

**REVIEW OF
NON-GENERAL FUND
REVENUE FORECASTING PROCESS**

INTERIM REPORT



AUDIT SUMMARY

The Commonwealth divides its revenue sources into two broad categories of funds: general funds and non-general funds. General funds are largely the general taxes paid by individuals and businesses. The Governor and General Assembly determine the use of these funds. Conversely, non-general funds represent a variety of revenues sources, which either the Virginia Constitution or legislation has specifically earmarked to fund certain programs or activities.

More than half of the operating budget of the Commonwealth in any given fiscal year is made up of non-general funds. This review focuses on the revenue forecasting process over non-general funds and will have two phases. This first phase report includes our work to gain an understanding of the forecasting process, including the significant types of non-general fund revenues and who does the forecasting. We also surveyed a sample of agencies to gain an understanding of their procedures and compared them to best practices.

While all agencies and universities must develop revenue forecasts for non-general funds as part of the budget development process, there are certain agencies that are central to the process. These agencies include the Department of Planning and Budget, the Department of Taxation, and the State Council for Higher Education in Virginia.

We found that most of the agencies we surveyed said they followed the basic elements of best practices when preparing their non-general fund revenue estimates. While the overall processes appear consistent with established practices, we did identify the following recommendations Planning and Budget as well as the Secretary of Finance should consider to strengthen the non-general fund revenue forecasting process.

- Consider whether the current forecasting process requires change to allow agencies to update their original revenue forecasts during the year as they become aware of changing circumstances.
- Consider implementing a more comprehensive statewide mechanism for monitoring and reporting on estimated and actual non-general fund revenues throughout the year.
- Prepare updated documentation, referred to as a revenue manual, on significant non-general fund revenue sources and the overall forecasting process.
- Consider providing more guidance to agencies on methodologies and best practices to use when forecasting their non-general fund revenues.

As discussed above, this review will include a second phase with a final report issued by January 2008. The second phase of our review will include a more detailed review of forecasting procedures at Planning and Budget and the individual agencies. We will select a sample of agencies and verify they are following the forecasting procedures outlined in this report. The final phase will also include a more detailed analysis of agency estimates and actual revenue collections, and how the budget development process uses this information.

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REVIEW OF NON-GENERAL FUND REVENUE FORECASTING PROCESS

Overview of Non-General Fund Revenues in the Commonwealth's Budget

The Commonwealth divides its revenue sources into two broad categories of funds: general funds and non-general funds. General funds are largely the general taxes paid by individuals and businesses. The Governor and General Assembly determine the use of these funds. Conversely, non-general funds represent a variety of revenues sources, which either the Virginia Constitution or legislation has specifically earmarked to fund certain programs or activities.

Historically, because general funds represent the largest portion of discretionary program and activity funding, the Governor, the General Assembly, and the public have focused their attention on the forecasting and collection of these revenues. However, non-general funds have historically made up more than half of the Commonwealth's operating budget. Non-general funds were about 51 percent of the estimated revenues for the operating budget for fiscal year 2006 and estimates predict that non-general fund revenues will continue to grow

The table below shows the Commonwealth's estimated revenues, broken down into general and non-general sources.

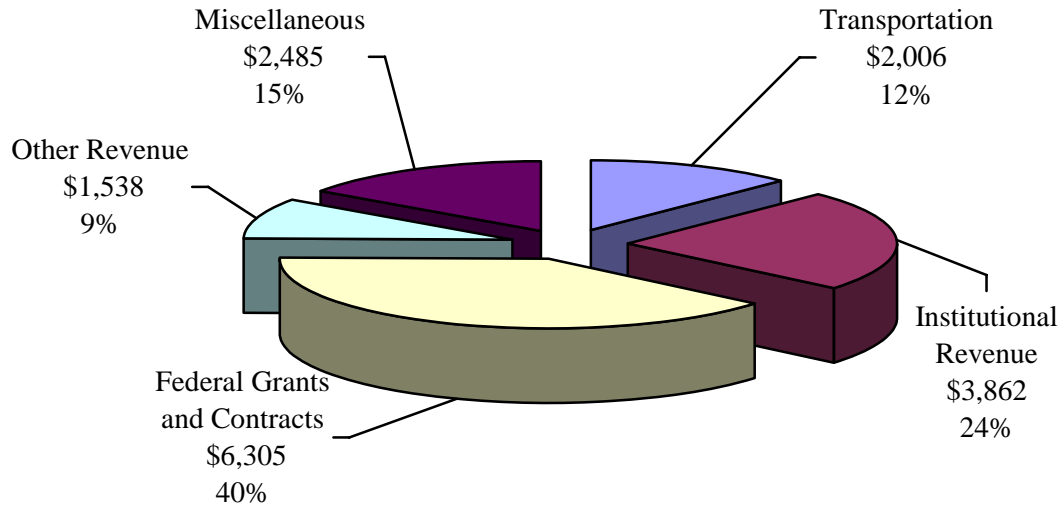
Estimated Operating General and Non-general Fund Revenues, Fiscal Year 2002 through Fiscal Year 2006
(in thousands)

