Case Study:
A Budget Aligned with Expectations

Lee Gerney, Chief Technology Officer, Yolo County California

I had good reason to fear this year's budget process. But thanks to a change in the way we prepared our budget proposal, everything went amazingly smoothly. I'll explain how we did it. But first, a bit of background….

The Difficult Situation

Yolo County is a small, rural county in California's central valley. There's not a lot of wealth in this area. So, the County has always been very resource constrained. We're used to getting by with limited headcount and budgets, and making tough decisions about priorities.

But this year was worse than usual. County tax revenues were flat, and the State was facing an estimated $68 billion deficit. In other words, our two major sources of county government funding were flat or shrinking.

Based on past experience, I expected that every Department would have to take a significant budget cut. But, as the saying goes, we were caught between a rock and a hard place. While funding was shrinking, we were facing rising costs in our vendor services and supplies, and escalating personnel costs to keep up with the labor market.

"Do More with Less"

Budget cuts alone aren't necessarily a problem – as long as expectations are reduced along with reduced resources. But that's not what usually happens. In the past, our budget had been reduced, but we were expected to continue to deliver an ever-growing set of operational services ("keep the lights on"), *plus* a list of key projects needed by the business.

It was the old "do more with less" demand, as if we could instantly become more productive thanks to a reduced budget.

That's just not possible. We don't have "fat" in our budget that we can simply cut out to save money. We are certainly not wasteful. And we were all running at top speed.

In fact, the opposite is likely. With high expectations and reduced resources, our staff are put under even more stress. The best people leave. The rest are frazzled. If anything, when we're asked to do more with less, our productivity goes down, not up.

"IT Is Just a Cost to be Minimized"

To add insult to injury, historically when budgets become a challenge, the County targets spending on things like travel, training, and consultants, without fully understanding the impacts those reductions cause.

Ultimately, cuts to spending in these various categories affect our productivity across the board, and only make us less able to deliver *any* of the expected projects and services.

Furthermore, when budget discussions focus on our spending, they just reinforce the unfortunate perception that IT is a cost center – something to be minimized – rather than a source of great investments that deliver real value to the business. The budget process did nothing to build County leadership's understanding of the value they got for their investments in technologies.

And by the way, consider this: Are our Chief Administrative Officer (CAO, the County's equivalent of a CEO) or our Chief Fiscal Officer really equipped to decide what IT needs to spend on training and consultants to keep our technologies running and our function viable? That's my job as CIO, not their field of expertise. By submitting a budget for those costs, we were setting ourselves up for micromanagement, and asking our senior leadership to make decisions that they're not equipped to make.

Poor Budget Decisions

In past years, after unproductive discussions of our costs, our final budget often came down last year's spending plus/minus a percentage.

This number had absolutely nothing to do with the needs of the business or the strategic investment opportunities ahead.

In IT, operational requirements were growing. Every time we implement a new application, our operational costs go up for years to follow. With a fixed (or reduced) budget, that means that an ever-larger portion of the budget goes to "keeping the lights on," leaving less and less each year for new projects.

The result is obvious: We were not funding some very high-payoff projects – in some cases, projects that could significantly reduce costs enterprisewide. We were walking away from some great investments.

Funding for Infrastructure and Innovation

In addition to the missed opportunities from high-payoff business-driven projects, our traditional budget process often failed to provide adequate funding for infrastructure and innovation. We were expected to make these internal investments without any explicit funding for them – as in "take it out of hide."

As our infrastructure ages, it gets more and more difficult to maintain. This so-called "technology debt" saves capital in the short-term, but drives up operating costs for years to come.

And the lack of funding for innovation – both staff education and innovation projects – inevitably leads to our skills become obsolete over time. And again, we miss out on some great investment opportunities which require emerging technologies that we aren't prepared to deliver.

Unrealistic Expectations

Perhaps the most insidious impacts of the traditional budgeting process came from the *lack of any linkage between budgets and deliverables* (next year's projects and services).

Sure, we itemize a few major strategic projects and their costs (at least their direct costs). But the bulk of our budget was a "black box." Nobody really knew what it did, and did not, pay for.

This created a number of problems:

First and foremost, clients' expectations far exceeded our resources. They would say, "Hey, we gave you all that money. Now it's your job to satisfy all our needs."

