
INTRODUCTORY SECTION

Comptroller's Letter of Transmittal to the Governor
Certificate of Achievement for Excellence in Financial Reporting
Organization of Executive Branch of Government
Organization of Government – Selected Government Officials – Executive Branch
Organization of the Department of Accounts



COMMONWEALTH of VIRGINIA

DAVID A. VON MOLL, CPA
COMPTROLLER

Office of the Comptroller

P. O. BOX 1971
RICHMOND, VIRGINIA 23218-1971

December 15, 2011

The Honorable Robert F. McDonnell
Governor of the Commonwealth of Virginia
State Capitol
Richmond, Virginia 23219

Dear Governor McDonnell:

It is my pleasure to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2011, in accordance with Section 2.2-813 of the *Code of Virginia*. This report consists of management's representations concerning the Commonwealth of Virginia's finances. Management assumes full responsibility for the completeness and reliability of all information presented. This report reflects my commitment to you, to the citizens of the Commonwealth, and to the financial community to maintain our financial statements in conformance with accounting principles generally accepted in the United States of America (GAAP) as established by the Governmental Accounting Standards Board (GASB). Data presented in this report is believed to be accurate in all material respects, and all disclosures that are necessary to enable the reader to obtain a thorough understanding of the Commonwealth's financial activities have been included.

The 2011 CAFR is presented in three sections. The Introductory Section includes this transmittal letter and organization charts for state government. The Financial Section includes the State Auditor's Report, management's discussion and analysis (MD&A), audited government-wide and fund financial statements and notes thereto, required supplementary information other than MD&A, and the underlying combining and individual fund financial statements and supporting schedules. The Statistical Section sets forth selected unaudited economic, financial trend, and demographic information for the Commonwealth on a multi-year basis.

The Commonwealth's management is responsible for the establishment and maintenance of internal accounting controls that ensure assets are safeguarded and financial transactions are properly recorded and adequately documented. To ensure that the costs of controls do not exceed the benefits obtained, management is required to use cost estimates and judgments to attain reasonable assurance as to the adequacy of such controls. The Commonwealth's established internal controls fulfill these requirements.

In accordance with Section 30-133 of the *Code of Virginia*, the Auditor of Public Accounts has audited the Commonwealth's financial statements for the year ended June 30, 2011. The audit was conducted in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards issued by the Comptroller General of the United States. The auditor's opinion is included in the Financial Section of this report. Audit testing for compliance with the Federal Single Audit Act Amendments of 1996 and the related OMB Circular A-133 is performed at the statewide level. The Commonwealth's Single Audit Report will be issued at a later date. I would like to acknowledge the Auditor of Public Accounts' staff for their many contributions to the preparation of this report.

GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, requires that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of MD&A. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. In addition to the financial analysis addressing the Commonwealth's governmental and business-type activities, the MD&A focuses on the Commonwealth's major funds: the General Fund, the Commonwealth Transportation Special Revenue Fund, the Federal Trust Special Revenue Fund, the Literary Special Revenue Fund, the State Lottery Fund, the Virginia College Savings Plan Fund, and the Unemployment Compensation Fund. The Commonwealth's MD&A can be found on page 27 immediately following the independent auditor's report.

PROFILE OF THE GOVERNMENT

REPORTING ENTITY

For financial reporting purposes, the Commonwealth's reporting entity consists of (1) the primary government, (2) component unit organizations for which the primary government is financially accountable (blended component units), and (3) other component unit organizations for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete (discrete component units). The funds and accounts of all agencies, boards, commissions, foundations, and authorities that have been identified as part of the primary government or a component unit have been included. Further information can be found in Note 1.B. to the Financial Statements.

Section 2100 of the GASB *Codification of Governmental Accounting and Financial Reporting Standards* describes the criteria for determining which organizations, functions, and activities should be considered part of the Commonwealth for financial reporting purposes. The basic criteria include appointing a voting majority of an organization's governing body, as well as the Commonwealth's ability to impose its will on that organization, or the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Commonwealth. The Commonwealth's discretely presented major component units are the Virginia Housing Development Authority, Virginia Public School Authority, University of Virginia, Virginia Polytechnic Institute and State University, and Virginia Commonwealth University.

The Commonwealth and its component units provide a wide range of services and funding to its citizens, including elementary, secondary and higher education; health and human services; economic development; environment and natural resources; public safety, corrections, and regulation; transportation; agriculture; and general government services. The financial activities associated with these services are reflected in both summary and detail throughout the CAFR.

