For more than a decade, Tim Quinn, CPA, CGMA, negotiated the tedious, back-and-forth magic of building the annual budget for Northern Quest Resort & Casino.

Every year, it was the same time-consuming endeavor: Quinn, the company’s vice president of finance, would send out budget worksheets to 45 department heads. The department heads would return them with inflated spending projections, or low-balled revenue projections, for the coming fiscal year. Quinn would question the validity of those projections. Pushback would ensue, but Quinn and his staff would prevail, often by adjusting the projections to something that more realistically reflected historical trends.

After several rounds of wrangling, voila: The budget was born.

That laborious process would take as long as five months—so long that business conditions usually changed in such a way that the approved budget ended up being more a window to the past than a guide to the future. “Once you’ve got it all approved, it’s irrelevant,” said Quinn, who has worked at Northern Quest since it opened in December 2000. “Because now life goes on, and things change, and what you thought was going to happen doesn’t happen.

“To go through that whole, long, arduous process to come up with a document that’s essentially useless—I decided it was kind of a crazy idea.”

So last year, about halfway through the process, Quinn surrendered. “I said, ‘Forget it, I’m done with this.’ ”

Poof. No more budget. In its place: a rolling forecast, something more companies are converting to or using in tandem with a budget.

Rather than locking into an annual budget, the company now uses quarterly financial results to update a 15-month outlook. Every three months, the forecast revises itself based on the most recent results. “It’s a living, breathing document,” Quinn said. “It’s more in tune with what reality is becoming.”

The transition has already begun to pay off. His finance staff now has a little more time to spend on forward-looking strategy. The use-it-or-lose-it mentality that plagues the budget process is fading. The rolling forecast also has begun to break down silos that the traditional budget built around various departments.

Quinn’s lessons from the journey—particularly in selling the idea to internal stakeholders and implementing a process and technology to support it—could benefit other companies contemplating the adoption of a more flexible budgeting and forecasting process.

COMPANIES NEED MORE AGILITY

In recent years, an increasing number of companies have eschewed or amended traditional budgeting techniques for a more flexible approach. Today, a majority of companies use a budget as well as a more forward-looking forecast when planning for the future, according to research by Quantrix, a maker of business modeling and analytics software. Only 14% of Quantrix customers surveyed in 2012 relied solely on a budget, down from 22% in 2011. Meanwhile, 7% had
eliminated the budget, up from 4% in 2011.

The need for agility is fueling the transition. The average company spends four months on budgeting, according to research by The Hackett Group. At the same time, companies are expected to react more quickly to changing regulations, budding innovations, new competition, and erratic economic events. The faster pace of business, aided by the rise of technology that can better automate control functions, is making traditional, line-item budgets less useful. Companies are finding that, to be more agile, their spending decisions are governed more by real-time risks and opportunities and less by a document completed a year earlier that dictates spending during a period.

“You put a ceiling on cost, and I guarantee they won’t spend a penny more. The problem is they rarely spend a penny less,” said Steve Player, CPA, CGMA, the North American program director of the Beyond Budgeting Round Table. “They spend right up to that ceiling. Instead of having cost consciousness, where people ask, ‘Should I be spending the money?’, they’re authorized and entitled based on assumptions that have become out of date. It’s an illusionary control. Why does spending spike at the end of a quarter or year? Everybody’s spending their budget.”

The spend-to-the-ceiling mentality was one reason Quinn ditched the budget at Northern Quest. The resort outside Spokane, Wash., features 250 hotel rooms; 14 restaurants, bars, lounges, and nightclubs; a 55,000-square-foot casino; and a pavilion that has featured Bill Cosby, Clint Black, and B.B. King.

“It’s a beautiful property, and we need to keep it that way,” Quinn said. And under the rolling forecast, “any reasonable cost that has to be incurred, you’re not going to be confined by a budget that says, ‘You only have $10,000 to spend, and you’ve now blown that.’ That’s not productive. It’s not going to make the property what it needs to be.”

The conversion to the rolling forecast has come in three stages. There was the buy-in phase, followed by the implementation phase. Then came the refinement phase, which involved change management and tweaks to the processes and technology that were implemented. The biggest step, though, was making the move in the first place, Quinn said.

ACHIEVING BUY-IN

Quinn started the transition to rolling forecasts by selling his case to stakeholders up and down the chain of command.

First, he had to convince the vice presidents and general managers at Northern Quest, which he said wasn’t too difficult. The COO liked the idea. The CFO of the Kalispel Tribal Economic Authority (KTEA)—the organization in charge of private enterprises of the casino’s owner, the Kalispel Tribe of Indians—initially was skeptical because he was accustomed to traditional budgets. But Quinn said he eventually came around.

Then Quinn presented the idea to the KTEA, which is essentially Northern Quest’s board. That group needed little convincing. “They never approved a line-item budget anyway,” Quinn said. “We just kind of gave them the top-level: ‘Here’s our revenues, here’s our projection, here’s our projected EBITDA.’ That’s all we ever presented to them in the first place. To go to a forecast, it was not that difficult a change. They were not seeing anything different.”

