

# The Movement Towards Priority- Base Budgeting: Whatever Happened to Zero- Base Budgeting?



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# **THE MOVEMENT TOWARDS PRIORITY-BASE BUDGETING:**

## **Whatever happened to Zero-Base Budgeting?**

### **Introduction**

The local government budget process is evolving into its own art form. Gone are the days of the three to five-month budget cycle for local and municipal governments. The latest economic downturn has citizens requesting more and more transparency and elected officials leading the charge for themselves as a governing body to focus more on the trees instead of the forest. For the City of Plano, our budget process has evolved over the years from a Line-Item Budget (LIB) to a Target-Base Budget (TBB) and is now moving towards a Priority-Base Budget (PBB). However, in recent months, several elected officials have called for the implementation of a Zero-Base Budget (ZBB), a budget process established in the 1970's in order to solve the city's growing budget deficit.

This paper will highlight, contrast and review several different budget methodologies including zero-base, target-base and priority-base budgets and provide an overview of the City of Plano's budget & strategic planning process. In addition, I will provide information regarding what approaches cities are using nationwide in order to deal with the economic downturn and then will provide alternatives for elected officials on how to move the City of Plano's budget process to the next level.

## Zero-Base Budget

As mentioned above, the City of Plano has had several city council members request the implementation of a zero-base budget process. *What is zero-base budgeting?* Zero-base budgeting (ZBB), in its original form, is a system of budgeting that begins every budget cycle at zero, rejecting any assumption that the activities that were funded in the last budget will continue in the coming one. It requires a rationale for each activity that will be funded for the new budget.<sup>1</sup> Peter A. Pyhrr developed the zero-base budget process in 1969 at Texas Instruments as a tool for planning, budgeting and control. He published an article about his budget experiences with divisions of Texas Instruments that caught the attention of Jimmy Carter who was then Governor of the State of Georgia. Jimmy Carter was so impressed with the budget system that he even had it implemented at the federal level in 1979. The system, however, did not continue for long and its formal application was stopped within a couple of years.<sup>2</sup> During this time, many state and local governments did try to implement the ZBB budget system, however, most ended the implementation of the system due to the major complaint filed that it generated too much paperwork and there was too little time to examine the paperwork it did generate.

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<sup>1</sup> Snell, Ron, NCSL, *Zero-Base Budgeting in the States*. Document from National Conference of State Legislatures, 2010.

<sup>2</sup> Handa, Prof. K.L. *Zero-Base Budgeting*. [cgda.nic.in/rt/rctblr/.../Zero-based%20Budgeting.htm](http://cgda.nic.in/rt/rctblr/.../Zero-based%20Budgeting.htm)

### **Why is the zero-base budget system so time consuming?**

The intent of zero-base budgeting is to force a rational and comprehensive re-examination of the way in which services are provided. Zero-base budgeting requires decision packages to be developed for each program, service and/or business that is offered by the government. The decision packages usually represent various tiers of funding and or service levels ranging from increasing or decreasing service levels or maintaining the same service level. Central budget authorities (e.g., city council, mayor, city manager) usually rank the decision packages and funding is allocated accordingly. At the City of Plano, we have 23 departments and have identified 449 programs or core businesses through our core business matrix process. Under the ZBB process, each program would be required to develop three different decision packages based on service levels and funding of each package. This illustration translates into 1,347 decision packages would require review and analysis. The decision packages would be required to answer the following questions:

1. What is the purpose and justification of the program?
2. Need to provide a description of the program?
3. What service level is the program currently operating?
4. What would be the benefit of funding the program? What are the consequences of not funding the program?
5. Are the goals and objectives of the program important enough to warrant the expenditure?
6. What are the alternative ways to provide the program or service?
7. Is there any measurable evidence of the value of the program under review?

8. What are the resources required to fund the program?
9. What are we getting for the resources we are providing?
10. What priority number is the program assigned?

