



A SELECTED READING

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The Municipal Budget and Auditing Process

Assembling, preparing and adopting a municipal budget requires about three months of hard work and deliberation. No statutory provision exists which expressly requires all municipalities of the state to establish any particular period for the fiscal year. It should be noted, however, that Section 1-3-4, Code of Alabama 1975, does state that “the fiscal year of the government shall commence on the first day of October and end on the thirtieth day of September”. This fiscal year shall be used for purposes of making appropriations and of financial reporting and shall be uniformly adopted by all departments, institutions, bureaus, boards, commissions and other state agencies.” The Attorney General has ruled that the term “government” is a very comprehensive term and “includes the affairs of a state, community, or society. It is all-inclusive.” AGO to Hon. H. K. Hawthorne, March 12, 1968. Therefore, most of the cities and towns of Alabama begin their fiscal years on October 1. Therefore, budget preparations for the next year should begin in the month of July.

The importance of a budget to municipal administration cannot be overemphasized. A budget is more than a perfunctory, itemized plan of proposed expenditures balanced against estimated revenues for the fiscal period. It is an authorization for the administration to implement municipal policy during the coming year. It is a means of attaining unity in administration by drawing all municipal programs together for overall scrutiny. It is also a means of assuring adequacy of municipal services in the most efficient manner.

Once adopted, a budget is the financial and administrative compass for the executive, administrative and legislative agencies of the municipality. The city or town that is budget-conscious throughout the year produces more services for its revenue, makes more capital improvements, keeps the public more reliably informed and adheres to the policies established by its governing body.

This article will discuss Alabama laws relating to municipal budgets, what a budget should accomplish, who is responsible for the budget, types of budgets, procedures generally followed in preparing a budget, the adoption of the budget and what it means and budget reporting to be followed throughout the fiscal year.

Municipal Budget Laws

Section 11-43-57, Code of Alabama 1975, is as close as Alabama law comes to requiring municipal budgets. That section states that in all cities under the mayor-council form of government, the council shall appropriate the sums necessary for the expenditures of the several city departments. It shall also appropriate the sums necessary for the interest on municipal indebtedness; the council shall not appropriate, in the aggregate, an amount in excess of its annual legally authorized revenue.

This section also permits the council to appropriate the sums necessary for the operation of city departments and for the interest on its bonded and other indebtedness, not exceeding in the aggregate within 10 percent of its estimated revenue. Municipalities may, though, anticipate any expected revenue for the year and contract for temporary loans or use bonds or appropriate anticipated revenue at any time for the current expenses of the city and interest municipal indebtedness.

In an opinion of the Attorney General, found in the April-June *Quarterly Reports of 1940* at page 304, it was held that this section does not apply to municipalities under 2,000 in population. The opinion pointed out that cities at that time were required to submit their budgets to the Division of Local Finance of the State Finance Department under the provisions of Title 55, Sections 151-154, Code of Alabama 1940. These code sections were repealed by the Acts of 1951. Therefore, there is certainly room to doubt that any Alabama cities or towns are actually required by general state law to make an annual budget. However, certain cities are required by local legislation to adopt budgets.

For example, Montgomery is required to have an annual budget by Article 5 of Act No. 618, 1973 Regular Session.

Similarly, Birmingham is required to make an annual budget under the provisions of Article 5 of Act No. 452, 1955 Regular Session, as amended.

Alabama laws which allow the employment of a city manager, found in Section 11-43-20 through 11-43-22, Code of Alabama 1975, do not require that a budget be made and submitted to the governing body. However, the Council-Manager Act, found at Sections 11-43A-1 through 11-43A-52, Code of Alabama 1975, as amended, provides for and requires a budget to be adopted by ordinance in municipalities operating under the council-manager form of government. *See*, Section 11-43A-29, Code of Alabama 1975, as amended. Also, Section 11-44C-1 through 11-44C-93, establishing the form of government for Mobile, requires the adoption of an annual budget. Other municipalities may have similar legislatively-created requirements.

