

Management's Discussion and Analysis

(Unaudited)

The following is a discussion and analysis of the Commonwealth of Virginia's (the Commonwealth) financial performance, including an overview and analysis of the financial activities of the Commonwealth for the fiscal year ended June 30, 2014. 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, including the notes to the financial statements, which are located after this analysis.

Financial Highlights

Government-wide Highlights

The primary government's assets and deferred outflows of resources exceeded its liabilities and deferred inflows of resources at June 30, 2014, by \$22.1 billion. Net position of governmental activities increased by \$753.0 million and net position of business-type activities increased by \$502.1 million. Component units reported an increase in net position of \$1.9 billion from June 30, 2013.

Fund Highlights

At the end of the fiscal year, the Commonwealth's governmental funds reported a combined ending fund balance of \$3.9 billion, a decrease of \$275.7 million in comparison with the prior year. Of this total fund balance, \$248.9 million represents nonspendable fund balance, \$1.9 billion represents restricted fund balance, \$2.5 billion represents committed fund balance, and \$16.8 million represents assigned fund balance. These amounts are offset by a negative \$781.5 million unassigned fund balance. The Enterprise Funds reported net position at June 30, 2014, of \$1.2 billion, an increase of \$499.7 million during the year which is primarily attributable to the Unemployment Compensation Fund and the Virginia College Savings Plan. See page 33 for additional information.

The General Fund recognized higher fund revenues and expenditures, as well as lower assets and liabilities when compared to fiscal year 2013. Deferred outflows and deferred inflows of resources were reported for the first time in fiscal year 2014. See page 34 for additional information.

Long-term Debt

The Commonwealth's total debt rose during the fiscal year to \$37.6 billion, an increase of \$383.7 million, or 1.0 percent. During the fiscal year, the Commonwealth issued new debt in the amount of \$646.2 million for the primary government and \$3.4 billion for the component units. These debt issuances increased the debt balances to \$12.3 billion for the primary government and \$25.3 billion for component units.

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 Position (pages 40 and 41) presents information on all of the Commonwealth's assets and deferred outflows of resources, and liabilities and deferred inflows of resources; net position represents the difference between all other elements in a statement of financial position and is displayed in three components – net investment in capital assets; restricted; and unrestricted. Over time, increases or decreases in net position may indicate whether the financial position of the Commonwealth is improving or deteriorating.

The Statement of Activities (pages 42 through 44) presents information showing how the Commonwealth's net position changed during fiscal year 2014. All changes in net position 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 Position 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 Virginia Lottery, Virginia College Savings Plan, and Unemployment Compensation Fund.

Discretely Presented Component Units – account for functions of legally separate entities for which the Commonwealth is financially accountable. The Commonwealth has 27 non-higher education component units and 22 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 48 and 52) that reconcile the amounts reported on the governmental fund financial statements (modified accrual accounting) with governmental activities on the appropriate government-wide statements (full 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 in the government-wide statements, 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 the governmental fund statements, but not deferred in the government-wide statements.
- Capital outlay spending in capital assets on the government-wide statements, but is reported as expenditures in the fund financial statements.
- Bond proceeds provide current financial resources on the fund financial statements, 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 of 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 46 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 12 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 8 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 Virginia Lottery. Enterprise funds are reported as business-type activities on the government-wide financial statements.

The enterprise funds use the full accrual basis of accounting and the only differences between amounts reported on the government-wide statements and the enterprise fund statements are due to internal service fund activity (see reconciliations on pages 54 and 56). 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 24 individual proprietary funds. Information is presented separately in the proprietary fund statements for the Virginia Lottery, Virginia College Savings Plan, 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 statements 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 Position and Changes in Fiduciary Net Position beginning on page 64.

The Commonwealth's fiduciary funds are the:

- Private Purpose Trusts, which reports the activities for 7 separate funds and accounts for transactions of trust arrangements in which the principal and income benefit individuals, private organizations, or other governments;
- Pension and Other Employee Benefit Trusts, which reports the activities of 13 separate pension and other employment retirement plans for employees;
- Investment Trust, which accounts for the activities of the external investment pool; and,
- Agency, which accounts for assets held on behalf of others in 20 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, Virginia Resources Authority, and Virginia College Building Authority, 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 funding progress and employer contributions for pension and other postemployment benefits, change in discount rate, and changes in employers' net pension liability, as well as 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 195 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 primary government's assets and deferred outflows of resources exceeded its liabilities and deferred inflows of resources by \$22.1 billion during the fiscal year. The net position of the governmental activities increased \$753.0 million, or 3.7 percent, primarily due to increases in capital assets and decreases in total liabilities and deferred inflows of resources. Capital assets are discussed further on page 35, the long-term liabilities are discussed further on page 36, and deferred inflows of resources are discussed in Note 13. Business-type activities had an increase of \$502.1 million, or 76.1 percent, primarily due to an increase for the Unemployment Compensation Fund and Virginia College Savings Plan as discussed on page 33. The government-wide beginning balance was restated for the implementation of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, and the correction of prior year errors to arrive at a restated beginning balance of \$20.9 billion.

Figure 11
Net Position as of June 30, 2014 and 2013
(Dollars in Thousands)

	Governmental Activities		Business-type Activities		Total	
	2013		2013		2013	
	2014	as restated	2014	as restated	2014	as restated
Current and other assets	\$ 8,966,466	\$ 9,502,616	\$ 4,042,573	\$ 3,796,505	\$ 13,009,039	\$ 13,299,121
Capital assets	27,898,540	26,846,700	168,539	95,305	28,067,079	26,942,005
Deferred outflow s of resources	53,940	-	-	-	53,940	-
Total assets and deferred outflow s of resources	36,918,946	36,349,316	4,211,112	3,891,810	41,130,058	40,241,126
Long-term liabilities outstanding	9,586,711	9,389,896	2,702,711	2,756,881	12,289,422	12,146,777
Other liabilities	4,807,694	5,168,201	346,579	475,222	5,154,273	5,643,423
Deferred inflow s of resources	1,562,385	1,582,014	-	-	1,562,385	1,582,014
Total liabilities and deferred inflow s of resources	15,956,790	16,140,111	3,049,290	3,232,103	19,006,080	19,372,214
Net position:						
Net investment in capital						
assets	22,316,758	20,294,314	12,312	29,773	22,329,070	20,324,087
Restricted	1,465,891	1,455,712	586,073	371,600	2,051,964	1,827,312
Unrestricted	(2,820,493)	(1,540,821)	563,437	258,334	(2,257,056)	(1,282,487)
Total net position	\$ 20,962,156	\$ 20,209,205	\$ 1,161,822	\$ 659,707	\$ 22,123,978	\$ 20,868,912

The largest portion of the primary government's net position reflects its investment in capital assets (e.g., land, buildings, equipment, infrastructure, construction-in-progress, and intangible assets including water rights, easements and software), less any related outstanding debt and deferred inflows of resources used to acquire those assets. These assets are recorded net of depreciation in the financial statements. The primary government uses these capital assets to provide services to citizens; therefore, these assets are not available for future spending. Although the primary government'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 (**Figure 11**). The governmental activities net investment in capital assets amount exceeds total net position due to a negative unrestricted net position amount unrelated to capital assets.

An additional portion of the primary government's net position represents restricted net position. These resources are subject to external restrictions or constitutional provisions specifying how they may be used. The remaining balance of negative \$2.3 billion is unrestricted net position (**Figure 11**).

Approximately 54.2 percent of the primary government's total revenue came from taxes. While the primary government's expenses cover many services, the largest expenses are for education and individual and family services. General revenues normally fund governmental activities. For fiscal year 2014, governmental program and general revenues exceeded governmental expenses by \$29.3 million. Program revenues exceeded expenses from business-type activities by \$1.2 billion. The following condensed financial information (**Figure 12**) was derived from the Government-wide Statement of Activities and provides detail regarding the change in net position (see page 42).

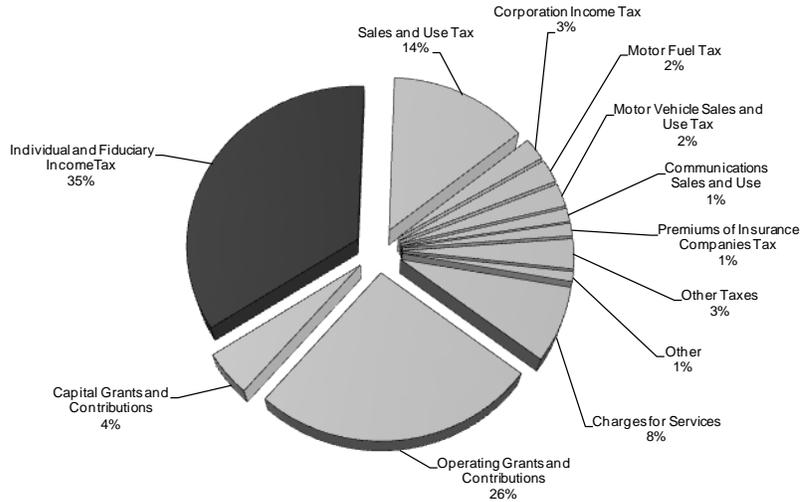
Figure 12
Changes in Net Position for the Fiscal Years Ended June 30, 2014 and 2013
(Dollars in Thousands)

