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# Notes to the Financial Statements

June 30, 2005

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### A. Basis of Presentation

The accompanying financial statements have been prepared in conformance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB).

### B. Reporting Entity

For financial reporting purposes, the Commonwealth of Virginia's (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, and they are financially accountable to the primary government (discrete component units). The funds 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. GASBS No. 39 was implemented in fiscal year 2004 and requires the inclusion of numerous organizations that raise and hold funds for the direct benefit of the primary government.

Section 2100 of the GASB *Codification of Governmental Accounting and Financial Reporting Standards* (GASB Codification) 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, and 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.

- (1) **Primary Government** – A primary government consists of all the organizations that make up its legal entity. All funds, organizations, institutions, agencies, and departments are, for financial reporting purposes, part of the primary government.
- (2) **Blended Component Units** – Though legally separate entities, these component units are, in substance, part of the primary government's operations. The blended component unit serves or benefits the primary government

almost exclusively. Financial information from these units is combined with that of the primary government. Blended component units are:

**Pocahontas Parkway Association** (Major Enterprise Fund) – The Association, a private, non-stock, nonprofit corporation was created to develop, construct, and provide financing for the Route 895 Connector Project. The Association is a blended component unit of the Department of Transportation (Primary Government) because it is fiscally dependent on the primary government and provides services entirely to the benefit of the Commonwealth. Ernst & Young, LLP audited the Association, and a separate report is available from the Association, Post Office Box 35033, Richmond, Virginia 23235.

**Virginia Public Building Authority (VPBA)** (Nonmajor Governmental Funds) – The Authority was created as a body politic and corporate and is fiscally independent. A government instrumentality, the Authority finances the acquisition and construction of buildings for the use of the Commonwealth and other approved purposes. The Governor appoints the seven-member board, and the primary government is able to impose its will on the Authority. The Auditor of Public Accounts audits the Authority, and a separate report is issued from the Department of the Treasury, Post Office Box 1879, Richmond, Virginia 23218.

- (3) **Discrete Component Units** – Discretely presented component units are reported in a separate column in the government-wide financial statements to emphasize that they are legally separate from the primary government. They are financially accountable to the primary government, or have relationships with the primary government such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. These discrete component units serve or benefit those outside of the primary government.

GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, was effective for fiscal year 2004. This Statement generally requires any organization that raises and holds economic resources for the direct benefit of the reporting entity to be reported as a component unit, even if the reporting entity is not financially accountable for the organization. The entities are included in the Commonwealth's reporting entity as nonprofit charitable organizations and exist solely to support the Commonwealth's higher

education institutions, museums, and the Library of Virginia. The higher education institution nonprofit organizations are included in the applicable higher education institution's column in the accompanying financial statements. The museum foundations, and the Library of Virginia Foundation, which are discretely presented, are more fully described later in this footnote. The Virginia Horse Center Foundation, a component unit of the Virginia Equine Center (Center) (Nonmajor Component Unit), is included in the Center's column in the accompanying financial statements. In all instances where separate disclosure of these nonprofit organizations is required in the accompanying footnotes, the entities' totals are aggregated and disclosed as "Foundations." Discretely presented component units are:

**Higher Education Institutions** – The Commonwealth's higher education institutions are granted broad corporate powers by State statutes. The Governor appoints the members of each institution's Board of Trustees. In addition to the annual appropriations to support the institutions' operations, the State provides funding for, and construction of, major academic plant facilities for the institutions. Therefore, there is a financial benefit/burden to the primary government. The bonds issued to finance the construction of these facilities are obligations of the State. The major higher education institutions are: University of Virginia, including the University of Virginia Hospital and the University of Virginia's College at Wise (formerly reported as Clinch Valley College); Virginia Polytechnic Institute and State University; and Virginia Commonwealth University, including the Virginia Commonwealth University Health System Authority (formerly reported as MCV Health Systems Authority). The nonmajor Higher Education Institutions are: the College of William & Mary, including Richard Bland College and the Virginia Institute of Marine Science; Virginia Military Institute; Virginia State University; Norfolk State University; University of Mary Washington; James Madison University; Radford University; Old Dominion University; George Mason University; Virginia Community College System; Christopher Newport University; and Longwood University. The Southwest Virginia Higher Education Center, the Roanoke Higher Education Authority, and the Institute for Advanced Learning and Research are also included as nonmajor higher education institutions. The colleges and universities are funded through State appropriations, tuition, Federal grants, and private donations and grants. As noted previously, certain Foundations are considered component units of the higher education institutions, and are included in the accompanying financial statements as well as the higher education institutions' individually published financial

statements. The Auditor of Public Accounts (APA) does not audit component units of the higher education institutions, including Foundations, but relies on the reports issued by other auditors to render their opinion.

The APA audits the colleges and universities, and individual reports are issued under separate cover. Complete financial statements for each institution may be obtained from their respective administrative offices. The addresses for these institutions may be obtained from the Virginia Department of Accounts, 101 North 14th Street, Richmond, Virginia 23219.

**Virginia Housing Development Authority (VHDA)** (Major) – The Authority was created as a political subdivision and instrumentality of the Commonwealth and is granted both political and corporate powers by the *Code of Virginia*. The Governor appoints a majority of the Authority's Board members and the remainder of the Board members are ex-officio. The Commonwealth may make grants to the Authority including, but not limited to, reserve funds, which is a potential financial benefit/burden to the primary government. The State is not legally obligated by the debt of the Authority. The Authority was created in the public interest to provide investment in and stimulate construction of low to moderate income housing which benefits the citizens of the Commonwealth. The administrative offices of the Authority are located at 601 South Belvidere Street, Richmond, Virginia 23220. KPMG, LLP audited the Authority, and a separate report is available.

**Virginia Public School Authority (VPSA)** (Major) – The Authority was created as a public body corporate, and an agency and instrumentality of the Commonwealth to finance capital projects of city and county school boards. The Governor appoints the board members, who serve at his pleasure. Therefore, the primary government is able to impose its will on the Authority. The Auditor of Public Accounts audits the Authority, and a separate report is issued from the Department of the Treasury, Post Office Box 1879, Richmond, Virginia 23218.

**Virginia Economic Development Partnership (VEDP)** (Nonmajor) – The Partnership was created as a body corporate and operates to encourage, stimulate, and support the development and expansion of commerce in the Commonwealth. The Governor appoints the 15-member board, and there is a financial benefit/burden to the primary government. The administrative offices are located at 901 East Byrd Street, Post Office Box 798, Richmond, Virginia 23218-0798. The Auditor of Public Accounts audits the Partnership, and a separate report is issued.

**Virginia Outdoors Foundation** (Nonmajor) – The Foundation was created as a body politic and is administratively assigned to the Department of Conservation and Recreation (Primary Government) and charged with promoting preservation through the acceptance of donated conservation easements and raising funds for the purchase of preservation land. The Governor appoints the seven-member Board of Trustees, and the primary government can impose its will on the Foundation. The administrative offices of the Foundation are located at 101 North 14<sup>th</sup> Street, 17<sup>th</sup> Floor, Richmond, Virginia 23219. The Auditor of Public Accounts audits the Foundation as part of the Department of Conservation and Recreation and discloses its existence in that report.

**Virginia Port Authority (VPA)** (Nonmajor) – The Authority was established as a corporate body and operates to serve the citizens and promote commerce through the harbors and ports of Virginia. The Governor appoints a majority of the 12-member board, and the primary government is able to impose its will on the Authority. There is also a financial benefit/burden to the primary government. The administrative offices of the Authority are located at 600 World Trade Center, Norfolk, Virginia 23510. The Auditor of Public Accounts audits the Authority, and a separate report is issued.

**Virginia Resources Authority (VRA)** (Nonmajor) – The Authority was created as a statewide public body corporate political subdivision of the Commonwealth to provide financing of infrastructure projects for water supply, wastewater, storm water, solid waste treatment, airports, public safety, brownfields remediation and redevelopment, and recycling. The Governor appoints the 11-member board and the Executive Director of the Authority. The primary government is able to impose its will on the Authority, and there is a financial benefit/burden to the primary government. The Commonwealth does not guarantee any bonds issued by the Virginia Resources Authority. The administrative offices of the Authority are located at 707 East Main Street, Suite 1350, Richmond, Virginia 23219. Goodman and Company, LLP audited the Authority, and a separate report is available.

**Virginia Tourism Authority** (Nonmajor) – The Authority was created as a public body corporate and as a political subdivision of the Commonwealth. The Authority encourages, stimulates, and promotes tourism and film production industries of the Commonwealth. The Governor appoints all of the board members, and there is a financial benefit/burden to the primary government. The administrative offices are located at 901 East Byrd Street, Nineteenth Floor, Richmond, Virginia 23219. The Auditor of Public Accounts

audits the Authority, and a separate report is issued.

**Virginia Tobacco Settlement Foundation** (Nonmajor) – The Foundation was created as a body corporate and as a political subdivision of the Commonwealth. The Foundation was established to determine the appropriate recipients of monies in the Virginia Tobacco Settlement Fund and to distribute monies in this fund for such efforts as restricting the use of tobacco products by minors and the enforcement of laws restricting the distribution of tobacco products to minors. The Governor appoints the majority of the board, and there is a financial benefit/burden to the primary government. The administrative offices are located at 701 East Franklin Street, Fifth Floor, Richmond, Virginia, 23219. The Auditor of Public Accounts audits the Authority, and a separate report is issued.

**Tobacco Indemnification and Community Revitalization Commission** (Nonmajor) – The Commission was created as a body corporate and as a political subdivision of the Commonwealth. The Commission was established to determine the appropriate recipients of the monies in the Tobacco Indemnification and Community Revitalization Fund. This fund is to provide payments to tobacco farmers as compensation for the adverse economic effects resulting from loss of investment in specialized tobacco equipment and barns, and lost tobacco production opportunities. It also provides monies to revitalize tobacco dependent communities. The Governor appoints the majority of the board, and there is a financial benefit/burden to the primary government. The administrative offices are located at 701 East Franklin Street, Suite 501, Richmond, Virginia 23219. The Auditor of Public Accounts audits the Commission, and a separate report is issued.

**Hampton Roads Sanitation District Commission** (Nonmajor) – The Commission was established as a political subdivision of the Commonwealth and a government instrumentality. The Commission, which is the governing Board of the District, was granted corporate powers by the *Code of Virginia*. The Governor appoints the Commission members, who serve at his pleasure. Therefore, the primary government is able to impose its will on the Commission. The Commonwealth is not obligated by the debt of the Commission. The Commission was established to benefit the inhabitants of the District and operates a sewage system for 17 localities in the Chesapeake Bay area. The address for the administrative offices of the Commission is 1436 Air Rail Ave, Post Office Box 5915, Virginia Beach, Virginia 23471. KPMG, LLP, audited the Commission, and a separate report is available.

**Virginia Biotechnology Research Park Authority** (Nonmajor) – The Authority is a legally separate, political subdivision of the Commonwealth created by the General Assembly to assist in the development of a biotechnology research park. The Governor appoints the board members of the Authority, and there is a potential financial benefit/burden to the primary government. The administrative offices of the Authority are located at 800 East Leigh Street, Richmond, Virginia 23219. The Auditor of Public Accounts audits the Authority, and a separate report is issued.

**Small Business Financing Authority (SBFA)** (Nonmajor) – The Virginia Small Business Financing Act of 1984 (Chapter 28, Title 9, *Code of Virginia*) established the Authority as a public body corporate and a political subdivision of the Commonwealth. The Governor appoints the 11-member board, and the primary government is able to impose its will on the Authority. The Authority was created to assist small businesses in the Commonwealth in obtaining financing for new businesses or the expansion of existing businesses. The Authority can provide financial assistance to small businesses by providing loans, guarantees, insurance, and other assistance, thereby encouraging the investment of private capital in small businesses in the Commonwealth. The Authority can loan money to local governments as defined by the *Code of Virginia* for economic development purposes. The Authority also guarantees loans made to small businesses by banks. The administrative offices of the Authority are located at 707 East Main Street, Suite 300, Richmond, Virginia 23219. The Auditor of Public Accounts audits the Authority, and a separate report is issued.

**Virginia Schools for the Deaf and Blind Foundation** (Nonmajor) – The Foundation operates as a non-private educational and fund raising organization solely in connection with, and exclusively for the benefit of the Virginia School for the Deaf and Blind at Staunton (Primary Government) and the Virginia School for the Deaf, Blind and Multi-Disabled at Hampton (Primary Government), and within the jurisdiction and management of the Virginia Board of Education. The Foundation uses a December 31 calendar year end. The administrative offices of the Foundation are located at the Virginia Department of Education, 101 North 14th Street, Richmond, Virginia, 23219. The Auditor of Public Accounts audits the Foundation along with the audit of the Department of Education, and a separate report is issued.

**Science Museum of Virginia Foundation** (Nonmajor) – The Foundation is a non-stock, non-profit corporation established to implement and fund programs, projects, and operations that are authorized and approved by the

Trustees of the Science Museum of Virginia (Primary Government). The administrative offices of the Foundation are located at the Science Museum of Virginia, 2500 W. Broad Street, Richmond, Virginia 23220. The audit was conducted by Rose Sanderson & Creasy; however this firm was acquired by Yount, Hyde & Barbour, PC, who will issue the report.

**Virginia Museum of Fine Arts Foundation** (Nonmajor) – The Foundation operates as a non-profit corporation under the laws of Virginia to fund exhibitions, programs, and capital asset expansion to ensure that the Virginia Museum of Fine Arts (Primary Government) has the space and resources for art to help improve the quality of life for many. The administrative offices of the Foundation are located at 2800 Grove Avenue, Richmond, Virginia 23221. KPMG, LLP, audits the Foundation and a separate report is issued.

**A. L. Philpott Manufacturing Extension Partnership** (Nonmajor) – The Partnership has the mission to foster economic growth by enhancing the competitiveness of Virginia's manufacturers. The Partnership provides manufacturing firms with fee-based technology consulting services, access to business modernization resources, and support for interfirm collaboration. Further, the Partnership provides direct assistance to increase sales, decrease costs, and improve quality, productivity, and competitiveness. The Partnership has a 23-member Board of Trustees. The Board consists of the presidents of two public four-year institutions of higher education; three community college presidents; the director of Virginia's Center for Innovative Technology; Virginia's Secretary of Commerce and Trade; and fifteen citizen members, representing manufacturing industries, appointed by the Governor. There is also a financial benefit/burden to the primary government. The administrative office is located at Patrick Henry Community College, 645 Patriot Avenue, Post Office Box 5311, Martinsville, Virginia 24115. The Auditor of Public Accounts audits the Partnership, and a separate report is issued.

**Virginia Equine Center Foundation** (Nonmajor) – The Foundation was created as a body politic and corporate, and operates the Virginia Equine Center (Center) for the benefit of the equine and tourism industries. In 1994, the Commonwealth began making grant payments to the Foundation to keep the Center from falling into default on its debt. The Governor appoints a majority of the 11-member board, and there is a financial benefit/burden to the primary government. As previously noted, the Center includes the Virginia Horse Center Foundation as part of its report, pursuant to GASBS No. 39. The address for the administrative offices of the Foundation is Post Office Box 1051, Lexington,

Virginia 24450. The accounting firm of William White, Sr., CPA audited the Foundation, and a separate report is available.

**Certified Nursing Facility Education Initiative** (Nonmajor) – The Initiative was created as a nonprofit corporation by the *Code of Virginia* to assist the Department of Medical Assistance Services (DMAS) (Primary Government). The Initiative provides early on-site training and assistance to certified nursing facilities to improve quality of care and life to certified nursing facility residents. The address for the administrative offices of the Initiative is Post Office Box 465, Orange, Virginia 22960. Cole & King, LLC, CPA's audited the Initiative, and a separate report is available. A note to the audited financial statements disclosed that the Initiative has relied on funding from DMAS to meet operating expenses and expressed concern that the Initiative might not be able to continue operations past June 30, 2005, should that funding not be renewed or replaced by another source.

**Virginia Land Conservation Foundation (VLCF)** (Nonmajor) – The Foundation was created as a body politic and corporate to serve the Department of Conservation and Recreation (Primary Government) by acquiring interests in preservation land and providing grants to other entities to acquire interests in preservation land. The Governor appoints the 18-member board, and the primary government can impose its will on the Foundation. The administrative offices of the Foundation are located at 203 Governor Street, Suite 402, Richmond, Virginia 23219. The Auditor of Public Accounts audits the Foundation as part of the Department of Conservation and Recreation and discloses its existence in that report.

**Virginia Arts Foundation** (Nonmajor) – The Foundation was created as a body politic and corporate to serve the Virginia Commission for the Arts (Primary Government) by promoting the arts in the Commonwealth. The Governor appoints the Board of Trustees for the Virginia Commission for the Arts, which also serves as the Board for the Virginia Arts Foundation. The Director of the Virginia Commission for the Arts serves as the Board chairman. In addition, the primary government can impose its will on the Foundation. The administrative offices of the Foundation are located at 223 Governor Street, Richmond, VA 23219. The Auditor of Public Accounts audits the foundation as part of the Virginia Commission for the Arts.

**Library of Virginia Foundation** (Nonmajor) – The Foundation was created as a private, nonprofit 501 (c) (3) corporation supporting the Library of Virginia. The Foundation was established in 1984 upon receipt of a major bequest. The articles of incorporation stipulate that the Foundation shall at all times be

operated solely in connection with, and exclusively for the benefit of the Virginia State Library. The Foundation is governed by a separate Board of Directors and promotes and supports the Library of Virginia in all activities. The audit was conducted by Rose Sanderson & Creasy; however this firm was acquired by Yount, Hyde & Barbour, PC, who will issue the report.

**Innovative Technology Authority (ITA)** (Nonmajor) – The Authority is granted corporate powers by the *Code of Virginia*. The Authority serves to facilitate the marketing, organization, and development of scientific research and technology by the State's institutions of higher education and private industry in the Commonwealth. The Governor appoints the 16-member board, and there is a financial benefit/burden to the primary government. The Authority's combined financial statements include the accounts of the Center for Innovative Technology (CIT) after elimination of all significant intercompany balances and transactions. CIT is a nonstock, not-for-profit corporation, which acts as the operating arm of the Authority. The address for the administrative offices of the Authority is CIT Building, Suite 600, 2114 Rock Hill Road, Herndon, Virginia 22070. The Auditor of Public Accounts audits the Authority, and a separate report is issued.

**Virginia College Building Authority (VCBA)** (Nonmajor) – The Authority was created as a public body corporate, a political subdivision, and an agency and instrumentality of the Commonwealth. The Governor appoints a majority of the board and members serve at his pleasure. Therefore, the primary government is able to impose its will on the Authority. The Authority finances certain capital projects and equipment purchases of State-supported colleges and universities. The Auditor of Public Accounts audits the Authority, and a separate report is issued from the Department of the Treasury, Post Office Box 1879, Richmond, Virginia 23218.

Only the activity of the Authority that relates to the financing of capital projects and equipment purchases by State-supported colleges and universities is included in the financial statements. The Authority assists private institutions of higher education in the financing and refinancing of a broad range of facilities. The Authority is authorized to issue obligations and lend the proceeds to private institutions; however, such financings or refinancings are not obligations of the Primary Government nor the Authority, but are payable solely from the revenues pledged by the respective private institution. This indebtedness, totaling \$390.6 million, is not included in the financial statements.

- (4) **Related Organizations** – Organizations for which a primary government is accountable because that government appoints a majority of the Board, but is not financially accountable, are related organizations. Related organizations are:

**Tobacco Settlement Financing Corporation** – The Corporation was created by the Tobacco Settlement Financing Corporation Act, Chapters 482 and 488 of the Acts of the General Assembly of the Commonwealth of Virginia (Commonwealth) during the 2002 General Assembly Session. The Corporation is a public body corporate entity and an independent instrumentality of the Commonwealth, managed by a six-member board, including the State Treasurer. The Corporation purchased fifty percent of the future tobacco settlement revenue belonging to the Tobacco Indemnification and Community Revitalization Commission, a discrete component unit of the Commonwealth. The Commonwealth's tobacco revenue was not securitized. The administrative offices of the Corporation are located at 101 N. 14<sup>th</sup> Street, 3<sup>rd</sup> Floor P.O. Box 1879 Richmond, Virginia 23218-1879. Goodman and Company, LLP audited the Corporation, and a separate report is available.

**Virginia Recreational Facilities Authority** – The Authority was created as a political subdivision and instrumentality of the Commonwealth and given separate corporate powers by the *Code of Virginia*. The Governor appoints the 13-member board of directors. The Authority operates educational programs, tourism, and commerce in the Roanoke Valley. The address for the administrative offices of the Authority is 3900 Rutrough Road, Roanoke, Virginia 24014. Foti, Flynn, Lowen and Company audited the Authority, and a separate report is available.

**Miller School of Albemarle** – The School was created through the will of Samuel Miller of Lynchburg to provide a quality education for poor and orphaned children in central Virginia. Initially, the Commonwealth was charged with oversight of the Miller Trust Fund, which supported the School. The Governor still appoints one-third of the board. The administrative offices of the School are located at 1000 Samuel Miller Loop, Charlottesville, Virginia 22903. Joseph J. Saunders, III, CPA, Inc. audited the School, and a separate report is available.

**Jamestown-Yorktown Educational Trust** – The Trust was created as a nonprofit corporation by the *Code of Virginia* to assist the Jamestown-Yorktown Foundation (Foundation). The Trust Board consists of six members selected from the Foundation's Board of Trustees. Several Commonwealth officials serve as ex-officio members of the

Foundation's Board, and the Governor appoints twelve members. The Trust operates the Jamestown Settlement and Yorktown Victory Centers' gift shops and café, oversees investments, and sponsors events. The address for the administrative offices of the Trust is Post Office Box 3605, Williamsburg, Virginia 23187. Goodman and Company, LLP, audited the Trust, and a separate report is available.

**Virginia Birth-Related Neurological Injury Compensation Program** – The Program was created to provide a no-fault alternative for birth-related neurological injuries. The Governor appoints the 7-member board. The administrative offices of the Program are located at 9100 Arboretum Parkway Suite 365, Richmond, Virginia 23236. Cherry, Bekaert, & Holland audited the Program, and a separate report is available.

**Chesapeake Bay Bridge and Tunnel Commission** – The Commission was created to establish policy and administer operations of the Chesapeake Bay Bridge Tunnel District. Any of the 11 members of the Commission appointed or reappointed on or after July 1, 1998, shall be appointed by the Governor, subject to confirmation by each house of the General Assembly. The administrative offices of the Commission are located at Post Office Box 111, 32386 Lankford Highway, Cape Charles, Virginia 23310. KPMG, LLP, audited the Commission, and a separate report is available.

**Assistive Technology Loan Fund Authority** – The Authority was created as a political subdivision and public body corporate by the *Code of Virginia*. The Governor appoints the board of directors as directed by the *Code*. The Authority manages a fund to provide loans to individuals to acquire assistive technology, other equipment, or other authorized purposes designed to help disabled individuals become more independent. The administrative offices are located at 1602 Rolling Hills Drive, Suite 106, Richmond, Virginia 23229. The Authority is audited by Goodman and Company, LLP.

### C. Government-wide and Fund Financial Statements

The government-wide financial statements, the Statement of Net Assets and the Statement of Activities, report information on all nonfiduciary activities of the primary government and component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which are normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Also, the primary government activity is reported separately from the

legally separate component units for which the Commonwealth is financially accountable.

The Statement of Activities demonstrates the degree to which direct expenses of a specific function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function, segment, or component unit. In addition, to the extent that indirect costs are allocated to the various functions, the program expenses will include both direct and indirect costs. Program revenues include charges to customers who purchase, use, or directly benefit from goods or services provided by a given function, segment, or component unit, as well as investment income generated by operations. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function, segment, or component unit. Taxes and other items properly excluded from program revenues are reported as general revenues.

Net assets are restricted when constraints are placed on them that are imposed by external parties or constitutional provisions. Designations solely imposed by the Commonwealth's management are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, the Commonwealth's policy is to use the restricted resources first. Some institutions of higher education may follow a different policy.

Separate financial statements are provided for governmental funds, proprietary funds, fiduciary funds, and component units. However, fiduciary funds are not included in the government-wide statements. Major governmental funds, enterprise funds, and component units are reported as separate columns in the fund financial statements, with nonmajor funds being aggregated into a single column.

#### **D. Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

**Government-wide Financial Statements** – The government-wide financial statements are reported using the economic resources measurement focus and the full accrual basis of accounting. Revenues are recorded when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**Governmental Fund Financial Statements** – The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Primary Government

considers revenues to be available if they are collected within 60 days of the end of the current fiscal year (or one year for Medicaid). Significant revenues subject to accrual include Federal grants and income and sales taxes. Income tax revenues for tax underpayments are only recognized to the extent of the Primary Government's estimated refunds for tax overpayments received. Revenues that the Primary Government earns by incurring obligations are recognized in the same period as when the obligations are recognized.

Expenditures generally are recorded when a liability is incurred, as under full accrual accounting. However, expenditures related to debt service, compensated absences, and claims and judgments are recorded only when the payment is due.

The Primary Government reports the following major governmental funds:

**General Fund** – Accounts for the transactions related to resources received and used for those services traditionally provided by a State government, which are not accounted for in any other fund. These services include general government, legislative and judicial activities, public safety, health and mental health programs, resources and economic development, licensing and regulation, and primary and secondary education.

**Commonwealth Transportation Special Revenue Fund** – Accounts for the revenues and expenditures associated with highway operations, maintenance, construction, and other transportation related activities. Funding for these programs is received from highway user taxes, fees, and funds received from the Federal government.

**Federal Trust Special Revenue Fund** – Accounts for all federal dollars received by the Commonwealth except those received by the Commonwealth Transportation Fund, the Unemployment Compensation Fund, and institutions of higher education. In addition, federal funds received from Medicaid intergovernmental transfers and for the Primary Government's share of claims are reported in the Other – Special Revenue Fund.

**Literary Fund Special Revenue Fund** – Accounts for revenues from fines, forfeitures, and proceeds from unclaimed property used primarily to support public education in the Commonwealth. This fund provides low interest loans to school divisions for construction, renovations, and expansion of school buildings.

**Proprietary Funds, Fiduciary Funds, and Component Units Financial Statements** – The financial statements of the proprietary funds, fiduciary funds, and component units are reported using the economic resources measurement focus and the full accrual basis of accounting. As with the government-wide statements, revenues are

recorded when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Agency funds have no measurement focus since they only report assets and liabilities.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating.

GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, provides governments two options for reporting their enterprise funds (including component units reporting as business-type activities). All enterprise funds reported herein, with the exception of the State Lottery, the Pocahontas Parkway (Major Enterprise Fund), Mental Health Local Funds (Nonmajor Enterprise Fund), the Virginia Port Authority (Nonmajor Component Unit), the A. L. Philpott Manufacturing Extension Partnership (Nonmajor Component Unit), the Virginia Equine Center (Nonmajor Component Unit), University of Mary Washington (Nonmajor Component Unit), the Roanoke Higher Education Authority (Nonmajor Component Unit), and the Innovative Technology Authority (Nonmajor Component Unit) apply all applicable GASB pronouncements and all FASB Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989, unless they conflict with or contradict GASB pronouncements. The State Lottery, the Pocahontas Parkway (Major Enterprise Fund), Mental Health Local Funds (Nonmajor Enterprise Fund), the Virginia Port Authority (Nonmajor Component Unit), the A. L. Philpott Manufacturing Extension Partnership (Nonmajor Component Unit), the Virginia Equine Center (Nonmajor Component Unit), the University of Mary Washington (Nonmajor Component Unit), the Roanoke Higher Education Authority (Nonmajor Component Unit), and the Innovative Technology Authority (Nonmajor Component Unit) apply all of these pronouncements, and also apply all FASB Statements and Interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements.

Foundations' (Component Units) financial statements are prepared using the economic resources measurement focus and the full accrual basis of accounting. The financial statements are prepared under FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations*. FASB rather than GASB pronouncements are followed. In some instances, activities of the Foundations (Component Units) are reported separately within

the footnotes because of the different reporting standards. Also, some Foundations (Component Units) have a calendar rather than a fiscal year end. Foundations (Component Units) with a calendar year-end are included in these financial statements for the year ending December 31, 2004.

The Primary Government reports the following major enterprise funds:

**State Lottery Fund** – Accounts for all receipts and expenses of the State Lottery.

**Virginia College Savings Plan Fund** – Administers the Virginia Prepaid Education Program.

**Pocahontas Parkway Fund** – Accounts for the Route 895 Connector Project. The Pocahontas Parkway Association is a blended component unit of the Department of Transportation (Primary Government).

**Unemployment Compensation Fund** – Accounts for receipts from employers and expenses incurred to provide benefits to eligible unemployed workers.

Additionally, the Primary Government reports the following fund types:

#### **Governmental Fund Types:**

**Special Revenue Funds** – Account for transactions related to resources received and used for restricted or specific purposes.

**Debt Service Funds** – Account for transactions related to resources retained and used for the payment of interest and principal on long-term obligations.

**Capital Project Funds** – Account for transactions related to resources received and used for the acquisition, construction, or improvement of capital facilities not reported in the other governmental or proprietary funds. The primary resource for these funds is the proceeds of bond issues. Principal uses are for construction and improvement of State office buildings, correctional and mental health facilities, and parks.

**Permanent Funds** – Account for transactions of the Commonwealth Health Research Fund and the Mental Health Endowment Funds whose principal must be maintained intact and whose income is used to benefit the Commonwealth's citizens and mental health patients.

#### **Proprietary Fund Types:**

**Enterprise Funds** – Account for transactions related to resources received and used for financing self-supporting activities of the Primary Government that offer products and

services on a user-charge basis to external users.

**Internal Service Funds** – Account for transactions related to the financing and sale of goods or services provided by the agencies of the Primary Government to other agencies and institutions of the Commonwealth. Activities include the provision of information technology, manufacturing activities, insurance programs, fleet services, facilities and property management, and engineering services.

#### **Fiduciary Fund Types:**

**Private Purpose Trust Funds** – Account for transactions of all other trust arrangements in which the principal and income benefit individuals, private organizations, or other governments. These trusts include those for escheat property, educational savings plans, and others.

**Pension Trust Funds** – Account for transactions of the Commonwealth administered retirement systems and other employment benefits.

**Investment Trust Funds** – Account for the external portions of the State Non-Arbitrage Program and Local Government Investment Pools that are sponsored by the Commonwealth.

**Agency Funds** – Account for amounts held in trust by the Primary Government for others. Agency funds include those funds established to account for the collection of taxes and fees for distribution to localities and other states, employee benefits, deposits of insurance carriers, child support collections and other miscellaneous accounts.

#### **E. Budgetary Process**

Budgetary amounts shown in the Required Supplementary Information and Combining and Individual Fund Statements Sections represent the total of the original budgeted amounts and all supplemental appropriations. The Commonwealth's budget is prepared principally on a cash basis and represents appropriations as authorized by the General Assembly. Unexpended appropriations at the end of the fiscal year generally lapse. However, they may be reappropriated for expenditure in the following fiscal year. The Governor, as required by the *Code of Virginia*, submits a budget composed of all proposed expenditures for the State, and of estimated revenues and borrowing for a biennium, to the General Assembly. Budgets are adopted for the General and Special Revenue Funds, except for the Literary (major) – Special Revenue Fund. Formal budgetary integration is not employed for the Capital Projects (nonmajor), Debt Service (nonmajor), Permanent Funds (nonmajor), and the Literary – Special Revenue (major) because effective budgetary control is alternatively achieved

through the General Fund and the remaining Special Revenue Funds.

The budget is prepared on a biennial basis; however, the budgets of the General and Special Revenue Funds contain separate appropriations for each year within the biennial budget, as approved by the General Assembly and signed into law by the Governor. For management control purposes, the budget is controlled at the program level. The Governor may transfer an appropriation within a State agency or from one State agency to another, provided that total fund appropriations, as contained within the budget, are not exceeded. Increases in General Fund appropriations must be approved by the General Assembly.

Appropriations for programs funded from Special Revenue Funds may allow expenditures in excess of the original appropriations to the extent that revenues of the funds exceed original budget estimates and such additional expenditures are approved by the Governor through supplemental appropriations.

#### **F. Cash, Cash Equivalents, and Investments**

##### **Cash**

In order to maximize the Commonwealth's earning potential, the majority of the Primary Government's cash balances are pooled together in the general account for investment purposes. The amounts required for operations are liquidated as needed. Since all amounts not required for operations are held in investment securities, it is possible that the cash balances could be negative due to timing differences in liquidating the investments.

As of June 30, 2005, the General Fund had a negative cash balance of \$3.6 billion. In order to properly reflect the general account position, this negative cash balance has been eliminated in the accompanying statements and offset against the Primary Government's cash equivalents and investments (see Note 5).

##### **Cash Equivalents**

Cash equivalents are investments with an original maturity of three months or less.

##### **Investments**

Investments are principally comprised of monies held by component units, Pension Trust Funds, and monies held by the State Treasurer in both the general account and other fiduciary accounts.

Governmental and proprietary funds, both primary government and component units, report investments in money market and in the Commonwealth sponsored investment pools at amortized cost. All other investments are reported at fair value, in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for*

### *Certain Investments and for External Investment Pools.*

Investments administered by the Virginia Retirement System (VRS) are reported at fair value. The cost of investments sold is the average cost of the aggregate holding of the specific investment sold. Investments in affiliated organizations are accounted for on the equity method of accounting and the VRS' share of their earnings (losses) for the period is included in investment income using the equity method.

