COMMONWEALTH of VIRGINIA

Joint Legislative Audit and Review Commission
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MEMORANDUM

TO:	Members of the Joint Legislative Audit and Review Commission
CC:	Robert Vaughn; Staff Director, House Appropriations Committee Betsey Daley; Staff Director, Senate Finance Committee
FROM:	Kimberly Sarte, Mark Gribbin
SUBJECT:	Annual Review of Internal Service Funds

The Joint Legislative Audit and Review Commission (JLARC) is vested with responsibility for overseeing the internal service funds (ISFs) managed by the Virginia Information Technologies Agency (VITA), Department of General Services (DGS), and Department of Accounts (DOA). JLARC's oversight is generally limited to monitoring the health of ISFs, including whether they are maintaining appropriate balances, making reasonable projections of future revenues and expenditures, and charging appropriate rates to recover the anticipated costs of services. This memo comments on the financial health of the ISFs as well as changes proposed in the 2015 governor's budget bill. The ISFs overseen by JLARC had appropriations of $536.1 million in FY 2015.

Key Findings

JLARC staff did not identify any major concerns regarding the health of the ISFs or changes proposed in the governor's budget bill.

- Although some VITA and DOA funds have negative balances due to long-term debt, the debt is being paid off and the ISFs have collected sufficient revenue to pay their operating expenses.
- The overall balances of the DGS funds could not be determined at this time due to data limitations, but the funds have all maintained positive cash balances.

- ISFs appear to be maintaining appropriate cash reserves.
- The ISF appropriations requested in the governor's budget bill are supported by reasonably determined projections of future expenditures.
- The ISF rate changes requested in the governor's budget bill were reasonably determined.
- The governor's budget bill proposes that future ISF rate changes must be approved in the Appropriation Act and vests the Department of Planning and Budget (DPB) with responsibility for establishing ISF rate policies (§ 4-5.03); JLARC staff found the proposed changes reasonable but recommend the language clarify that contractually determined vendor fees do not need to be approved in the Act and that DPB should consult with the ISF agencies in establishing rate policies.

Background

Internal Services Funds (ISFs) are a financial mechanism used to recoup costs incurred by one agency when performing services or procuring goods on behalf of other agencies. For example, DGS leases office space in downtown Richmond to several customer agencies, which pay rent to DGS through an ISF. Likewise, VITA provides IT services to customer agencies, and customers pay VITA through an ISF.

Fund status

JLARC staff recommend that ISFs maintain positive fund balances. A positive fund balance indicates that a fund has regularly collected sufficient revenue to pay its expenses. Some funds have negative balances because they are carrying long-term debt. These funds should make steady progress towards reducing their debt.

Over the years, JLARC oversight staff have generally recommended that ISF funds maintain a sufficient cash reserve to cover short-term operating expenses. JLARC has used a 60- to 90-day standard, but the appropriate amount of the cash reserve depends on the fund and its unique cash requirements. As a benchmark comparison, the federal government uses a 60-day standard for this type of cash reserve. The amount of cash held by a fund can vary substantially over the course of a year depending on the types of services provided and when they are paid for.

Appropriations

The 2014 Appropriation Act began requiring General Assembly approval of specific ISF appropriation amounts. VITA, DGS, and DOA are only allowed to spend the amounts appropriated in the Act. The ISF agencies make appropriation requests according to their spending projections, which are based on anticipated demand for services from customer agencies. Each customer agency budgets general or non-general funds to pay for the ISF services it uses, which means that the appropriations for customer agencies drive actual ISF spending.

Rates

As a result of the 2014 change to the ISF appropriation process, the process for approving ISF rates also changed. In accordance with this change, JLARC amended its ISF policy to stop approving rates but to retain general oversight authority.

ISF rates should be set to avoid both under- and over-collection from customer agencies. Rates must be sufficient to recover expenditures but not place an undue financial burden on customer agencies. Over time, rates can vary depending on the expenses that need to be recovered, such as the costs of vendor services or employee compensation, and depending on customers' demand for services.

Virginia Information Technologies Agency

The Virginia Information Technologies Agency (VITA) provides information technology (IT) goods and services to most executive branch agencies. VITA provides IT infrastructure services, such as data center services, personal computers, and internet connectivity, through third-party vendors such as Northrop Grumman. VITA also provides security oversight and central support services directly to agencies. VITA collects revenues for all of these services through its Information Technology and Management ISF. VITA charges 416 unique rates for the services it offers.