	<u>Fiscal Year</u> <u>2002</u>	<u>Fiscal Year</u> <u>2003</u>	<u>Fiscal Year</u> <u>2004</u>	<u>Fiscal Year</u> <u>2005</u>	<u>Fiscal Year</u> <u>2006</u>
General Fund	\$12,175,845	\$12,204,431	\$12,574,348	\$14,435,652	\$16,052,105
Non-general Fund	<u>12,454,457</u>	<u>13,530,535</u>	<u>14,960,922</u>	<u>16,442,920</u>	<u>16,851,497</u>
Total	<u>\$24,630,302</u>	<u>\$25,734,966</u>	<u>\$27,535,270</u>	<u>\$30,878,572</u>	<u>\$32,903,602</u>

* Figures taken from corresponding Appropriation Acts. General Fund figures taken from the "Total General Fund Resources Available for Appropriation" line; Non-general Fund figures taken from the "Official Revenue Estimates" line.

There are a variety of revenue streams that make up non-general fund revenues, the most significant source being federal grants and contracts. The chart below provides a breakdown of non-general fund revenues into several large categories, illustrating the significance of federal grants and contracts revenue. Federal grants and contracts make up close to 40 percent of non-general fund revenues and fund a variety of programs. For example, these funds support Medicaid services, public education, and foster care.

Breakdown of Non-General Fund Revenues by Category



Numbers shown in Millions. Figures taken from the 2007 Executive Budget Document. Categories have been modified for purposes of this chart. The "Transportation" category includes Motor Vehicle Fuel Tax, Special Highway Tax from Sales Tax, and Motor Vehicle Sales and Use Tax.

The other most significant source of non-general fund revenue is Institutional Revenue, which is largely student tuition and fees, patient revenue and other fees at the University of Virginia Medical Center and public mental health institutions, and some miscellaneous revenues from the correctional facilities and correctional enterprises. The Transportation non-general funds are taxes, fees, debt proceeds for highway construction, and tolls earmarked for various transportation projects. Other Revenue comes from several sources, the most significant is child support enforcement collected by the Department of Social Services and immediately paid to the custodial parent. The Miscellaneous category also includes several sources revenues, including Unemployment Compensation Payroll taxes and Master Tobacco Settlement Agreement funds.

Scope of Our Review

As discussed above, non-general fund revenues constitute a significant portion of the Commonwealth's operating budget and the process for the projection of these revenues and their monitoring is not only important to the budgeting process, but is also an essential internal control function to determine if agencies and institutions are effectively collecting and managing their revenue streams. Agencies and institutions which heavily depend on non-general funds can encounter operating difficulties if they cannot effectively project revenues or cannot collect those revenues to sustain operations. Conversely, agencies which can effectively project revenues, but do not accurately report them, may use this information to fund projects and activities outside of the normal budgetary process by asking for and receiving permission to spend excess collections.

