OPPAGA
OFFICE OF PROGRAM POLICY ANALYSIS & GOVERNMENT ACCOUNTABILITY

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The Legislature Has Taken Steps to Promote the Self-Sufficiency of Regulatory Programs

at a glance

Consistent with our recommendations, the 2006 Legislature required agencies to begin reporting fiscal and self-sufficiency data for their regulatory programs. In addition, the Legislature created a workgroup to study the feasibility of developing a uniform cost allocation methodology for calculating and reporting direct and indirect unit costs.

Our review of legislative budget requests for a sample of regulatory programs revealed that most agencies generally provided complete documentation. However, some agencies inconsistently reported fiscal data and information related to self-sufficiency. To avoid these inconsistencies, the legislative budget requests could be modified in several ways.

Scope

In accordance with state law, this progress report describes actions taken by the Legislature to address the findings and recommendations of our 2005 report. [1]

Background

To promote public health, safety, and welfare, the Legislature has authorized programs to regulate various professions, businesses, and products. Funding for these programs is derived from three major sources—user charges, federal funds, and general revenue.

In general, user charges should be the primary source of funding for the state's regulatory programs and should be sufficient to cover all of the associated direct and indirect costs. [2, 3] In some cases, however, regulated programs provide a service that benefits the public, or it is not financially feasible to place the entire cost of regulation on the affected group. In these situations, subsidizing user fees with other revenues (e.g., general revenue) may be appropriate.

[1] *Legislature Should Consider Uniform Process to Determine Appropriate Regulatory Program Funding Levels,* OPPAGA Report No. 05-57, December 2005.

[2] Direct costs are labor and material costs that can be linked exclusively to the conduct of the regulatory program, and vary with fluctuations in the number of individuals or businesses being regulated. These costs would likely be eliminated if the regulatory program no longer existed.

[3] Indirect costs include the costs of providing executive direction, legal services, and administrative support services such as personnel, finance, and budgeting, as well as the costs of shared space, equipment, or services. Indirect costs also include the costs of program direction, program monitoring, rule making, and other activities that are essential to operate the program.

At the direction of the Legislature, in 2005 OPPAGA reviewed funding for 190 state regulatory programs. The review found that only 43% of regulatory programs were statutorily required to be self-sufficient. Furthermore, the review found that there was no overall legislative policy governing how regulatory programs should be funded, which resulted in regulatory programs varying widely with regard to self-sufficiency requirements, funding sources, and types of user fees assessed to regulated entities.

In addition, our prior report noted that several factors should be considered when determining the appropriate allocation of funding sources for regulatory programs. These factors include the distribution of benefits (e.g., benefits one specific group or the general public), the feasibility of collecting user fees, and the impact of various types of fees on regulated entities.

Finally, our 2005 report determined that the state accounting system hindered efforts to determine appropriate funding levels for regulatory programs, because the system does not identify the total direct costs for all regulatory programs, and agencies are using different methodologies to calculate the indirect costs of these programs. This limited the Legislature's ability to determine whether user charges are sufficient to meet funding requirements as well as to assess program alternatives such as privatization.

To address these concerns, we recommended four policy changes for the Legislature's consideration.

1. Eliminate statutory caps on regulatory fee amounts to help ensure that programs remain self-supporting over the long term. These limits can become outdated if not updated over time to reflect inflation.
2. Revise legislative budget requests (LBR) instructions to require agencies to provide written justification when requesting general revenue for a regulatory program, which would assist the Legislature in determining whether the program provides sufficient broad public benefits to justify general revenue funding.
3. Revise legislative budget request instructions to establish a uniform methodology for calculating regulatory program costs, which would help ensure that regulatory fees are based on total program costs.
4. Require agencies to establish rules regarding the mix of user charges needed to meet the funding requirements for each regulatory program. The rulemaking process would allow stakeholder involvement before a final determination is made. Involvement by administering agencies, program recipients, and consumers will help ensure that the appropriate amount is adopted for each of the various user charges that are available for each regulatory program.