And we had no basis for saying, "That wasn't covered in our budget. We'd like to help you, but we'll need additional resources to do that." It's as if we're expected to deliver infinite services with very finite resources.

We were set up to fail. Clients blamed us for unresponsiveness, or worse, an inability to support their businesses.

To make matters worse, as we scrambled to satisfy demands far in excess of our supply, we cut corners and quality suffered. Of course, this negatively impacted our reputation and our relationships with our clients throughout the County. And ultimately, short cuts drive up future costs.

"You Cost Too Much"

Rubbing salt into the wound, on occasion, we would get accused of costing too much.

What was this based on? I assure you that it was not based on data. Nobody ever compared our rates (unit costs) with alternatives like outsourcing. And high-level benchmarks of our spending versus other counties don't take into account our unique needs, such as the strategic initiatives of our County's Board of Supervisors or the forward-thinking technology visions of our County departments.

The real source of this accusation was that everybody knows how much money we're given; but they didn't have a sense of the value the County was getting for that money. They had a clear perception of our costs, but not the benefits of the spending. Of course, IT appeared to be too expensive!

The strain on relations that this created was exacerbated by our system of allocating support costs to the business. IT costs (in several categories) are assigned to Departments (our word for business units) based on high-level formulas, like PCs or payroll transactions.

Of course, the Departments cannot control these allocations. Combine that with a lack of perception of what they get for that "tax" and you have a formula for resentment. It's no wonder they criticized our spending. They know it hits their bottom lines.

Unfair Comparisons to Decentralization and Outsourcing

Another form that this accusation can take is unfair comparisons with decentralization and outsourcing. We are a highly collaborative culture, so this has not been a major problem for me in recent years. But I remember a time when Departments demanded their own IT groups.

Why? They thought they could save money by hiring their own IT staff rather than working with enterprise IT (us).

But this was a false economy. They were looking at only a portion of the true enterprise costs of IT. They'd implement a software package on their own, and then we'd still have to provide installation and integration, ongoing support and maintenance, infrastructure services, and cybersecurity management. Considering only one-time implementation costs was like looking at the tip of an iceberg.

But we never communicated the costs of those other things that we'd need to do to support their applications. Again, we didn't link our budget to our services.

So, we couldn't make the case that their costs plus our costs to support their decisions added up to more than if they had just worked through us. Just the opposite. Decentralization was actually driving total County costs up.

My predecessor was able to consolidate the largest of the decentralized IT groups into our shared-services group. But that only went so far. The Departments that turned their IT staff over to us continued to fund those positions, even though they reported to us. And Departments felt that since they were funding the positions, they had complete control of the employees.

This made it tough for us to manage our resources. And it caused somewhat of an identity crisis for the staff. Were they an IT employee or an employee of the Department that was paying the bill? It was not a healthy situation for us or them.

Meanwhile, the Departments were only seeing a portion of the costs of their technology investment decisions. They paid the direct costs of labor, but not all the costs of IT support staff and infrastructure that contributed to the implementation and ongoing life-cycle support of those technologies. Since everything looked less expensive, they bought applications that may or may not have been economically wise.

Clients Felt Out of Control

Our clients know they need IT. Some even understand that technology can deliver strategic value to their businesses. "Digital government" is not new news.

But the traditional budget process gave our clients no voice. They couldn't say, "I really need that. We need to fund this project, but we can do without that one." How could they? Our budget submissions didn't describe the costs of our projects and services.

As a result, clients felt they could not control (or even influence) our priorities. Said another way, there was no systemic process to ensure our alignment with clients' business strategies.

Internal Teamwork

The ill effects of a traditional budget process extended into the fiscal year.

Each group within IT was given a budget. Its manager was expected to work within that constraint. All our managers were aware of our major strategic initiatives. But beyond that, each had to set their own priorities for their resources.

Of course, if one group's highest priority is another group's lowest, teamwork is impossible. All the team-building in the world won't help. The problem was systemic. We couldn't set priorities among projects across the entire IT department because budgets were associated with groups rather than projects across groups.

Differing priorities undermined teamwork. Our managers learned to be self-sufficient – to minimize the need for teamwork. As a result, we became less specialized. With our staff trying to be competent at multiple specialties, our productivity was negatively impacted. Generalists just cannot perform as well as teams of specialists in the complex world of technology.

