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Summer 2019

Exchange

Association for Financial Professionals' Quarterly Magazine

What's Next for FP&A?

Financial Planning & Analysis Ponders Its Future

Decentralized Budgeting Meets Headcount Planning

How Machine Learning Improves Forecasting

The First FinNext Tech Challenge Champion

5 Practices of Highly Effective FP&A Teams

Case Study: Verizon Upskills Finance

Can Finance Measure Innovation?

PLUS:
Libor Fallback Language

How LOW Can You GO

Decentralized budgeting meets headcount planning

JOANNE E. BRUNN, PH.D.

Even for organizations that have embraced a decentralized or collaborative approach to financial planning, the finance and HR teams often manage headcount planning in a fully centralized or hybrid approach. What's behind this disconnect and which method is best for your organization?

Decentralized budgeting philosophies go by many names, including collaborative or distributed, and the specific execution may vary among organizations. For this discussion, we are using the terms "decentralized" or "collaborative" to describe a planning and budgeting process where employees, including budget managers and department heads, are empowered to make and be held accountable for key input and decisions.

It goes without saying that engaging multiple participants is more complex and challenging than performing a simple percentage increase in an annual exercise controlled completely by finance. But for organizations willing to invest the time and energy, decentralized budgeting returns some impressive benefits:

- More accurate budget numbers: Both in the accuracy of actual spend as well as estimates of which costs and when those costs will fluctuate throughout the year (monthly spreading)
- Increases in accuracy translate to cost savings: This enables organizations to dramatically reduce the size of contingency or slush/overage accounts
- Employee engagement rises as well: Employees are more motivated and have greater job satisfaction and performance.

"[A decentralized approach] has been a very positive change for us," said Karen D'Anjolell, Enterprise Reporting Administrator, NJM Insurance Group. "We've experienced a more collaborative effort from all of our departments. Staff are definitely more engaged. They like being able to get right down into the details. While the finance team gets access to timely information that is way more accurate. For example, in 2018 actual results were only off budgeted amounts by 1.4 percent."

Headcount planning

In most organizations, staffing costs represent the single, largest expense of overall budgeting—commonly, 50 percent to 80 percent. It's also often the area of greatest variability and complexity. So, no surprise that the benefits of decentralized budgeting are even greater when the approach is extended to include headcount planning. Yet, even in organizations that embrace a decentralized approach to budgeting there's a good chance that personnel budgeting and headcount planning are held outside of the budgeting process.

What's so different about headcount planning that makes it such a common exception to the decentralized rule? The answers seem to fall into three key areas of concern: confidentiality, challenges of execution, and culture.

Confidentiality is perhaps the most obvious and often reported concern of HR and finance teams. No one wants to run the risk of salary and benefit information falling into the wrong hands. This is a particularly challenging issue for organizations using Excel templates for budgeting. Distributing multiple iterations of spreadsheets out across the organization to all of the managers involved in the budgeting process can be a confidentiality nightmare. Lacking the ability to effectively limit who sees what data with a secure user login makes many senior managers wary of a decentralized approach.

Ensuring proper controls are in place to avoid the disclosure of salary and benefit information outside of appropriate staff is mandatory for a fully decentralized implementation of headcount planning. For organizations without these controls, a hybrid approach may be a better fit, gathering non-confidential information from department heads on:

- Numbers of anticipated new hires, replacements, retirements, terminations and various types of leave of absence or anticipated temporary staffing
- Costs associated with transitions including severance, recruiting, moving, signing bonuses, training costs, etc.
- Insight into seasonality or market-related fluctuations—e.g. anticipated overtime of hourly workers staffing weekend events or a new product-launch.

With this approach, HR and finance retain responsibility for detailed verification of salary rates and related benefits, bonuses and headcounts but gain critical knowledge of anticipated staffing-related variances and cost-drivers.

Collaborative budgeting is a double-edged sword that can produce great benefits as well as unique execution challenges. You are pushing the budget process down to front-line managers because they are the domain experts in their respective departments or areas. But even though they are experts in their area they usually aren't savvy Excel gurus.

"We have 104 budget managers across six colleges," said Courtney Bonnell, Director of Budgeting and Planning, A.T. Still University. "Our staff have talents and skills in lots of areas but not all of them have financial skills. We needed to ensure our approach to collaborative budgeting guided managers with clear instructions from one step to the next to provide us with the information we need. With this approach we've been able to gain transparency and consistency from year-to-year and department-to-department. We're finally at the point where we can actually identify every dollar and what it's for."

