

Management's Discussion and Analysis

The following is a discussion and analysis of the Commonwealth of Virginia's (Commonwealth) financial performance, including an overview and analysis of the financial activities of the Commonwealth for the fiscal year ended June 30, 2002. Readers should consider this information in conjunction with the transmittal letter, which is located in the Introductory Section of this report, and the Commonwealth's financial statements, which are located after this analysis. The Commonwealth implemented the new reporting standard, GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* during FY 2002. GASB Statement No. 34 requires the inclusion of infrastructure and the use of full accrual accounting in the Government-wide Statements. Since this is the first year of implementation much of the information reported in the financial statements is not comparable to prior years. As a result, this discussion and analysis provides few comparisons with FY 2001, but future reports will include extensive comparisons.

FINANCIAL HIGHLIGHTS

Government-wide Highlights

The Commonwealth's assets exceeded its liabilities at June 30, 2002, by \$11.3 billion. Net assets of governmental activities increased by \$237.9 million and net assets of business type activities decreased by \$338.9 million.

Fund Highlights

At the end of the fiscal year, the Commonwealth's governmental funds reported a combined ending fund balance of \$1.9 billion, a decrease of \$825.9 million in comparison with the prior year. Of this total fund balance, \$1.3 billion represents unreserved fund balance and the remaining \$629.6 million represents amounts reserved for specific purposes, such as the Revenue Stabilization Fund and education. The proprietary funds reported net assets at June 30, 2002, of \$814.9 million, a decrease of \$339.5 million during the year.

Long-term Debt

The Commonwealth's total debt rose during the fiscal year to \$17.4 billion, an increase of \$2.6 billion or 17.7 percent. During FY 2002, the Commonwealth issued \$2.6 billion of new debt. More detailed information regarding these activities begins on page 238.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is an introduction to the Commonwealth's basic financial statements, which include three components: 1) government-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. The report also contains additional required supplementary information and other information.

Government-wide Statements

The government-wide financial statements are designed to provide readers with a broad overview of the Commonwealth's finances in a manner similar to a private-sector business. The statements provide both short-term and long-term information about the Commonwealth's financial position which helps readers determine whether the Commonwealth's financial position has improved or deteriorated during the fiscal year. These statements include all non-fiduciary financial activity on the full accrual basis of accounting. This means that all revenue and expenditures are reflected in the financial statements even if the related cash has not been received or paid as of June 30.

The Statement of Net Assets (pages 42 and 43) presents information on all of the Commonwealth's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may indicate whether the financial position of the Commonwealth is improving or deteriorating.

The Statement of Activities (pages 44 and 45) presents information showing how the Commonwealth's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both the Statement of Net Assets and Statement of Activities report three separate activities. These activities are described as follows:

Governmental Activities – account for functions of the Commonwealth that are primarily supported by taxes and intergovernmental revenues. The majority of the Commonwealth’s basic services, such as education, individual and family services, transportation, resources and economic development, administration of justice, and general government, fall within this category.

Business-type Activities – account for functions that are intended to recover all or a significant portion of their costs through user fees and charges. The major business-type activities of the Commonwealth include the State Lottery, Virginia College Savings Plan, Pocahontas Parkway (a privatized toll-road project), and Unemployment Insurance Fund.

Discretely Presented Component Units – account for functions of legally separate entities for which the Commonwealth is financially accountable. The Commonwealth has 16 authorities and 19 higher education institutions that are reported as discretely presented component units. Information regarding the individual financial statements of the component units is presented in the notes to the financial statements.

This report includes two schedules (pages 50 and 54) that reconcile the amounts reported on the governmental fund financial statements (modified accrual accounting) with governmental activities on the appropriate government-wide statements (accrual accounting). The following indicates some of the reporting differences between the government-wide financial statements and the fund financial statements.

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Long-term liabilities, unless due and payable, are not included in the fund financial statements. These liabilities are only included in the government-wide statements.
- Internal service funds are reported as governmental activities, but are reported as proprietary funds in the fund financial statements.
- Other long-term assets that are not available to pay for current period expenditures are deferred in governmental fund statements, but not deferred on the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are reported as expenditures in the fund financial statements.
- Bond proceeds provide current financial resources on the fund financial statement, but are recorded as long-term liabilities in the government-wide financial statements.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Commonwealth, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All the Commonwealth’s funds can be divided into three categories: governmental, proprietary, and fiduciary. Each of these categories uses different accounting approaches. Fund financial statements begin on page 47 and provide detailed information about the major individual funds.

