$$\frac{\text{Actual Year-End Revenue}}{\text{Budgeted Revenue}}$$

### Data Sources:

- **Actual Year-End Revenue:** Annual Audit and Financial Report.
- **Budgeted Revenue:** Annual Budget.

**Warning Signal:** Increasing and/or Consecutive Revenue Shortfalls

### FACTOR 12 - REVENUE SHORTFALL CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Actual Year-End Revenues					
2. Budgeted Revenues					
3. Revenue Shortfall (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Actual Year-End Revenues					
2. Budgeted Revenues					
3. Revenue Shortfall (Line 1 divided by Line 2)					



## **FACTOR 12 - REVENUE SHORTFALL ACTION ITEMS**

If you are experiencing revenue shortfalls on a recurring basis, you may want to consider the following:

- Ideally, revenue estimates should be a little on the conservative side. At year-end, actual revenue received should be 2% - 5% above budget estimates.
- Operating deficits are or may soon be realized unless the municipality is able to keep spending levels below budget amounts. Financial reports comparing actual versus budgeted revenue and expenditures should be monitored closely throughout the year. This will allow municipal officials the opportunity to make adjustments in a timely fashion and prevent or minimize a fiscal crisis.
- Assuming efforts are being made to come up with an accurate budget, the procedure for estimating revenue should be examined. There may be factors at work in the community over which you have no control (assessment changes, recession-oriented changes in the wage tax base). There may also be a need to review the revenue collection systems to assure that they are efficient and effective.
- In the event that shortfalls persist, each major source of revenue should be reviewed separately to determine where the shortfall is and exactly what is causing the estimating problem.
- Regularly overestimating revenue is a trap that can give municipal officials a false sense of fiscal security and may prevent them taking difficult actions necessary to live within their means.

## Factor 13: Budget Overruns

### DESCRIPTION

Evaluation of the budget overruns factor is a way to assess (1) how well the estimates for anticipated expenditures for the year were prepared and (2) how closely the budgeted versus actual expenses were monitored throughout the year. The factor shows whether a pattern of municipal expenses exceeding appropriations has developed. It should be reviewed in conjunction with revenue shortfalls to determine how well the budget is managed overall.

A combined graph depicting both Factor 12 - Revenue Shortfalls and Factor 13 - Budget Overruns will indicate how accurately the annual budget is prepared. The accepted gauge is that actual expenditures at year-end should be 2 - 5% less than budgeted appropriations and actual revenues at year-end should be 2 - 5% in excess of the budget estimates.

The formula establishes a ratio where a result of 1.0 indicates an exact budget to actual expense match; a ratio of more than 1.0 indicates that actual expenditures exceed the amounts budgeted; and a value less than 1.0 represents actual expenditures below those budgeted.

### Formula:

$$\frac{\text{Year-End Actual Expenditures}}{\text{Budgeted Expenditures}}$$

### Data Sources:

- **Year-End Actual Expenditures:** Annual Audit and Financial Report
- **Budgeted Expenditures:** Annual Budget

**Warning Signal:** Consecutive Budget Overruns

### FACTOR 13 - BUDGET OVERRUNS CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Year-End Actual Expenditures					
2. Budgeted Expenditures					
3. Budget Overrun (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Year-End Actual Expenditures					
2. Budgeted Expenditures					
3. Budget Overrun (Line 1 divided by Line 2)					



## **FACTOR 13 - BUDGET OVERRUNS ACTION ITEMS**

If you are experiencing a problem in this area, you may want to consider the following:

