Best Practices for Planning and Budgeting

A white paper prepared by PROPHIX Software

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Executive Summary

The continual changes in the business climate constantly challenge companies to find more effective business practices. However, common budgeting limitations are preventing companies from moving forward; they have become so universal and accepted in the marketplace that it is becoming more difficult to move ahead and progress the business. Flexibility, accuracy and control over the budgeting process are three prominent factors slowing this progression.

Three elements finance professionals most want to change:

- *"time it takes to collect data"*
- *"data gathering tools"*
- *"process by which data is collected"*

—John Cummings
Business Finance, February 2005

Many finance professionals want to grasp the big picture of the company's position by having the flexibility to evaluate and understand the effect of various factors. They want the ability to review previous years' budgets, add/remove accounts or change budgeting assumptions with ease. However, with the lack of flexibility in their current tools, the depth of understanding and awareness are very limited.

Data integrity and control issues are also very common challenges that companies report during the budgeting process. The whole budgeting process can become very difficult to manage and various stakeholders begin to lack data ownership and confidence. Finance professionals begin to consume too much valuable time dealing with the gaps and errors in the data.

Yes, budgeting is a necessary evil that, if done improperly, can bring distress and anguish throughout the company. Yet, by resolving these issues, companies truly can gain a tangible competitive advantage by effectively budgeting and optimizing the use of their resources. With a comprehensive view of financial and non-financial data, you are able to make better, more informed decisions; you can accurately understand the true cost of your products and services and the budgeting process becomes much more efficient—ultimately leading to more time for advanced analysis and improved teamwork and data ownership.

Attainable & Measurable Best Practices

This white paper focuses on best practices that will enable companies to transform the planning cycle into an evolutionary process, bringing tangible and intangible returns for the organization and leadership back into the finance department.

You can improve business management through the application and adherence of budgeting and planning best practices. Read on to learn the twelve best practices that have been adopted by leading companies.

"The focus is now on the quality of information and the company's ability to analyze it."

—Peter Krass
CFO IT, September 15, 2003

1. Identify the Infrastructure Supporting the Budgeting Process

Understanding the components that support your budget plan is crucial for effective budgeting. From employees and knowledge to processes and technology, know how these components affect the business. Begin by correctly accessing employees' skill levels and assign tasks and responsibilities accordingly. Employees who are trained (and cross-trained) in the appropriate tasks offer greater stability to the company and to items in the budget plan.

Once the individuals have been assigned tasks and responsibilities, the next crucial step is providing the correct tools and processes for them to complete these successfully. Subsequently, by ensuring the budgeting process has been well documented and communicated, the tool will allow flexibility and control throughout the process.

With the right resource allocation, knowledge transfer increases and dependability on key personnel decreases. Companies following this best practice are given more time to focus on the analysis of pertinent information rather than managing the process.

2. Define a Budgeting Process

"More than half of corporate financial officers say their biggest challenge in preparing accurate forecasts is the amount of time it takes to collect appropriate data, according to an Accenture survey of 200 finance, treasury and cash management executives in the United States and the United Kingdom."

—John Cummings,
Business Finance, February 2005

Budgeting processes are used to help ensure the flow between planning phases and identifying the most efficient procedures.

Avoid the temptation to skip creating a well thought-out budgeting process. It is essential for laying the groundwork for a successful and efficient budget cycle. To begin, identify the project using tools such as a needs analysis and project management consultants. For an effective budget process, the following should be clearly defined:

With a comprehensive understanding of the budget, companies are able to make better, more informed decisions and can accurately recognize the true cost of products and services. An efficient budgeting process provides more time for analysis and improves the ability to react quickly to change.

Please see Appendix A for a budgeting process illustration.

3. Choose a Dedicated Planning and Budgeting Software

Companies often seek software applications to increase the efficiency, accuracy, and consistency of the planning, budgeting, and reporting process. Today's applications make it easier to perform tasks that are difficult or impossible

"Seventy-three percent of the respondents indicated that they were using Excel spreadsheets. Now, two years later, 69 percent of survey participants still say that they use the same software."

