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# INTRODUCTORY SECTION

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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, VA 23218-1971

December 14, 2009

The Honorable Timothy M. Kaine  
Governor of the Commonwealth of Virginia  
State Capitol  
Richmond, Virginia 23219

Dear Governor Kaine:

It is my pleasure to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2009, 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 2009 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, 2009. 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

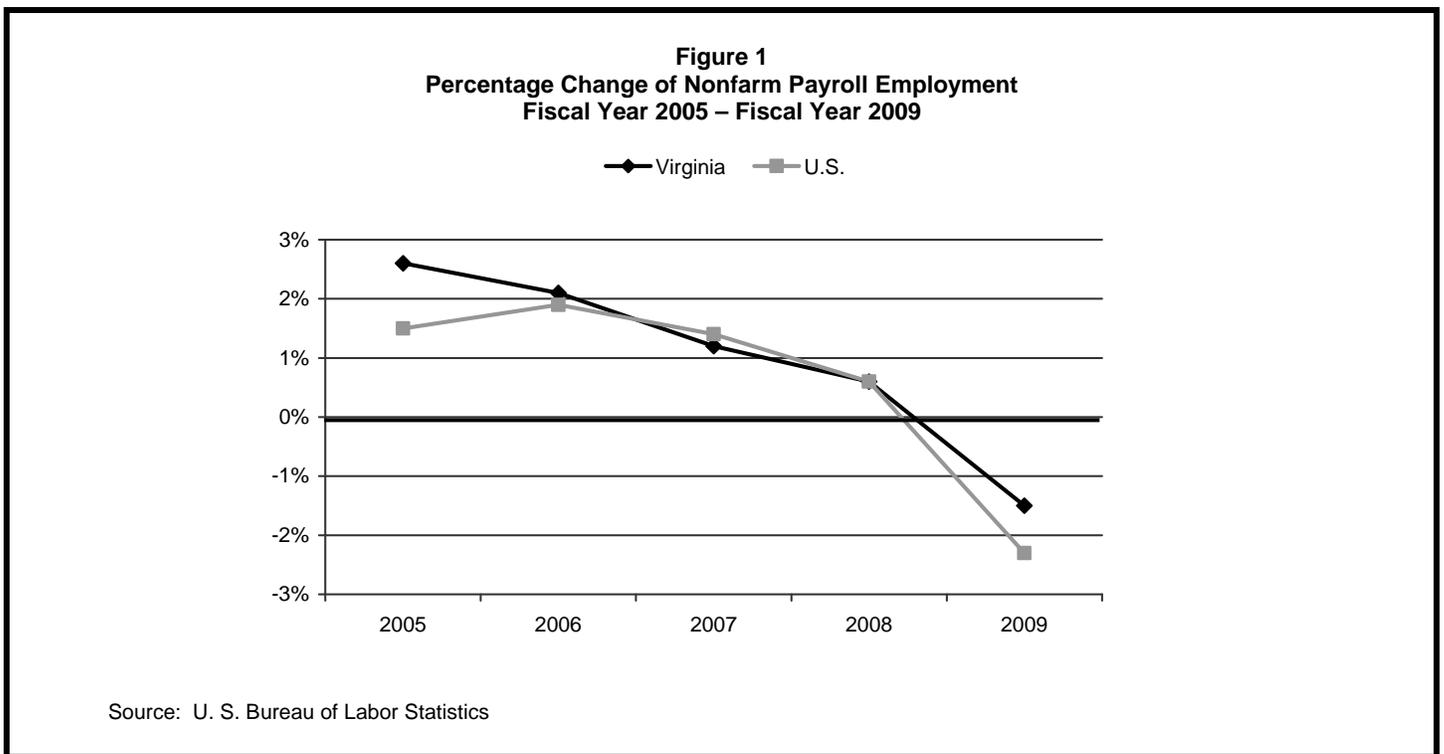
## LOCAL ECONOMY

### Introduction

An economist at the University of Virginia's Weldon Cooper Center for Public Service prepared this section on recent developments in the Virginia economy. In fiscal year 2009, the Commonwealth's economy was caught in what many have called "the Great Recession" – the most severe economic downturn since the Great Depression of the 1930s. The recession, which began midway through fiscal year 2008 in December 2007, reached full force in the next fiscal year. In fact, the official arbiter of recessions, the National Bureau of Economic Research, has yet to establish the bottom, even though many economists think a slow turnaround is likely in the near future. The analysis in this section covers the last five fiscal years in order to provide perspective on recent developments. 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

Virginia's nonfarm payroll employment fell by 55,300 or -1.5 percent in fiscal year 2009. The national growth rate in fiscal year 2009 fell even lower (-2.3 percent). As shown in **Figure 1**, the rate of growth diminished in each year.



