The IT Budgeting Process

Problems with IT Budgets

- Organizations of all types struggle with IT budgeting.
- This often happens because the IT team doesn't understand the budgeting process and the finance team doesn't understand IT…..two separate worlds and the gulf

Key Concepts in IT Budgeting

● **Fiscal IT budget** (i.e., those prepared for the CFO):

-- Capital expenditures – consist of large expenses spread over multiple years.

-- Operating Expenses – consist of the annual costs of running the business.

Key Concepts in IT Budgeting (continued)

Capital budgets
IT Expenditures that may be capitalized include:

-- Project development
-- Infrastructure
-- Consulting fees
-- Major technology purchases

Key Concepts in IT Budgeting (continued)

- **Functional IT budgets**

  Used by IT managers as spending plans and are based on:

  -- Operations costs

  -- Strategic investment

Key Concepts in IT Budgeting (continued)

- **Operations costs:**

  -- Costs to "Keep the Lights On".

  -- Includes maintenance costs, computing and peripheral functions, in-house support and outsourced support.

  -- May include operating and capital costs.

Key Concepts in IT Budgeting (continued)

Strategic investment:

-- Consists of "New" technology spending.
-- May include business improvement initiatives, business-enabling initiatives to transform company operations or new technology business opportunity projects.
-- May be classified as capital or operating costs.

- **Cost allocation**:

   -- the process of identifying, aggregating, and assigning **costs** to **cost** objects.

   A **cost** object is any activity or item for which you want to separately measure **costs**. Examples: a research project, a customer, a sales region, and a department

   -- Allocation may be based upon a formula using factors such as size of business unit, prior year spending, or percentage of use of IT services.

   -- May lead to artificiality in allocating development resources.

IT-specific expenditures:

- *Hardware.* This encompasses equipment and other fixed assets, installation costs, maintenance contracts, warranties, etc.
- This is any expenditure that results in ownership of a physical asset or is associated with the continued use and maintenance of such an asset.

IT-specific expenditures:

- ***Software.*** This includes software licenses and support contracts, usually with a set price for a fixed term.
- ***Subscriptions.*** These could be associated with hardware, software, training, cloud computing and managed-service providers.
- Subscriptions can have a fixed or variable price and a fixed or variable term.

IT-specific expenditures:

- ***Services.*** In this group are advisers, consultants, service providers, auditors and legal counsel.
- This item covers direct and indirect cost of services needed to support IT operations and initiatives.

The Importance of Budgets

1. **Fiscal Discipline**

2. **Strategy Implementation**

Fiscal Discipline

- "IT Costs too Much".
- Demonstrating the realities of business finance has become a significant part of IT leadership.
- IT budgets may be used to limit or manage demand.
- Used to hold IT leadership accountable for what it spends.

Strategic Implementation

- Budgets link long-term goals to short-term execution through the allocation of resources.
- Where IT shillings/dollars are spent can impact corporate performance.
- How discretionary IT shillings/dollars are spent impacts project outcomes.
- The budget process reinforces strategic decision making.

Poor IT Budget

- Can cause firms to invest in technology that adds layers of complexity
- Lead to lack of investment in technology that might be critical to operations
- Unintentionally, it may create an infrastructure that is siloed & contributes to overall inefficient processes

Poor IT Budget (continued)

- Can create a disconnect between IT department & all other departments leading to failed technology implementation
- Can lead to purchase of technology that might not be a best fit for the organization