Culture

One additional effect haunted us throughout the year. The traditional budget process sent the signal that, to get budget, you have to please your boss – not your real customers in the business. This is the opposite of customer focus.

In fact, managers were put in an awkward position. They had limited budgets and many clients demanding their services. It would be understandable if they saw clients as supplicants – a nuisance – rather than valued customers.

Furthermore, they didn't have time or incentives to be entrepreneurial – to be creative, innovative, and open to risks in order to find new ways to add value to the County's business. Just the opposite – new ideas would only serve to create more demand, but not necessarily incremental resources to deliver it. Creativity would just make the imbalance between expectations and resources worse.

Our budget process drove our culture in the wrong direction – away from customer focus, innovation, and entrepreneurship.

Please don't misunderstand. Our staff are great people, and work very hard to please our clients. But the relationships between IT and the business were, at times, contentious for lack of effective customer-supplier partnerships.

Summary: The Traditional Budget Process was Counterproductive

In summary, the traditional budget process was causing many serious problems, including:

- Impossible "do more with less" demands
- Perception that IT is just a cost to be minimized
- Asking the boss to tell us how to run our function (micromanagement)
- Budget decisions unrelated to the needs of the business
- Unreliable funding for infrastructure, innovation
- Unrealistic expectations
- Accusations that we cost too much
- Unfair comparisons to decentralization, outsourcing
- Clients felt out of control, lack of alignment
- Differing priorities across groups undermined teamwork
- Lack of internal customer focus, entrepreneurship

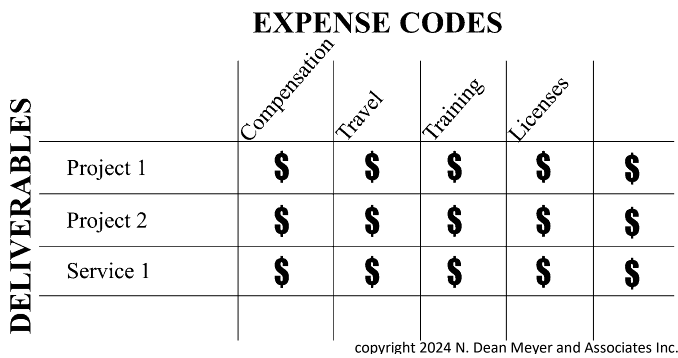
As I looked ahead to the budget process in a tough year, you can understand my trepidation.

And as I thought about why these problems were happening and what I could do about them, I realized that it all came down to one thing….

The Solution: Investment-based Budgeting

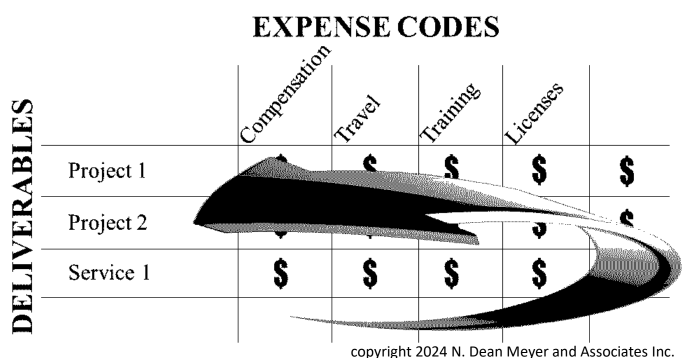
All these problems are rooted in the lack of *linkage between budgets and deliverables*.

Dean Meyer [www.ndma.com], the father of "investment-based budgeting," asks you to imagine a budget spreadsheet:



Of course, this was familiar to me. But Dean points out that the mistake so many organizations make is that they total the *columns* and submit a budget for what they plan to spend.

Clearly, the right answer is to total the *rows* and submit a budget proposal that describes the costs of the projects and services our clients are requesting, as well as our own ideas for high-value projects, and our own investment needs such as infrastructure and innovation.



This struck me as the key to transforming our budget discussions into something productive, and solving the many problems we had experienced in the past.

Reference: ndma.com/resource/ndm7537.htm

Implementing Investment-based Budgeting

The concept of investment-based budgeting is simple. But as you might expect, "the devil is in the details." It's especially challenging to apportion all our indirect costs (not project-specific, the bulk of our costs) to the right deliverables.

Fortunately, we were able to engage Dean to help. He had developed a process and a tool for investment-based budgeting called *FullCost*. The good news: It's an incredibly powerful method and tool. The bad news: It takes time to implement it, and it costs more than we could afford.

