

Management's Discussion and Analysis

(Unaudited)

The following is a discussion and analysis of the Commonwealth of Virginia's (the Commonwealth) financial performance, including an overview and analysis of the financial activities of the Commonwealth for the fiscal year ended June 30, 2015. Readers should consider this information in conjunction with the transmittal letter, which is located in the Introductory Section of this report, and the Commonwealth's financial statements, including the notes to the financial statements, which are located after this analysis.

Financial Highlights

Government-wide Highlights

The primary government's assets and deferred outflows of resources exceeded its liabilities and deferred inflows of resources at June 30, 2015, by \$20.8 billion. Net position of governmental activities increased by \$868.1 million and net position of business-type activities increased by \$303.0 million. Component units reported an increase in net position of \$1.1 billion from June 30, 2014.

Fund Highlights

At the end of the fiscal year, the Commonwealth's governmental funds reported a combined ending fund balance of \$4.3 billion, an increase of \$402.8 million in comparison with the prior year. Of this total fund balance, \$282.5 million represents nonspendable fund balance, \$2.2 billion represents restricted fund balance, \$2.5 billion represents committed fund balance, and \$28.8 million represents assigned fund balance. These amounts are offset by a negative \$713.1 million unassigned fund balance. The Enterprise Funds reported net position at June 30, 2015, of \$1.4 billion, an increase of \$303.9 million during the year which is primarily attributable to the Unemployment Compensation Fund and the Virginia College Savings Plan. See page 33 for additional information.

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

Long-term Debt

The Commonwealth's total debt rose during the fiscal year to \$41.9 billion, an increase of \$4.3 billion, or 11.4 percent. During the fiscal year, the Commonwealth issued new debt in the amount of \$1.4 billion for the primary government and \$5.0 billion for the component units. These debt issuances increased the debt balances to \$14.7 billion for the primary government and \$27.2 billion for component units.

Overview of the Financial Statements

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

Government-wide Statements

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

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

The Statement of Activities (pages 42 through 44) presents information showing how the Commonwealth's net position changed during fiscal year 2015. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

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

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

Business-type Activities – account for functions that are intended to recover all or a significant portion of their costs through user fees and charges. The major business-type activities of the Commonwealth include the Virginia Lottery, Virginia College Savings Plan, and Unemployment Compensation Fund.

Discretely Presented Component Units – account for functions of legally separate entities for which the Commonwealth is financially accountable. The Commonwealth has 26 non-higher education component units and 22 higher education institutions that are reported as discretely presented component units. Information regarding the individual financial statements of the component units is presented in the notes to the financial statements.

This report includes two schedules (pages 48 and 52) that reconcile the amounts reported on the governmental fund financial statements (modified accrual accounting) with governmental activities on the appropriate government-wide statements (full accrual accounting). The following indicates some of the reporting differences between the government-wide financial statements and the fund financial statements.

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

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Commonwealth, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the Commonwealth’s funds can be divided into three categories: governmental, proprietary, and fiduciary. Each of these categories uses different accounting approaches. Fund financial statements begin on page 46 and provide detailed information about the major individual funds.

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

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

The Commonwealth reports 12 individual governmental funds. Information is presented separately in the governmental fund statements for the General, Commonwealth Transportation, Federal Trust, and Literary funds, which are all considered major funds. Data from the other 8 governmental funds are aggregated into a single column on the fund statements. Individual fund data for these nonmajor governmental funds is provided in the combining financial statements immediately following the required supplementary information.

- **Proprietary funds** – The Commonwealth maintains two different types of proprietary funds, enterprise and internal service. These funds report activities that operate more like those of private-sector business and use the full accrual basis of accounting. Enterprise funds report activities that charge fees for supplies or services to the general public like the Virginia Lottery. Enterprise funds are reported as business-type activities on the government-wide financial statements.

The enterprise funds use the full accrual basis of accounting and the only differences between amounts reported on the government-wide statements and the enterprise fund statements are due to internal service fund activity (see reconciliations on pages 54 and 56). Internal service funds report activities that charge fees for supplies and services to other Commonwealth agencies, like Fleet Management. Internal service funds are reported as governmental activities in the government-wide statements because these types of services predominantly benefit governments rather than business-type functions.

