Best budget plans sweat the details

The budget and strategic plan are needed to drive, direct, change and control your company and individual projects.

by JAMES HUSTON, MBA

A budget is a strategic plan that is "reduced to numbers," to help you organize, control and direct the company.

A well-planned budget will also provide the vital feedback you need to analyze the results and effectiveness of your organization.

The budgeting process produces key standards—or targets—that will help you to run jobs, as well as the overall business.

Estimating is one portion of the four main functional areas in your business. I would say, however, that it is the most important because everything else, including total quality management, is built upon it.

The budgeting process produces cost standards and targets for:

sales (by division); direct costs (by division); gross profit margin (by division); overhead (not necessarily by division); net profit margin (not necessarily by division); labor burden for office and field personnel; field labor hours; equipment; average wage.

These cost standards are then combined with other job-related information in order to determine the cost of the project. Once we identify direct costs on an individual job, we than add markups and margins (net profits, overhead, labor burden, sales tax, etc.)

The break even point for the project is identified once overhead is added to the direct costs. A contingency factor and profit are added to the break even point in rder to arrive at the final price for the project.

It is these two numbers—the break even point and final price—that you are constantly attempting to identify during the estimating process. They answer two critical questions and identify a bidding "envelope" or range within which you need to price your jobs.

The break even point determines how low you can bid the job and still cover all costs. It is a compilation of costs for a job and is therefore fairly analytical in nature. However, the final price is subjective and determines how high you can bid and still get the job.

Bid to make money

What pricing structure will the market bear? Can you add 40 percent gross profit margin GPM to the project and still get the job? Or will this market and this particular job realistically only allow you to add 15 to 18 percent GPM above direct costs in order to have a real chance of winning the bid?

You must always determine and monitor the BEP and GPM on jobs being bid. This helps you measure, control and allocate the overhead dollars in an overhead budget. Because overhead costs are "indirect" costs, there is no right or wrong amount of overhead costs to allocate to a job being bid. Subsequently, the five different methods of pricing jobs are not right or wrong concerning overhead recovery. There simply is no right or wrong way to determine the amount of overhead costs to put in a particular job being bid.

The question to ask is not, "How much overhead should I add to a job and by which method?"

Ask instead: "If I sell a job for a certain price and complete the job on-budget, will it help me achieve my budgeted gross and

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Monthly payments fuel cash flow

Larry Iorii, president of Down to Earth, Wilmington, DE, obtains payments from clients at the beginning of every year, not the beginning of spring. The influx of cash is a hedge against new season overhead.

From April to December, Iorii's clients may make up to 10 payments on service that is scheduled or already completed.

"Let's say for 1997, we have a $10,000 commercial account. If we don't start work till mid-March, we pick up an installment in January. If a $10,000 account does not want to pay you in advance, we have a very heavy first installment payment. We'll ask for $3000 in March, then divide the remaining payments out over the remainder of the contract."

Iorii: Payment plans work!

For his lawn care accounts, Iorii asks for 60 percent of the contract amount, due on March 15, with the balance due October 15. □

Know the four revenue sources

Perhaps the most important part of your budget is the process you develop to establish revenue.

With reasonable record keeping, doing a revenue projection is a simple process. You need the following:

a list of current contracts;

sales goals for the next year;

sales achieved for the past three years;

about two, uninterrupted hours.

Here's the process:

1. Establish your backlog. This is contracted work that extends into the coming year for a specific time period.

2. Calculate your renewals. Renewals are contracted work that expires during the upcoming year, work you want to renew.

3. Project your new sales. This represents new jobs you anticipate starting that will generate income during the new year.

4. Anticipate your one-time extras. These are add-on sales to existing clients or small jobs that will occur only once.

Set up a spreadsheet that runs from January through December across the top and list backlog renewals, new sales and one time extras down the side (Table 1). Now fill in the blanks.

Your **backlog** will be a decreasing number as you total by month your existing contracts out to their expiration dates. Fill in those monthly totals across the spread sheet next to the backlog heading. These numbers are hard numbers.

Renewals are an extension of your backlog. You must assign a percentage to your chance of renewing the business when the contract expires. Be honest; it is not 100 percent for each job, and some may be zero percent.

Multiply the percentage you assign by the original contracted value to get your renewal dollars. Do this for each job from the point the existing contract expires through the rest of the year. Total these dollars by months and fill in across the spreadsheet next to renewals. This should be an increasing number across the sheet and—if you are true about your chance of renewal—a pretty accurate number.

New sales is difficult if you have not kept records of new jobs sold during a particular year. If you have, take a snapshot of your last three years. Look for trends, business attitudes, economics, or marketing goals. A pattern should show that says "we have been consistently selling X dollars in new business every year. If the number is real, then trust your historical data. If you plan an aggressive sales year, be prepared to review your budget quarterly to make adjustments.

It's a challenge to try to anticipate when new sales will begin. Use your historical data and a trend should show when you "hit" most frequently. Remember, you will only receive a portion of contracts revenue. They won't all start January 1st and end December 31st. Set up another spread sheet that runs January through December on both the top and side. Go back to your new sales goal and spread it out by month down the left side so that the total at the bottom equals your sales goal. Now, go back and divide each month's goal by twelve and, working both across and down, insert that number across the spread sheet (Table 2).