The IT Budget and Planning Process
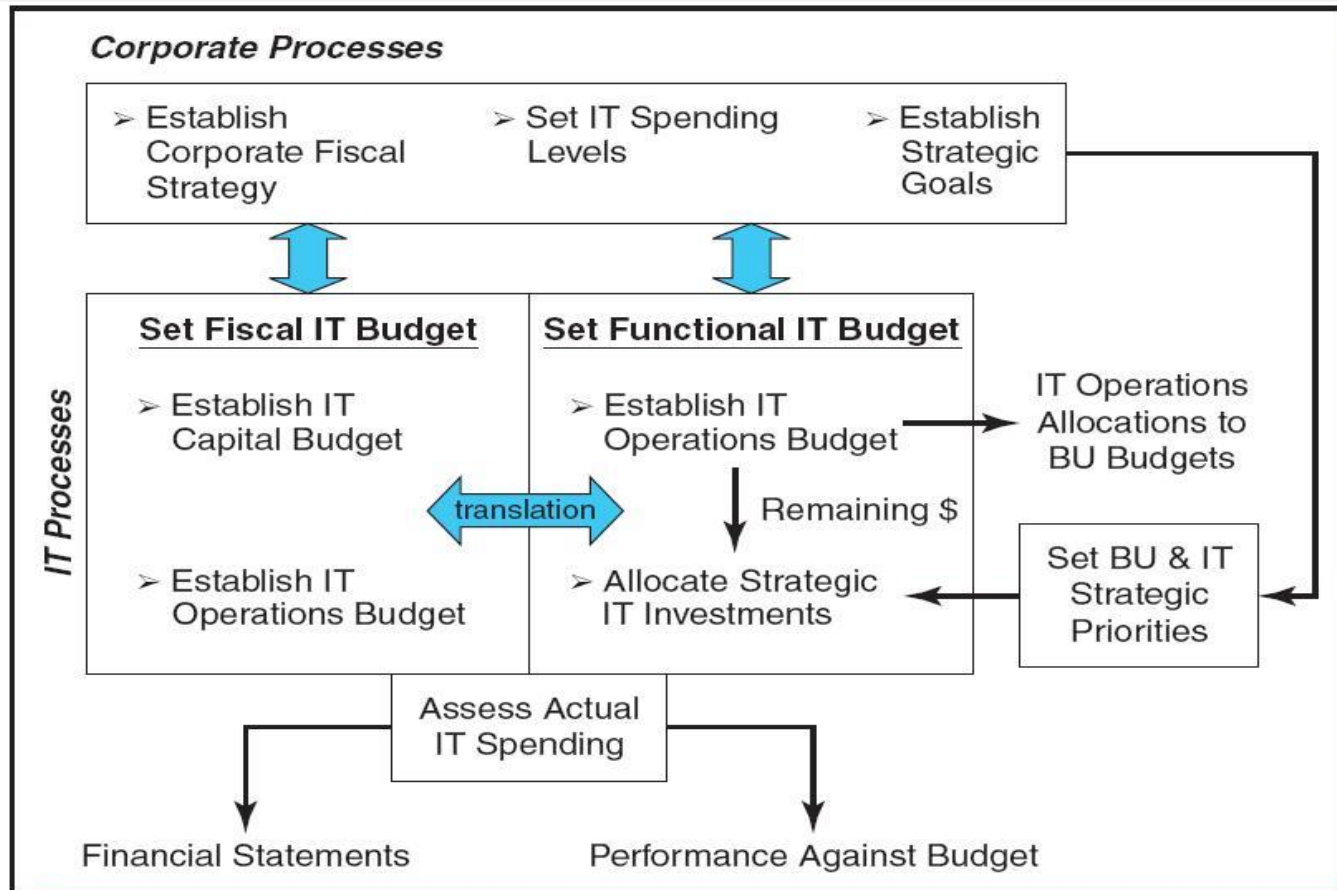
A Generic IT Planning and Budgeting Process

Corporate processes:

-- Establish corporate fiscal policy.

-- Establish strategic goals.

-- Set IT spending levels.

The IT Budget and Planning Process (continued)

Factors that Affect IT Spending Levels

- Number of competitors

- Uncertainty

- Diversification of products and services

- Affordability

- Growth

- Previous year's spending

IT Processes

- **Set functional IT budget** – determine what is spent on IT operations and strategic investment.

- **Set the fiscal IT budget** – transform the functional IT budget into operating and capital spending categories.

IT Budgeting Practices that Deliver Value

1. Appoint an IT finance specialist

2. Use budgeting tools and methodologies

3. Separate operations from innovation

4. Adopt enterprise funding models

5. Adopt rolling budget cycles

IT Budgeting Practices that Deliver Value (continued)

1. **IT finance specialist**:

-- Understand IT costs and drivers.

-- Can manage the translation between the IT functional and fiscal budget.

-- Can develop business cases for new projects.

2.   **Use budgeting tools and methodologies**

--   Link IT Budgets to IT Plans.

--   Link IT Budgets to Corporate Strategic Plans.

--   Link IT Budgets to Resource Strategies.

--   Link IT Budgets to Performance Metrics.

3.   **Separate operations from innovation:**

--   Split operations costs from new project development costs.

4.   **Adopt enterprise funding models:**

--   Used to develop IT operations budgets at an enterprise level.

5. Adopt rolling budget cycles:

-- IT Plans and budgets need updating more than once per year.

-- Quarterly eighteen month rolling plans enable new projects to be funded more quickly.

Conclusion

- The IT budget process can be a critical lynchpin between many different stakeholders: finance, business units, corporate strategy, and IT.

- **IT budgets play a key role in implementing strategy and controlling costs.**