	Governmental Activities		Business-type Activities		Total	
	2013		2013		2013	
	2014	as restated	2014	as restated	2014	as restated
Revenues:						
Program Revenues:						
Charges for Services	\$ 2,560,863	\$ 2,459,370	\$ 4,131,281	\$ 3,866,556	\$ 6,692,144	\$ 6,325,926
Operating Grants and Contributions	8,731,809	8,819,681	264	337	8,732,073	8,820,018
Capital Grants and Contributions	1,508,880	1,753,789	69,595	61,104	1,578,475	1,814,893
General Revenues:						
Taxes:						
Individual and Fiduciary Income	11,681,808	11,399,891	-	-	11,681,808	11,399,891
Sales and Use	4,597,105	3,941,074	-	-	4,597,105	3,941,074
Corporation Income	769,832	805,474	-	-	769,832	805,474
Motor Fuel	791,944	966,616	-	-	791,944	966,616
Motor Vehicle Sales and Use	780,817	581,693	-	-	780,817	581,693
Communications Sales and Use	420,371	423,639	-	-	420,371	423,639
Deeds, Contracts, Wills, and Suits	394,834	435,619	-	-	394,834	435,619
Premiums of Insurance Companies	459,933	406,506	-	-	459,933	406,506
Alcoholic Beverage Sales	132,044	126,801	-	-	132,044	126,801
Tobacco Products	182,110	182,430	-	-	182,110	182,430
Estate	149	-	-	-	149	-
Public Service Corporations	119,074	115,973	-	-	119,074	115,973
Beer and Beverage Excise	43,050	42,813	-	-	43,050	42,813
Wine and Spirits/ABC Liter	25,620	25,436	-	-	25,620	25,436
Bank Stock	22,581	20,321	-	-	22,581	20,321
Other Taxes	95,415	75,641	9,142	9,142	104,557	84,783
Unrestricted Grants and Contributions	48,730	74,134	-	-	48,730	74,134
Investment Earnings	44,571	6,349	1,735	1,183	46,306	7,532
Miscellaneous	233,716	306,172	358	448	234,074	306,620
Total Revenues	33,645,256	32,969,422	4,212,375	3,938,770	37,857,631	36,908,192
Expenses:						
General Government	3,362,086	3,097,364	-	-	3,362,086	3,097,364
Education	9,430,802	9,280,657	-	-	9,430,802	9,280,657
Transportation	3,602,208	3,253,600	-	-	3,602,208	3,253,600
Resources and Economic Development	940,376	946,709	-	-	940,376	946,709
Individual and Family Services	13,115,503	12,941,609	-	-	13,115,503	12,941,609
Administration of Justice	2,927,249	2,760,486	-	-	2,927,249	2,760,486
Interest and Charges on Long-term Debt	237,782	254,964	-	-	237,782	254,964
Virginia Lottery	-	-	1,265,839	1,194,247	1,265,839	1,194,247
Virginia College Savings Plan	-	-	104,354	155,889	104,354	155,889
Unemployment Compensation	-	-	535,715	584,433	535,715	584,433
Alcoholic Beverage Control	-	-	554,812	532,835	554,812	532,835
Risk Management	-	-	13,471	12,265	13,471	12,265
Local Choice Health Care	-	-	308,295	296,237	308,295	296,237
Route 460 Funding Corporation of Virginia	-	-	82,257	70,082	82,257	70,082
Virginia Industries for the Blind	-	-	37,521	31,058	37,521	31,058
Consolidated Laboratory	-	-	8,724	7,469	8,724	7,469
eVA Procurement System	-	-	19,827	19,693	19,827	19,693
Department of Environmental Quality Title V	-	-	11,786	10,724	11,786	10,724
Wireless E-911	-	-	37,315	42,449	37,315	42,449
Museum and Library Gift Shops	-	-	6,201	6,810	6,201	6,810
Behavioral Health Canteen and Work Activity	-	-	442	468	442	468
Total Expenses	33,616,006	32,535,389	2,986,559	2,964,659	36,602,565	35,500,048
Excess before transfers	29,250	434,033	1,225,816	974,111	1,255,066	1,408,144
Transfers	723,701	670,348	(723,701)	(670,348)	-	-
Increase in net position	752,951	1,104,381	502,115	303,763	1,255,066	1,408,144
Net position, July 1, as restated	20,209,205	19,104,824	659,707	355,944	20,868,912	19,460,768
Net position, June 30	\$ 20,962,156	\$ 20,209,205	\$ 1,161,822	\$ 659,707	\$ 22,123,978	\$ 20,868,912