Investments of higher education institutions (Component Units) are reported at fair value, except for money market investments and investments in the Commonwealth sponsored investment pools, which are reported at amortized cost.

### **Derivatives**

Derivative instruments are used to improve return on investments and modify risk exposures (see Note 5).

### **G. Receivables**

Receivables in the governmental funds consist primarily of the accrual of taxes, as well as Federal receivables of the Primary Government's Medicaid program. Receivables in the Proprietary Funds consist primarily of tuition contributions receivable. Receivables of Fiduciary Funds are primarily the accrual of member and employer contributions in the Pension Trust Funds and the accrual of local sales taxes in the Agency Funds. Receivables of the Component Units consist primarily of mortgage receivables, loans receivable, patient receivables, and student receivables. Receivables are recorded net of allowances for doubtful accounts (see Note 6).

### **H. Contributions Receivable, Net**

Contributions Receivable reported by the foundations (Component Units) represents pledges or unconditional promises to give that have been discounted (see Note 7).

### **I. Internal Balances**

Interfund receivables and payables have been eliminated from the Statement of Net Assets, except for the residual amounts due between governmental and business-type activities (see Note 8).

### **J. Inventory**

Inventories consist of materials and supplies and are reported as expenditures when consumed. These assets are offset by a fund balance reserve that indicates they are not available for spending. Inventories exceeding \$1 million of the General and the Special Revenue Funds are maintained at cost

using the first-in, first-out (FIFO) methodology, except for the following:

- Department of State Police (VSP)
- Virginia Department of Transportation (VDOT)
- Department of Health (VDH)
- Department for the Blind and Vision Impaired (DBVI)

VSP inventories are recorded in the General (major) and Dedicated Special Revenue (nonmajor) Funds using the average cost methodology and are maintained at cost. VDOT inventories are recorded in the Commonwealth Transportation Fund (major) using the FIFO and average cost methodologies and are maintained at either cost or average cost. VDH inventories are recorded in the General (major), Other Special Revenue (nonmajor), and Federal Trust (major) Funds. These inventories are maintained at cost based on either FIFO or the average cost methodology. DBVI inventories are maintained at cost or average cost based on the FIFO methodology.

Inventories maintained by Correctional Enterprises (Internal Service Fund) are stated at the lower of cost or market using FIFO. Inventories maintained by the Virginia Museum of Fine Arts (Nonmajor Enterprise Fund), the Science Museum of Virginia (Nonmajor Enterprise Fund), the Consolidated Laboratory (Nonmajor Enterprise Fund) and the Library of Virginia (Nonmajor Enterprise Fund) are stated at cost using FIFO. Inventories maintained by the Internal Service Funds except for Correctional Enterprises are stated at cost using FIFO.

The Department of Alcoholic Beverage Control (Nonmajor Enterprise Fund) maintains inventories using the average cost methodology. The Virginia Industries for the Blind (Nonmajor Enterprise Fund) maintains inventories at cost using the average cost methodology. The State Lottery Department's (Major Enterprise Fund) inventory consists of unsold instant tickets that are valued at cost and expensed over the life of each game as it is sold to retailers.

Institutions of higher education (Component Units) use several methods for inventory valuations, including cost using FIFO, the lower of cost or market using FIFO, or weighted average methods. Inventories maintained by the Virginia Equine Center Foundation (Nonmajor Component Unit) are stated at the lower of cost or market using FIFO. Inventories maintained by the Virginia Port Authority (Nonmajor Component Unit) are reported using the moving average cost methodology. The Virginia Outdoors Foundation (Nonmajor Component Unit) maintains inventories using the average cost method and the Virginia Housing Development Authority (Major Component Unit) maintains inventories at the lower of cost or fair value.

**K. Prepaid Items**

Prepaid assets for rent, insurance, and similar items are recognized when purchased and expensed when used.

**L. Interfund Loans Receivable/Payable**

Loans Receivable/Payable represents working capital advances from one fund to another (see Note 8).

**M. Other Assets**

Other Assets include those balances of a miscellaneous nature that are not specifically classified elsewhere (see Note 9).

**N. Capital Assets**

Capital assets of governmental funds are recorded as expenditures at the time of purchase and capitalized in the governmental activities column of the Government-wide Statement of Net Assets. Capital assets of the other funds and component units are capitalized in the fund in which they are utilized. All depreciable capital assets are depreciated on the straight-line basis over their useful lives (see Note 11).

Capital assets are stated at historical cost or, in some instances, estimated historical cost. Donated capital assets are stated at fair market value at the time of donation. The Primary Government capitalizes all equipment that has a cost or value greater than \$50,000 and expected useful life of greater than two years. The Primary Government capitalizes all property, plant, and infrastructure that have a cost or value greater than \$100,000 and an expected useful life of greater than two years. Selected agencies and institutions of higher education utilize a capitalization limit lower or higher than the Primary Government's established thresholds for various reasons. Accordingly, reported capital assets may include some items that cost less than those thresholds. Infrastructure, including highways, bridges, and rights-of-way, is capitalized using the historical approach.

The Primary Government's capitalization policy regarding works of art/historical treasures is that capitalization is encouraged, but not required, for works of art/historical treasures that meet the following conditions:

- The collection is held for public exhibition, education, or research in furtherance of public service, rather than financial gain;
- The collection is protected, kept unencumbered, cared for and preserved; and,
- The collection is subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for the collection.

The Primary Government capitalizes construction-in-progress when project expenditures exceed \$100,000. Interest incurred during construction is

not capitalized in governmental funds. Interest incurred during the construction of proprietary fund assets is included in the capitalized value of the asset. Expenditures are classified as construction-in-progress if:

- (1) they extend the asset life, improve productivity, or improve the quality of service; and
- (2) they fall into the planning, acquisition, construction, improvement, renovation, repair, replacement, relocation or demolition phase of the asset life.

The estimated lives of capital assets are as follows:

	<u>Years</u>
Buildings	15–50
Equipment	2–20
Infrastructure	5–50

Selected institutions of higher education may utilize estimated lives and policies that differ from the above for various reasons.

**O. Accounts Payable**

Accounts payable represent amounts, including salaries and wages, owed for goods and services received prior to year-end. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, accounts payable also include payments for nonexchange transactions that met eligibility requirements prior to year-end (see Note 18).

**P. Unearned and Deferred Revenue**

Unearned revenue represents monies received or revenues accrued but not earned as of June 30, 2005. Deferred revenue represents revenues accrued but not available to finance expenditures of the current fiscal period. The majority of unearned revenue is reported by higher education institutions (Component Unit), where it is primarily composed of revenue for student tuition accrued in advance of the semester and advance payments on grants and contracts. In the General Fund (major), deferred revenue represents receivables that will be collected after August 31, 2005. In the Special Revenue Funds, unearned revenue is composed primarily of Federal grant money received but not spent. In the Enterprise Funds, a majority of unearned revenue represents on-line ticket monies received by the State Lottery (major) for which corresponding drawings have not been held and unearned revenues of Consolidated Laboratory (nonmajor). In the Internal Service Funds, it represents primarily unearned premiums for the Risk Management Fund, prepaid rent and work orders for the Maintenance and Repair Fund, and capital asset transfers from various agencies to the Virginia Information Technologies Agency Internal Service Fund. The unearned revenue related to capital assets will be amortized to income over the life of the assets. Unearned revenues in the other

component units consist primarily of the deferral of fees related to various activities.

#### **Q. Deferred Taxes**

Deferred taxes represent the deferral of income taxes withheld or received for the period January through June 2005. This amount is the estimate to be refunded (overpayments by taxpayers) reduced by the estimate to be received (underpayments from taxpayers) that will be finalized when income tax returns are filed in subsequent years. Individual income tax estimated overpayments total \$558,116,928 and estimated underpayments total \$298,055,396. This results in deferred taxes of \$262,688,416. Corporate income tax estimated overpayments total \$35,103,334 and estimated underpayments total \$52,165,286. When underpayments exceed overpayments, revenue on the fund statements is only recognized to the extent of estimated overpayments. Since underpayments exceed overpayments for corporate income taxes, the deferred tax amount is zero for the fiscal year.

#### **R. Claims Payable**

Claims payable, reported in the proprietary funds of the primary government, represent both health and liability insurance claims payable at June 30, 2005. This includes both actual claims submitted, as well as actuarially determined claims incurred but not reported. Claims relating to the Primary Government's liability insurance programs are reported in the Risk Management – Internal Service Fund, and the Risk Management – Nonmajor Enterprise Fund. Also, health insurance claims are reported in the Health Care – Internal Service Fund and the Local Choice Health Care – Nonmajor Enterprise Fund (see Note 17.A. and 17.B.).

#### **S. Obligations Under Securities Lending Program**

In accordance with GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions*, liabilities resulting from these transactions have been recorded as obligations under security lending transactions.

#### **T. Other Liabilities**

Other liabilities represent amounts owed for various governmental and proprietary activities. Some of these amounts will be paid shortly after fiscal year-end (see Note 19).

Short-term debt results from borrowings from anticipation notes, lines of credit, and similar loans with parties external to the Primary Government. The Primary Government's policy is to disclose activity related to short-term borrowings occurring during the fiscal year. Any short-term debt balances outstanding at June 30 are reported as Other Liabilities. For fiscal year 2005, the Primary Government's agencies did not participate in short-term borrowings with external parties. Higher Education Institutions' Foundations (Component Units) have lines of credit outstanding as of year-

end that amount to approximately \$42.7 million. The Virginia Commonwealth University (Major Component Unit) has short-term debt of \$25 million as of year-end. Also, the University of Virginia (Major Component Unit) reports approximately \$84.9 million of commercial paper as Long-term Liabilities – Due in More than One Year because it was in anticipation of a bond issuance.

#### **U. Long-term Liabilities**

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities or business-type activities column. The governmental fund statements reflect the portion of long-term liabilities that will be paid from expendable resources. The proprietary fund statements and discrete component unit statements reflect total long-term liabilities and distinguish between those portions payable within one year and those payable in future years (see Note 20).

Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bond. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

Expenditures for principal and interest payments for governmental fund general obligation bonds and revenue bonds are recognized in the Debt Service Fund (nonmajor) when due. In these fund statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuance are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures (see Note 20).

#### **V. Reserved Fund Balances**

Reserved fund balances indicate that portion of fund balance that is not available to fund operations or is legally segregated for specific future use. Fund balance reservations are not specifically denoted in instances where the nature of the fund dictates the entire amount is reserved.

#### **W. Unreserved, Designated Fund Balances**

Designations of fund balance, as shown in Note 3, are established to reflect tentative plans for future utilization of current financial resources. It is the policy of the Primary Government to designate the portion of fund balance set aside by the General Assembly through the Appropriation Act to fund tentative but approved future plans. Unexpended appropriations approved by the Governor to be used to fund expenditures of the ensuing fiscal year are also reflected through a designation of fund

balance. It is the policy of the Primary Government to limit such designations in the event that their accumulation and presentation would cause a negative unreserved, undesignated fund balance to occur.

#### **X. Unreserved, Undesignated Fund Balances**

The unreserved, undesignated basis of budgeting fund balance is the amount of fund balance remaining from operations of the current and prior years, net of amounts established as reserved and designated fund balance described in Notes 1.V. and 1.W. above.

#### **Y. Cash Management Improvement Act**

Included in "Due to Other Governments" is the Commonwealth's Cash Management Improvement Act (CMIA) interest liability to the Federal government, which is calculated in accordance with the interest calculation and exchange provisions of the Federal Cash Management Improvement Act of 1990. The Commonwealth's interest liability is subject to review and final confirmation by the Financial Management Service (FMS) of the U.S. Treasury. The payment is to be made on or before March 1, 2006. Payment will be made from a sum sufficient appropriation authorized for this purpose by the Appropriation Act. The CMIA interest rate of exchange is based by law on the annualized average earnings rate of 13-week Treasury Bills.

#### **Z. Interest, Dividends, Rents, and Other Investment Income**

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, all investment income is reported in this line item. Since this amount includes changes in the fair value of investments, the amount reported may be negative. In addition, the amount reported also includes rent payments received on properties owned by the Commonwealth.

#### **AA. Intrafund Eliminations**

Eliminations have been incorporated into the report to eliminate intrafund transactions within the related fund type. These eliminations prevent overstatement of financial activity.

#### **BB. Interfund Activity**

Generally, the effect of interfund activity has been eliminated from the government-wide statements. Exceptions to this rule are 1) activities between funds reported as governmental activities and funds reported as business-type activities and 2) activities between funds that are reported in different functional categories in either the governmental or business-type activities column. Elimination of these activities would distort the direct costs and program revenues for the functions.

In the fund financial statements, transfers represent flows of assets without equivalent flows of assets in

return or a requirement for repayment. In addition, transfers are recorded when a fund receiving revenue provides it to a different fund that expends the resources.

## **2. RESTATEMENT OF BEGINNING BALANCES**

The government-wide beginning balance restatements resulted from the following:

- Governmental Activities have been restated primarily for unamortized premiums and accrued interest payable not recorded in previous years, and the correction of prior year errors regarding the overstatement of capital assets.
- Business-type Activities have been restated due to reporting entity changes and correction of prior year errors. The Division of Legislative Services was reported as a Nonmajor Enterprise Fund in fiscal year 2004, but will be reported as part of Special Revenue Other in fiscal year 2005. Commuter Rail was reported as part of Risk Management (Nonmajor Enterprise Fund) in fiscal year 2004, but is reported as an Agency Fund in fiscal year 2005. The restatement is also due to correction of prior year errors regarding capital assets.
- Component Units have been restated primarily due to the correction of prior year errors related to the understatement of accounts payable and unrecorded capital assets.

The various individual fund amounts have been restated due to the following:

- The General Fund restatement is due to prior year errors related to the overstatement of payables and inventory.
- The Special Revenue Commonwealth Transportation and Special Revenue Federal Funds have been restated due to prior year errors related to expenditures and receivables.
- The Special Revenue Dedicated and Special Revenue Other Funds were restated due to prior year errors related to receivables. The Special Revenue Other Fund was also restated due to a change in methodology for reporting the administration portion of the Child Support Agency Fund. The Virginia Land Conservation Foundation was restated because it is reported as a discrete component unit in fiscal year 2005.
- Enterprise Funds have been restated due to reporting entity changes of the Division of Legislative Services and Risk Management. The Virginia Industries for the Blind restatement is due to the correction of prior year errors regarding capital assets.
- Investment Trust Funds were restated due to prior year errors related to unrecorded cash and cash equivalents.

- The University of Virginia amount has been restated primarily due to the understatement of accounts payable in the prior year.
- Nonmajor Higher Education Institution amounts have been restated for various reasons. Most of the restatement is because of Longwood University's correction of prior year errors in reporting capital asset amounts.
- Nonmajor Component Units have been restated for various reasons. Most of the restatement is because the Virginia Land Conservation Foundation and Virginia Arts Foundation were reported as blended component units in fiscal year 2004, but are reported as discrete component units in fiscal year 2005.
- Agency Funds have been restated due to reporting entity changes. The Child Support Collections Fund was restated due to a change in methodology for reporting the administration portion of the fund which is now reported in the Special Revenue Other Fund. The Optional Life Insurance Fund has been outsourced and is no longer an Agency Fund. The Milk Commission Fund is reported as part of the Consumer Services Fund starting in fiscal year 2005. Commuter Rail, reported as part of Risk Management in prior years, is reported as an Agency Fund beginning in fiscal year 2005.

#### Beginning Balance Restatement

(Dollars in Thousands)

	Balance as of June 30, 2004	Correction of Prior Year Errors	Change in Reporting Entity	Balance June 30, 2004 as restated
<b>Government-wide Activities:</b>				
Primary Government:				
Governmental Activities	\$ 12,552,160	\$ (193,540)	\$ -	\$ 12,358,620
Business-type Activities	184,223	5,246	(15,435)	174,034
Total Primary Government	<u>\$ 12,736,383</u>	<u>\$ (188,294)</u>	<u>\$ (15,435)</u>	<u>\$ 12,532,654</u>
Component Units	<u>\$ 12,692,838</u>	<u>\$ 5,722</u>	<u>\$ 4,752</u>	<u>\$ 12,703,312</u>
<b>Major Governmental Funds:</b>				
General	\$ 446,239	\$ (245)	\$ -	\$ 445,994
Special Revenue Funds:				
Commonwealth Transportation	1,320,629	(10,604)	-	1,310,025
Federal Trust	21,114	1,809	-	22,923
Literary	337,000	-	-	337,000
<b>Nonmajor Governmental Funds:</b>				
Special Revenue Funds:				
Dedicated Special Revenue Fund	200,513	298	-	200,811
Other Special Revenue Fund	352,215	13,926	14,072	380,213
Virginia Land Conservation Foundation Fund	2,168	-	(2,168)	-
Total Special Revenue	<u>554,896</u>	<u>14,224</u>	<u>11,904</u>	<u>581,024</u>
Debt Service Funds:				
Primary Government	74,088	-	-	74,088
Virginia Public Building Authority	1,343	-	-	1,343
Total Debt Service	<u>75,431</u>	<u>-</u>	<u>-</u>	<u>75,431</u>
Capital Project Funds:				
Primary Government	8,324	-	-	8,324
Virginia Public Building Authority	(33,698)	-	-	(33,698)
Total Capital Projects	<u>(25,374)</u>	<u>-</u>	<u>-</u>	<u>(25,374)</u>
Permanent Funds:				
Commonwealth Health Research Fund	27,182	-	-	27,182
Mental Health Endowment Funds	251	-	-	251
Virginia Arts Foundation	298	-	(298)	-
Total Permanent Funds	<u>27,731</u>	<u>-</u>	<u>(298)</u>	<u>27,433</u>
<b>Total Nonmajor Governmental Funds</b>	<u>632,684</u>	<u>14,224</u>	<u>11,606</u>	<u>658,514</u>
<b>Total Governmental Funds</b>	<u>\$ 2,757,666</u>	<u>\$ 5,184</u>	<u>\$ 11,606</u>	<u>\$ 2,774,456</u>

**Beginning Balance Restatement  
Proprietary Funds**

*(Dollars in Thousands)*

	<b>Balance as of June 30, 2004</b>	<b>Correction of Prior Year Errors</b>	<b>Change in Reporting Entity</b>	<b>Balance June 30, 2004 as restated</b>
<b>Major Enterprise Funds:</b>				
State Lottery	\$ (2,309)	\$ -	\$ -	\$ (2,309)
Virginia College Savings Plan	(128,493)	-	-	(128,493)
Pocahontas Parkway	(115,062)	-	-	(115,062)
Unemployment Compensation	371,845	-	-	371,845
<b>Nonmajor Enterprise Funds:</b>				
Department of Alcoholic Beverage Control	(6,740)	(251)	-	(6,991)
Risk Management	21,640	-	(15,429)	6,211
Local Choice Health Care	15,366	-	-	15,366
Virginia Industries for the Blind	6,748	5,497	-	12,245
Consolidated Laboratory	681	-	-	681
eVA Procurement System	(4,309)	-	-	(4,309)
Department of Environmental Quality	7,786	-	-	7,786
Wireless E-911 Service Board	15,285	-	-	15,285
Virginia Information Providers Network	284	-	-	284
Virginia Museum of Fine Arts	917	-	-	917
Science Museum of Virginia	266	-	-	266
Mental Health Local Funds	256	-	-	256
Division of Legislative Services	6	-	(6)	-
Library of Virginia	-	-	-	-
School for the Deaf and Blind - Staunton	1	-	-	1
<b>Total Nonmajor Enterprise Funds</b>	<b>58,187</b>	<b>5,246</b>	<b>(15,435)</b>	<b>47,998</b>
<b>Total Enterprise Funds</b>	<b>\$ 184,168</b>	<b>\$ 5,246</b>	<b>\$ (15,435)</b>	<b>\$ 173,979</b>
<b>Total Internal Service Funds</b>	<b>\$ (116,941)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (116,941)</b>

**Beginning Balance Restatement  
Fiduciary Funds**

*(Dollars in Thousands)*

	<b>Balance as of June 30, 2004</b>	<b>Correction of Prior Year Errors</b>	<b>Balance June 30, 2004 as restated</b>
Private Purpose Funds	\$ 7,682,237	\$ -	\$ 7,682,237
Pension Trust Funds	40,043,807	-	40,043,807
<b>Investment Trust Funds:</b>			
Local Government Investment Pool (LGIP)	2,251,393	401	2,251,794
State Non-Arbitrage Pool (SNAP)	1,308,946	76,962	1,385,908
SNAP Individual Investment Accounts	161,651	-	161,651
<b>Total Investment Trust Funds</b>	<b>3,721,990</b>	<b>77,363</b>	<b>3,799,353</b>
<b>Total Fiduciary Funds</b>	<b>\$ 51,448,034</b>	<b>\$ 77,363</b>	<b>\$ 51,525,397</b>

**Beginning Balance Restatement  
Component Units**

*(Dollars in Thousands)*

	<u>Balance as of June 30, 2004</u>	<u>Correction of Prior Year Errors</u>	<u>Change in Reporting Entity</u>	<u>Balance June 30, 2004 as restated</u>
<b>Major Component Units</b>				
Virginia Housing Development Authority	\$ 1,542,876	\$ -	\$ -	\$ 1,542,876
Virginia Public School Authority	24,773	-	-	24,773
University of Virginia	4,452,949	(16,314)	-	4,436,635
Virginia Polytechnic Institute and State University	1,000,681	-	-	1,000,681
Virginia Commonwealth University	1,073,762	-	-	1,073,762
<b>Nonmajor Component Units</b>				
Virginia Economic Development Partnership	189	-	-	189
Virginia Outdoors Foundation	7,892	-	-	7,892
Virginia Port Authority	342,596	-	-	342,596
Virginia Resources Authority	920,440	-	-	920,440
Virginia Tourism Authority	1,253	-	-	1,253
Virginia Tobacco Settlement Foundation	7,006	-	-	7,006
Tobacco Indemnification and Community Revitalization Commission	83,645	-	-	83,645
Hampton Roads Sanitation District Commission	353,144	-	-	353,144
Virginia Biotechnology Research Park Authority	13,010	(927)	-	12,083
Virginia Small Business Financing Authority	30,114	-	-	30,114
Virginia School for the Deaf and Blind Foundation	2,539	-	-	2,539
Science Museum of Virginia Foundation	11,496	(167)	-	11,329
Virginia Museum of Fine Arts Foundation	165,082	-	-	165,082
A. L. Philpott Manufacturing Extension Partnership	853	-	-	853
Virginia Equine Center Foundation	2,917	-	-	2,917
Certified Nursing Facility Education Initiative	170	-	-	170
Virginia Land Conservation Foundation	-	-	2,168	2,168
Virginia Arts Foundation	-	-	298	298
Library of Virginia Foundation	-	4,515	-	4,515
College of William and Mary	717,602	-	-	717,602
Virginia Military Institute	344,518	-	-	344,518
Virginia State University	86,920	-	-	86,920
Norfolk State University	54,893	-	-	54,893
University of Mary Washington	97,731	-	-	97,731
James Madison University	302,333	-	-	302,333
Radford University	146,314	-	-	146,314
Old Dominion University	315,055	-	-	315,055
George Mason University	317,849	-	-	317,849
Virginia Community College System	505,772	-	-	505,772
Christopher Newport University	106,267	-	-	106,267
Longwood University	114,126	15,815	-	129,941
Southwest Virginia Higher Education Center	10,364	-	-	10,364
Roanoke Higher Education Authority	11,794	2,800	-	14,594
Innovative Technology Authority	21,843	-	-	21,843
Institute of Advanced Learning and Research	-	-	2,286	2,286
Virginia College Building Authority	(497,930)	-	-	(497,930)
<b>Total Nonmajor Component Units</b>	<u>4,597,797</u>	<u>22,036</u>	<u>4,752</u>	<u>4,624,585</u>
<b>Total Component Units</b>	<u>\$ 12,692,838</u>	<u>\$ 5,722</u>	<u>\$ 4,752</u>	<u>\$ 12,703,312</u>

**Beginning Balance Restatement  
Agency Funds**

*(Dollars in Thousands)*

	<b>Balance as of July 1, 2004</b>	<b>Change in Reporting Entity</b>	<b>Balance as of July 1, 2004 as restated</b>
<b>Agency Funds</b>			
Funds for the Collection of Taxes and Fees	\$ 196,730	\$ -	\$ 196,730
Employee Benefits Fund	3,249	-	3,249
Contractor Deposits Fund	25,407	-	25,407
Deposits of Insurance Carriers Fund	397,452	-	397,452
Inmate and Ward Fund	6,745	-	6,745
Child Support Collections Fund	29,584	(21,009)	8,575
Mental Health Patient Trust Fund	2,446	-	2,446
Mental Health Non-patient Trust Fund	23	-	23
Optional Life Insurance Fund	3,419	(3,419)	-
Comptroller's Debt Setoff Fund	960	-	960
Unclaimed Property of Other States	2,157	-	2,157
Legal Settlement Fund	2,014	-	2,014
Consumer Services Fund	570	2	572
Department of State Police Fund	769	-	769
Aviation Fund	167	-	167
Virginia School for the Deaf and Blind Fund	35	-	35
Woodrow Wilson Rehabilitation Center Fund	6	-	6
Dog and Cat Sterilization Fund	2	-	2
Milk Commission Fund	2	(2)	-
Commuter Rail Fund	-	16,126	16,126
Environmental Quality Fund	3,000	-	3,000
<b>Total Agency Funds</b>	<b>\$ 674,737</b>	<b>\$ (8,302)</b>	<b>\$ 666,435</b>

Enterprise Funds have been restated due to reporting entity changes of the Division of Legislative Services and Risk Management.

**Beginning Cash and Cash Equivalents Restatement  
Proprietary Funds**

*(Dollars in Thousands)*

	<u>Balance as of June 30, 2004</u>	<u>Change in Reporting Entity</u>	<u>Balance June 30, 2004 as restated</u>
<b>Major Enterprise Funds:</b>			
State Lottery	\$ 7,697	\$ -	\$ 7,697
Virginia College Savings Plan	98,804	-	98,804
Pocahontas Parkway	5,046	-	5,046
Unemployment Compensation	298,571	-	298,571
<b>Nonmajor Enterprise Funds:</b>			
Department of Alcoholic Beverage Control	598	-	598
Risk Management	19,966	(2,497)	17,469
Local Choice Health Care	18,635	-	18,635
Virginia Industries for the Blind	2,382	-	2,382
Consolidated Laboratory	2,174	-	2,174
eVA Procurement System	717	-	717
Department of Environmental Quality	9,979	-	9,979
Wireless E-911 Service Board	13,561	-	13,561
Virginia Information Providers Network	843	-	843
Virginia Museum of Fine Arts	748	-	748
Science Museum of Virginia	203	-	203
Mental Health Local Funds	364	-	364
Division of Legislative Services	6	(6)	-
Library of Virginia	-	-	-
School for the Deaf and Blind - Staunton	1	-	1
<b>Total Nonmajor Enterprise Funds</b>	<u>70,177</u>	<u>(2,503)</u>	<u>67,674</u>
<b>Total Enterprise Funds</b>	<u>\$ 480,295</u>	<u>\$ (2,503)</u>	<u>\$ 477,792</u>
<b>Total Internal Service Funds</b>	<u>\$ 174,504</u>	<u>\$ -</u>	<u>\$ 174,504</u>

### 3. GENERAL FUND ANALYSIS – BASIS OF BUDGETING

The following schedule represents reservations and designations of General Fund balance on the basis of budgeting presented in the General Fund Preliminary (Unaudited) Annual Report dated August 15, 2005.

**Reservations and Designations of Fund Balance**  
**General Fund, Basis of Budgeting**  
 June 30, 2005

*(Dollars in Thousands)*

Reserved Fund Balance:		
Revenue Stabilization Reserve Fund	\$ 482,259	
Revenue Stabilization Reserve 2004	181,936	
Payroll Reserve for July 1, 2005 Payroll	74,220	
Unexpended Lottery Proceeds	352	
Total Reserved Fund Balance	738,767	
Unreserved Fund Balance:		
Designated:		
Amount Required for Reappropriation of 2004 Unexpended Balances:		
Mandatory Reappropriations	145,445	
Discretionary Reappropriations	19,202	
Capital Outlay	115,876	
Amount Required to Balance Chapter 951, 2005 Acts of Assembly	300,355	
Virginia Water Quality Improvement Fund - Part A	54,450	
Virginia Water Quality Improvement Fund - Part B	2,134	
Natural Disaster Sum Sufficient	26,818	
Accelerated Sales Tax for Transportation Trust Fund	26,204	
Revenue Stabilization Fund Contribution	402,223	
Standards of Quality (SOQ) Replacement 2nd Year	8,869	
Base Realignment and Closure (BRAC) Allocation	25,000	
Total Designated Fund Balance	1,126,576	
Fund Balance, June 30, 2005	\$ 1,865,343	

### 4. REVENUE STABILIZATION FUND

In accordance with Article X, Section 8 of the *Constitution of Virginia*, the amount estimated as required for deposit to the Revenue Stabilization Fund must be appropriated for that purpose by the General Assembly. Management has designated \$402.2 million for deposit into the Fund during fiscal year 2007. This amount designated for deposit is allowed under the provisions of Article X, Section 8 of the *Constitution of Virginia*.

The *Constitution* requires a deposit based on growth in income and retail sales tax revenue and allows revenue growth from increases in tax rates or the repeal of exemptions to be excluded, in whole or part, from the deposit calculation for up to six years. The minimum mandatory deposit would have been \$354.1 million if all revenue increases from tax reform (including those derived from estimates) were excluded from the deposit calculations, and the maximum mandatory deposit would have been \$600.6 million if all tax increases from tax reform were included. The fiscal year 2005 deposit designation of \$402.2 million excludes that impact of

revenue increases resulting from the repeal of the public service corporation exemption (\$29.8 million in revenue) and the sales tax rate increase (\$295.3 million in revenue).

Section 2.2-1829(b) of the *Code of Virginia* requires an additional deposit into the Fund when specific criteria have been met. No designation is required since the specified criteria were not met for fiscal year 2005.

The Revenue Stabilization Fund has principal and interest on deposit of \$482.3 million reserved as a part of General Fund balance. The amount on deposit cannot exceed ten percent of the Commonwealth's average annual tax revenues derived from taxes on income and retail sales for the preceding three fiscal years. The maximum amount allowed is \$977.8 million and \$1.1 billion for fiscal year 2005 and fiscal year 2006, respectively.

## 5. CASH, CASH EQUIVALENTS, AND INVESTMENTS

The Governmental Accounting Standards Board (GASB) issued Statement No. 40, *Deposit and Investment Risk Disclosures*, which modifies previous disclosure requirements related to investment risk, and is effective for reporting periods beginning after June 15, 2004. Required investment risk disclosures address credit risk, including custodial credit risk, concentrations of credit risk, interest rate risk, and foreign currency risk. The Commonwealth implemented this new accounting standard for the fiscal year ended June 30, 2005.

At June 30, 2005, the carrying amount of cash for the primary government was \$2,562,013,719 and the bank balance was \$227,252,983. The carrying amount of cash for the component units was \$1,195,209,818 and the bank balance was \$351,446,938. Cash equivalents are investments with an original maturity of three months or less. Cash and cash equivalents for Foundations (Component Units) totaled \$203,090,115 as of year-end. A portion of this amount and some balances during the year exceeded Federal Deposit Insurance Corporation (FDIC) insurance coverage. Foundation Investments are disclosed at Interest Rate Risk section in this note.

The deposits of the primary government and the component units, excluding Foundations (Component Units), are secured in accordance with the provisions of the Virginia Security for Public Deposits Act, Section 2.2-4400 of the *Code of Virginia*. The Act requires any public depository that receives or holds public deposits to pledge collateral to the Treasury Board to cover public deposits in excess of Federal deposit insurance. The required collateral percentage is determined by the Treasury Board and ranges from 50 percent to 100 percent of public deposits in the case of a bank and 100 percent to 110 percent for a savings institution.

Securities pledged by banks and savings institutions, under the Act, are held by an approved escrow agent for the Treasury Board. In the event a depository bank defaults or becomes insolvent, the Treasury Board first assesses the collateral of the defaulting or insolvent institution and then assesses the collateral pledged by other public depositories on a statutory based ratio to the extent necessary to satisfy the assessment against the defaulting bank. The collateral pledged by all banks is sufficient to cover the uncollateralized public deposits of any single bank. Upon default or insolvency of a savings institution, the Treasury Board assesses the institution the amount of public funds on deposit in excess of FDIC insurance. The State Treasurer liquidates the necessary pledged collateral of the institution to reimburse public depositors to the extent of the institution's deposit liability to them. As a result, these deposits are considered insured.

Certain deposits are held by trustees in accordance with the Trust Subsidiary Act, Section 6.1–32.8 et seq. of the *Code of Virginia*. The Act requires that cash held by trustees while awaiting investment or distribution is not to be used by an affiliate bank of the trustee in the conduct of its business unless the affiliate bank delivers securities to the trust department as collateral that is at

least equal to the fair value of the trust funds held on deposit in excess of amounts insured by the FDIC.

The Commonwealth is authorized, in accordance with the guidelines set forth in Section 2.2-4500 et seq. of the *Code of Virginia*, to invest in the following:

- U.S. Treasury and agency securities
- Corporate debt securities of domestic corporations
- Asset-backed securities
- Mortgage-backed securities
- AAA rated obligations of foreign governments
- Bankers' acceptances and bank notes
- Negotiable certificates of deposit
- Repurchase agreements
- Money market funds

Permitted investments include agency mortgage-backed securities, reported as U.S. Treasury and agency securities, and asset-backed securities, reported as corporate notes, which by definition usually expose the investor to prepayment risk.