**Figure 2** shows changes in employment by industry based on the North American Industry Classification System (NAICS). Of the 15 industries shown, only five (education and health services, other services such as repair and laundry, federal government, state government, and local government) reported gains. Major sectors such as construction, manufacturing, and retail trade sustained large losses. Developments at the national level were similar, but in total, the relative loss was worse.

**Figure 2**  
**Nonfarm Payroll Employment**  
**Fiscal Year 2005 – Fiscal Year 2009**

NAICS Industry	Virginia Employment (000)					Change, Fiscal Year 2008 to Fiscal Year 2009		
	2005	2006	2007	2008	2009	Virginia		U.S.
						Number (000)	Percent	Percent
Mining and logging	10.4	11.1	11.2	10.8	11.2	0.4	3.7	3.4
Construction	237.3	248.9	244.7	232.5	206.7	(25.8)	(11.1)	(9.6)
Manufacturing	298.0	292.7	282.8	271.5	254.0	(17.5)	(6.4)	(7.2)
Wholesale trade	115.7	118.6	120.6	120.4	115.7	(4.7)	(3.9)	(3.2)
Retail trade	414.8	422.3	425.4	426.2	414.9	(11.3)	(2.7)	(2.9)
Transportation and utilities	121.1	120.5	119.4	119.7	118.1	(1.6)	(1.3)	(3.3)
Information services	94.9	92.0	91.2	89.1	84.1	(5.0)	(5.6)	(3.0)
Financial activities	190.8	194.0	195.1	191.1	187.1	(4.0)	(2.1)	(3.3)
Professional and business services	593.6	618.6	637.6	653.1	648.6	(4.5)	(0.7)	(4.0)
Education and health services	387.4	399.6	411.9	430.1	441.3	11.2	2.6	2.6
Leisure and hospitality	325.1	334.4	342.4	348.5	344.5	(4.0)	(1.1)	(1.4)
Other services	180.5	181.1	183.6	187.2	187.5	0.3	0.2	(0.8)
Federal government	151.7	152.7	156.3	157.4	163.6	6.2	3.9	2.1
State government	147.6	151.3	153.2	153.4	156.0	2.6	1.7	1.0
Local government	357.4	364.6	370.1	377.0	379.7	2.7	0.7	0.6
Total nonfarm employment	<u>3,626.3</u>	<u>3,702.2</u>	<u>3,745.5</u>	<u>3,768.0</u>	<u>3,712.7</u>	<u>(55.3)</u>	<u>(1.5)</u>	<u>(2.3)</u>

Source: U. S. Bureau of Labor Statistics  
Note: Details may not add to totals due to rounding.

Virginia has 11 Metropolitan Statistical Areas (MSAs), dominated by three – (1) the Virginia portion of the Washington-Arlington-Alexandria DC-VA-MD-WV MSA, labeled the Northern Virginia MSA, (2) the Virginia Beach-Norfolk-Newport News MSA, often referred to as the Hampton Roads MSA, and (3) the Richmond MSA. Together the three areas account for 72 percent of the Commonwealth's nonfarm payroll employment. **Figure 3** shows the annual percentage change in employment for ten of the MSAs. No information is shown for the Kingsport-Bristol TN-VA MSA because most of the area's economic activity is in Tennessee. All three of the major MSAs experienced negative growth in fiscal year 2009, as did Charlottesville, Danville, Harrisonburg, Roanoke, and Winchester. Blacksburg-Christiansburg-Radford and Lynchburg, two areas with relatively large numbers of higher education employees, eked out small gains.

