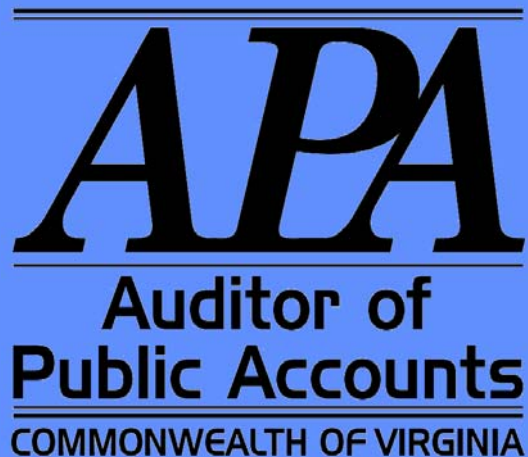


**REVIEW OF NON-GENERAL FUND
REVENUE FORECASTING PROCESS**

FINAL REPORT



AUDIT SUMMARY

The Commonwealth's budget includes non-general fund revenues which fund approximately half of the total budget. We found a general lack of review in the forecasting and monitoring of these funds at a statewide level. In addition, current budgeting practices result in a distortion of at least \$2 billion (8 percent) of the fiscal year 2007 revenue estimate. These practices include potentially showing some estimated Medicaid funding for services provided by state agencies twice, and including collections for others in the revenue estimate.

Non-general funds represent a variety of collections, many of which specifically fund certain programs or activities. Many of the forecasting and reporting processes in place for general funds are not in place for non-general funds, and we recommend improvements in the forecasting and monitoring processes for these revenues. The Commonwealth cannot effectively fund its programs and services without a thorough understanding of its revenue structure, both general and non-general fund sources.

We analyzed estimated and actual non-general fund revenues at both the category and agency level for fiscal year 2007. Based on the results of our review, the Commonwealth needs to make significant improvements in the forecasting and monitoring processes over these revenues and our report includes the following recommendations:

- ✓ *Planning and Budget and the Secretary of Finance should develop a quarterly statewide mechanism to monitor and report on actual non-general fund revenue collections in comparison to the estimates in the approved budget. Currently, there is no mechanism in place to provide comprehensive statewide reporting to the legislature or to the public.*
- ✓ *Planning and Budget and the Secretary of Finance need to analyze the non-general fund revenue portfolio to determine which sources represent actual revenue and how best to present these sources in the budget. We found approximately \$1 billion in estimated collections that really are collections for others. In addition, we found another \$1 billion in Medicaid funding that may appear twice in the revenue estimate. In both cases, these revenue streams support appropriations in the budget, but current budget practices distort the user's ability to understand exactly what resources are available to fund programs and services. Planning and Budget and the Secretary of Finance should analyze revenues and evaluate alternative presentations in the budget that would more clearly differentiate the different types of collections of non-general funds.*
- ✓ *Individual agencies and Planning and Budget should strengthen their procedures over the estimating of non-general fund revenues. We found a number of errors in the non-general fund revenue information currently accumulated and reported in the Executive Budget Document. It is important for agencies to understand the budgeting as well as the accounting for their various revenue streams so they can properly develop revenue estimates for Planning and Budget.*

In addition, it is important for Planning and Budget staff to understand the budgeting and accounting for the revenue streams to ensure the information they are compiling and reporting is comparable and accurate. Planning and Budget needs to dedicate adequate resources to this area so they can comply with their statutory requirement to verify the accuracy of agency estimates.

- ✓ *Planning and Budget does not have adequate documentation to support their current procedures for accumulating and reporting non-general fund revenue information in the Executive Budget Document. In considering this recommendation, the Secretary of Finance and the Director of Planning and Budget must consider whether or not Planning and Budget has adequate resources to meet their other statutory requirements.*

- TABLE OF CONTENTS -

	<u>Pages</u>
AUDIT SUMMARY	
REVIEW OF NON-GENERAL FUND REVENUE FORECASTING PROCESS	
Approach to Our Review	1-2
Overview of Non-general Fund Revenues in the Commonwealth's Budget	2
Non-general Fund Revenue Forecasting Process	3-4
Analysis of Fiscal Year 2007 Estimated and Actual Revenues	4-12
Other Issues	13-14
TRANSMITTAL LETTER	
Review Objectives, Scope and Methodology	15
Results of Review	16
Exit Conference and Report Distribution	16
APPENDIX A – Model Revenue Forecasting Process	17
APPENDIX B - Internal Medicaid Payments for Services	18
RESPONSE TO REPORT	19-20

Review of Non-general Fund Revenue Forecasting Process

Approach to Our Review

Our review of the non-general fund revenue forecasting process had two phases; each is discussed below. In the first phase, we focused on gaining an understanding of the forecasting process, and we issued an interim report in May 2007. During the completion of this report, we reviewed the status of the phase one recommendations.

Phase One

Findings

During the first phase, we gained an overall understanding of the revenue forecasting process for both individual agencies and universities, and also at the statewide level. We surveyed agencies and universities to determine their compliance with established best practices for revenue forecasting. We found that while the overall processes appeared consistent with established practices, there were items for Planning and Budget as well as the Secretary of Finance to consider which would strengthen the non-general fund revenue forecasting process.

Recommendations

These recommendations were as follows:

1. 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.
2. Consider implementing a more comprehensive statewide mechanism for monitoring and reporting on estimated and actual non-general fund revenues throughout the year.
3. Prepare updated documentation, referred to as a revenue manual, on significant non-general fund revenue sources and the overall forecasting process.
4. Consider providing more guidance to agencies on methodologies and best practices to use when forecasting their non-general fund revenues.

Follow up

In their response to our interim report, Planning and Budget stated the first two recommendations were complex statewide issues, which they planned to address within the Virginia Enterprise Applications Project (VEAP) project, which will revamp the accounting, budgeting, and financial reporting systems for the Commonwealth. Planning and Budget also responded that they intended to begin addressing the last two recommendations as part of the next budget development cycle. Currently, no action has been taken on the first three recommendations.