Prepayment risk, or the prepayment option granted the borrower, can create uncertainty concerning cash flows, can affect the price of the security causing negative convexity, and can expose the investor to reinvestment risk. Similarly, many agency and corporate securities are callable after some predetermined date at a predetermined price. The call options in regular agency debentures and some corporate securities can be open ended and may significantly impact cash flows, security pricing, and reinvestment risks of these securities.

Certain investments held in trust by the Treasurer of Virginia in accordance with bond indentures and resolutions may have more restrictive investment policies. Investment policies of institutions of higher education (Component Units) are established by the institutions' governing boards.

The Board of Trustees of the Virginia Retirement System (VRS) (Primary Government) has full power to invest and reinvest the trust funds in accordance with Section 51.1–124.30 of the *Code of Virginia*, as amended. This section requires the Board to discharge its duties solely in the interest of the beneficiaries and to invest the assets with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. The Board must also diversify such investments so as to minimize the risk of large losses unless under the circumstances it is clearly prudent not to do so. The VRS does not have investment policies that place specific restrictions on investments related to custodial risk, interest rate risk, credit risk, or foreign currency risk. The VRS investment portfolio is intended to be managed through diversification and prudent judgment, rather than through specific policy restrictions.

The information presented for the external investment pools was obtained from audited financial statements. Copies of the State Non-Arbitrage Program (SNAP) report may be obtained by writing PFM Asset Management LLC, One Keystone Plaza, Suite 300,

North Front & Market Streets, Harrisburg, Pennsylvania 17101-2044. Copies of the Local Government Investment Pool (LGIP) report may be obtained by writing the Department of the Treasury, Post Office Box 1879, Richmond, Virginia 23218. Participation in these pools is voluntary, except for participants who borrow through the Virginia Public School Authority's pooled bond program and must participate in SNAP.

SNAP is an open-end management investment company registered with the Securities Exchange Commission (SEC). LGIP is not SEC-registered; however, it maintains a policy to operate in a manner consistent with SEC Rule 2a7.

**Custodial Risk**

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Commonwealth may not be able to recover the value of its investment or collateral securities that are in the possession of an outside party.

Policies related to credit risk pertaining to the Commonwealth securities lending program are found in the securities lending section of this note.

As of June 30, 2005, the primary government had \$546,523,639 of cash equivalents and investments that were exposed to custodial risk as uninsured and uncollateralized. The VRS had \$462,387,000 of this amount that consisted of various types of debt and equity securities that were held by counterparties' trust departments or agents, but not in the VRS' name. Investments held by broker-dealers under securities loan for U.S. Government and Agency Securities represented \$229,118,000 and U.S. Treasury and Agency Securities represented \$121,582,403 of the total. The remainder was for various types of debt and equity securities. The component units had \$43,304,381 of cash equivalents and investments that were exposed to custodial risk as uninsured and uncollateralized. Repurchase Agreements represented \$25,358,438 of the total and the remainder was for various types of debt and equity securities.

As of June 30, 2005, the investments of the Pension Trust Funds were approximately 65 percent of the primary government investments, and 85 percent of those that were exposed to custodial risk.

**Interest Rate Risk**

Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Commonwealth has elected the Segmented Time Distribution method of disclosure.

The State Treasurer guidelines restrictions limit the following maximum durations for any single security of the following investment types:

<u>Security Type</u>	<u>Maximum Duration</u>
Corporate Security	15 years
Asset-Backed Securities	5 years
Sovereign Government Obligations (Excluding U.S.)	5 years
Negotiable Certificates of Deposit and Negotiable Bank Notes	5 years

The State Treasurer guidelines further describe target durations for the overall General Account portfolio of 1.6 years, with a 2.3 year maximum and a 0.4 year minimum duration.

The VRS manages the risk within the portfolio using the effective duration or option-adjusted methodology. It is widely used in the management of fixed income portfolios in that it quantifies, to a much greater degree, the risk of interest rate changes. The methodology takes into account optionality on bonds and scales the risk of price changes on bonds depending upon the degree of change in rates and the slope of the yield curve.

At June 30, 2005, the Commonwealth had the following investments and maturities:

**Primary Government Investments**

*(Dollars in Thousands)*

<u>Investment Type</u>	Fair Value	Investment Maturities (in years)			
		Less Than 1	1-5	6-10	More Than 10
<u>Debt Securities</u>					
U. S. Treasury and Agency Securities	\$ 4,427,049	\$ 2,242,114	\$ 1,267,445	\$ 335,842	\$ 581,648
Corporate Notes	1,223,530	955,717	256,882	6,128	4,803
Corporate Bonds	2,760,577	484,272	717,448	902,329	656,528
Commercial Paper	3,798,172	3,798,172	-	-	-
Negotiable Certificates of Deposit	1,474,685	1,437,775	36,910	-	-
Non-negotiable Certificates of Deposit	73,132	73,132	-	-	-
Repurchase Agreements	3,975,266	3,970,817	-	-	4,449
Municipal Securities	84,880	8,549	27,876	20,478	27,977
Asset Backed Securities	995,339	41,142	421,420	320,779	211,998
Agency Mortgage Backed	2,637,750	18,225	188,077	218,862	2,212,586
Mutual and Money Market Funds (Include SNAP)	1,967,077	1,967,077	-	-	-
The Boston Company Pooled Employee Trust Fund	1,274,734	1,274,734	-	-	-
Guaranteed Investment Contracts	177,989	2,986	175,003	-	-
Fixed Income and Commingled Funds	1,631,369	237,910	739,049	396,184	258,226
Deposits with the U.S. Treasury for Unemployment Compensation	478,665	478,665	-	-	-
Investments held by broker-dealers under securities loans					
U. S. Government and Agency Securities	2,477,507	71,077	1,263,265	437,186	705,979
Corporate Notes	117,336	117,336	-	-	-
Corporate Bonds	380,246	104,025	59,997	111,997	104,227
Other	802,584	252,712	19,162	20,447	510,263
<b>Total</b>	<b>\$ 30,757,887</b>	<b>\$ 17,536,437</b>	<b>\$ 5,172,534</b>	<b>\$ 2,770,232</b>	<b>\$ 5,278,684</b>

**Component Unit Investments**

*(Dollars in Thousands)*

<u>Investment Type</u>	Fair Value	Investment Maturities (in years)			
		Less Than 1	1-5	6-10	More Than 10
<u>Debt Securities</u>					
U. S. Treasury and Agency Securities	\$ 489,450	\$ 326,044	\$ 147,758	\$ 3,939	\$ 11,709
Corporate Notes	151,848	87,917	55,765	7,358	808
Corporate Bonds	15,678	2,645	8,022	1,405	3,606
Commercial Paper	118,793	118,793	-	-	-
Banker's Acceptance	3,593	3,593	-	-	-
Negotiable Certificates of Deposit	1,608	1,580	28	-	-
Non-negotiable Certificates of Deposit	8,350	8,190	160	-	-
Repurchase Agreements	454,490	443,123	6,874	-	4,493
Municipal Securities	2,463,687	-	28,979	63	2,434,645
Asset Backed Securities	254,377	969	22,784	40,296	190,328
Agency Mortgage Backed	249,802	80,192	43,738	11,076	114,796
Mutual and Money Market Funds (Include SNAP)	841,247	785,065	27,036	29,146	-
Guaranteed Investment Contracts	627,475	342,198	-	1,515	283,762
Investments held by broker-dealers under securities loans					
U. S. Government and Agency Securities	7,992	3,460	3,445	-	1,087
Other	388,901	347,434	-	564	40,903
<b>Total</b>	<b>\$ 6,077,291</b>	<b>\$ 2,551,203</b>	<b>\$ 344,589</b>	<b>\$ 95,362</b>	<b>\$ 3,086,137</b>

## Foundation Investments

(Dollars in Thousands)

<u>Investment Type</u>	<u>Fair Value</u>
U.S. Treasury and Agency Securities	\$ 341,225
Common & Preferred Stocks	1,023,071
Corporate Notes	31,992
Corporate Bonds	125,670
Commercial Paper	8,250
Negotiable Certificates of Deposit	2,027
Municipal Securities	17,647
Asset Backed Securities	138,671
Agency Mortgage Backed	10,107
Mutual and Money Market Funds	1,397,677
Bankers' Acceptance	497
Real Estate	109,152
Index Funds	98,269
Hedge Funds	1,753,039
Others	500,096
Investments in Local Government Investment Pool	5,800
<b>Total</b>	<b>\$ 5,563,190</b>

Note: Foundations represent FASB reporting entities defined in Note 1.B. A portion of these amounts are reported at cost rather than fair value because fair value was not available or readily determinable.

### Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The State Treasurer of the Commonwealth places emphasis on securities of high credit quality and marketability. At the time of purchase, the following limitations are in place:

- Bankers acceptances: P-1, Moody's and A-1, S&P
- Negotiable CDs and bank notes:
  - maturities of one year or less: P-1, Moody's and A-1, S&P
  - maturities over one year: Aa, Moody's and AA, S&P
- Commercial paper: P-1, Moody's; A-1, S&P
- Corporate Notes and Bonds and Busted Convertibles: A or better by two nationally recognized rating agencies, one of whom must be Moody's or S&P
- Taxable Municipal Bonds: A or better by two nationally recognized rating agencies, one of whom must be Moody's or S&P
- Asset-backed securities: AAA or better by two nationally recognized rating agencies, one of whom must be Moody's or S&P
- Dollar denominated obligations of sovereign governments: Aaa, Moody's and AAA, S&P
- Commercial Mortgage-Backed Securities (CMBS), Collateralized Mortgage Obligations (CMOs), and Planned Amortization Classes (PACs): AAA or

better by two nationally recognized rating agencies, one of whom must be Moody's or S&P

The following tables present the credit ratings for the majority of the investments of the primary government and component units as of June 30, 2005. The ratings presented below are using Standard & Poor's (S&P) and Moody's Investors Service (Moody's) rating scales. Within the primary government, the investments presented in the table represented 88.60 percent of the total debt securities, 14.39 percent of which were invested in obligations guaranteed by the U.S. Government. Within the component units, the investments presented in the table represented 95.98 percent of the total debt securities, 40.06 percent of which were invested in Municipal Securities.

Credit risk for derivative instruments held by the Commonwealth results from counterparty risk assumed by the Commonwealth. This is essentially the risk that the borrower will be unable to meet its obligation. Information regarding the Commonwealth's credit risk related to derivatives is found in the Derivative Financial Instruments note.

Policies related to credit risk pertaining to the Commonwealth's securities lending program are found in the Securities Lending note.

**Credit Rating - Primary Government**  
(Dollars in Thousands)

<u>Investment</u>	<u>Amount</u>	<u>Rating</u>	<u>Percent of Portfolio</u>
U. S. Treasury and Agency Securities	\$ 4,426,162	Unrated	14.39%
Agency Mortgage Backed Investments held by broker-dealers under securities loans (U.S. Government and Agency Securities)	2,618,355	AAA	8.51%
Commercial Paper	2,289,493	AAA	7.44%
Commercial Paper	1,899,197	Unrated	6.17%
Commercial Paper	1,898,975	A-1	6.17%
Mutual and Money Market Funds (Include SNAP)	1,813,809	AAA	5.90%
Repurchase Agreements	1,546,358	Unrated	5.03%
Negotiable Certificates of Deposit	1,474,685	Unrated	4.79%
Repurchase Agreements	1,326,100	AAA	4.31%
The Boston Company Pooled Employee Trust Fund	1,274,734	AA	4.14%
Repurchase Agreements	1,068,688	A-1	3.47%
Asset Backed Securities	929,219	AAA	3.02%
Corporate Bonds	622,614	A	2.02%
Fixed Income and Commingled Funds	570,201	BBB	1.85%
Corporate Bonds	531,029	BBB	1.73%
Deposits with the U.S. Treasury for Unemployment Compensation	478,665	Unrated	1.56%
Fixed Income and Commingled Funds	474,596	A	1.54%
Corporate Bonds	457,805	B	1.49%
Other	456,378	AAA	1.48%
Corporate Bonds	407,819	BB	1.33%
Corporate Notes	367,606	A-1	1.20%
Fixed Income and Commingled Funds	319,928	Aaa	1.04%

**Credit Rating - Component Units**  
(Dollars in Thousands)

<u>Investment</u>	<u>Amount</u>	<u>Rating</u>	<u>Percent of Portfolio</u>
Municipal Securities	\$ 2,434,367	Unrated	40.06%
Mutual and Money Market Funds (Include SNAP)	751,955	AAA	12.37%
Guaranteed Investment Contracts	627,475	Unrated	10.32%
U. S. Treasury and Agency Securities	489,450	Unrated	8.05%
Repurchase Agreements	449,997	Unrated	7.40%
Other	382,478	Unrated	6.29%
Asset Backed Securities	252,908	Aaa	4.16%
Agency Mortgage Backed	149,796	Aaa	2.46%
Mutual and Money Market Funds (Include SNAP)	85,103	Unrated	1.40%
Corporate Notes	76,273	AAA	1.26%
Agency Mortgage Backed	71,567	Unrated	1.18%
Commercial Paper	61,836	A-1	1.02%

## Concentration of Credit Risk

Concentration of credit risk is related to the risk of loss that may be attributed to the magnitude of a government's investment in a single issuer.

It is the State Treasurer's policy that each portfolio will be diversified with no more than 5 percent of the value of the fund invested in the securities of any single issuer. This limitation shall not apply to the U.S. Government, or Agency thereof, or U.S. Government sponsored corporation securities and fully insured and/or collateralized certificates of deposit.

The VRS investment guidelines for each specific portfolio also limit investments in any corporate entity to no more than 5 percent of the market value of the account for both the internally and externally managed portfolios. There is no concentration of investments in any one organization that represents 5 percent or more of plan net assets available for benefits.

## Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. All investments exposed to foreign currency risk were part of the VRS portfolio at June 30, 2005.

The VRS' currency risk exposures, or exchange rate risk, primarily exists in the international and global equity investment holdings. From time to time, the VRS' external managers may hedge their portfolios' foreign currency exposures with currency forward contracts. This will depend upon their views about a specific foreign currency relative to the U.S. dollar. The VRS' exposure to foreign currency risk is highlighted in the table below.

Currency Exposures by Asset Class

(Dollars in Thousands)

Currency	Cash & Cash Equivalents	Common & Preferred Stocks	Equity Index & Pooled Funds	Corporate Bonds	Total
Euro Currency unit	\$ 17,908	\$ 1,153,194	\$ 1,358,687	\$ 59,889	\$ 2,589,678
British Pound Sterling	126,370	604,399	1,011,566	-	1,742,335
Japanese Yen	12,328	732,032	884,572	12,219	1,641,151
Swiss Franc	3,127	173,889	238,480	-	415,496
Canadian Dollar	7,274	144,387	168,333	3,698	323,692
Australian Dollar	(1,257)	313,968	1,037	6,575	320,323
Hong Kong Dollar	(3,095)	156,035	112,900	-	265,840
South Korean Won	-	242,959	-	-	242,959
New Taiwan Dollar	5,183	215,152	6,090	-	226,425
Swedish Krona	4,193	73,949	85,191	-	163,333
Norwegian Krone	2,882	101,883	42,997	-	147,762
South African Comm Rand	4,088	86,972	5,938	-	96,998
Singapore Dollar	4,845	38,081	44,496	-	87,422
Indian Rupee	1,091	53,393	12,513	-	66,997
New Turkish Lira	271	62,021	-	-	62,292
Mexican New Peso	265	30,106	30,498	-	60,869
Malaysian Ringgit	711	41,381	4,883	-	46,975
Brazil Real	890	9,305	35,138	-	45,333
Danish Krone	2	10,269	34,678	-	44,949
Polish Zloty	39	25,277	4,930	-	30,246
Egyptian Pound	116	16,362	13,754	-	30,232
Thailand Baht	171	23,248	5,636	-	29,055
Indonesian Rupian	-	19,607	7,206	-	26,813
Russian Rubel (New)	-	1,257	15,237	-	16,494
Hungarian Forint	293	14,944	1,241	-	16,478
Philippines Peso	146	11,358	4,702	-	16,206
Israeli Shekel	858	11,321	1,192	-	13,371
New Zealand Dollar	2	2,400	9,810	-	12,212
Argentina Peso	-	-	7,714	-	7,714
Turkish Lira	7,189	(295)	295	-	7,189
Colombian Peso	525	3,291	220	-	4,036
Chilean Peso	-	-	1,474	-	1,474
Czech Koruna	35	1,428	10	-	1,473
Chinese Yuan Renminbi	-	1	950	-	951
Pakistan Rupee	-	455	-	-	455
German Mark	-	-	54	-	54
Peruvian Nuevo Sol	-	15	-	-	15
Slovak Koruna	-	-	(202)	-	(202)
<b>Total</b>	<b>\$ 196,450</b>	<b>\$ 4,374,044</b>	<b>\$ 4,152,220</b>	<b>\$ 82,381</b>	<b>\$ 8,805,095</b>

## Securities Lending

The State Treasury's securities lending program is managed by its Master Custodian, JP Morgan Chase and Company, under a contract dated December 1, 2000. The enabling legislation for the securities lending program is Section 2.2-4506 of Chapter 45 Investment of Public Funds of the *Code of Virginia*, as amended. No violations of legal or contractual provisions were noted during the year. The general account participated in the securities lending program for the entire year.

All securities lending loans are on an open-ended or one-day basis and may be terminated by Treasury with a 24-hour notice. Per the contract with JP Morgan Global Securities Lending, all pledged cash and other collateral attributable to loans made on the Commonwealth's behalf shall be maintained by the Master Custodian Bank, and Treasury cannot pledge or sell such collateral absent a default.

The State Treasury's contract with JP Morgan Global Securities Lending provides for loss indemnification against borrower default as defined in the applicable Master Securities Lending Agreement. Additionally, JP Morgan Chase is liable for any losses experienced from reinvestment of cash collateral in investments not authorized by the provisions of the investment guidelines for the Commonwealth of Virginia agreed upon by both parties and made a part of the Securities Lending Agreement. There were no losses resulting from default during the reporting period, or recoveries of prior period losses during this reporting period.

When securities are loaned, the collateral received is at least 102 percent of fair value of the securities loaned and must be maintained at 100 percent or greater. There are no stated restrictions on the amount of securities that may be loaned, but the basic composition of the general account portfolio effectively caps the maximum percentage of the portfolio that may be loaned. During the past fiscal year, approximately 35 percent of the general account securities were on loan.

During the past year, a combination of U.S. Treasury, Agency, Agency mortgage and corporate securities have been loaned, with the majority of the loaned securities being U.S. Government securities. Collateral received included a combination of cash and non-cash securities, with the non-cash collateral being U.S. Government securities.

Securities loaned for the general account as of June 30, 2005, had a carrying value of \$3,243,515,438 and a fair value of \$3,158,189,560. The fair value of the collateral received was \$3,209,451,980 providing for coverage of 101.6 percent. As a result, the State Treasury assumes no credit risk.

Current cash investment guidelines allow for a maximum weighted-average portfolio maturity of 120 days. At June 30, 2005, the open portion of the cash reinvestment portfolio had a weighted average maturity of 42 days. Treasury's current cash reinvestment guidelines allow for investment in Government securities, AAA rated sovereign governments, commercial paper and corporate notes, negotiable

certificates of deposit, certificates of deposit and time-deposits collateralized under the Virginia Security for Public Deposits Act, bankers' acceptances, bank notes, repurchase agreements collateralized by U.S. Treasury and Agency issues, and registered money market funds. At June 30, 2005, cash reinvestments were as follows: \$1,092 million in repurchase agreements and cash, \$256 million in floating rate corporate notes, \$70 million in commercial paper, and \$40 million in negotiable certificates of deposit. Non-cash collateral value at June 30, 2005, was approximately \$1,752 million in U.S. Government securities.

Under authorization of the Board, the VRS lends its fixed income and equity securities to various broker-dealers on a temporary basis. This program is administered through an agreement with the VRS' custodial agent bank. All security loan agreements are collateralized by cash, securities, or irrevocable letter of credit issued by major banks, and have a market value equal to at least 102 percent of the market value for domestic securities and 105 percent for international securities. Securities received as collateral cannot be pledged or sold by the VRS unless the borrower defaults. Contracts require the lending agents to indemnify the VRS if the borrowers fail to return the securities lent and related distributions, and if the collateral is inadequate to replace the securities lent. All securities loans can be terminated on demand by either the VRS or the borrowers. The majority of loans are open loans – meaning the rebate is set daily. This results in a maturity of one or two days on average, although securities are often on loan for longer periods. The maturity of loans generally does not match the maturity of collateral investments, which averages 62 days. At year-end, the VRS has no credit risk exposure to borrowers because the amounts it owes the borrowers exceed the amounts the borrowers owe it. The market value of securities on loan at June 30, 2005 was \$4,401,317,000. The June 30, 2005 balances were composed of U.S. Government and agency securities of \$2,440,464,000, corporate and other bonds of \$296,354,000 and common and preferred stocks of \$1,664,499,000.

The value of collateral (cash and non-cash) at June 30, 2005 was \$4,573,872,000.

Securities on loan are included with investments on the statement of net assets. The invested cash collateral is included in the statement of net assets as an asset and corresponding liability.

As authorized by Section 2.2-4506 of the *Code of Virginia*, the Virginia Lottery, through its master custodian, JP Morgan Chase Bank, New York, N. Y., N. A., lends securities to various security brokers and lenders on a temporary basis for a fee. Up to 100 percent of the securities may be available for loan. All security loan agreements are collateralized at loan inception at 102 percent of market value by cash or U.S. Government obligations and adjusted to market daily to cover fair value fluctuations. As a result management believes there is no assumed credit risk.

The Virginia Lottery does not have the ability to use cash collateral or to pledge or sell collateral securities

absent borrower default. The Lottery's contract with JP Morgan Chase Bank provides for loss indemnification against borrower default as a result of bankruptcy, insolvency, reorganization, liquidation, receivership, or similar event. There were no losses resulting from default during the reporting period, or recoveries of prior period losses during this reporting period. At June 30, 2005, the fair value of investment account securities on loan was \$326,662,712 secured by \$330,703,032 in cash deposits, and \$62,857,840 secured by \$64,114,996 in market value securities that cannot be pledged or loaned.

### **Derivative Financial Instruments**

Derivative instruments are financial contracts whose values depend on the values of one or more underlying assets, reference rates, or financial indexes. They include futures, forwards, options, or swap contracts. Some traditional securities, such as structured notes, can have derivative-like characteristics. In this case, the return may be linked to one or more indexes and asset-backed securities such as collateralized mortgage obligations (CMO), which are sensitive to changes in interest rates and prepayments. Futures, forwards, options, and swaps are generally not recorded on the financial statements, whereas structured notes and asset-backed investments generally are recorded.

The VRS is a party, both directly and indirectly, to various derivative financial investments that may or may not appear on the financial statements that are used in the normal course of business to enhance returns on investments and manage risk exposure to changes in value resulting from fluctuations in market conditions. These investments may involve, to varying degrees, elements of credit and market risk in excess of amounts recognized on the financial statements. Credit risk is the possibility that loss may occur from failure of a counterparty to perform according to the terms of the contract. Market risk arises from adverse changes in market prices, interest rates and foreign exchange rates that may result in a decrease in the market value of a financial investment or an increase in its funding cost, or both.

In addition to exposure from directly held derivative financial instruments, the VRS may have indirect exposure to risk through its ownership interests in commingled investment funds that use, hold, or write derivative financial instruments. Indirect exposure may also arise from stock lending programs in which the commingled funds participate. Such programs usually reinvest a portion of their cash collateral holdings in derivative instruments. The VRS' pro rata share of the contractual or notional amounts of outstanding derivative transactions in commingled investment funds and their related security lending programs approximated \$961,708,000 at June 30, 2005.

The Virginia Housing Development Authority (Authority) (major) manages its interest risk on single and multi-family loan commitments through short sales of investment securities. These transactions meet the requirements for hedge accounting as all hedged items are specifically identified, probable of occurring, and highly correlated to the hedging instrument. The gain or

loss from hedging transactions is recorded as an unamortized premium or discount and recognized as an adjustment to yield over the remaining life of the loan. The Authority periodically assesses correlation in order to determine the ongoing appropriateness of hedge accounting. During the year ended June 30, 2005, the Authority experienced a net loss of \$2,142,074 from hedging transactions settled during the year. At June 30, 2005, \$12,316,968 of short sales was outstanding which had an unrealized loss of \$102,610. The Authority's policy is to make adjustments to interest rates of loans related to such hedging transactions to reflect the losses or gains on such hedging transactions.

The University of Virginia (major) from time to time may use, through its investments and through investments in pooled funds, a variety of derivative securities including futures, options, and forward foreign currency contracts. These financial instruments are used to modify market risk exposure. Futures contracts and options on futures contracts are traded on organized exchanges and require collateral or margin in the form of cash or marketable securities. The net change in the futures contract value, if any, is settled with a cash transaction on a daily basis. Holders of futures contracts look to the exchange for performance under the contract and not the entity holding the offsetting futures position. Accordingly, the amount of risk due to non-performance of counterparties to the futures contracts is minimal. Foreign exchange contracts are used to protect the University's portfolio against fluctuations in the values of foreign currencies. The credit risk of forward currency contracts traded over-the-counter lies with the counterparty. Asset swap contracts are privately negotiated agreements between two participants to exchange the return stream derived from their assets to each other without exchanging underlying assets. The University uses asset swaps to gain exposure to certain market sectors in lieu of direct investment. The credit risk lies with the intermediary who arranges the asset swap. The University had no direct exposure to derivative instruments at June 30, 2005.

### **Forward, Futures, and Options Contracts**

Forward contracts are contracts to purchase or sell, and futures contracts are contracts to deliver or receive financial instruments, foreign currencies or commodities at a specified future date and at a specified price or yield. Futures contracts are traded on organized exchanges (exchange traded) and require initial margin (collateral) in the form of cash or marketable securities. The net change in the futures contract value is settled daily in cash with the exchanges. Holders of futures contracts look to the exchange for performance under the contract and not to the entity holding the offsetting futures position. Accordingly, the amount at risk posed by nonperformance of counterparties to futures contracts is minimal. In contrast, forward contracts traded over-the-counter are generally negotiated between two counterparties. They are subject to credit risks resulting from nonperformance of one of the counterparties and to market risks resulting from adverse fluctuations in market prices, interest rates, and foreign exchange rates.

Options may be either exchange traded or negotiated directly between two counterparties over-the-counter. Options grant the holder the right, but not the obligation, to purchase or sell a financial instrument at a specified price and within a specified period of time from the 'writer' of the option. As a purchaser of options, the VRS typically pays a premium at the outset. The premium is reflected as an asset on the financial statements. The VRS then retains the right but not the obligation to exercise the option and purchase the underlying financial instrument. Should the option not be exercised, it expires worthless and the premium is recorded as a loss. A writer of options assumes the obligation to deliver or receive the underlying financial instrument on exercise of the option. Certain option contracts may involve cash settlements based on specified indexes such as stock indexes. As a writer of options, the VRS receives a premium at the outset. The premium is reflected as a liability on the financial statements and the VRS bears the risk of an unfavorable change in the price of the financial instrument underlying the option.

Forward, futures, and options contracts provide the VRS with the opportunity to build passive benchmark positions, manage portfolio duration in relation to various benchmarks, adjust portfolio yield curve exposure, and gain market exposure to various indexes in a more efficient way and at lower transaction costs. Credit risks depend on whether the contracts are exchange traded or are exercised over-the-counter. Market risks arise from adverse changes in market prices, interest rates, and foreign exchange rates. At June 30, 2005, the VRS had purchased S & P, Russell Index Treasury Bonds and notes and global indices futures and options with a notional value of \$3,997,496,000 and sold Treasury bonds and notes global indices futures and options with a notional value of \$1,149,667,000. At June 30, 2005, the VRS had pledged as collateral U.S. Treasury and U.S. Government Agency securities with a total market value of \$177,992,000 as the margin requirement for futures contracts.

In addition to unsettled purchases and sales, accounts receivable and accounts payable for security transactions at June 30, 2005, included receivables for deposits with brokers for securities sold short of \$1,248,041,000 and payables for securities sold short and not covered with market values of \$1,353,204,000.

### **Asset-Backed Securities**

Among the instruments with derivative-like characteristics that the VRS invests in and that appear on the financial statements are various asset-backed securities such as collateralized mortgage obligations (CMO), principal-only strips (PO), and interest-only strips (IO). These instruments are used primarily to enhance returns by taking advantage of opportunities available in this sector of the securities markets. CMO securities are bonds collateralized by mortgage-backed securities and issued in several tranches that represent a reallocation of the underlying mortgage-backed securities cash flows. Both PO and IO securities are created by splitting the asset-backed securities into

principal-only and interest-only portions. At June 30, 2005, the VRS held CMO securities with a fair market value of \$442,404,000, and IO and PO securities with a fair market value of \$2,188,000 and ABS with a market value of \$531,264,000.

The credit risks on the various asset-backed securities in which the VRS invests are usually very low. Many of the securities held by the VRS are issued by quasi-U.S. governmental agencies. Others are issued by organizations with AAA or AA credit ratings. The market risk of these securities depends on changes in interest rates and the level of the underlying prepayments, i.e., when the mortgagors repay the underlying principal and interest.

### **Foreign Exchange Contracts**

Foreign exchange contracts include forward, futures, and options contracts. They involve either the exchange of specific amounts of two currencies or the delivery of a fixed amount of a currency at a future date and specified exchange rate. Forward and futures contracts settle three or more business days from the contract date. Forward contracts are negotiated over-the-counter between two counterparties, while futures contracts are exchange traded. Foreign currency options, which are either negotiated between two counterparties or are exchanged traded, grant the buyer the right, but not the obligation, to purchase or sell at a specified price, a stated amount of an underlying currency at a future date. At June 30, 2005, the VRS had sold foreign currency contracts with a notional value of \$7,237,509,000 and had purchased foreign currency contracts with a notional value of \$7,222,991,000.

Foreign exchange contracts are used by the VRS to effect settlements and to protect the base currency (\$US) value of portfolio assets denominated in foreign currencies against fluctuations in the exchange rates of those currencies. The credit risk of currency contracts that are exchange traded lies with the clearinghouse of the exchange where the contracts are traded. The credit risk of currency contracts traded over-the-counter lies with the counterparty, and exposure is usually equal to the unrealized profit on in-the-money contracts. The market risk in foreign currency contracts is related to adverse movements in currency exchange rates.

### **Swap Agreements**

Swaps are negotiated contracts between two counter parties for the exchange of payments at certain intervals over a predetermined time frame. The payments are based on a notional principal amount and calculated using either fixed or floating interest rates or total returns from certain instruments or indices. During fiscal year 2005, the VRS entered into interest rate and total return swaps with a total notional value of \$684,638,000. Swaps are used to manage risk and enhance returns. To reduce the risk of counter party non-performance, the VRS generally requires collateral on any material gains from these transactions.

## 6. RECEIVABLES

The following schedule details the accounts, loans, taxes, and other receivables presented in the major funds, aggregated nonmajor funds by type, internal service funds, fiduciary funds, major component units, and aggregated nonmajor component units, as of June 30, 2005:

	<u>Accounts Receivable</u>	<u>Loans Receivable</u>	<u>Taxes Receivable</u>	<u>Other Receivables</u>	<u>Allowance for Doubtful Accounts</u>	<u>Net Accounts Receivable</u>	<u>Amounts to be Collected Greater than One Year</u>
<b>Primary Government:</b>							
General	\$ 497,020	\$ -	\$ 667,196	\$ 11,085	\$ (306,967)	\$ 868,334	\$ 18,203
Major Special Revenue Funds:							
Commonwealth Transportation	95,702	57,972	105,017	-	(3,254)	255,437	58,263
Federal Trust	408,787	53	-	-	(8,267)	400,573	1
Literary	19,031	380,539	-	-	-	399,570	348,118
Nonmajor Governmental Funds	108,007	4	224	233	(34,277)	74,191	706
Major Enterprise Funds:							
State Lottery	46,283	-	-	-	-	46,283	-
Virginia College Savings Plan (2)	2,611	-	-	306,740	-	309,351	233,883
Pocahontas Parkway	-	-	-	777	-	777	-
Unemployment Compensation	131,536	-	-	-	(23,410)	108,126	-
Nonmajor Enterprise Funds	24,099	-	2,320	-	(63)	26,356	-
Internal Service Funds	20,074	-	-	96	(15)	20,155	-
Private Purpose	3	-	-	646	-	649	-
Pension Trust (2)	128,990	-	-	2,478,287	-	2,607,277	-
Investment Trust Funds	-	-	-	7,984	-	7,984	-
Agency Funds	275	-	57,702	-	-	57,977	1
<b>Total Primary Government (1)</b>	<u>\$ 1,482,418</u>	<u>\$ 438,568</u>	<u>\$ 832,459</u>	<u>\$ 2,805,848</u>	<u>\$ (376,253)</u>	<u>\$ 5,183,040</u>	<u>\$ 659,175</u>
<b>Discrete Component Units:</b>							
Virginia Housing Development Authority	\$ -	\$ 121,468	\$ -	\$ 2,058	\$ -	\$ 123,526	\$ 118,540
Virginia Public School Authority	-	-	-	53,281	-	53,281	53,280
University of Virginia	307,765	21,181	-	49,151	(173,736)	204,361	74,075
Virginia Polytechnic Institute and State University	39,875	15,103	-	19,960	(2,041)	72,897	17,944
Virginia Commonwealth University	341,659	23,331	-	32,415	(250,458)	146,947	29,068
Nonmajor Component Units	116,445	1,803,027	3,956	105,959	(7,605)	2,021,782	1,785,129
<b>Total Component Units</b>	<u>\$ 805,744</u>	<u>\$ 1,984,110</u>	<u>\$ 3,956</u>	<u>\$ 262,824</u>	<u>\$ (433,840)</u>	<u>\$ 2,622,794</u>	<u>\$ 2,078,036</u>

Note (1): Fiduciary net receivables in the amount of \$2,673,887 (dollars in thousands) are not included in the Government-wide Statement of Net Assets.