Determining how low in an organization to push the budgeting or headcount planning process requires a realistic time/benefit analysis. Evaluate the capabilities and availability of your current staff as well as the application you are currently using for budgeting and planning with questions such as:

- Can you export data or run reports with detailed salary and benefits information?
- Can you quickly remove costs associated with an unexpected termination, or flexibly shift hire dates and reflect the impact across the budget?
- Can you easily set compensation cost drivers for benefits and salary increases?

If you answered "no" to any of these questions, then a technology audit may be in order and a hybrid or fully centralized approach may be a better fit for headcount budgeting.

Organizational culture and how it influences a decision to centralize or decentralize budgeting overall—and headcount planning specifically—involves a complex mix of issues and considerations:

- Flexibility or control: Which is more valued or critical to achieving your objectives?
- How important is transparency and communication to your culture? And, to employee morale or performance?
- And perhaps most importantly: Does the detailed expertise and hands-on knowledge of your department heads influence the accuracy of your final budget numbers?

"Organizations often overlook the impact of poor communication on employee engagement and culture," explains Leslie Grossman, author on collaborative leadership and Faculty Director, Women's Leadership Program, at The George Washington University Center for Excellence in Public Leadership. "As organizations expand, communication becomes less organic and more structured. Employees have limited input and insight into the 'why' behind strategic decisions. Historical knowledge is lost with employee transitions. Each of these small issues can add up to a loss of trust in management and resentment between departments."

Collaborative budgeting can actually be leveraged to increase transparency, improve two-way communication, share strategic goals and improve ownership. Just by asking for input you are empowering and validating your staff. Research shows that even if you don't implement all of an employee's suggestions or budget requests, they still have an increased engagement and satisfaction level.

Here's how finance teams can facilitate a collaborative approach to headcount planning while still feeling confident that the right controls are in place:

1. Ensure confidentiality. Maintaining privacy of headcount data is top priority in a decentralized budgeting model. Proper security measures should be put in place allowing access to view or change employee data based on role or title and department.
2. Audit data for accuracy. Just one or two inaccuracies in the data can result in thousands of dollars of hidden errors in your budget. Include a detailed review by each department head of current employee data, including ID and position number, title, salary grade, employee class, etc. With proper security controls in place, this should also include a review of salary data.
3. Assess fluctuations and impact throughout the year. Hiring, firing or planned leaves have an obvious financial impact. But the key to accuracy in your final numbers lies in being able to anticipate the impact (both cost and timing) on the budget and to make adjustments if necessary. While it's not realistic to know every staff change in advance, department heads have the best "intel." Leveraging their insights can get you significantly closer to budgeted vs. actual spend at the end of the year.
4. Be transparent. Budget managers should be made aware of their portion of the cost for any employees allocated across departments. It's true that they may not like the situation or have any control over these costs. However, research shows transparency into the total budget by department increases ownership, engagement and accuracy.
5. Simplify benefit calculations and salary increases. A built-in calculation of benefits (based on the rules for that department, by individual employee, or some combination thereof) provides convenience for your budgeting manager. At the same time it ensures proper controls are in place for the finance team. Similarly, providing a default salary increase (across the board or by employee class) frees up managers to focus on the employees who should be an exception to the rule based on merit, market adjustment, etc.
6. Dig for details. Provide prompts for critical but often overlooked compensation information that is only available to the employee's direct manager. This includes costs like sales or performance bonuses, overload payments, stipends or overtime.
7. Document the decisions and rationale. Ensure there is a mechanism to capture the justification behind each key decision. This information provides insight for the finance and management teams if adjustments to the budget are needed. In addition, it increases the ability to track budget to actuals throughout the year and captures historical knowledge to inform next year's budget or in the case of turnover.
8. Provide a detailed checklist, ideally a guided process, to ensure less financially-savvy department heads don't miss any of these key steps along the way.

Joanne E. Brunn, Ph.D. serves as Chief Executive Officer of XLerant, www.xlerant.com, provider of cloud-based budgeting, forecasting and reporting solutions for small and mid-sized businesses. She holds an MBA in Finance as well as a PH.D in Human Sciences.