VITA's total budgeted ISF appropriations for FY 2015 are $347.9 million. The services offered under this ISF fall under four different budget programs (Table 1). Almost 90 percent of VITA appropriations, or $309.6 million, are "pass-through" payments to Northrop Grumman and other vendors that provide IT infrastructure services to state agencies. The remaining ISF appropriations are for VITA's administrative costs ($23.7 million), central support services that VITA directly provides to agencies ($11.8 million), and VITA's security oversight ($2.8 million).

TABLE 1: VITA ISF and services

Program within fund	Services provided	FY 2015 appropriation
Vendor IT infrastructure services	Data center, personal computing, internet, and telecommunications services from Northrop Grumman and other vendors	$309.6 million
VITA administrative overhead	Agency operations costs not related to direct services or security, including staff costs for contract oversight, customer relations, and administrative functions	$23.7 million
VITA central support services	Support services directly provided by VITA including support for the Medicaid Information Technology Architecture initiative, collaborative software applications, and applications security testing	$11.8 million
VITA security oversight	Security oversight services directly provided by VITA including incident response and IT security audit reviews	$2.8 million
Total all programs		**$347.9 million**

Source: 2014 Appropriation Act (Chapter 3).

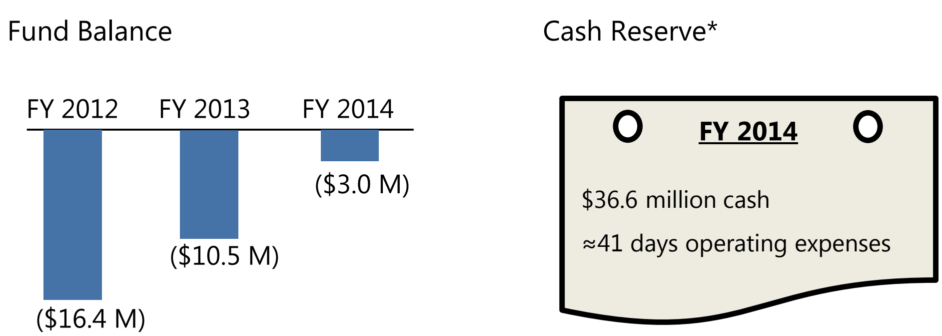
Fund status

One key measure of ISF status is whether the fund maintains an appropriate, positive fund balance over time. VITA's ISF has a negative balance, but the balance has been steadily improving and so is not currently a concern. VITA's balance has been negative since FY 2010, when it recorded substantial losses because VITA's old rate structure did not capture costs incurred for the then-newly transformed Northrop Grumman services. VITA was given a line of credit from the state comptroller to meet its vendor payment obligations and was allowed to charge a temporary one-time debt recovery rate to collect additional revenue and offset losses. These revenues provided income to reduce the negative fund balance and cash to help repay the line of credit. Since that rate was implemented, the fund's balance has consistently improved from year to year, and was −$3.0 million at the close of FY 2014 (Figure 1). VITA discontinued the debt recovery rate at the end of FY 2014, in accordance with its sunset provisions, because the fund's balance is close to positive.

A second measure of ISF status is whether a fund has a sufficient cash reserve to cover short-term operating expenses. VITA's ISF appears to be maintaining an appropriate cash reserve. At the close of FY 2014, the ISF had sufficient cash to cover 41 days of operating expenses. Although this is lower than the federal 60-day benchmark, it is within the fund's historical norms. VITA also has a standing line of credit with the state's Department of the Treasury, which can be used in the event that VITA does not have sufficient cash on hand to cover expenses. The governor's budget bill proposes transferring $4.5 million in cash out of VITA's ISF fund to the general fund. Based on the ISF's end-of-year cash balance, this would reduce its cash reserve to the equivalent of 36 days.

FIGURE 1: Key ISF status indicators

Information Technology and Management



Source: VITA financial statements.
* The cash reserve represents the number of days of operating expenses that the end-of-year cash balance can cover. The end-of-year cash balance includes prepayments for ISF services to be rendered in the following fiscal year, meaning that a substantial portion of cash is already obligated for future expenses.

Appropriations

VITA's appropriation requests are supported by estimates of future ISF expenditures. VITA's estimates reflect the anticipated costs of serving its ISF customer agencies, including the cost of its own operations and its contractual obligations to vendors.

The governor's budget bill proposes reducing the amounts appropriated for VITA's ISF, especially in FY 2016 (Table 2). JLARC staff reviewed changes to the ISF's appropriations and found that they were reasonably determined and supported by the agency's projections.