Current Status

To address the issues highlighted in our prior report, the 2006 Legislature required agencies to begin reporting on the self-sufficiency of their regulatory programs via legislative budget requests. In addition, the Legislature created a workgroup to study the feasibility of developing a uniform cost allocation methodology for direct and indirect unit costs.

Our review of LBRs for a sample of regulatory programs revealed that agencies generally provided complete documentation as required. However, some agencies inconsistently reported fiscal data and provided minimal information about the self-sufficiency of their regulatory programs. To avoid these inconsistencies, the legislative budget requests could be modified in several ways.

The Legislature required agencies to submit regulatory program fiscal data and created a unit cost workgroup. Consistent with our recommendations, the 2006 Legislature enacted Ch. 2006-93, *Laws of Florida,* which expressed the Legislature's intent that the fees charged by state agencies for providing a regulatory service or regulating a profession or business cover the costs of services and/or oversight. The law also required that each state agency, as part of its legislative budget request, provide information regarding alternatives for realigning revenues or costs to make regulatory services and programs self-sufficient or justify a subsidy from other state funds. The Legislature will use this information to review the regulatory fee structure for all businesses and professions at least once every five years. Appendix A includes the legislative budget request schedule and forms developed per this law. [4]

In addition, Ch. 2006-146, *Laws of Florida,* addressed our recommendation regarding consideration of developing an agency uniform cost accounting methodology. Specifically, the law created a workgroup to develop a cost allocation methodology for agencies to use in the computation of activity and unit costs. To develop the cost allocation methodology, the Legislature directed the workgroup to consider federal standards and guidelines and to recommend procedures to ensure that the cost allocation methodology produces auditable activity and unit cost information that can be produced by the state accounting system and used to compare the performance of each reported activity over time.

To accomplish its purpose, the workgroup reviewed agencies' current method of calculating unit cost data submitted with their legislative budget requests. It also examined selected agencies' current use of federal Office of Management and Budget Circular A-87, direct and indirect cost allocation methodologies, and Statewide Cost Allocation Plan methodology. [5]

The workgroup concluded that, to fully achieve the primary goal of creating auditable and comparable unit cost data, the Legislature should consider a number of changes to current cost accounting and indirect cost allocation practices prior to the development of a new unit cost methodology. According to the workgroup, the implementation of any of these changes, separately or in combination, should result in a more comparable or uniform unit cost data. However, significant improvement with respect to comparability could only be achieved with the implementation of all or most of these changes. Proposed changes include

- re-evaluating and re-designing activities so that they are comparable across state agencies and developing a uniform method of accumulating activity costs;
- developing guidelines for uniformity in the types of costs that should be included and not included in the unit cost calculation;
- developing a uniform method for distributing agency indirect costs to activities for the purpose of calculating unit cost; and
- developing comparable data regarding the performance of private entities or finding existing unit cost data and determining if it is comparable to state agency activity unit cost data.

The workgroup reported that implementing these changes would require significant and potentially costly changes to current accounting and cost allocation practices. It also found that proposed changes should be thoroughly evaluated to determine the costs and benefits of switching to a uniform accounting process and suggested that the Legislature consider establishing a workgroup composed of agency experts in direct and indirect cost accounting to explore the cost benefits of the changes.

[4] In accordance with the new legislation, agencies submitted a Schedule 1A in their annual legislative budget requests for Fiscal Year 2007-08. The instructions were published by the Office of Policy and Budget and are designed to provide agencies with instructions for compiling their requests. Agencies are required to furnish a Schedule 1A for each regulatory program within a trust fund and for each trust fund.

[5] Circular A-87 is the federal cost allocation methodology that requires agencies to develop an indirect cost allocation plan to apportion their indirect costs to programs and activities. These plans would serve as the basis for computing indirect and direct costs for each regulatory program.

Agencies vary in how they are reporting regulatory program fiscal data and explaining lack of self-sufficiency. To assess agency implementation of the new regulatory program reporting requirements, OPPAGA reviewed legislative budget requests (LBRs) for the six agencies with the largest number of regulatory programs in our 2005 report. [6] For each agency, we examined the related LBR schedules for their five regulatory programs with highest annual expenses. However, because two of the agencies did not provide program specific budgets, we reviewed all of the regulatory programs in the legislative budget requests for these agencies. Therefore, our sample included 61 regulatory programs across six agencies.