But Dean had recently developed a simplified version of FullCost for small organizations such as ours. I jumped at the opportunity to pilot *FullCost Light*.

Most of the data was readily available. We just plugged it into the model. Direct costs were assigned to specific rows. The model apportioned indirect costs (at both the group and IT Department levels) to the appropriate rows.

The two new, and challenging, inputs were (1) the list of deliverables (the rows), and (2) the level of effort each IT group planned to put into those rows.

We had already worked with Dean on our organizational structure. So, we were familiar with the concept of internal lines of business, each of which offered catalogs of products and services. This, combined with coaching from Dean, guided us in developing our list of deliverables.

As for the level of effort, Dean came up with a very simple algorithm. Each manager was given a spreadsheet with our list of deliverables, and a simple guideline for assigning level of effort. The model took care of converting that level of effort to hours and assigning compensation costs to the rows.

With the tool and Dean's help, we assembled the entire budget proposal in less than four months.

What Happened

To my delight, budget negotiations were a "piece of cake" – so much easier than in past years.

Once the model was ready, I reviewed it with each of my peers – the senior executives across the County. I showed them just the rows that benefitted them. And I told them, "If you don't want this project/service, I'll take it out. But if you want it, I expect you to defend my budget for it. After all, it's for your benefit, not mine."

The reaction was extremely positive. They loved the transparency, and they loved having a say in our priorities. Thanks to these one-on-one discussions, my peers came to understand all the value they were getting from those allocations, and more broadly, from IT.

For example, one Department leader said, "Finally I understand where my IT dollars go, and what I am getting in return."

Another said, "As part of the budget instructions, we get these IT charges that I know I need to pay. But I didn't fully understand why and what they covered. Now I know exactly what I am getting. And I understand that if I need more, I'm going to have to provide more funding."

It worked! They communicated their support for my budget to our common boss, the County's CAO.

When the time came to present my budget to the CAO and CFO, the entire meeting took just 20 minutes. They asked for savings. I pointed them to the rows (not columns like training and vendor services). They saw that there was very little that was discretionary and could be cut.

Well, they had to cut something. Every other Department was getting hit hard, with much tighter budgets and hiring freezes. So, they found one row – our transformation budget – to cut (even though they honestly saw and appreciated the positive effects our transformation process had already had). But through our work with Dean on structure and investment-based budgeting, much of our organizational transformation was already in place. We'll just have to postpone some of our next steps.

The Bottom Line

In the end, in a difficult year of significant cuts, we came out with a budget very close to last year's. We fared so much better than any other Department, and so much better than I'd expected.

But the point was not maximizing our budget (a cost to the County). We can live with any level of budget, *as long as expectations are in line with resources*. The key was the linkage between our budget and our deliverables.

Investment-based budgeting allowed us to:

- Avoid unproductive haggling over our costs
- Build everyone's perception of the value of IT – as a worthwhile investment, not just a cost to be minimized
- Counter the general impression that we cost too much, and reduce pressure for decentralization
- Engage clients in defending our budget, and aligning our priorities with their needs
- Highlight needed funding for infrastructure and innovation
- Make budget decisions based on business needs
- Bring clients' expectations in line with our resources
- Encourage internal teamwork and our culture of customer focus and entrepreneurship

From my perspective as the County's CIO, I believe that investment-based budgeting was one of the highest-payoff projects we did all year. I'm recommending it to all my peers, in both other internal support functions and our various citizen-facing business units. And I dream of the day when we're all doing investment-based budgeting, and fund County initiatives and align priorities enterprisewide.

Lee Gerney is the Chief Information Officer and Director of IT for Yolo County, California. He oversees an annual operating budget of just over $8 million and leads a team of 42 employees.

Lee started his career in 1998 as the IT manager in public education. He transitioned to county government in 2004, beginning as a network engineer. Lee quickly advanced through the ranks to become the County's Chief Information Security Officer (CISO), and ultimately assumed the role of County IT Director.

Lee has earned multiple industry certifications, including CISSP, CISM, and CISA, which reflect his deep commitment to cybersecurity, information management excellence, and life-long learning. Additionally, he is a certified county executive through the "Credentialed California County Technology Executive" program, accredited by the California State Association of Counties (CSAC).