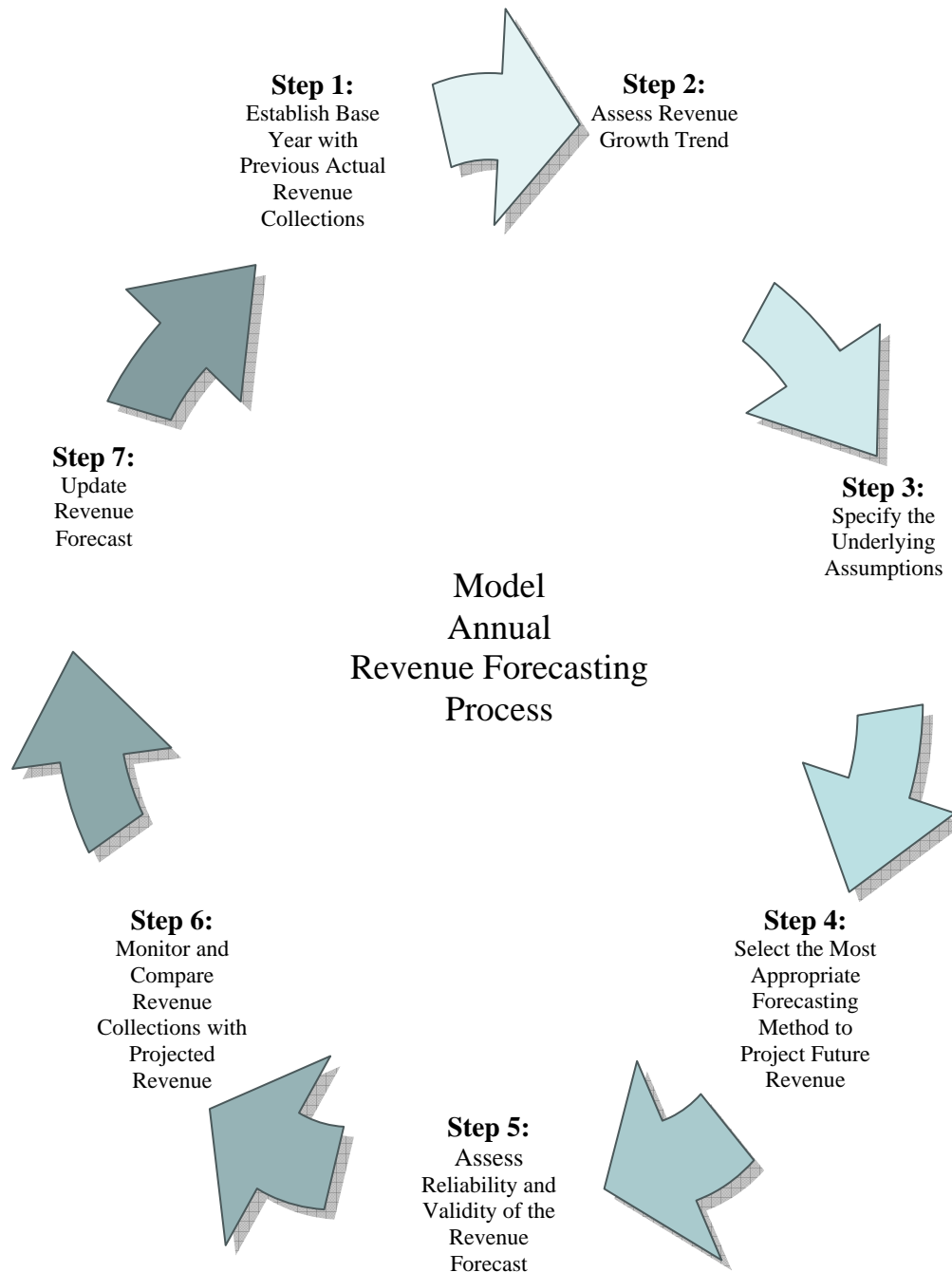
We will review the non-general fund revenue forecasting process in two phases. This interim report discusses our understanding of the process, including the significant types of non-general fund revenues and the agencies and institutions involved in the forecasting process. We also surveyed a sample of agencies to gain an understanding of their procedures and compare them to best practices. The comparison of agency procedures to best practices uses the results of our surveys; therefore, we are relying on this information during this phase of the review.

In the final phase of our review, we will select a sample of agencies and verify their procedures. The final phase will also include a more detailed analysis of agency estimates and actual revenue collections, and how the budget development process uses this information.

Best Practices

We conducted a review of existing literature and guidance on budget development and monitoring practices to determine the best practices for forecasting non-general fund revenues sources. The most comprehensive document we found, *Recommended Budget Practices*, was a joint effort of the National Advisory Council on State and Local Budgeting (NACSLB) with the Government Finance Officers Association (GFOA). The intent of this document was to serve as a model set of best practices.