- Review this factor in relation to Factor 12, Revenue Shortfalls. If actual expenditures consistently exceed estimated expenditures by more than 2 - 5% and the cause can not be attributed to an emergency, unanticipated or extraordinary circumstance, then the community's budget preparation or budget monitoring procedures may need revision. The problem can be compounded if actual revenues prove to be less than expected.
- To alleviate the situation, each area of major expense should be examined. The rationale for budget estimates for each type of expense should be clearly understood by both elected and appointed officials. For most municipalities, much of the budget is comprised of uncontrollable items—employee contracts, specified employee benefits, contracts for services such as garbage collection and disposal, insurance premiums, utility charges and debt service. Efforts to force the budget to balance by shortchanging these areas are especially ill advised. For example, the full cost for employees over the 12-month fiscal year should be reflected in the budget unless decisions are made at the time the budget is adopted to reduce the workforce during the year and a timetable is developed to implement these decisions. Otherwise, the community will likely end the year with unpaid bills and obligations.
- A companion to good budgeting is the implementation of a conscientious budget monitoring process. Each month, close scrutiny of reports depicting comparisons of actual versus budgeted revenues and expenses will allow elected and appointed officials recognize fiscal problems as they arise. Reviewing budget reports on a timely basis allows local officials to take corrective actions during the course of the year to reduce expenditures and perhaps prevent a crisis at year-end.



## Factor 14: Uncollected Property Tax

### DESCRIPTION

Given the importance of property taxes in Pennsylvania, a good indicator of fiscal health is the dollar amount and percentage of property taxes not paid each year. An increase in uncollected property taxes may indicate a decline in the capacity of the community to provide basic services.

Traditionally, property taxes carry the lowest rate of delinquency. A municipality is considered typical by financial institutions and credit rating agencies, if it collects 97-98% of the real estate taxes levied. A delinquency rate of 5-7% is a negative sign and could indicate a long-term problem for the community.

The formula produces a percentage value for uncollected property tax as compared to the total real estate tax levy. The higher the percentage, the greater the uncollected taxes.

### Formula:

$$\frac{\text{Uncollected Property Tax}}{\text{Net Property Tax Levy}}$$

### Data Source:

- **Net Property Tax Levy:** Annual operating budget.
- **Uncollected Property Tax:** Net property tax levy minus current year actual collections.

**Warning Signal:** Increasing Amount of Uncollected Property Taxes as a Percent of Net Property Tax Levy

### FACTOR 14 - UNCOLLECTED PROPERTY TAX CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Uncollected Property Tax					
2. Net Property Tax Levy					
3. % of Uncollected Property Tax (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Uncollected Property Tax					
2. Net Property Tax Levy					
3. % of Uncollected Property Tax (Line 1 divided by Line 2)					

**FACTOR 14 - UNCOLLECTED PROPERTY TAX TRENDS AND ANALYSIS**

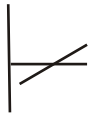
**Instructions:** List the years to be examined across the bottom and plot the percentage of uncollected property tax against the vertical axis.

**Percent**

**16**

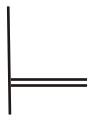

**0**

**Years ->**



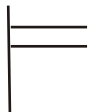
**Unfavorable Trend** (*Color Code = Red*)

An increasing share of property tax is not being collected. The collection system should be reviewed. Collecting less than 95% of the annual real estate tax levy on a current basis is considered unfavorable.



**Stable Trend** (*Color Code = Yellow*)

Provided the line is situated at the low end of the scale, this is an acceptable trend and may actually be favorable. Collecting at least 97% of the annual real estate levy on a current basis is considered acceptable.



**Favorable Trend** (*Color Code = Green*)

A low percentage rate indicates a high level of tax collection. Consistently collecting 97% - 98% of the annual real estate levy on a current basis is considered favorable.