Note (2): The Other Receivables amount for Pension Trust includes deposits for pending security transactions and the Other Receivables amount for Virginia College Savings Plan represents tuition contributions receivable.

## 7. CONTRIBUTIONS RECEIVABLE, NET

The following schedule details the contributions receivable for Foundations<sup>(1)</sup> included with the major component units, and aggregated nonmajor component units, as of June 30, 2005:

(Dollars in Thousands)

	<u>Due in Less Than One Year</u>	<u>Due Between One and Five Years</u>	<u>Due in More Than Five Years</u>	<u>Subtotal</u>	<u>Present Value Discount (2)</u>	<u>Allowance for Doubtful Accounts</u>	<u>Contributions Receivable, Net</u>
<b>Discrete Component Units:</b>							
University of Virginia	\$ 36,620	\$ 53,301	\$ 12,627	\$ 102,548	\$ (8,665)	\$ (8,812)	\$ 85,071
Virginia Polytechnic Institute & State University	16,705	21,252	5,267	43,224	(3,067)	(1,669)	38,488
Virginia Commonwealth University	10,610	19,565	4,134	34,309	(2,774)	(866)	30,669
Nonmajor Component Units	37,699	86,721	20,065	144,485	(19,802)	(9,393)	115,290
<b>Total Component Units</b>	<u>\$ 101,634</u>	<u>\$ 180,839</u>	<u>\$ 42,093</u>	<u>\$ 324,566</u>	<u>\$ (34,308)</u>	<u>\$ (20,740)</u>	<u>\$ 269,518</u>

Note (1): Foundations represent FASB reporting entities defined in Note 1.B.

Note (2): The discount rate used to determine present value ranges from 1.13 percent to 10.0 percent.

## 8. INTERFUND ASSETS/LIABILITIES

### Due from/to Other Funds

Due from Other Funds are amounts to be received from one fund by another fund for goods sold or services rendered. Due to Other Funds are amounts owed by one fund to another fund for goods purchased or services obtained.

Included in the category Due from Other Funds are "Due from Other Funds and Primary Government" and "Due from Component Units." Included in the category Due to Other Funds are "Due to Other Funds and Primary Government" and "Due to Component Units." The following schedule shows the Due from/to Other Funds as of June 30, 2005.

**Schedule of Due from/to Other Funds**

June 30, 2005

*(Dollars in Thousands)*

Due From	Amount	Due To	Amount
<b>Primary Government</b>		<b>Primary Government</b>	
General Fund	\$ 8,128	Major Enterprise Funds:	
		State Lottery	\$ 21
		Nonmajor Enterprise Funds	8,107
Major Special Revenue Funds:		General Fund	26,204
Commonwealth Transportation	28,603	Nonmajor Enterprise Funds	2,399
Federal Trust	10,289	General Fund	2,083
		Nonmajor Governmental Funds	8,206
Nonmajor Governmental Funds	7,545	Major Special Revenue Funds:	
		Commonwealth Transportation	7,233
		Nonmajor Governmental Funds	27
		Major Enterprise Funds:	
		Unemployment Compensation	285
Major Enterprise Funds:		General Fund	225
Unemployment Compensation	459	Major Special Revenue Funds:	
		Commonwealth Transportation	42
		Federal Trust	97
		Nonmajor Governmental Funds	55
		Major Enterprise Funds:	
		State Lottery	30
		Nonmajor Enterprise Funds	10
Internal Service Funds	39,648	General Fund	18,294
		Major Special Revenue Funds:	
		Commonwealth Transportation	8,146
		Federal Trust	6,938
		Nonmajor Governmental Funds	4,853
		Major Enterprise Funds:	
		State Lottery	149
		Nonmajor Enterprise Funds	801
		Internal Service Funds	467
Pension Trust	15,465	Pension Trust	15,465
<b>Total Primary Government</b>	<u>110,137</u>		<u>110,137</u>

*Continued on next page*

Note: The above schedule does not include \$21.1 million due to the Commonwealth Transportation Fund from Pocahontas Parkway that will not be repaid within one year.

**Schedule of Due from/to Other Funds**

June 30, 2005

*(continued)*

*(Dollars in Thousands)*

<b>Due From</b>	<b>Amount</b>	<b>Due To</b>	<b>Amount</b>
<b>Component Units</b>		<b>Primary Government</b>	
University of Virginia	2,193	Nonmajor Governmental Funds	2,193
Virginia Polytechnic Institute & State University	8,124	<b>Primary Government</b>	
		Nonmajor Governmental Funds	165
		<b>Component Units</b>	
		Nonmajor Component Units	7,959
Virginia Commonwealth University	6,144	<b>Primary Government</b>	
		Nonmajor Governmental Funds	124
		<b>Component Units</b>	
		Nonmajor Component Units	6,020
Nonmajor Component Units	23,354	<b>Primary Government</b>	
		Nonmajor Governmental Funds	12,682
		<b>Component Units</b>	
		Nonmajor Component Units	10,672
Total Component Units	<u>39,815</u>		<u>39,815</u>
Total	<u>\$ 149,952</u>		<u>\$ 149,952</u>

**Interfund Receivables/Payables**

Interfund Receivables/Payables are loans made by one fund to another.

The following schedule shows the Interfund Receivables/Payables for the Primary Government as of June 30, 2005. There were no Interfund Receivables/Payables for the Component Units as of June 30, 2005.

**Interfund Receivables/Payables**

June 30, 2005

*(Dollars in Thousands)*

<b>Receivable From:</b>	<b>Amount</b>	<b>Payable To:</b>	<b>Amount</b>
<b>Primary Government</b>		<b>Primary Government</b>	
Nonmajor Governmental Funds	\$ 70,019	Major Special Revenue Funds:	
		Federal Trust	\$ 4,485
		Major Enterprise Funds:	
		State Lottery Department	15,000
		Nonmajor Governmental Funds	3,350
		Nonmajor Enterprise Funds	38,965
		Internal Service	8,219
<b>Total</b>	<u>\$ 70,019</u>	<b>Total</b>	<u>\$ 70,019</u>

**Loans Receivable/Payable Between Primary Government and Component Units**

The \$13.6 million in Loans Receivable from Component Units represents loans from the Special Revenue Fund to Higher Education (Component Unit). The Virginia Commonwealth University (Major Component Unit) loan of \$2.6 million and the College of William and Mary (Nonmajor Component Unit) loan of \$.8 million were used to fund programs until bonds were issued. George Mason University's (Nonmajor Component Unit) loan of \$8.5 million and the Virginia Community College System's (Nonmajor Component Unit) loan of \$.7 million were used to advance fund federally-funded grant

programs. Longwood University's (Nonmajor Component Unit) loan of \$1.0 million will be used for the University's housing sprinkler project.

The \$168.3 million in Loans Receivable from Primary Government represents loans from the VPSA to the Literary Fund. The VPSA makes grants to local school divisions to finance the purchase of educational technology equipment. The VPSA makes these grants using the proceeds of notes issued for that purpose which will be repaid from appropriations to be made by the Virginia General Assembly from the Literary Fund.

**9. OTHER ASSETS**

The following table summarizes Other Assets as of June 30, 2005:

*(Dollars in Thousands)*

	<b>Cash and Travel Advances</b>	<b>Unamortized Bond Issuance Expense</b>	<b>Other Assets</b>	<b>Total Other Assets</b>
<b>Primary Government:</b>				
General	\$ 1,479	\$ -	\$ -	\$ 1,479
Major Special Revenue Funds:				
Commonwealth Transportation	870	-	1,846	2,716
Federal Trust	1,658	-	-	1,658
Nonmajor Governmental Funds	939	-	259	1,198
Major Enterprise Funds:				
State Lottery	3	-	-	3
Pocahontas Parkway	-	5,120	-	5,120
Nonmajor Enterprise Funds	218	-	-	218
Internal Service Funds	1,039	-	-	1,039
Investment Trust Funds	-	-	9,140	9,140
Agency Funds	-	-	1,610	1,610
Total Primary Government (1)	<u>\$ 6,206</u>	<u>\$ 5,120</u>	<u>\$ 12,855</u>	<u>\$ 24,181</u>
<b>Discrete Component Units:</b>				
Virginia Housing Development Authority	\$ -	\$ -	\$ 5,236	\$ 5,236
University of Virginia	757	-	24,454	25,211
Virginia Polytechnic Institute and State University	-	254	2,605	2,859
Virginia Commonwealth University	358	2,700	7,547	10,605
Nonmajor Component Units	540	5,096	23,018	28,654
Total Component Units	<u>\$ 1,655</u>	<u>\$ 8,050</u>	<u>\$ 62,860</u>	<u>\$ 72,565</u>

Note (1): Other Fiduciary assets in the amount of \$10,750 (dollars in thousands) are not included in the Government-wide Statement of Net Assets.

## 10. RESTRICTED ASSETS

Restricted assets represent monies or other resources that must be used for specific legal or contractual requirements. The Virginia Housing Development Authority (Major Component Unit) reported restricted assets totaling \$6.1 billion (of which \$9.3 million is reported as Depreciable Capital Assets, net). The Virginia Public School Authority (Major Component Unit) reported restricted assets of \$81.4 million. Both Major Component Unit's assets are restricted for debt service under a bond indenture agreement or other agreements. The Virginia Port Authority (Nonmajor Component Unit) reported restricted assets of \$142.8 million. Of this amount \$70.3 million is assets placed in escrow account for a construction project, \$18.8 million for debt service under a bond indenture agreement, and \$25.6 million for other bond service projects, and 28.1 million reserved as part of the Port Facility Revenue Bond requirement. The Virginia Resources Authority (Nonmajor Component Unit) reported restricted assets of \$61.5 million. Of this amount \$50.7 million is restricted for loans to local governments, bond indentures, or federal

and state regulations for various revolving funds. \$5.1 million is restricted for the Operating Reserve Fund for the newly structured Virginia Pooled Financing Program. The Tobacco Indemnification and Community Revitalization Commission (Nonmajor Component Unit) reported restricted assets of 390.2 million. The Higher Education Institutions (Component Units) reported restricted assets totaling approximately \$2.6 billion primarily for endowment and other contractual obligations. Included in this amount is approximately \$2.1 billion of Foundations' restricted assets. The two museum foundations, the Virginia Museum of Fine Arts Foundation (Nonmajor Component Unit) and the Science Museum of Virginia Foundation (Nonmajor Component Unit) had restricted assets of \$152.9 million and \$11 million, respectively, primarily for donor-imposed restricted endowments. The remaining \$16.7 million is spread among the Hampton Roads Sanitation District Commission (Nonmajor Component Unit), the Virginia Equine Center (Nonmajor Component Unit), the Small Business Financing Authority (Nonmajor Component Unit), and the Library of Virginia Foundation (Nonmajor Component Unit).

## 11. CAPITAL ASSETS

The following schedule presents the changes in the Capital Assets:

### Schedule of Changes in Capital Assets

#### Governmental Activities

(Dollars in Thousands)

	Balance July 1, as restated	Increases	Decreases	Balance June 30
<b>Nondepreciable Capital Assets:</b>				
Land	\$ 1,452,614	\$ 174,566	\$ (51,344)	\$ 1,575,836
Construction in Progress	2,693,041	1,388,644	(1,334,131)	2,747,554
Total Nondepreciable Capital Assets	<u>4,145,655</u>	<u>1,563,210</u>	<u>(1,385,475)</u>	<u>4,323,390</u>
<b>Depreciable Capital Assets:</b>				
Buildings	2,127,174	33,360	(3,017)	2,157,517
Equipment	583,708	87,216	(73,372)	597,552
Infrastructure	16,601,161	1,327,700	(265,392)	17,663,469
Total Capital Assets being Depreciated	<u>19,312,043</u>	<u>1,448,276</u>	<u>(341,781)</u>	<u>20,418,538</u>
<b>Less Accumulated Depreciation for:</b>				
Buildings	729,096	54,907	(1,172)	782,831
Equipment	351,020	41,910	(54,937)	337,993
Infrastructure	8,409,522	392,480	(11,413)	8,790,589
Total Accumulated Depreciation	<u>9,489,638</u>	<u>489,297</u>	<u>(67,522)</u>	<u>9,911,413</u>
Total Depreciable Capital Assets, Net	<u>9,822,405</u>	<u>958,979</u>	<u>(274,259)</u>	<u>10,507,125</u>
Total Capital Assets, Net	<u>\$ 13,968,060</u>	<u>\$ 2,522,189</u>	<u>\$ (1,659,734)</u>	<u>\$ 14,830,515</u>

Note: Beginning balances have been restated by \$49,622 (dollars in thousands) due to prior year errors, as discussed in Note 2.

**Depreciation Expense Charged to Functions of the Primary Government**

June 30, 2005

*(Dollars in Thousands)*

Governmental Activities:	
General Government	\$ 9,223
Education	4,564
Transportation	406,726
Resources and Economic Development	8,141
Individual and Family Services	11,370
Administration of Justice	32,378
Capital Assets held by the Internal Service	
Funds are charged to various functions	16,895
Total	<u>\$ 489,297</u>

**Schedule of Changes in Capital Assets**

**Business-type Activities**

*(Dollars in Thousands)*

	<b>Balance July 1, as restated</b>	<b>Increases</b>	<b>Decreases</b>	<b>Balance June 30</b>
<b>Nondepreciable Capital Assets:</b>				
Land	\$ 16,412	\$ -	\$ -	\$ 16,412
Construction in Progress	5,497	6,708	(6,313)	5,892
Total Nondepreciable Capital Assets	<u>21,909</u>	<u>6,708</u>	<u>(6,313)</u>	<u>22,304</u>
<b>Depreciable Capital Assets:</b>				
Buildings	10,752	6,313	-	17,065
Equipment	78,475	3,114	(5,940)	75,649
Infrastructure	314,737	-	-	314,737
Total Capital Assets being Depreciated	<u>403,964</u>	<u>9,427</u>	<u>(5,940)</u>	<u>407,451</u>
<b>Less Accumulated Depreciation for:</b>				
Buildings	9,786	136	(1)	9,921
Equipment	46,825	9,589	(5,864)	50,550
Infrastructure	19,292	10,552	-	29,844
Total Accumulated Depreciation	<u>75,903</u>	<u>20,277</u>	<u>(5,865)</u>	<u>90,315</u>
Total Depreciable Capital Assets, Net	<u>328,061</u>	<u>(10,850)</u>	<u>(75)</u>	<u>317,136</u>
Total Capital Assets, Net	<u>\$ 349,970</u>	<u>\$ (4,142)</u>	<u>\$ (6,388)</u>	<u>\$ 339,440</u>

Note: Beginning balances have been restated by \$5,497 (dollars in thousands) due to prior year errors, as discussed in Note 2.

**Schedule of Changes in Capital Assets**

**Component Units**

*(Dollars in Thousands)*

	Balance			Subtotal June 30	Foundations (1)	Total June 30
	July 1, as restated	Increases	Decreases			
<b>Nondepreciable Capital Assets:</b>						
Land	\$ 359,808	\$ 6,739	\$ (2,368)	\$ 364,179	\$ 109,735	\$ 473,914
Construction in Progress	835,398	701,426	(432,116)	1,104,708	82,223	1,186,931
Inexhaustible Works of Art / Historical Treasures	70,042	982	-	71,024	12,632	83,656
Livestock	951	-	(190)	761	2,396	3,157
Total Nondepreciable Capital Assets	<u>1,266,199</u>	<u>709,147</u>	<u>(434,674)</u>	<u>1,540,672</u>	<u>206,986</u>	<u>1,747,658</u>
<b>Depreciable Capital Assets:</b>						
Buildings	5,002,525	338,211	(15,092)	5,325,644	488,094	5,813,738
Infrastructure	1,452,840	102,608	(29,150)	1,526,298	357	1,526,655
Equipment	1,890,464	242,302	(122,371)	2,010,395	82,153	2,092,548
Improvements Other Than Buildings	291,956	10,410	(390)	301,976	12,484	314,460
Library Books	558,650	26,297	(8,202)	576,745	-	576,745
Total Capital Assets being Depreciated	<u>9,196,435</u>	<u>719,828</u>	<u>(175,205)</u>	<u>9,741,058</u>	<u>583,088</u>	<u>10,324,146</u>
<b>Less Accumulated Depreciation for:</b>						
Buildings	1,896,201	146,850	(1,671)	2,041,380	96,375	2,137,755
Infrastructure	792,441	45,317	(18,140)	819,618	303	819,921
Equipment	1,211,100	164,422	(100,863)	1,274,659	58,632	1,333,291
Improvements Other Than Buildings	132,268	13,422	(447)	145,243	6,475	151,718
Library Books	443,590	25,607	(8,197)	461,000	-	461,000
Total Accumulated Depreciation	<u>4,475,600</u>	<u>395,618</u>	<u>(129,318)</u>	<u>4,741,900</u>	<u>161,785</u>	<u>4,903,685</u>
Total Depreciable Capital Assets, Net	<u>4,720,835</u>	<u>324,210</u>	<u>(45,887)</u>	<u>4,999,158</u>	<u>421,303</u>	<u>5,420,461</u>
Total Capital Assets, Net	<u>\$ 5,987,034</u>	<u>\$ 1,033,357</u>	<u>\$ (480,561)</u>	<u>\$ 6,539,830</u>	<u>\$ 628,289</u>	<u>\$ 7,168,119</u>

Note (1): Foundations represent FASB reporting entities defined in Note 1.B.

Beginning balances have been restated due to reclassifications and corrections of prior year errors. The following schedule is a summary of the restatement amounts.

**Capital Asset Restatement - Component Units**

*(Dollars in Thousands)*

	Balance July 1 Increase/(Decrease)
<b>Nondepreciable Capital Assets:</b>	
Construction in Progress	\$ (27,951)
Total Nondepreciable Capital Assets	<u>(27,951)</u>
<b>Depreciable Capital Assets:</b>	
Buildings	35,616
Infrastructure	83,914
Improvements Other Than Buildings	(59,473)
Total Capital Assets being Depreciated	<u>60,057</u>
<b>Less Accumulated Depreciation for:</b>	
Buildings	(53)
Infrastructure	68,314
Improvements Other Than Buildings	(57,629)
Total Accumulated Depreciation	<u>10,632</u>
Total Depreciable Capital Assets, Net	<u>49,425</u>
Total Capital Assets, Net	<u>\$ 21,474</u>

**12. RETIREMENT AND PENSION SYSTEMS**

A separately issued financial report that includes financial statements and required supplemental information for each of the individual plans discussed below is publicly available. Copies may be obtained by writing to Virginia Retirement System, P. O. Box 2500, Richmond, Virginia 23218-2500.

**A. Plan Description**

The Virginia Retirement System (VRS), a mixed agent and cost-sharing multiple-employer retirement plan, provides defined benefit pension plan coverage for Commonwealth employees, teachers, political subdivision employees, and other qualifying employees. The assets accumulated by the plan may legally be used to pay all benefits provided by the plan to any of the plan members or beneficiaries. At June 30, 2005, the VRS had 798 contributing employers. The State Police Officers' Retirement System (SPORS), the Judicial Retirement System (JRS), and the Virginia Law Officers' Retirement System (VaLORS) are single-employer defined benefit retirement plans. The SPORS provides retirement benefits to Virginia state police officers, the JRS provides retirement benefits to the Commonwealth's judiciary, and the

VaLORS provides benefits to law enforcement and correctional officers other than state police officers. All retirement systems are administered by the VRS, an independent agency of the Commonwealth.

Benefit provisions and all other requirements are established by Title 51.1 of the *Code of Virginia*. All full-time, salaried, permanent employees of the Commonwealth, with the exception of certain full-time faculty and administrative staff of higher education institutions and eligible employees of the Commonwealth's teaching hospitals who have the option not to participate in the VRS, must participate in the VRS, SPORS, JRS, or VaLORS. Benefits vest after five years of service.

Employees are eligible for an unreduced retirement benefit at age 65 with five years of service (age 60 for participating law enforcement officers) or at age 50 with at least 30 years of service if elected by the employer (age 50 with at least 25 years of service for participating law enforcement officers). Employees may retire with a reduced benefit at age 50 with at least ten years of credited service or at age 55 (age 50 for participating law enforcement officers) with at least five years of credited service.

Annual retirement benefits are payable monthly for life in an amount equal to 1.7 percent of their average final salary (AFS) for each year of credited service. AFS is defined as the highest consecutive 36 months of salary. Benefits are actuarially reduced for retirees who retire prior to becoming eligible for full retirement benefits. Members of the SPORS and VaLORS may receive a monthly benefit supplement if they retire prior to age 65. Members of VaLORS hired before July 1, 2001, were allowed to make a one-time election to increase the multiplier from 1.7 percent to 2.0 percent instead of receiving the supplement. Members of VaLORS hired after June 30, 2001, have their benefit computed using the 2.0 percent multiplier and are not eligible for the supplement. Members of the JRS receive weighted years of creditable service for each year of actual service under JRS. The VRS, SPORS, VaLORS, and JRS also provide death and disability benefits. These benefit provisions and all other requirements are established by State statute.

## **B. Summary of Significant Accounting Policies**

### **Basis of Accounting**

The financial statements of the pension trust funds are prepared using the economic resources measurement focus and the accrual basis of accounting. Employee and employer contributions are recognized when due, pursuant to formal commitments, as well as statutory or contractual requirements. Investment income is recognized as

earned by the pension plans. Benefits and refunds are recognized when due and payable in accordance with the terms of the plans.

### **Method Used to Value Investment**

Investments are reported at fair value as determined by the VRS master custodian, Mellon Trust, from its Global Pricing System. This system assigns a price source, based on asset type and the vendor pricing products to which the master custodian subscribes, for every security held immediately following its acquisition. Prices supplied by these sources are monitored on a daily basis by the master custodian.

The pricing sources utilized by the master custodian provide daily prices for equity securities, corporate, government and mortgage-backed fixed income securities, private placement securities, futures and options on futures, open-ended funds, and foreign exchange rates. Depending on the vendor, collateralized mortgage obligations, adjustable rate mortgages, and asset-backed securities are priced either daily, weekly or twice a month, and at month end. Municipal fixed income securities and options on Treasury/Government National Mortgage Association securities are priced at month end.

When a pricing source is unable to provide a price, quotes are sought from major investment brokers and market-making dealers or internal calculations are applied if feasible. As a last resort, the master custodian will contact investment managers for a price. The master custodian prices commingled funds, partnerships, and real estate assets from statements received from the funds, partnerships, or investment managers.

The retirement plans have no concentrations of investments in any one organization that represent 5 percent or more of plan net assets available for benefits.

## **C. Funding Policy**

Employer and employee contributions are required by Title 51.1 of the *Code of Virginia*. The Commonwealth pays the 5 percent of employees' annual salaries that employees are required to contribute to the retirement system.

The annual required contributions for the current year were determined during the actuarial valuations conducted as of June 30, 2003. Employer contributions by the Commonwealth to VRS, SPORS, VaLORS, and JRS were 3.91 percent, 16.49 percent, 16.99 percent, and 30.55 percent, respectively, of covered payrolls.

#### D. Annual Pension Cost and Net Pension Obligation

The following table (dollars in thousands) shows the Commonwealth's annual pension cost and net pension obligation to the VRS, SPORS, JRS, and VaLORS for the current and prior years.

	VRS			SPORS		
	2005	2004	2003	2005	2004	2003
Annual required contribution	\$ 156,313	\$ 156,192	\$ 145,138	\$ 25,891	\$ 23,031	\$ 21,791
Interest on net pension obligation	43,427	39,209	27,322	4,326	3,266	2,203
Adjustment to annual required contribution	(39,694)	(34,269)	(23,880)	(3,945)	(2,854)	(1,925)
Annual pension cost	160,046	161,132	148,580	26,272	23,443	22,069
Contributions made	(117,225)	(108,412)	-	(14,475)	(10,328)	(8,781)
Increase in net pension obligation	42,821	52,720	148,580	11,797	13,115	13,288
Net pension obligation, beginning of year, as restated	542,840	490,120	341,532	53,941	40,826	27,538
Net pension obligation, end of year	\$ 585,661	\$ 542,840	\$ 490,112	\$ 65,738	\$ 53,941	\$ 40,826
Percentage of annual pension cost contributed	73.2%	67.3%	0.0%	55.1%	44.1%	39.8%

  

	JRS			VaLORS		
	2005	2004	2003	2005	2004	2003
Annual required contribution	\$ 24,943	\$ 23,114	\$ 22,266	\$ 84,353	\$ 79,569	\$ 76,564
Interest on net pension obligation	2,683	2,029	1,322	10,997	7,801	4,423
Adjustment to annual required contribution	(2,452)	(1,773)	(1,156)	(10,052)	(6,818)	(3,865)
Annual pension cost	25,174	23,370	22,432	85,298	80,552	77,122
Contributions made	(15,269)	(15,190)	(13,604)	(50,495)	(40,596)	(34,895)
Increase in net pension obligation	9,905	8,180	8,828	34,803	39,956	42,227
Net pension obligation, beginning of year	33,539	25,359	16,531	137,467	97,511	55,284
Net pension obligation, end of year	\$ 43,444	\$ 33,539	\$ 25,359	\$ 172,270	\$ 137,467	\$ 97,511
Percentage of annual pension cost contributed	60.7%	65.0%	60.6%	59.2%	50.4%	45.2%

The VRS pension liability for the Virginia Economic Development Partnership (VEDP) (Component Unit), the Virginia Tourism Authority (VTA) (Component Unit), and the Virginia Outdoors Foundation (VOF) (Component Unit) are reported in the financial statements. However, since the Commonwealth is not considered the employer for VEDP, VTA, or VOF, the Commonwealth's net pension obligation shown above at the end of the year does not include VEDP's pension liability of \$1.4 million, VTA's pension liability of \$354,204, or VOF's pension liability of \$6,476.

The most recent actuarial valuations were conducted as of June 30, 2003. The valuations were prepared using the entry age normal cost method. The actuarial assumptions included (a) 8.00 percent investment rate of return, per year compounded annually; (b) projected salary increases ranging from 4.00 percent to 6.30 percent, including a 3.00 percent inflation component; and (c) 3.00 percent per year COLA. Valuation techniques were applied to smooth the effects of short-term volatility in the market value of investments over a five-year period. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll. The remaining closed amortization period at June 30, 2005, was 23 years or less.

**E. Defined Contribution Plan for Political Appointees**

Officers appointed by the Governor, officers elected by popular vote or the General Assembly, and executive branch chief deputies and confidential assistants may participate in the Deferred Contribution Plan for Political Appointees, rather than the VRS. This optional retirement plan is authorized by the *Code of Virginia* and offered through the Great West Company. This is a defined contribution plan where the retirement benefits are based upon the Commonwealth's (3.91 percent) and the employee's (5.0 percent) contributions, plus interest and dividends. The Commonwealth pays the required employee contributions. During the year ended June 30, 2005, the total contributions to this plan were \$676,100.

The summary of significant accounting policies for the plan is in accordance with those discussed in Section B.

**F. Higher Education Fund (Component Unit)**

The Commonwealth's colleges and universities participate in the VRS, a mixed agent and cost-sharing multiple-employer retirement plan. The VRS issues a separate stand-alone report that is publicly available as previously discussed.

In addition, full-time faculty and certain administrative staff of the Commonwealth's colleges and universities may participate in an optional retirement annuity program, rather than the VRS. Optional Retirement Plans are authorized by the *Code of Virginia* and provide retirement and death benefits. The optional retirement annuity

programs are offered through Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF) Insurance Companies, Variable Annuity Life Insurance Company (VALIC), Fidelity Investments, Inc., Great West Life, Inc., T. Rowe Price, Inc., Metropolitan Life and Vanguard. These are defined contribution programs where the retirement benefits received are based upon the Commonwealth's (5.4 percent) and employees' (5.0 percent) contributions, plus interest and dividends. The Commonwealth pays the required employee contributions. During the year ended June 30, 2005, the total contributions to these plans were:

TIAA-CREF	\$	73,253,025
VALIC		2,106,529
Fidelity Investments		30,695,670
Great West Life		78,967
T. Rowe Price		269,570
Vanguard		1,350,922
Total	\$	<u>107,754,683</u>

The Virginia Commonwealth University Health System Authority (Authority) (a blended component unit of the Virginia Commonwealth University – Major) contributes to the VRS. The VRS issues a separate stand-alone report that is publicly available as previously discussed. Effective July 1, 1997, the Authority established the Virginia Commonwealth University Health System Authority Defined Contribution Plan (the Plan). All employees, excluding house staff, working at least 20 hours per week in a benefit eligible position are eligible to participate in the Plan. Per the Plan document as approved by the Authority's Board of Directors, the Authority contributes up to 10.0 percent of the participant's salary to the Plan not to exceed the lesser of (a) the amount in accordance with Code 415(d), or (b) 100 percent of the participant's compensation for such limitation year. Total contributions for the year ended June 30, 2005, were approximately \$8,217,000. The Authority has the right at anytime, and without the consent of any party, to terminate the Plan in its entirety. The Authority's Board of Directors must approve any changes to the provisions of the Plan, including the contribution requirements, in writing. The Authority has also established the Virginia Commonwealth University Health System Authority Health Care Providers Defined Contribution Plan (the HCP Plan). All persons hired as a health care provider on or after July 1, 1993, and prior to July 1, 1997, and working at least 35 hours of service per week were eligible to participate in the HCP Plan. At June 30, 2005, there were six actively employed participants in the HCP Plan. Total contributions to the HCP Plan for the year ended June 30, 2005, were approximately \$30,400.

Previously, the Medical College of Virginia Associated Physicians (MCVAP) (a Component Unit of the Authority) sponsored the MCVAP 403(b) Retirement Fund (the 403(b) Plan), a defined contribution plan which covered substantially all non-medical employees of MCVAP. As of

January 1, 2002, no additional contributions were made to this Plan.

MCVAP also sponsors the MCVAP 401(a) Retirement Plan (the 401(a) Plan), a noncontributory, defined contribution plan which covers substantially all benefit eligible clinical providers of MCVAP. Contributions to the 401(a) Plan, as determined annually at the discretion of the Board of Directors were approximately \$5,288,000 for the year ended June 30, 2005.

MCVAP also sponsors the VCUHS 401(a) Retirement Plan a defined contribution plan which covers all non-medical employees of MCVAP and the VCUHS 457(b) Retirement Plan, a salary reduction plan that represents employee contributions. These plans became effective on January 1, 2002, and replaced the MCVAP 403 (b) plan for all non-medical staff. The contributions to the VCUHS 401(a) for the period ended June 30, 2005, were approximately \$2,210,000.

VA Premier (a Component Unit of the Authority) adopted a 401(k) plan sponsored by Prudential Mutual Fund Management, Inc. Employees may enter into the plan on the first day of the month coinciding with or following the date on which the employee begins employment. There is no minimum service or age requirement to be in the 401(k) plan. Employees may contribute 1 percent to 15 percent of their compensation. VA Premier will match 50 percent of the employees' contributions up to 4 percent of the employees' compensation. Matching will occur based on the bi-weekly pay periods. In addition, VA Premier contributes 3 percent of the employee's compensation after each bi-weekly payroll effective when the employee begins employment. Employees are fully vested after four years of service in which the employees have at least 1,000 hours of service each year. The total expense to VA Premier in fiscal year 2005 was approximately \$463,000.

Effective January 1, 1997, James Madison University (nonmajor) established a Supplemental Retirement Plan for tenured faculty members. The plan was designed to provide flexibility in the allocation of faculty positions. The plan is a qualified plan within the meaning of section 401(c) of the Internal Revenue Code of 1986 (the Code) and is a governmental plan within the meaning of section 414(d) of the Code. Since it is a governmental plan, the plan is not subject to the Employee Retirement Income Security Act of 1974 as amended. Since inception, 112 faculty members have elected to enroll in the plan. As of June 30, 2005, 44 participants remain, including 3 new participants who retired under this plan during fiscal year 2005. In order to satisfy IRS requirements, a trust fund has been established as means to make the payments to the plan participants. The University prepaid the entire fiscal year 2006 plan contribution of \$885,277 in fiscal year 2005.

The Innovative Technology Authority (ITA) (nonmajor) has a defined contribution retirement plan covering substantially all employees. Under the plan, contributions are fixed at a percentage of each employee's compensation to pay premiums for individual retirement annuity contracts written by TIAA-CREF. Pension contributions for the plan totaled \$403,425 in fiscal year 2005.

## **G. Other Component Units**

Note 1.B. outlines the component units included in the Commonwealth's reporting entity. The Virginia Historic Preservation Foundation (Blended - Primary Government), the Virginia Public Building Authority (Blended - Primary Government), the Virginia Public School Authority (major), the Virginia College Building Authority (nonmajor), the Virginia State Parks Foundation (Blended - Primary Government), the Virginia Schools for the Deaf and Blind Foundation (nonmajor), and the Pocahontas Parkway Association (Blended - Primary Government) have no employees. The Virginia Economic Development Partnership, the Small Business Financing Authority, the Hampton Roads Sanitation District Commission, the Virginia Biotechnology Research Park Authority, the A. L. Philpott Manufacturing Extension Partnership, the Virginia Outdoors Foundation, the Virginia Tourism Authority, the Tobacco Indemnification and Community Revitalization Commission, the Virginia Tobacco Settlement Foundation, the Virginia Land Conservation Foundation, the Virginia Arts Foundation, and the Library of Virginia Foundation (all nonmajor) contribute solely to the VRS, a mixed agent and cost-sharing multiple-employer retirement plan. The VRS issues a separate stand-alone report that is publicly available as previously discussed.