The more complex discussion has been on the ground, among the finance staff and department heads who had to change the way they looked at the numbers (see sidebar, “Four Ways to Embrace Rolling Forecasts”). Much of the convincing centered on explaining how rolling forecasts would work, not to mention the benefits.

The finance team was easier to convince. Under the old process, each department’s budget was rolled into an unwieldy, multi-tabbed Excel document. “People would manage to change a line, they’d end up blowing it up, and it doesn’t import right,” Quinn said. “They’re not missing that.”

Research by the American Productivity & Quality Center shows that companies employing rolling forecasts save between five and 25 days each year in their budgeting process.

Quinn estimated that time saved by killing the budget will be redistributed in the new process. “The three- or four-month process is going to get spread out over the year, but it’s going to be far more accurate when this all gets fine-tuned,” he said. The accuracy will ultimately help drive up revenue and reduce costs, Quinn said.

Convincing department heads outside of finance has been a bigger challenge at Northern Quest.

"THIS NUMBER'S NOT REAL"

During the era of traditional budgeting, Quinn continued to see departments throw around budget numbers that went against historical trends. The defensive inclination by some was to project bigger-than-expected costs and lower-than-expected revenues. If approved, the thinking went, the department in question wouldn’t be constrained by a tight budget,
but it also wouldn’t be at fault if it underperformed on the revenue side. Sandbagging.

“...I would sit down with managers and say, ‘This number’s not real,’ or ‘That doesn’t trend right, so explain it to me,’ ” Quinn said. “If they couldn’t provide details, then I’d just cut it.”

That exchange was rarely easy. “People freak out and say, ‘I can’t do this. That’s not my budget,’ ” Quinn said. “It creates silos in my opinion.... It creates a roadblock for progress.”

One challenge in the transition has been getting managers to appreciate the constant participation needed to make rolling forecasts work properly, or just getting them to focus on it on a routine enough basis so that it’s a fresh, viable document.

But Quinn has been able to convince many of the managers that an ongoing conversation about revenue and expenses can help the organization move more quickly when needs arise (see the sidebar, “How It Works”). Compared with the previous process, the rolling forecast keeps department heads on their toes.

“The individual departments should be reviewing it routinely and saying, ‘Yeah, that makes sense,’ ” Quinn said. “You’re constantly looking at it in chunks and trying to make sure your numbers are trending where you think they should trend. So you know if you have a whole bunch of expenses coming up, you can adjust your forecast and make other adjustments in the organization to allow for that.”

The fluid nature of, and better visibility provided by, the forecast is breaking down spending silos across departments, Quinn said. For instance, if one department underspends or exceeds revenue expectations during a period, Quinn and his team can more easily make adjustments to help another department facing unexpected expenses.

“[If] I’ve got to go build this wall, or tear up this carpet and redo all this stuff I didn’t factor in, now I know that things are going to change, and I can make adjustments and still move forward and still run the organization to be what it needs to be,” he explained. “We need the ability to constantly look and adjust, and see what other places I can adjust to possibly get close to where we need to be and still meet the guest needs, keeping our duties up, and still be a nice place to come play.”

So building trust among the other managers—in large part by communicating how the change will benefit the organization—has been a big part of the transition.

“Making sure everyone understands how we need to move forward, that’s still going on,” Quinn said. But he’s confident doubters will get on board, and he takes comfort in one reality: “I always have the threat of, ‘If we can’t make this work, we can always go back to budgets.’ That’s always a nice hammer to hold.”

Quinn’s main regret is making the jump when he did, even though the timing was never going to be perfect.

“We sort of jumped into it without having all the performance indicators in place completely,” he said. “But it’s one of those things, where sooner or later, you have to make the jump anyway. I think if you had everything lined up perfectly, it would be great. But I don’t know if you’re ever going to.”

CONSIDERING MORE THAN JUST THE BUDGET

While Northern Quest made a clean break from its budget, that strategy won’t suit every company. Some organizations have simply cut the amount of detail in the budget, while others use a traditional budget in tandem with a rolling forecast.

Some of the companies that have caught on to the rolling forecast model think they’ve made major strides just by doing so, explained Player of the Beyond Budgeting Round Table. In reality, that is just the first of many steps to move to a more flexible forecasting model.

A company that is considering eliminating its budget should ask process questions about how that change would affect target setting, resource allocation, or incentive compensation plans, Player advised. There are also leadership questions: How does it change the way teams work? How does it change team and individual accountability? How does it change the company’s mission? “If you’re making the transition, what you should do is make sure you’ve thought this through,” he said.

Karen Schartman, the CFO for Kaiser Permanente’s Northwest region, said her company is moving away from a detail-driven budget, setting targets for broad categories such as payroll expenses and steering clear of item-by-item minutiae.