—Tad Leahy, Business Finance, August 2005

without the use of technology. As a best practice, invest in a package that not only becomes part of the Business Performance Management/Corporate Performance Management process but also automates the process and adds a Business Intelligence component to finance.

Packages such as PROPHIX, Hyperion, Proclarity, and OutlookSoft offer this solution. Thoroughly research various options and choose software that best meets the company's needs. Speak to management consultants, attend user conferences, and review software life cycle models to understand all options. The key is to have a technology that works for the company and supports your current and future requirements.

4. Establish and Define the Correct Budget Level

Providing too much detail in the budget can be as inefficient as supplying too little. The time spent on focusing on details that do not influence the plan can be better spent elsewhere. Only supply detail that is significant to the budget. For example, is it necessary to plan a budget for paperclips or is a general budget for office expenses sufficient? Alternatively, perhaps a budget for total expenses is adequate. Remember that the budget does not need to reflect the actuals (i.e. general ledger). Budgets are meant to draw attention to significant variances so they can be investigated through actuals and by other means.

With the correct level of detail in the budget, all accessible data is relevant. This decreases the time required for budgeting and reviewing. Ultimately, a successful budget plan provides enough detail for budgeting assumptions and decisions and still offers the flexibility to adjust business finances as needed.

5. Define Key Performance Metrics (Indicators)

Key Performance Indicators (KPIs) are financial and non-financial metrics used to quantify objectives to reflect the strategic performance of an organization. KPIs give a greater understanding of key business drivers, which ultimately allows for effective time and monetary investments. They gauge and help control the present state of the business.

"Simplify their existing process and focus on the few key performance indicators that are the most important and dynamic to their business"

—Tad Leahy, Business Finance, August 2005

Depending on the industry your organization is operating in, industry-specific KPIs could be researched through industry trend reports or annual reports of peer companies. Every industry will have unique measurements for determining the financial health of an organization. Examples of commonly used KPIs are revenue growth, earnings growth, debt reduction, and EBITDA margin.

As a best practice, limit the KPIs to only those factors that are crucial to the organization reaching its goals. They must reflect the organization's goals, must be key to its success, and must be measurable. A good KPI includes the definition, the measurement (how the KPI is measured), and the target goal. Once KPIs have been defined, they must be clearly communicated across the organization. With all departments relying on the same benchmarks, the company improves internal inefficiencies and clarifies goals.

6. Make Planning and Budgeting a Collaborative Process

To gain a greater understanding of the planning and budgeting processes, involve resources across all levels of the organization—have reviewers provide the direction, managers validate the details, and budgeters gather the information. For example, for a budget approval process model, executives need to decide on a business strategy, management needs to implement the plan, and budgeters need to provide the necessary data.

A collaborative process offers greater accountability and a better execution of corporate strategy. To achieve this, use managerial meetings, feedback forums, and surveys as tools.

7. Align Operating Tasks with Strategic Planning

"For a budget to be effective, it should mesh smoothly with a company's strategic plan. However, the 2005 survey shows most organizations have not been able to closely integrate the budgeting process with scorecards and metrics management. Overall, only 15 percent say these elements are closely integrated."

—Tad Leahy,
Business Finance, August 2005

It is important that day-to-day operations support the high-level corporate plan to ensure that planning efforts are cohesive throughout all departmental levels of the organization. Many successful companies support this best practice by extending the corporate strategic plan from top management to the rest of the company. For example, once upper management sets strategic goals, Finance translates the goals into specific departmental plans, expense drivers, and linked incentives. Departmental managers subsequently use these specifics to operate the business.

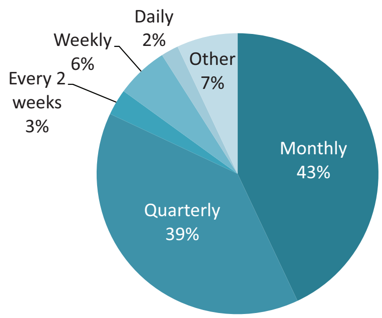
Tracking, measuring, and documenting are the next steps in maintaining the success of operations and strategic goals. With the alignment of operating tasks and the strategic plan, the detection and adjustment phase becomes more efficient, and companies gain the competitive advantage of achieving clear corporate objectives.