## **FACTOR 14 - UNCOLLECTED PROPERTY TAX ACTION ITEMS**

If uncollected property taxes are *increasing*, you may want to consider the following:

- Is your real estate tax collection system efficient? Are the penalties and interest applied to late payments at the maximum allowable rate? Are delinquent properties liened or turned over to the tax claim bureau or delinquent collector on a timely basis?
- Does your municipality have a policy to track unpaid taxes returned to the county tax claim bureau?
- If adverse economic conditions exist, are you willing to accept installment payments of real estate taxes?
- What is the composition of the delinquent properties?
  1. are low-income homeowners no longer able to pay increases in property taxes? Consider instituting a real estate tax deferral program for low-income homeowners under the Real Estate Tax Deferral Program Act. This allows deferral of increases in tax bills until the property is sold or inherited.
  2. are properties being abandoned in some neighborhoods? Have you considered the sale of abandoned properties in conjunction with other taxing bodies as a means to return the properties to the active tax rolls?

## Factor 15: User Charges/Fees

### DESCRIPTION

While this may be a difficult factor for municipalities to analyze, it is included because many communities have user charges or fees for services such as garbage collection and disposal, water supply, sewage collection and treatment, recreation and building inspection. Communities, therefore, should know whether these charges or fees are high enough to cover all of the costs associated with providing the services. If they are not, a subsidy from general tax revenues is the result, even if unintended.

The degree the municipality finances services from user charges and fees is a policy decision, as is the extent of any tax subsidy from general revenues. This formula calculates the ratio of expense to revenue with 100 percent indicating that the cost of the service is totally covered from user charges.

If the local government has a variety of charges or fee-based services, it is useful to independently examine each in terms of how much of the function it supports.

### Formula:

$$\frac{\text{Fees and User Charge Revenues}}{\text{Total Cost of Providing Service}}$$

### Data Sources:

- **Fees and User Charge Revenue:** Annual Audit and Financial Report.
- **Total Cost of Providing Service:** Annual Audit and Financial Report.

**Warning Signal:** Decreasing Percentage of Revenue to Cover the Cost of User Services

### FACTOR 15 - USER CHARGES/FEES CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Fees & User Charge Revenue					
2. Total Cost of Providing Service					
3. % of Coverage (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Fees & User Charge Revenue					
2. Total Cost of Providing Service					
3. % of Coverage (Line 1 divided by Line 2)					



## **FACTOR 15 - USER CHARGES/FEE ACTION ITEMS**

If an unfavorable trend results for this factor, you may want to consider the following:

- If you are subsidizing user charge/fee based services, you may want to raise the policy question of whether this is the intent of the governing body and whether a tax subsidy on a continuing basis is affordable. While some special areas, such as swimming lessons, may warrant such a subsidy, others that are consumer-oriented—water, sewer, garbage collection—should not be. Rate schedules be evaluated as part of the annual budget process and revised as necessary to ensure that services continue to be self-sufficient.
- How efficient and effective are your billing and collection systems for the charges and fees? Significant delinquency rates may make presumably self-sufficient service fees and charges inadequate. Does your billing and collection process need to be more aggressive? Are your penalty and interest rates at the maximum allowable by law? Do you aggressively discontinue service for nonpayment of fees and charges where authorized?
- When considering the provision of new services, all projected costs should be measured against expected revenue, if a fee or charge is involved.

## Factor 16: Employees Per Capita

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### DESCRIPTION

Productivity is a difficult factor to measure with a simple formula. Nevertheless, a community must have some indication of whether the workforce is increasing in relationship to some standard.

One of the measures is to look at the trend of employees per capita, that is, the number of employees per resident of the community. The trend produced by this formula should only be the beginning of an examination of municipal expenditures. Ultimately, each function within the municipality may have to be examined separately to determine where the areas of growth are occurring.

In order to have the ratio result in more manageable whole numbers, it is suggested that the result be multiplied by 1,000.

### Formula:

$$\frac{\text{Full Time Municipal Employees}}{\text{Population}} \times 1,000 = \text{Municipal Employees Per 1,000 Population}$$

### Data Sources:

- **Full-Time Municipal Employees:** Payroll records. Use the same time period for each year.
- **Population:** See Factor 1.

