BUDGETING WORST PRACTICES
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Managing Expectations

N. Dean Meyer

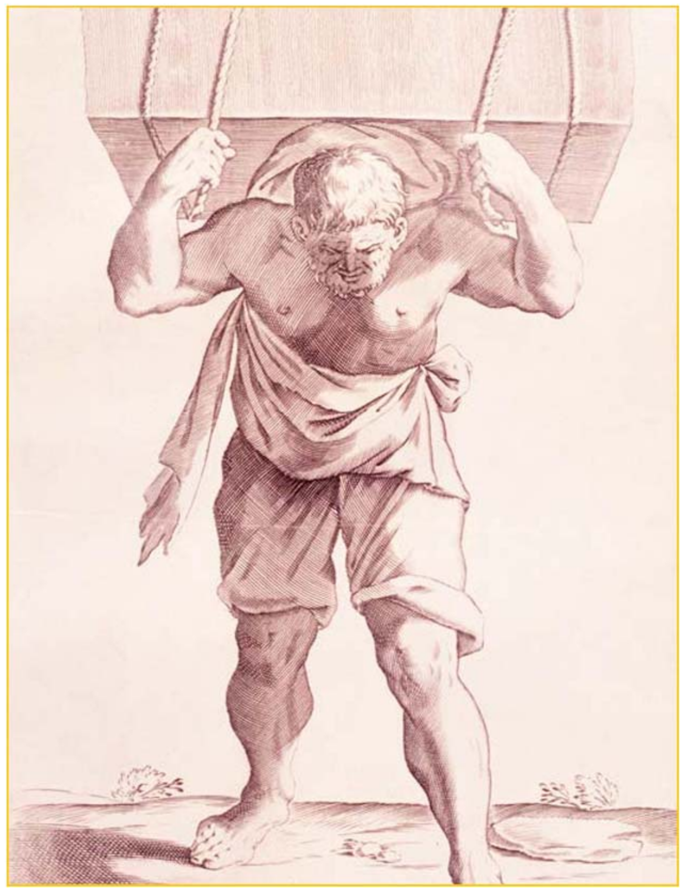
"Honey, come here. Sit down. We gotta' talk."

"What did I do now?"

"You've been home for two hours. And you've done nothing but knock around the house like a billiard ball. You rushed through your dinner like a robot. You've hardly heard a word I've said. What's going on?"

"Oh, you're right. I'm sorry, sweetheart. It's just that... well, my people are really hurting."

"How so?"



"They're under extreme pressure on projects. Plus, they've got all these little change requests stacking up. They're working 60 or 70 hour weeks, and I'm afraid they're going to burn out. Not only that, we're postponing all our training and product R&D activities, which isn't good for the long term. We're starting to lose some of our best people. And we're getting bad press for delivering things late, for cutting corners, for being unresponsive, and for not even having time to answer clients' voice messages."

"How'd you get into this situation in the first place?"

"We just don't have enough resources to satisfy all the demands on us."

"Why don't you have enough resources?"

"Well, I guess the story goes back to months ago. I submitted a budget for the resources we need. But then they had to do some cutting. They killed a few big projects. Then, they cut my training and travel to near nothing. And finally, they made me go back and cut the total some more."

"And why is that a reason not to notice that I made your favorite, Beef Wellington?"

"Well, now we're paying the piper. I've got fewer resources. But that doesn't mean that clients expect less."

"What? That's ridiculous! They give you less money, so you do less. That's pretty obvious, isn't it?"

"To you, it is. But for some reason, it's not so obvious to our executive team. Now that the total's fixed, they're going to go on demanding everything that was in the original budget, and everything they got last year. And my reputation gets trashed when we can't do everything they want. I guess I've done a lousy job of managing expectations."

"Why don't you just show them what's covered in your budget, and what's not. If they make the number smaller, you have to tell them what they're not going to get."

"Hmmm.... Figure out what's in the budget, and what exactly we're not going to be able to do without incremental funding? I wish we knew how to do that…."

"Why is that so hard?"

"Well, a given project or service is delivered by a team of people, so it represents a small piece of the costs of a bunch of different groups. Then, there are all those internal support groups that we need, but we can't tie to specific projects and services. And we have fixed costs that won't go down if they cancel one or two services. Plus, we have overhead, like me. It's pretty complicated."

"But if you could?"

"It would be great. At a minimum, I'd be able to negotiate expectations that I can deliver on. And maybe after they see what's not funded, the business units might even kick in more budget."

"Then you just have to figure out how to re-do your budget that way."

"You know, you're right; we will. Oh, and sweetie, thanks for the Beef Wellington."

"You noticed!"

"Um, not really."

The Root of the Problem

When budgets are presented by cost center, with line items like compensation, travel, and training, then it's impossible to tie budgets to results, to benefits, to ROI.

Without knowing the payoff of these costs, executives are forced to pick at cost factors (your training budget) and to make arbitrary budget decisions, like "last year minus five percent."

Meanwhile, clients don't know what's funded and what's not. They're likely to say, "Hey, you got your budget. Now it's your job to deliver on all my requirements."

Of course, this is an impossible situation. You can't deliver infinite service for a fixed price. But you have no basis for saying to a demanding client, "Great idea. We'd love to do it. But it wasn't covered in our core budget, so let's you and I go look for incremental funding." Nobody knows what is and isn't covered by your budget.

The Way Out

The antidote is obvious: a budget for products and service—for *deliverables*, not for cost centers and general-ledger accounts.

This is termed an "investment-based budget."

When budgets are built and negotiated this way, the budget process becomes a rational, fact-based discussion of what the corporation can and cannot afford.

But if it's too late for that, a leadership team can "reverse engineer" the current budget that it was given. By re-casting the budget into the costs of deliverables, it will become apparent that clients' appetites exceed the enterprise's available resources.

Then, business leaders will have to make tough priority decisions and decide what projects and services they'll do without or fund in other ways.

And later, after learning the method while reverse engineering this year's budget, your leadership team will be ready to prepare the following year's budget with a new approach.

Practicalities

Investment-based budgeting is simple in concept, but "the devil's in the details."

Each group must clearly identify its products and services – its catalog. Then, each group must do a demand forecast – who will buy what of that catalog. At this step, the efforts of all contributors to each project team have to be linked.

Indirect costs must be apportioned to these deliverables. And across all groups, overhead costs must be spread in just the right proportions.

While this may seem daunting, it is, in fact, quite feasible. It just requires the right tools, a clear step-by-step process, and supporting documentation with definitions and guidelines.

In other words, it's entirely within your power to manage expectations, while remaining customer focused and responsive to the business. ❒

For a library of information and case studies on investment-based budgeting, the method, and the tool, go to fullcost.com. *And CIOs interested in a private sounding board on their resource-governance processes may enjoy a private consultation with Dean Meyer. Contact NDMA at 203-790-1100, or* info@ndma.com.