The following diagram outlines the ideal budget process for any governmental unit. We provide the diagram, since the process whether for the budget as a whole or of a segment, such as non-general fund revenues, is the same.



This portion of the review focused on the largest categories of non-general fund revenues and included the following revenues.

- Motor Vehicle Fuel Tax
- Special Highway Tax from Sales Tax
- Motor Vehicle Sales and Use Tax
- Other Taxes, and Rights and Privileges Unemployment Compensation Payroll Tax
- Sales of Property and Commodities
- Institutional Revenue
- Federal Grants and Contracts
- Other Revenue.

Based upon an analysis of the agencies and institutions with the highest collections of these revenue sources, we selected eight agencies and four universities for review. Below are the agencies and institutions in our survey.

Agencies

- Department of Alcohol and Beverage Control
- Department of Education
- Department of Health
- Department of Medical Assistance Services
- Department of Social Services
- Department of Transportation
- University of Virginia Medical Center
- Virginia Employment Commission

Universities

- University of Virginia
- Virginia Polytechnic Institute and State University
- George Mason University
- Virginia Commonwealth University

For each of the agencies and institutions, we administrated a standardized survey, which was used to determine how their practices compared to the best practices noted above. We also sought to determine the following.

- If the instructions developed by the Department of Planning and Budget (Planning and Budget) and provided to agencies for the development of the individual agencies' non-general fund revenue estimates were deemed sufficient to facilitate the preparation of the estimates;
- If there were any specific recommendations or ideas that were identified by the agencies in relation to the preparation of the non-general fund revenue forecast for the Commonwealth; and

- The extent to which tuition and fees contribute to the development of the budget for colleges and universities, and to determine if State Council of Higher Education for Virginia's (SCHEV) role in the tuition enrollment target projections was satisfactory and sufficient to facilitate the development of an accurate enrollment target projection.

Non-General Fund Revenue Forecasting Process

As discussed already, more than half of the Commonwealth's operating budget is non-general funds. Given the impact of these funds on the Commonwealth's budget, the forecasting process for these funds is a critical part of the budget development process. The forecasting process for these funds involves multiple agencies, and spans several months during the budget development process. There are several central agencies that are critical to the process, Planning and Budget, the Department of Taxation (Tax) and the SCHEV.

Planning and Budget provides agencies with annual instructions for submitting the non-general fund revenue forecasts as part of the budget development process. Section 2.2 – 1503.1 of the Code of Virginia requires the Governor's biennial budget submission include non-general fund revenue estimates, and forecasted estimates for an additional four years. This requirement means that agencies are preparing a six-year estimate of non-general fund revenues annually.

Section 4-1.04 3c of Chapter 951 of the Appropriation Act also states that each agency and institution was to develop a "reasonable estimate" of non-general fund revenues, which Planning and Budget must review as part of the budget development process. Planning and Budget staff review the estimates and compile these as part of the budget development process for the Governor's budget proposal each December.

Another agency critical to the process of non-general revenue estimation is Tax. Tax generates non-general fund revenue estimates for some specific taxes, most of which relate to Transportation. Tax undertakes this process in conjunction with the Governor's Advisory Council on Revenue Estimates. Using econometric methodologies, Tax develops a revenue estimate that considers leading economic indicators such as demographic and wage information and trends, and provides the Governor's Advisory Board of Economists both its underlying assumptions and estimated revenues for their review and comment. After considering the Board comments, Tax refines the assumptions and estimates, and then provides the information to the appropriate agencies and Planning and Budget for inclusion in the Governor's budget proposal.

Finally, a third primary agency in the development of non-general fund revenue estimates is SCHEV. One of the primary sources of funding for colleges and universities is the collection of tuition and fees. One of the driving forces in the preparation of a particular college or university's budget is the preparation of enrollment target projections, which then serve as the primary basis for the development of the institution's budget. SCHEV's role for Virginia's colleges and universities is similar in some respects to that of Planning and Budget. Colleges and universities will prepare an estimate of their projected enrollment targets, and SCHEV will then report total projected enrollment targets for the Commonwealth's public institutions as a whole. Colleges and universities also report estimates of their non-general fund revenues to Planning and Budget for inclusion in the Governor's Executive Budget Document prepared annually.