“When we want to drive performance, we don’t need to know the budget for pencils,” she said. “We need to know, ‘What did we spend our money on today, and does it make sense?’”
Spending less time on a budget and more on analyzing performance benefits a company in the long run, she explained. What formerly was a dollars-and-cents exercise—budgeting for hundreds of line-item categories—now plays a role in target setting and frees up talent throughout the organization.

“It’s so important that you’re spending your time on something that adds value,” Schartman said. “If people are spending time on something that’s just an exercise, nobody likes working that way.

“Human capital in organizations is scarce; it’s got to be directed on the right work. The world is depending on creativity in decision-making. People need to be free to act. The control constraints that we might have needed in the past don’t make sense today.”

How It Works

This hypothetical assumes that over a five-year period, Northern Quest spent an average of $100,000 a year on soap for its hotel rooms. In the old budget model, that would mean the housekeeping department’s allocation for soap would probably be about $100,000 for the next 12-month period. That number is locked in—even if, halfway through the year, a stock-market crash leaves consumers with less disposable income and, in turn, the resort with fewer visitors. So the problem under the old-budget scenario was that a dip in revenue caused by fewer visitors—never mind the dip in the need for soap—might have still translated into $100,000 spent on soap that year.

In the forecasting model—again, using the same hypothetical numbers—Northern Quest might plan to spend $25,000 every quarter on soap. If in the middle of the first quarter the same negative event translates into a 20% decline in visitors—and therefore 20% less soap used—the soap budget can be adjusted downward to $20,000. Quinn can then reassign the excess $5,000 to another department. If, on the other hand, occupancy is higher than expected, creating more need for soap, the additional revenue can be allocated for more soap.

Four Ways to Embrace Rolling Forecasts

**Get over the mental hurdle.** One of the biggest challenges in implementing a rolling forecast is the mindset of accountants themselves, said Aubrey Joachim, CGMA, who presided over a switch away from traditional budgets at Sydney Water. “They have in their mind that you have to come up with a number for one year ahead,” said Joachim, a former president of the Chartered Institute of Management Accountants. “That thought process is very old.” He said that in today’s dynamic environment, data can provide instant analysis, meaning the focus must be on shorter-term goals.

**Let technology do some of the work.** A recently purchased software tool has helped automate the forecasting process at Northern Quest Resort & Casino, said Tim Quinn, CPA, CGMA, the vice president of finance at the Airway Heights, Wash., company. Instead of relying on multiple Excel spreadsheets that rolled up into the full budget, Quinn can set up a forecast to account for a variety of scenarios. “The software pulls numbers directly out of our general ledger, and it can pull history instantaneously,” he said. “If I want to look ahead and factor in growth of 1% or 2%, I can see what that looks like.” He can also factor in an increase in expenses, such as departmental or companywide merit increases for employees.

**Encourage collaboration.** Perhaps the biggest hurdle to incorporating forecasting is getting others to understand why it’s important. Another hurdle: getting a few minutes of their time. “Participation breeds acceptance,” said Mark Biersmith, CPA, CGMA, the CEO of RoadMasters Holdings, a Texas trucking company. “Getting people to sit down and take part can often be difficult. If you do it alone, people don’t buy into the plan as well. There is a learning curve, but every year you do it, you have more integrity built into the model.”

**Show faith in managers.** Persuading department heads to stop padding their budgets could take time, but Joachim said the right approach can help train unit managers—and show that they can be trusted. Show them that requests for funding or resources, based on current conditions and targeted toward delivering outcomes, will be honored, and they are less likely to make arbitrary additions to their budget. “You give them a guarantee of, ‘You are responsible managers, we know how you are spending, and we will give you resources on an ongoing basis as you need,’ ” Joachim said.

EXECUTIVE SUMMARY

Traditional budgeting arose as a way for companies to limit costs. However, some say it is not very useful in today’s more volatile business climate. As a result, some companies are moving to a planning model that incorporates a rolling forecast as opposed to a static, annual budget.

The faster pace of business, and better technology that can automate control functions, is making traditional,
line-item budgets less useful. The average company spends four months on budgeting, according to one report. Some in finance say the document produced by all that work has little to no value once the fiscal year begins.

Traditional budgets have often been used as benchmarks to determine incentive compensation. That model can limit a department’s drive to innovate, because the leader is rewarded if the department stays “within budget.” Finance experts say that profit and other performance metrics should be used to determine incentive pay.

Rolling forecasts force business units to more closely track spending, which means there is more continuous monitoring than in the traditional budgeting model. Still, this model, according to those who have eliminated—or trimmed detail from—their annual budget, creates time savings for departments, which can focus more on driving value.

Neil Amato is a JofA senior editor. To comment on this article or to suggest an idea for another article, contact him at namato@aicpa.org or 919-402-2187.

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Publication

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Website

CGMA.org rolling forecast tools (member login required)

OTHER RESOURCES

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Website

Beyond Budgeting Round Table, bbrt.org