Full-time employees of the Virginia Housing Development Authority (major) participate in a defined contribution employees' retirement savings plan administered by the Authority. This is a noncontributory plan where the Authority incurs employment retirement savings expense equal to 8.0 percent of full-time employees' compensation. Total retirement savings expense under this plan was \$1,453,215 in fiscal year 2005.

The Virginia Port Authority (nonmajor) contributes to the VRS. The Authority also sponsors two single-employer noncontributory defined benefit pension plans. The Virginia Port Authority Pension Plans are administered by the Authority and provide retirement, disability, and death benefits to plan members and beneficiaries. Benefit provisions and obligations are established and may be amended by the Board of Commissioners of the Authority. The plan was restated October 1, 2001, to ensure compliance with additional regulations.

The components of annual pension cost and prepaid pension obligation for the first single-employer noncontributory defined benefit pension plan are as follows:

**Trend Information**

	<b>2005</b>	<b>2004</b>	<b>2003</b>
Service cost - benefits earned during the year	\$ 1,642,100	\$ 1,156,600	\$ 987,000
Interest cost on projected benefit obligation	2,653,000	2,260,700	2,144,000
Expected return on assets	(2,972,100)	(2,675,000)	(2,429,000)
Net amortization and deferral	643,600	151,300	76,400
Annual pension cost	1,966,600	893,600	778,400
Contributions made	(1,104,900)	(1,299,000)	(2,916,100)
Increase in prepaid pension obligation	861,700	(405,400)	(2,137,700)
Prepaid pension obligation, beginning of year	(8,167,800)	(7,762,400)	(5,624,700)
Prepaid pension obligation, end of year	<u>\$ (7,306,100)</u>	<u>\$ (8,167,800)</u>	<u>\$ (7,762,400)</u>

The annual pension cost for the current year was determined as part of the September 30, 2003, actuarial valuation using the aggregate actuarial cost method, which does not identify and separately amortize unfunded actuarial liabilities. The discount rate used in determining the actuarial present value of projected benefit obligation was 6.75 percent in fiscal year 2005, 7.5 percent in fiscal year 2004, and 8.0 percent in fiscal year 2003. The expected long-term rate of return on assets used in determining net periodic pension cost was 8.0 percent.

The following table sets forth the plan's funded status and the related amounts recorded in the Authority's balance sheets at June 30, 2005, 2004, and 2003.

<b>Trend Information</b>			
<b>Fiscal Year Ended June 30</b>	<b>Annual Pension Cost (APC)</b>	<b>Percentage of APC Contributed</b>	<b>Prepaid Pension Obligation</b>
2005	\$ 1,966,600	56 %	\$ (7,306,100)
2004	\$ 893,600	145 %	\$ (8,167,800)
2003	\$ 778,400	375 %	\$ (7,762,400)

In November 2001, the second plan was amended to provide benefits to sworn police officers that more closely resemble the new retirement benefits provided to members of the Virginia Law Enforcement Officers Retirement System. The effect of those changes is included in the accompanying pension data.

The components of annual pension cost and prepaid pension obligation for the second single-employer noncontributory defined benefit pension plan are as follows:

**Trend Information**

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Service cost - benefits earned during the year	\$ 329,902	\$ 348,524	\$ 197,071
Interest cost on projected benefit obligation	157,419	138,803	111,771
Expected return on assets	(107,220)	(167,011)	(36,821)
Net amortization and deferral	83,198	183,283	87,904
Annual pension cost	<u>463,299</u>	<u>503,599</u>	<u>359,925</u>
Contributions made	(506,915)	(149,822)	(802,299)
Additional minimum liability	<u>945,384</u>	<u>(435,518)</u>	<u>158,952</u>
Increase in pension obligation	901,768	(81,741)	(283,422)
Pension obligation, beginning of year	502,017	583,758	867,180
Pension obligation, end of year	<u>\$ 1,403,785</u>	<u>\$ 502,017</u>	<u>\$ 583,758</u>

The annual pension cost for the current year was determined as part of the August 2005 actuarial valuation using the aggregate actuarial cost method, which does not identify and separately amortize unfunded actuarial liabilities. Actual value of assets was determined using market value. The discount rate used in determining the actuarial present value of the projected benefit obligation was 5.3 percent in 2005, 6.3 percent in 2004, and 6.0 percent in 2003. The expected long-term rate of return on assets used in determining net periodic pension cost was 8.0 percent.

The following table sets forth the plan's funded status and the related amounts recorded in the Authority's balance sheets at June 30, 2005, 2004, and 2003.

elected to defer participation in the VRS, whereby 12 percent of eligible employees' salary is contributed on an annual basis. For the year ended June 30, 2005, VRS retirement expense was \$27,876 and total retirement savings expense was \$54,358, a portion of which is reimbursed.

The Virginia Equine Center Foundation has a defined contribution plan which covers all full-time employees of the Foundation who have one year of service and are age twenty-one or older. The plan is subject to the provisions of the Employee Retirement Income Security Act of 1974. Contributions to the plan are discretionary and the Foundation will determine the amount to contribute to the plan each year. No contributions were made on behalf of the employees for the fiscal year ended June 30, 2005.

**Trend Information**

<u>Fiscal Year Ended June 30</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Prepaid Pension Obligation</u>
2005	\$ 463,299	109 %	\$ 1,403,785
2004	\$ 503,599	30 %	\$ 502,017
2003	\$ 359,925	223 %	\$ 583,758

The Authority also sponsors two noncontributory supplemental plans covering certain key employees. The Authority's current policy is not to fund the costs of these plans. The plans had assets of \$1,838,656 and an accrued liability of \$2,132,829.

As of January 1, 2005, The Virginia Resources Authority began mandatory participation for all new employees and optional participation for then-current employees who chose to enroll in the VRS. The Authority continues to sponsor a retirement savings plan for the employees noted above who

**13. OTHER EMPLOYMENT BENEFITS**

In addition to the pension plans, the Commonwealth participates in three other employment benefit plans, Group Life Insurance, Retiree Health Insurance Credit, and Virginia Sickness and Disability Program, which are administered by the Virginia Retirement System (VRS). The VRS administers a fourth other employment benefit plan, the Volunteer Firefighters' and Rescue Squad Workers' Fund, in which the Commonwealth does not participate, but may provide funding. The significant accounting policies for all four plans are the same as those described in Note 12 for pension plans. A separately issued financial report that includes financial statements for Group Life Insurance, Retiree Health Insurance Credit, and Virginia Sickness and Disability Program is publicly available. Copies may be obtained by writing to Virginia Retirement System, P. O. Box 2500, Richmond, Virginia 23218-2500.

## Group Life Insurance

The Group Life Insurance Plan provides life insurance benefits for Commonwealth employees, teachers, employees of political subdivisions participating in the VRS, State police officers, judges, and other qualifying employees. In fiscal year 2005 there were approximately 340,251 Commonwealth employees and 112,346 retirees in the program.

As part of this plan, the Commonwealth provides life insurance benefits for retired employees in accordance with Title 51.1 of the *Code of Virginia*. To be eligible, the employee must have retired or terminated employment after age 50 and have had at least ten years of service (including five years of continuous service) or at age 55 and have had five years of continuous service (age 50 for participating law enforcement officers, firefighters of political subdivisions, and judges) or retired because of disability. At retirement or termination, natural death coverage starts to reduce by 25 percent each year until coverage reaches 25 percent of its value at retirement or termination.

Postemployment life insurance benefits are advance funded on an actuarially determined basis using the aggregate cost actuarial method. Rates were determined in a June 30, 2001, actuarial valuation using the same actuarial assumptions used for determining pension plan contribution rates. The modified market value of plan assets was used for valuation purposes. Retirees are not required to contribute to the group life plan. The Commonwealth's actuarially required contribution rate for the current year was 1.14 percent of payroll. This contribution covers premiums for active employees and actual death claims for retirees.

The accrued liabilities for postemployment death benefits actuarially determined through an actuarial valuation performed as of June 30, 2004, were \$1,802.0 million. The actuarial value of the program's assets available for benefits on that date was \$834.3 million, leaving a present value of future contributions of \$967.7 million.

## Retiree Health Insurance Credit

The Retiree Health Insurance Credit Plan provides health insurance credits against the monthly health insurance premiums for retired Commonwealth employees, State police officers, and judges with at least 15 years of creditable service on the current disbursement basis. Benefit provisions and eligibility requirements are established by Title 51.1-1400 of the *Code of Virginia*. Approximately 69,114 Commonwealth retirees were receiving health insurance credits at June 30, 2005.

The monthly credit amounts to \$4.00 per year of service not to exceed a maximum allowance of \$120.00. The contribution rate was determined as part of the June 30, 2001, actuarial valuation that determined the pension plan contribution rates. The Commonwealth's actuarially required contribution rate for "full funding" and "pay-as-you-go" would have been 1.79 and 1.19 percent of payroll, respectively, for the current year; however, contributions were paid at 1.04 percent of payroll. The

Commonwealth recognized Retiree Health Insurance Credit expenses of \$68.9 million during the fiscal year ended June 30, 2005.

## Virginia Sickness and Disability Program

The Virginia Retirement System (VRS) administers the Virginia Sickness and Disability Program (VSDP) to provide income protection for absences due to sickness or disability from the first day on the job. After a seven calendar-day waiting period following the first incident of disability, eligible employees receive short-term disability benefits ranging from 60 to 100 percent of compensation up to a maximum of 125 work days, based upon months of Commonwealth service. After a 180 calendar-day waiting period (125 work days of short-term disability), eligible employees receive long-term disability benefits equal to 60 percent of compensation until they return to work, until age 65 (age 60 for State police officers), or until death.

The VSDP was established on January 1, 1999, for all full-time, classified Commonwealth employees, including State police officers and other State law enforcement and corrections officers, hired on or after January 1, 1999. Part-time, classified employees who work at least 20 hours a week on a salaried basis and who accrue leave are also covered. Eligible Commonwealth employees and State police officers of the Commonwealth employed prior to January 1, 1999, had the option to elect to participate in the VSDP or to remain in the Commonwealth's existing disability retirement and sick leave program (see Notes 12 and 16). Eligible employees enrolled in the VSDP are not eligible for disability retirement benefits under VRS, the State Police Officers' Retirement System (SPORS), or the Virginia Law Officers Retirement System (VaLORS).

Faculty of Virginia institutions of higher education hired or appointed on or after January 1, 1999, who elected the VRS as their retirement plan, must make an irrevocable election to participate in the VSDP or in the institution's disability program. If there is no institution program, the faculty is covered under this program.

All Commonwealth agencies are required to contribute to the cost of providing long-term disability benefits. Initial contribution requirements to fund the program were determined by the VRS actuary based on an estimate of the amount of the liability for disability benefits that would transfer from the VRS and SPORS to the VSDP for the anticipated new participants in the VSDP. This contribution requirement was 1.65 percent of payroll for Commonwealth employees, State police officers and VaLORS employees during the fiscal year. The Commonwealth recognized long-term disability expenses of \$25.8 million during the fiscal year. As of June 30, 2005, there were approximately 67,567 participants.

## Volunteer Firefighters' and Rescue Squad Workers' Fund

Volunteer firefighters and rescue squad workers may participate in an optional postemployment benefit plan. This optional plan is authorized by the *Code of Virginia*. The Board of Trustees of the VRS manages the

investments of the Fund as custodian. Members of the plan contribute \$30 per quarter. The Commonwealth will contribute an amount determined by the Board and appropriated by the General Assembly, if such funds are appropriated, for a period not to exceed twenty years. For fiscal year 2005, \$78,000 was appropriated. At June 30, 2005, there were 1,091 workers participating in the Fund.

#### **14. DEFERRED COMPENSATION PLANS**

The Commonwealth offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The Virginia Retirement System (VRS) administers the deferred compensation plan, pursuant to the Government Employees Deferred Compensation Plan Act, Section 51.1, Chapter 6 et seq. of the *Code of Virginia*. The VRS contracts with private corporations or institutions subject to the standards set forth in the *Code* to provide investment products as well as any other goods and services related to the administration of the deferred compensation plan. The Department of Accounts is responsible for the accounting, reconciliations, and record keeping associated with State employees' enrollment, payment to the plan through payroll deductions, and timely transfer of withheld funds to the trustee designated by the VRS for investment. The plan provides a number of investment options and is designed so that each participant retains investment control of his/her individual account. The plan, available to all State employees, permits them to defer a portion of their salary until future years. The deferred compensation is held in trust for the exclusive benefit of plan participants and their beneficiaries and is not available to employees until termination, retirement, death, or unforeseeable emergency. Since the VRS has no fiduciary relationship with plan participants, plan assets of \$728.5 million are not included in the financial statements.

In addition, the Commonwealth provides a cash match under Internal Revenue Code Section 401(a) for employees participating in the deferred compensation plan who have been employed at least one year. The match amount for an employee was established at 50 percent of the voluntary contributions to the deferred compensation plan. During the current fiscal year, the maximum match was \$20 per pay period or \$40 per month. The fair value of assets in the cash match savings plan at June 30, 2005, was \$73.4 million, which is also excluded from the financial statements.

The Virginia Housing Development Authority (Major Component Unit) and the Virginia Resources Authority (Nonmajor Component Unit) have a deferred compensation plan available to all employees created in accordance with Internal Revenue Section 457. The Plan permits participants to defer a portion of their salary or wage until future years. The deferred compensation is not available to employees until termination, retirement, or death. The assets of the Plan are in an irrevocable trust with an external trustee and, accordingly, no assets or liabilities are reflected in the financial statements.

The Virginia Port Authority (VPA) (Nonmajor Component Unit) offers three deferred compensation plans and two matching savings plans under Internal Revenue Code Sections 457 and 401(a), respectively. Employees who maintain status under VRS are covered under the Deferred Compensation Plan administered by the VRS as discussed above. The VPA deferred compensation plan covers all employees hired after July 1, 1997, and those employees electing coverage under the Authority's deferred compensation plan. The VPA also offers a matching savings plan that covers substantially all employees. The matching savings plan requires the VPA to match contributions in an amount equal to 50 percent of the first 6 percent of the participant's base pay contributed to the plan. VPA's total contribution to the matching savings plan was \$112,835 for the fiscal year ended June 30, 2005. Further, the right to modify, alter, amend, or terminate the deferred compensation plan and matching savings plan rests with the VPA Board of Commissioners.

The third deferred compensation plan and second matching savings plan covers substantially all nonunion employees with 90 days or more of service. The matching savings plan requires the VPA to match employee contributions in an amount equal to 50 percent of the first 3 percent of the participant's base pay contributed to the deferred compensation plan. VPA's total contribution to the matching savings plan was \$288,913 for the fiscal year ended June 30, 2005.

The Hampton Road Sanitation District's (the District) Commission adopted a post-retirement health benefit for qualifying employees beginning after July 1, 2002. The program furnishes health and dental benefits for life for all employees with at least 15 years of service and who also qualify for an unreduced retirement benefit through the Virginia Retirement System. The program allows the retiree at their expense to cover their spouse and dependent under the District's health care provider. The District funded the estimated prior service cost of approximately \$7,000,000 in a separate trust established for this purpose from the sale of land and additional designated revenue. For the year ended June 30, 2005, the estimated ongoing annual required contribution is approximately \$500,000, and is funded through operations. The fair market value of the Trust as of June 30, 2005, was \$8,577,578.

#### **15. COMMITMENTS**

##### **A. Construction Projects**

###### **Highway Projects**

At June 30, 2005, the Department of Transportation (Primary Government) had contractual commitments of approximately \$1,705.3 million for construction of various highway projects. Funding for these expenditures is expected to be provided as follows: (1) Federal Funds – approximately 20.2 percent or \$344.0 million, (2) State Funds – approximately 75.7 percent or \$1,291.5 million, and (3) Proceeds from Bonds – approximately 4.1 percent or \$69.8 million.

## Mass Transit Projects

At June 30, 2005, the Department of Rail and Public Transportation (Primary Government) had contractual commitments of approximately \$182.3 million for various public transportation and rail preservation projects. Funding of the future expenditures is expected to be as follows: (1) State Funds – approximately 73 percent or \$133.7 million, and (2) Federal Funds – approximately 27 percent or \$48.6 million.

	Primary Government		Component Units (1)
	Governmental Activities	Business-type Activities	
2006	\$ 52,584	\$ 12,231	\$ 43,372
2007	36,154	8,349	31,712
2008	28,041	5,981	22,276
2009	20,229	3,622	17,555
2010	12,548	1,603	14,155
2011-2015	22,454	1,004	22,564
2016-2020	4,664	-	7,486
2021-2025	914	-	823
2026-2030	106	-	823
2031-2035	75	-	823
2036-2040	-	-	823
2041-2045	-	-	823
2046-2050	-	-	659
Total	\$ 177,769	\$ 32,790	\$ 163,894

## Port Projects

At June 30, 2005, the Virginia Port Authority (Nonmajor Component Unit) was committed to construction contracts totaling \$255.7 million.

## Sanitation District Project

At June 30, 2005, the Hampton Roads Sanitation District Commission (Nonmajor Component Unit) was committed to construction programs totaling \$37.8 million.

Note (1): The above amounts exclude operating lease obligations of Foundations.

## Higher Education Institutions

Many of the colleges and universities (Component Units) are committed to construction contracts. As of June 30, 2005, these commitments totaled approximately \$588.2 million. Higher Education Foundations' commitments total approximately \$57.0 million and are primarily for construction contracts.

Foundations (2)	
2006	\$ 863
2007	708
2008	631
2009	535
2010	511
Thereafter	5,131
Total	\$ 8,379

Note (2): Foundations represent FASB reporting entities defined in Note 1.B. Rental expense for the year ended June 30, 2005, was approximately \$1.3 million.

## Correctional Institutions

The Department of Corrections is committed to construction contracts at the Buckingham, Dillwyn, Fluvanna, and Nottoway Correctional Centers. As of June 30, 2005, these commitments totaled approximately \$8.2 million.

Lease agreements are for various terms and all leases contain nonappropriation clauses indicating that continuation of the lease is subject to funding by the General Assembly.

## B. Operating Leases

The Commonwealth has entered into numerous agreements to lease land, buildings, and equipment. Most of the operating leases contain the provision that the Commonwealth may renew the operating leases at the expiration date of the lease on a month-to-month basis. In most cases, management expects that in the normal course of business, leases will be renewed or replaced by other leases of a similar nature. Rental expense for the primary government under these operating leases for the year ended June 30, 2005, was \$74.8 million for governmental activities (including Internal Service Funds) and \$15.1 million for business-type activities. Rental expense for the discrete component units (excluding Foundations) for the year ended June 30, 2005, was \$77.6 million. The Commonwealth has, as of June 30, 2005, the following minimum rental payments due under the above leases (dollars in thousands):

## C. Investment Commitments – Virginia Retirement System

The Virginia Retirement System extends investment commitments in the normal course of business, which, at June 30, 2005, amounted to \$3.5 billion.

## D. Tobacco Grants

The Tobacco Indemnification and Community Revitalization Commission (Commission) (Nonmajor Component Unit) has \$49.1 million in grant award commitments not reflected in these statements since eligibility requirements were not met as of June 30, 2005, in accordance with GASBS No. 33. The Commission awarded an additional \$7 million in grants in July 2005 that are also not reflected in these statements.

The Virginia Tobacco Settlement Foundation (Nonmajor Component Unit) has \$3.5 million in grant commitments and \$4.8 million in outstanding contracts not reflected in these statements since eligibility requirements were not met as of June 30, 2005, in accordance with GASBS No. 33.

**E. Maintenance Contracts**

The Virginia Economic Development Partnership (Nonmajor Component Unit) entered into a 3-year contract for maintenance on its Microsoft products for a total cost of \$135,223. As of June 30, 2005, one year is remaining on this commitment, amounting to \$45,074.

**16. ACCRUED LIABILITY FOR COMPENSATED ABSENCES**

Employees accrue annual leave at a rate of four to nine hours semimonthly, depending on their length of service. The maximum leave accumulation is dependent upon years of service, but in no case may it exceed 432 hours. The maximum compensation for annual leave balances is also dependent upon years of service, but in no case may an employee be compensated for more than 336 hours.

All employees hired after January 1, 1999, are required to enroll in the Virginia Sickness and Disability Program (VSDP) (see Note 13). Under the VSDP, employees receive a specified number of sick and personal leave hours, depending on their length of service, and any balances at the end of the calendar year revert. Individuals employed at January 1, 1999, had the option of converting to the VSDP or remaining in the original sick leave plan. If converting, the employee's sick leave balance could be used to purchase retirement credits or be converted to disability credits. If an employee opted to remain in the original sick leave program, sick leave accrues at a rate of five hours semimonthly. Employees who leave State service after a minimum of five years employment receive the lesser of 25 percent of the value of their disability credits or accumulated sick leave at their current earnings rate or \$5,000. All employees leaving State service are paid for accrued annual leave up to the maximum calendar year limit at their current earnings rate.

In conformance with Section C60 of GASB Codification, the monetary value of accumulated annual and sick leave and disability credits payable upon termination is included in the accompanying financial statements. In the government-wide statements, proprietary fund statements, and discrete component unit fund statements, amounts are segregated into two components – the amount due within one year and the amount due in more than one year. In the governmental fund statements, amounts to be paid from expendable resources are recognized as fund liabilities in the applicable governmental fund types as long-term liabilities and represent payments for separations that occurred prior to June 30. Amounts not payable from expendable resources are reflected in the governmental activities column in the Government-wide Statement of Net Assets (see Note 20). All amounts related to the fiduciary funds are recognized in those funds.

The liability at June 30, 2005, was computed using salary rates effective at that date, and represents vacation, compensatory and sick leave earned or disability credits held up to the allowable ceilings.

**17. INSURANCE**

**A. Self-Insurance**

The Commonwealth maintains two types of self-insurance plans. The first type of self-insurance is a health care plan administered by the Department of Human Resource Management for Commonwealth employees. The plan is accounted for in the Health Care – Internal Service Fund. Interfund premiums are accounted for as internal activity receipts from other funds. At June 30, 2005, \$77.7 million is reported as the estimated claims payable for this fund, which is undiscounted as nearly all health care claims are current in nature. The estimated liability is based upon actual claims that have been submitted as well as actuarially determined claims incurred but not reported as described in Note 1.R. Changes in the balances of claims liabilities (dollars in thousands) during the current and prior fiscal years are as follows:

	Current			
	Year Claims			
	Balance	and Changes	Claim	Balance
	July 1,	in Estimates	Payments	June 30,
2004-2005	\$ 85,706	\$ 661,590	\$ (669,579)	\$ 77,717
2003-2004	\$ 78,800	\$ 613,508	\$ (606,602)	\$ 85,706

The second type of plan, risk management, is administered by the Department of the Treasury, Division of Risk Management and the Department of Human Resource Management, Worker's Compensation Program. This plan is accounted for in the Risk Management – Internal Service Fund. Interfund premiums are accounted for as internal activity receipts from other funds. The claims payable is an estimated liability based upon actual claims that have been submitted as well as actuarially determined claims incurred but not reported. Risk management coverage includes worker's compensation, property, general (tort) liability, medical malpractice, and automobile plans. At June 30, 2005, \$243.3 million is reported as the estimated claims payable for the risk management plan. This amount is discounted to present value at a rate of 3 percent. Undiscounted claims payable at June 30, 2005, is \$291.3 million. The estimated losses are based upon actual claims that have been submitted, as well as claims incurred but not reported. Changes in the balances of claims liabilities (dollars in thousands) during the current and prior fiscal years are as follows:

	<b>Balance</b>	<b>Current</b>	<b>Claim</b>	<b>Balance</b>
	<b>July 1,</b>	<b>Year Claims</b>	<b>Payments</b>	<b>June 30,</b>
		<b>and Changes</b>		
		<b>in Estimates</b>		
2004-2005	\$ 219,505	\$ 83,164	\$ (59,412)	\$ 243,257
2003-2004	\$ 189,185	\$ 80,445	\$ (50,125)	\$ 219,505

For workers' compensation, the Commonwealth assumes the full risk of claims filed. For tort, including general and automobile liability, liability is assumed at \$2,000,000 per occurrence. Medical malpractice liability is assumed at the maximum per occurrence recovery limit stated in Section 8.01-581.15 of the *Code of Virginia* (\$1,800,000 for the year ending June 30, 2005, increasing annually until 2008 when it will reach \$2,000,000 per occurrence). For property damage, Risk Management purchases \$500,000,000 of insurance with a \$2,500,000 per occurrence deductible for named windstorms, \$4,000,000 per occurrence deductible for floods, and a \$1,000,000 deductible for all other perils.

The Commonwealth has not had any insurance settlements exceed the coverage during the past three years.

The Virginia Port Authority (Nonmajor Component Unit) is partially self-insured for certain workers' compensation claims. The Authority maintains insurance coverage of \$5,000,000 per claim, but is obligated to pay the first \$1,000,000 of any individual's claims per incident. The Authority is also partially self-insured for employee health coverage. The Authority is responsible for actual claim costs up to \$75,000 per individual per calendar year. Insurance coverage is maintained for claims in excess of the individual employee limit and for aggregate claims in excess of \$3,866,745.

## B. Public Entity Risk Pools

The Commonwealth administers two types of public entity risk pools for the benefit of local governmental units: health care and risk management insurance. The Local Choice Health Care plan was established to make comprehensive health care insurance available to localities and political subdivisions at affordable rates and with stable premiums. During the fiscal year, there were 237 local government units participating in the pool. This includes 29 school districts, 30 counties, 87 cities/towns, and 91 other subdivisions. This program is accounted for in the Local Choice Health Care Enterprise Fund (nonmajor).

The Department of Human Resource Management, under Section 2.2-1204 of the *Code of Virginia*, has the authority to design, set rates, and administer

the Local Choice Health Care fund. The pool's standard contract period is one year. However, a member group may withdraw on the last day of any month with three month's written notice. Contributions are based on the current necessary contribution and the amortization of experience adjustments in the pool. At June 30, 2005, \$16.2 million is reported as the actuarially determined estimated claims payable for this fund based on claims incurred but not reported.

The actuarial liability is determined for the membership pool in total and then adjusted for each locality based on individual historic and demographic data. If the pool's assets were to be exhausted, the program participants would share the responsibility for any liabilities or deficits.

The Department of Treasury, Division of Risk Management administers risk management pools for public official and governmental liability in accordance with Section 2.2-1839 of the Code of Virginia. These pools were established to provide an economical low-cost, internally managed alternative to the commercial insurance market for the Commonwealth's political subdivisions. These risk programs are accounted for in the Risk Management Enterprise Fund (nonmajor). The pool is established subject to the approval of the Governor. It may be insurance, self-insurance, or any combination thereof, and must provide protection and legal defense against liability. Local participation is voluntary and open to any political subdivision. As of June 30, 2005, there were 527 units of local government in the pool. This includes 3 cities, 43 towns, and 34 counties. The balance includes a large variety of boards, commissions, authorities, and special districts.

The pool has a minimum membership period of one year. However, a member group can cancel their membership and withdraw from the plan on their coverage anniversary date or at the end of the fiscal year with thirty days notice.

The pool is actuarially valued annually and is considered sound. Investment income is considered in the anticipation of premium deficiencies. No excess insurance or reinsurance is provided, but a "stability fund" is incorporated into the actuarially determined required reserves. If, however, the plan assets and reserves were to be exhausted, the members would be responsible for any deficits or liabilities.

For the liability insurance pool, local participation is voluntary and open to any political subdivision. The risk assumed by the local public entity pool for member liability is \$1,000,000 per occurrence.

At June 30, 2005, \$10.5 million is reported as estimated claims payable for these programs. This figure is actuarially determined for the fund in total and is reported at gross and does not reflect possible reimbursements for insurance recoveries.

The following schedule (dollars in thousands) shows the changes in claims liabilities for the past two fiscal years.

	<b>Local Choice Health Care</b>		<b>Risk Management</b>	
	<b>June 30, 2005</b>	<b>June 30, 2004</b>	<b>June 30, 2005</b>	<b>June 30, 2004</b>
Unpaid Claims and Claim				
Adjustment Expenses at Beginning of Fiscal Year (1)	\$ 15,198	\$ 12,993	\$ 10,472	\$ 9,895
Incurred Claims and Claim Adjustment Expenses:				
Provision for Insured Events of the Current Fiscal Year	144,944	124,887	4,441	4,603
Changes in Provision for Insured Events of Prior Fiscal Years	-	-	(2,196)	(1,786)
Total Incurred Claims and Adjustment Expenses	144,944	124,887	2,245	2,817
Payments:				
Claims and Claim Adjustment Expenses Attributable to				
Insured Events of the Current Fiscal Year	143,930	122,682	227	161
Claims and Claim Adjustment Expenses Attributable to				
Insured Events of the Prior Fiscal Year	-	-	2,354	2,144
Total Payments	143,930	122,682	2,581	2,305
Change in Provision for Discounts	-	-	331	322
Total Unpaid Claims and Claim Adjustment Expenses at				
End of the Fiscal Year (Discounted)	\$ 16,212	\$ 15,198	\$ 10,467	\$ 10,729
Total Unpaid Claims and Claim Adjustment Expenses at				
End of the Fiscal Year (Undiscounted)	\$ 16,212	\$ 15,198	\$ 10,926	\$ 10,914

Note (1): Unpaid Claims and Claim Adjustment Expenses at Beginning of Fiscal Year for Risk Management excludes the amount for Commuter Rail due to reporting entity changes.

## 18. ACCOUNTS PAYABLE

The following table (dollars in thousands) summarizes Accounts Payable as of June 30, 2005.

	<u>Vendor</u>	<u>Salary/ Wage</u>	<u>Retainage</u>	<u>Other</u>	<u>Foundations (1)</u>	<u>Total</u>
<b>Primary Government:</b>						
General	\$ 117,692	\$ 97,927	\$ 125	\$ -	\$ -	\$ 215,744
Major Special Revenue Funds:						
Commonwealth Transportation	167,641	33,789	14,936	-	-	216,366
Federal Trust	74,348	14,662	1,752	3	-	90,765
Literary	196	-	-	-	-	196
Nonmajor Governmental Funds	55,118	24,300	5,874	2	-	85,294
Major Enterprise Funds:						
State Lottery	979	1,295	-	3,578	-	5,852
Virginia College Savings Plan	119	180	-	755	-	1,054
Pocahontas Parkway	108	-	-	-	-	108
Unemployment Compensation	-	99	-	-	-	99
Nonmajor Enterprise Funds	27,008	3,969	-	-	-	30,977
Internal Service Funds	34,926	6,023	-	5,078	-	46,027
Private Purpose	121	80	-	120	-	321
Pension Trust	378	1,048	-	23,321	-	24,747
Agency Funds	-	-	-	6,045	-	6,045
<b>Total Primary Government (2)</b>	<u>\$ 478,634</u>	<u>\$ 183,372</u>	<u>\$ 22,687</u>	<u>\$ 38,902</u>	<u>-</u>	<u>\$ 723,595</u>
<b>Discrete Component Units:</b>						
Virginia Housing Development Authority	\$ 46,570	\$ -	\$ -	\$ -	\$ -	\$ 46,570
Virginia Public School Authority	70	-	-	-	-	70
University of Virginia	66,422	60,945	7,401	38,573	27,275	200,616
Virginia Polytechnic Institute and State University	38,699	42,785	4,264	-	9,951	95,699
Virginia Commonwealth University	52,900	59,564	2,531	-	3,890	118,885
Nonmajor Component Units	105,443	114,684	13,883	5,119	19,462	258,591
<b>Total Component Units</b>	<u>\$ 310,104</u>	<u>\$ 277,978</u>	<u>\$ 28,079</u>	<u>\$ 43,692</u>	<u>\$ 60,578</u>	<u>\$ 720,431</u>

Note (1): Foundations represent FASB reporting entities defined in Note 1.B.

Note (2): Fiduciary liabilities of \$31,113 (dollars in thousands) are not included in the Government-wide Statement of Net Assets. In addition, Governmental Fund liabilities of \$56,360 (dollars in thousands) are included in the Government-wide Statement of Net Assets, but excluded from the above amounts.

## 19. OTHER LIABILITIES

The following table (dollars in thousands) summarizes Other Liabilities as of June 30, 2005.