8. Align Resource Allocations with Objectives and Strategy

In every company, each function requires resources—some experiencing shortages and others in excess. To avoid wasted resources and misinformed decisions, identify, prioritize, and invest in projects that align with corporate strategy. By clearly defining strategies, risks, and opportunities, companies can better invest in projects that will produce desired outcomes.

Before allocating resources, leading companies define objectives and strategies, and identify key performance metrics that align with the corporate plan. The use of BI (Business Intelligence) tools helps management identify risks and

Ideally, how often would you like to reforecast?



—Tad Leahy, Business Finance, August 2005

opportunities and allows for the proper allocation of resources to projects that support key objectives. Dashboarding, scorecarding, and what-if scenarios help monitor results, which is essential to the success of the allocation efforts.

This practice focuses on corrective actions and investigation that allows companies to refine and improve processes. With a close alignment of resource allocations and objectives, productivity and accuracy increases, benefiting the overall health of the organization.

9. Be Timely and Precise

Many companies struggle with time-consuming planning processes. Some planning cycles take up to six months, which results in irrelevant data by the time the plan is operational. With a clear definition of KPIs, the project plan, and the timeline, planning cycles can be prepared within two months. For example, a company adhering to an agenda can complete the planning cycle in five weeks:

Week 1: Define corporate and operational goals, as well KPIs, and link to incentives

Week 2: Communicate planning process to company and accept feedback

Week 3: Complete first pass of budget

Week 4: Complete second pass of budget

Week 5: Finalize budget and communicate to departments

Because of a shorter cycle, data is kept up-to-date and relevant. By applying best practices and leveraging technology, leading companies have been able to create planning cycles quickly, allowing for sufficient time and resources to meet objectives.

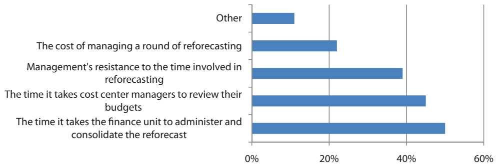
10. Manage the Ever-Changing Market Conditions

Leading companies use planning processes that can quickly adapt to external conditions. This decreases the amount required for analysis and increases the merit of the data. Businesses perform more efficiently with the ability to respond to the business climate, to consolidate plan data, and to analyze information, all in a timely manner. Key practices to develop flexible processes include the use of monthly re-forecasting, rolling forecasts, and what-if analyses.

Monthly Re-forecasting. The flexibility to re-forecast and revise processes is important, especially in today's market conditions. Frequent re-forecasting continually gages company performance to crucial aspects, such as the market, budget plan, and business competitors.

Rolling Forecasts. What better way to manage your plan than to reflect the continuous business outlook. This type of forecast acknowledges that companies

What is the most significant barrier to generating more frequent re-forecasats in your organization?



—Tad Leahy,
Business Finance, August 2005

function as an ongoing operation. By utilizing rolling forecasts, businesses gain a forward-looking plan that allows management to take remedial action on unexpected changes.

What-if Analyses. Having the ability to input several assumptions and to create numerous scenarios is often overlooked due to the misconception that more time and effort is required. Companies are able to gain more insight on multiple variables, allowing for better decision making. Trends are easier to spot when data is up-to-date, thorough and readily available.

Managing market conditions is the foundation for making better decisions. More informed decisions are possible in all areas, such as cash flow situations, price changes, product line changes, capital allocations, and organizational changes.

11. Support the Project

Once the budget has been approved, support and maintenance is necessary to keep the project successful. Become a visible sponsor of the project by adhering to the plan and communicating ideas to the rest of the organization. E-mails, newsletters, and open forums are a few methods used to share information.