Planning and Budget has taken some action on our fourth recommendation. We found that Planning and Budget added narrative to include recommended best practices and general guidelines for appropriate methodologies for revenue estimates in its "Instructions for Completing the Six Year Non-general Fund Revenue Estimates" document for the fiscal 2008. This document serves as the primary instructional guide for agencies and universities during the development of their non-general fund revenue forecast. Based on this follow up, we have repeated some of the recommendations from the interim report in this report.

Phase Two

In this second phase, we analyzed estimated and actual non-general fund revenues at both the category and agency level based on information reported by Planning and Budget. Our review focused primarily on the non-general funds used to support the operating budget. Planning and Budget accumulates estimated revenue information and summarizes this in twelve broad categories that are included in the Executive Budget Document. We prepared an analysis of estimated and actual revenue for fiscal year 2007 based on these twelve categories. Our analysis was prepared based on information reported by Planning and Budget in the Executive Budget Documents from December 2006 and December 2007.

We analyzed this information and sought to identify the causes of any significant variances between the estimated and actual collections. The report identifies and describes the categories in detail later. After identifying those categories with significant variances, we determined the primary agencies or universities that contributed significantly to the variance. We then contacted the agency to determine the nature and extent of the variance, and to determine the reason for the variance and whether this variation occurred outside the agency or institution's ability to predict the change. We include our analysis and findings in the section entitled "*Analysis of Fiscal Year 2007 Non-General Fund Revenues.*"

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

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 roughly just more than half of the Commonwealth's operating budget. Non-general funds were about 50 percent of the estimated revenues for the operating budget for fiscal year 2007, and estimates predict that non-general fund revenues will continue to grow. The table below shows the Commonwealth's estimated revenues, broken out into general and non-general fund revenue sources.

Estimated Operating General and Non-general Fund Revenues, FY 2004 -FY 2008
(in thousands)

	<u>FY 2004</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>
General Fund	\$ 12,574,348	\$ 14,435,652	\$ 16,052,105	\$ 18,259,907	\$ 17,321,001
Non-general Fund	<u>14,960,922</u>	<u>16,442,920</u>	<u>16,851,497</u>	<u>18,240,532</u>	<u>18,691,824</u>
Total	\$27,535,270	\$30,878,572	\$32,903,602	\$36,500,439	\$36,012,825

* 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.

As illustrated in the chart above, non-general funds typically comprise more than half of the Commonwealth's operating budget during the course of any given fiscal year. Non-general funds come from a variety of sources, ranging from fees for certain services to federal funds to support federally mandated programs such as Medicaid. The structure and function of each of the non-general funds depends upon a variety of factors, including the agency collecting the revenues, the use of the revenues, and the original source of the revenues.

Non-general Fund Revenue Forecasting Process

Our interim report discussed the forecasting process in detail; this report will summarize the process. As part of the annual budget development process, individual agencies and universities prepare estimates of their non-general fund revenue sources. The Code of Virginia and the Appropriation Act direct each state agency and institution to provide reasonable estimates of non-general fund revenues. The sophistication of the forecasting process varies from agency to agency, and is largely dependent upon the types of revenues that the agency collects. In certain cases, agencies rely on other agencies to prepare their revenue estimates, such as the Department of Taxation (Tax). Tax prepares revenue estimates for several of the large non-general fund revenue items, including several transportation revenues streams.

Annually, Planning and Budget develops instructions for agencies on preparing and submitting their non-general fund revenue estimates during budget development. These instructions focus on the mechanics of submitting the information to Planning and Budget, and do not provide substantive guidance to the agencies on methodologies for estimating various revenue types. After preparing and forwarding the non-general fund revenue estimates to Planning and Budget, Planning and Budget analysts perform a cursory review of the estimates as part of budget development. Planning and Budget staff then compile the non-general fund estimates for all Commonwealth agencies and institutions, and prepare a statewide estimate for non-general fund revenue. This estimate, along with the General Fund revenue estimate, provides the basis for the Governor's proposed budget. The Governor's Executive Budget Document, which is a companion document to the Budget Bill, contains more information on the estimate broken down into eleven major categories.

The proposed budget is subject to review and amendment by the General Assembly. During the course of the session, the General Assembly will typically amend the non-general fund revenue forecast. After finalizing the Appropriation Act, Planning and Budget compiles the final non-general fund revenue forecast and forwards the information to the Department of Accounts (Accounts). Accounts records the revenue estimate in the Commonwealth Accounting and Reporting System (CARS) for each respective agency and university, by revenue source. Accounts uses some of this information to report budget and actual information as part of the Comprehensive Annual Financial Report.

As discussed above, Planning and Budget summarizes and reports non-general fund revenue estimates in eleven major categories. The following table summarizes each of the categories and also provides some information on the primary agencies involved in the collection and forecasting of the revenue. We included a similar table in our interim report, but have updated the information and included additional information in this table.

Major Category of Non-General Fund Revenue	Description of Revenue	Primary Agencies Responsible for Collecting Revenue	Primary Agencies Responsible for Forecasting Revenue
Federal grants and contracts	Federal grants and contracts collected by various agencies and colleges	Various agencies and institutions	Individual agencies and institutions
Institutional revenue	Patient fees collected at mental health facilities; tuition and fees collected by colleges	Colleges, universities, and other state institutions	Colleges, universities, and other state institutions
Other revenue	Revenues collected to support programs at agencies, including Child Support Enforcement collections, includes proceeds from the Master Tobacco Settlement agreement	Social Services, DMAS, and Department of the Treasury	Individual agencies
Motor vehicle fuel tax	Received from sale of fuels in the Commonwealth	Department of Motor Vehicles (Motor Vehicles) and Transportation	Department of Taxation (Tax)
Rights and privileges	Revenue from licenses, fees, permits, and other similar items	Motor Vehicles and Transportation	Tax
Sales of property and commodities	Lottery sales, Virginia College Savings Plan proceeds, and sales of alcoholic beverages	Alcohol and Beverage Control (ABC)	ABC, Lottery, College Savings Plan
Motor vehicle sales and use tax	Received from the sales of motor vehicles	Motor Vehicles and Transportation	Tax
Special highway tax from sales tax	Derived from a portion of the Commonwealth's sales tax	Transportation, and Department of Rail and Public Transportation	Tax
Unemployment compensation payroll tax	Payroll taxes dedicated to support the unemployed	Virginia Employment Commission (VEC)	VEC
Other taxes	Various taxes used to support various programs, including Direct Aid and Medicaid	Education and DMAS	Tax
Interests, dividends, and rents	Revenue generated from interest earnings and rental income	VEC, Transportation, and transfers from the Department of Accounts	Individual agencies