BUDGETARY CONTROL

In addition to the internal controls previously discussed, the Commonwealth maintains budgetary controls to ensure compliance with the legal provisions of the Commonwealth's Appropriation Act, which reflects the General Assembly's approval of a biennial budget. The financial transaction process begins with development and approval of the budget, after which budgetary control is maintained through a formal appropriation and allotment system. The budgeted amounts reflected in the accompanying financial statements represent summaries of agency budgets.

The Commonwealth's budget is prepared principally on a cash basis and represents appropriations as authorized by the General Assembly on a biennial basis at the program level. The Commonwealth monitors spending activity to ensure the expenditures do not exceed the appropriated amounts at the agency level. The State Comptroller maintains a central general ledger that records total appropriations and related expenditures for all agencies and institutions included in the approved budget. Systemic controls are in place to prevent disbursements that exceed authorized appropriations. Additional information regarding the Commonwealth's budgetary process can be found in Note 1.E. to the Financial Statements.

Economic Review

Local Economy

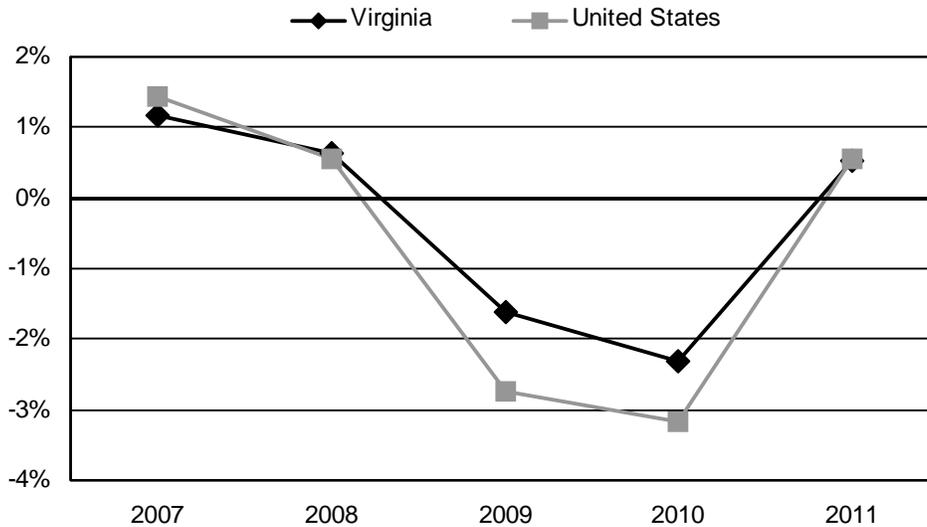
Introduction

This economic overview for the Commonwealth of Virginia was prepared by the economics research team at Virginia Commonwealth University's Center for Urban Development. In fiscal year 2011, Virginia's economy began what appears to be a slow recovery path following the so-called "Great Recession" – the worst financial and economic downturn in the United States since the "Great Depression" of the 1930's. It is still too early to tell whether this downturn has been reversed for the state and the nation. Data presented in this report, however, allow us to be fairly optimistic – particularly for Virginia, where the recent upturn in economic indicators has been greater than at the national level. All of the data are the most recent available for the time period covered. This means that many of the earlier observations in last year's analysis have been revised to incorporate new benchmarks and more plentiful information.

Employment

After a dramatic decrease of 3.9 percent and the loss of almost 150,000 jobs between fiscal years 2007 and 2010, Virginia's nonfarm payroll employment experienced slight growth to a level of 0.5 percent in fiscal year 2011 (see **Figure 1**). The change in employment was small (just 18,600 jobs created in fiscal year 2011) and it is still too early to know for sure if the economic downturn has reversed.

Figure 1
Annual Percentage Change in Nonfarm Payroll Employment
Fiscal Years 2007 - 2011



Source: U.S. Bureau of Labor Statistics

Figure 2 shows changes in Virginia's nonfarm employment by industry for fiscal years 2007 - 2011, along with the employment change between fiscal years 2010 and 2011 for Virginia and the U.S. Fiscal year 2011 showed timid signs of economic recovery at both the state and national levels, following a three-year period (from 2008 to 2010) in which almost all industry groups experienced significant job losses. Notable exceptions to the upturn in fiscal year 2011 are construction, manufacturing, information services, financial activities, leisure and hospitality, and local government. Each of these sectors had a decline in employment between fiscal years 2010 and 2011. The largest decreases in nonfarm employment in Virginia, between fiscal years 2010 and 2011, were in information services (a loss of 4.4 percent, or 3,400 jobs) and local government (a loss of 1.9 percent, or 7,200 jobs).