TABLE 2: VITA ISF budget and proposed changes by program

	FY 2015	FY 2016
Vendor IT infrastructure services (program 820)		
Appropriation Act (2014)	$309,552,088	$324,404,793
Reduction in service use	(0)	(11,868,767)
Governor's budget bill (2015)	**$309,552,088**	**$312,536,026**
VITA administrative overhead (program 899)		
Appropriation Act (2014)	$23,736,795	$23,882,173
Increase in benefits cost	470,673	497,222
Elimination of vacant positions	(1,089,895)	(1,497,424)
Governor's budget bill (2015)	**$23,117,573**	**$22,881,971**
VITA central support services (program 824)		
Governor's budget bill (2015)*	**$11,806,841**	**$11,806,841**
VITA security oversight (program 829)		
Appropriation Act (2014)	$2,769,036	$2,895,664
Increase in benefits cost	67,022	81,274
Elimination of vacant positions	(235,397)	(377,025)
Governor's budget bill (2015)	**$2,600,661**	**$2,599,913**
Total ISF budget		
Appropriation Act (2014)	$347,864,760	$362,989,471
Net change to ISF	(787,597)	(13,164,720)
Governor's budget bill (2015)	**$347,077,163**	**$349,824,751**

Source: Performance budgeting data, 2014 Appropriations Act (Chapter 3) and 2015 governor's budget bill.
* No changes proposed to the VITA central support services budget. The initial and revised budgets are identical

VITA's pass-through vendor expenditures account for the majority of its ISF appropriation. The governor's budget bill requests a $312.5 million appropriation for pass-through vendor expenditures in FY 2016, which is $11.9 million lower than appropriated in the 2014 Appropriation Act. VITA's vendor-related ISF spending is expected to be lower due to changes in customer demand. VITA previously assumed that demand for vendor services would increase two percent from FY 2015 to FY 2016, but now assumes that demand will remain relatively flat due to agency budget reductions.

Even though service use is expected to remain flat, overall ISF spending for vendor services is expected to rise slightly from the FY 2015 level. This is primarily due to a contractually obligated cost-of-living increase of 3.02 percent for services provided by the state's largest IT vendor, Northrop

Grumman, and other contractual price increases that are expected to be triggered by declining use of some IT infrastructure services.

VITA's second largest ISF expenditure is for administrative overhead. The governor's budget bill proposes reducing administrative overhead costs by eliminating several vacant positions, four of which directly support management and delivery of ISF services, including management of vendor services. In addition to these reductions, the bill proposes an increase in appropriations for personal services to cover increases in the cost of employee benefits.

VITA's third and fourth largest ISF expenses are for its central support services and security oversight. No changes to central support services were proposed in the governor's budget bill. However, the bill proposes reducing security oversight expenditures by eliminating three vacant security positions. As with administrative overhead, the bill also proposes an increase in appropriations for personal services to cover increases in the cost of employee benefits.

Rates

Each of the VITA rates includes a "fee" component and a "surcharge" component. The fee component recovers either the direct cost of vendor services or the costs of services provided by VITA staff, such as its central support services. The surcharge component recoups VITA's administrative overhead and security oversight costs.

The governor's budget bill proposes requiring that changes in ISF rates must be approved in the Appropriation Act (§ 4-5.03). Consistent with this new requirement, the bill proposes changing the VITA surcharge that is used to collect VITA administrative overhead expenses. The bill proposes a VITA surcharge of 8.26 percent for FY 2015 and 7.81 percent for FY 2016. The 8.26 surcharge is consistent with the surcharge that is currently in place. This surcharge was reviewed by JLARC staff prior to its implementation and was considered to have been reasonably determined. The lower 7.81 percent surcharge proposed for FY 2016 appears sufficient to recover VITA's anticipated expenses, given the revised ISF appropriations set forth in the governor's budget bill.

Although the VITA surcharge will decrease from FY 2015 to FY 2016, VITA anticipates that its overall rates (fees plus surcharge) will generally increase by 2.22 percent in FY 2016, using a weighted average of rates. This is attributable to two factors. First, the prices charged by the state's largest IT services vendor, Northrop Grumman, are expected to increase by 3.02 percent as part of a contractually determined cost-of-living adjustment. Second, VITA anticipates that customers will reduce their use of several major IT infrastructure services, which will cause the prices for these services to increase.