The Commonwealth reports 24 individual proprietary funds. Information is presented separately in the proprietary fund statements for the Virginia Lottery, Virginia College Savings Plan, and Unemployment Compensation Funds, all of which are considered major funds. Data from the other enterprise funds are aggregated into a single column on the fund statements. All internal service funds are aggregated into a single column on the fund statements. Individual fund data for all nonmajor proprietary funds is provided in the combining financial statements immediately following the required supplementary information.

- **Fiduciary funds** – These funds are used to account for resources held for the benefit of parties outside the government and use the full accrual basis of accounting. Fiduciary funds are excluded from the government-wide financial statements because the resources of these funds are restricted and cannot be used to finance the Commonwealth's operations. The Commonwealth's fiduciary activities are reported in separate Statements of Fiduciary Net Position and Changes in Fiduciary Net Position beginning on page 64.

The Commonwealth's fiduciary funds are the:

- Private Purpose Trusts, which reports the activities for 7 separate funds and accounts for transactions of trust arrangements in which the principal and income benefit individuals, private organizations, or other governments;
- Pension and Other Employee Benefit Trusts, which reports the activities of 13 separate pension and other employment retirement plans for employees;
- Investment Trust, which accounts for the activities of the external investment pool; and,
- Agency, which accounts for assets held on behalf of others in 20 separate funds.

Individual fund data for all fiduciary funds is provided in the combining financial statements immediately following the required supplementary information.

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

Notes to the Financial Statements

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

Required Supplementary Information

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

Other Information

The combining statements referred to earlier in connection with nonmajor funds and component units can be found beginning on page 197 of this report. The individual fund information is aggregated into a single total on the combining financial statements, which carries forward to the fund financial statements.

Government-wide Financial Analysis

The primary government's assets and deferred outflows of resources exceeded its liabilities and deferred inflows of resources by \$20.8 billion during the fiscal year. The net position of the governmental activities increased \$868.1 million, or 4.7 percent, primarily due to increases in capital assets and deferred outflows of resources offset by increases in total liabilities and deferred inflows of resources. Capital assets are discussed further on page 35, the long-term liabilities are discussed further on page 36, and deferred inflows and outflows of resources are discussed in Note 13, "Deferred Outflows and Deferred Inflows of Resources." Business-type activities had an increase of \$303.0 million, or 28.2 percent, primarily due to an increase for the Unemployment Compensation Fund and Virginia College Savings Plan as discussed on page 33. The government-wide beginning balance was restated for the implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68*, and the correction of prior year errors to arrive at a restated beginning balance of \$19.6 billion.

Figure 11
Net Position as of June 30, 2015 and 2014
(Dollars in Thousands)

	Governmental Activities		Business-type Activities		Total	
	2015	2014 as restated	2015	2014 as restated	2015	2014 as restated
Current and other assets	\$ 9,244,081	\$ 8,966,466	\$ 4,425,736	\$ 4,042,573	\$ 13,669,817	\$ 13,009,039
Capital assets	29,347,883	27,908,070	40,227	168,539	29,388,110	28,076,609
Deferred outflow s of resources	507,048	53,940	13,438	-	520,486	53,940
Total assets and deferred outflow s of resources	<u>39,099,012</u>	<u>36,928,476</u>	<u>4,479,401</u>	<u>4,211,112</u>	<u>43,578,413</u>	<u>41,139,588</u>
Long-term liabilities outstanding	11,953,821	11,996,146	2,736,277	2,779,870	14,690,098	14,776,016
Other liabilities	4,790,020	4,801,203	342,291	354,809	5,132,311	5,156,012
Deferred inflow s of resources	2,918,314	1,562,385	21,371	-	2,939,685	1,562,385
Total liabilities and deferred inflow s of resources	<u>19,662,155</u>	<u>18,359,734</u>	<u>3,099,939</u>	<u>3,134,679</u>	<u>22,762,094</u>	<u>21,494,413</u>
Net position:						
Net investment in capital assets	23,406,620	22,326,288	34,519	12,312	23,441,139	22,338,600
Restricted	1,435,961	1,465,891	845,213	586,073	2,281,174	2,051,964
Unrestricted	(5,405,724)	(5,223,437)	499,730	478,048	(4,905,994)	(4,745,389)
Total net position	<u>\$ 19,436,857</u>	<u>\$ 18,568,742</u>	<u>\$ 1,379,462</u>	<u>\$ 1,076,433</u>	<u>\$ 20,816,319</u>	<u>\$ 19,645,175</u>