You can imagine how much time it would take a department head to prepare a budget for each individual decision package. Department heads may view ZBB as additional paperwork having little substance at best, or as a central executive device, which may curtail their departments at worst. One goal of ZBB is to produce more information for the chief executive about the programmatic impact of increments or decrements to a department's budget.<sup>3</sup> In the end, governments need to analyze whether the time and effort to prepare a ZBB is truly going to yield any results other than their current budget process. The essence of ZBB requires that programs be re-justified over and over again so that the traditional base budget, which received little attention, is scrutinized by the governing body every year. However, is it really worth the time and effort to re-scrutinize the police and fire departments budget every year? Are citizens really willing to decrease services in these areas?

### **Target-Base Budget**

The target-base budget (TBB) is a derivative of the zero-base budget (ZBB) process. Target-base budgeting does not attempt to comprehensively re-examine base spending. Each decision unit (e.g., department, cost center, division) is given a target-

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<sup>3</sup> Moore, Perry, Wright State University. 1980. Zero Based Budgeting in America Cities. *Public Administration Review*. May/June 1980 – Perry Moore, Wright State University. p. 253-258

spending amount and is requested to submit a budget for that amount. The decision unit may submit above the target amount with a decision package. The significant difference from ZBB is that there are no decision packages for cutback spending levels. Rather scrutiny is focused on the single target budget and decision packages are formed for additional spending. Decision packages are ranked, according to alignment with goals and objectives by the department submitting the package as well as the central budget authority. Based on these rankings, some decision packages maybe added to the target amount and submitted to the board as a recommended budget. TBB places a higher premium amount on revenue projections than ZBB because available revenues are used to determine the target budget as well as to fund decision packages. TBB also provides a clear target for managers on how to design their budget requests. TBB has emerged as a less paper intensive budget approach with the same results as ZBB over the past two decades.

### **Priority-Base Budget**

The priority-base budget (PBB) process allows the municipality to identify its most important strategic priorities, rank services according to how well they align with the priorities, and allocate resources according to the ranking. “Budgeting for Outcomes” is the most well known variant of the priority-base budget. The PBB process consists of the following steps:

1. Identify available resources – Clearly identify the level of resources that are available to fund the next year’s budget as well as one-time expenditures and capital projects.

2. Identify your priorities – What are the priorities your governing body have set out in their strategic plan.
3. Define your priorities – Define why the organization exists.
4. Prepare decision units for evaluation – Evaluate the services against the priority results.
5. Score programs against results – Develop a process by which it can objectively evaluate how the program can achieve or influence the priority results.
6. Compare scores between programs – Information is compiled in order to view a top-to-bottom comparison of prioritized programs.
7. Allocate resources – Once the scoring is in place, resources can be allocated to the programs.
8. Create accountability – Establish standards of evidence against which the performance of the programs will be judged.

One of the advantages to implementing a priority-base budget system is that it aligns the budget with the government's most strategic priorities. However, the government must have their strategic plan in place in order to implement and most do not. Prioritizing helps a jurisdiction better articulate why its programs exist, what value they offer citizens, how they benefit the community, what price we pay for them, and what objectives and citizens demands they are achieving. PBB is about directing resources to those programs that create the greatest value for the public.<sup>4</sup> This is a primary difference between ZBB and PBB; ZBB focuses on preparing a budget from the ground up with no attention to the strategic plan.

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<sup>4</sup> Kavanaugh, Shayne C., Jon Johnson, and Chris Fabian. Anatomy of a Priority-Based Budget Process; *Government Finance Review April 2010*. P. 8-16

## **The City of Plano's Budget Process**

When asked the question, what budget methodology would you say best describes your city's budget process, most municipalities will report a combination of all of them. At the City of Plano, our budget process has evolved from a line-item budget process in the 70's and mid-80's, to a target-base budget process from the late 80's thru mid 2000's, to a combination target-base and priority-base process starting in 2008 to today. What brought about the changes to cause the evolution to the budget process we use today? Many factors contributed to the evolution including technological innovations, implementation of forecasting and revenue models, shifting to a strategic focus, growth in the population of the city and its revenues and an excellent management team.