Providing a supportive and open environment also reduces the chance of failure. The following practices encourage such an environment:

- Create a feedback loop.
- Allow recover time.
- Implement a testing phase.
- Solve problems.

12. Implement Incentives

Many companies use incentives to encourage productivity and support. However, incentives are often tied to targets rather than the objectives. Meeting budget targets should be a secondary goal to meeting other measures. Allow department managers to produce their own goals and offer reward packages to those who meet them.

By giving managers the responsibility, the importance of the company's planning process becomes relevant to all parts of the organization. Objectives and operating strategies become better aligned. Executing such a practice is as simple as identifying the correct measures and encouraging achievements. When the planning process becomes part of the corporate culture, companies will excel in business management as well as financial management.

"Other challenges for improving the budgeting process include making major changes to existing processes and gaining employees' acceptance of the new budgeting system."

—Tad Leahy, Business Finance, August 2005

Obstacles to Adopting Best Practices

Best practices are management ideas that help outline a more effective method and/or process to deliver a particular outcome. The best practices described in this paper will provide companies with a more accurate forward-looking view of their business. Budgeting and planning practices help to ensure that an organization's goals are being met, while identifying any inefficiency within the process.

Although budgeting and planning are important, it is often overlooked because of the difficulties usually faced within the corporate infrastructure of the organization. The tools, people and processes inherent in the budgeting process need to be fully engaged in order to achieve a comprehensive understanding of the direction of the company.

The tool that many companies are still using to manage the planning process is spreadsheets. Although spreadsheets do provide an excellent tool for quickly manipulating data and adjusting information, they are truly meant for individual analysis. Spreadsheets do not provide a comprehensive, collaborative tool that will allow successful implementation of best practices.

The next key obstacle is your stakeholders. Your employees and outside peers need to have a full understanding and appreciation for the best practices you are trying to implement. These practices need to be communicated to them; they need to know why they should care about these changes and how it will directly affect them.

With the ability to overcome these issues and implement best practices, companies are able to plan more efficiently and project more frequently. With frequent plans, companies are able to gain more insight on multiple variables, allowing for better decision making. Trends are easier to spot when data is up-to-date, thorough and readily available, and a company can truly succeed in their marketplace.

The following are reported benefits to adopting budgeting and planning best practices:

- Automation and reduction in errors
- Ownership and accountability brought back to the process
- Control over the information processes
- Faster and more reliable monthly closes and consolidations
- Better communication throughout the company
- Increased satisfaction from upper management with financial outcomes
- Detailed, advanced analysis in a user-friendly end-to-end package
- Strategy alignment within departments and company as a whole

The PROPHIX Software Solution

For over fifteen years, PROPHIX has been a leader in delivering data analysis solutions including budgeting, reporting, forecasting, planning, consolidation and personnel planning. PROPHIX maintains an outstanding reputation with its customers by consistently delivering tangible value and exceptional ROI, with a low total cost of ownership.

At PROPHIX, our priority is to understand your goals and objectives. It is critical to translate those strategic objectives into operational plans. As business people with accounting designations, we understand the challenges you're facing. Decision making is at the heart of management's responsibilities, and this is only possible with timely and accurate data. At PROPHIX, we're exclusively in the business of delivering data to improve an organization's decision-making ability. It doesn't end when the software is installed, it just begins.

For more information on PROPHIX Software, call 1-800-387-5915 or visit www.prophix.com.

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Appendix A – Budgeting Process: Reaching the TIPPING Point

The TIPPING Point is the completion of your budget, your budget adjustments and the balancing of your budget data—the exact point where advancing your budgeting process can take place. By investing in your information infrastructure and by establishing a five-stage budgeting process, Setting Goals & Objectives, Planning & Preparation, Manipulating Budget Data, Finalizing Budget & Adjustments, Monitoring Results & Measuring Success, the TIPPING Point can be reached. Investing in your information and creating a data repository will bring a superior return on your information. By forecasting your information, conducting what-if analysis, creating management-style reports, dashboarding, and performing sales analysis, a more accurate and concise forward-looking view of your business will be created.