Analysis of Fiscal Year 2007 Estimated and Actual Revenues

There is currently no statewide comprehensive reporting of estimated and actual revenue collections. The Governor's Executive Budget Document, published annually in December, provides some information on non-general fund revenue; however, there is no comparison or analysis of actual to estimated revenues. While the Secretary of Finance's monthly revenue report includes some transportation revenues, there are other revenue streams, such as Federal grants and contracts, for which there is no monitoring or reporting done collectively on a statewide basis. Best practices suggest that monitoring revenue collections and comparing them to the projections is an essential part of a good forecasting process.

Section 4-8.01 of the Appropriation Act requires the Governor to provide information annually to the Chairmen of the Senate Finance, House Finance, and House Appropriations Committees concerning the receipt of any non-general funds above the amount(s) specifically appropriated, their sources, and the amounts for each agency affected. Accounts sends monthly CARS reports to the Chairmen to satisfy this requirement; however, these reports are of limited use without a thorough understanding of the various revenue streams.

Recommendation #1

We recommend the Secretary of Finance and Planning and Budget develop a mechanism for statewide comprehensive monitoring and reporting of estimated and actual collections of non-general fund revenues and include this information as part of quarterly reports to both the General Assembly and the public. The practice of measuring actual revenues against estimates is a best practice in a revenue forecasting process and this information is needed to make sound financial management and service delivery decisions.

We reviewed the non-general fund revenue information compiled by Planning and Budget and reported in the Executive Budget Document. In some cases, it was difficult to understand Planning and Budget's approach to compiling and reporting this information due to a general lack of documentation. Aside from some documentation maintained by Taxation on forecasting for certain revenue sources, there is little to no documentation on Planning and Budget's policies and procedures for compiling non-general fund revenue estimates during budget development.

As an example, there is no documentation on the overall approach to forecasting revenues in some major areas, such as federal grants and contracts. There is also no documentation to explain relationships between agencies which affect the forecasting and collection of various revenues. Another example of information that Planning and Budget should document is the practice of letting certain colleges and universities estimate federal grants revenue in a lump sum, while recording actual collections to the specific revenue sources. Lastly, there are cases where Planning and Budgets adjusts or eliminates agency revenue estimates for various reasons. There is no documentation that supports why Planning and Budget has done this.

Recommendation #2

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 approach for these revenues. Aside from limited documentation maintained by Taxation on certain revenue sources, there is no documentation maintained by Planning and Budget that details an understanding of the various revenue streams, the overall approach to forecasting non-general fund revenues or information on how information is currently compiled and reported in the Executive Budget document. This type of information is critical to have an understanding of when compiling and analyzing various revenues. In addition, this information should be documented to provide continuity of operations in the event of employee turnover.

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.

Based on information from Planning and Budget in the December 2006 and 2007 Executive Budget Documents, we prepared the following analysis. Overall, we found non-general fund revenue overestimated by \$1.4 billion, or 7.7 percent in fiscal year 2007.

The chart below shows that a significant portion of the overall variance was due to the Federal Grants and Contracts category. We analyze this category further, along with several of other categories with significant variances, later in this report.

Estimated-to-Actual Non-General Fund Revenue Collections for Fiscal 2007

Non-general Fund Revenue Category	Estimated Revenue	Revenue Collected	Variance (in Dollars)	Variance (Percent)
Federal grants and contracts	\$ 7,739,545,605	\$ 6,502,920,746	(\$1,236,624,859)	(16.0)%
Institutional revenue	4,175,909,044	4,110,501,709	(65,407,335)	(1.6)%
Other revenue	1,861,061,545	1,725,190,143	(135,871,402)	(7.3)%
Motor vehicle fuel tax	938,051,716	921,084,208	(16,967,508)	(1.8)%
Rights and privileges	789,129,839	777,165,990	(11,963,849)	(1.5)%
Sale of property and commodities	697,140,146	755,929,098	58,788,952	8.4%
Motor vehicle sales tax and use tax	587,500,000	597,638,358	10,138,358	1.7%
Special highway tax from sales tax	508,700,000	517,276,934	8,576,934	1.7%
Unemployment compensation payroll tax	456,900,000	437,517,444	(19,382,556)	(4.2)%
Other taxes	344,707,690	302,934,098	(41,773,592)	(12.1)%
Interest dividends and rents	141,886,370	184,298,540	42,412,170	29.9%
Total	\$18,240,531,955	\$16,832,457,268	(\$1,408,074,687)	(7.7)

“Total Estimated Revenue” figures are taken from the Appropriation Act, Chapter 847. “Revenue Collected” total amount is taken from the December 2007 Executive Budget Document.

In doing our analysis, we found certain budgeting practices that distort the non-general fund revenue estimate. We found these practices affect at least \$2 billion of the \$18.2 billion estimate for fiscal year 2007. One practice is the inclusion of funding streams in the budget which represent collections for others, and are not available to fund the Commonwealth’s operations. Two of the largest collection streams are Child Support Enforcement and Unemployment Compensation Taxes, which combined are over \$ 1 billion. Another example is Virginia College Savings Plan collections which represent funds held for others and used for future payments.