The budget process of today scarcely resembles the budget process of three decades ago which included using a pencil and a green ledger pad to prepare the budget. Today's budget process actually begins in June of each year when the prior year's budget is still underway. In June, a city council retreat, lead by an outside consultant is conducted. At the retreat, the citywide goals for the next five years (2010-2015) are developed along with an action plan for the next fiscal year (2010-11). The goals developed at the June 2010 retreat were:

1. Financially strong city with service excellence
2. Safe large city
3. Strong local economy
4. Great neighborhoods – 1<sup>st</sup> choice to live
5. Exciting urban centers – Destination for residents and guests
6. Partnering for community benefit

These goals are then set in motion in the budget process with the development of our core business matrix. The core business matrix is a tool that simply ties programs and/or businesses offered by the City of Plano back to our strategic plan in order for organizational decisions to be made regarding service delivery, how we value our services, and divesting lower priority services by council, management and citizens. The core business matrix process begins after the adoption of the annual budget in September. Departments are requested to update their matrix by assigning which strategic goals their programs and/or businesses relate. Departments also update associated revenues and expenditures for each program and determine how many full-time equivalents it takes to administer the program. Each program is assigned a service hierarchy descriptor.<sup>5</sup> The following descriptors are used:

***Core Business – “No Choice”***

Program must be legally mandated. If we did not provide the service, we would be fined or go to jail.

*Examples: Public Records, Clean Water Act, Storm water*

***Core Business – “Choice”***

Core services are necessary for daily living. If we did not provide these services, we would not have a city. They are necessary for daily living.

*Examples: Fire, Police, Traffic Safety, Streets, Water, Code Enforcement*

***Quality of Life***

Distinguishes our city from other cities. It is what makes our city unique from the others. Enhances and protects assets.

*Examples: Dog Park, Rental Inspection Program, Rec Centers, Day Labor Centers*

***Community “Add On’s”***

Community identity, pride, distinguishes cities from counties.

Community add on’s are events that have crept into the services.

*Example: The Arts Center because both Dallas and Richardson have one. July 4<sup>th</sup> is a Quality of Life, Blackland Prairie Festival is an Add On.*

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<sup>5</sup> Lyle Sumeck & Associates, Service Hierarchy, Copyright 2008

After the matrix is complete, each department prioritizes its programs. Illustrated below is an example of the Planning Department’s Core Business Matrix.