Governmental Activities Revenues

Figure 13 is a graphical representation of the Statement of Activities revenues for governmental activities. Governmental activities revenues increased by \$675.8 million, or 2.0 percent. The net increase is mainly attributable to increases in the General Fund, which are discussed on page 34.

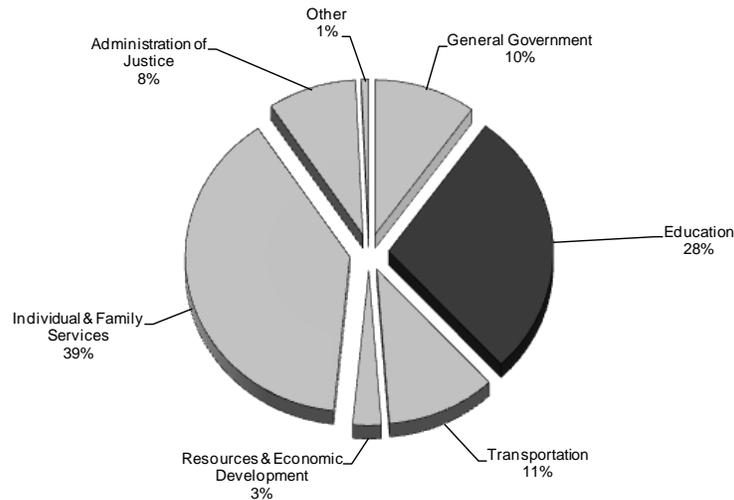
Figure 13
Revenues by Source – Governmental Activities
 Fiscal Year 2014



Governmental Activities Expenses

Figure 14 is a graphical representation of the Statement of Activities expenses for governmental activities. Governmental activities expenses increased by \$1.1 billion, or 3.3 percent. This change is primarily attributable to increases in all expense types with the exception of Resources and Economic Development and Interest and Charges on Long-term Debt. See pages 34 and 35 for additional information.

Figure 14
Expenses by Type – Governmental Activities
 Fiscal Year 2014



Net Position of Business-type Activities

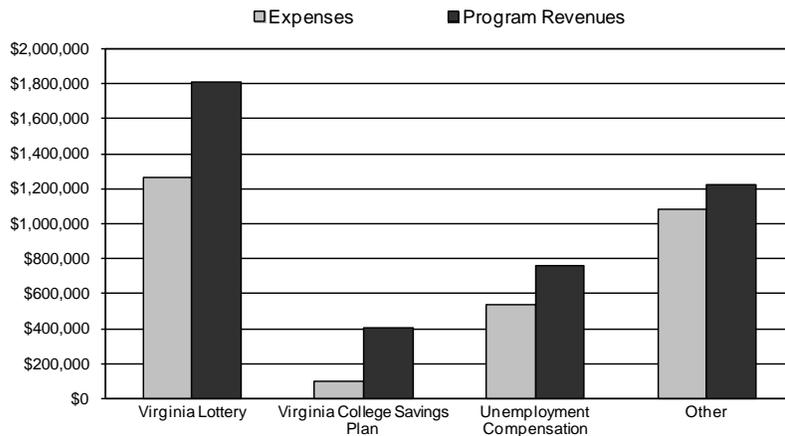
Net position of business-type activities increased by \$502.1 million during the fiscal year. As shown in **Figure 15**, highlights of the changes in net position for the major enterprise funds were as follows:

- Lottery sales were \$1.8 billion, an increase of \$121.6 million over the prior year. Net income was \$546.1 million, an increase of \$49.4 million (9.9 percent) from fiscal year 2013. Sales of scratch games increased by \$101.5 million (11.4 percent) and online sales increased by \$20.1 million (2.5 percent). This is offset by an increase of \$72.1 million (6.0 percent) in total expenses, primarily attributable to the cost of prizes and claims.
- Virginia College Savings Plan's net position increased by \$303.0 million (140.8 percent) during the fiscal year. This change is primarily attributable to an increase in investment income and a decrease in tuition benefits expense.
- Unemployment Compensation Fund net position increased by \$214.5 million during fiscal year 2014, primarily as a result of a decrease in benefit claims and an increase in the Employer Contribution schedule designed to recoup fund losses following recessionary periods. Operating expenses decreased by \$48.7 million. These factors combined give the Trust Fund the large increase.

The Trust Fund became insolvent in October 2009, which required obtaining Federal repayable advances under Title XII of the Social Security Act totaling \$938.3 million during fiscal years 2010, 2011, 2012 and 2013. No advances were required during fiscal year 2014.

Over the one year period July 1, 2013, to June 30, 2014, the unemployment rate declined from 5.6 percent to 5.2 percent. Additionally, there were approximately 30,912 fewer initial unemployment claims filed than in the previous year. These declines were offset by increases in the average weekly benefit amounts from approximately \$286 to \$290 in fiscal year 2014 and increases in the average benefit duration from 15.9 weeks to 16.3 weeks in fiscal year 2014. These multiple influences led to a decrease in the total benefit payments of \$48.7 million over the prior year.

Figure 15
Business-type Activities
Program Revenues and Expenses
 For the Fiscal Year Ended June 30, 2014
 (Dollars in Thousands)



Fund Statements Financial Analysis

As of the end of the fiscal year, the primary government's governmental funds reported combined ending fund balances of \$3.9 billion, including a negative unassigned fund balance of \$781.5 million indicating that restricted and committed amounts exceed the available modified accrual basis fund balance. The remainder of fund balance is nonspendable, restricted or committed to indicate that it is not available for new spending.

General Fund Highlights

At the end of the fiscal year, the General Fund reported a combined ending fund balance of \$629.6 million, a decrease of \$8.3 million in comparison with the prior year. Of this total fund balance, \$110.5 million represents nonspendable fund balance, \$970.5 million represents restricted fund balance, and \$330.1 million represents committed fund balance. These amounts are offset by a negative \$781.5 million unassigned fund balance.

Fiscal year 2014 General Fund revenues were 1.5 percent, or \$260.3 million, higher than fiscal year 2013 revenues. This revenue change results from increases of \$426.8 million primarily attributable to individual and fiduciary income taxes (\$280.7 million), interest, dividends, rents, and other investment income (\$65.3 million), and premiums of insurance companies taxes (\$52.0 million) offset by decreases of \$166.5 million primarily attributable to deeds, contracts, wills and suits taxes (\$69.7 million), other revenue primarily relating to expenditure recoveries from prior years (\$47.4 million), and tobacco master settlement revenue (\$25.3 million).

Fiscal year 2014 expenditures increased by 2.8 percent, or \$507.0 million, when compared to fiscal year 2013. This was primarily attributable to increases in education, individual and family services, and administration of justice expenditures of \$181.5 million, \$152.1 million, and \$95.2 million, respectively. Net other financing sources and uses increased by \$112.8 million, which is primarily due to lower transfers out to and higher transfers in from nongeneral funds.

Budget Highlights

The General Fund began the year with an original revenue budget that was \$629.8 million, or 3.6 percent, higher than the final fiscal year 2013 revenue budget. Additionally, the final revenue budget was slightly lower (\$69.1 million or 0.4 percent) than the original budget. The change between the original and final budget was primarily attributable to decreases in the final budget for sales and use taxes of \$118.9 million and corporation income of \$69.9 million due to revised economic forecasts. This was offset by increases in the final budget for individual and fiduciary income taxes of \$44.5 million and deeds, contracts, wills and suits of \$41.1 million. Total actual General Fund revenues were lower than final budgeted revenues by \$453.4 million due to weaker than anticipated collections.

Total final budget expenditures were higher than original budget expenditures by \$110.7 million, or 0.6 percent. This increase was primarily attributable to budgeted expenditures for education of \$111.6 million, administration of justice of \$108.8 million, and resources and economic development of \$78.6 million, offset in part by a decrease in general government of \$192.0 million.