Figure 2
Nonfarm Payroll Employment
Fiscal Years 2007 - 2011

NAICS Industry*	Virginia Employment (000)					Change, Fiscal Year 2011 over Fiscal Year 2010		
	2007	2008	2009	2010	2011	Virginia		U. S.
						Number (000)	Percent	Percent
Mining and Logging	11.2	10.8	10.9	10.1	10.4	0.3	3.0	10.1
Construction	244.7	232.7	206.2	184.0	183.5	(0.5)	(0.3)	(2.6)
Manufacturing	282.8	271.5	252.5	233.1	230.9	(2.2)	(0.9)	0.8
Wholesale Trade	120.6	120.5	116.6	109.9	111.0	1.1	1.0	0.3
Retail Trade	425.4	426.2	409.3	396.9	402.3	5.4	1.4	0.4
Transportation and Utilities	119.4	119.7	116.2	111.8	112.3	0.5	0.4	1.2
Information Services	91.2	89.1	84.5	77.9	74.5	(3.4)	(4.4)	(1.8)
Financial Activities	195.1	191.1	184.5	177.9	177.4	(0.5)	(0.3)	(0.8)
Professional and Business Services	637.6	653.3	649.9	640.4	657.2	16.8	2.6	2.5
Educational and Health Services	411.9	430.4	444.9	452.8	459.3	6.5	1.4	2.1
Leisure and Hospitality	342.4	348.6	345.1	339.4	335.3	(4.1)	(1.2)	0.9
Other Services	183.6	187.3	187.8	185.0	185.5	0.5	0.3	1.5
Federal Government	156.3	157.4	163.2	171.0	173.3	2.3	1.3	(2.3)
State Government	153.2	153.2	153.5	152.8	156.0	3.2	2.1	(0.4)
Local Government	370.1	377.0	382.3	379.1	371.9	(7.2)	(1.9)	(1.7)
Total	3,745.5	3,768.8	3,707.4	3,622.1	3,640.8	18.7	0.5	0.5

Source: U. S. Bureau of Labor Statistics
* North American Industry Classification System

Figure 3 shows the annual percentage change in nonfarm employment for ten of the eleven Metropolitan Statistical Areas (MSAs) in Virginia. The Kingston-Bristol MSA is not included in this table because most of it is located in Tennessee and data are not reported separately for the Virginia portion of the MSA. It should be noted, also, that three MSAs – Northern Virginia, Virginia Beach-Norfolk-Newport News (typically referred to as the Hampton Roads MSA), and Richmond – have accounted for over 75 percent of Virginia’s nonfarm payroll employment in recent years. This is particularly significant when we compare data from fiscal year 2011 with fiscal years 2009 and 2010. In fiscal years 2009 and 2010, each of Virginia’s MSAs experienced job losses. In 2011, however, over half of the MSAs reversed this negative trend and, once again, had positive job growth. The Northern Virginia MSA alone increased its employment by 14,600, a positive percentage change of 1.1 percent over fiscal 2010. In the Richmond and Hampton Roads MSAs, however, declines in employment continued (combined, a loss of almost 3,000 jobs).

Figure 3
Nonfarm Payroll Employment in Virginia’s MSAs
 Fiscal Years 2007 - 2011

Area	Percent Change				
	2007	2008	2009	2010	2011
Virginia	1.2	0.6	(1.6)	(2.3)	0.5
Metropolitan areas^(a)					
Blacksburg-Christiansburg-Radford	(0.6)	(0.0)	(0.6)	(3.8)	(0.1)
Charlottesville	4.0	1.4	(1.6)	(1.9)	0.8
Danville	(4.7)	0.4	(1.4)	(4.1)	1.7
Harrisonburg	3.6	(1.4)	(1.7)	(1.7)	1.3
Lynchburg	1.5	1.1	(1.5)	(4.1)	1.1
Northern Virginia	1.6	0.8	(0.9)	(0.8)	1.1
Richmond	1.8	0.3	(2.0)	(3.2)	(0.1)
Roanoke	1.2	(0.1)	(2.2)	(3.0)	(0.5)
Virginia Beach-Norfolk-Newport News ^(b)	0.8	0.2	(2.4)	(2.6)	(0.3)
Winchester ^(c)	2.9	(2.0)	(3.5)	(2.8)	2.4