**Warning Signal:** Increasing Number of Municipal Employees Per 1,000 Population

### FACTOR 16 - EMPLOYEES PER CAPITA CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Full-time Employees					
2. Population					
3. Employees Per Capita (Line 1 divided by Line 2)					
4. Municipal Employees Per 1,000 Population (Line 3 X 1000)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Full-time Employees					
2. Population					
3. Employees Per Capita (Line 1 divided by Line 2)					
4. Municipal Employees Per 1,000 Population (Line 3 X 1000)					

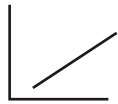
## FACTOR 16 - EMPLOYEES PER CAPITA TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom and employees per capita against the vertical axis.

**Employees / 1,000 Population**

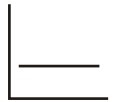

0

Years ->



**Unfavorable Trend** (*Color Code = Red*)

There is an increase in employees per capita. An examination of each functional area should be made to determine why.



**Stable Trend** (*Color Code = Yellow*)

Provided the workforce is productive, this is a good sign.



**Favorable Trend** (*Color Code = Green*)

Increased productivity and/or reduced number of services are evident here.



## **FACTOR 16 - EMPLOYEES PER CAPITA ACTION ITEMS**

If you are experiencing an *increase* in the number of employees per capita, you may want to consider the following:

- Are expenditures rising faster than revenues? Is the local government becoming more labor intensive? Is employee productivity diminishing? Has the municipality maintained the same number of employees even though it has recently contracted for a service previously performed by municipal employees?
- If you believe that your local government is becoming more labor intensive or productivity is declining, examine each functional or programmatic area to determine where the changes are occurring.
- Is the increase due to an increased demand for services or an expansion in services? Have demands for service changed due to changes in the composition of the population?
- Have provisions in labor agreements resulted in a decrease in productivity and, if so, are negotiators aware of the impact when involved in discussions of work rules and employee practices?
- Has there been any attempt to incorporate performance measures for each function or program into the annual budget? If so, how do those measures compare from year to year?
- Have you consulted with similarly sized municipalities in your areas that provide comparable services? If you find a similarly sized municipality performing the functions/programs with fewer employees, consult with them and learn from their experience. Municipalities are generally proud of their accomplishments and happy to share success stories.

## Factor 17: Property Value

### DESCRIPTION

This factor measures the growth in property value over time and is designed to indicate whether there is growth from year to year. Not only do property taxes represent a major source of revenue for most local governments, but growth in real estate valuations also reflects the pace of economic development.

This is an especially critical factor for municipalities that are approaching or have reached their millage limit. In such cases, where there is a decline or little growth in property values, the ability of the municipality to support basic services may be impaired.

This factor calculates the percentage change in property value from year to year. For this factor, either the market value or assessed value may be used. In some counties the common level ratio will change radically during the study period due to countywide reappraisal or change in the predetermined ratio. For municipalities in these counties, only the market value will give a realistic picture of changes in property values.

### Formula:

$$\frac{\text{Current Year Property Value Minus Last Year's Property Value}}{\text{Last Year's Property Value}}$$

### Data Source:

- **Assessed Value:** Annual Audit and Financial Report.
- **Market Value:** Calculate using the county common level ratio determined annually by the State Tax Equalization Board. Divide assessed value by the common level ratio.

**Warning Signal:** Diminishing Growth or Decline in Market or Assessed Value

### FACTOR 17 - PROPERTY VALUE CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Current Property Value					
2. Previous Year's Property Value					
3. Change in Value (Line 1 - Line 2)					
4. % Change in Value (Line 3 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Current Property Value					
2. Previous Year's Property Value					
3. Change in Value (Line 1 - Line 2)					
4. % Change in Value (Line 3 divided by Line 2)					



## **FACTOR 17 - PROPERTY VALUE ACTION ITEMS**

If you are experiencing a *decrease* in the growth of property values, you may want to consider the following:

- Have major parcels been removed from the tax rolls due to acquisition by the taxing jurisdictions or tax exemptions?
- Is the municipality actively pursuing development? Are the local zoning and land development regulations conducive to current types of development? If you have lost a major industrial property, you may be faced with the need to develop a new land use plan to accommodate diverse types of development.
- Is the condition of the local infrastructure inhibiting the reuse of existing commercial and industrial properties? The community may need to initiate an infrastructure rehabilitation program to attract and retain uses that will maintain local property values.