**Figure 3**  
**Nonfarm Payroll Employment of Virginia MSAs**  
**Fiscal Year 2005 – Fiscal Year 2009**

Area	Percent Change				
	2005	2006	2007	2008	2009
Statewide	2.6	2.1	1.2	0.6	(1.5)
<b>Metropolitan areas*</b>	2.7	2.3	1.5	0.4	(2.8)
Blacksburg-Christiansburg-Radford	0.6	1.0	(0.6)	(0.1)	0.6
Charlottesville	3.1	3.7	3.9	1.5	(1.7)
Danville	(2.5)	(1.2)	(4.7)	0.2	(2.4)
Harrisonburg	0.2	2.3	3.7	(1.6)	(1.4)
Lynchburg	2.0	2.2	1.5	1.0	0.3
Northern Virginia	4.1	3.4	1.6	0.8	(0.5)
Richmond	2.5	1.5	1.8	0.3	(2.4)
Roanoke	0.6	2.3	1.2	(0.1)	(1.3)
Virginia Beach-Norfolk-Newport News, VA-NC**	1.7	1.2	0.8	0.2	(0.9)
Winchester VA-NC**	2.2	3.7	3.0	(2.1)	(4.0)

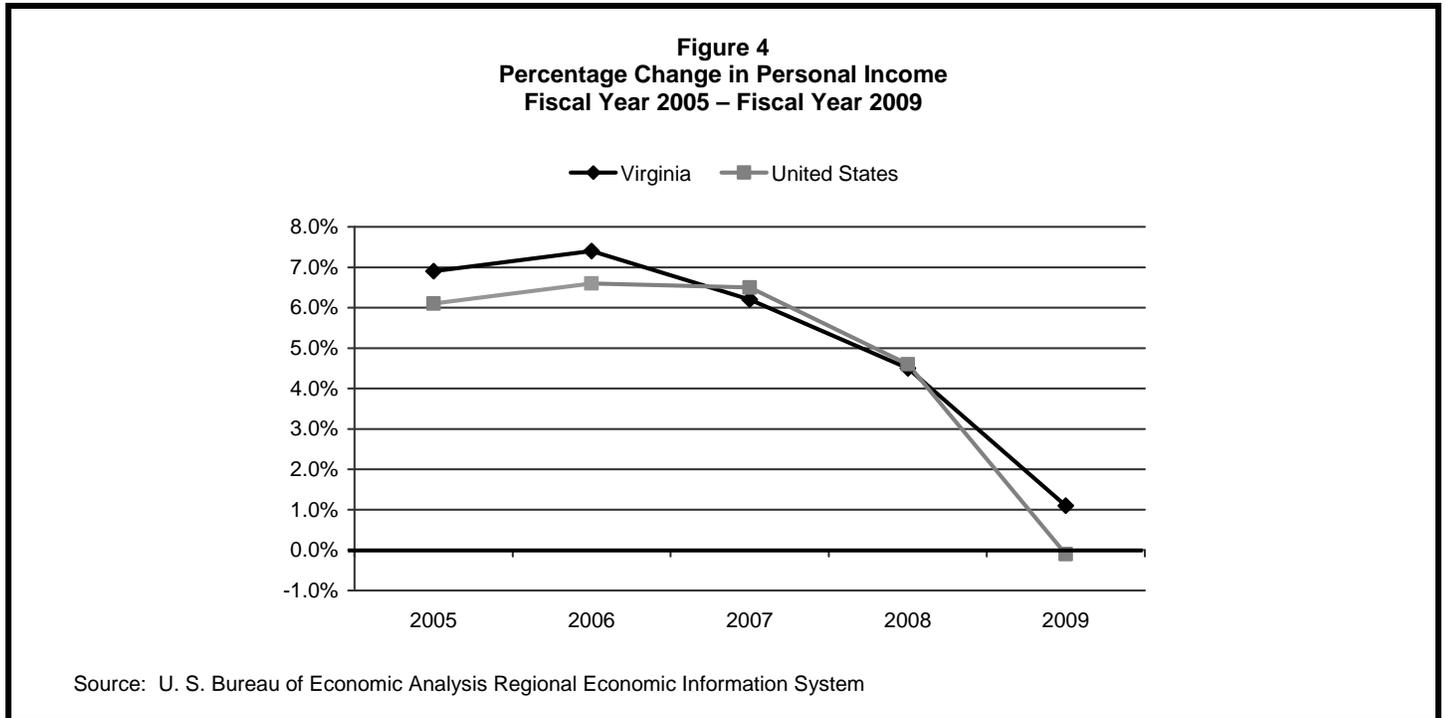
Source: U. S. Bureau of Labor Statistics

\* Excludes Kingsport-Bristol MSA, most of which is located in Tennessee

\*\* Includes non-Virginia portion.