Source: U. S. Bureau of Labor Statistics

(a) Excludes Kingsport-Bristol MSA, most of which is located in Tennessee

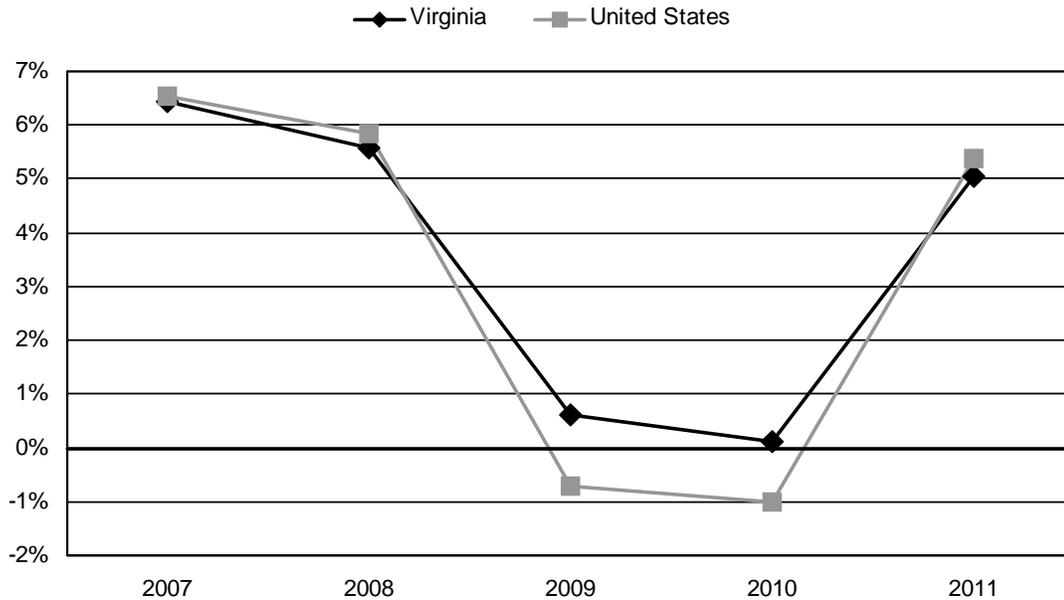
(b) Includes portion in North Carolina

(c) Includes portion in West Virginia

Personal Income

Personal income is an important indicator of Virginia's economy because most of the state government revenues, income and retail taxes in particular, are directly or indirectly related to personal income. As shown in **Figure 4**, personal income increased dramatically in fiscal year 2011. Following three years of declining personal income, there was an increase of 5.0 percent in Virginia and 5.4 percent at the national level.

Figure 4
Percentage Change in Personal Income
Fiscal Years 2007 - 2011



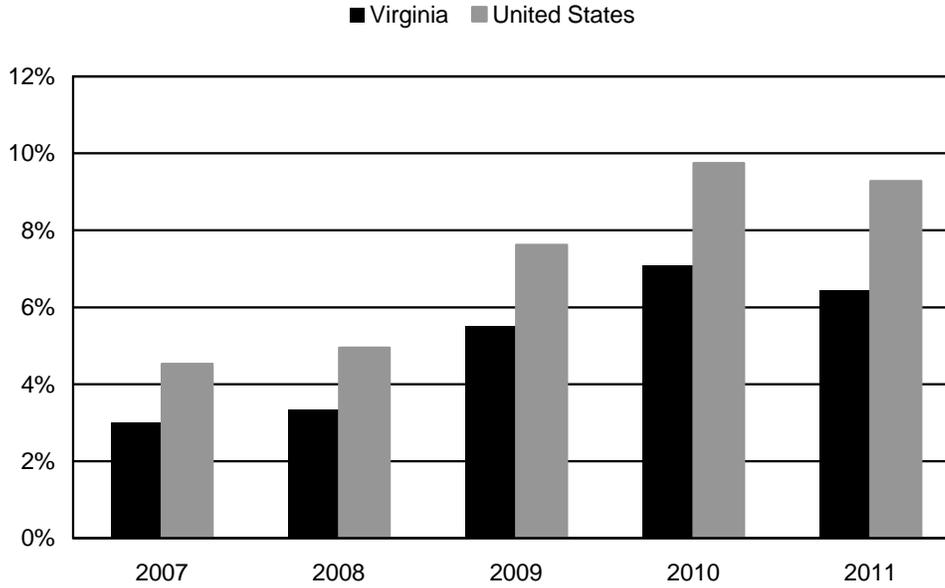
Source: U.S. Bureau of Economic Analysis, Regional Economic Information System