	Primary Government				
	General	Commonwealth Transportation	Federal Trust	Nonmajor Governmental Funds	State Lottery
Lottery Prizes Payable	\$ -	\$ -	\$ -	\$ -	\$ 35,537
Due to Program Participants, Escrows, and Providers	-	-	-	-	-
Medicaid Payable	186,739	-	187,487	-	-
Family Access to Medical Insurance Security Payable	828	-	1,537	-	-
Accrued Interest Payable	-	-	-	-	-
Tax Refunds Payable	213,715	-	-	-	-
Other Liabilities	-	-	-	2,174	-
Deposits Pending Distribution	1,416	2,814	2	1,915	-
Car Tax Refund Payable	39,164	-	-	-	-
Matured Debt Payable	-	-	-	15	-
<b>Total Other Liabilities</b>	<b>\$ 441,862</b>	<b>\$ 2,814</b>	<b>\$ 189,026</b>	<b>\$ 4,104</b>	<b>\$ 35,537</b>

	Primary Government				
	Virginia College Savings Plan	Pocahontas Parkway (1)	Unemployment Compensation	Nonmajor Enterprise Funds	Internal Service Funds
Lottery Prizes Payable	\$ -	\$ -	\$ -	\$ -	\$ -
Due to Program Participants, Escrows, and Providers	4	-	20,291	-	-
Medicaid Payable	-	-	-	-	-
Family Access to Medical Insurance Security Payable	-	-	-	-	-
Accrued Interest Payable	-	3,421	-	-	-
Tax Refunds Payable	-	-	-	-	-
Other Liabilities	-	21,074	-	1,571	5,372
Deposits Pending Distribution	-	-	-	179	-
Car Tax Refund Payable	-	-	-	-	-
Matured Debt Payable	-	-	-	-	-
<b>Total Other Liabilities</b>	<b>\$ 4</b>	<b>\$ 24,495</b>	<b>\$ 20,291</b>	<b>\$ 1,750</b>	<b>\$ 5,372</b>

(Continued on next page)

Note (1): The \$21,074 (dollars in thousands) shown above represents an interfund liability to the Commonwealth Transportation Fund that will not be repaid within one year. This amount is reclassified to an internal balance on the Government-wide Statement of Net Assets.

**Primary Government (continued from previous page)**

	<b>Pension Trust Funds</b>	<b>Investment Trust Funds</b>	<b>Agency Funds</b>	<b>Total Primary Government (2)</b>
Lottery Prizes Payable	\$ -	\$ -	\$ -	\$ 35,537
Due to Program Participants, Escrows, and Providers	-	-	420,189	440,484
Medicaid Payable	-	-	-	374,226
Family Access to Medical Insurance Security Payable	-	-	-	2,365
Accrued Interest Payable	-	-	-	3,421
Tax Refunds Payable	-	-	-	213,715
Other Liabilities	1,354	147,468	20,471	199,484
Deposits Pending Distribution	-	-	29,448	35,774
Car Tax Refund Payable	-	-	-	39,164
Matured Debt Payable	-	-	-	15
<b>Total Other Liabilities</b>	<b>\$ 1,354</b>	<b>\$ 147,468</b>	<b>\$ 470,108</b>	<b>\$ 1,344,185</b>

Note (2): Fiduciary liabilities of \$618,930 (dollars in thousands) are not included in the Government-wide Statement of Net Assets. In addition, Governmental Fund liabilities of \$314,218 (dollars in thousands) are included in the Government-wide Statement of Net Assets, but excluded from the above amounts.

**Component Units**

	<b>Virginia Housing Development Authority</b>	<b>Virginia Public School Authority</b>	<b>University of Virginia</b>	<b>Virginia Polytechnic Institute &amp; State University</b>	<b>Virginia Commonwealth University</b>
Accrued Interest Payable	\$ 64,400	\$ 47,542	\$ -	\$ 258	\$ 3,909
Other Liabilities	-	376	20,101	24,314	93,850
Deposits Pending Distribution	-	-	254,871	13,480	26,743
Short-term Debt	-	-	29,940	-	25,000
Matured Debt Payable	3,208	-	-	-	-
Grants Payable	-	-	-	-	-
<b>Total Other Liabilities</b>	<b>\$ 67,608</b>	<b>\$ 47,918</b>	<b>\$ 304,912</b>	<b>\$ 38,052</b>	<b>\$ 149,502</b>

**Component Units**

	<b>Nonmajor Component Units</b>	<b>Total Component Units</b>
Accrued Interest Payable	\$ 42,569	\$ 158,678
Other Liabilities	57,749	196,390
Deposits Pending Distribution	11,903	306,997
Short-term Debt	12,845	67,785
Matured Debt Payable	-	3,208
Grants Payable	12,536	12,536
<b>Total Other Liabilities</b>	<b>\$ 137,602</b>	<b>\$ 745,594</b>

### Medicaid Payable

Medicaid Payable represents services rendered but not billed by providers and potential liability resulting from cost reports not settled as of year-end. Providers subject to cost settlement are paid in the interim based on established per diem or diagnosis related group rates for services.

The Department of Medical Assistance Services (DMAS) estimates, based on past experience, the total amount of Medicaid claims that will be paid from the Medicaid program in the future which relate to services provided before year-end. At June 30, 2005, the estimated liability related to Medicaid claims totaled \$374.2 million. Of this amount \$186.7 million is reflected in the General Fund (major) and \$187.5 million in the Federal Trust Special Revenue Fund (major).

### Family Access to Medical Insurance Security Payable

DMAS estimates the total amount of claims that will be paid from the Family Access to Medical Insurance Security program in the future which relate to services provided before year-end. At June 30, 2005, the estimated liability related to claims totaled \$2.37 million. Of this amount, \$0.83 million is reflected in the General Fund (major) and \$1.54 million in the Federal Trust Special Revenue Fund (major).

### Tax Refunds Payable

Tax refunds payable represent refunds due on individual tax returns filed for the calendar year ended December 31, 2004, and on business tax returns filed for corporate fiscal years ending on or before June 30, 2005. The individual tax return filing deadline is May 1 of each year for the preceding calendar year. The corporate tax return filing deadline is the 15th day of the fourth month following the close of the corporate fiscal year.

### Car Tax Refund Payable

During the year ended June 30, 1998, the General Assembly passed the Personal Property Tax Relief Act. Under the terms of this legislation, the Commonwealth will assume financial responsibility for the personal property taxes assessed by localities over a five-year period beginning in 1998. The amount reported on the balance sheet represents personal property taxes assessed by the localities before June 30, 2005, and paid by the Commonwealth after June 30, 2005. The majority of the amount pertains to the 2005 personal property taxes. However, some prior year reimbursements are also included due to delinquent taxpayer payments. The tax years and applicable rates are as follows:

2005	70.0%
2004	70.0%
2003	70.0%
2002	70.0%
2001	70.0%
2000	47.5%
1999	27.5%
1998	12.5%

Chapter 1 of Special Session 1 (2004) established a \$950 million limit on the amount the state would appropriate for personal property tax relief, beginning for tax year 2006. It further established that each county, city, and town would receive a fixed percentage of the \$950 million, with payments to begin on or after July 1, 2006 (fiscal year 2007).

### Short-term Debt

Various Higher Education Institutions' Foundations (Component Units) have lines of credit with banks. University of Virginia Foundations (Major Component Unit) report \$29.9 million and Nonmajor Component Unit Foundations report \$12.8 million. This short-term debt is for working capital, property acquisition, construction costs, and operating costs. Virginia Commonwealth University (Major Component Unit) reports \$25 million in a line of credit for working capital that will be repaid with a new bond.

The balance of Other Liabilities is spread among various other funds.

## 20. LONG-TERM LIABILITIES

Commonwealth bonds are issued pursuant to Section 9 of Article X of the Constitution of Virginia. Section 9(a) bonds have been issued to redeem previous debt obligations. Section 9(b) bonds have been authorized by the citizens of Virginia through bond referenda to finance capital projects. These bonds are retired through the use of State appropriations. Section 9(c) bonds are issued to finance capital projects which, when completed, will generate revenue to repay the debt. Section 9(a), 9(b), and 9(c) bonds are tax-supported general obligation bonds and are backed by the full faith, credit, and taxing power of the Commonwealth. No other long-term debt or obligations are backed by the full faith, credit, and taxing power of the Commonwealth.

Section 9(d) bonds are revenue bonds and are not backed by the full faith, credit and taxing power of the Commonwealth. These bonds are not general obligation bonds and are not deemed to constitute a legal liability of the Commonwealth. This debt may be supported by State appropriations in whole or in part, as in the case of certain debt of the VPA (Nonmajor Component Unit), VPBA (Primary Government), ITA (Nonmajor Component Unit), and VCBA (Nonmajor Component Unit). Other 9(d) revenue bonds are payable from general revenues of the component units, or from revenues of specific revenue-producing capital projects such as the teaching hospitals, dormitories, student centers, and dining halls at the various colleges and universities (Component Units). Additionally, the 9(d) Transportation Bonds (Primary Government) are payable solely from revenues or earnings, and other available sources of funds appropriated by the General

Assembly. The 9(d) Pocahontas Parkway Association Bonds (Primary Government) are special, limited obligations of the Association, secured by a gross revenue pledge and payable solely from revenues prior to payment of current expenses and from monies held in certain funds and accounts held in trust.

Certain 9(d) bonds are considered, with 9(a), 9(b), and 9(c) bonds, to be tax-supported debt of the Commonwealth. Tax-supported debt includes all bond issues and short-term debt supported by tax revenues (net of sinking fund requirements), for which debt service payments are made or are ultimately pledged to be made from general governmental funds.

Other 9(d) revenue bonds are considered debt not supported by taxes. For this debt, the Commonwealth has no direct or indirect pledge of tax revenues. However, in some cases, the Commonwealth has made a moral obligation pledge. A government's moral obligation pledge provides a deficiency make-up for bondholders should underlying project revenues prove insufficient. The mechanics involve funding a debt service reserve fund when the bonds are issued. If a revenue deficiency exists, reserve fund monies are used to pay bondholders. The issuer then informs the legislative body requesting that it replenish the reserve fund before subsequent debt service is due. The legislative body may, but is not legally required to, replenish the reserve fund. These bonds are considered to be moral obligation debt.

The following schedule presents the total long-term liabilities of the Commonwealth, and the portion of these amounts which are due within one year, as reported on the Government-wide Statement of Net Assets.

**Total Long-term Liabilities**  
June 30, 2005

<i>(Dollars in Thousands)</i>	<b>Balance At June 30</b>	<b>Amount Due Within One Year</b>
<b>Primary Government:</b>		
Governmental Activities:(1)		
<b>General Obligation Bonds: (2)</b>		
9(b) Transportation Facilities (3)	\$ 34,792	\$ 4,620
9(b) Public Facilities (3)	520,655	42,015
9(c) Parking Facilities (3)	11,040	1,035
9(c) Transportation Facilities (3)	90,545	10,775
Total General Obligation Bonds	<u>657,032</u>	<u>58,445</u>
<b>Non-General Obligation Bonds - 9(d):</b>		
Transportation Debt (3) (4)	1,788,274	126,740
Virginia Public Building Authority (3)	1,142,070	78,660
Total Non-General Obligation Bonds	<u>2,930,344</u>	<u>205,400</u>
<b>Other Long-term Obligations:</b>		
Pension Liability	621,969	-
Compensated Absences	313,896	167,829
Capital Lease Obligations	133,799	9,230
Regional Jail Financing Payable	15,030	1,655
Notes Payable	31,155	2,576
Installment Purchase Obligations	24,047	9,106
Industrial Development Authority Obligations	27,100	3,940
Other Liabilities	18,761	2,800
Total Other Long-term Obligations	<u>1,185,757</u>	<u>197,136</u>
Total Governmental Activities (3)	<u>4,773,133</u>	<u>460,981</u>
Business-type Activities: (1) (6)		
<b>Non-General Obligation Bonds - 9(d):</b>		
Pocahontas Parkway Association Bonds (3)	463,357	5,300
<b>Other Long-term Obligations:</b>		
Pension Liability	12,990	-
Compensated Absences	7,859	3,314
Installment Purchase Obligations	9,709	5,310
Tuition Benefits Payable	1,430,383	60,900
Lottery Prizes Payable	375,041	58,144
Total Other Long-term Obligations	<u>1,835,982</u>	<u>127,668</u>
Total Business-type Activities (3)	<u>2,299,339</u>	<u>132,968</u>
<b>Total Primary Government</b>	<u>7,072,472</u>	<u>593,949</u>

*(Continued on next page)*

**Total Long-term Liabilities**  
June 30, 2005  
(continued from previous page)

<i>(Dollars in Thousands)</i>	<b>Balance At June 30</b>	<b>Amount Due Within One Year</b>
<b>Component Units:</b>		
<b>General Obligation Bonds: (2)</b>		
Higher Education Fund - 9(c) Bonds (3)	296,963	28,984
<b>Non-General Obligation Bonds:</b>		
Higher Education Institutions - 9(d) (3) (6)	546,062	20,277
Virginia College Building Authority (3)	641,450	55,012
Innovative Technology Authority	8,635	700
Virginia Port Authority (3) (7)	408,168	15,419
Virginia Housing Development Authority (3) (8)	4,627,186	196,385
Virginia Resources Authority (3) (8)	1,286,295	45,775
Virginia Public School Authority (3) (6)	2,449,447	160,452
Hampton Roads Sanitation District Commission (6)	138,509	11,525
Virginia Equine Center Foundation (6)	15,540	220
Virginia Biotechnology Research Park Authority (3) (9)	67,335	2,975
Foundations (6) (10)	332,019	9,730
Total Non-General Obligation Bonds	<u>10,520,646</u>	<u>518,470</u>
<b>Other Long-term Obligations:</b>		
Pension Liability (5)	238,463	-
Compensated Absences	187,489	107,790
Capital Lease Obligations	46,272	4,118
Notes Payable (6)	1,139,395	406,717
Installment Purchase Obligations	85,614	10,870
Other Liabilities (6)	368,920	39,577
Total Other Long-term Obligations (Excluding Foundations)	<u>2,066,153</u>	<u>569,072</u>
<b>Other Long-term Obligations (Foundations): (6) (10)</b>		
Pension Liability	23,177	-
Compensated Absences	5,085	4,897
Capital Lease Obligations	372	143
Notes Payable	149,708	26,008
Installment Purchase Obligations	149	50
Trust and Annuity Obligations (11)	90,909	3,068
Other Liabilities	43,110	7,652
Total Other Long-term Obligations - Foundations	<u>312,510</u>	<u>41,818</u>
Total Other Long-term Obligations	<u>2,378,663</u>	<u>610,890</u>
<b>Total Component Units</b>	<u>13,196,272</u>	<u>1,158,344</u>
<b>Total Long-term Liabilities</b>	<u>\$ 20,268,744</u>	<u>\$ 1,752,293</u>

1. Pursuant to GASB Statement No. 34, governmental activities include Internal Service Funds. Business-type Activities are considered Enterprise Funds.
2. Total general obligation debt of the Commonwealth is \$954.0 million.
3. Amounts are net of any unamortized discounts, premiums, and deferrals.
4. This debt includes \$746.9 million that is not supported by taxes.
5. This includes pension obligations that do not relate to the Virginia Retirement System from Virginia Commonwealth University of \$2.8 million, Virginia Port Authority of \$3.5 million and Virginia Outdoors Foundation of \$30 thousand. It does not include pension obligations from fiduciary funds of \$1.8 million.
6. This debt is not supported by taxes.
7. This debt includes \$142.6 million that is not supported by taxes.
8. This debt is not supported by taxes; however, \$623.7 million from VHDA and \$695.1 million from VRA is considered moral obligation debt.
9. This debt includes \$12.7 million that is not supported by taxes.
10. Foundations represent FASB reporting entities defined in Note 1.B.
11. These generally represent split-interest agreements that represent donor contributed assets with the requirement that an annual distribution be made to the donor or specified beneficiary. The annual distributions are usually for a fixed dollar amount or a fixed percentage of the trust's fair market value. The present value of these commitments is reported as Trust and Annuity Obligations.

**Primary Government**

**Transportation Facilities Debt**

Transportation Facilities Bonds include \$34,791,565 of 9(b) general obligation bonds, \$90,545,384 of 9(c) general obligation bonds, and \$1,788,274,413 of 9(d) revenue bonds. Principal and interest requirements for the current year totaled \$219,776,410. The Section 9(b) transportation facilities bonds represent Powhite Refunding Bonds. The Section 9(c) Transportation Facilities Bonds were issued to fund the construction and improvement of the Omer L. Hirst - Adelard L. Brault Expressway and the George P. Coleman Bridge. The Section 9(d) Transportation Facilities Bonds were issued to fund the construction of State Route 28, U.S. Route 58, the Northern Virginia Transportation District Program, and the Oak Grove Connector (Chesapeake). On November 10, 2004, the Commonwealth Transportation Board issued \$89,400,000 of 9(d) Transportation Revenue Refunding Bonds Series 2004A and \$232,260,000 in Transportation Revenue Refunding Bonds Series 2004B. The Series 2004A bonds were issued to advance refund outstanding Series 1996A, Series 1999A, and Series 2001A bonds. The Series 2004B bonds were issued to advance refund outstanding Series 1996B, Series 1999B, and Series 2001B bonds. The interest rates for these bonds range from 2.00 percent to 7.25 percent and the issuance dates range from June 28, 1989, to November 10, 2004.

The following schedules detail the annual funding requirements necessary to amortize Transportation Facilities 9(b), 9(c) and 9(d) bonds:

**9(b) TRANSPORTATION FACILITIES BONDS  
Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 4,620,000	\$ 1,588,750	\$ 6,208,750
2007	4,885,000	1,357,750	6,242,750
2008	5,130,000	1,113,500	6,243,500
2009	5,415,000	857,000	6,272,000
2010	5,715,000	586,250	6,301,250
2011-2015	6,010,000	300,500	6,310,500
Less:			
Deferral on Debt Defeasance	(710,000)	-	(710,000)
Add:			
Unamortized Premium	3,726,565	-	3,726,565
<b>Total</b>	<b>\$ 34,791,565</b>	<b>\$ 5,803,750</b>	<b>\$ 40,595,315</b>

**9(c) TRANSPORTATION FACILITIES BONDS  
Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 10,775,117	\$ 3,957,561	\$ 14,732,678
2007	10,798,630	3,581,732	14,380,362
2008	10,844,756	3,191,150	14,035,906
2009	7,539,000	2,808,613	10,347,613
2010	4,590,000	2,618,763	7,208,763
2011-2015	26,680,000	9,385,475	36,065,475
2016-2020	17,825,000	3,248,469	21,073,469
2021-2025	3,295,000	168,869	3,463,869
Less:			
Unamortized Discount	(1,811,943)	-	(1,811,943)
Deferral on Debt Defeasance	(2,000,000)	-	(2,000,000)
Add:			
Unamortized Premium	2,009,824	-	2,009,824
<b>Total</b>	<b>\$ 90,545,384</b>	<b>\$ 28,960,632</b>	<b>\$ 119,506,016</b>

**9(d) TRANSPORTATION FACILITIES DEBT  
Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 126,740,000	\$ 82,005,549	\$ 208,745,549
2007	132,415,000	75,959,212	208,374,212
2008	138,860,000	69,453,683	208,313,683
2009	143,255,000	62,497,789	205,752,789
2010	153,970,000	55,139,429	209,109,429
2011-2015	526,030,000	178,871,997	704,901,997
2016-2020	327,518,820	82,998,713	410,517,533
2021-2025	152,675,875	22,487,275	175,163,150
2026-2030	27,897,169	1,002,000	28,899,169
2031-2035	3,541,804	-	3,541,804
Add:			
Accretion on Capital Appreciation Bonds	5,312,174	-	5,312,174
Less:			
Deferral on Debt Defeasance	(41,280,484)	-	(41,280,484)
Add:			
Unamortized Premium	91,339,056	-	91,339,056
<b>Total</b>	<b>\$ 1,788,274,414</b>	<b>\$ 630,415,647</b>	<b>\$ 2,418,690,061</b>

**Pocahontas Parkway Association Bonds**

The Pocahontas Parkway Association Route 895 Connector Toll Road Revenue Bonds, Senior Current Interest Bonds, Series 1998A were issued on July 9, 1998 in the amount of \$168,862,562. Bonds mature in annual installments on August 15 in the years 2005 through 2011, and 2026 through 2028. Interest is payable on each February 15 and August 15 beginning in 1999 at rates varying from 5.0 percent to 5.5 percent.

The Pocahontas Parkway Association Route 895 Connector Toll Road Revenue Bonds, Senior Capital Appreciation Bonds, Series 1998B were issued on July 9, 1998, in the principal amount of \$148,310,627 and the maturity value of \$690,200,000. Bonds mature in annual installments on August 15 in the years 2012 through 2025, and 2029 through 2035. The Senior Capital Appreciation Bonds were issued at a discount to yield, approximately, 5.50 percent to 5.95 percent. Principal accreted for the year ended June 30, 2005, was \$12,328,234.

The Pocahontas Parkway Association Route 895 Connector Toll Road Revenue Bonds, First Tier

Subordinate Capital Appreciation Bonds, Series 1998C were issued on July 9, 1998, in the principal amount of \$35,867,236 and the maturity value of \$137,300,000. Bonds mature in annual installments on August 15 in the years 2005 through 2035. The First Tier Subordinate Capital Appreciation Bonds were issued at a discount to yield, approximately, 5.40 percent to 6.25 percent. Principal accreted for the year ended June 30, 2005, was \$3,065,571.

The Second Tier Subordinate Toll Road Revenue Bond, Series 1998D was issued on July 9, 1998, in the principal amount of \$18,000,000 to the Commonwealth Transportation Board (CTB). The Series 1998D Bond was issued in exchange for \$18,000,000 loaned to the Association for paying certain non-construction costs of the Project, and shall mature on August 15, 2028. The Series 1998D Bond shall bear interest at a floating rate equal to the Commonwealth's Transportation Trust Fund Earnings Rate, compounded semiannually. The Series 1998D Bond shall bear interest from the date that amounts are advanced from the Series 1998D Bond Proceeds Account for application to non-construction costs of the Project on the amount of such advances until paid. Also earnings on the Series 1998D Bond Proceeds Account shall be transferred monthly to the Virginia Department of Transportation. The original proceeds disbursed for non-construction costs as of June 30, 2005, were \$17,989,424 and accrued interest was \$5,719,695. The average interest rate for fiscal year 2005 was 2.90 percent.

During the years 2002, 2004, and 2005, the Association issued non-interest bearing Second Tier Subordinate Bonds representing previously incurred operating expenses for which the Association was to reimburse the Commonwealth. These bonds, Series 2001A for \$443,386, Series 2004A for \$2,362,136, and Series 2005A for \$1,859,112, are issued on a parity in terms of payment with other Second Tier Subordinate Bonds and will be payable only after all payments of principal, accreted value, premium, if any, and interest on the Senior Bonds and First Tier Subordinate bonds then due have been paid.

The Route 895 Connector Toll Road Revenue Bonds are special limited obligations of the Association, secured by a gross revenue pledge and payable solely from revenues and other property included in the Trust Estate. The Association is a private, non-stock, nonprofit corporation and has no taxing powers. Neither the 1998, 2001, 2004, nor the 2005 Bonds are a debt of the Commonwealth, the Virginia Department of Transportation, the CTB, or any other agency, instrumentality or political subdivision of the Commonwealth, moral or otherwise. Neither the full faith and credit nor taxing power of the Commonwealth, is pledged to the payment of this debt.

The following schedule details the annual funding requirements necessary to repay the Series 1998A, 1998B, 1998C, 1998D, 2001A, 2004A and 2005A bonds:

<b>POCAHONTAS PARKWAY ASSOCIATION</b>				
<b>Debt Service Requirements to Maturity</b>				
<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>	
2006	\$ 5,300,000	\$ 9,046,250	\$	14,346,250
2007	8,000,000	8,841,250		16,841,250
2008	9,000,000	8,548,500		17,548,500
2009	10,100,000	8,199,375		18,299,375
2010	11,300,000	7,797,750		19,097,750
2011-2015	87,800,000	33,245,000		121,045,000
2016-2020	126,300,000	32,037,500		158,337,500
2021-2025	165,900,000	32,037,500		197,937,500
2026-2030	243,662,689	16,304,750		259,967,439
2031-2035	273,000,000	-		273,000,000
2036-2040	79,500,000	-		79,500,000
Less:				
Unamortized Discount	(848,512)	-		(848,512)
Imputed interest bond discount	(3,345,310)	3,345,310		-
Unaccreted Capital Appreciation Bonds	(552,311,732)	-		(552,311,732)
Total	<u>\$ 463,357,135</u>	<u>\$ 159,403,185</u>		<u>\$ 622,760,320</u>

### Public Facilities Bonds

Section 9(b) general obligation bonds consist of Public Facilities Bonds, Series 1993B, Series 1996, Series 1996 refunding, Series 1997, Series 1998 refunding, Series 1998, Series 1999A, Series 2002 Refunding, Series 2003A Refunding, Series 2004A and Series 2004B refunding. All bonds were issued to fund construction projects for higher educational institutions, mental health, and/or park facilities. The Series 2003A bonds were issued to advance refund outstanding Series 1993A and B, Series 1994, and Series 1996 bonds. The Series 2004B bonds were issued to advance refund outstanding Series 1997, Series 1998, and Series 1999A bonds. Principal and interest requirements for the current year totaled \$64,224,739. The interest rates for all bonds range from 2.0 percent to 5.65 percent and the issuance dates range from June 1, 1996, to November 1, 2004. The following schedule details the annual funding requirements necessary to repay these bonds:

**9(b) PUBLIC FACILITIES BONDS**  
**Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 42,015,000	\$ 24,180,901	\$ 66,195,901
2007	41,825,000	22,247,611	64,072,611
2008	39,550,000	20,235,849	59,785,849
2009	41,470,000	18,337,686	59,807,686
2010	41,205,000	16,395,943	57,600,943
2011-2015	188,695,000	52,177,610	240,872,610
2016-2020	70,105,000	17,742,650	87,847,650
2021-2025	39,755,000	4,345,450	44,100,450
Less:			
Deferral on Debt Defeasance	(11,812,125)	-	(11,812,125)
Add:			
Unamortized Premium	27,847,568	-	27,847,568
<b>Total</b>	<b>\$ 520,655,443</b>	<b>\$ 175,663,700</b>	<b>\$ 696,319,143</b>

**Parking Facilities Bonds**

Section 9(c) general obligation bonds consist of Parking Facilities Bonds, Series 1996, 2002 Refunding, 2003A Refunding and 2004A. The Series 1996 bond was issued to fund the renovation of the Seventh and Marshall Street parking deck. The Series 2002 and 2003A bonds were issued to advance refund outstanding Series 1996 and Series 1993 Refunding bonds. The Series 2004A bond was issued to fund the renovation of the Ninth and Franklin Street parking deck. The interest rates for these bonds range from 2.5 percent to 5.7 percent and the issuance dates range from June 6, 1996, to August 1, 2004. Current year principal and interest requirements totaled \$1,503,908.

The following schedule details the annual funding requirements necessary to repay these bonds:

**9(c) PARKING FACILITIES BONDS**  
**Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 1,034,572	\$ 521,623	\$ 1,556,195
2007	1,075,042	469,276	1,544,318
2008	1,148,715	414,886	1,563,601
2009	1,000,426	356,776	1,357,202
2010	1,046,985	307,004	1,353,989
2011-2015	2,178,102	990,655	3,168,757
2016-2020	1,525,000	597,500	2,122,500
2021-2025	1,525,000	181,200	1,706,200
Less:			
Deferral on Debt Defeasance	(357,000)	-	(357,000)
Add:			
Unamortized Premium	863,586	-	863,586
<b>Total</b>	<b>\$ 11,040,428</b>	<b>\$ 3,838,920</b>	<b>\$ 14,879,348</b>

**Virginia Public Building Authority**

Virginia Public Building Authority (VPBA ) Section 9(d) bonds consist of Series 1992B, 1995A, 1996A refunding, 1997A, 1998A refunding, 1998B, 1999A, 1999B, 2000A, 2001A, 2002A, 2003A refunding, 2004A refunding, 2004B, 2004C refunding, 2004D refunding, 2005A refunding, and 2005B refunding. All bonds were issued for the purpose of constructing, improving, furnishing, maintaining, and acquiring public buildings

for the use of the Commonwealth and also to reimburse localities, regional jail authorities or other combination of localities under the Regional Jail Financing Program. The Series 2004C and 2005A bonds were issued to refinance certain capital lease obligations of the Commonwealth. The Series 2004D bonds were issued to advance refund outstanding Series 1997A, Series 1999B, and Series 2000A bonds. The Series 2005B bonds were issued to advance refund outstanding Series 1996A, Series 1998B, and Series 1999A bonds. The interest rates for all bonds range from 2.5 percent to 6.6 percent and the issuance dates range from June 15, 1992, to May 5, 2005. Current year principal and interest requirements totaled \$101,780,347. The following schedule details the annual funding requirements necessary to repay these bonds:

**9(d) VIRGINIA PUBLIC BUILDING AUTHORITY BONDS**  
**Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 78,660,000	\$ 47,065,929	\$ 125,725,929
2007	77,835,000	45,668,886	123,503,886
2008	86,300,000	42,624,916	128,924,916
2009	90,965,000	39,273,415	130,238,415
2010	94,585,000	35,611,480	130,196,480
2011-2015	408,135,000	117,861,516	525,996,516
2016-2020	224,380,000	40,305,017	264,685,017
2021-2025	76,495,000	7,912,075	84,407,075
Less:			
Unamortized Discount	(11,371,528)	-	(11,371,528)
Deferral on Debt Defeasance	(36,510,459)	-	(36,510,459)
Plus:			
Unamortized Premium	52,596,495	-	52,596,495
<b>Total</b>	<b>\$ 1,142,069,508</b>	<b>\$ 376,323,234</b>	<b>\$ 1,518,392,742</b>

**Regional Jail Financing Program**

The Regional Jail Financing Program of the Commonwealth of Virginia Treasury Board was created during the 1993 Session of the General Assembly to establish a method of reimbursing localities, regional jail authorities or other combination of localities for a portion of the capital and financing costs of a jail project, made pursuant to Sections 53.1-80, 53.1-81, or 53.1-82 of the *Code of Virginia*. The General Assembly, upon recommendation from the Department of Planning and Budget, may determine to reimburse localities for approved capital costs over time through a contractual Reimbursement Agreement between the localities or authority and the Treasury Board. The Board of Corrections determines the amount of reimbursable capital costs. If approved for reimbursement over time, the Treasury Board determines the amount of reimbursable financing costs and calculates the periodic reimbursement payments.

In 1996, the General Assembly adopted legislation that authorized funding of jail project reimbursements through bonds issued by the Virginia Public Building Authority (VPBA). As of June 30, 1998, all future jail reimbursements were approved for funding through the VPBA as opposed to the Treasury Board. All reimbursements, whether up front or over time, are subject to appropriation by the General Assembly.

The following schedule details the annual funding requirements necessary to repay these obligations:

REGIONAL JAILS FINANCING Financial Obligations to Maturity			
Calendar Year Obligations	Capital Costs	Financing Costs	Total
2006	\$ 1,655,357	\$ 981,369	\$ 2,636,726
2007	1,681,599	951,891	2,633,490
2008	1,712,928	919,166	2,632,094
2009	1,749,353	884,436	2,633,789
2010	1,785,867	847,422	2,633,289
2011-2015	6,444,840	1,653,323	8,098,163
Total	<u>\$ 15,029,944</u>	<u>\$ 6,237,607</u>	<u>\$ 21,267,551</u>

### Industrial Development Authority Obligations

In fiscal year 2002, the Newport News Industrial Development Authority (IDA) issued Section 9(d) revenue bonds to pay a portion of the cost of construction and equipping of the Virginia Advanced Shipbuilding and Carrier Integration Center for use by the Newport News Shipbuilding and Dry Dock Company. The Commonwealth's obligation is set out in a payment agreement between Newport News IDA and the Treasury Board, in which the Treasury Board agrees to make payments equal to the debt service from amounts appropriated by the General Assembly. The interest rates for these bonds range from 2.75 percent to 5.03 percent and the issue date is July 27, 2000. Current year principal and interest requirements totaled \$5,310,682. The following schedule details the annual funding requirements necessary to repay these bonds:

NEWPORT NEWS INDUSTRIAL DEVELOPMENT AUTHORITY Debt Service Requirements to Maturity			
Maturity	Principal	Interest	Total
2006	\$ 3,940,000	\$ 1,352,190	\$ 5,292,190
2007	4,150,000	1,144,390	5,294,390
2008	4,370,000	920,545	5,290,545
2009	4,615,000	678,288	5,293,288
2010	4,875,000	417,313	5,292,313
2011-2015	5,150,000	141,625	5,291,625
Total	<u>\$ 27,100,000</u>	<u>\$ 4,654,351</u>	<u>\$ 31,754,351</u>

### Component Units

#### Higher Education Institution Bonds

Higher Education Institution Bonds are comprised of both 9(c) general obligation bonds and 9(d) revenue bonds. Section 9(d) bonds are from several sources as shown on the following schedule (dollars in thousands):

College and university bonds backed by pledge of general revenue or revenue from specific revenue-producing capital projects \$ 445,392

College and university debt backed exclusively by pledged revenues of an institution 100,670

Total Higher Education Institution 9(d) debt \$ 546,062

The interest rates for these bonds range from 1.5 percent to 9.25 percent and the issuance dates range from June 30, 1979 to November 1, 2004. The following schedules detail the annual funding requirements necessary to amortize Higher Education Institution 9(c) and 9(d) bonds:

9(c) HIGHER EDUCATION INSTITUTION BONDS Debt Service Requirements to Maturity			
Maturity	Principal	Interest	Total
2006	\$ 29,095,311	\$ 14,347,869	\$ 43,443,180
2007	28,701,328	13,083,943	41,785,271
2008	29,706,529	11,795,771	41,502,300
2009	29,139,574	10,466,207	39,605,781
2010	28,023,015	9,216,834	37,239,849
2011-2015	98,233,898	28,806,163	127,040,061
2016-2020	50,520,000	9,795,913	60,315,913
2021-2025	17,300,000	1,788,019	19,088,019
Less:			
Unamortized Discount	(1,142,210)	-	(1,142,210)
Deferral on Debt Defeasance	(12,615,000)	-	(12,615,000)
Total	<u>\$ 296,962,445</u>	<u>\$ 99,300,719</u>	<u>\$ 396,263,164</u>

9(d) HIGHER EDUCATION INSTITUTION BONDS Debt Service Requirements to Maturity			
Maturity	Principal	Interest	Total
2006	\$ 21,182,472	\$ 24,526,475	\$ 45,708,947
2007	25,375,721	23,561,956	48,937,677
2008	25,989,067	22,584,065	48,573,132
2009	22,107,515	21,518,699	43,626,214
2010	19,171,067	20,623,339	39,794,406
2011-2015	124,862,485	87,306,227	212,168,712
2016-2020	92,103,841	60,679,199	152,783,040
2021-2025	73,783,876	39,688,935	113,472,811
2026-2030	44,925,000	25,054,675	69,979,675
2031-2035	106,825,000	9,885,875	116,710,875
Less:			
Deferral on Debt Defeasance	(10,264,100)	-	(10,264,100)
Total	<u>\$ 546,061,944</u>	<u>\$ 335,429,445</u>	<u>\$ 881,491,389</u>

**9(d) VIRGINIA COLLEGE BUILDING AUTHORITY BONDS**  
Debt Service Requirements to Maturity

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 53,460,000	\$ 27,850,451	\$ 81,310,451
2007	54,375,000	26,946,250	81,321,250
2008	46,200,000	24,369,944	70,569,944
2009	41,045,000	22,168,894	63,213,894
2010	34,495,000	20,171,725	54,666,725
2011-2015	136,070,000	80,417,235	216,487,235
2016-2020	149,640,000	43,696,350	193,336,350
2021-2025	96,295,000	10,924,448	107,219,448
Less:			
Deferral on Debt Defeasance	(4,631,000)	-	(4,631,000)
Add:			
Unamortized Premium	34,500,760	-	34,500,760
Total	<u>\$ 641,449,760</u>	<u>\$ 256,545,297</u>	<u>\$ 897,995,057</u>

Various Higher Education Institutions' Foundations (Component Units) have bonds outstanding as of year-end. The purpose of a majority of these bonds is for construction, property acquisition, and defeasance of prior debt. Many principal and interest payments are to banks or industrial development authorities located throughout the Commonwealth. The following schedule details the future principal payments:

**HIGHER EDUCATION INSTITUTIONS' FOUNDATIONS' BONDS (1)**  
Debt Service Requirements to Maturity

<i>Maturity</i>	<i>Principal</i>
2006	\$ 9,729,824
2007	5,641,709
2008	5,881,160
2009	6,039,046
2010	6,179,045
Thereafter	298,548,247
Total	<u>\$ 332,019,031</u>

Note (1): Foundations represent FASB reporting entities defined in Note 1.B.