Once completed, the non-general fund revenue forecast, along with the general fund revenue forecast, provide the basis for appropriations recommended in the Governor's budget proposal. The Executive Budget Document includes detailed information on the make up of the non-general fund projection as well as

estimated and actual information from the prior year. Planning and Budget prepares this document annually and it is a companion document to the Governor's introduced budget.

The table below comes from the Executive Budget Document and shows the fiscal year 2006 non-general fund revenue projections for three years as it appeared in each budget bill and the actual amount collected for fiscal year 2006. Revenue projections undergo annual revision as part of the budget development process. The original estimate for fiscal year 2006 appeared in the 2004 Executive Budget Document with revisions in 2005 and again in 2006.

This chart illustrates several factors that are consistent with revenue forecasting. First, certain revenue sources are more volatile than others, and thus providing accurate forecasting in the out years of a forecast is an inherently challenging task. Second, in general, the closer a forecast is to the actual time of revenue collections, the more reliable and valid the forecast becomes.

As shown in the final two rows of the chart, the non-general fund revenue projections from the Executive Budget Document and the final Appropriation Act will differ slightly. These changes reflect legislative adjustments made during the General Assembly session in the development of an Appropriation Act. These amounts represent the final approved non-general fund forecasted revenues for the Commonwealth's agencies and universities. Actual non-general fund revenues collected were approximately \$650 million less than the most recent forecast, with most of this difference occurring in federal grants and contracts.

Summary of Estimated and Actual Non-General Fund Revenues
Fiscal Year 2006
(in millions)

<u>Non-general Fund Revenue Category</u>	<u>Original Estimate 2004</u>	<u>Revised Estimate 2005</u>	<u>Revised Estimate 2006</u>	<u>Actual Revenue</u>
Motor vehicle fuel tax	\$ 950.2	\$ 957.1	\$ 926.8	\$ 931.2
Unemployment compensation payroll tax	616.9	581.8	581.8	535.9
Special highway tax from sales tax	467.5	463.4	479.8	476.3
Motor vehicle sales and use tax	612.5	625.1	610.5	598.5
Other taxes	237.7	81.6	326.2	302.0
Rights and privileges	706.9	769.1	837.7	756.1
Sales of property and commodities	478.9	498.9	503.5	664.8
Institutional revenue	3,531.5	3,683.9	3,812.8	3,862.1
Interest, dividends, and rents	84.3	67.2	87.2	136.1
Federal grants and contracts	6,217.1	7,029.8	7,121.5	6,304.8
Master tobacco settlement agreement funds	76.7	127.8	99.3	89.7
Other revenue	1,856.2	1,805.9	1,454.8	1,538.1
Public education SOQ/local real estate property tax relief *	n/a	221.3	n/a	n/a
Taxes on tobacco products *	<u>n/a</u>	<u>210.5</u>	<u>n/a</u>	<u>n/a</u>
Total estimated revenue - introduced budget	<u>\$ 15,836.4</u>	<u>\$ 17,123.4</u>	<u>\$ 16,841.9</u>	
Total estimated revenue - appropriation act	<u>\$ 16,009.5</u>	<u>\$ 17,215.7</u>	<u>\$ 16,851.5</u>	
Total revenues collected				<u>\$16,195.5</u>

* Public Ed. SOQ/Local Real Estate Property Tax Relief” and “Taxes on Tobacco Products”, were included as part of Governor Warner’s budget reform proposal in 2004. These revenues have subsequently been absorbed into other funding categories.

The categories of non-general fund revenues in the Executive Budget Document represent various revenues sources from many agencies. There are also many different agencies involved in the revenue forecasting process. The chart below looks at the major non-general fund revenue categories from the Executive Budget Document. For each category, we have identified the agencies that are primarily involved in the collection of the actual revenue and the agencies identified in the forecasting for the revenues.