Core Business	Program/Description	Annual Cost	Funding Source	Annual Revenues	FTE's	Priority
<b>PROTECT PUBLIC SAFETY, HANDLE EMERGENCIES</b>						
Quality of Life	<b>Buffington Community Services Grant Program:</b> Provide City funds at \$2 per capita to support social service agencies who assist citizens in need. Funding is directed to agencies that provide emergency services.	\$ 554,009	General Fund: \$520,400 Grants \$33,609 Administration	\$ -	0.37	6
<b>FACILITATE, STIMULATE AND INITIATE FUTURE DEVELOPMENT AND REDEVELOPMENT</b>						
Choice	<b>Development Review:</b> Manage the City's residential and commercial development and redevelopment using the Zoning and Subdivision Ordinances and other rules/regulations.	\$ 907,549	General Fund	\$ 192,704	12.37	1
Choice	<b>Geographic Information Systems/Mapping (GIS):</b> Provide maps and information through GIS for the City's 9-1-1 system, solid waste truck routes, crime prevention program, and other planning activities.	\$ 1,247,074	General Fund \$940,673 Water & Sewer \$222,636 Municipal Drainage \$83,765		12.08	2
Choice	<b>Long-Range Planning:</b> Plan for the City's future growth by maintaining and implementing the Comprehensive Plan and related long-range planning studies and by tracking demographic changes.	\$ 431,366	General Fund		4.30	3
Choice	<b>CDBG and HOME Grant Programs:</b> Prevent neighborhoods from deteriorating and support social service agencies who assist citizens in need using federal grant funds. Majority of funds are used to rehabilitate housing for low- and moderate-income homeowners and assist with down-payment and closing costs for qualifying first time buyers. Up to 15% of the funds are granted to community social service agencies.	\$ 2,068,821	Grant Fund \$1,819,163 General Fund \$249,658	\$ 1,819,163	8.08	4
Choice	<b>Heritage Preservation:</b> Oversee the City's historic preservation program and historic districts, including the City's grant program for historic preservation agencies.	\$ 780,574	General Fund \$102,864 Convention/Tourism Fund \$677,710	\$ 677,710	1.37	5
Quality of Life	<b>Day Labor Center:</b> Operation of the City's Day Labor Center, where contractors and homeowners can hire daily workers in a safe and orderly manner.	\$ 218,391	General Fund	\$ 26,210	3.23	7
Quality of Life	<b>Community Building:</b> Provide support and education for residents in older parts of the City through the neighborhood planning program to address neighborhood decline.	\$ 159,381	General Fund		1.17	8
Quality of Life	<b>Downtown Plano:</b> Coordinate programs to promote the revitalization of Downtown Plano and provide assistance to area merchants, property owners and developers.	\$ 165,193	General Fund		1.03	9
<b>TOTAL \$</b>		<b>6,532,358</b>		<b>\$ 2,715,787</b>	<b>44.00</b>	

The city council reviews each core business matrix at a retreat scheduled in the fall. Both priority assignments and service hierarchy are discussed for each core business. Department heads discuss service level impact and justification of programs at the retreat. Based on discussions with the city council, the city manager and departments prepare a list of recommended reductions or increased revenue sources that can be utilized in case of a budget deficit. Our three-year financial forecast is delivered to

the city council in March. For the last three years, we have projected double-digit deficits. If required, a second city council core business matrix retreat is scheduled in April to review and make comments on further budget reductions. Budget reductions are incorporated into the budget process via supplements and are reviewed again for inclusion in the recommended budget by the city manager in June and the city council in August. These reductions are posted on the internet and several public hearings are held for public comment on the recommended budget, the core business matrix and associated budget reductions. Once the budget is adopted, the whole process begins again.

### **Accomplishments - Current Budget Process**

The City of Plano has eliminated over 30% of the general fund's operating budget utilizing our core business matrix process since 2008. This translates into eliminating \$33.2 million in expenditure reductions including the elimination of (129) full-time positions and (17) part-time positions from the general fund budget plus increasing fees for services of \$2.1 million. Our process has eliminated the need for across-the-board cuts. Reductions are based on service level impact by program/business with focus on lower priority services. In addition, the City of Plano passed its first tax rate increase of 1.51 cents from 47.35 cents to 48.86 cents per \$100 of assessed property valuation since 1990 with the exclusion of the two-cents added for economic development purposes. The tax rate increase was primarily due to the city council's involvement in the core business matrix process.

The city council, citizens and the media love the transparency of the core business matrix. The document contains program identification, justification for each program, allocation of costs and revenues and provides the priority level for each program. In addition, it is very easy to read and comprehend by citizens and the matrix is posted on the city's web site for increased visibility.

### **Pitfalls - Current Budget Process**

There are some pitfalls to our current process. The most notable is that it does take time to implement. Due to the fact the city does not have a cost allocation system or activity based costing module, the assignment of all overhead and employee costs for each program must be manually calculated. When the system was first implemented, we encountered departments whose matrix reported double the amount of staffing allocated within their budgets. In addition, their amount of funding required to fund the program/service were astronomical compared to the adopted budget. These problems, with additional training by the Budget Department, have been eliminated. Other pitfalls recognized within the current system:

1. There is a tendency for the city council and citizens to micro-manage the budget.
2. Most departments think their programs should have a "no choice" service hierarchy identifier when actually they should be a "choice" program.
3. There is a discrepancy between what departmental, citizen and city council priorities.

