Financial capacity is the ability to acquire and manage sufficient funds to effectively operate and maintain your water system. This handout series is designed to help you develop a sound water system budget, which is the key element to developing financial capacity.

The budget process is more than just cataloging revenues and expenses, developing reserves, and balancing those accounts. The budget is also about meeting water system goals, and stakeholder needs. This means there is a process involved in drafting and adopting a budget. In this handout we offer four key actions to generate and execute an effective budget to better manage your water system.
When preparing a budget, there are four key actions to take - each of which is critical for your water system's success.

1. **Establish Broad Goals to Guide Decision Making**

   **Assess Community Needs, Priorities, Challenges, and Opportunities**
   Engage the community in the process of setting goals for the water system. This process can start by determining the level of service you are currently providing (e.g., the minimum operating pressure, the response time for repairs or customer complaints, the quantity of water loss, etc.) and asking your customers if these levels are appropriate. This could occur through surveys, informal meetings, or workshops. This will allow the community to have an explicit understanding of the level of service they are paying for.

   **Develop and Distribute Broad Goals**
   After you seek community input and establish both internal and community goals for the system, you should record and prioritize these goals, and circulate them to customers. The goals should be measured over time to see if they are met.

2. **Develop Approaches to Achieve Goals**

   **Adopt Written Financial Policies**
   Financially sustainable systems will have written policies for things such as fees and charges, reserves, debt levels, use of one-time revenues, and contingency planning.

   **Develop Operating and Capital Policies and Plans**
   Begin by developing a simple asset management plan with infrastructure condition, determination of critical assets, replacement, and identification of funding. While doing this, keep in mind the level of service you want to provide.

   **Develop Programs and Services that are Consistent with Policies and Plans**
   Take a look at your activities and services periodically. Can you do things more effectively or efficiently? All programs should have a regular evaluation component including benchmarks to help you track progress.

3. **Develop a Budget Consistent with Approaches to Achieve Goals**

   **Develop a Process for Preparing and Adopting a Budget**
   This includes establishing things such as an annual budget process calendar, budget guidelines and instructions.

   **Develop and Evaluate Financial Options**
   This may include: conducting long-range financial planning; projecting future revenues from rates and fees; evaluating the effect of changes to revenue source rates and bases; analyzing tax and fee exemptions; preparing spending projections; and developing a capital improvement plan.

   **Make Choices Necessary to Adopt a Budget**
   Finally, you'll be in a position to make choices necessary to adopt a budget. At this stage you will: Prepare and present a recommended budget, describe key policies, plans, and goals, prepare a budget summary and adopt the budget.

4. **Evaluate Performance and Make Adjustments**

   **Monitor Progress Throughout the Fiscal Year**
   After passing the budget, there's still work to be done. As with any workplan, a budget requires regular updating as facts on the ground change or predictions prove inaccurate. You must monitor, measure and evaluate performance of your budget. Monthly or quarterly spending plans and reviews are perhaps the most important way to evaluate budget performance.

   It is important to monitor the overall performance of the water system - i.e., ability to meet level of service goals, the capital improvement program and community satisfaction. It is likely that you will have to make adjustments to one, or even all of these things. This evaluation process helps you prepare for next year's budget, making your job easier every year. Your improvement over time will earn the respect and trust of your community.