JLARC staff generally agree with the proposal in the governor's budget bill to have future rate changes approved in the Appropriation Act. This will ensure that ISF rates align with approved spending. However, most VITA rates include contractually determined pass-through fees charged by vendors. The fees represent a contractual obligation of the state for which legislative approval should not be necessary. According to DPB, the new language in the bill was not intended to require legislative approval of vendor fees. JLARC staff recommend the bill be amended to clarify that legislative approval of contractually determined vendor fees is not required.

Department of General Services

The Department of General Services (DGS) provides a variety of goods and services to executive branch agencies. These services are provided under nine different ISFs (Table 3). DGS charges over 50 unique rates for the services it offers.

TABLE 3: DGS ISFs and services

Fund	Services provided	FY 2015 appropriation
Real Estate Services	Administration of leases for agencies that rent office space	$63.0 million
Maintenance and Repair Projects	Lease and maintenance activities on state-owned property under the Bureau of Facilities Management	39.5
Virginia Distribution Center	Sale of food and housekeeping products	32.0
Fleet Management	Management of cars, trucks, and fuel programs used by state agencies	19.0
Bureau of Capital Outlay Management	Assistance planning and procuring construction services	4.5
Analytical Testing Services	Laboratory testing of environmental, agricultural, and other samples	3.2
State Surplus Property	Sale or donation of state surplus items to agencies, nonprofits, and the public	1.9
Federal Surplus Property	Sale or donation of federal surplus items to agencies, nonprofits, and certain small businesses	0.9
Graphic Communications	Printing and graphics services	0.1
Total all funds		**$164.1 million**

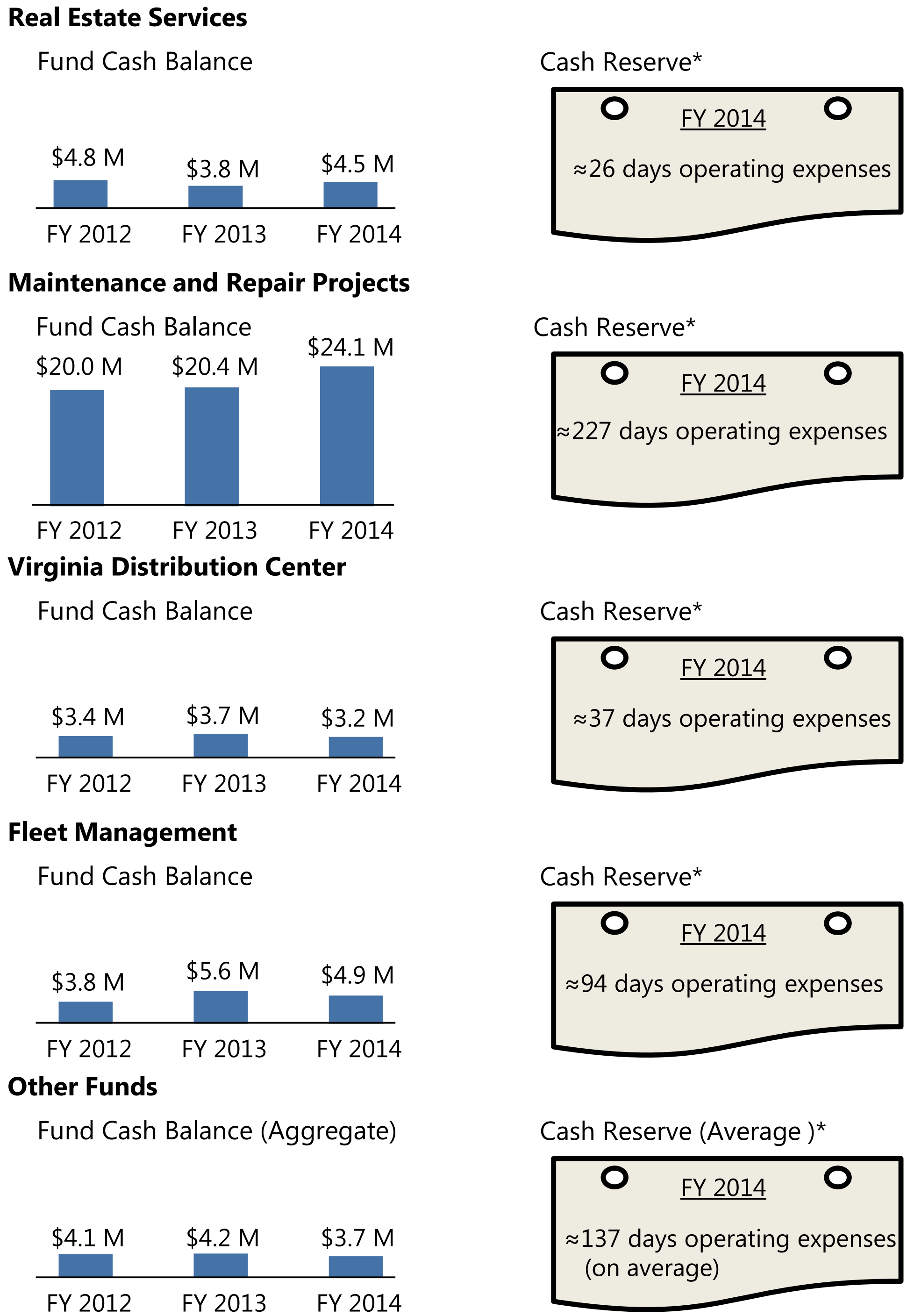
Source: 2014 Appropriation Act (Chapter 3).
Note: In addition to ISF services, DGS provides procurement services to state agencies and others through the eVA system. These services are provided through an enterprise fund instead of an internal service fund.