Non-general Fund Revenue Categories	Primary Agencies Involved in Collecting	Entity Responsible for Forecasting
Motor vehicle fuel tax	Department of Motor Vehicles (DMV), and Virginia Department of Transportation (VDOT)	Department of Taxation (Tax)
Unemployment compensation payroll tax	Virginia Employment Commission (VEC)	VEC
Special highway tax from sales tax	VDOT, and the Department of Rail and Public Transportation	Tax
Motor vehicle sales and use tax	DMV and VDOT	Tax
Other taxes	Dept. of Education (Direct Aid), and Department of Medical Assistance Services (DMAS)	Tax
Rights and privileges	DMV and VDOT	Tax
Sales of property and commodities	Department of Alcohol and Beverage Control (ABC)	ABC
Institutional revenue	Colleges, universities, and other state institutions	Colleges, universities, and other state institutions
Interests, dividends, and rents	VEC, VDOT, and transfers from the Department of Accounts	Individual agencies
Federal grants and contracts	DMAS, Department of Education, Department of Social Services, VDOT	Individual agencies
Master tobacco settlement agreement funds	Virginia Tobacco Settlement Foundation	Virginia Tobacco Settlement Foundation
Other revenue	Department of Social Services, DMAS, and Department of the Treasury	Individual agencies

As mentioned previously, Tax plays a significant role in the development of the Commonwealth's non-general fund revenue estimation process. As shown above, Tax solely prepares five of the twelve non-general fund revenue categories reported in the Executive Budget Document. These five categories combined made up nearly \$3.1 billion (or almost 19 percent) of actual non-general fund revenues collected by the Commonwealth in fiscal year 2006. The most significant of the non-general fund revenues are the Highway Maintenance and Operating Fund and the Commonwealth Transportation Trust Fund, which Tax estimated at approximately \$2.4 billion for fiscal year 2006.

Tax's forecasting process for its non-general fund revenues estimates differs from other agencies and universities in several distinct ways. Tax, in conjunction with the Secretary of Finance, prepares revenue estimates using complex statistical econometric modeling. The Governor's Advisory Council on Revenue Estimate reviews the economic assumptions used to prepare the revenue estimates. Tax presents these estimates to the Governor's Board of Economic Advisors for additional review before using them in the development of the Executive Budget Document. Ultimately, these estimates go to Planning and Budget for inclusion in the budget.

We reviewed documentation provided by Tax to understand the process of developing the estimates for these non-general fund categories. Global Insight, a private economic and financial analysis firm, developed the economic assumptions for the official revenue forecasts for fiscal year 2006. Global Insight prepared a standard economic forecast and alternate forecast to allow for the possibility of more than one perspective. Tax developed their forecasts using these outlooks.

After reviewing Tax's processes for the development of their non-general fund revenue estimates, we found that the process used for the estimates prepared by Tax is inherently more transparent than that of most of the other sources of non-general fund revenues. This transparency occurs because Tax uses many of the same processes and techniques to estimate general fund revenues. Additionally, the Secretary of Finance reports some of these non-general funds in the monthly revenue reports given to the General Assembly.

After final adoption of the Appropriation Act, Planning and Budget and the Department of Accounts enter the non-general fund revenue estimates, along with the rest of the budgeted amounts, into the Commonwealth Accounting and Reporting System (CARS). Once the budget has been approved, agencies can request additional non-general funds if circumstances change. For example, increases can occur because either the amount actually collected differed from estimates or for changes such as action by the U.S. Congress providing changes in a federal revenue source. In 2006, these appropriation increases totaled more than \$1 billion and represented approved adjustments by Planning and Budget. Although Planning and Budget collects the information, there is no revision of the agency's revenue estimate either in Planning and Budget's database or in the CARS. The Commonwealth only updates agency revenue estimates annually as part of the budget development process.

The current process for monitoring the non-general fund revenue forecasts against actual collections occurs primarily at the individual agency level. There is no statewide process to monitor and report these revenues against the forecasts as part of the budget development process. The Secretary of Finance monitors and reports on actual revenue collections on a monthly basis; however, this reporting focuses primarily on general fund revenue collections. The only non-general fund revenue collections included in the monthly report process are related to the various transportation revenues.

RECOMMENDATIONS FOR MANAGEMENT

We noted several issues and processes we believe could strengthen the overall process of non-general fund revenue forecasting. Some of these findings are similar to findings of the Joint Legislative Audit and Review Commission reported in the early 1990s in a review of the Executive Budget Process.

