Smart approaches to top-level decision making

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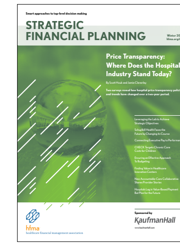

// planning insights //

Ensuring an Effective Approach to Budgeting

By Jeff Goldstein and Jay Spence

Organizations first should perform assessments of their current budget processes to better understand potential shortcomings.

Nearly every healthcare provider is working to reduce or manage costs without impacting continuous improvement of care quality. Cost management requires having an accurate budget to measure against to ensure that cost reductions are sustained over time. With a rapidly changing healthcare environment and the fact that the budgeting process can be lengthy and require multiple iterations, organizations risk spending significant time and effort to produce budgets that are inaccurate by the time the new fiscal year starts.

With the proper process, tools, and feedback mechanisms, however, budgeting can be accurate and provide a solid mechanism for ensuring accountability. To enact effective change, organizations first should do an introspective assessment of their current processes to better understand the potential shortcomings. While no two budgeting processes are the same, they often follow similar patterns. Three common approaches are described next.

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Type 1: Finance as 'Wish Takers'

Organizations in this category do not have strict processes for reviewing monthly budget variances. In most cases, finance owns the budget process but does not have buy in or accountability from department managers. Managers essentially share a "wish list" as their proposed budget, and there often are major gaps between that input and financial targets. The budget process involves significant negotiations to reconcile manager requests and annual targets.

Budgeting is a four- to six-month process, with no correlation to long-range planning, which runs as a separate process.

Type 2: Finance as 'Scorekeepers'

For organizations in this category, budgets are formalized at the finance level using run rates from the prior year. Managers have little ownership or buy in. The result is a finance-owned budget that feeds into monthly variance processes that do not enact needed monthly spending changes.

Budgeting typically is a three- to four-month process. There may be a link between budget and long-range planning goals because both are owned by the same finance team, but those links do not produce more accurate or shortened processes.

Type 3: Finance as 'Advisers'

This category provides the most efficient and effective approach. Here, organizations have strict monthly budget variance review processes, and managers are accountable for hitting their budget targets each month. Requests to add new FTEs or to change productivity standards must be reviewed by an FTE approval committee and require supporting data in the form of financial analysis and regulatory or other operational reasoning. The budget and long-range financial planning processes are in sync and are run as integrated processes, and the gap between budget target financial goals and manager input is minimal. Current-year overspending is not rewarded, and budgeting is typically a two-month process.

Optimizing Budget Processes

As illustrated in this third category, intrinsic links should exist between organizations' long-range financial plans and their budgets. Essentially, budgets should flow directly from the upcoming year's long-range plans, making budgets the "last step" in annual planning processes. Budget processes simply become allocation exercises to match resources to financial targets established in annual financial plans.

Cycle times to produce budgets are significantly reduced as a result, allowing organizations to start with more months of actual data and minimize the time spent negotiating manager requests. The following practices can improve the accuracy and efficiency of budgeting processes.

Start with eight months of actual data. Shortening budget cycles in this way forces discussions about cost cutting to occur more efficiently, leading to more timely decision making and less negotiating.

Limit input time for managers to two weeks. By limiting the amount of time that managers have to input their budget requests, organizations allow more time for critical budget review. It helps to start input times mid-week—ideally on Wednesdays—so that the two-week budget input cycles span three calendar weeks.

Compare financial plans to proposed budgets to identify gaps. The outcomes of financial planning processes form the guidelines and goals for budget processes. Running monthly variance reports helps to identify any spending gaps and develop action plans as needed to close those gaps.

Establish a monthly variance review. If not in place already, a monthly cadence for budget variance review sessions should be established. These meetings require managers to review any variances for their departments, thus ensuring accountability to their peers and to executive management.

The "finance as adviser" approach facilitates meaningful conversations throughout the year and reduces the likelihood that spending will rise above budget targets. Engraining this behavior change allows managers to have ownership of budget outcomes, because they are working as partners with finance to achieve targets. //

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