DGS's total budgeted ISF appropriations for FY 2015 are $164.1 million. Four DGS funds account for 94 percent of ISF appropriations: the Real Estate Services fund ($63.0 million), the Maintenance and Repair Projects fund ($39.5 million), the Virginia Distribution Center fund ($32.0 million), and the Fleet Management fund ($19.0 million). The five other DGS funds were substantially smaller and together account for another $10.6 million in appropriations.

Fund status

The funds managed by DGS have maintained positive cash balances but, due to data limitations, the overall status of the funds cannot be determined at this time. All of the funds have maintained positive cash balances over the past three years (Figure 2). However, the overall fund balances may be higher or lower than the cash balance depending on the assets and liabilities associated with each fund. For example, the cash balance for the Maintenance and Repair Projects fund does not include the value of other assets associated with the fund, such as the Capitol Square facilities. It also does not include liabilities, such as a $3 million outstanding loan for the purchase of the Old City Hall building.

FIGURE 2: Key ISF status indicators



Source: DGS financial statements.
* The cash reserve represents the number of days of operating expenses that the end-of-year cash balance can cover. The end-of-year cash balance for several funds includes prepayments for ISF services to be rendered in the following fiscal year, meaning that a substantial portion of cash is already obligated for future expenses.

DGS's ISFs appears to be maintaining appropriate cash reserves. At the close of FY 2014, all of DGS's ISFs reported cash reserves sufficient to cover several days of operating expenses. Reported cash reserves were below the federal 60-day benchmark for the Virginia Distribution Center fund (37 days) and Real Estate Services fund (26 days). Although the reserve for the Real Estate Services fund was relatively low, it is within the fund's historical norms and DGS indicated that the fund did not have a cash flow problem.

Two of DGS's funds had relatively high cash reserves, but these large balances were explained by operating factors unique to the funds. The Maintenance and Repair Projects fund reported a cash reserve well above the federal 60-day benchmark (227 days). DGS indicated this was because many of its customers prepay their rent obligations for the coming year at the end of the prior year. The fund has a large cash reserve at the time when the cash balance is reported, but this amount will be spent down during the course of the year. The Fleet Management fund also reported a relatively large cash reserve (94 days). DGS indicated that this fund requires a large reserve because of how vehicles are purchased and the need to pay for maintenance projects at the fleet management facility. The governor's budget bill proposes transferring $1.7 million out of the Fleet Management ISF to the general fund. Based on the fund's end-of-year cash balance, this would reduce its cash reserve to 61 days.

The five smallest DGS funds averaged cash reserves sufficient to cover 137 days. The actual reserve amount varied substantially from fund to fund. The two biggest funds in this group held cash reserves of 34 and 84 days, respectively, and so were close to the federal 60-day benchmark. The remaining three funds had much larger cash reserves relative to operating expenses. The governor's budget bill proposes transferring $0.7 million out of one of these funds, the State Surplus Property fund, to the general fund. Based on the fund's end-of-year cash balance, this would reduce its cash reserve from 214 days to 60 days.

Appropriations

DGS's appropriation requests are supported by estimates of future ISF expenditures. DGS estimates reflect the anticipated costs of serving ISF customer agencies, including the cost of compensating DGS employees and making payments to vendors for goods and services.

The governor's budget bill proposes minor adjustments to ISF appropriations for DGS. These include a small reduction in the overall ISF appropriations for FY 2015 and a small increase in FY 2016 (Table 4). JLARC staff reviewed these changes and found that they were reasonably determined and supported by the agency's projections. Individual changes proposed in the bill are summarized as follows:

- An increase of $25,000 in FY 2016 for the Division of Real Estate Services to conduct a special review of whether the state should take ownership of the facility that currently houses the Center for Innovative Technology. The review would be paid for from the balance of the Real Estate Services fund, which appears sufficient to absorb the cost.