Each of the three major components of personal income – net earnings by place of residence; dividends, interest and rent; and transfer payments – experienced a significant increase during fiscal year 2011. The most important of these three components (net earnings by place of residence) grew only 4.3 percent in Virginia, however, as compared with 5.2 percent growth for the U.S.

Unemployment

After three fiscal years (2008, 2009, and 2010) during which unemployment grew dramatically, the unemployment rate finally decreased at both the state and national levels in fiscal year 2011 (**Figure 5**). Although we are still far from the low unemployment rates of the period before the recent recession (3.0 percent in Virginia and 4.5 percent in the U.S., during 2007), the decline in unemployment rates is an important indicator that allows us to be optimistic for the future of Virginia's economy.

Figure 5
Civilian Unemployment Rate
 Fiscal Years 2007 - 2011



Source: U.S. Bureau of Labor Statistics and Virginia Employment Commission

Figure 6 shows unemployment rates for each of Virginia's MSAs over a period of five fiscal years. Each MSA had a lower unemployment rate in fiscal year 2011 than in fiscal year 2010, although some, primarily Danville and Kingsport-Bristol, maintained rates that were significantly higher than the state average. In contrast, the lowest unemployment rates in fiscal year 2011 were in the Northern Virginia (4.8 percent) and Charlottesville (5.4 percent) MSAs.

Figure 6
Civilian Unemployment Rate for Virginia's MSAs
 Fiscal Years 2007 - 2011

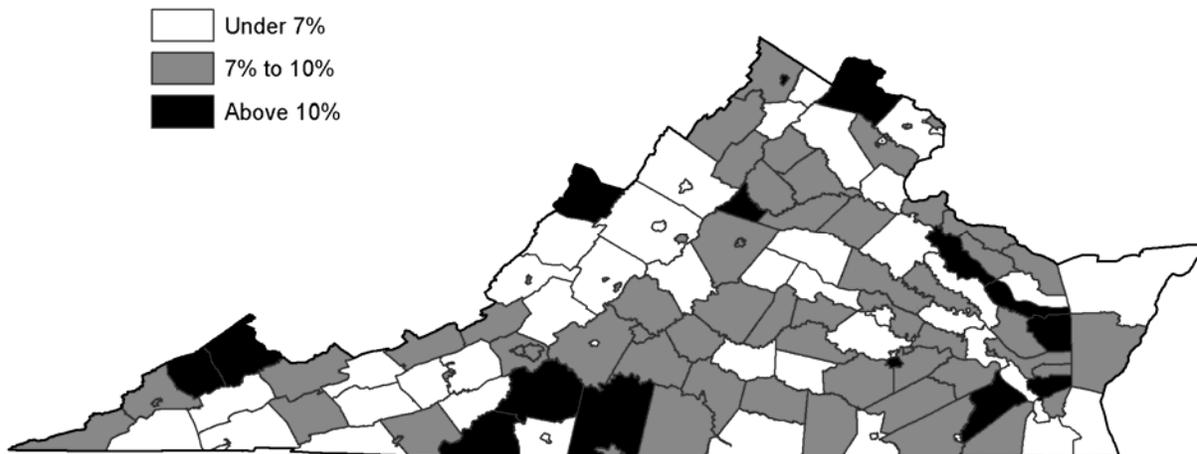
Area	Unemployment Rate (Percent)				
	2007	2008	2009	2010	2011
Virginia	3.0	3.3	5.5	7.1	6.5
Metropolitan areas					
Blacksburg-Christiansburg-Radford	3.7	4.0	7.0	8.6	7.4
Charlottesville	2.5	2.7	4.6	6.0	5.4
Danville	6.7	6.4	10.3	12.0	10.4
Harrisonburg	2.5	3.0	5.2	6.6	6.2
Kingsport-Bristol*	4.4	4.8	7.2	9.3	8.6
Lynchburg	3.3	3.6	6.0	7.9	7.2
Northern Virginia	2.2	2.5	4.2	5.3	4.8
Richmond	3.1	3.5	6.0	8.0	7.3
Roanoke	3.1	3.4	5.7	7.7	6.9
Virginia Beach-Norfolk-Newport News*	3.2	3.6	5.7	7.4	7.1
Winchester*	2.8	3.5	6.4	7.6	6.5