Another practice which distorts the revenue estimate is the reporting of over \$1 billion in Medicaid funding. Medical Assistance Services receives federal Medicaid funding which the Commonwealth matches with general funds. In fiscal year 2007, Medical Assistance Services paid various state agencies \$1 billion for services they provided to Medicaid recipients. Both Medical Assistance Services and these state agencies estimate this funding stream, resulting in a potential overstatement of Medicaid revenues in the budget. We have included a table in Appendix B from our 2007 Secretary of Health and Human Services report, which details Medicaid payments from Medical Assistance Services to other state agencies and universities in 2007.

Since Virginia's Constitution and other enabling legislation requires agencies have an appropriation before spending funds from the State Treasury, these collections are included in the Appropriation Act as part of non-general fund revenue. The current budget presentation makes it difficult to understand the nature of the various funding streams supporting the revenue estimate. For example, the budget should segregate collections for others in a separate budgetary grouping to show that these collections are not available to fund operating expenses and the Commonwealth is only the custodian of these funds.

Recommendation #3

Planning and Budget and the Secretary of Finance need to analyze the non-general fund revenue portfolio to determine which sources represent actual revenue and how best to present these sources in the budget. Current budget practices distort the user's ability to understand exactly what non-general fund resources are available to fund programs and services. Planning and Budget and the Secretary of Finance should analyze revenues and evaluate alternative presentations in the budget that would more clearly differentiate the different types of collections of non-general funds.

In addition, we found a number of errors in the information reported by Planning and Budget that affect the reliability and accuracy of the analysis. These errors fall into two general types, both of which are due to either a lack of understanding about the budget and accounting for the revenue streams, or the lack of scrutiny applied to the information.

First, we found some revenue estimates for specific revenue items that were not supporting an appropriation in the budget, or another agency had already included the revenue in their estimate. In either case, the result is the overstatement of the revenue estimates in the budget. These errors resulted when individual agencies submitted incorrect revenue estimates, and these errors were not detected and corrected by Planning and Budget staff during budget development.

Secondly, we found errors in the actual revenue collections reported by Planning and Budget in the December 2007 Executive Budget Document. Planning and Budget staff compile actual revenue collections from CARS. These errors were more pervasive and resulted when Planning and Budget reported actual collections for individual revenue sources that were not part of the original estimate and did not support an appropriation in the budget. These errors result in an overstatement of actual collections reported for fiscal year 2007 and affect the ability to make any meaningful comparison to the estimates.

Recommendation # 4

Agencies and Planning and Budget need to strengthen their procedures over the non-general fund revenue estimation and accumulation process. We found a number of errors in the non-general fund revenue information currently accumulated and reported in the Executive Budget Document. These errors affect the reliability and accuracy of information currently reported.

Agencies need to strengthen their procedures by ensuring staff who prepare budget development information have a clear understanding of the budgeting and accounting for their various revenue streams, and how others will use the information during budget development. Currently, Planning and Budget issues annual instructions to agencies on non-general fund revenue estimates during budget development; however, these instructions focus

primarily on the mechanics of submitting the information to Planning and Budget. While Planning and Budget did add some guidance in their most recent set of instructions, we believe there are opportunities for Planning and Budget to provide further, more substantive guidance.

It is equally important for Planning and Budget staff to understand the budgeting and accounting for the revenue streams to ensure the information they are compiling and reporting is comparable and accurate. Planning and Budget must review and verify the accuracy of non-general fund agency revenue estimates according to Section 2.2 -1501 of the Code of Virginia. In addition, their procedures for compiling and reporting actual collections in the Executive Budget Document are not adequate to ensure the information is accurate, reliable, and comparable. Planning and Budget needs to strengthen this entire process, and determine whether they have allocated adequate resources to this function to ensure compliance with their statutory requirements.

Federal Grants and Contracts

Revenue in the Federal Grants and Contracts category represents funding received by various agencies from the federal government, and there was an overestimation of approximately \$1.2 billion, or sixteen percent for fiscal 2007. We analyzed the variance and have included the following table which details some of the specific revenue items in this category that contributed to the large variance.

Agency	Description of Revenue	Estimated Revenue	Revenue Collected	Variance (in dollars)
Department of Transportation	Federal highway planning and construction funds	\$1,354,852,181	\$612,929,772	(\$741,922,409)
Department of Rail and Public Transportation	Federal and capital grants (Dulles Project)	99,000,000	12,529,104	(86,470,896)
Department of Rail and Public Transportation	Local funds (Dulles Project)	65,866,000	9,943	(65,856,057)
Department of Social Services	Medicaid transfer from DMAS.	56,100,000	(71,992)	(56,171,992)
Total		\$1,575,818,181	\$625,396,827	(\$950,421,354)

The single largest contributor to the variance for the Federal Grants and Contracts category is Transportation. The federal government allocated roughly \$1.35 billion for fiscal year 2007 to Virginia for Transportation, but the Commonwealth can only claim and collect less than half of this amount, giving the appearance of overestimating revenues by over \$700 million. This variance stems primarily from the nature of federal highway construction funding as well as the Commonwealth's approach to budgeting for this type of activity.

Annually, the federal government provides individual states with an allocation of funding, which allows state transportation officials to commit this amount of funding to long term construction projects. Because construction projects typically span several years, Transportation will be able to draw down revenue against their fiscal 2007 federal highway appropriation for several years as they incur construction costs.

The two items from Rail and Public Transportation represent most of the variance in the estimate of federal funding primarily related to the Dulles Metro Rail project. Since Rail and Public Transportation originally developed the estimate, there have been delays in the Dulles Metro Rail project, which led to the significant reductions in amounts of revenue collected to support the project.

The variance for Social Services represents funds coming from Medical Assistance Services to pay for Social Services' administrative expenses for Medicaid eligibility determinations. Medical Assistance Services bills and collects the money from the federal government and then transfers the money to Social Services. However, both Social Services and Medical Assistance Services include this estimated revenue in their estimates overstating anticipated collections by \$56 million.