- Reductions in both years for the Bureau of Capital Outlay Management. DGS was providing inspection services for the Dulles Corridor Metrorail project in northern Virginia, but the first phase of the project is now complete and this spending authority is not currently needed.

- An increase of $600,000 in FY 2016 for the Analytical Testing Services fund to pay for the cost of drug testing services provided to the Department of Corrections. DGS expects to collect this additional revenue under its existing rates and is requesting matching spending authority.

- An increase of $109,000 in FY 2016 to add a new analyst position to support internal service fund financial operations and rate reviews. The cost of the new position would be proportionally spread across the nine ISFs, but the allocation amounts have not yet been determined, so the item is reported here as an unallocated ISF appropriation.

TABLE 4: DGS ISF budget and proposed changes by fund

	FY 2015	FY 2016
Real Estate Services (Fund 601)		
Appropriation Act (2014)	$63,039,232	$63,039,232
Increase for special analysis of CIT lease options	0	25,000
Governor's budget bill (2015)	**63,039,232**	**63,064,232**
Maintenance and Repair Projects (Fund 604)		
Governor's budget bill (2015)*	**$39,527,539**	**$40,471,393**
Virginia Distribution Center (Fund 600)		
Governor's budget bill (2015)*	**$32,000,000**	**$32,000,000**
Fleet Management (Fund 610)		
Governor's budget bill (2015)*	**$18,993,189**	**$18,993,189**
Bureau of Capital Outlay Management (Fund 607)		
Appropriation Act (2014)	$4,482,200	$4,996,200
Decrease based on changed service use assumptions	(170,600)	(575,400)
Governor's budget bill (2015)	**4,311,600**	**4,420,800**
Analytical Testing Services (Fund 606)		
Appropriation Act (2014)	$3,162,854	$3,162,854
Increase to account for DOC testing revenue	0	600,000
Governor's budget bill (2015)	**3,162,854**	**3,762,854**
State Surplus Property (Fund 603)		
Governor's budget bill (2015)*	**$1,865,000**	**$1,865,000**
Federal Surplus Property (Fund 605)		
Governor's budget bill (2015)*	**$936,900**	**$936,900**
Graphic Communications (Fund 602)		
Governor's budget bill (2015)*	**$145,600**	**$145,600**
Unallocated ISF appropriation*		
Appropriation Act (2014)	$0	$0
Decrease based on changed service use assumptions	0	109,000
Governor's budget bill (2015)	**$0**	**$109,000**
Total ISF budget		
Appropriation Act (2014)	$164,152,514	$165,610,368
Net change to ISF	(170,600)	158,600
Governor's budget bill (2015)	**$163,981,914**	**$165,768,968**

Source: Performance budgeting data, 2014 Appropriations Act (Chapter 3), and 2015 governor's budget bill.
* Additional ISF appropriations proposed for new ISF analyst position. Costs will be allocated across all existing ISFs but the methodology has not yet been determined.

Rates

Each of the DGS rates is structured differently depending on the ISF and service provided. Some service rates are flat fees, such as hourly fees for construction inspection services, and others are fixed percentage markups charged on top of the price paid for each good or service a customer buys.

The governor's budget bill proposes changes to the hourly billable rate for building inspection services provided under the Bureau of Capital Outlay Management. The rate would be set at $128 per hour in FY 2015 and $139 per hour in FY 2016. The $128 hourly rate is consistent with the rate that is currently in place. The rate was reviewed by JLARC staff prior to its implementation and was found to have been reasonably determined. The $139 hourly rate for FY 2016 is higher than the $132 rate that JLARC reviewed and approved last year. DGS indicated that demand for inspection services has not met expectations and employee benefit costs have increased substantially since the initial rate was approved. A rate increase is therefore needed to avoid under-collection. According to DGS, the fund is already expected to under-collect by $315,000 in FY 2015, and could lose an additional $178,000 in FY 2016 if the rate is not adjusted. JLARC staff reviewed DGS's rate calculations and found them to be reasonably determined.

Department of Accounts

The Department of Accounts (DOA) oversees ISFs that support financial services provided to state agencies. The costs for these financial services are recovered through two ISFs—the Enterprise Applications ISF and the Payroll Services Bureau ISF.