- **Governmental funds** – Most of the basic services provided by the Commonwealth are reported in the governmental funds. These statements provide a detailed, short-term view of the functions reported as governmental activities in the government-wide financial statements. The government-wide financial statements are reported using the full accrual basis of accounting, but the governmental fund financial statements are reported using the modified accrual basis of accounting. This allows the reader to focus on assets that can be readily converted to cash and determine whether there are adequate resources to meet the Commonwealth’s current needs.

Because the focus of governmental funds is more limited than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. This comparison can help readers better understand the long-term impact of the Commonwealth’s near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The Commonwealth reports 16 individual governmental funds. Information is presented separately in the governmental fund statements for the General, Commonwealth Transportation, Federal Trust, and Literary funds, which are all considered major funds. Data from the other 12 governmental funds are aggregated into a single column on the fund statements. Individual fund

data for these nonmajor governmental funds is provided in the combining financial statements immediately following the Required Supplementary Information.

- **Proprietary funds** – The Commonwealth maintains two different types of proprietary funds, enterprise and internal service. These funds report activities that operate more like those of private sector business and use the full accrual basis of accounting. Enterprise funds report activities that charge fees for supplies or services to the general public, like the State Lottery. Enterprise funds are reported as business-type activities on the government-wide financial statements. Since enterprise funds use the full accrual basis of accounting, there are no differences between amounts reported on the government-wide statements and the Enterprise Fund statements. Internal Service funds report activities that charge fees for supplies and services to other Commonwealth agencies, like Fleet Management. Internal Service funds are reported as governmental activities in the government-wide statements because these types of services predominantly benefit governments rather than business-type functions.

The Commonwealth reports 29 individual proprietary funds. Information is presented separately in the proprietary fund statements for the State Lottery Department, Virginia College Savings Plan, Pocahontas Parkway Association, and Unemployment Compensation Funds, all of which are considered major funds. Data from the other enterprise funds are aggregated into a single column on the fund statements. All internal service funds are aggregated into a single column on the fund statements. Individual fund data for all nonmajor proprietary funds is provided in the combining financial statements immediately following the Required Supplementary Information.

- **Fiduciary funds** – These funds are used to account for resources held for the benefit of parties outside the government and use the full accrual basis of accounting. Fiduciary funds are excluded from the government-wide financial statement because the resources of these funds are restricted and cannot be used to finance the Commonwealth's operations. The Commonwealth's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Nets Assets beginning on page 66.

The Commonwealth's fiduciary funds are the:

- Private-purpose Trust, which reports the activities for 6 separate funds and accounts for transactions of trust arrangements in which the principal and income benefit individuals, private organizations, or other governments;
- Pension Trust, which reports the activities of 9 separate pension and other employment retirement plans for employees;
- Investment Trust, which accounts for the activities of the 3 external investment pools; and,
- Agency, which accounts for assets held on behalf of others in 21 separate funds.

Individual fund data for all fiduciary funds is provided in the combining financial statements immediately following the Required Supplementary Information.

- **Component Units** – The government-wide financial statements report information for all component units aggregated in a single column. Information is provided separately in the component unit fund statements for the Virginia Housing Development Authority, Virginia Public School Authority, University of Virginia, Virginia Polytechnic Institute and State University, and Virginia Commonwealth University, all of which are considered major component units. Data from the other component units are aggregated into a single column on the fund statements. Individual fund data for all nonmajor component units is provided in the combining financial statements immediately following the Required Supplementary Information.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found immediately following the component unit fund financial statements

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section includes budgetary comparison schedules reconciling the statutory and generally accepted accounting principles fund balances at June 30. It also includes information concerning the Commonwealth's progress in funding pension benefits and trend information for Commonwealth-managed risk pools.

