

**REPORT OF
AD HOC OPERATIONS AND CAPITAL BUDGET COMMITTEE
TO THE HSV BOARD OF DIRECTORS
OCTOBER 4, 2019**

The 2020 operating and capital budget AD HOC Committee was formed in July 2019. It was formed under the authority of Article XII, Section 6 of the Bylaws of Hot Spring Village Property Owners' Association.

Section II of the committee's charter defined the committee's purpose as "To advise, assist and lend expertise to the CFO in preparation of the 2020 operating and capital budgets."

Section V, subsection A stated that "the Committee is not a governing body. As such it shall not independently set or implement policy, issue directives, discipline employees or exercise approval authority."

Section IV of the charter: Duties and Responsibilities stated in the committee was to advise and lend assistance to the CFO in these areas (per the direction of the board, we have also included our recommendations / observations):

1. Compliance with all POA Policies and board directives as they relate to the 2020 budget process.

Recommendations / Observations:

Board directives:

- We did not have exposure to the total process due to the late time of our Committee's involvement, but from what we did observe it appears POA policies and Board directives were followed in the development of the 2020 budget.

- We would like to add in the Police area that a Bidding Policy should be incorporated in the Board Purchasing Policy for projects to include application of internal labor, bid requirements, RFP (Request for Bids) standards, templates, etc.

2. Revenue validation and expense management.

Recommendations / Observations:

Reforecasting:

- A policy be written concerning reforecasting of the projected expenses in the current fiscal year and should be included in each Quarterly financial report.

Revenue Validation:

- The committee found the revenue amounts included in the budget were not in keeping with reasonable expectations of performance. Our consensus is that the revenue amounts in the budget are overly optimistic, particularly in the golf and food and beverage areas.

3. Capital expenditure prioritization, in alignment with CMPAC Operations & Maintenance expenditure plans.

Recommendations / Observations:

Capital Budgeting:

- For items requiring Board approval, each item over the amount delegated to the CEO should be identified and approved separately with a detailed rationale for the expenditure. Justifications for capital expenditures over \$25,000 must include ROI (Return on Investment) calculations and preferably yield a payback in three years or less.
- Detailed Capitalization / Depreciation Policy should be developed. Policy should cover areas such as type of assets, asset life, depreciable term, application of capitalized labor from the staff, etc. POA outside Auditors should be consulted for recommendations in development of this policy.
- Asset depreciation policy must conform to current IRS and GAAP guidelines.

Delegation of Authority (DOA):

- Current DOA should be reviewed to insure the appropriate amount of authority is being delegated for an organization with this size budget.
- Emergency delegation process should be developed and documented to allow for repairs of utilities, actions taken to preserve POA or member properties or to prevent injury or loss of value.

4. Budget presentation and supporting documentation format.

Recommendations / Observations:

Operating budget / forecasting:

- A policy needs to be written concerning reforecasting of the projected expenses in the current fiscal year and it should be included in each quarterly financial report and provided throughout the year.
- Formal budget parameters should be provided to all departments. Parameters should include guidelines for level of operating cost increases or decreases as well as the same for revenue increases and decreases.
- Budgets should be developed from a bottoms-up perspective. Current process is based on expected increases versus the prior year. Each year, the budget process should be based on zero expenditures and the expense levels established by projects, programs and necessary operating expenses.
- Budgets should be established under a limited number of division, the number to be determined.
- Monthly reporting to the Board should follow the format of the budget. Examples were given by the Committee to Staff. 2020 budget presentation does follow much of this recommendation.
- Revenue budget forecasting must always be realistic so the Village has achievable expectations at all times. Stretch goals may be set for the individual managers but such stretch

goals should never be the budgeted revenue expectation.

Payroll / organization structure:

- As noted in recommendations for Operating Budget / Forecasting, it appears the organizational structure makes managing and budgeting more difficult.
- Compensation should be benchmarked against other POA organizations to ensure our payroll costs are appropriate. Compensation in the 2020 budget is 48 percent of the revenue budget and 14.4 percent more than operating expense. This seems to be excessive and further analysis is required.
- Organization structure should be benchmarked to ensure the proper management personnel / employee ratio based on a non-profit organization of our size.

Technology:

- The current technology (spreadsheet based) used for budgeting and forecasting of financial records is outdated and should be upgraded as soon as possible. The software upgrade will ensure a fuller knowledge of Village operations and ensure the Finance function has the proper tools to do their job (accounting, reporting, banking, etc.). There is a potential here to save money on labor and materials which could offset the cost of the technology upgrade.

5. Numeric accuracy and tie-out:

We had limited review of the accuracy and tie-out process. Although we did make observations on certain areas that needed additional analysis.

6. Additional recommendations:

Finance Committee:

- We recommend that a permanent Finance Committee be established. The committee should include property owners, CFO as staff liaison and a Board liaison. The Finance Committee should report directly to the Board. Its responsibilities should include assisting the CFO in areas such as reporting, budgeting, financial policy reviews, technology and any other area where the CFO requires assistance as well as providing reports directly to the Board on any financial matters facing the Village or procedural improvements for financial budgeting and reporting.

Summary

In closing, we believe that during the time this committee was active, it adhered to all the requirements and limitations imposed upon it by its charter. The committee's role was primarily advisory in nature with the key focus areas being those outlined above.

However, due to the limited time involved, the committee report is neither an endorsement or repudiation of the budget process. We appreciate the opportunity to assist on this year's budget process. We enjoyed working with all the staff members with whom we interacted and appreciated them taking the time to answer our questions. All of us believe more in-depth assistance can be provided in both the budget and finance areas which is why we are recommending that a full-time Finance Committee be established.

Thank you for the opportunity to serve on the committee.

Chairman Bud Hallinan, Vice Chairman Wayne Foltz, Secretary Dan Aylward and John Gonzales