The Enterprise Applications ISF recovers costs related to the Cardinal and the Performance Budgeting systems. The state is in the process of implementing Cardinal, which will replace the legacy Commonwealth Accounting and Reports System and will result in an updated enterprise financial management system. The FY 2015 approved appropriation for Cardinal is $17.6 million (Table 5). This covers the costs associated with operating and maintaining the system and does not include the costs to implement Cardinal statewide, which are paid through a working capital advance. These implementation costs will eventually be recovered through future ISF charges to customers.

The Performance Budgeting system is the Commonwealth's core enterprise budget system and has an approved appropriation of $4.0 million for FY 2015. Nearly half of the budget for this system supports contract and internal staffing. A large part of the remaining portion of the budget is used to repay a working capital advance that funded the development and implementation of the system.

The second ISF overseen by DOA is for the Payroll Services Bureau. The Payroll Services Bureau is a shared services center for processing payroll, leave, and other employee benefits at 58 state agencies. The FY 2015 approved appropriation for the Payroll Services Bureau ISF is $2.5 million. Nearly 70 percent of the budget for the Payroll Services Bureau supports staffing for payroll and benefits processing.

TABLE 5: DOA ISFs and services

Fund	Services provided	FY 2015 appropriation
Enterprise Application – Cardinal	Central financial reporting services	$17.6 million*
Enterprise Application – Performance Budgeting	Central budget reporting services	4.0
Payroll Service Bureau	Agency payroll, leave, and other employee benefits processing	2.5
Total all funds		**$24.1 million**

Source: 2014 Appropriation Act, Chapter 3.
* The ISF appropriation amount for Cardinal is to pay for the system's operations and maintenance expenses. In addition to these funds, DOA is expected to draw down $19.1 million in FY 2015 from a working capital advance to pay for one-time costs associated with implementing the Cardinal system statewide.