Source: U.S. Bureau of Labor Statistics and Virginia Employment Commission

* Includes only the portion of the MSA located in Virginia

In **Figure 7**, each of Virginia's localities (95 counties and 39 independent cities) is color coded according to its unemployment rate. Three categories are represented on the map: unemployment rates that are under 7 percent, 7 to 10 percent, and above 10 percent. The map for fiscal year 2011 includes localities with higher unemployment rates (above 7 percent) in most of Virginia's MSA regions – including Northern Virginia and Hampton Roads.

Figure 7
Unemployment Rate by Locality
 Fiscal Year 2011

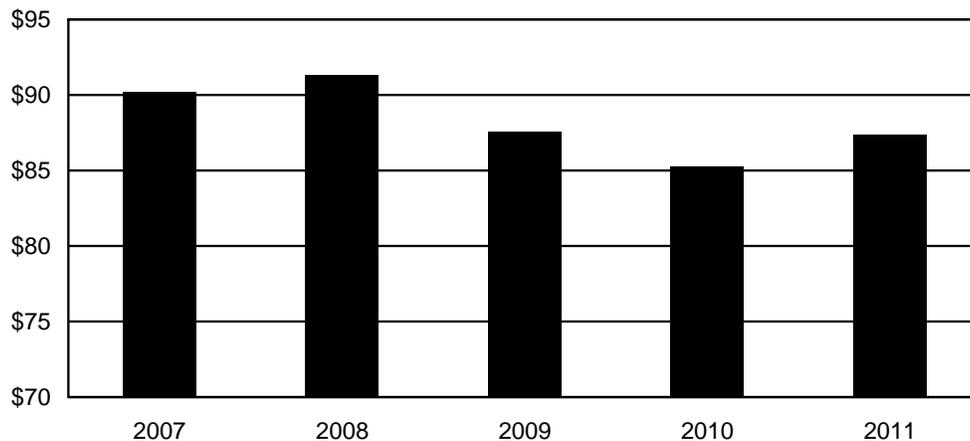


Source: Virginia Employment Commission

Taxable Sales

Since current data on retail sales are not produced for states, this report follows the approach used in previous years and presents information on taxable sales. These data are used as a proxy for retail sales, even though they do not include motor vehicle and motor fuel sales. (Unlike the Census Bureau's data on retail sales, however, taxable sales includes sales at restaurants and lodging places.) **Figure 8** shows that after two years of sharp decline, fiscal year 2011 registered a slight upturn with total taxable sales around \$87 billion. This level was 2.5 percent greater than fiscal year 2010, but still down from a high during the five-year period of \$91 billion in fiscal 2008.