**Innovative Technology Authority**

The Innovative Technology Authority (ITA) has issued Taxable Lease Revenue Bonds, Series 1989, and Series 1997 refunding. The Series 1989 bonds were issued to cover a portion of the costs related to the construction of a software development center and office building. Series 1997 bonds were issued to advance refund \$11.2 million of the outstanding 1989 bonds.

The 1989 bonds had an average interest rate of 10.3 percent and the 1997 bonds have an average interest rate of 7.4 percent. The bonds were issued on March 1, 1989, and May 1, 1997, respectively. The following schedule details the annual funding requirements necessary to amortize ITA bonds:

**9(d) INNOVATIVE TECHNOLOGY AUTHORITY BONDS**  
Debt Service Requirements to Maturity

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 700,000	\$ 641,855	\$ 1,341,855
2007	790,000	591,525	1,381,525
2008	875,000	534,013	1,409,013
2009	855,000	470,050	1,325,050
2010	935,000	407,208	1,342,208
2011-2015	4,480,000	867,809	5,347,809
Total	<u>\$ 8,635,000</u>	<u>\$ 3,512,460</u>	<u>\$ 12,147,460</u>

**Virginia Port Authority**

The Virginia Port Authority (VPA) has issued Section 9(d) revenue bonds and notes pursuant to powers provided to its Board of Commissioners by the *Code of Virginia*. The interest rates for these bonds range from 2.7 percent to 5.75 percent and the issuance dates range from October 23, 1996, to April 14, 2005. Series 1998 bonds were issued to advance refund \$71.0 million of the outstanding 1988 bonds. The following schedule details the annual funding requirements necessary to amortize VPA bonds:

**9(d) VIRGINIA PORT AUTHORITY DEBT**  
Debt Service Requirements to Maturity

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 15,240,000	\$ 19,575,132	\$ 34,815,132
2007	17,715,000	19,607,230	37,322,230
2008	19,625,000	18,641,788	38,266,788
2009	20,660,000	17,589,008	38,249,008
2010	11,120,000	16,767,173	27,887,173
2011-2015	64,615,000	74,546,866	139,161,866
2016-2020	73,290,000	55,526,892	128,816,892
2021-2025	86,885,000	35,009,096	121,894,096
2026-2030	76,700,000	11,359,178	88,059,178
2031-2035	16,580,000	1,258,047	17,838,047
Plus:			
Unamortized Premium	5,738,140	-	5,738,140
Total	<u>\$ 408,168,140</u>	<u>\$ 269,880,410</u>	<u>\$ 678,048,550</u>

**Virginia Housing Development Authority**

The Virginia Housing Development Authority (VHDA) issued Section 9(d) revenue bonds. The interest rates for these bonds range from 3.59 percent to 8.18 percent and the origination dates range from June 30, 1982, to June 14, 2005. The following schedule details the annual funding requirements necessary to amortize these bonds:

9(d) VIRGINIA HOUSING DEVELOPMENT AUTHORITY BONDS  
Debt Service Requirements to Maturity

Maturity	Principal	Interest	Total
2006	\$ 196,385,000	\$ 220,378,369	\$ 416,763,369
2007	144,745,000	226,821,042	371,566,042
2008	172,490,000	219,461,791	391,951,791
2009	189,640,000	211,891,184	401,531,184
2010	195,445,000	203,440,518	398,885,518
2011-2015	957,245,000	876,953,378	1,834,198,378
2016-2020	860,955,000	634,453,758	1,495,408,758
2021-2025	671,830,000	423,740,052	1,095,570,052
2026-2030	490,737,264	253,054,212	743,791,476
2031-2035	455,885,098	114,749,040	570,634,138
2036-2040	164,790,000	43,085,335	207,875,335
2041-2045	109,660,000	12,788,305	122,448,305
2046-2050	15,800,000	199,931	15,999,931
Add:			
Unamortized Premium	3,645,000	-	3,645,000
Less:			
Unamortized Discount	(2,066,000)	-	(2,066,000)
Total	<u>\$ 4,627,186,362</u>	<u>\$ 3,441,016,915</u>	<u>\$ 8,068,203,277</u>

Virginia Resources Authority

The Virginia Resources Authority (VRA) issued Section 9(d) revenue bonds. The interest rates for these bonds range from 1.36 percent to 8.70 percent and the origination dates range from December 1, 1985, to June 30, 2005. The following schedule details the annual funding requirements necessary to amortize these bonds:

9(d) VIRGINIA RESOURCES AUTHORITY BONDS  
Debt Service Requirements to Maturity

Maturity	Principal	Interest	Total
2006	\$ 45,775,000	\$ 53,843,125	\$ 99,618,125
2007	48,465,000	54,595,408	103,060,408
2008	52,660,000	52,758,026	105,418,026
2009	55,790,000	50,675,112	106,465,112
2010	56,940,000	48,405,070	105,345,070
2011-2015	327,845,000	197,865,199	525,710,199
2016-2020	293,395,000	126,268,530	419,663,530
2021-2025	235,705,000	63,196,700	298,901,700
2026-2030	124,905,000	26,049,288	150,954,288
2031-2035	74,200,000	12,039,774	86,239,774
2036-2040	10,520,000	258,366	10,778,366
Add:			
Unamortized Premium	42,551,716	-	42,551,716
Less:			
Unamortized Discounts and Issuance Expenses	(29,650,886)	-	(29,650,886)
Unaccrued Capital Appreciation			
Bonds	(52,805,581)	-	(52,805,581)
Total	<u>\$ 1,286,295,249</u>	<u>\$ 685,954,598</u>	<u>\$ 1,972,249,847</u>

Virginia Public School Authority

The Virginia Public School Authority (VPSA) issued Section 9(d) revenue bonds. The interest rates for these bonds range from 2.00 percent to 6.00 percent and the origination dates range from July 1, 1994, to May 25, 2005. The following schedule details the annual funding requirements necessary to amortize these bonds:

9(d) VIRGINIA PUBLIC SCHOOL AUTHORITY BONDS  
Debt Service Requirements to Maturity

Maturity	Principal	Interest	Total
2006	\$ 161,880,000	\$ 113,932,845	\$ 275,812,845
2007	175,975,000	109,258,889	285,233,889
2008	165,280,000	100,887,713	266,167,713
2009	165,045,000	92,656,909	257,701,909
2010	160,090,000	84,554,463	244,644,463
2011-2015	706,265,000	309,281,553	1,015,546,553
2016-2020	555,972,063	148,301,869	704,273,932
2021-2025	285,205,000	43,190,944	328,395,944
2026-2030	62,425,000	6,325,825	68,750,825
2031-2035	1,195,000	26,888	1,221,888
Less:			
Deferral on Debt Defeasance	(60,016,000)	-	(60,016,000)
Plus:			
Unamortized Premium	70,130,646	-	70,130,646
Total	<u>\$ 2,449,446,709</u>	<u>\$ 1,008,417,898</u>	<u>\$ 3,457,864,607</u>

Hampton Roads Sanitation District Commission

The Hampton Roads Sanitation District Commission issued bonds under a Master Trust Indenture and a Trust Agreement dated December 1, 1993, and March 1, 2003. The interest cost for these bonds ranges from 2.5 percent to 4.75 percent. The following schedule details the annual funding requirements necessary to amortize these bonds:

HAMPTON ROADS SANITATION DISTRICT COMMISSION  
Debt Service Requirements to Maturity

Maturity	Principal	Interest	Total
2006	\$ 11,525,000	\$ 4,358,000	\$ 15,883,000
2007	11,919,000	3,941,000	15,860,000
2008	8,339,000	4,678,000	13,017,000
2009	8,617,000	4,492,000	13,109,000
2010	8,941,000	4,102,000	13,043,000
2011-2015	50,925,000	13,872,000	64,797,000
2016-2020	19,499,000	4,667,000	24,166,000
2021-2025	13,454,000	1,863,000	15,317,000
2026-2030	5,290,000	201,000	5,491,000
Total	<u>\$ 138,509,000</u>	<u>\$ 42,174,000</u>	<u>\$ 180,683,000</u>

### Virginia Equine Center Foundation

The Virginia Equine Center Foundation issued Series 2001 IDA of Rockbridge County Virginia Horse Center Revenue Bonds. Coupon interest rates range from 6.125 percent to 8.0 percent.

**VIRGINIA EQUINE CENTER FOUNDATION**  
**Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 780,000	\$ 1,050,162	\$ 1,830,162
2007	600,000	1,011,665	1,611,665
2008	640,000	971,414	1,611,414
2009	680,000	928,467	1,608,467
2010	725,000	882,854	1,607,854
2011-2015	12,115,000	5,563,590	17,678,590
Total	<u>\$ 15,540,000</u>	<u>\$ 10,408,152</u>	<u>\$ 25,948,152</u>

The above listed debt of the Virginia Equine Center Foundation is not an obligation of the Commonwealth, and neither the full faith and credit nor taxing power of the Commonwealth is pledged to the payment of this debt.

### Virginia Biotechnology Research Park Authority

The Virginia Biotechnology Research Park Authority issued Series 1996, 1998, 1999A, 1999B, and 2001 Commonwealth of Virginia Lease Revenue bonds. Coupon interest rates range from 4.0 percent to 6.4 percent. The Series 1996 Virginia Biotechnology Research Park Authority Lease Revenue Bonds were refinanced with VPBA Series 2005A bonds on March 1, 2005.

**VIRGINIA BIOTECHNOLOGY RESEARCH PARK AUTHORITY**  
**Debt Service Requirements to Maturity**

<i>Maturity</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>
2006	\$ 2,975,000	\$ 3,303,415	\$ 6,278,415
2007	3,130,000	3,155,879	6,285,879
2008	3,280,000	3,009,030	6,289,030
2009	3,440,000	2,855,894	6,295,894
2010	3,610,000	2,692,851	6,302,851
2011-2015	21,225,000	10,420,435	31,645,435
2016-2020	20,185,000	4,771,350	24,956,350
2021-2025	9,040,000	457,750	9,497,750
Plus:			
Unamortized Premium	449,996	-	449,996
Total	<u>\$ 67,334,996</u>	<u>\$ 30,666,604</u>	<u>\$ 98,001,600</u>

Total principal outstanding at June 30, 2005, on all Component Unit bonds amounted to \$10.8 billion.

The following schedule summarizes the changes in long-term liabilities:

Schedule of Changes in Long-term Debt and Obligations (1) (2)

(Dollars in Thousands)

	Balance July 1, 2004 as restated	Issuances and Other Increases	Retirements and Other Decreases	Subtotal June 30, 2005
<b>Primary Government</b>				
<b>Governmental Activities:</b>				
<b>Long-term Debt Bearing the Pledge of the Full Faith and Credit of the Commonwealth:</b>				
General Obligation Bonds - 9(b) and 9(c):				
Public Facilities Bonds (3) (4)	\$ 389,219	\$ 265,090	\$ (133,654)	\$ 520,655
Parking Facilities Bonds (3) (4)	6,367	5,756	(1,083)	11,040
Transportation Facilities Bonds (3) (4)	140,800	1,096	(16,559)	125,337
<b>Total General Obligation Bonds</b>	<b>536,386</b>	<b>271,942</b>	<b>(151,296)</b>	<b>657,032</b>
<b>Long-term Debt / Obligations Not Bearing the Pledge of the Full Faith and Credit of the Commonwealth:</b>				
<b>Debt:</b>				
Non-General Obligation Bonds - 9(d)				
Transportation Facilities Bonds (3) (4)	1,909,581	350,951	(472,258)	1,788,274
Virginia Public Building Authority Bonds (3) (4)	887,828	540,312	(286,070)	1,142,070
Regional Jails Financing Payable	16,654	-	(1,624)	15,030
Industrial Development Authority Obligations	30,845	-	(3,745)	27,100
Installment Purchase Obligations	29,228	5,705	(10,886)	24,047
Notes Payable - Virginia Public Broadcasting Board	17,950	-	(2,175)	15,775
Notes Payable - Transportation	12,325	-	-	12,325
Notes Payable - Aviation	3,341	-	(286)	3,055
<b>Obligations:</b>				
Compensated Absences	304,839	15,673	(6,616)	313,896
Capital Lease Obligations (5)	235,839	1,089	(103,129)	133,799
Pension Liability	542,471	79,498	-	621,969
Other	20,928	376	(2,543)	18,761
<b>Total Long-term Debt / Obligations Not Bearing the Pledge of the Full Faith and Credit of the Commonwealth</b>	<b>4,011,829</b>	<b>993,604</b>	<b>(889,332)</b>	<b>4,116,101</b>
<b>Total Governmental Activities</b>	<b>4,548,215</b>	<b>1,265,546</b>	<b>(1,040,628)</b>	<b>4,773,133</b>
<b>Business-type Activities:</b>				
<b>Long-term Debt / Obligations Not Bearing the Pledge of the Full Faith and Credit of the Commonwealth:</b>				
<b>Debt:</b>				
Non-General Obligation Bonds - 9(d)				
Pocahontas Parkway Association Bonds (3)	447,372	15,985	-	463,357
Installment Purchase Obligations	12,475	2,003	(4,769)	9,709
<b>Obligations:</b>				
Compensated Absences	7,852	4,149	(4,142)	7,859
Pension Liability	11,601	1,389	-	12,990
Lottery Prizes Payable	398,195	9,198	(32,352)	375,041
Tuition Benefits Payable	1,157,712	311,191	(38,520)	1,430,383
<b>Total Business-type Activities</b>	<b>2,035,207</b>	<b>343,915</b>	<b>(79,783)</b>	<b>2,299,339</b>
<b>Total Primary Government</b>	<b>\$ 6,583,422</b>	<b>\$ 1,609,461</b>	<b>\$ (1,120,411)</b>	<b>\$ 7,072,472</b>
<b>Component Units</b>				
<b>Long-term Debt Bearing the Pledge of the Full Faith and Credit of the Commonwealth:</b>				
General Obligation Bonds - Higher Education 9(c) (3)	\$ 316,923	\$ 109,554	\$ (129,514)	\$ 296,963
<b>Long-term Debt / Obligations Not Bearing the Pledge of the Full Faith and Credit of the Commonwealth:</b>				
<b>Debt:</b>				
Bonds (3) (4)	9,340,756	2,568,649	(1,720,778)	10,188,627
Installment Purchase Obligations	25,227	72,416	(12,029)	85,614
Capital Lease Obligations	44,123	7,385	(5,236)	46,272
Notes Payable (8)	858,030	485,174	(203,809)	1,139,395
<b>Obligations:</b>				
Compensated Absences	182,306	121,916	(116,733)	187,489
Pension Liability	220,290	20,944	(2,771)	238,463
Trust and Annuity Obligations	-	-	-	-
Other (6)	291,564	91,429	(14,073)	368,920
<b>Total Component Units</b>	<b>\$ 11,279,219</b>	<b>\$ 3,477,467</b>	<b>\$ (2,204,943)</b>	<b>\$ 12,551,743</b>

<u>Foundations (7)</u>	<u>Balance June 30, 2005</u>	<u>Due Within One Year</u>
\$ -	\$ 520,655	\$ 42,015
-	11,040	1,035
-	125,337	15,395
-	<u>657,032</u>	<u>58,445</u>
-	1,788,274	126,740
-	1,142,070	78,660
-	15,030	1,655
-	27,100	3,940
-	24,047	9,106
-	15,775	2,290
-	12,325	-
-	3,055	286
-	313,896	167,829
-	133,799	9,230
-	621,969	-
-	18,761	2,800
-	<u>4,116,101</u>	<u>402,536</u>
-	<u>4,773,133</u>	<u>460,981</u>
-	463,357	5,300
-	9,709	5,310
-	7,859	3,314
-	12,990	-
-	375,041	58,144
-	1,430,383	60,900
-	<u>2,299,339</u>	<u>132,968</u>
\$ -	<u>\$ 7,072,472</u>	<u>\$ 593,949</u>
\$ -	\$ 296,963	\$ 28,984
332,019	10,520,646	518,470
149	85,763	10,920
372	46,644	4,261
149,708	1,289,103	432,725
5,085	192,574	112,687
23,177	261,640	-
90,909	90,909	3,068
43,110	412,030	47,229
<u>\$ 644,529</u>	<u>\$ 13,196,272</u>	<u>\$ 1,158,344</u>

- (1) Pursuant to GASB Statement No. 34, governmental activities include Internal Service Funds. Business-type Activities are considered Enterprise Funds.
- (2) Payments on bonded debt that pertain to the Commonwealth's governmental activities are made through the debt service funds. Payments for installment purchases, compensated absences, capital leases, pension, and other obligations that pertain to the Commonwealth's governmental activities are made through the general and special revenue funds. Internal service funds predominantly serve the governmental funds. Accordingly, long-term liabilities for these funds are included as part of the total for governmental activities. Enterprise funds, or business-type activities, are self-supporting funds. Accordingly, long-term liabilities are paid from each respective fund.
- (3) Amounts are net of any unamortized discounts, premiums, and deferrals.
- (4) The beginning balance has been increased from the prior year to reflect unamortized bond premium liability.
- (5) The beginning balance has been increased from the prior year to reflect restatement of capital lease obligations.
- (6) The beginning balance has been decreased from the prior year by a higher education component unit to reflect a restatement.
- (7) Foundations represent FASB reporting entities defined in Note 1.B.
- (8) The beginning balance has been increased from the prior year to reflect reclassifications.

## Bond Defeasance

### Primary Government

In November 2004, the Commonwealth issued \$170,530,000 General Obligation Refunding Bonds, Series 2004B Refunding, pursuant to Sections 9(b) and 9(c) of Article X of the Constitution, with a true interest cost (TIC) of 3.53 percent to advance refund \$173,115,000 of certain outstanding bonds. The bonds that were refunded include \$34,645,000 of outstanding Higher Education Institution Bonds, Series 1997, \$7,150,000 of outstanding Higher Education Institution Bonds, Series 1998, \$15,975,000 of outstanding Higher Education Institution Bonds, Series 1999, \$31,735,000 of outstanding Higher Education Institution Refunding Bonds, Series 2001, \$45,990,000 of outstanding Public Facilities Bonds, Series 1997, \$28,080,000 of outstanding Public Facilities Bonds, Series 1998, and \$9,540,000 of outstanding Public Facilities Bonds, Series 1999. The net proceeds from the sale of the Refunding Bonds of \$187,378,800 (after payment of underwriter's fees and other issuance costs) were deposited in an irrevocable trust with an escrow agent to provide for all future debt service and redemption premiums on the refunded bonds. The debt defeasance resulted in an accounting loss of \$14,263,000. It will, however, reduce total debt service payments over the next 16 years by \$9,709,464 resulting in an economic gain of \$8,194,030 discounted at the rate of 3.44 percent.

In December 2004, the Virginia Public Building Authority (VPBA) issued \$106,460,000 State Building Revenue Bonds Series 2004D. A portion of the proceeds refunded \$23,595,000 of Series 1997A bonds, \$11,605,000 of Series 1999B bonds, and \$67,085,000 of Series 2000A bonds. Bond proceeds of \$113,202,001 were placed with an escrow agent to provide for the redemption of the bonds. The debt defeasance resulted in an accounting loss of \$10,917,001. It will, however, reduce total debt service payments over the life of the bonds by \$6,107,495 resulting in an economic gain of \$5,034,051 discounted at 3.90 percent. In May 2005, VPBA issued \$135,675,000 State Building Revenue Bonds Series 2005B. A portion of the proceeds refunded \$71,070,000 of Series 1996A bonds, \$25,120,000 of Series 1998B bonds, and \$45,405,000 of Series 1999A bonds. Bond proceeds of \$147,174,006 were placed with an escrow agent to provide for the redemption of the bonds. The debt defeasance resulted in an accounting loss of \$5,579,006. It will, however, reduce total debt service payments over the life of the bonds by \$8,183,288 resulting in an economic gain (savings) of \$7,885,362 discounted at 3.59 percent. In accordance with GASB Statement No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities*, the difference between the reacquisition price and the net carrying amount of the bonds defeased with refunding debt is amortized as a component of interest on bonds over the remaining life of the refunded debt. Therefore, bonds payable, as reflected on the government-wide statements, has been reduced by \$36,510,459 to reflect the remaining deferral on debt defeasance at June 30, 2005.

On November 10, 2004, the Commonwealth Transportation Board issued \$89,400,000 in Transportation Revenue Refunding Bonds Series 2004A and \$232,260,000 in Transportation Revenue Refunding Bonds Series 2004B with a true interest cost (TIC) of 3.96 percent. The bonds that were refunded with the Series 2004A Transportation Refunding Bonds include \$48,375,000 of outstanding Transportation Revenue Bonds, Series 1996A, \$19,755,000 of outstanding Transportation Revenue Bonds, Series 1999A, and \$17,730,000 of outstanding Transportation Revenue Bonds, Series 2001A. The bonds that were refunded with the Series 2004B Transportation Refunding Bonds include \$75,645,000 of outstanding Transportation Revenue Bonds, Series 1996B, \$121,465,000 of outstanding Transportation Revenue Bonds, Series 1999B, and \$30,880,000 of outstanding Transportation Revenue Bonds, Series 2001B. The net proceeds from the sale of the refunding portion of the bonds of \$347,105,184 (after payment of underwriter's fees and other issuance costs) were deposited in an irrevocable trust with an escrow agent to provide for all future debt service and redemption premiums on the Refunded Bonds. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the governmental activities column of the statement of net assets. The reacquisition price exceeded the net carrying amount of the old debt by \$33,255,184. This amount is being netted against the new debt and amortized over the remaining life of the refunded debt or the new debt, whichever is shorter. Total debt service payments over the next 17 years will be reduced by \$15,211,130 resulting in an economic gain of \$14,490,113 discounted at a rate of 3.75 percent.

### VPBA Refinancings

The Virginia Public Building Authority issued \$39 million and \$47 million in Public Facilities Revenue Refunding Bonds, Series 2004C and 2005A, respectively, during the fiscal year ended June 30, 2005. The issuance of the bonds resulted in the refunding of certain lease obligations secured and payable by the Commonwealth of Virginia.

### Component Units

In October 2004, the Virginia College Building Authority (VCBA) issued \$103,205,000 of Series 2004B Pooled Program Educational Facilities Revenue Refunding bonds. The proceeds of the Pooled Program Educational Facilities Revenue Refunding bonds were used to refund \$26,685,000 of Series 1997A Pooled Program bonds, \$5,465,000 of Series 1998A Pooled Program bonds, \$45,150,000 of Series 1999A Pooled Program bonds and \$24,130,000 of Series 2000A Pooled Program bonds. Bond proceeds of \$111,313,545 were placed with an escrow agent to provide for the redemption of the bonds. The debt defeasance of the Pooled Program Educational Facilities bonds resulted in an accounting loss of \$10,068,000. Total debt service payments over the next 15 years will be reduced by \$7,209,455 resulting in a present value savings of \$5,650,847 discounted at a rate of 3.64 percent. In accordance with GASB Statement No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary*

*Activities*, the difference between the reacquisition price and the net carrying amount of the bonds defeased with refunding debt is amortized as a component of interest on bonds over the remaining life of the refunded debt. However, the deferral amount for the Pooled Program Educational Facilities bonds has been allocated to the participating institutions that are responsible for future debt service payments of the bonds in accordance with loan agreements. Notes payable of the related Higher Education Institutions rather than bonds payable of the Authority has been reduced by \$9,306,000 to reflect the remaining deferral on debt defeasance at June 30, 2005.

In December 2004, the VCBA issued \$61,395,000 of Series 2004B 21<sup>st</sup> Century College Program Educational Facilities Revenue Refunding bonds. The proceeds of the 21<sup>st</sup> Century College Program Revenue Refunding bonds were used to refund \$31,160,000 of Series 1996 21<sup>st</sup> Century College Program bonds, \$20,705,000 of Series 1998 21<sup>st</sup> Century College Program bonds and \$9,750,000 of Series 2000 21<sup>st</sup> Century College Program bonds. Bond proceeds of \$66,630,000 were placed with an escrow agent to provide for the redemption of the bonds. The debt defeasance of the 21<sup>st</sup> Century College Program Educational Facilities bonds resulted in an accounting loss of \$5,015,000. The total debt service payments over the next 16 years will be reduced by \$1,808,217 resulting in a present value savings of \$2,131,608 discounted at a rate of 3.90 percent. In accordance with GASB Statement No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities*, the difference between the reacquisition price and the net carrying amount of the bonds defeased with refunding debt is amortized as a component of interest on bonds over the remaining life of the refunded debt. The Authority's Bonds Payable have been reduced by \$4,631,500 to reflect the remaining deferral on debt defeasance at June 30, 2005, related to the 21<sup>st</sup> Century College Program refunding.

GASB Statement No. 7, *Advance Refundings Resulting in Defeasance of Debt*, provides that refunded debt and assets placed in escrow for the payment of related debt service be excluded from the financial statements. As of June 30, 2005, there were \$877.9 million in bonds from the Primary Government that have been refunded and defeased in-substance from the governmental activities column by placing existing assets and the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments. In addition, there were \$1.1 billion in bonds outstanding considered defeased from the Component Units.

### **Arbitrage Rebate**

The Tax Reform Act of 1986 requires that governmental entities issuing tax-exempt debt subsequent to August 1986 calculate and rebate arbitrage earnings to the Federal government. The U.S. Treasury has issued regulations on calculating the rebate amount and complying with the provisions of the Tax Reform Act of 1986. Governmental issuers must comply with the rebate regulations in order for their bonds to maintain tax-exempt status. The regulations require the excess of the aggregate amount earned on investments

purchased with bond proceeds over the amount that would have been earned if the proceeds were invested at a rate equal to the bond yield, to be rebated to the Federal government. Income earned on excess earnings is also subject to rebate. Rebate liability, if any, must be paid every five years over the life of the bonds. Some bonds may be exempt from the rebate requirements if they qualify for certain regulatory exceptions. Governmental issuers may elect to pay a penalty in lieu of rebate. If the issuer meets one of the exceptions, the issuer retains any arbitrage earnings. Rebate and penalty payments are calculated and paid as required by law on bond issues that do not qualify for an exception.

Amounts remitted to the Federal government for rebate liability are generally paid from earnings derived from the issue. However, if all proceeds (including earnings) have been expended and depending on the type of issue, it may be necessary to use project revenues or general or non-general fund appropriations to satisfy any rebate liability. During the year, the Commonwealth paid \$15,007 to the Federal government for rebate liability on Commonwealth general obligation bonds, Series 1999. The Virginia College Building Authority (Nonmajor Component Unit) remitted \$141,095 in rebate liability on its Series 1999 Pooled Bond Program. The Virginia Department of Transportation paid \$940,813 in rebate liability on its Series 1999A Northern Virginia Transportation District and 1999B U.S. Route 58 bond Series.

Rebate liability on bonds of the Virginia Public School Authority (Major Component Unit) is payable from earnings on related bond funds and from local issuers whose local school bonds were purchased by the VPSA. During the year, \$801,775 was paid to the Federal government for rebate on various VPSA School Financing Bonds.

### **Capital Leases**

The Commonwealth leases buildings and equipment under various agreements that are accounted for as capital leases. The lease agreements are for various terms and all leases contain nonappropriation clauses indicating that continuation of the lease is subject to funding by the General Assembly.

Gross minimum lease payments, together with the present value of the net minimum lease payments as of June 30, 2005, are shown in the following table (dollars in thousands). There were no capital lease amounts associated with business-type activities.

	<u>Governmental Activities</u>	<u>Component Units (1)</u>
2006	\$ 18,818	\$ 6,436
2007	18,127	6,443
2008	17,171	6,198
2009	16,305	6,047
2010	16,018	6,064
2011-2015	72,852	22,042
2016-2020	37,708	7,777
2021-2025	<u>9,497</u>	<u>369</u>
Total Gross Minimum Lease Payments	206,496	61,376
Less: Amount Representing Executory Costs	<u>9,419</u>	<u>1</u>
Net Minimum Lease Payments	197,077	61,375
Less: Amount Representing Interest	<u>63,278</u>	<u>15,103</u>
Present Value of Net Minimum Lease Payments	<u>\$ 133,799</u>	<u>\$ 46,272</u>

Note (1): The above amounts exclude capital lease obligations of Foundations.

	<u>Foundations (2)</u>
2006	\$ 143
2007	113
2008	54
2009	48
2010	<u>15</u>
Net Minimum Lease Payments	373
Less: Amount Representing Interest	<u>1</u>
Present Value of Net Minimum Lease Payments	<u>\$ 372</u>

Note (2): Foundations represent FASB reporting entities defined in Note 1.B.

At June 30, 2005, assets purchased under capital leases were included in depreciable capital assets as follows (dollars in thousands). The amounts are net of accumulated depreciation where applicable. For a portion of these assets, ownership will pass to the Commonwealth at the end of the lease term.

	<u>Buildings</u>	<u>Equipment</u>	<u>Total</u>
<b>Governmental Activities:</b>			
Gross Capital Assets	\$ 180,551	\$ 361	\$ 180,912
Less: Accumulated Depreciation	<u>43,876</u>	<u>248</u>	<u>44,124</u>
<b>Total Governmental Activities</b>	<u>\$ 136,675</u>	<u>\$ 113</u>	<u>\$ 136,788</u>
<b>Component Units:</b>			
Gross Capital Assets	\$ 39,425	\$ 29,965	\$ 69,390
Less: Accumulated Depreciation	<u>7,303</u>	<u>12,313</u>	<u>19,616</u>
Subtotal (excluding Foundations)	<u>32,122</u>	<u>17,652</u>	<u>49,774</u>
Foundations:			
Gross Capital Assets	-	676	676
Less: Accumulated Depreciation	<u>-</u>	<u>263</u>	<u>263</u>
Subtotal Foundations	<u>-</u>	<u>413</u>	<u>413</u>
<b>Total Component Units</b>	<u>\$ 32,122</u>	<u>\$ 18,065</u>	<u>\$ 50,187</u>
Total Capital Lease Assets	<u>\$ 168,797</u>	<u>\$ 18,178</u>	<u>\$ 186,975</u>

### Notes Payable

Notes Payable consist of several items as shown in the following schedule (dollars shown in thousands):

<b>Primary Government</b>	
Transportation Note	\$ 12,325
Virginia Public Broadcasting Board Note	15,775
Aviation Note	3,055
Installment Notes	<u>33,756</u>
<b>Total Primary Government</b>	<u>64,911</u>
<b>Component Units</b>	
Virginia Public School Authority	168,315
Virginia Housing Development Authority	326,595
University of Virginia	72,521
Virginia Polytechnic Institute and State University	92,871
Virginia Commonwealth University	114,544
Nonmajor Component Units	364,549
Installment Notes	85,614
Subtotal (excluding Foundations)	<u>1,225,009</u>
Foundations:	
Notes Payable	149,708
Installment Notes	<u>149</u>
Subtotal - Foundations	<u>149,857</u>
<b>Total Component Units</b>	<u>1,374,866</u>
<b>Total Notes Payable</b>	<u>\$ 1,439,777</u>

The Transportation (Primary Government) Note listed above represents an interest free note payable to Fairfax County, Virginia, of \$4,325,000 which was issued pursuant to the State Revenue Bond Act, Article 5, Title 33.1, *Code of Virginia* to pay for the acquisition and construction of the Omer L. Hirst - Adalard L. Brault Expressway. This note is to be repaid on December 1, 2008. Additionally, the Virginia Department of Transportation (Primary Government) entered into an interest free note payable to Chesterfield County, Virginia, of \$8,000,000 for the repayment of the Powhite Parkway Extension Toll Road from surplus net revenues of the project prior to the retirement of all the bonds issued.