While the Transportation item noted above represents an unusually large variance, we noted other instances during the course of our review of the Federal Grants and Contracts category where other agencies and institutions have similar occurrences, but not of the same magnitude. In general, the Commonwealth typically collects federal grants and contract funding to reimburse incurred costs. For many federal grants, an agency has a period of time in which it can claim reimbursements for expenses occurred. This period of time generally covers a span of several years. The nature of federal revenue complicates the forecasting process and makes an analysis of estimated to actual revenues inherently difficult.

Congress can change the program and funding levels every year which adds to the difficulty of estimating federal grant and contract funding. In many instances, there is the risk of changes directly to the legislation authorizing the program as well as changes Congress and the President can implement through the budget and appropriation process. Finally, the federal budget development and implementation time schedule does not coincide with the Commonwealth's budget development and implementation schedule.

Other Revenue

The Other Revenue category represents revenues from a variety of different sources, including the Master Tobacco Settlement Agreement. There were several items that contributed significantly to the variance in the Other Revenue, and these items are listed below.

Agency	Description of Revenue	Estimated Revenue	Revenue Collected	Variance (in dollars)
Direct Aid – Education	Literary Fund	\$178,618,054	\$ -	(\$178,618,054)
Department of Social Services	Child Support Enforcement program	635,500,000	577,231,161	(58,268,839)
Health Professions	Oxycontin settlement	-	20,000,000	(20,000,000)
Virginia College Savings Plan	VPEP Realized Gains	-	43,220,614	43,220,614
Virginia College Savings Plan	VEST Interest	1,000,000	32,892,424	31,892,424
Total		\$815,118,054	\$673,344,199	(\$181,773,855)

The largest single contributor to the variance in the Other Revenue category is the amount that Education receives for the Literary Fund. The Literary Fund revenue forecast is prepared by Treasury, and a portion of the Literary Fund is appropriated by the General Assembly as part of Education's Direct Aid to Public Education budget. Literary Fund collections come from the payment of certain fines and fees assessed in the courts, forfeitures, and the sale and collection of unclaimed property by the Department of the Treasury. A portion of these collections goes to Education to support teacher retirement benefits and provides funding to support the construction of public schools by local school divisions.

Based on a review of the actual revenues reported in CARS for 2007, it appears that Treasury transferred \$116 million from the Literary Fund into the Direct Aid budget. The remaining \$63 million from the Fund is appropriated to provide debt service payments for the education technology grant programs from the Virginia Public School Authority. Historically, Education has received this appropriation for debt service payments, but the payments have been made by Treasury. At the request of Education, the debt service appropriation has been removed from their non-general fund budget in the new budget which will more accurately reflect the actual funding of payments from the Literary Fund.

Social Services has a Child Support Enforcement program that collects child support from responsible parents and pays the collection to the custodial parent and also collects money from responsible parents where their failure to make support payments results in the custodial parent receiving public support. A portion of the payment from the responsible parent, where the custodial parent receives public support, becomes funding to the Commonwealth and is a small amount compared to total collections.

The amount above represents Social Services estimate of collection and disbursement of Child Support payments, which for the majority of users is voluntary and requires use only if the responsible parent does not pay the custodial parent. Estimating usage of the program is difficult; therefore, the variance, while significant, is reasonable.

The Health Professions' variance results from the Commonwealth's settlement of the Oxycontin case, which resulted in a \$20,000,000 one time receipt.

Overall, the College Savings Plan has some unique programs, and it is not clear what approach Planning and Budget uses to estimate revenues and appropriate funds for these programs in the budget. The variances related to VPEP realized gains at Virginia College Savings Plan are due to adjustments made by Planning and Budget in accumulating and reporting this information in the Executive Budget. During budget development, Virginia College Savings Plan submitted a revenue estimate of \$30 million for this revenue item; however, Planning and Budget reduced this to zero. The estimated revenue for VEST interest above is \$1 million, and this was not adjusted by Planning and Budget; however, it appears this revenue should be reported in the Interest, Dividends and Rents category.

Sales of Property and Commodities

This revenue category includes alcoholic beverage sales as well as various other revenues from agencies like the Virginia College Saving Plan and Lottery. The most significant variances between estimated and actual revenue in this category are related to the Virginia College Savings Plan and Lottery.

Agency	Description of Revenue	Estimated Revenue	Revenue Collected	Variance (in dollars)
Virginia College Savings Plan	VEST Contributions	\$ -	\$198,939,436	\$198,939,436
Virginia College Savings Plan	VPEP Contract Payments	71,000,000	-	(71,000,000)
State Lottery Department	Lottery instant ticket revenue	40,000,000	-	(40,000,000)
State Lottery Department	Lottery on-line ticket revenue	37,957,609	-	(37,947,609)
Total		\$148,957,609	\$198,939,436	\$ 49,991,827

The two largest variances above are related to College Savings Plan. As already discussed in another section, College Savings Plan has some unique programs, and it is not clear what approach Planning and Budget uses to estimate revenues and appropriate funds for these programs in the budget. VEST contributions were estimated at \$50 million by College Savings Plan, but this was reduced to zero by Planning and Budget. In addition, College Savings Plan collected \$121 million in VPEP Contract Payments, but this actual revenue was not reported by Planning and Budget.

A portion of Lottery instant and online ticket revenues are estimated in the budget because they support an appropriation for administrative expenses of the Lottery; however, Planning and Budget does not report related collections in the Executive Budget analysis.

Other Taxes

Other Taxes represent various taxes collected throughout the Commonwealth that are generally earmarked for a specific purpose, and includes the Motor Vehicle Rental Tax. The approach for estimating motor vehicle rental tax revenue has resulted in the variances below for both Motor Vehicles and Transportation. The tax is originally collected by Motor Vehicles and then transferred to other based up on requirements set forth in the Code of Virginia.