## Factor 18: Fiscal Capacity

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### DESCRIPTION

Because of the importance of property taxes in Pennsylvania, another measure of a community's health is the amount of assessed valuation *per capita*. This factor computes that relationship and will show whether "fiscal capacity," that is, the ability of a community to meet its obligations, is reflected in its major asset, property value.

#### Formula:

$$\frac{\text{Assessed Valuation}}{\text{Population}}$$

#### Data Source:

- **Assessed Valuation:** Annual Audit and Financial Report.
- **Population:** See Factor 1.

**Warning Signal:** Decreasing Amount of Assessed Valuation Per Capita

### FACTOR 18 - FISCAL CAPACITY CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Assessed Valuation					
2. Population					
3. Fiscal Capacity (Line 1 divided by Line 2)					

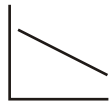
ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Assessed Valuation					
2. Population					
3. Fiscal Capacity (Line 1 divided by Line 2)					

## FACTOR 18 - FISCAL CAPACITY TRENDS AND ANALYSIS

**Instructions:** List the years to be examined across the bottom and plot fiscal capacity against the vertical axis.

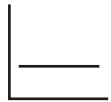
Dollars


Years ->



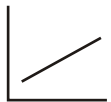
**Unfavorable Trend** (*Color Code = Red*)

The value of property per person is declining. The reasons for this circumstance should be reviewed.



**Stable Trend** (*Color Code = Yellow*)

Population growth and property values are keeping pace with each other. This could be a bad sign particularly in times of general property value growth due to inflation.



**Favorable Trend** (*Color Code = Red*)

Property values on a per person basis are rising.

## FACTOR 18 - FISCAL CAPACITY ACTION ITEMS

If you are experiencing a decrease in your fiscal capacity, then you may want to consider the following issues related to the previous property value factor.

- Have major parcels been removed from the tax rolls due to delinquency or tax exemption?
- What is the relationship between market value as reported by the State Tax Equalization Board and the assessed valuation? A major discrepancy would make this factor head in the wrong direction, perhaps without just cause.
- Are you actively coordinating potential economic development and municipal zoning and planning considerations to promote development within the community? If you have lost a major industrial use, you may be faced with a need to develop a new community land use plan to accommodate different types of development for the property.
- Even if your fiscal capacity trend is positive, you should know if your municipality is dependent on a small number of large taxpayers. A chart as shown below might be useful if you believe this is the case. Obviously, the risk of losing one of these proportionately large taxpayers can create overnight distress and could neutralize any positive trends in overall capacity.

Ten Largest Taxpayers	% of Total Taxes Paid
1.	
2.	
3.	
4.	
5.	
6.	
7.	
8.	
9.	
10.	
<b>TOTAL:</b>	

## Factor 19, 20: Employment Base/Community Jobs

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### DESCRIPTION

In examining a municipality's fiscal health, one of the important factors is the examination of the employment base. Because community characteristics vary, the employment base may be more significant if measured in one of two ways: either the number of jobs in the community (measured by occupational privilege taxpayers/local services tax payers) or the number of residents who are employed (measured by earned income taxpayers). In communities with a more even mix of residential, commercial and industrial uses, both factors may deserve examination. The formulas suggested produce a percentage of growth/decline over time.

### Formula:

*Employment Base:*

$$\frac{(\text{Number of OPT/LST Accounts—Current Year}) \text{ Minus } (\text{Number of Accounts—Prior Year})}{\text{Number Of Accounts for Prior Year}}$$

*and/or*

*Community Jobs:*

$$\frac{(\text{Number of EIT Accounts—Current Year}) \text{ Minus } (\text{Number Accounts— Prior Year})}{\text{Number of Accounts for Prior Year}}$$

### Data Sources:

- Data should be obtained from the municipality's collector of occupation privilege and/or earned income taxes to calculate this factor.