Other Information

The combining statements referred to earlier in connection with nonmajor funds and component units can be found beginning on page 163 of this report. The individual fund information is aggregated into a single total on the combining financial statements, which carries forward to the fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The Commonwealth's combined net assets exceeded its liabilities by \$11.3 billion during the fiscal year. The net assets of the governmental activities increased \$237.9 million or 2.3 percent, while business-type activities had a decrease of \$338.9 million or 29.4 percent.

Figure 22
Net Assets as of June 30, 2002
(Dollars in Thousands)

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Current and other assets	\$ 4,921,175	\$ 2,435,046	\$ 7,356,221
Capital assets	12,377,199	352,387	12,729,586
Total assets	<u>17,298,374</u>	<u>2,787,433</u>	<u>20,085,807</u>
Long-term liabilities outstanding	3,921,764	1,682,817	5,604,581
Other liabilities	2,925,260	289,103	3,214,363
Total liabilities	<u>6,847,024</u>	<u>1,971,920</u>	<u>8,818,944</u>
Net assets:			
Invested in capital assets, net of related debt	9,152,089	23,472	9,175,561
Restricted	1,433,486	899,794	2,333,280
Unrestricted	(134,225)	(107,753)	(241,978)
Total net assets	<u>\$ 10,451,350</u>	<u>\$ 815,513</u>	<u>\$ 11,266,863</u>

Note: Since the Commonwealth implemented GASB Statement No. 34, during FY 2002, prior year information is not available.

The largest portion of the Commonwealth's net assets (80 percent) reflects its investment in capital assets (e.g., land, buildings, equipment, construction in progress, and infrastructure), less any related outstanding debt used to acquire those assets. These assets are recorded net of depreciation in the financial statements. The Commonwealth uses these capital assets to provide services to citizens; therefore, these assets are not available for future spending. Although the Commonwealth's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities (see Figure 22).

An additional portion of the Commonwealth's net assets (20 percent) represents restricted net assets. These resources are subject to external restrictions or constitutional provisions specifying how they may be used. The remaining balance of unrestricted net assets (\$134 million) represents debt associated with assets that are recorded in component units. (i.e. assets that reside in the component unit statements of colleges and universities, but the debt resides in governmental activities) (see Figure 22).

Approximately 96.4 percent of the Commonwealth's total general revenue came from taxes. While the Commonwealth's expenses cover many services, the largest expenses are for education, social services, and public safety. General revenues normally fund governmental activities. For FY 2002, governmental activity expenses exceeded program revenues, resulting in the use of \$12.4 billion in general revenue (primarily taxes). Revenues exceeded net expenses from business-type activities by \$65 million. The following condensed financial information was derived from the Government-wide Statement of Activities and provides detail regarding the change in net assets (see Statement of Changes in Net Assets on page 45).

Figure 23
Changes in Net Assets for the Fiscal Year Ended June 30, 2002
(Dollars in Thousands)