Figure 8
Taxable Retail Sales in Virginia
 Fiscal Years 2007 – 2011

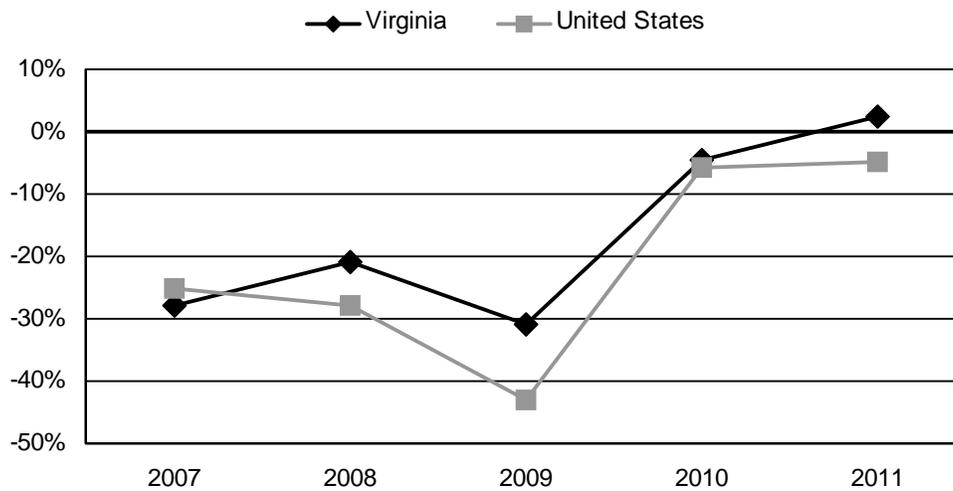


Source: Virginia Department of Taxation

Housing Market

After three fiscal years of dramatic decline (fiscal years 2007 to 2009) where the annual percentage change in new privately owned housing units authorized in Virginia ranged between negative 20.0 percent and negative 30.0 percent, fiscal years 2010 and 2011 showed some signs of recovery, especially in Virginia. While fiscal year 2010 still showed a decline in new units authorized (percentage change of negative 4.5 percent), Virginia experienced a positive, although small, percentage change (2.5 percent) in fiscal year 2011 for the first time since the recession. For the U.S. as a whole, however, the decline is still ongoing (percentage change of negative 4.9 percent in fiscal year 2011), although not at the high levels reached during the recession – a time when the percentage change in new units authorized dropped to a low of negative 42.9 percent in fiscal year 2009 (**Figure 9**).

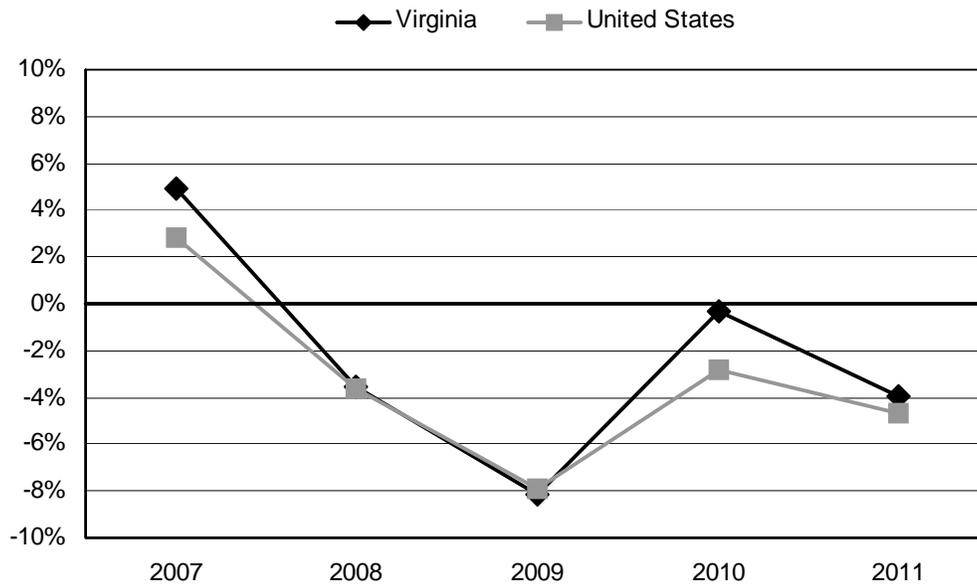
Figure 9
New Privately Owned Housing Units Authorized
Annual Percentage Change
Fiscal Years 2007 – 2011



Source: U.S. Census Bureau

Finally, another indicator for understanding Virginia's housing market is the percentage change in house prices published by the Federal Housing Finance Agency. **Figure 10** shows what can be considered the most significant negative data for fiscal year 2011 included in this report. Following a steep decline during the economic recession (a drop of almost 8.0 percent at both state and national levels) and a timid recovery in 2010 (a decline of only 0.4 percent in Virginia), fiscal year 2011 saw housing prices dropping again. During fiscal year 2011, housing prices fell by 4.0 percent in Virginia and 4.7 percent nationally.

Figure 10
Percentage Change in Housing Prices
Fiscal Years 2007 - 2011



Source: Federal Housing Finance Agency

Conclusion

Fiscal year 2011 can be considered as a year of economic growth, following the previous three years when the Great Recession severely impacted the state and national economies. It is still too early to know if the upturns are trends that will continue, but economic indicators are showing positive signs. While it is important to keep in mind that most of the data presented in this report for fiscal year 2011 are at levels lower than they were before the recession, fiscal year 2011 data allow us to be optimistic for Virginia. The Commonwealth has performed better than the nation in many areas of growth. Most of the success of this recovery, however, will depend on the next fiscal year, when the economic indicators need to confirm these signs of economic recovery.