The Virginia Public Broadcasting Board (Primary Government) Note listed above represents a loan agreement entered into with the Harrisonburg Industrial Development Authority for \$23,840,000. The purpose of the loan was to grant funds to Virginia's public television stations to assist with the cost of conversion to the Federal Communication Commission's new digital standard. The agreement was entered into February 27, 2001, and has a variable rate of interest. The General Assembly authorized these grants in Chapter 1073 of the 2000 Appropriation Act.

The Aviation Note listed above represents a loan agreement with the Virginia Resources Authority in the amount of \$6,600,000. The purpose of the loan was to finance and refinance grants-in-aid made to The Peninsula Airport Commission to provide funding for capital improvements at the Newport News/Williamsburg International Airport. The principal amount shall be paid semi-annually with the final payment due in 2017.

The Virginia Public School Authority (Major Component Unit) notes of \$168,315,000 are for the School Equipment Financing Notes Educational Technology program. The note proceeds were used to make grants to school divisions for the purchase of educational technology equipment. The notes will be repaid from appropriations to be made by the Virginia General Assembly from the Literary Fund (Major Special Revenue Fund).

The Virginia Housing Development Authority (Major Component Unit) notes of \$326,595,000 are for the Federal Home Loan Bank program. The proceeds along with bond proceeds are used to make mortgage loans.

An additional amount of \$644,485,000 is comprised primarily of Higher Education (Component Unit) promissory notes with the Virginia College Building Authority (Nonmajor Component Unit) to finance the construction of various higher education facilities. The principal amount net of deferred loss on debt defeasance is \$622,889,000. Interest rates range from 2.5 percent to 5.7 percent and shall be paid semi-annually. The final principal payment is due in 2035. The Virginia Equine Center (Nonmajor Component Unit) has a note payable in the amount of \$31,927 for a Chevrolet Tahoe to be used as a company car. The interest rate is 1.9 percent and the note is due in 2009.

The Higher Education Institutions (Component Units) also have notes payable. The University of Virginia (Major Component Unit) has notes payable of \$2,721,000 which are three to five year notes for equipment and other working capital expenses at an interest rate of 3.0 percent to 6.0 percent. The College of William and Mary (Nonmajor Component Unit) has notes payable of \$4,776,674 with SunTrust Bank to partially finance the multi-year implementation of a new administrative and financial system. This first note matures in 2008 and has an interest rate of 5.82 percent. The second note has an interest rate of 3.75 percent and matures in 2011. Virginia State University (Nonmajor Component Unit) has a note payable of \$2,324,258, which is the result of a loan agreement with the U.S. Department of Housing and Urban Development to repair seven dormitories. The loan is to be repaid over 30 years at 3.0 percent interest per annum, and is secured by a lien on the net revenues from the ownership, operation, and use of the seven dormitories under repair. Norfolk State University (Nonmajor Component Unit) has a note payable of \$106,837, which is the result of an agreement with the City of Norfolk to purchase the Brambleton Center. The loan is payable in six full scholarships each year varying from \$4,593 to \$13,308 with the final amount due in 2019. George Mason University (Nonmajor Component Unit) has a note payable of \$11,635,178 with SunTrust Corporation to pay for the implementation of the Siemens Energy Contract. The interest rate is 3.81 percent and matures in 2021.

Various Foundations (Component Units) have notes outstanding as of year-end. The purpose of a majority of these notes is for property acquisition, working capital, and refinancing. Most of these notes are with banks. Future principal payments as of June 30, 2005, are shown in the following table (dollars in thousands).

<b>Maturity</b>	<b>Principal</b>
2006	\$ 26,047
2007	4,276
2008	23,453
2009	24,631
2010	10,493
Thereafter	<u>60,808</u>
Total	<u>\$ 149,708</u>

Note (1): Foundations represent FASB reporting entities defined in Note 1.B.

Installment purchase obligations have been entered into by agencies and institutions of the Commonwealth. These agreements, other than those in the component units and certain institutions of higher education, contain nonappropriation clauses indicating that continuation of the installment purchase obligations is subject to funding by the General Assembly. Installment purchase obligations represent \$119,370,996 of the total outstanding debt of the Commonwealth. The

Foundations (Component Units) had installment purchase obligations totaling \$149,344 as of year-end. Presented in the following tables are repayment schedules for installment purchase obligations.

**Installment Purchase Obligations - Governmental Funds**  
June 30, 2005

<b>Maturity</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2006	\$ 9,107,305	\$ 671,629	\$ 9,778,934
2007	6,167,944	431,567	6,599,511
2008	3,030,260	279,229	3,309,489
2009	2,226,899	182,346	2,409,245
2010	2,130,221	99,043	2,229,264
2011-2014	1,074,142	93,420	1,167,562
2015-2019	298,752	32,802	331,554
2020-2024	11,446	55	11,501
<b>Total</b>	<b>\$ 24,046,969</b>	<b>\$ 1,790,091</b>	<b>\$ 25,837,060</b>

**Installment Purchase Obligations - Business-type Activities**  
June 30, 2005

<b>Maturity</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2006	\$ 5,310,471	\$ 216,015	\$ 5,526,486
2007	2,760,720	93,109	2,853,829
2008	714,731	39,252	753,983
2009	510,851	20,750	531,601
2010	412,912	6,743	419,655
<b>Total</b>	<b>\$ 9,709,685</b>	<b>\$ 375,869</b>	<b>\$ 10,085,554</b>

**Installment Purchase Obligations - Component Units (1)**  
June 30, 2005

<b>Maturity</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2006	\$ 10,870,234	\$ 2,080,570	\$ 12,950,804
2007	10,801,673	2,987,981	13,789,654
2008	9,359,741	2,318,579	11,678,320
2009	8,030,748	2,034,828	10,065,576
2010	6,846,142	1,744,297	8,590,439
2011-2015	27,813,043	5,346,639	33,159,682
2016-2019	10,942,723	1,717,807	12,660,530
2020-2024	950,038	26,754	976,792
<b>Total</b>	<b>\$ 85,614,342</b>	<b>\$ 18,257,455</b>	<b>\$ 103,871,797</b>

Note (1): The above amounts exclude capital lease obligations of Foundations.

**Installment Purchase Obligations - Foundations (2)**  
June 30, 2005

<b>Maturity</b>	<b>Principal</b>
2006	\$ 50,000
2007	50,000
2008	49,344
2009	-
2010	-
Thereafter	-
<b>Total</b>	<b>\$ 149,344</b>

Note (2): Foundations represent FASB reporting entities defined in Note 1.B.

**Lottery Prizes Payable**

Lottery prizes are paid in 20, 25, 26, or 30 installments. The first installment is paid on the day the prize is claimed. The subsequent annual payments are funded with U.S. Treasury STRIPS purchased by the Virginia Lottery. For Life prizes payable represent estimated prizes payable monthly, quarterly or annually for the life of the winner based on life expectancy tables from the Virginia Bureau of Insurance, and funded with a pool of U.S. Treasury STRIPS.

Lottery prizes payable represent the future annual prize payments valued at cost plus accrued interest (present value of securities held to maturity) of the investment securities funding the payments.

Lottery prizes payable for the fiscal year ended June 30, 2005, are shown in the following table:

	<b>Lottery</b>	<b>For Life</b>	<b>Total</b>
Due within one year	\$ 56,445,980	\$ 1,698,176	\$ 58,144,156
Due in subsequent years	294,570,861	22,325,856	316,896,717
Total (present value)	351,016,841	24,024,032	375,040,873
Add:			
Interest to Maturity	123,865,159	22,321,968	146,187,127
Lottery Prizes Payable at Maturity	\$ 474,882,000	\$ 46,346,000	\$ 521,228,000

## Tuition Benefits Payable

The Virginia College Savings Plan administers the Virginia Prepaid Education Program (VPEP). VPEP offers contracts which, for actuarially determined amounts, provide for guaranteed full future tuition payments at State higher education institutions. The contract provisions also allow the benefits to be used for private or out-of-state institutions at a prorated amount based upon the amounts charged by the State's higher education institutions.

At June 30, 2005, tuition benefits payable of \$1.4 billion have been recorded for the VPEP program on the balance sheet for the actuarially determined present value of future obligations anticipated for payment of benefits and administrative expenses for the VPEP program. In addition, a receivable in the amount of \$304.1 million has been recorded to reflect the actuarially determined present value of future payments anticipated from contract holders.

## 21. OTHER REVENUE

The following table (dollars in thousands) summarizes Other Revenue for the fiscal year ended June 30, 2005.

	<b>Assessments and Receipts for Support of Special Services</b>	<b>Fines, Forfeitures, Court Fees, Penalties, and Escheats</b>	<b>Receipts from Cities Counties, and Towns</b>	<b>Private Gifts, Grants, and Contracts</b>	<b>Sales of Property</b>
<b>Primary Government:</b>					
General	\$ 366	\$ 179,925	\$ 9,446	\$ 1	\$ 11,778
Major Special Revenue Funds:					
Commonwealth Transportation	18,411	11,246	76,557	-	3,758
Federal Trust	-	121	-	-	178
Literary	-	61,701	-	-	-
Nonmajor Governmental Funds	86,177	51,865	84,373	28,707	21,321
Nonmajor Enterprise Funds	-	12,215	-	-	-
Private Purpose	-	-	-	-	-
Pension Trust	-	-	-	-	-
Total Primary Government	<u>\$ 104,954</u>	<u>\$ 317,073</u>	<u>\$ 170,376</u>	<u>\$ 28,708</u>	<u>\$ 37,035</u>

	<b>Proceeds from Unclaimed Property</b>	<b>Tobacco Master Settlement</b>	<b>Taxes</b>	<b>Other</b>	<b>Total Other Revenue</b>
<b>Primary Government:</b>					
General	\$ -	\$ 52,126	\$ -	\$ 136,068	\$ 389,710
Major Special Revenue Funds:					
Commonwealth Transportation	-	-	-	39,285	149,257
Federal Trust	-	-	-	70,188	70,487
Literary	85,909	-	-	-	147,610
Nonmajor Governmental Funds	-	-	-	114,556	386,999
Nonmajor Enterprise Funds	-	-	12,096	2,405	26,716
Private Purpose	-	-	-	22	22
Pension Trust	-	-	-	743	743
Total Primary Government	<u>\$ 85,909</u>	<u>\$ 52,126</u>	<u>\$ 12,096</u>	<u>\$ 363,267</u>	<u>\$ 1,171,544</u>

## 22. PRIZES AND CLAIMS

The following table summarizes Prizes and Claims Expense for the fiscal year ended June 30, 2005.

*(Dollars in Thousands)*

	<u>Insurance Claims</u>	<u>Lottery Prize Expense</u>	<u>Total Prizes and Claims</u>
<b>Proprietary Funds:</b>			
Major Enterprise Funds:			
State Lottery	\$ -	\$ 765,248	\$ 765,248
Unemployment Compensation	359,189	-	359,189
Nonmajor Enterprise Funds	147,326	-	147,326
Total Enterprise Funds	<u>\$ 506,515</u>	<u>\$ 765,248</u>	<u>\$ 1,271,763</u>
Internal Service Funds	<u>\$ 755,745</u>	<u>\$ -</u>	<u>\$ 755,745</u>

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## 23. DEPRECIATION AND AMORTIZATION

The following table summarizes Depreciation and Amortization Expense for the fiscal year ended June 30, 2005.

*(Dollars in Thousands)*

	<u>Depreciation</u>	<u>Amortization</u>	<u>Total Depreciation and Amortization</u>
<b>Proprietary Funds:</b>			
Major Enterprise Funds:			
State Lottery	\$ 5,489	\$ -	\$ 5,489
Virginia College Savings Plan	64	-	64
Pocahontas Parkway	10,552	306	10,858
Nonmajor Enterprise Funds	4,172	-	4,172
Total Enterprise Funds	<u>\$ 20,277</u>	<u>\$ 306</u>	<u>\$ 20,583</u>
Internal Service Funds	<u>\$ 16,895</u>	<u>\$ -</u>	<u>\$ 16,895</u>

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## 24. OTHER EXPENSES

The following table summarizes Other Expenses for the fiscal year ended June 30, 2005.

*(Dollars in Thousands)*

	Grants and Distributions to Localities	Expendable Equipment	Other	Total Other Expenses (1)
<b>Proprietary Funds:</b>				
Major Enterprise Funds:				
Virginia College Savings Plan	\$ -	\$ 44	\$ -	\$ 44
Nonmajor Enterprise Funds	68	1,327	381	1,776
Total Enterprise Funds	<u>\$ 68</u>	<u>\$ 1,371</u>	<u>\$ 381</u>	<u>\$ 1,820</u>
Internal Service Funds	\$ -	\$ 26,269	\$ 10,551	\$ 36,820
Private Purpose	-	-	10	10
Pension Trust	-	-	444	444
	<u>\$ 68</u>	<u>\$ 27,640</u>	<u>\$ 11,386</u>	<u>\$ 39,094</u>

Note (1): Fiduciary expenses of \$454 (dollars in thousands) are not included in the Government-wide Statement of Activities.

## 25. OTHER NON-OPERATING REVENUE/EXPENSES

The following table summarizes Other Non-Operating Revenue/Expenses for the fiscal year ended June 30, 2005.

*(Dollars in Thousands)*

	Gain (Loss) on Sale of Capital Assets	Other	Total Non- Operating Revenue/ Expenses
<b>Proprietary Funds:</b>			
Major Enterprise Funds:			
State Lottery	\$ -	\$ (721)	\$ (721)
Virginia College Savings Plan	-	(381)	(381)
Nonmajor Enterprise Funds	(37)	(438)	(475)
Total Enterprise Funds	<u>\$ (37)</u>	<u>\$ (1,540)</u>	<u>\$ (1,577)</u>
Internal Service Funds	<u>\$ (500)</u>	<u>\$ (783)</u>	<u>\$ (1,283)</u>

## 26. TRANSFERS

The following table summarizes Transfers In and Transfers Out for the fiscal year ended June 30, 2005 (dollars in thousands).

<b>Transfers In (Reported In):</b>					
<b>Transfers Out (Reported In):</b>	<b>General</b>	<b>Commonwealth Transportation</b>	<b>Federal Trust</b>	<b>Literary Fund</b>	<b>Nonmajor Governmental Funds</b>
<b>Primary Government</b>					
General	\$ -	\$ 365,323	\$ -	\$ -	\$ 273,623
Major Special Revenue Funds:					
Commonwealth Transportation	47,357	-	985	-	224,719
Federal Trust	309	23,823	-	-	1,591
Nonmajor Governmental Funds	60,036	1,054	810	-	12,427
Major Enterprise Funds:					
State Lottery	423,521	-	-	9,311	-
Virginia College Savings Plan	121	-	-	-	-
Pocahontas Parkway	-	204	-	-	-
Unemployment Compensation	-	-	3,500	-	-
Nonmajor Enterprise Funds	103,792	-	-	4	58
Internal Service Funds	1,185	-	-	-	1,054
<b>Total Primary Government</b>	<b>\$ 636,321</b>	<b>\$ 390,404</b>	<b>\$ 5,295</b>	<b>\$ 9,315</b>	<b>\$ 513,472</b>

Transfers are used to (1) move revenues from the fund that the *Code of Virginia* or budget requires to collect them to the fund that the *Code of Virginia* or budget requires to expend them; (2) move receipts restricted for debt service from the funds holding the resources to the debt service fund as principal and interest payments become due; (3) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations; and (4) to reimburse the General Fund for expenses incurred on behalf of nongeneral funds.

During the fiscal year, the following significant transfers were made that do not occur on a routine basis or are inconsistent with the activities of the fund making the transfer.

- Various non-general funds transferred approximately \$30.3 million to the General Fund for disbursements appropriated by Chapter 951, 2005 Acts of Assembly.

- The Department of Motor Vehicles transferred certain fees of approximately \$10.1 million to the General Fund as required by Chapter 951, 2005 Acts of Assembly.
- Various non-general funds transferred approximately \$9.5 million to the General Fund resulting from reduced retirement and post-employment benefit contribution disbursements appropriated by Chapter 951, 2005 Acts of Assembly.

## 27. ON-BEHALF PAYMENTS

Higher Education Institutions (Component Units) recognized various foundation and association on-behalf payments for fringe benefits and salaries during fiscal year 2005 totaling \$1,850,122. This activity was recorded as Program Revenue – Operating Grants and Contributions in the amount of \$1,820,122; and Program Revenue – Charges for Services in the amount of \$30,000, with corresponding expenditures.

Nonmajor Enterprise Funds	Internal Service Funds	Total Primary Government
\$ -	\$ -	\$ 638,946
-	283	273,344
363	-	26,086
5,018	115	79,460
-	-	432,832
-	-	121
-	-	204
-	-	3,500
-	-	103,854
-	-	2,239
<u>\$ 5,381</u>	<u>\$ 398</u>	<u>\$ 1,560,586</u>

## 28. DEFICIT FUND BALANCES / NET ASSETS

The State Lottery (Major Enterprise Fund) and Department of Alcoholic Beverage Control (Nonmajor Enterprise Fund) ended the year with deficit net assets of \$2.5 million and \$7.6 million respectively. This was solely attributable to the net pension obligation resulting from GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*. Since the Commonwealth is the employer, the agencies do not report this liability in their individually published financial statements.

The Virginia College Savings Plan (Major Enterprise Fund) ended the year with a deficit net assets balance of \$60.2 million which is attributable to the projected unfunded actuarial liability calculated by the Plan's actuary. While the Plan remains in a deficit position, there was significant improvement over the prior year deficit, which was reduced from \$128.5 million to the current \$60.2 million. This improvement is primarily attributable to lower than projected tuition increases for the 2005-2006 academic year, actual returns on the Plan's investments exceeding the assumed rate of return by a substantial margin, and increases in the actuarial reserve from new contract sales. The Board remains committed to reducing the actuarial deficit over time and will continue to work closely with the actuary and investment consultant to enhance investment performance and add to the actuarial reserve whenever possible.

The Pocahontas Parkway (Major Enterprise Fund) ended the year with a deficit net assets balance of \$140.3 million. This is attributable to debt service and

operating expenses exceeding revenues and a deficit in beginning net assets.

The eVA Procurement System (Nonmajor Enterprise Fund) ended the year with a deficit net assets balance of \$1.9 million. This is attributable to a deficit in beginning net assets, operating expenses exceeding revenues and the net pension obligation resulting from GASB Statement No. 27, as previously explained.

The Health Care Fund (Internal Service Fund) ended the year with a deficit net assets balance of \$11.0 million. The deficit is attributable to the fact that health care premiums are lower than the actuarially determined rates.

Maintenance and Repair (Internal Service Fund) ended the year with a deficit net assets balance of \$1.1 million due to revenue refunds to agencies which were mandated by the Department of Planning and Budget.

The Risk Management Fund (Internal Service Fund) ended the year with a deficit net assets balance of \$195.4 million. The deficit was the result of estimated claims payable exceeding the available equity in the fund. Claims are paid on a pay-as-you-go basis. To the extent that claims exceed current resources, they will ultimately become a liability of the fund from which the claim originated.

The Graphic Communications Fund (Internal Service Fund) ended the year with a deficit net assets balance of \$12,000. This was solely attributable to the net pension obligation resulting from GASB Statement

No. 27, *Accounting for Pensions by State and Local Governmental Employers.*

The Virginia Public Building Authority Capital Projects Fund (Nonmajor Governmental Fund) ended the year with a deficit fund balance of \$33.3 million. The Authority issues bonds based on estimated expenditures for approved capital projects. This deficit occurred because expenditures were incurred prior to year-end, but will not be paid until fiscal year 2006 when additional bonds are issued.

The Virginia College Building Authority (Nonmajor Component Unit) ended the year with a deficit net assets balance of \$549.4 million. This deficit occurs because the Authority issues 21<sup>st</sup> Century and Equipment bonds subject to future appropriations from

the General Fund of the Commonwealth without any other security.

**29. ENDOWMENTS**

Donor restricted endowments reside primarily within the higher education institutions. The net appreciation available for expenditure is \$716,670,270, and of this amount, \$714,199,242 is reported as restricted net assets and \$2,471,028 is reported as unrestricted net assets. The *Code of Virginia* authorizes acceptance of donations. The governing boards of these entities and the donor agreements determine whether net appreciation can be spent and the accepted spending rate. These policies are entity specific and vary with each institution.

**30. CASH FLOWS – ADDITIONAL DETAILED INFORMATION**

The following table (dollars in thousands) summarizes specific cash flows for the fiscal year ended June 30, 2005.

	State Lottery	Virginia College Savings Plan	Pocahontas Parkway	Unemployment Compensation
Cash Flows Resulting from:				
Payments for Prizes, Claims, and Loss Control:				
Lottery Prizes	\$ (848,144)	\$ -	\$ -	\$ -
Claims and Loss Control	-	-	-	(363,376)
Total	<u>\$ (848,144)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (363,376)</u>
Other Operating Revenues:				
Other Operating Revenue	\$ -	\$ -	\$ -	\$ -
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Other Operating Expenses:				
Payments for Contractual Services	\$ (29,241)	\$ (2,910)	\$ -	\$ -
Other Operating Expenses	-	-	(1,023)	-
Total	<u>\$ (29,241)</u>	<u>\$ (2,910)</u>	<u>\$ (1,023)</u>	<u>\$ -</u>
Other Noncapital Financing Receipt Activities:				
Advances/Contributions from the Commonwealth	\$ 15,000	\$ -	\$ -	\$ -
Receipts from Taxes	-	-	-	-
Other Noncapital Financing Receipt Activities	1,290	-	-	-
Total	<u>\$ 16,290</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Other Noncapital Financing Disbursement Activities:				
Repayments of Advances/Contributions from the Commonwealth	\$ -	\$ -	\$ -	\$ -
Other Noncapital Financing Disbursement Activities	-	-	-	-
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Nonmajor Enterprise Funds	Total Enterprise Funds	Internal Service Funds
\$ -	\$ (848,144)	\$ -
(142,825)	(506,201)	(728,991)
<u>\$ (142,825)</u>	<u>\$ (1,354,345)</u>	<u>\$ (728,991)</u>
\$ 5,528	\$ 5,528	\$ 1
<u>\$ 5,528</u>	<u>\$ 5,528</u>	<u>\$ 1</u>
\$ (38,722)	\$ (70,873)	\$ (143,068)
(39)	(1,062)	(9,237)
<u>\$ (38,761)</u>	<u>\$ (71,935)</u>	<u>\$ (152,305)</u>
\$ 6,494	\$ 21,494	\$ -
123,296	123,296	-
368	1,658	48
<u>\$ 130,158</u>	<u>\$ 146,448</u>	<u>\$ 48</u>
\$ -	\$ -	\$ (632)
(92)	(92)	(1)
<u>\$ (92)</u>	<u>\$ (92)</u>	<u>\$ (633)</u>

### **31. TOBACCO SETTLEMENT AND SECURITIZATION**

On November 23, 1998, 46 states' Attorneys General and the major tobacco companies signed a proposed settlement that reimburses states for smoking-related medical expenses paid through Medicaid and other health care programs. Virginia could receive approximately \$4.1 billion over the next 25 years. The settlement was approved in a Consent Decree in December 1998. On March 29, 1999, the General Assembly enacted a law approving the establishment of the Virginia Tobacco Indemnification and Community Revitalization Commission (Commission), in compliance with the Consent Decree, to help communities in Virginia hurt by the decline of tobacco.

The Commission was established for the purposes of determining the appropriate recipients of monies in the Tobacco Indemnification and Community Revitalization Fund. The monies are to be used to provide payments to tobacco farmers as compensation for the tobacco equipment and barns and lost tobacco production opportunities associated with a decline in quota. The monies are also to be used to revitalize tobacco dependent communities.

The General Assembly also created The Virginia Tobacco Settlement Foundation (Foundation). The purpose of the Foundation is to determine the appropriate recipients of monies in the Virginia Tobacco Settlement Fund. The Foundation will also be responsible for distributing monies for the purposes provided in the legislation. Disbursements can be made to assist in financing efforts to restrict the use of tobacco products by minors, through educational and awareness programs describing the health effects of tobacco use on minors, and laws restricting the distribution of tobacco products to minors. The Virginia Tobacco Indemnification and Community Revitalization Commission and the Virginia Tobacco Settlement Foundation are included in the Comprehensive Annual Financial Report as governmental component units.

Additionally, the General Assembly created two special non-reverting funds. The Tobacco Settlement monies will be deposited to these funds and the General Fund. Fifty percent of the Settlement monies will be deposited into the Tobacco Indemnification and Community Revitalization Fund. Ten percent of the Settlement monies will be deposited into the Virginia Tobacco Settlement Fund. The remaining 40 percent will be deposited to the General Fund.

In May 2005, pursuant to a Purchase and Sale Agreement with the Commonwealth, acting as an agent on behalf of the Tobacco Indemnification and Community Revitalization Commission (Commission), the Commonwealth sold to the Tobacco Settlement Financing Corporation (Corporation) 25 percent of its future right, title and interest in the Tobacco Settlement Revenues (TSRs). Specifically, these rights include half of the 50 percent share of the TSRs received by the Commission starting May 15, 2005, and in perpetuity under the Master Settlement Agreement. The Commission is a discrete component unit of the Commonwealth and the Corporation is disclosed as a related organization.

Consideration paid by the Corporation to the Commission for TSRs consisted of a cash amount deposited into an endowment to fund the long-term spending plan approved by the Commission. The bonds of the Corporation are asset-backed instruments secured solely by the TSRs, and the Corporation's right to receive TSRs is expected to produce funding for its obligations.

### **32. PUBLIC-PRIVATE PARTNERSHIP**

The Department of Taxation (Department) has entered into a partnership agreement with the American Management Systems, Inc. (AMS). The purpose of this partnership is to finance the Department's technology needs. As of June 30, 2004, enough revenue has been generated to fully fund the total contract cost. As of June 30, 2005, the Department has paid AMS \$151.2 million towards the \$171.6 million contract cost.

### **33. INTERGOVERNMENTAL TRANSFERS**

In making payments under an approved Medicaid State Plan per Title XIX of the Social Security Act, Federal regulation allowed states to pay different rates to different classes of providers. The Virginia Medicaid State Plan allowed the Commonwealth, without violating the upper payment limit regulation, to make enhanced Medicaid payments to nursing homes, hospitals and clinics owned and operated by local governments. Payments were also made to state owned hospitals and health clinics. These enhanced payments were capped by an upper payment limit. The Department of Medical Assistance Services made these enhanced payments to locally owned hospitals, health clinics and nursing homes as well as state owned health clinics using "intergovernmental transfers." In fiscal year 2005, and previous fiscal years, this activity was reported in Other Special Revenue (nonmajor). The program of enhanced Medicaid payments to nursing homes, hospitals and clinics owned and operated by local government Intergovernmental Transfer transactions was ended by the Federal government on June 30, 2005

### **34. CONTINGENCIES**

#### **A. Grants and Contracts**

The Commonwealth has received Federal grants for specific purposes that are subject to review and audit by the grantor agencies. Claims against these resources are generally conditional upon compliance with the terms and conditions of grant agreements and applicable Federal regulations, including the expenditure of resources for allowable purposes. Any disallowance resulting from a Federal audit may become a liability of the Commonwealth.

Institutions of higher education (Component Units) and other State agencies are required to comply with various Federal regulations issued by the Office of Management and Budget, if such agencies

are recipients of Federal grants, contracts, or other sponsored agreements. Failure to comply with certain requirements of these regulations may result in questions concerning the allowability of related direct and indirect charges pursuant to such agreements. It is believed that the ultimate disallowance pertaining to these regulations, if any, will be immaterial to the overall financial condition of the Commonwealth.

The U.S. Department of Health and Human Services (DHHS) Office of the Inspector General conducted a review and indicated that the Commonwealth's Statewide Indirect Cost Allocation Plan rates have allowed over-recoveries in the Internal Service Funds. The U.S. DHHS has reviewed and approved the 2006 cost allocation plan, which is based on state fiscal year 2004 data. The Commonwealth believes this liability has the potential to total \$1,612,063 as of June 30, 2005.

Virginia's combined overpayment and underpayment food stamp error rate for federal fiscal year 2004 was 6.59 percent. The national average combined error rate was 5.88 percent. There is a two year liability system in place, which was effective with Federal fiscal year 2003. Under this system, a liability amount is established when, for the second or subsequent consecutive fiscal year, USDA determines that there is a 95% statistical probability that a State's payment error rate exceeds 105% of the national performance measure. Virginia fell within this tolerance level for 2004 and therefore does not count as a first year of potential liability for our state.

## **B. Litigation**

The Commonwealth is named as a party in legal proceedings and investigations that occur in the normal course of governmental operations, some involving substantial amounts. It is not possible at the present time to estimate ultimate outcome or liability, if any, of the Commonwealth in respect to the various proceedings; however, it is believed that any ultimate liability resulting from these suits or investigations will not have a material, adverse effect on the financial condition of the Commonwealth.

## **C. Subject to Appropriation**

Both the primary government and the discretely presented component units enter into agreements and issue debt secured solely by future appropriations from the General Fund of the Commonwealth. The primary government has leases and other agreements of such debt of \$1.3 billion. The discretely presented component units have such debt of \$641.5 million.

## **35. SUBSEQUENT EVENTS**

### **Primary Government**

In August 2005, principal and interest payments for the Pocahontas Parkway Association totaling \$7,560,625

became due on the Senior Current Interest Bonds, Series 1998A, which were paid out of the Senior Bond Debt Service Account. On the same date, a principal payment of \$2,300,000 became due on the First Tier Subordinated Capital Appreciation Bonds, Series 1998C. A draw of \$450,000 was made on the First Tier Subordinated Debt Service Reserve Fund to enable the payment in accordance with the terms of the Master Indenture. In addition, a toll rate study has recommended a toll increase of \$0.25 to be effective January 1, 2006.

In September 2005, the Commonwealth Transportation Board issued \$250,000,000 in Federal Highway Reimbursement Anticipation Notes, Series 2005. The proceeds of the notes will be used by the Commonwealth to finance a portion of the costs of certain eligible Transportation Board projects.

In November 2005, Governor Mark R. Warner approved an interim agreement with Northrop Grumman Corporation to modernize the state's information technology infrastructure. The interim agreement approved by Governor Warner permits the state to plan the transition of IT infrastructure services to Northrop Grumman pending approval by the General Assembly for implementation. If approved by the General Assembly, the Commonwealth will enter into a ten-year, \$2 billion contract to provide these services.

In November 2005, the Commonwealth issued \$172,645,000 in General Obligation Bonds, Series 2005A to fund capital projects for educational facilities, parks and recreational facilities of the Commonwealth, and various institutions of higher education.

In November 2005, the Virginia Public Building Authority issued \$165,810,000 in Public Facilities Revenue Bonds, Series 2005C to finance or refinance the acquisition, construction, improvement, rehabilitation, furnishing, and equipping of various public facilities for use by the Commonwealth and its agencies or the Commonwealth's share of various regional and local jails and juvenile detention facility projects.

### **Component Units**

Subsequent to June 30, 2005, and through August 24, 2005, the Virginia Resource Authority closed four loans totaling \$6,823,141 and increased an existing loan by \$14,153,653.

In July 2005, the Virginia Housing Development Authority redeemed \$6,130,000 in Multi-Family Housing Bonds and \$46,120,000 in Commonwealth Mortgage Bonds.

In July 2005, the University of Virginia issued \$193,335,000 in General Revenue Bonds, Series 2005. The 2005 Series was issued to refund University of Virginia 1998A 9(d) bonds with an outstanding par amount of \$61,775,000, reducing the aggregate debt service by \$4,395,470 and representing a net present value savings of \$3,262,829. In addition, \$84,963,000 was issued to refund the University's outstanding commercial paper program and \$54,981,258 was issued to fund new construction on the grounds of the University of Virginia.

In August 2005, the Virginia Museum of Fine Arts Foundation issued Variable Rate Tax-exempt Revenue Bonds through the Virginia Small Business Financing Authority in the aggregate principle amount of \$30,000,000. The bond proceeds will be used for the Museum's capital expansion project. The foundation also entered into a \$30,000,000 fixed rate forward swap agreement with Wachovia Bank, N. A. in September 2005.

In September 2005, the Virginia Housing Development Authority redeemed \$90,365,000 in Commonwealth Mortgage Bonds and \$29,000,000 in Rental Housing Bonds.

In September 2005, the Virginia College Building Authority approved the issuance of up to \$140 million in Educational Facilities Revenue Bonds, (Public Higher Education Financing Program), Series 2005A. The proceeds of the Series 2005A Bonds will be used to purchase institutional notes from higher education institutions. The institutions will in turn use the proceeds of the notes to finance capital projects.

In November 2005, the Virginia Public School Authority issued approximately \$211.0 million of School Financing Bonds (1997 Resolution) Series 2005D to purchase certain general obligation local school bonds to finance capital projects for public schools.