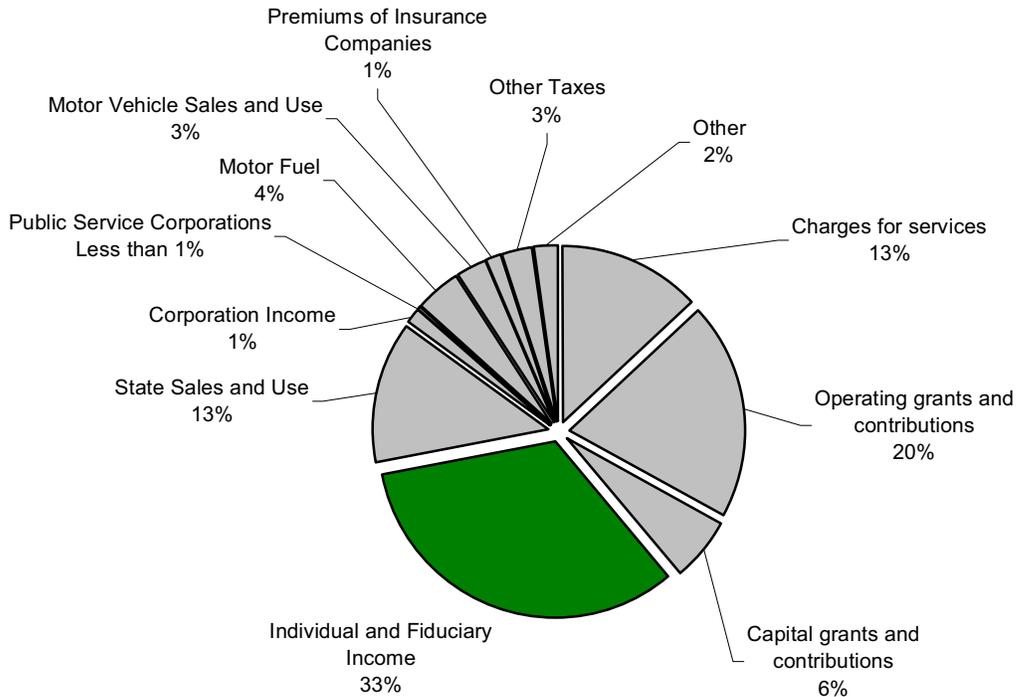
	Governmental Activities	Business-type Activities	Total
Revenues:			
Program Revenues:			
Charges for Services	\$ 2,672,386	\$ 1,947,754	\$ 4,620,140
Operating Grants and Contributions	3,997,917	277,904	4,275,821
Capital Grants and Contributions	1,188,434	-	1,188,434
General revenues:			
Taxes:			
Individual and Fiduciary Income	6,713,858	-	6,713,858
State Sales and Use	2,658,482	-	2,658,482
Corporation Income	240,147	-	240,147
Public Service Corporations	82,079	-	82,079
Motor Fuel	854,340	-	854,340
Motor Vehicle Sales and Use	526,121	-	526,121
Premiums of Insurance Companies	293,323	-	293,323
Other Taxes	602,252	2,821	605,073
Unrestricted Grants and Contributions	60,392	-	60,392
Investment Earnings	200,445	14,740	215,185
Miscellaneous	164,389	1,758	166,147
Other Financing Sources (Uses)	-	-	-
Total Revenues	20,254,565	2,244,977	22,499,542
Expenses:			
General Government	1,602,712	-	1,602,712
Education	6,405,822	-	6,405,822
Transportation	2,194,797	-	2,194,797
Resources and Economic Development	771,184	-	771,184
Individual and Family Services	6,919,239	-	6,919,239
Administration of Justice	2,323,021	-	2,323,021
Interest and Charges on Long-Term Debt	224,112	-	224,112
Unallocated Depreciation	-	-	-
State Lottery	-	742,920	742,920
Virginia College Savings Plan	-	258,851	258,851
Pocahontas Parkway	-	25,022	25,022
Unemployment Insurance	-	656,332	656,332
Nonmajor	-	476,558	476,558
Total Expenses	20,440,887	2,159,683	22,600,570
Excess before contributions to term and permanent endowments, special and extraordinary items, and transfers	(186,322)	85,294	(101,028)
Transfers	424,174	(424,174)	-
Increase (Decrease) in net assets	237,852	(338,880)	(101,028)
Net assets, July 1	10,213,498	1,154,393	11,367,891
Net assets, June 30	\$ 10,451,350	\$ 815,513	\$ 11,266,863

Note: Since the Commonwealth implemented GASB Statement No. 34, during FY 2002, prior year information is not available.

Governmental Activities Revenues

The following is a graphical representation of the Statement of Activities revenues for governmental activities.