Official Responsibility

While state laws do not require cities and towns to adopt a budget, most municipal governing bodies realize the importance of planning their finances in advance and do operate under a budget. Section 11-43-56, Code of Alabama 1975, gives the council control over the municipal purse strings in mayor-council cities and towns. Some cities and towns require, by ordinance, the preparation of a budget and designate the officer or employee responsible for its preparation and how the budget is to be compiled and submitted. In other municipalities, a budget is prepared and presented to the governing body without formal requirement in keeping with long standing precedent.

Adopting a budget is the responsibility of the municipal governing body. The budget reflects wage and salary policy for the coming year, municipal programs which will be added or deleted, whether services will be increased or reduced, and the amount of planned capital improvements which will be undertaken. Regardless of who prepares the budget, once adopted it becomes the established financial and administrative policy for the coming year.

Who Prepares the Budget?

The responsibility for preparing a budget should rest with the officer who administers the overall municipal operation. This officer is in the best position to prepare the budget and should be given the opportunity to present a program for consideration by the council. Section 11-43-81, Code of Alabama 1975, makes the mayor the chief executive in charge of municipal administration in a mayor-council city or town. Therefore, the mayor should see that a budget is prepared, under his or her direction, for presentation to the council in ample time for consideration and adoption before October 1, or the start of the municipal fiscal year. If the council adopts an ordinance requiring the preparation and submission of a budget, it is doubtful that the mayor can be required to perform this duty because of constitutional issues of separation of powers. The council should require the clerk, treasurer, or comptroller to prepare the budget under the mayor's supervision for presentation to the council at its first meeting in September.

The officer charged with the responsibility of submitting the budget explains and stands up for departmental requests when the governing body considers the budget. Once adopted, it is very important that each member of the governing body support the budget before the public. If a particular cut in service or deleted program is criticized, it can be pointed out that in the council's considered judgment the sacrifice was made for a more necessary function.

Types of Budgets

There are three principal types of budgets – the lump-sum budget, the line-item budget, and the program budget. Actually, the **lump-sum budget** should not be regarded as a budget at all. It merely makes a lump-sum appropriation for expenditures by a department or agency without any restrictions as to what the appropriation is for. It provides no means of oversight during the fiscal year to ensure the various administrative agencies are performing their duties or operating within their appropriations.

The **line-item budget** itemizes the appropriations to be made to each department or agency of the municipality. Generally, it is a detailed summary of all the various expense accounts in each department with an allotment for each. This type of budget is probably used by more cities and towns than either of the other two types. Nevertheless, it leaves much to be desired. The main deficiency with the line-item budget is that it concentrates the governing body's attention on a host of detailed accounts and fails to correlate expenditures with definite programs or services. It serves well because it is an accurate method of determining if various departments and agencies are operating within their detailed appropriations during the year.

The **program budget**, or performance budget, shows the overall cost of major municipal functions, the amount allotted to each organizational unit performing these functions by particular activity, and the detailed objects of expenditures within each unit breakdown.

A program budget reveals departmental objectives, the programs used to achieve these objectives, the volume of work required to accomplish each program and serves as a combined management and fiscal control instrument. The program budget allows a governing body to determine appropriations by programs and services as opposed to concentrating its time on a multitude of meaningless cost items. Program budgets reveal administrative policy as established by the council and present an understandable fiscal picture to the press and public.

The foundation of a proper and satisfactory budget lies in the use of an adequate classification and chart of accounts. When the budget is being prepared, the budget officer should seriously consider whether the accounting system of the municipality facilitates the preparation and execution of budgets for the coming year. If the current system is considered to be inadequate, recommendations for change during the next fiscal year should be offered along with an estimated cost for the change.

Content of the Budget

The budget should contain a budget message from the official who prepared it, followed by a listing of estimated revenues, recommended agency expenditure appropriations, and capital improvement appropriations. The message explains the budget, shows what it does and what it fails to do and denotes any significant changes which occurred over the past year. Six important features of the message are listed below:

- it sets out the policy and general objectives of the city;
- it presents and carries forward the comprehensive theme developed by the budget officer in reviewing and formulating the budget;
- it gives a general statement of the financial status of the city;
- it highlights major program changes, tax increases or decreases and sets out significant data;
- it accurately states problems still remaining to be solved and recommends improvements to the revenue structure; and
- it should be attractive, easy to understand, and brief.