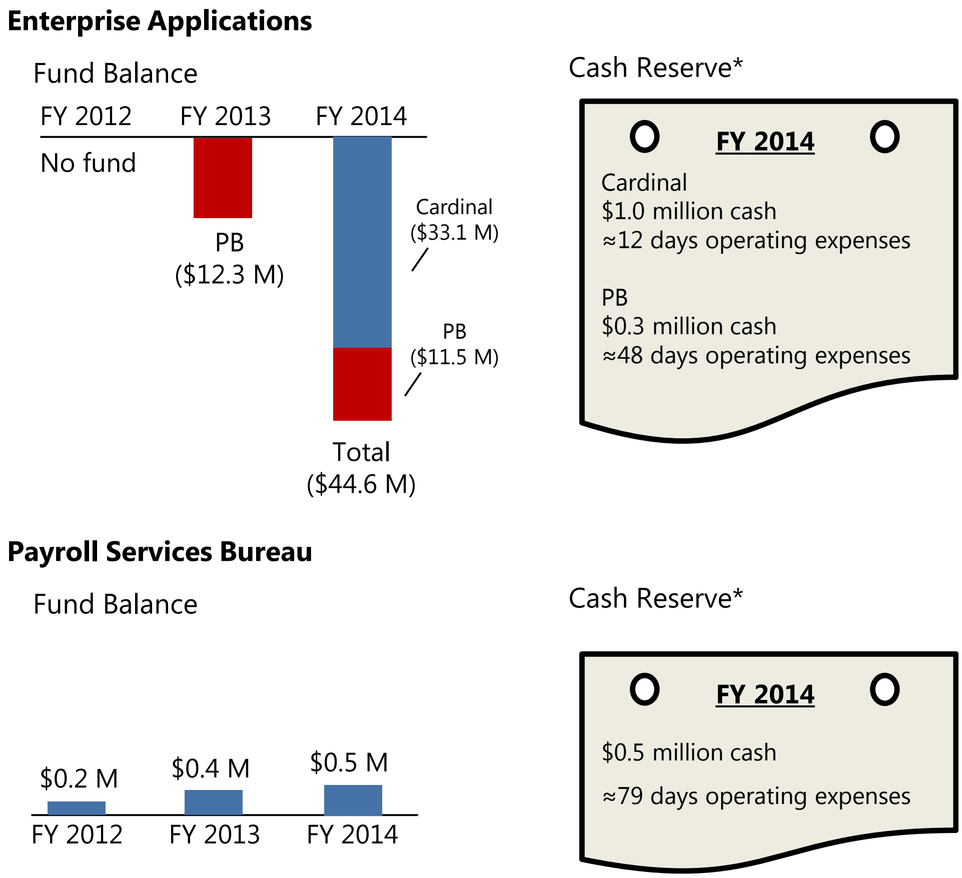
Fund status

DOA's Enterprise Applications ISF has a negative balance, which stems from the fund's creation and is expected to begin improving. DOA began collecting revenue for the Performance Budgeting portion of the Enterprise Applications ISF in FY 2013 and for the Cardinal portion in FY 2014. As of the end of FY 2014, the Enterprise Applications ISF had a negative fund balance of -$44.6 million, 75 percent of which was attributable to Cardinal (Figure 3). The negative balance reflects WCA debt used to fund the development and implementation of the systems. The negative balance will be reduced over time as DOA uses revenue recovered from customer agencies to pay back this debt.

The Enterprise Applications ISF appears to be maintaining an appropriate cash reserve, given the fund's relatively new status. The Cardinal portion of the fund had sufficient cash to cover 12 days of operating expenses and the Performance Budgeting portion had cash available to cover 48 days of expenses. The cash reserve for the fund is lower than the federal 60-day benchmark because cash is being used to pay not only operating costs but also project development costs. As the ISF begins recovering funds to pay back project development costs, the cash balance will improve. The Appropriation Act authorizes a Treasury loan in the event that the Enterprise Applications ISF does not have sufficient cash to cover expenses.

The Payroll Services Bureau ISF, which is more established than the Enterprise Applications ISF, currently has an appropriate balance and cash reserve. The Payroll Services Bureau ISF had a positive fund balance from FY 2012 through FY 2014 (Figure 3). The fund balance increased significantly in FY 2013, reflecting the need for a higher cash reserve. While the cash reserve exceeded the federal 60-day benchmark in FY 2014, it fell well short of the benchmark in FY 2012.

FIGURE 3: Key ISF status indicators



Source: DOA financial statements.
* The cash reserve represents the number of days of operating expenses that the end-of-year cash balance can cover.

Appropriations

DOA requests ISF appropriations according to what it expects to spend under its funds. DOA's appropriation requests are supported by estimates of future ISF expenditures. For the Enterprise Applications ISF, the estimates of future expenditures reflect the anticipated costs of operating and maintaining enterprise applications, including staff compensation, VITA expenses, payments to contractors, and repayment of the working capital advances used to develop and implement the systems. For the Payroll Services Bureau ISF, the estimates of future expenditures largely reflect the expected cost of compensating DOA staff that process agency payroll services. The governor's budget bill does not propose changes to the appropriations for DOA's ISFs from the levels approved in the 2014 Appropriation Act, Chapter 3 (Table 6).

TABLE 6: DOA's ISF budget by program*

	FY 2015	FY 2016
Enterprise Application (711)		
Governor's budget bill (2015) – Cardinal	$17,620,483	$17,973,016
Governor's budget bill (2015) – Performance Budgeting	3,961,775	3,961,775
Payroll Services Bureau (826)		
Governor's budget bill (2015)	2,495,148	2,495,148
Total ISF budget		
Governor's budget bill (2015)	**$24,077,406**	**$24,429,939**

Source: 2014 Appropriations Act (Chapter 3), and 2015 governor's budget bill.
* No changes are proposed to DOA's ISFs in the governor's budget bill compared to the 2014 Appropriation Act, Chapter 3. The ISF appropriation amounts for Cardinal are to pay for the system's operations and maintenance expenses. In addition to these funds, DOA is expected to draw down $19.1 million in FY 2015 and $13.5 million in FY 2016 from a working capital advance to pay for one-time costs associated with implementing the Cardinal system statewide.

Rates

The governor's budget bill does not propose changes to ISF rates in FY 2015 or FY 2016 for either the Enterprise Applications ISF or the Payroll Services Bureau ISF. DOA expects the rate charged for the Cardinal portion of the Enterprise Applications ISF to increase by 46 percent in FY 2017 (from $1.05 to $1.53 per financial transaction). This increase, which was expected when the ISF was established, will be required to repay the working capital advance (WCA) that was used to develop and implement Cardinal.

The governor's budget bill proposes increasing the WCA for Cardinal from $60 million to $75 million and adds language that would allow the WCA to pay for the development of other approved statewide systems. DOA indicated that the WCA increase would be used to develop an enterprise application to replace the state's payroll system (CIPPS). CIPPS will need to be replaced because the software provider for the 30-year-old system will cease providing support in 2018. This WCA increase will need to be recovered in future years through an increase in rates charged to customer agencies. DOA has not yet developed specific estimates for the expected rate increase or in which biennium the increase will occur.