Figure 24

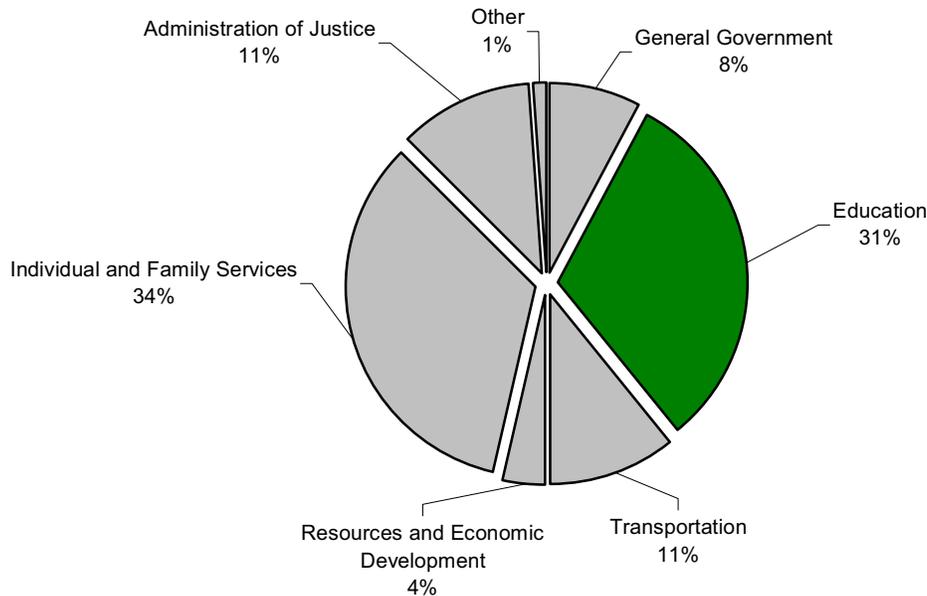


In fiscal year 2002, total revenues fell by 3.8 percent, trailing the official forecast by \$237 million. Fiscal year 2002 collections marked the largest revenue decline since the Commonwealth began keeping revenue forecasting records in 1960. Most of the shortfall was due to a drop in collections of individual income tax, which declined for the first time since fiscal year 1990. A sharp drop in non-withholding, higher growth in refunds, and dramatically slowing withholding growth collectively pulled growth in net individual collections down 7.1 percent from fiscal year 2001. Several factors account for the sluggish growth in withholding. The recession stalled job growth in the Commonwealth and payroll employment declined throughout fiscal year 2002. The malaise in both the high-tech and telecommunications sectors led to the loss of tens of thousands of high-paying jobs, particularly in Northern Virginia. In addition, as the stock market weakened, the flurry of activity in exercising stock options, which occurred in the late 1990's, is no longer boosting growth in this source. The decline in collections of non-withholding in fiscal year 2002 was three times larger than that experienced during the last recession. Growth in this source is largely driven by stock market activity, and the drop in fiscal year 2002 follows a 13 percent decline in the S&P 500 stock index during calendar year 2001. Finally, a record number of refunds was issued in fiscal year 2002 and the size of the average refund increased by 18 percent. The fall 2002 revenue forecasting process is underway, but the current outlook calls for total revenue growth of a modest 0.8 percent in fiscal year 2003 and 4.5 percent in fiscal year 2004.

Governmental Activities Expenses

The following is a graphical representation of the Statement of Activities expenses for governmental activities.