Agency	Description of Revenue	Estimated Revenue	Revenue Collected	Variance (in dollars)
Department of Motor Vehicles	Motor Vehicle Rental Tax	\$15,756,342	\$ -	(\$ 15,756,342)
Department of Transportation	Motor Vehicle Rental Tax	24,239,600	6,053,229	(18,186,371)
Total		\$39,995,942	\$6,053,229	(\$33,942,713)

The Motor Vehicles variance above is related to the 2 percent motor vehicle rental tax that is transferred to the General Fund to pay for debt service on VPBA bonds issued for the STARS System. The revenue is estimated and collected by Motor Vehicles; it is subsequently transferred to the General Fund, resulting in a zero balance above for collections. The non-general fund revenue estimate was overstated by \$15 million because this item was already included in the General Fund revenue estimate in the approved budget.

The variance from Transportation is due to adjustments to the revenue estimates which resulted in an overstatement of estimated revenue here. The amount of the rental tax which gets allocated to Rail and Public Transportation was included twice, resulting in an overstatement of estimated revenue by \$21 million.

Interest, Dividends, and Rents

Revenues from the Interest, Dividends, and Rents category are primarily derived from interest income and rental income collected by various agencies. We found the following items that contributed significantly to the variance for this category for fiscal 2007:

Agency	Description of Revenue	Estimated Revenue	Revenue Collected	Variance (in dollars)
State Lottery Department	Interest on cash balances	\$ -	\$ 10,135,416	\$10,135,416
Department of Transportation	Interest on cash balances	4,949,210	11,436,263	6,487,053
Department of Transportation	Interest on toll facility revolving account	15,805,842	34,145,224	18,339,382
Department of Transportation	Interest on cash balances	-	5,905,040	5,905,040
Department of Rail and Public Transportation	Interest on cash balances	-	5,715,224	5,715,224
Total		\$20,755,052	\$ 67,337,167	\$46,582,115

The majority of the variances in this category are due to Transportation underestimating interest revenue. This occurred because of higher than expected cash balances and increased interest rates. The Transportation item included in the table above that does not have an estimate represents interest that is not estimated during the budget development process due to the volatile nature of the interest.

The variance in this category related to the Lottery is due to interest not being estimated during budget development. This is correct in that these funds are not used to support the Lottery's appropriation for administrative expenses. Given this, Planning and Budget should not include the actual revenue collected in the information reported in the Executive Budget Document.

One other observation from our review of this category is that there does not appear to be a consistent approach to estimating interest revenue. Our review of the estimated and actual revenue information shows that some agencies estimate this revenue, while others do not. We could not find any formal guidance issues to agencies on how to approach this revenue item.

Recommendation #5

Planning and Budget should provide guidance to agencies for estimating interest revenue during budget development. Currently, there does not appear to be a consistent approach for this revenue stream.

Other Issues

During the course of our review, we identified some additional issues in the forecasting process for specific agencies. Since these errors were not material enough to warrant discussion elsewhere in the report, we have detailed them in this section by agency and specific revenue item.

Department of Criminal Justice Services

Criminal Justice had an incorrect formula in their forecasting spreadsheet which resulted in an error in the 2007 revenue estimate for crime victim witness fees.

Description of Revenue	Estimated Revenue	Actual Revenue	Variance
Crime victim witness fees	\$ 8,484,259	\$ 4,487,382	(\$3,996,877)

The 2007 revenue estimate submitted to Planning and Budget represented a 100 percent increase over the 2006 revenue estimate. (Fiscal 2006 estimated revenue was \$4.1 million, actual revenue was \$4.3 million.) Given this increase, this error should have been detected either by Criminal Justice Service's staff prior to submission to Planning and Budget, or by the Planning and Budget analyst during their review of revenue estimates for budget development.

Virginia Information Technologies Agency

The Virginia Information Technologies Agency (VITA) eliminated the following revenue source during fiscal year 2006, yet VITA retained the revenue source code in their non-general fund estimates for an additional year while no revenue was collected under this source.

Description of Revenue	Estimated Revenue	Actual Revenue	Variance
Recording, copying, and certifying public records	\$ 6,339,918	(\$360,749)	(\$6,700,667)

Given that the revenue source had been eliminated during the prior fiscal year, this revenue source should have been eliminated for fiscal 2007 by VITA prior to their submission of non-general funds to Planning and Budget, and the Planning and Budget analyst should have noted its elimination during the review of VITA's revenue estimates for budget development.

Attorney General's Office – Division of Debt Collection

Description of Revenue	Estimated Revenue	Actual Revenue	Variance
Collections of overdue accounts receivable	\$ 13,000,000	\$1,198	(\$12,998,802)

The revenue item represents recoveries received by the Division of overdue accounts receivables. These collections are not recorded as revenue in CARS nor are they supporting an appropriation. As a result, this item should not be included in estimated revenue.

Department of General Services

The Department of General Services (General Services) incorrectly identified the source of revenue which led to the apparent under collection of revenues. After additional research, we found that General Services actually collected approximately \$13 million for fees associated with the eVA procurement system.

Description of Revenue	Estimated Revenue	Actual Revenue	Variance
Vendor registration fees	\$11,293,000	\$92,150	(\$11,200,850)
Vendor transaction fees	-	12,864,033	12,864,033

The original 2007 estimate for vendor registration fees submitted to Planning and Budget by General Services represents a substantial increase over the 2006 revenue. Given the significant changes, these errors should have been detected either by General Services prior to submission to Planning and Budget, or by the Planning and Budget analyst during their review of revenue estimates for budget development.

General Services also estimated revenue for an item that is already estimated by the Department of Health. This is for a federal grant that is drawn down at Health and then transferred over the General Services. Since it is estimated at both agencies, revenue is overestimated by \$7,700,000.