## Personal Income

Personal income is the broadest dollar measure of the Virginia economy that is currently available for the period under review. Developments in personal income have a strong bearing on state government revenues since collections from the individual income and other taxes are related directly or closely to personal income. In fiscal year 2009, Virginia personal income in current dollars grew by only 1.1 percent. As shown in **Figure 4**, this was slightly better than the 0.1 percent negative growth for the nation, but substantially less than in the four previous years. In fact, measured in both current and constant dollars, Virginia's personal income growth was lower in fiscal year 2009 than in any other fiscal year since fiscal year 1970, the first year that the Bureau of Economic Analysis published state quarterly income estimates – the series used to develop fiscal year estimates of personal income.

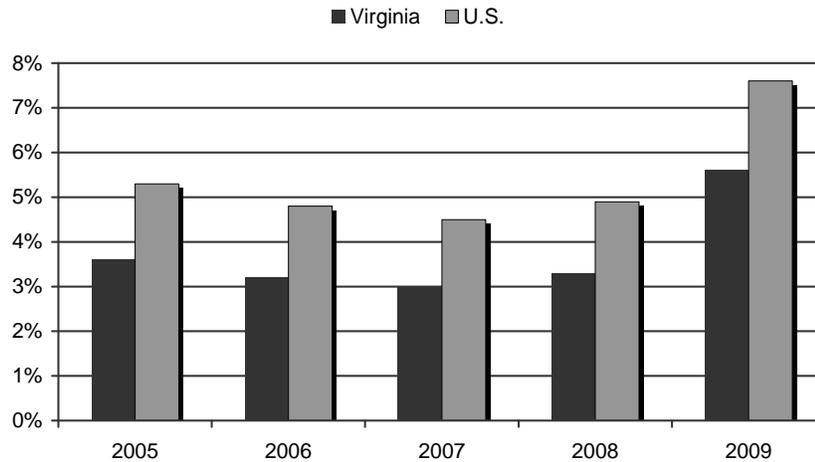


There are three major components of personal income. The first and largest is net earnings by place of residence, which is the sum of wages and salaries and proprietors' income. In fiscal year 2009, net earnings accounted for 71 percent of Virginia personal income and increased by 0.5 percent from the previous year. The second component, dividends, interest, and rent accounted for 17 percent of income. Reflecting poor financial markets, this component declined 2.3 percent from the previous fiscal year. Income transfers, which are mainly Social Security benefits, Medicaid and Medicare benefits, and unemployment insurance payments, accounted for 12 percent of personal income in fiscal year 2009 and grew by 9.9 percent.

## Unemployment

Rising unemployment is a hallmark of a recession. Thus, it is not surprising that the Commonwealth's unemployment rate has risen in recent years. After a small rise in fiscal year 2008, the rate moved up sharply in fiscal year 2009, averaging 5.6 percent, as shown in **Figure 5**. Nonetheless, Virginia's unemployment rate was much lower than the national average of 7.6 percent.

**Figure 5**  
Civilian Unemployment Rate  
Fiscal Year 2005 – Fiscal Year 2009



Source: Virginia Employment Commission

As shown in **Figure 6**, each of the Commonwealth's 11 MSAs experienced an increase in unemployment in fiscal year 2009. Among the metropolitan areas the lowest unemployment rates were in Northern Virginia (4.2 percent) and Charlottesville (4.7 percent). By far the highest rate was in Danville (11.0 percent), an area hit hard by declines in textile manufacturing.