The Commonwealth spent less than planned so actual expenditures were \$342.4 million, or 1.8 percent, lower than final budget expenditures.

Budget Outlook

In order to mitigate the effects of difficult economic conditions over the past several years, the Commonwealth adopted temporary budget solutions such as accelerated sales taxes.

While some of the conditions left by the financial and economic downturn experienced between 2008 and 2010 are still visible in certain sectors, Virginia's economy continued to recover, however at a slower rate than in prior years. Data regarding the primary economic indicators – jobs and new housing units that looked promising in prior fiscal years has tapered off. During fiscal year 2014, the two General Fund revenue sources most closely tied to current economic activity – individual income taxes and retail sales taxes – experienced a reduction when compared to the 2013 collections by \$86.6 million (0.8 percent) and \$153.3 million (4.8 percent), respectively. The individual income tax collections were less than the estimated revenue by \$415.8 million (3.6 percent) while the retail sales taxes were slightly less than the estimated revenue by \$12.9 million (0.4 percent). These declines were due, at least in part, to declines in federal contractors and the restraint Virginia consumers have demonstrated in response to the federal government cutbacks.

Although the fiscal year 2014 revenue collections compared to the estimate required a re-estimate for fiscal year 2015, there is planned growth in the adopted budget for the 2015-2016 biennium (fiscal years 2015 and 2016). Based on the most recent General Fund revenue estimate, fiscal year 2015 revenue is projected to increase 2.8 percent over the fiscal year 2014 revenue collections. While there is anticipated revenue growth, the Governor has instructed Cabinet Secretaries to prepare and submit plans for 5.0 percent and 7.0 percent reductions in General Fund spending for fiscal years 2015 and 2016, respectively. The Governor will release his amendments to the 2015-2016 biennial budget on December 17, 2014.

Major Special Revenue Fund Highlights

The Commonwealth Transportation Fund ended the fiscal year with a fund balance of \$2.3 billion, a decrease of \$138.2 million from the prior year. Approximately \$4.6 billion is contractually committed for various highway, public transportation, and rail preservation projects (see Note 20). The decrease in fund balance was primarily due to transportation expenditures exceeding revenues. Additionally, revenues and expenditures increased \$681.9 million, or 15.8 percent, and \$520.9 million, or 11.2 percent, respectively. This increased activity is primarily due to expenditures for highway maintenance, acquisition and construction.

The Federal Trust Fund balance increased by \$27.4 million, or 25.4 percent. This was primarily due to an increase in fines and forfeitures (reported as Other Revenue) of \$84.5 million, or 781.9 percent, and a net decrease in the Federal Grants and Contracts revenue of approximately \$103.4 million, or 1.2 percent. This change in the Federal Grants and Contracts revenue was primarily attributable to an increase in Medicaid funding of \$265.7 million, offset by the following decreases: lower American Recovery and Reinvestment Act revenue (\$92.6 million), unemployment insurance (\$152.6 million), food and home energy assistance programs (\$101.3 million), and education grants (\$29.3 million). Additionally, total expenditures decreased approximately \$26.5 million, or 0.3 percent. Net other financing sources and uses increased by \$7.3 million, or 37.3 percent.

The Literary Fund experienced a fund balance decrease of \$50.3 million, or 78.9 percent, in fiscal year 2014 when compared to fiscal year 2013. The decrease is the result of net disbursements exceeding net receipts by \$60.2 million, offset by a cash transfer in of \$9.8 million from the Virginia Lottery representing unclaimed prizes.

Capital Asset and Long-term Debt

Capital Assets. The primary government's investment in capital assets for its governmental and business-type activities as of June 30, 2014, amounts to \$28.1 billion (net of accumulated depreciation totaling \$15.4 billion). This investment in capital assets includes land, buildings, improvements, equipment, infrastructure, construction-in-progress, and intangible assets including water rights, easements, and software. Infrastructure assets are items that are normally immovable such as roads, bridges, drainage systems, and other similar assets. As noted on page 30, increases in capital assets and decreases in total liabilities and deferred inflows of resources resulted in an increase in net position of the governmental activities of \$753.0 million, or 3.7 percent. The increase in the primary government's net investment in capital assets was primarily attributable to increases in infrastructure and construction-in-progress of \$771.6 million and \$295.9 million, respectively. These increases are primarily attributable to transportation. The primary government reports equipment with a value of \$50,000 or greater and an expected useful life of two or more years. The primary government capitalizes all land, buildings, infrastructure, and intangible assets that have a cost or value greater than \$100,000 and an expected useful life of two or more years. Additional information on the primary government's capital assets can be found in Note 12, "Capital Assets."