In addition, some budget officers like to include a brief summary of the budget and a table of contents to first allow an overall view, with references for more detailed examination.

Steps to Prepare a Budget

The budget officer should set up a calendar of steps to be followed in preparing a budget. The League recommends the following minimum steps.

First, each department and agency of the city or town should be notified to begin the preparation of budget requests for the coming year. Approximately one month should be allowed to submit budget requests and a deadline date should be set. With this notice, the budget officer gives department heads worksheets and guidelines relating to the information desired and the form in which it is to be submitted. The budget officer should also indicate where statistical and financial data not available in their immediate departments may be obtained.

After receipt of departmental and agency requests, the budget officer should allow approximately 10 days to study and preliminarily assemble the budget. After this step, the officer then schedules hearings with departmental and agency heads for discussion of their requests. These meetings reveal categories where requests need to be cut, omissions which should have been included, duplication of services and ideas for better service at a saving. Furthermore, these conferences give each department head a chance to see the budget instrument in its entirety and to feel that they are included as a member of the team for overall municipal accomplishment.

Following departmental conferences, which may continue for about 10 days, the budget officer should allow approximately 10 days to draft the message and prepare the budget instrument in final form. The budget is presented to the governing body in time to allow one month for study and hearings before final adoption.

Upon presentation, the budget is explained by the budget officer who sits with the council during deliberations. Often, department heads are asked to be present for these conferences to give detailed explanations of activities planned for the coming year in their departments. The governing body may or may not hold a public hearing on the budget. Whether or not information relating to the budget is released to the press before its adoption is a matter which the governing body should decide.

The last step is the adoption of the budget finally decided upon by the governing body. This should be done before the beginning of the fiscal year on October 1.

Most budget officers confer informally with members of the governing body during the preparation process, generally at council committee meetings. In this way, the budget officer learns the feelings of the final arbiters on important points such

as possible salary and wage increases, increased taxes, and program increases before the budget is prepared and submitted. This procedure often eliminates many changes which might otherwise result at a council meeting.

Estimating Revenues

The procedure generally followed in estimating revenues is to list the receipts from each particular revenue source over the last three to five years and project the trend of increase or decrease for the coming year. Caution must be exercised in making such projections where license or tax rates have been changed during the projection period.

A careful check should be made to determine if any state legislation might affect receipts from state-shared revenues for the coming year or if any other factors might affect this source of revenue. If a new license tax is being considered, computations should be made to find out what revenue the tax will be expected to produce. This may be done by contacting a municipality of the same population range. Finally, the budget officer should check with the tax assessor for the assessed valuation of properties within the municipality for the coming year. Ad valorem tax receipts can be computed from these figures. Information relating to auto tag receipts should be obtained from the office of the probate judge.

Budget Reporting

Budgeting is a year-round process. Each month the governing body should receive a report from the officer in charge of finances showing revenues and expenditures during the month and through that date for the year. This report should also show the budgeted figure for such revenues and expenditures. From this report, the governing body should be able to determine if it was accurate in its appropriations, if departments are performing as they should and if it will be necessary to take remedial action.

Municipal Audits

In 2022, the Alabama Legislature passed Act 2022-345, otherwise known as the Municipal Audit Clarification Act, which amended Section 11-43-85. The Act made changes to the frequency of municipal audits depending on the amount of a municipality's annual expenditures. First, in a municipality with annual expenditures of three hundred thousand dollars (\$300,000) or more, the mayor or city manager shall provide for and cause to be made an annual audit of the financial affairs and transaction of all funds and activities of the municipality by an independent public accountant for each fiscal year of the municipality. Nothing has changed here. An annual audit continues to be the requirement for larger municipalities. Second, for municipalities with annual expenditures of less than three hundred dollars (\$300,000), the mayor or city manager shall provide for and cause to be made a biennial (every 2 years) audit of the financial affairs and transactions of all funds and activities of the municipality by an independent public accountant for each fiscal year of the municipality. The audit conducted pursuant to this subdivision shall include each fiscal year since the preceding audit. However, for those municipalities with annual expenditures of less than one hundred thousand dollars (\$100,000), the city council may elect to provide for and direct the mayor city manager to cause to be made, in lieu of the biennial audit, an annual report that complies with procedures established by the Department of Examiners of Public Accounts. The report should include the following:

1. Proof and reconciliation of cash.
2. Confirmation of cash balances.
3. A list of bank balances.
4. A statement of cash receipts and cash disbursements.
5. A statement of compliance with state law.
6. A report of agreed upon procedures.
7. A report of motor fuel excise taxes collected and the distribution and use of those proceeds.
8. Any other procedures established by the Department.

Although Section 11-43-85, as amended in 2022, only requires an annual report conducted in lieu of a biennial audit be submitted to the council at its first meeting after the completion of the report and be spread on the minutes, it is still standard operating procedure for any municipal audit conducted to be submitted to the council at its first meeting after completion of the audit and spread on the minutes. In addition, a municipal audit under section 11-43-85 must be conducted in accordance with generally accepted auditing standards in a format prescribed by the Department of Examiners of Public Accounts. The municipal audit requirements of Section 11-43-85 cannot be waived. AGO 2010-068.

Also, a municipal audit or annual report under section 11-43-85 shall be provided to the Department of Examiners of Public Accounts in accordance with Section 41-5A-12.1, otherwise known as the Municipal Audit Accountability Act.

Section 41-5A-12.1 gives the Examiners the authority to perform an audit of a municipality when fraud or mismanagement of funds is suspected or when the mayor of a municipality does not provide for an audit or examination to be conducted on the municipality as required by law. Further, Section 41-5A-12.1 requires that upon receipt of the final report of the independent audit or examination, the municipality shall provide a copy of the report to the department within 60 days after completion. This information is then placed in a repository established by the Examiners. The department is also charged with providing, on a weekly basis, notice to the public of reports received; and, upon request, provide copies of reports received to the public. It is important that municipalities comply with the provisions of 41-5A-12.1 because unlike in the past, when the law did not provide for penalties for municipal officials who failed secure an audit, the law now provides that if a municipality fails to comply with the reporting requirements, the Department has the authority to assess financial penalties up to \$250 per week against municipal officials or municipal councils for failure or refusal to perform audits or submit audits requested by the Department. These penalties are assessed against individuals personally.

The council's role in the municipal audit is limited. It is the mayor's responsibility to select an independent accounting to perform the audit, not the council's. Section 11-43-85 authorizes the mayor or the city manager to enter into a contract fixing the accountant's fee at a reasonable amount without the approval of the council, however, if annual audits have been made for previous years and were accepted by the council, the mayor may not employ, without the consent of the council, an auditor to re-audit the books of the city for such years. AGO to Hon. E. R. Caldwell, June 15, 1965. If the council is not satisfied with the audit provided by the mayor's auditor, the council may order an additional audit to be made by the auditor of its choice, but this audit does not constitute the official audit required by law to be performed under the direction of the mayor. There is no prohibition against employing the same accountant for successive years, although Acts applicable to some municipalities prohibit hiring the same auditors in some circumstances. Section 11-43-85, as amended, no longer requires the Department of Examiners of Public Accounts to conduct a municipal annual or biennial audit when requested by the mayor; but rather, the mayor is required to employ an independent public accountant to conduct the municipal audit.

Section 36-25-4(a)(7), Code of Alabama 1975, authorizes the Ethics Commission to direct the state director of the Examiners of Public Accounts to audit a municipality.

Conclusion

This article does not attempt to cover every particular facet of the budget and auditing processes because space does not allow it. Items such as public improvement assessments, bonded indebtedness and capital improvement budgeting have not been mentioned. It is hoped that the municipal official has found a few helpful suggestions in the foregoing material. The goal of this article is to emphasize the importance of a budget as a management and policy tool, an aid to be used continuously rather than a financial instrument to be adopted and forgotten.