MAJOR INITIATIVES

The CAFR has received unqualified audit opinions from fiscal year 1986 through fiscal year 2010. During this period, the Commonwealth has also received the Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting. While we are very proud of these unqualified audit opinions and awards, we must be mindful of the fact that they are not automatic. The successes of the State Comptroller's office are directly attributable not only to the professionalism, experience and integrity of the State Comptroller's technical and accounting personnel, but also to the professionalism, experience and integrity of the financial and accounting personnel throughout the Commonwealth. These major initiatives will support efforts to continue our legacy of quality financial management.

LONG-TERM FINANCIAL PLANNING

In 1992, an amendment to the Constitution of Virginia required the establishment of a Revenue Stabilization Fund. Annually, revenue collections are evaluated to determine whether deposits are required to the Fund. Withdrawals can only occur if the general fund revenues appropriated exceed the revised general fund revenue forecast by more than two percent of the certified tax revenues collected in the most recently ended fiscal year. Additionally, a withdrawal from the Fund cannot compensate for more than one-half of the difference between the general fund appropriations and revised estimate nor can it exceed more than one-half of the Fund balance. Further, pursuant to the constitutional amendment of Article X, Section 8, effective January 1, 2011, the amount on deposit cannot exceed 15 percent of the Commonwealth's average annual tax revenues derived from taxes on income and retail sales for the preceding three fiscal years. This is an increase of the previous limit of 10 percent.

ENTERPRISE APPLICATION PROJECT

The Cardinal Project represents a shared vision between the offices of the Secretary of Transportation, Secretary of Finance and the Virginia Information Technologies Agency to replace the Commonwealth's financial system (CARS) and the Virginia Department of Transportation's (VDOT) financial system with a modern enterprise wide financial system (base financial system). The base financial system will provide a solid foundation for the Commonwealth to expand system functionality and facilitate better integration of key administrative systems across the state. This foundation will enable the Commonwealth to re-engineer activities to include taking advantage of shared services, increasing functionality for better fiscal management, and reducing redundant agency financial systems and related cost. The Cardinal project will implement the base financial system in two phases. The first phase implemented VDOT's planned functionality on December 5, 2011, and the second phase will implement the Commonwealth's base financial system at the Department of Accounts (DOA) in calendar year 2012. A future phase of the project includes rolling Cardinal out to all other state agencies, at which time CARS and potentially other redundant financial systems could be retired. DOA has representation on the Steering Committee and has assigned full-time resources to this project.

AMERICAN RECOVERY AND REINVESTMENT ACT

In February 2009, the United States Congress and the President passed the American Recovery and Reinvestment Act (ARRA) to help facilitate recovery for the nation's economy. In order to provide reporting transparency and appropriate use of these monies, stringent reporting requirements accompanied these federal funds. In order to help ensure the Commonwealth complied with the ARRA reporting requirements, the Comptroller's staff facilitated collaboration through a variety of communications with fiscal officers throughout the Commonwealth and modified the General Ledger to allow separate reporting for each individual ARRA grant. Further, the Comptroller's staff performed validation reviews of information being reported to the Office of Management and Budget throughout fiscal year 2011.

AWARDS AND ACKNOWLEDGMENTS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded the Certificate of Achievement for Excellence in Financial Reporting to the Commonwealth for its CAFR for the fiscal year ended June 30, 2010. The Certificate of Achievement is a prestigious national award that recognizes conformance with the highest standards for preparation of state and local government financial reports. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report that conforms to program standards. Such reports must satisfy both accounting principles generally accepted in the United States of America and all applicable legal requirements.

A Certificate of Achievement is valid for a period of one year. The Commonwealth has received a Certificate of Achievement for the last 25 consecutive years (fiscal years 1986-2010). I believe that this year's report continues to conform to the Certificate of Achievement program requirements and we are submitting it to GFOA.

This report could not have been prepared without the full cooperation of all state agencies within the Executive Branch, the Legislature, the Judiciary, the Component Units, and especially the dedication and professionalism of the financial reporting staff in the Department of Accounts.

Respectfully submitted,

David A. Von Moll
Comptroller of the Commonwealth of Virginia

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Commonwealth of Virginia

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2010

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director