**Warning Signal:** Decreasing Number of Community Jobs and/or Employed Residents

### FACTOR 19/20 - EMPLOYMENT BASE/COMMUNITY JOBS CALCULATIONS

*NOTE: The same work sheet can be used for both the Employment Base and Community Jobs factors.*

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Current Year Accounts					
2. Prior Year Accounts					
3. Growth (Line 1 - Line 2)					
4. Percent Growth (Line 3 divided by Line 2)					





## **FACTORS 19/20 - EMPLOYMENT BASE/COMMUNITY JOBS ACTION ITEMS**

If the employment base or community jobs factors indicate a *declining* trend, you may want to consider the following:

- Are tax collection procedures efficient and essentially reliable and as a consequence all eligible taxpayers are in the system?
- Have major employers reduced their workforce or shut down?
- Are zoning and development ordinances up-to-date and facilitate rather than hinder creation of new jobs?
- Have you examined other factors (Revenue Per Capita, Employees Per Capita, etc.) to make sure that you are adjusting your expenditure levels to economic conditions within the community?



**Instructions:** Enter the changes from year to year on the Factor Summary Chart in the front of this book as follows.

- (+) or green - Favorable
- (0) or yellow - Stable
- (-) or red - Unfavorable

## **FACTOR 21 - CONSTRUCTION ACTIVITY ACTION ITEMS**

If the number and value of building permits is *declining*, you may want to consider the following:

- Are municipal tax structures and zoning/building/land development ordinances designed to encourage residential, commercial, and/or industrial development?
- Is land available for development or redevelopment purposes? Are major infrastructure improvements necessary to facilitate the development or redevelopment of local properties? A cost/benefit analysis of the municipality's implementation of such improvements might be advantageous.
- A national recession over which you have no control may be the reason for a temporary decline in construction activity.
- What other issues should the municipality address to encourage construction activity? For instance, is the local tax structure, the quality of local schools, recreational and other amenities, and/or public transportation a factor discouraging investment in the community?

## **Factor 22, 23, 24: Municipal Demographics: Population (Population Growth), Personal Income and Percent of Population Over 65**

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### **DESCRIPTION**

There are many demographic characteristics that can be used to analyze the economic and fiscal health of a community. Unfortunately, many of these are produced officially only at census time, although estimates are made intermittently. Nevertheless, a municipality may want to begin charting these numbers to get a look at what is happening to its population.

Three statistics are suggested here, population (or population growth), personal income and percent of population over age 65.

Adverse trends in these areas may be the result of unique community characteristics so no specific action agenda is suggested. Efforts should be made to keep a balanced population, and long-range plans for the community should address this issue. The ability to collect taxes, both property and income, usually depends on a stable workforce.

### **Data Sources:**

All of the data comes from U.S. Census information available from the county planning department, regional planning commission, or the State Data Center at 717-948-6336 or [www.psd.c.hbg.psu.edu](http://www.psd.c.hbg.psu.edu).

**Warning Signal:** Decline in Population or Personal Income or Increase in Percent of Population Over 65



## Factor 25: Capital Outlay

### DESCRIPTION

How much current revenue does a municipality allocate on an annual basis to fund capital expenditures? A capital expenditure is generally defined as a nonrecurring cost in excess of a certain dollar value set by the legislative body. It includes vehicles, equipment, sanitary sewer, storm sewer, and water systems, roads, buildings and other facilities used by the municipality to provide services and programs. Overall, it represents the community's infrastructure or assets. Over a period of time, a municipality ought to commit essentially the same proportion of its current revenue to fund the acquisition or replacement of its infrastructure as well as finance the engineering and design work for major capital projects. A decrease in the percentage of capital expense funded from current revenue as compared to the total operating budget may mean that needs have diminished or needs are being deferred. The latter reason could force the community into crisis, if equipment, vehicles, buildings and other facilities are in constant need of repair or become inadequate for the performance of necessary services.