For each regulatory program within our sample, we determined

- if all of the required documentation was present;
- if it was possible to determine regulatory program self-sufficiency from the documentation provided; and
- whether an explanation was provided when general revenue was used to subsidize a regulatory program.

Our review determined that agencies vary widely in the completeness of the regulatory program information provided in their legislative budget requests. The majority of the agencies in our sample provided complete documentation for most of their regulatory programs. However, some agencies provided incomplete fiscal data and/or did not adequately document self-sufficiency for their regulatory programs. Without comprehensive information about all regulatory programs, the Legislature will have difficulty conducting its review of the regulatory fee structure for all businesses and professions every five years.

For example, four of the six agencies we reviewed provided generally complete fiscal information for each regulatory program as required by LBR instructions. As required, these agencies furnished individual budget schedules for each regulatory program.

However, two of the agencies in our sample generally provided inadequate fiscal information for their regulatory programs. These agencies typically combined multiple regulatory programs into a single budget schedule in their LBR. In total, 41 regulatory programs of these two agencies were not reported as separate budget schedules but were instead combined into five generic budget schedules. In addition, no budget schedule was provided for three regulatory programs. As a result, legislators and budget staff cannot determine the individual regulatory program expenditures and revenues and the level of self-sufficiency for these programs. This is problematic, because it impedes the determination of whether the fees charged by state agencies for providing a specific regulatory service or regulating a profession or business cover the direct and indirect costs of services and/or oversight.

Moreover, three of the six agencies sometimes provided insufficient detail in response to LBR questions about plans to attain self-sufficiency or achieve operational efficiencies. For example, some agencies provided "yes" or "no" answers in response to questions such as, "Can operational efficiencies be achieved in the underlying program?" Such responses do not provide the Legislature enough detail to determine if the agencies have assessed the self-sufficiency of their regulatory programs and made feasible plans to improve self-sufficiency and/or operational efficiecy.

Steps could be taken to clarify LBR instructions and ensure accurate reporting of regulatory program data. To address this problem, we identified options for improving the LBRs to help ensure that the Legislature has adequate information to complete its comprehensive review of the regulatory fee structure for all businesses and professions.

[6] The six agencies are the Agency for Health Care Administration and Departments of Agriculture and Consumer Services, Business and Professional Regulation, Environmental Protection, Financial Services, and Health.

Specifically, some questions in the *Examination of Regulatory Fees: Part I* (see Appendix A, page 7), could be rephrased or expanded. For example, Question 1 could be revised to ask, "What specific steps has the agency taken to maximize operational efficiencies in the underlying program?" Phrasing the question in this manner would encourage the provision of complete answers rather than "yes" or "no" responses. In addition, the LBR form could be revised to include the questions below.

- What recent operational efficiencies have been achieved to either decrease costs or improve services? If costs have been reduced, how much money has been saved during the fiscal year?
- What additional operational efficiencies are planned? What are the estimated savings associated with these efficiencies during the next fiscal year?
- If the regulatory program is not self-sufficient, can the regulated business/profession reasonably support a fee increase? If "yes," how much? If "no," why not?
- If the regulatory program is not self-sufficient and provides a public benefit worthy of state subsidization, please provide a plan for reducing the state subsidy.

In addition, budget directors who provided us feedback made several suggestions for improving the regulatory program related LBR instructions. These suggestions included more clearly defining what constitutes a regulatory program, delineating the specific revenues to include in the schedules, and providing a preferred methodology for accounting for indirect costs. Moreover, one budget director noted that it would be helpful to have a clear explanation of how the information provided in the LBRs will be used, to ensure that the data best meets legislative needs.