Figure 25
Expenditures by Type – Governmental Activities
FY 2002

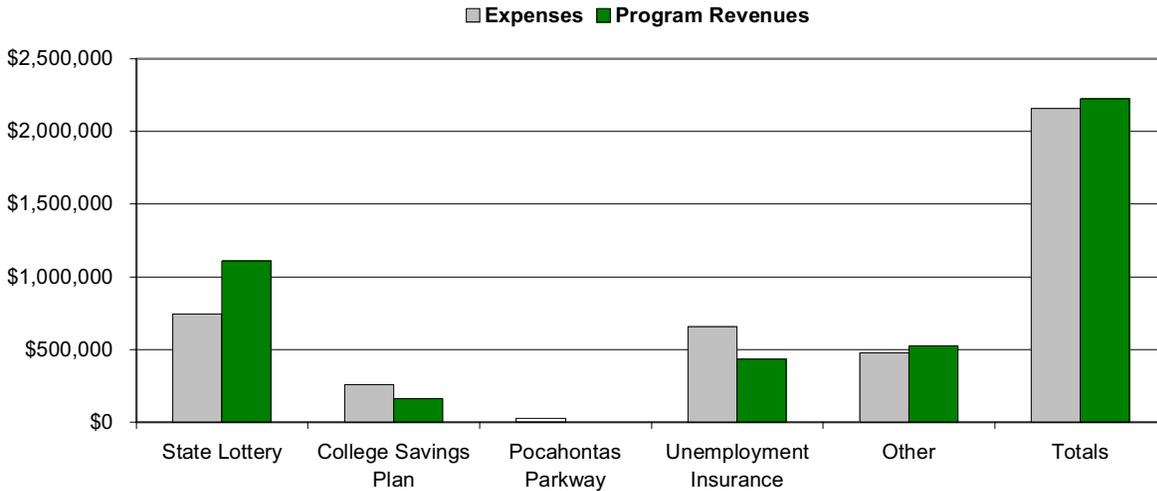


Net Assets of Business-type Activities

Net assets of business-type activity decreased by \$338.9 million during the fiscal year. Factors contributing to this change were:

- Lottery sales increased by \$105.2 million (10.5 percent) over last year to a record \$1.108 billion. Net income was a record \$367.7 million, an increase of \$38.6 million (11.7 percent) from FY 2001. Sales of most Lottery products increased in FY 2002 and sales for the scratch games, Pick 4 and the Big Game broke all prior sales records. The primary reason for this was Lottery's introduction of 500 additional retail locations and the purchase of more efficient terminals to speed up the delivery of products. Additionally, the Big Game/Mega Millions sales were up 57.5 percent due in large part to a \$331 million jackpot in April.
- Virginia College Savings Plan's net assets of the business-type activities decreased by \$99 million. The decrease was due to poor economic performance of long-term investments of the Virginia Prepaid Education Program (VPEP) and the sharp increase in tuition and mandatory fees at Virginia's higher education institutions. VPEP's actuarially determined liabilities exceeded actuarially projected net assets by approximately 8 percent at June 30, 2002, resulting in an unfunded liability of \$57.9 million. This compares to an over funding situation in fiscal year 2001, where projected net assets exceeded actuarial liabilities by 8.5 percent.
- Pocahontas Parkway Association revenues decreased \$4.1 million (44 percent) over last year. Investment earnings declined \$4.7 million (50 percent) as funds were expended to finance continued construction of the Route 895 Connector Toll Road Project. Offsetting this decrease were \$0.6 million in liquidated damages received for the late opening of the facility and the start-up of toll operations. Expenditures increased to \$25 million in FY 2002 from \$24.6 million in FY 2001, as current operating expenses increased in preparation of the opening of the roadway. The Association's accumulated deficit balance increased to (\$48) million in FY 2002 from (\$28.3) in FY 2001. This change is due to debt service expenditures exceeding revenues by \$19.7 million.
- Unemployment Insurance Fund cash balance decreased \$210.6 million during FY 2002. This reduction is the result of a continuation of 67 percent of employers still enjoying a zero rate for unemployment insurance in a year of continued economic downturn. The Commonwealth's average unemployment rate in FY 2002 was 4.1 percent, as compared to 2.4 percent in FY 2001. FY 2002 saw an increase of \$403.8 million (159.9 percent) in benefits paid for unemployment, and a reduction of \$10.1 million in unemployment insurance paid by employers due to layoffs and company closures.

Figure 26
Business-Type Activities
Program Revenues and Expenses
For the Fiscal Year Ended June 30, 2002
(Dollars in Thousands)



FUND STATEMENTS FINANCIAL ANALYSIS

As of the end of the fiscal year, the Commonwealth's governmental funds reported combined ending fund balances of \$1.9 billion. Of this total amount, \$1.3 billion, or 67.4 percent, constitutes unreserved fund balance. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to a variety of other restricted purposes such as outstanding debt and capital outlay.

General Fund Highlights

The General Fund is the chief operating fund of the Commonwealth. At the end of the current fiscal year, unreserved fund balance of the general fund was (\$749.1) million and reserved fund balance was \$532.4 million. Total fund balance of the general fund decreased by (\$779.2) million during the fiscal year due to lower tax collections and a slowing economy. The FY 2002 revenues were 4.5 percent lower than the FY 2001 revenues.