Description of Revenue	Estimated Revenue	Actual Revenue	Variance
Federal grants – CDC Investigations and Technical Assistance	\$7,700,000	\$ -	(\$7,700,000)

It is our understanding from discussion with Planning and Budget staff that they usually adjust the estimated revenue for this type of situation; however, this estimate was not adjusted in 2007.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

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

May 20, 2008

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

The Honorable M. Kirkland Cox
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

We have reviewed the **non-general fund revenue forecasting practices for the Commonwealth of Virginia** and are pleased to submit our report entitled "Review of Non-General Fund Revenue Forecasting Process, Final Report." This report is a follow up to an interim report that we issued in May 2007 entitled "Review of Non-General Fund Revenue Forecasting Process, Interim Report." We conducted this review in accordance with generally accepted Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Review Objectives, Scope, and Methodology

Our review of the non-general fund revenue forecasting process was completed in two phases. The first phase of our review focused on gaining an understanding of the processes and evaluating those against best practices. Our objectives in this phase were to determine the extent to which Planning and Budget monitors and reviews non-general fund revenue estimates, and whether their procedures comply with their statutory requirements; to determine how non-general fund revenue estimates are incorporated into the Appropriation Act and into the Commonwealth Accounting and Reporting System; and to determine the appropriateness and reasonableness of the methodologies and estimates utilized and provided by the individual agencies and universities to develop non-general fund revenue estimates.

As part of our review, we analyzed estimated and actual non-general fund revenues for fiscal year 2007. Our analysis was based on the non-general fund revenue estimate used in Chapter 847 of the Appropriation Act, and actual revenue reported in the Executive Budget Document in December 2007. Based on this analysis, we followed up selected significant variances to determine whether or not they were reasonable. We relied on information provided by Planning and Budget as well as agency staff in completing this work.

Results of Review

Our review of non-general fund revenue forecasting revealed several areas where improvements need to be made. We found a general lack of review in the forecasting and monitoring of these funds at a statewide level, as well as certain practices that distort the estimated revenue in the budget. We have included our specific recommendations throughout the course of this report.

Exit Conference and Report Distribution

We discussed this report with management from the Department of Planning and Budget on May 20, 2008. Their response has been included at the end of this report.

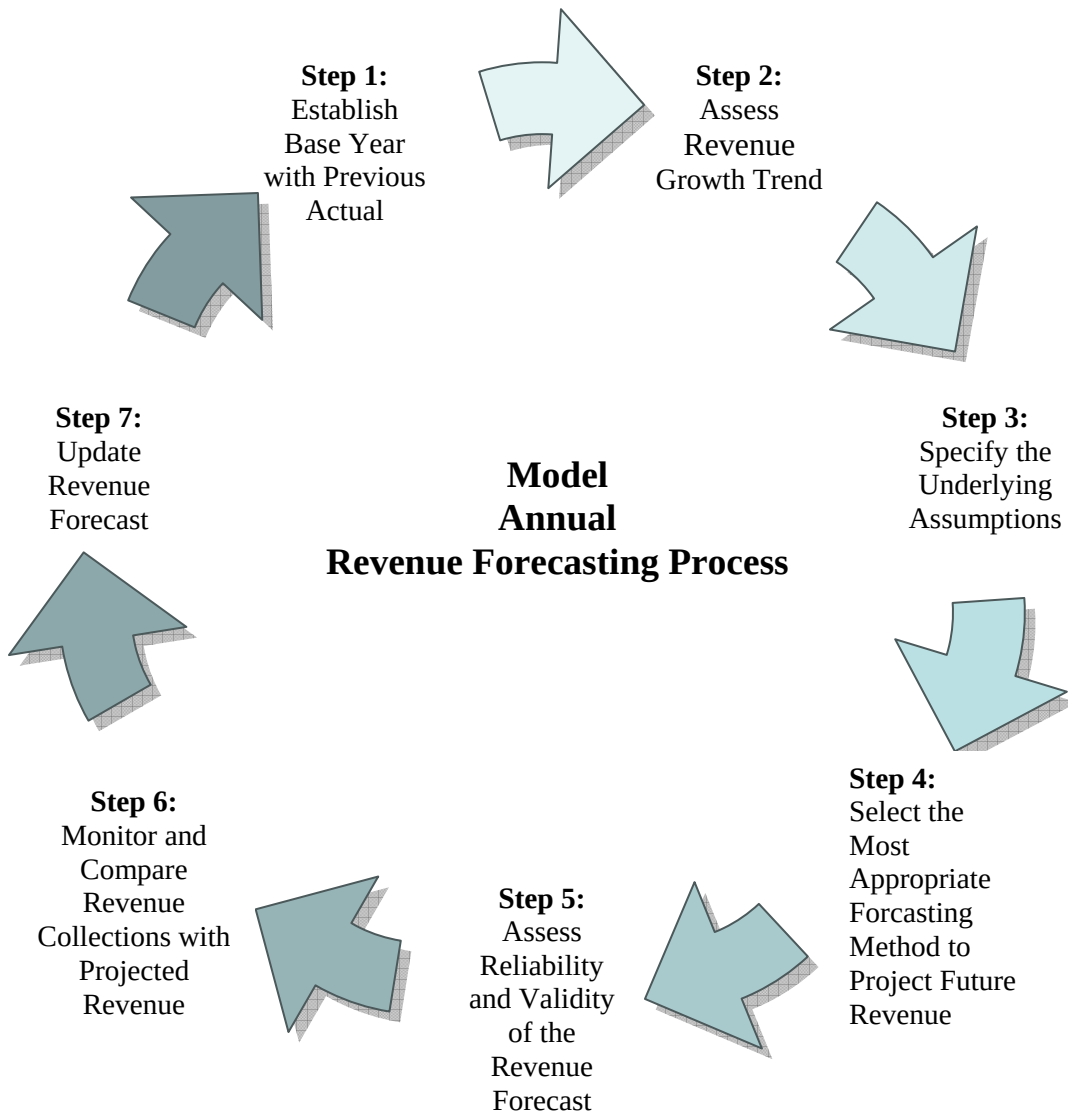
This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

LCW/wdh

Appendix A

This diagram represents the recommended best practices for the development of revenue forecasting, as derived in conjunction with the National Advisory Council on State and Local Budgeting (NACSLB) with the Government Finance Officers Association (GFOA).