## **Next Steps?**

The City of Plano's current target/priority base budget and core business matrix process has assisted the city in reducing our General Fund budget by 30% over the last three years. The implementation of the core business matrix and the assignment of priorities to our core businesses/programs have allowed the city to provide a higher level of understanding among our city leaders regarding the scope, costs and impact of various core services and better articulate how we value our services, invest in our priorities and divest ourselves of lower priorities. The system has allowed the city to identify its most important strategic priorities and move away from traditional across-the-board budget cuts in order to solve our budget deficit. The problem with traditional across-the-board budget cuts is that they treat each department equitably across an organization. Core businesses do not equally influence the strategic plan within our organization. Some core services have a greater influence on the city's strategic plan than do others. (e.g., police, fire, public safety) An example would be your own household budget. Under times of financial duress, items such as mortgage payments and car payments are likely to remain constant but items such as eating out and entertainment are more discretionary.

One of the major weaknesses with our current core business matrix system is the priority system we have in place. Currently, departments upon completion of their core business matrix must assign a priority to each of their core business/programs. The priority system is based on numerical 1, 2, 3, etc. The problem with this system is that city leaders are unable to evaluate how every program compares to each other in terms of relevance across the entire city. The current priority system allows city leaders to see how the program is evaluated within that department. The City of Plano has recently

signed a contract with Johnson and Fabian Advisory Group out of Denver, Colorado to develop a citywide prioritization matrix, which will allow for the prioritization of all core business/programs relative to each strategic goal and basic program attributes. The result of this process will provide a priority base budget system, which will allow for city leaders to be able to use a tool to identify priorities based on how they compare to services desired by the community and based on the strategic goals of the city.

### **Conclusion**

In today's current economic environment, federal, state and local governments are trying to figure out how to maintain current services while not increasing taxes. In order to balance budgets, ideas have to be generated and change must happen. The "New Normal" is here. Which budget process local governments' select depends on their organizational structure, elected officials opinions, how much will the change cost, and other variables. On November 8, 2010, the zero-base budgeting concept was presented to the city council of Plano. Based on our research, it would cost over \$2 million and take two years to implement if a change to zero-based budgeting was initiated. The majority of the cost is associated with a complete restructure of our financial system in order to accommodate the process. **Is the change really worth it?** To the disappointment of its early advocates, ZBB, as a process, has not had a major impact on reducing spending nor did ZBB really change the way agencies budget.<sup>6</sup> Whether the results are worth the

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<sup>6</sup> Draper, Frank D., Bernard T. Pitsvada. 1981 ZBB – Looking Back After Ten Years; *Public Administration Review*, Vol. 41. No. 1 (Jan. – Feb. 1981), pp. 76-83. – Whitepaper. National Science Foundation

additional time and effort is the crucial question.<sup>7</sup> The City of Plano conducted a survey of 32 nationwide cities regarding the use of a true zero-base budgeting system within their government entities. According to our survey 0% reported that they used zero-base budgeting, 35% reported target-base budgeting, 15% reported priority-base budgeting while 65% reported prescribing to a combination of budget approaches. Through our research, several states have implemented the ZBB system over the years but due to the time commitment, they only have their agencies go through the process during their sunset review. At the end of the presentation, the city council chose to remain with our current target/priority base system, at least for the present time. Within their discussion, it became evident that what they are truly in search of are the details behind the budget. Our current budget process can provide the details they want without the price tag of implementing ZBB. The city council is looking forward to the implementation of our new prioritization system mid-January. In addition, they have asked for several budget work sessions to be scheduled in order to spend more time going over the details of the budget. The time for transparency is here but there are other ways to provide it without the implementation of ZBB.

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<sup>7</sup> Moore, Perry, Wright State University. 1980. Zero Based Budgeting in America Cities. *Public Administration Review*. May/June 1980 – Perry Moore, Wright State University. p. 253-258