### Formula:

$$\frac{\text{Capital Outlay From Current Operating Funds}}{\text{Operating Expenditures}}$$

### Data Sources:

- **Capital Outlay from Current Operating Funds:** Municipal accounting records
- **Operating Expenditures:** See Factor 4.

**Warning Signal:** Decreasing Capital Outlay from Operating Funds as a Percentage of Operating Expenditures

### FACTOR 25 - CAPITAL OUTLAY CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Capital Outlay from Current Operating Funds					
2. Total Operating Funds					
3. Capital Outlay from Current Operating Funds as a % of Total Operating Funds (Line 1 divided by Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Capital Outlay from Current Operating Funds					
2. Total Operating Funds					
3. Capital Outlay from Current Operating Funds as a % of Total Operating Funds (Line 1 divided by Line 2)					

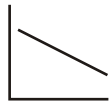
## FACTOR 25 - CAPITAL OUTLAY TRENDS AND ANALYSIS

**Instructions:** List years to be examined across the bottom of the chart and plot the percentage of the budget associated with capital expenditures against the vertical axis.

**Percent**


0

**Years ->**



**Unfavorable Trend** (*Color Code = Red*)

Decline in percentage of vehicle, equipment and other infrastructure expenses or engineering/design of major capital improvements financed from current operating revenues.



**Stable Trend** (*Color Code = Yellow*)

Consistency in the proportion of vehicle, equipment and other infrastructure expenses or engineering/design of major capital improvements financed from current operating revenues.



**Favorable Trend** (*Color Code = Green*)

Increase in percentage of vehicle, equipment and other infrastructure expenses or engineering/design of major capital improvements financed from current operating revenues.



## **FACTOR 25 - CAPITAL OUTLAY ACTION ITEMS**

If the percentage of capital expenses financed from current operating revenues as compared to total operating expenses is diminishing, you should consider the following:

- Are decisions to defer replacement of existing vehicles, equipment and other facilities or the acquisition of new vehicles, equipment or other facilities being deferred to avoid having to generate additional revenues?
- If your municipality is unable to fund the replacement or acquisition of equipment, vehicles, equipment or facilities, would it be beneficial to institute a more aggressive maintenance and repair program to extend the life and utility of existing infrastructure?
- Is the lack of capital outlay due to the municipality's lack of capacity to fund expensive equipment, vehicles, and other infrastructure from one year's budget? Would the development of a capital reserve fund where funds could be accumulated to finance such items be a feasible alternative?
- Or, has the community recently replaced or acquired all necessary equipment, vehicles, facilities and systems and consequently has no current capital needs to fund?

## Factor 26: Fund Balance

### DESCRIPTION

Municipal finance experts consider a balanced budget exists when estimated current revenues are equal to estimated current expenditures. Using cash balances from prior years to fund operating expenditures for subsequent budget years is not considered a sound financial management practice. Frequently, balances are used to avoid tax or fee increases. At some point, cash balances are likely to be exhausted and the municipality will be forced to raise existing tax and/or fee rates or find new sources of revenue to maintain services and programs. Or, without additional revenues, services and programs will have to be reduced or eliminated. When surplus cash exists, it should be allocated as emergency operating reserve funds, used to finance capital improvements or other nonrecurring expenses, pay down debt or to create a capital reserve fund for future capital projects.