- Planning and Budget and the Secretary of Finance should consider whether the current forecasting process requires change to allow agencies to update their original revenue forecasts during the year as they become aware of changing circumstances. There is no process to allow agencies or universities to update their original revenue estimates during the year and there are times when agencies need to increase or decrease their original estimates for a change in circumstances. In a related issue, agencies do have the capability to increase appropriations if they collect more funds than estimated; however, there is no corresponding adjustment to the revenue estimate to support the change. This issue has resulted in some financial reporting issues for non-general funds in the Commonwealth's Comprehensive Annual Financial Report.
- Planning and Budget and the Secretary of Finance should consider implementing a more comprehensive statewide mechanism for monitoring and reporting on estimated and actual non-general fund revenues throughout the year. There is no process in place to monitor or report on estimated and actual non-general fund revenue collections during the year at a statewide level. The only monitoring of the non-general fund revenue estimates occurs at the agency level. The only statewide reporting on all non-general fund revenues occurs after the end of the fiscal year, as part of the Governor's proposed budget in December.
- Planning and Budget and the Secretary of Finance should prepare updated documentation, referred to as a revenue manual, on significant non-general fund revenue sources and the overall forecasting process to promote continuity of operations in the event of employee turnover. Currently, there is no up-to-date documentation at a statewide level discussing the different non-general fund revenues and detailed information concerning their sources and methods of collection.

The National Advisory Council on State and Local Budgeting (NACSLB), in conjunction with the Government Finance Officers Association (GFOA), developed a set of best practices in its *Recommended Budget Practices*. Best practices include the preparation and maintenance of a revenue manual, which details the sources of all revenues for an entity. This practice ensures there is a central source of critical budgetary information regarding major revenues that staff can quickly access in the event of employee turnover, as well as to promote further understanding about the nature of a government's sources of revenue.

- Planning and Budget issues annual instructions to agencies on forecasting for non-general fund revenues, but these instructions contain very little guidance on methodologies or best practices that agencies should or could use in the forecasting process. During our correspondence with the selected agencies and universities, we noted that general forecasting best practices and guidance on appropriate methodologies could help facilitate a better and more consistent approach to the development of non-general fund revenue estimates. We recommend Planning and Budget consider whether this type of guidance would be useful for agencies, and would promote consistency in some cases.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

**Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218**

March 25, 2007

The Honorable Timothy M. Kaine
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Thomas K. Norment
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

Gentlemen:

We have completed the interim phase in our **Review of the Non-General Fund Revenue Forecasting Process**. We conducted our review in accordance with standards for performance audits set forth in the Government Auditing Standards issued by the Comptroller General of the United States.

Purpose

Our review of the non-general fund revenue forecasting process will be completed in two phases. This interim report includes our work done in the first phase of this review. Our objectives in this phase were to gain an understanding of the process, including the significant types of non-general fund revenues and who was involved in the forecasting process, and to survey a sample of agencies to gain an understanding of their procedures and compare them to best practices.

Scope and Methodology

In gaining an understanding of the non-general fund revenue forecasting process, we identified the major revenue sources that make up non-general funds. We also identified the primary agencies involved in the development of the non-general fund revenue estimates, and compared the methodologies and practices of a sample of agencies against best practices for revenue forecasting. We have included more detailed information on the scope of our review in the section entitled "Scope of our Review."

Results of Review

Overall, based on our survey results, we found the forecasting procedures at the selected agencies followed the basic elements of recommended forecasting practices. As was expected, certain agencies had a more complex and sophisticated level of applied forecasting methodologies, but the methodologies identified and utilized by the agencies appeared to be reasonable in relation to their collection and use of non-general fund revenues. All of the agencies surveyed exhibited a basic understanding of the proper elements of a non-general fund revenue forecasting process.

We did identify recommendations for Planning and Budget and the Secretary of Finance to consider to strengthen the process. These are reported in the section entitled “Recommendations for Management.”

Phase 2 of Review

The second phase of this review will build on the understanding of the process we developed in the initial phase of our review. We will review the following areas with an expected final report by January 2008.

- Review the role of Planning and Budget and their statutory responsibilities over the non-general fund revenue forecasting.
- Evaluate and verify revenue forecasting procedures at individual agencies through in-depth review of their 2006 revenue forecasts.