**Figure 6**  
Civilian Unemployment Rates of Virginia MSAs  
Fiscal Year 2005 – Fiscal Year 2009

Area	Unemployment Rate (Percent)				
	2005	2006	2007	2008	2009
State	3.6	3.2	3.0	3.3	5.6
Blacksburg-Christiansburg-Radford	4.1	3.6	3.6	4.0	7.1
Charlottesville	3.2	2.8	2.4	2.7	4.7
Danville	7.6	7.0	6.7	6.5	11.0
Harrisonburg	3.4	2.9	2.5	3.0	5.2
Kingsport-Bristol TN-VA*	4.9	4.6	4.4	4.7	7.4
Lynchburg	4.1	3.5	3.3	3.6	6.0
Northern Virginia portion of Washington-Arlington-Alexandria DC-VA-MD-WV*	2.6	2.3	2.2	2.5	4.2
Richmond	3.8	3.4	3.0	3.5	6.2
Roanoke	3.6	3.1	3.0	3.4	5.8
Virginia Beach-Norfolk-Newport News VA-NC*	4.0	3.5	3.2	3.5	5.8
Winchester VA-WV*	3.0	2.6	2.8	3.4	6.6

Source: Virginia Employment Commission

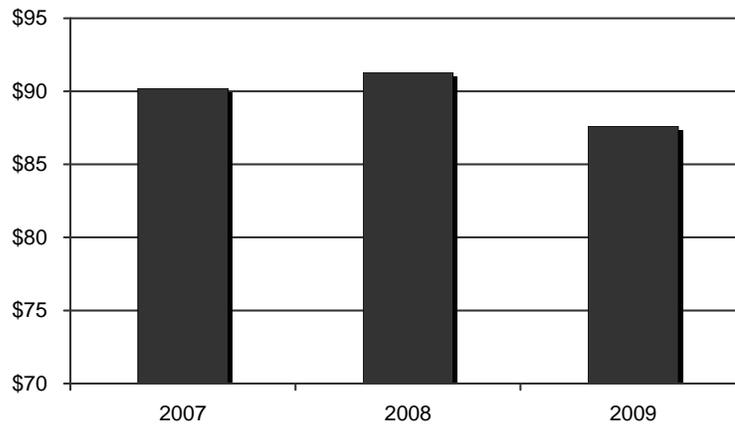
\* Excludes non-Virginia portion.

## Taxable Sales

Current data on retail sales are not produced for states. Nevertheless, sales taxed under the Virginia sales and use tax are available for Virginia. The taxable sales series serves as a very rough proxy for retail sales. However, the data do not include motor vehicle and motor fuel sales and, unlike the Bureau of the Census information on retail sales, taxable sales also include restaurants and lodging places. Comparable data on taxable sales are available for fiscal years 2007, 2008, and 2009. During fiscal year 2006 Virginia changed its reporting methodology with the result that data for years prior to fiscal year 2007 are not comparable.

Virginia taxable sales dropped by 4.1 percent in fiscal year 2009 following an anemic rise of 1.2 percent in fiscal year 2008 as shown in **Figure 7**. Adjusted for inflation, taxable sales dropped 2 percent in fiscal year 2008 and an additional 5.6 percent in fiscal year 2009. (The personal consumption expenditures price index was used for the inflation adjustment.)

**Figure 7**  
**Virginia Taxable Sales**  
**Fiscal Year 2007 – Fiscal Year 2009**  
(Dollars in Billions)

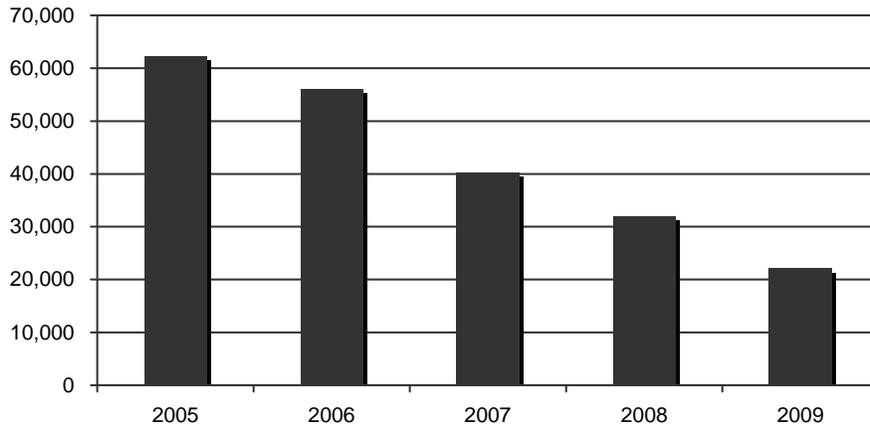


Source: Virginia Department of Taxation

## Housing Market

The housing downturn, which began in fiscal year 2006, deepened severely in subsequent years as shown in **Figure 8**. By fiscal year 2009, new privately owned housing units authorized were down to a level of 22,020, a 31 percent drop from the previous year and far below the fiscal year 2005 level of 62,263. As bad as they were for Virginia, relative declines for the nationwide totals were even greater in fiscal year 2008 and fiscal year 2009.