The Commonwealth's revenue forecasts mirrored the weakening national economic condition. The original FY 2002 General Fund revenue forecast of \$12.1 billion was reduced by \$1.2 billion. Actions taken by the Governor and the 2002 General Assembly to offset softening FY 2002 revenues included a combination of transfers, budget reductions, additional revenues, and alternative funding strategies:

- Transfer In from the Revenue Stabilization Fund of \$467.7 million;
- Transfer In pursuant to an intergovernmental transfer from the Department of Medical Assistance Services of \$259 million;
- Reduced agency operating budgets by \$139.1 million;
- Increased sales and use tax revenue by accelerating tax payments from FY 2003 into FY 2002 by \$149.4 million. This included \$21.3 million subsequently transferred to the Transportation Trust Fund;
- Increased interest revenue by suspending fourth quarter nongeneral fund interest allocations by \$15.6 million;
- Shifted funding for teacher retirement contributions from the General Fund to the Literary Fund of \$110 million; and,
- Shifted funding for planned capital outlay and transportation projects using alternative funding strategies of \$178.1 million.

Final FY 2002 revenues fell short of the forecast by over \$200 million. This shortfall was more than offset by unexpended agency operating and capital outlay appropriations of \$242.2 million.

Concurrent with the FY 2002 revenue forecast reduction, the revenue forecast for the 2003-2004 biennium was reduced by \$2.5 billion. The budget was balanced using many of the same strategies as those instituted for FY 2002 including reductions in agency-authorized spending of 7 and 8 percent in FY 2003 and 2004 respectively.

In August, an additional General Fund revenue shortfall of \$1.3 billion was forecast for the biennium. In October, the Governor approved General Fund spending reduction plans totaling \$725.1 million for FY 2003 and 2004. To soften the impact of the slowing economy, budget amendments proposing additional spending reductions will be introduced during the 2003 General Assembly session.

Major Special Revenue Fund Highlights

The Commonwealth Transportation Fund ended the fiscal year with a fund balance of \$1.1 billion, an increase of \$100.0 million from the prior year. The increase was largely the result of increased federal revenues collected from the Federal Highway Administration resulting from an increased emphasis on federal participating construction projects and better federal funds management. Additionally, the Priority Transportation Fund did not incur any expenditures as management has chosen to utilize the proceeds of the Federal Highway Reimbursement Anticipation Notes as the first funding source for projects listed in the Virginia Transportation Act of 2000.

The Federal Trust Fund received \$248.6 million more in federal funds than the previous year. The majority of the increase is associated with programs at the Departments of Social Services, Medical Assistance Services, Education and other individual and family service agencies.

The Literary Fund ended the fiscal year with a fund balance of \$424.4 million, a decrease of \$85.7 million from the previous fiscal year. Revenues decreased by \$7.7 million, and expenditures and other uses increased by \$85.6 million primarily due to the payment of teacher retirement contributions of \$110 million and an increase in debt service payments of \$15.4 million. Additionally, the Literary Fund experienced a decline in loan disbursements of \$39.8 million.

Capital Asset and Debt Administration

Capital assets. This is the first year that the Commonwealth will report depreciation on governmental activities' assets. The Commonwealth's investment in capital assets for its governmental and business type activities as of June 30, 2002, amounts to \$12.7 billion (net of accumulated depreciation totaling \$9.2 billion). This investment in capital assets includes land, buildings, improvements, equipment, construction in progress, and infrastructure. Infrastructure assets are items that are normally immovable such as roads, bridges, drainage systems, and other similar assets. The beginning net assets infrastructure balance was \$5.5 billion. The total increase in the Commonwealth's investment in governmental capital assets was \$7.9 billion with \$6.3 billion attributable to infrastructure being reported for the first time.

Additional information on the Commonwealth's capital assets can be found in Note 9, "Property, Plant, Equipment, and Infrastructure."

Figure 27
Capital Assets as of June 30, 2002
 (Net of Depreciation)
 (Dollars in Thousands)

	Governmental Activities	Business-type Activities	Total
Land	\$ 1,198,544	\$ 1,726	\$ 1,200,270
Buildings	1,442,508	965	1,443,473
Equipment	410,101	38,854	448,955
Infrastructure	6,257,386	-	6,257,386
Construction in progress	3,068,660	310,842	3,379,502
Total	\$ 12,377,199	\$ 352,387	\$ 12,729,586

Note: Since the Commonwealth implemented GASB Statement No. 34, during FY 2002, prior year information is not available.