You now have your new sales goal plotted and more importantly, your revenue received for the budget year. Total each month down and fill in the numbers across the spread sheet next to new sales.

One time extras are fairly simple. These are the extras your client base requests or the upgrades you recommend to them. If you do not track these jobs, a look into accounts receivable would give you the information. Quantify an annual number, divide it by twelve and fill it in across the spread sheet next to one time extras.

With all the numbers plugged in, you have monthly and yearly budgets and goals, or a *revenue projection* (Table 3). □

Mike Guthrie, vice president, Maintenance Division, Ground Control Landscaping, Orlando, Fla.

TABLE 1

	January	February	March	April	May	Etc.
Backlog						
Renewals						
New sales						
1-time extras						

TABLE 2

	January	February	March	April	May	Etc.
50,000 Jan.	4167	4167	4167	4167	4167	
30,000 Feb.		2500	2500	2500	2500	
80,000 Mar.			6667	6667	6667	
50,000 Apr.				4167	4167	
20,000 May					1667	
Etc.						

TABLE 3

	January	February	March	April	May	Etc.
Backlog	100,000	90,000	80,000	70,000	50,000	
Renewals	1,000	5,000	10,000	15,000	20,000	
New sales	4,167	6,667	13,334	17,501	19,168	
1-time extras	500	500	500	500	500	

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net profit dollar goal for the year?"

The goal: measure, allocate and control overhead costs throughout the budget year. Don't argue over which method is correct—there is none!

Job costing

All jobs have to be job costed in order to run effectively. The profit and loss financial statement and the balance sheet are your "report cards" for the company or division as a whole. This can be done two ways:

1) Individual jobs need to be monitored by job costing.

2) You monitor your entire company as though it were one big "job." What difference would it make if individual jobs were profitable, if you did not have enough of them to support the overhead structure and the costs for the company as a whole?

Major items to monitor are:

— overhead costs

—field-labor hours and costs

— equipment costs

These are the items you need to be checking constantly in order to run you entire company and not just your individual jobs.

The budgeting and controlling process for a landscape and irrigation contracting company is a never-ending series of events that often occur simultaneously: goals are set; action is taken; progress is monitored, adjusted and fine-tuned. The goal is to have your company run smoothly during all the chaos.

Estimating budgets recover costs

Three types of budgets are used to plan and control the business:

—the estimating budget: to help you bid your work and recover all costs;

—the accounting (or tax) budget: required to meet government and tax regulations;

—the cash flow budget.

The cash flow budget is designed to help you predict cash flow, identify those periods of weaker cash flow, so you can compensate if necessary by means of a loan or increased line of credit.

The estimating budget is developed in 12-month increments, not necessarily a fiscal or calendar year. It can be either, but we can also develop a budget for the immediate next 12 months, starting at any time during the year.

It is easier to prepare an estimating budget parallel to a company's fiscal year—which may be the calendar year—but it is not necessary to do so.

I tell seasonal contractors that it takes two to three seasons to really get your operation under control, to get it running smoothly. Businesses with year-round seasons, such as those in Southern California or Florida, usually take about the same amount of time to achieve the same results. This may seem like a long time, but remember that there will be lots of other things to do while you are trying to implement the estimating system.

Think long term! The process takes time and persistence! **LM**

The author is a green industry business consultant and author of Estimating for Landscape & Irrigation Contractors, published by Smith Huston, Inc., Denver, Co. To order, call (800) 451-4588.

Supers: computerize & categorize!

1) Get a computer! You'll save the cost of it in one year by tracking your own expenses and comparing them to the Profit/Loss sheet put out monthly by your controller. You will be surprised how many items can be coded into your department that don't belong there!

2) Break down your accounts much farther that what the board of directors or owner receives. For example: most clubs have an account number for "Chemicals." Break the "Chemicals" category down into divisions: fungicides; herbicides; insecticides; pond/lake care; rodenticides; soil penetrants; permits.

Be sure you break down your "Manager's Expense" line item into many categories. Smaller dollar amounts in each category will look better to a budget committee and enable you to get more for education, dues, licenses and travel.

Break down your line items to make it easy to answer surveys, and questions from members or supervisors.

3) When you budget "Capital Equipment" expenditures, always budget at "List Price." This will give you room for price increases, and maybe for an unexpected item that may be needed. When it comes time to buy, you can then negotiate prices with your vendors.

I note in my proposal that these prices are list, and should come in 10 to 15 percent lower.

Don't be afraid to ask for all the equipment you might need. If you don't ask for it, you won't get it! Having these items on "Proposed Budgets" leaves a good paper trail when the time comes that you are asked, a fairway mower broke down during the week of the year's biggest tournament.

4) "Proposed Capital Expenses to the Golf Course," or projects to be done in-house should be priced out at 20 to 30 percent higher than expected costs, similar to the profit a contractor would add. This allows for extra expenses that come up in most projects. A contingency of 10 percent should be added to all projects that are to be bid by contractors for the above same reasons. □

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