### Formula:

(Estimated current operating revenue) minus (estimated current operating expenditures) = Use of cash balance

### Data Source:

- **Estimated current operating revenue, estimated current expenditures and use of cash balance:**  
Annual Operating Budget

**Warning Signal:** Using prior years' cash balance to fund operating expenditures for subsequent years.

### FACTOR 26 – FUND BALANCE CALCULATIONS

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Estimated Revenue					
2. Estimated Expenditures					
3. Use of Cash (Line 1 minus Line 2)					

ANNUAL CALCULATIONS					
Data Item	Year	Year	Year	Year	Year
1. Estimated Revenue					
2. Estimated Expenditures					
3. Use of Cash (Line 1 minus Line 2)					



# Appendix A: Standards for Effective Local Government

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The following standards are drawn from *Standards for Effective Local Government* published in 1989 by the Southwestern Pennsylvania Commission. As noted in the text, they define sound management practices and legislative policies to help a municipality establish and maintain a solid financial condition.

## Financial Management Standards

### FACTOR: THE MUNICIPAL BUDGET/FISCAL PLAN

**Standard No. 7** Revenue projections are realistic—based on solid support data.

**Standard No. 8** Expenditure projections are realistic—based on solid support data.

### FACTOR: MULTIYEAR CAPITAL IMPROVEMENTS PLANNING

**Standard No. 1** The municipality, each year, prepares a multiyear capital improvements plan. This plan identifies each capital project; its anticipated start and completion, the amount to be spent each year and the method of financing the project.

**Standard No. 2** The capital budget, included as part of the annual municipal budget, is drawn from the multiyear capital improvements plan.

**Standard No. 4** Decisions with respect to long-term borrowing or other means of financing are made in accordance with the provisions in the municipality's capital improvements plan.

**Standard No. 5** Detailed schedules of future debt service are presented along with the annual capital budget.

**Standard No. 6** Bond maturity schedules are designed so that they do not exceed the expected life of the projects financed by such bonds.

**Standard No. 7** Funds borrowed for longer than one year are used to finance capital projects, not current operating expenses.

**Standard No. 8** The replacement and maintenance of municipal equipment, vehicles or facilities is in accordance with a formal schedule. This plan is used for capital improvements planning and in preparing the annual operating budget.

### FACTOR: REVENUE COLLECTION

**Standard No. 1** All tax and non-tax revenues are deposited on the day of receipt by the elected real estate tax collector, all Act 511 tax collectors, and/or employees who are responsible for revenue collections.

**Standard No. 2** There are established procedures to ensure that all individuals legally liable for payment of the earned income tax are on the tax rolls.

**Standard No. 5** Interest and penalty charges on taxes and fees comply with law, or are adequate to encourage prompt payment.

**Standard No. 6** The municipality periodically analyzes tax delinquencies and has a program in place to aggressively attempt to collect these delinquent taxes.

**Standard No. 7** Where fees and service charges have been established, they are adequate to recoup all direct and indirect costs of providing the service.

**FACTOR: ACCOUNTING**

**Standard No. 1** The municipality has a formalized accounting system, and the responsibility for the accounting function rests with an individual who has had training in accounting procedures and processes, and who understands Generally Accepted Accounting Principles (GAAP).

**Standard No. 2** The municipality operates on a modified accrual basis of accounting—not a cash basis—for governmental funds, including the general fund, special revenue funds, capital projects funds and debt service funds.

**Standard No. 3** Regular monthly reports of actual revenues and expenditures compared to budgeted amounts are prepared and presented to the governing body each month, with appropriate commentary from the individual who prepared it.

**FACTOR: CASH MANAGEMENT AND INVESTMENT**

**Standard No. 1** The municipality has a cash management plan—it projects and displays both expected revenues and disbursements on a monthly, weekly or daily basis, as appropriate.

**Standard No. 2** All revenue is consolidated for investment purposes.

**Standard No. 3** Investment responsibilities are vested in a single individual within the local government.

**Pennsylvania Department of Community & Economic Development**  
**Governor's Center for Local Government Services**  
Commonwealth Keystone Building  
400 North Street, 4th Floor  
Harrisburg, PA 17120-0225

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DEPARTMENT OF COMMUNITY  
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