Exit Conference

We discussed this report with the Secretary of Finance and Planning and Budget management on May 10, 2007.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

LCW/sks



COMMONWEALTH of VIRGINIA
Department of Planning and Budget

Richard D. Brown
Director

1111 E. Broad St., Room 5040
Richmond, VA. 23219

May 21, 2007

Mr. Walter J. Kucharski
Auditor of Public Accounts
P. O. Box 1295
Richmond, Virginia 23218

Dear Walt:

Thank you for the chance to review your interim report entitled "Review of Non-General Fund Revenue Forecasting Process." It is evident from your research and findings that you recognize the complexities associated with forecasting the numerous sources of nongeneral fund revenue included in this exercise and that you acknowledge the extensive effort that the Department of Planning and Budget (DPB) allocates to this endeavor. The fact that we presently cover the basics, however, does not mean that the process cannot be improved and you offer four specific recommendations for this purpose.

Two of these recommendations deal with processes or tasks that are internal to DPB. You recommend that:

- DPB update its documentation, referred to as a revenue manual, on significant nongeneral fund resources and the overall forecasting process, and
- DPB consider providing more guidance to agencies on methodologies and best practices so that agencies can use this information when forecasting their nongeneral fund revenues.

It's DPB's intent to begin to act on both of these recommendations in the next budget cycle. The so-called revenue manual we currently have in use needs revision. DPB will update it to more accurately reflect current priorities and make the revised manual available to budget analysts. The instructions for forecasting nongeneral fund revenues we presently provide to agencies will also be revised to include more information on methodologies and best practices with regard to revenue forecasting and budgeting. Since your interim report cites some existing sources of such information, DPB will further consult with APA staff in an effort to be more informative and helpful to state agencies on this front.

The other two recommendations in your report are not applicable solely to DPB. Rather, they aim at the overall process of monitoring and reporting for the various sources of nongeneral fund revenue collected statewide by numerous state agencies. Here you recommend, as a matter of policy, the state (through the lead of the Secretary of Finance) consider the following:

- alter the current forecasting process to allow state agencies to update their original projections of nongeneral fund revenue during the course of the year as they become aware of changed circumstances, and
- implement a more comprehensive statewide mechanism for monitoring and reporting on estimated and actual nongeneral fund revenues throughout the year.

With respect to these issues, the Office of the Secretary of Finance and DPB believe that most of the inherent difficulties associated with efforts to monitor and report on nongeneral fund revenues stems from the fact that these sources are very numerous and that the revenue collection activities for these sources are performed by many state agencies. This characteristic complicates reporting in the absence of systematic and enterprise-wide data gathering efforts. This situation is vastly different from that of the general fund where three sources of revenue (individual income, corporate income, and the general sales tax) constitute nearly 90 percent of all the collections and where the Department of Taxation is, for the most part, responsible for the collection of all three of these sources.

Accordingly, major improvements in the way we monitor and report on nongeneral fund revenues are not going to fall on a single state agency (like DPB), per se, as much as they are on the overall statewide reporting system that we use to gather nongeneral fund revenue projection and collection data from various agencies that have such data. In other words, such improvements must systematically address the manner in how nongeneral fund revenue data is kept within the framework of the statewide financial system. Only then, will we be able to expand our reporting capabilities both in terms of the quality of reports and the quantity of reports provided throughout the year.

Given the nature of this challenge, the Office of the Secretary of Finance and the Department of Planning and Budget suggest that your recommendations in this area be addressed within the context of the Virginia Enterprise Applications Program (VEAP) currently underway to revamp the accounting, budgeting, and financial reporting systems in the Commonwealth. We strongly believe that the VEAP is the appropriate entity for this purpose as it is currently evaluating the need to reengineer the Commonwealth's business processes. Therefore, the Secretary of Finance will refer this issue to the VEAP and ask it to examine your recommendation within the overall scope of its work on the state's financial systems. Moreover, since the APA has advisory representation on many of the work groups associated with the VEAP effort, it should be easier for you to keep informed about the progress of your recommendations as well as to evaluate their feasibility within a more systematic approach to improve financial reporting.

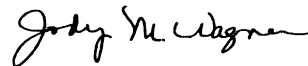
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May 21, 2007

Again, thank you for the opportunity to review your well-researched report on this very complex issue.

Sincerely,



Richard D. Brown



Jody M. Wagner
Secretary of Finance

RDB/tcm

c: The Honorable William H. Leighty