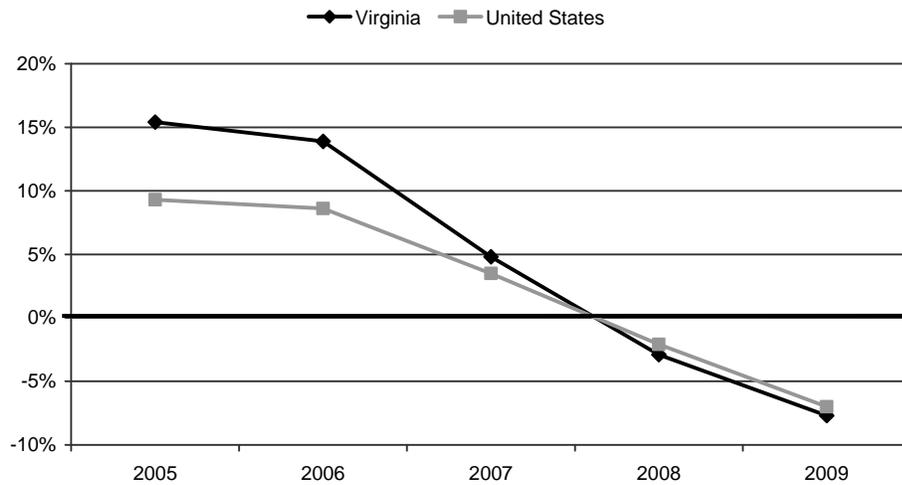
**Figure 8**  
**Virginia New Privately Owned Housing Units Authorized**  
**Fiscal Year 2005 – Fiscal Year 2009**



Source: U. S. Bureau of the Census

Another housing market indicator is the Federal Housing Finance Agency series on house prices. This series was previously published by the Office of Federal Housing Oversight. As shown in **Figure 9**, fiscal year appreciation of existing houses grew at rapid rates in fiscal years 2005 and 2006. Beginning in fiscal year 2008, the change in prices moved into negative territory, dropping by 2.9 percent in fiscal year 2008 and by 7.7 percent in fiscal year 2009. The price changes in Virginia mirrored the national experience in both years.

**Figure 9**  
**Percentage Change in House Prices**  
**Fiscal Year 2005 – Fiscal Year 2009**



Source: Office of Federal Housing Enterprise Oversight

### Conclusion

Fiscal year 2009 was a difficult year for Virginia – a description that applied to the vast majority of states. Compared to national averages for major economic measures, the Commonwealth generally fared better than the nation, a result stemming from Virginia's proximity to the nation's capital, its importance as a defense contractor and location of military personnel, the positive role of the deepwater port at Hampton Roads, and the Commonwealth's strategic location on the eastern seaboard.

## **MAJOR INITIATIVES**

The CAFR has received unqualified audit opinions from fiscal year 1986 through fiscal year 2008. 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 *Virginia Constitution* 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. A continued sluggish economy contributed to declining General Fund revenue collections during FY 2009. Accordingly, the declining revenue collections have required both a revenue re-estimate and fiscal year 2010 budget reductions. It is anticipated that additional budget reductions will be required during fiscal year 2011. Further, the General Assembly authorized a withdrawal from the Fund in FY 2009. Refer to page 34 for additional information.

## **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 implements VDOT's financial system on July 1, 2011, and the second phase implements the Commonwealth's base financial system at the Department of Accounts (DOA) by July 1, 2012. A future phase of the project includes converting all other executive branch state agencies to the Cardinal financial system, 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 conducted readiness assessments for each agency that received ARRA funds to help ensure the appropriate processes were in place and performed validation reviews of information being reported to the Office of Management and Budget.

## **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, 2008. 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 23 consecutive years (fiscal years 1986-2008). 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. VonMoll  
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, 2008

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.



A handwritten signature in black ink, appearing to read "M. L. R. M.", written in a cursive style.

President

A handwritten signature in black ink, appearing to read "Jeffrey R. Emer", written in a cursive style.

Executive Director