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Appendix A

Legislative Budget Request Schedule and Forms for Regulatory Programs

SCHEDULE 1A: DETAIL OF FEES AND RELATED PROGRAM COSTS

Department: ______________ **Budget Period: 20___-___**
Program: ______________
Fund: ______________

Specific Authority: ______________
Purpose of Fees Collected: ______________

Type of Fee or Program: (Check **ONE** Box and answer questions as indicated.)

☐	Regulatory services or oversight to businesses or professions (Complete Sections I, II, and III and attach **Examination of Regulatory Fees** Form - Part I and II.)
☐	Non-regulatory fees authorized to cover full cost of conducting a specific program or service. (Complete Sections I, II, and III only.)

SECTION I - FEE COLLECTION	**ACTUAL FY 20 ___ - ___**	**ESTIMATED FY 20 ___ - ___**	**REQUEST FY 20 ___ - ___**
Receipts:			
______________			
______________			
______________			
______________			
Total Fee Collection to Line (A) - Section III	-	-	-
SECTION II - FULL COSTS			
Direct Costs:			
Salaries and Benefits			
Other Personal Services			
Expenses			
Operating Capital Outlay			
______________			
______________			
Indirect Costs Charged to Trust Fund			
Total Full Costs to Line (B) - Section III	-	-	-

Basis Used: ______________

SECTION III - SUMMARY				
TOTAL SECTION I	(A)	-	-	-
TOTAL SECTION II	(B)	-	-	-
TOTAL - Surplus/Deficit	(C)	-	-	-

EXPLANATION of LINE C:

____

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Examination of Regulatory Fees – Part I

Department:____

Regulatory Service to or Oversight of Businesses or Professions
Program:____

1. Can operational efficiencies be achieved in the underlying program? If so describe the efficiencies proposed.

2. Is the regulatory activity an appropriate function that the agency should continue at its current level?

3. Are the fees charged for the regulatory service or oversight to businesses or professions based on revenue projections that are prepared using generally accepted governmental accounting procedures or official estimates by the Revenue Estimating Conference, if applicable?

4. Are the fees charged for the regulatory service or oversight to businesses or professions adequate to cover both direct and indirect costs of providing the regulatory service or oversight?

5. Are the fees charged for the regulatory service or oversight to businesses or professions reasonable and do they take into account differences between the types of professions or businesses that are regulated? For example, do fees reflect the amount of time required to conduct inspections by using a sliding scale for annual fees based on the size of the regulated business; or do fees provide a financial incentive for regulated entities to maintain compliance with state standards by assessing a re-inspection fee if violations are found at initial inspection?

6. If the fees charged for the regulatory services or oversight to businesses or professions are **not** adequate to cover direct and indirect program costs provide either:

   a) information regarding alternatives for realigning revenues or costs to make the regulatory service or program totally self-sufficient, including any statutory changes that are necessary to implement the alternative; or

   b) demonstrate that the service or program provides substantial benefits to the public which justify a partial subsidy from other state funds, specifically describing the benefits to the general public (statements such as 'providing consumer benefits' or 'promoting health, safety and welfare' are not sufficient justification). For example, the program produces a range of benefits to the general public, including pollution reduction, wildlife preservation, and improved drinking water supply. Alternatively, the agency can demonstrate that requiring self-sufficiency would put the regulated entity at an unfair advantage. For example, raising fees sufficiently to cover program costs would require so high an assessment as to damage its competitive position with similar entities in other states.

Office of Policy and Budget - July, 2007

Examination of Regulatory Fees - Part II

Department:

Regulatory Service to or Oversight of Business or Profession Program:

Does Florida Statutes require the regulatory program to be financially self-sufficient? (Yes or No and F.S.):

What percent of the regulatory cost is currently subsidized? (0 to 100%)

If the program is subsidized from other state funds, what is the source(s)?

What is the current annual amount of the subsidy? $

Service / Product Regulated	Specific Fee Title	Statutory Authority for Fee	Maximum Fee Authorized (cap)	Year of Last Statutory Revision to Fee	Is Fee Set by Rule? (Yes or No)	Current Fee Assessed	Fund Fee Deposited in (indicate General Revenue or Specific Trust Fund)