Figure 16
Capital Assets as of June 30, 2014
(Net of Depreciation)
(Dollars in Thousands)

	Governmental Activities	Business-type Activities	Total
Land	\$ 2,821,220	\$ 1,977	\$ 2,823,197
Buildings	2,509,680	18,053	2,527,733
Equipment	482,538	13,661	496,199
Water Rights/Easements	64,870	-	64,870
Infrastructure	17,782,546	-	17,782,546
Software	253,556	2,683	256,239
Construction-in-Progress	3,984,130	132,165	4,116,295
Total	\$ 27,898,540	\$ 168,539	\$ 28,067,079

Long-term Debt. The Commonwealth is prohibited from issuing general obligation bonds for operating purposes. At the end of the current fiscal year, the Commonwealth had total debt outstanding of \$37.6 billion, including total tax-supported debt of \$15.4 billion and total debt not supported by taxes of \$22.2 billion. Bonds backed by the full faith and credit of the government and tax-supported total \$1.7 billion. Debt is considered tax-supported if Commonwealth tax revenues are used or pledged for debt service payments. An additional \$831.2 million is considered moral obligation debt which is not tax-supported. The Commonwealth has no direct or indirect pledge of tax revenues to fund reserve deficiencies. However, in some cases, the Commonwealth has made a moral obligation pledge to consider funding deficiencies in debt service reserves that may occur. The remainder of the Commonwealth's debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

During fiscal year 2014, the Commonwealth issued \$4.0 billion of new debt for various projects. Of this new debt, \$646.2 million was for the primary government and \$3.4 billion for the component units. Additional information on the Commonwealth's outstanding debt can be found on page 147 in Note 26, "Long-Term Liabilities," as well as in the section entitled "Debt Schedules." 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 may be issued to fund the defense of the Commonwealth; to meet casual deficits in revenue or in anticipation of the collection of revenues; or to redeem previous debt obligations, and are limited to 30.0 percent of 1.15 times the annual tax revenues for fiscal year 2014. 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 2012, 2013, and 2014. 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 2012, 2013, and 2014. The current debt limitation for the Commonwealth is \$5.3 billion, \$16.8 billion, and \$16.6 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. Currently, there is no 9(a) debt outstanding.

Figure 17
Outstanding Debt as of June 30, 2014
General Obligation Bonds
(Dollars in Thousands)

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
General obligation bonds				
9(b)	\$ 706,192	\$ -	\$ 706,192	\$ -
9(c)	36,677	-	36,677	925,086
Total	\$ 742,869	\$ -	\$ 742,869	\$ 925,086

Economic Factors and Review

During fiscal year 2014, the Commonwealth continued a slow recovery that began in 2011 from the recession of 2008-10. However, the recovery has tapered off, which is a cause for moderate concern. The Commonwealth experienced a weaker job growth rate than at the national level (0.3 percent at the state level versus 1.7 percent nationally), widening the gap between the Commonwealth's job growth rate and that of the nation during the last fiscal year. Personal income growth continued to rise at a very modest 1.4 percent rate during fiscal year 2014, compared to 3.3 percent in fiscal year 2013. Unemployment in the Commonwealth and at the national level continued to decline during the fiscal year, reaching 5.2 percent and 6.8 percent, respectively. Total taxable sales in the Commonwealth experienced a slight increase of 0.9 percent over fiscal 2013. Economic indicators show that during fiscal year 2014, the housing market both in the Commonwealth and at the national level declined dramatically for the first time since the recession. Additionally, housing prices in the Commonwealth again showed a positive change for fiscal year 2014, with an increase of nearly 3.2 percent, compared to almost 7.0 percent at the national level. Fiscal year 2014 indicates that Virginia's recovery from the recession shows a slowdown in the employment and personal income indicators. Therefore, the positive outlook shown in fiscal year 2013 has been replaced with moderate concern.

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. This report is also available for download at www.doa.virginia.gov.

The Commonwealth's component units issue their own separate financial statements. Contact information regarding each component unit is provided in Note 1.B.