Source: GFOA Budget Series, Volume 2, *Revenue Analysis and Forecasting*

Appendix B
Internal Medicaid Payments for Services

<u>Entity</u>	<u>Services</u>	<u>Entity Provided Match</u>	<u>Funding from the Department of Medical Assistance Services</u>	<u>Total Medicaid Funding</u>	<u>Total Available Funding for Services</u>	<u>Medicaid Funding as a Percent of Total Funding for Services</u>
DMHMRSAS	Inpatient Care, Facilities and Other	\$ 27,530,014	\$ 240,307,767	\$ 252,307,767	\$ 556,137,478	45%
Community Service Boards	Community Care	-	274,172,085	274,172,085	783,348,814	35%
Comprehensive Services	Residential Psychiatric Treatments and Utilization Management Reviews	46,805,143	46,805,143	93,610,286	316,164,675	30%
University of Virginia Health System	Patient Care	-	190,077,245	190,077,245	882,400,985	22%
VCU Medical Center	Patient Care	-	247,956,798	247,956,798	1,230,558,294	20%
Social Services, State & Local	Outreach and Eligibility Determination and Other	62,357,790	62,357,790	124,715,580	629,647,855	20%
Local School Divisions	Student Care	14,594,894	14,594,894	29,189,788	541,575,468	5%
Virginia Commonwealth University	Research	458,661	458,661	917,322	18,000,000	5%
Department of Health	Various Services, Including Outpatient Care	3,092,186	3,279,201	6,371,387	220,959,335	3%
Department of Rehabilitative Services	Eligibility Determination	987,373	987,373	1,974,746	90,755,900	2%
Woodrow Wilson Rehabilitation Hospital	Rehabilitation	-	371,476	371,476	19,903,732	2%
Department for the Aging	Medicaid Ombudsman Program	166,148	166,148	332,296	30,806,751	1%
Department of Health Professions	Nurse Aide Training and Certification Program	-	211,840	211,840	23,092,461	1%
Total		<u>\$ 155,992,209</u>	<u>\$ 1,081,746,421</u>	<u>\$ 1,222,208,616</u>	<u>\$ 5,343,351,748</u>	23%

Source: Secretary of Health and Human Resource Report for fiscal year 2007, issued by APA in February, 2008



COMMONWEALTH of VIRGINIA
Department of Planning and Budget

Richard D. Brown
Director

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

May 28, 2008

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

Dear Mr. Kucharski:

There are two general issues raised by the Auditor of Public Accounts' (APA) review of the nongeneral fund (NGF) revenue estimation process. The first is the accuracy of the estimates including supporting documentation on the preparation of these estimates. The second centers on the monitoring of actual revenues against the budget estimates.

The Department of Planning and Budget (DPB) generally agrees that the documentation and accuracy surrounding the NGF revenue estimates can be improved. DPB will seek to improve its instructions to analysts to facilitate their review of the estimates prepared by the various state agencies. A fundamental issue to be clarified in this endeavor is whether the agencies should include estimates of all NGF revenues collected or whether the revenues reported by agencies should be tailored to only those supporting appropriations in the general appropriation act. One of the main causes for variance between the estimates and actual revenues stems from the fact that some NGF revenues are appropriated by language (e.g. sum sufficient appropriations, etc.) rather than specific amounts in the appropriation. DPB agrees that for comparison purposes the estimates of NGF revenue for budgetary purposes should be compatible with the actual revenues appropriated in the appropriation act.

The lack of time to thoroughly analyze agency submissions prior to the release of the budget bill in December also contributes to such inconsistencies. It may be possible for DPB to broaden the length of its review of NGF revenue data submitted by the agencies by working with General Assembly staff during the legislative session to correct any inconsistencies included in the introduced budget bill because of inadequate time to complete a rather comprehensive and complex review of NGF revenues. To this end, DPB will devote more effort to address the accuracy of these estimates and explore options to lengthen the review period for preparation of these estimates.

Mr. Walter J. Kucharski
May 28, 2008
Page Two

The second issue raised by the APA deals with the monitoring of actual NGF revenue collections. In this context, it must be pointed out that DPB is not a revenue collection agency and DPB has no responsibilities for accounting for NGF revenue collections or for reporting on them outside of the budgetary process. The APA's review assumes that the responsibility for ongoing monitoring of these revenues should be assigned to DPB. That assumption may not be an accurate one since the only place the status of actual collections is reported by state agencies is to the State Comptroller and not DPB.

Accordingly, DPB will change its annual report on NGF revenue projections to the General Assembly to include a comparison of actual and budgeted revenues for the most recently completed fiscal year. However, DPB does not have the staff to monitor these collections on a more frequent basis. A report comparing actual collections to the revenue estimates on a more frequent basis is complicated by the lack of automated systems able to capture this data on an on-going basis. As a result, such comparisons take a great deal of man hours to complete and staff is simply not available to perform this undertaking on a more frequent basis. Again, DPB's basic statutory responsibilities in the area of NGF revenues pertain to developing estimates for use in the budget and in the six-year revenue plan of the Commonwealth and the agency has never been staffed for an effort to monitor nongeneral fund revenues on a comprehensive basis.

On a final note, the aging financial systems of the Commonwealth are at the core of many of the issues raised by the APA in its review of nongeneral fund revenues. The ability to monitor and account for such revenues and to properly incorporate them into the state's budget is dependent on the ability of DPB to access and manipulate such data. The fact that nongeneral fund revenues are numerous, vary greatly in size, are often collected and spent by different state agencies, and have various accounting treatments greatly hinder the ability of any one agency, such as DPB, to accurately track such revenues without better automation or a great deal of manpower and time devoted to the effort. Ultimately, the issue boils down to whether the state is willing to update its financial systems to capture more accurate and timely information on this front. The answer to that question will have a greater impact on the ability of the Commonwealth to monitor and estimate nongeneral fund revenues than a pledge by DPB to make a greater staff effort in this endeavor.

I thank you for a chance to review this report prior to its publication.

Sincerely,



Richard D. Brown

c: The Honorable Jody M. Wagner
Paul D. Bender
Donald D. Darr