Long-term debt. The Commonwealth does not issue debt for operating purposes. At the end of the current fiscal year, the Commonwealth had total debt outstanding of \$17.4 billion. Total tax supported debt is \$4.9 billion and total debt not supported by taxes is \$12.5 billion. Total debt backed by the full faith and credit of the government is \$579.3 million and \$2.2 billion is considered moral obligation debt. The remainder of the Commonwealth's debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

During FY 2002, the Commonwealth issued \$2.6 million of new debt for various projects. Additional information on the Commonwealth's outstanding debt can be found in Note 17, "Long-term Liabilities". Further, the Commonwealth maintains a "triple A" bond rating for general obligation debt from the three rating agencies: Moody's Investors Service, Standard & Poor's Ratings Group, a division of The McGraw Hill Companies, Inc., and Fitch, Inc.

State statutes limit the amount of general obligation debt the Commonwealth may issue for each specific type of debt. The 9(a) bonds, which have been issued to redeem previous debt obligations, are limited to 30 percent of 1.15 times the annual tax revenues for FY 2002. The 9(b) bonds, which have been authorized by the citizens of Virginia through bond referenda to finance capital projects, are limited to 1.15 times the average of selected tax revenues for fiscal years 2000, 2001, and 2002. The 9(c) bonds, which have been issued to finance capital projects that will generate revenue upon their completion, are limited to 1.15 times the average of selected tax revenues for fiscal years 2000, 2001, and 2002. The current debt limitation for the Commonwealth is \$3.3 billion, \$11.1 billion, and \$11.1 billion, respectively, for the 9(a), 9(b), and 9(c) general obligation bond issues. These limits significantly exceed the Commonwealth's outstanding general obligation debt. In November 2002, the citizens of the Commonwealth authorized a bond issuance of General Obligation Bonds in the amounts of \$900.5 million and \$119.0 million for capital projects at higher education institutions and state parks, respectively.

Figure 28
Outstanding Debt as of June 30, 2002
General Obligation and Revenue Bonds
(Dollars in Thousands)

	Governmental Activities	Business-type Activities	Total
General obligation bonds			
9(A)	\$ -	\$ -	\$ -
9(B)	451,700	-	451,700
9(C)	504,059	-	504,059
Revenue bonds	-	418,850	418,850
Total	<u>\$ 955,759</u>	<u>\$ 418,850</u>	<u>\$ 1,374,609</u>

Note: Since the Commonwealth implemented GASB Statement No. 34, during FY 2002, prior year information is not available.

Economic Factors and Outlook

Like the nation, the Virginia economy experienced a recession and remains in a weak recovery. Economic growth in Virginia was weaker than expected in fiscal year 2002, with employment and income growing well below forecasted growth rates. The predominance of the high-tech industry in Virginia, previously a stabilizing force and the primary driver of growth, adversely affected the state's economy in fiscal year 2002, as the meltdown in that industry trickled throughout the Commonwealth. The terrorist attacks of September 11 contributed to the downturn, especially in Northern Virginia, where tourism and business travel were particularly hard hit. Because of the substantial amount of uncertainty surrounding the Virginia economy, an interim economic and revenue forecasting process was undertaken this summer. Economic events that have occurred since the interim forecast prepared this summer support the path chosen by both the Governor's Advisory Board of Economists and the Governor's Advisory Council on Revenue Estimates. The outlook is for another year of negative employment growth in Virginia, followed by several years of modest growth. Virginia should experience income growth similar to that in the nation over the next few years, lower than that seen in 1990's, but well above the 3 percent rate of fiscal year 2002. For a more in-depth discussion on the Commonwealth's economy see "Virginia Economic Highlights" on page 17.

Requests for Information

This financial report is designed to provide a general overview of the Commonwealth's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the State Comptroller's Office, Commonwealth of Virginia, P. O. Box 1971, Richmond, Virginia 23218.

The Commonwealth's component units issue their own separate financial statements. Contact information regarding each component unit is provided in Note 1B, "Summary of Significant Accounting Policies, The Reporting Entity."