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

An additional portion of the primary government's net position represents restricted net position. These resources are subject to external restrictions or constitutional provisions specifying how they may be used. The remaining balance of negative \$4.9 billion is unrestricted net position (**Figure 11**).

Approximately 55.4 percent of the primary government's total revenue came from taxes. While the primary government's expenses cover many services, the largest expenses are for education and individual and family services. General revenues normally fund governmental activities. For fiscal year 2015, governmental program and general revenues exceeded governmental expenses by \$274.3 million. Program revenues exceeded expenses from business-type activities by \$986.0 million. The following condensed financial information (**Figure 12**) was derived from the Government-wide Statement of Activities and provides detail regarding the change in net position (see page 42).

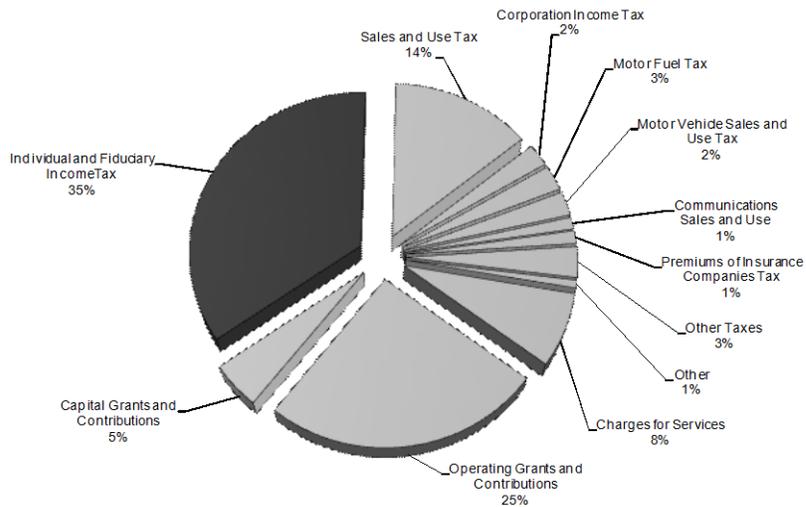
Figure 12
Changes in Net Position for the Fiscal Years Ended June 30, 2015 and 2014
(Dollars in Thousands)

	Governmental Activities		Business-type Activities		Total	
	2015	2014 as restated	2015	2014 as restated	2015	2014 as restated
Revenues:						
Program Revenues:						
Charges for Services	\$ 2,594,514	\$ 2,560,863	\$ 3,953,679	\$ 4,131,281	\$ 6,548,193	\$ 6,692,144
Operating Grants and Contributions	8,914,631	8,731,809	183	264	8,914,814	8,732,073
Capital Grants and Contributions	1,618,761	1,508,880	-	69,595	1,618,761	1,578,475
General Revenues:						
Taxes:						
Individual and Fiduciary Income	12,265,530	11,681,808	-	-	12,265,530	11,681,808
Sales and Use	4,829,677	4,597,105	-	-	4,829,677	4,597,105
Corporation Income	801,165	769,832	-	-	801,165	769,832
Motor Fuel	888,348	791,944	-	-	888,348	791,944
Motor Vehicle Sales and Use	846,197	780,817	-	-	846,197	780,817
Communications Sales and Use	416,051	420,371	-	-	416,051	420,371
Deeds, Contracts, Wills, and Suits	440,896	394,834	-	-	440,896	394,834
Premiums of Insurance Companies	453,376	459,933	-	-	453,376	459,933
Alcoholic Beverage Sales	139,832	132,044	-	-	139,832	132,044
Tobacco Products	178,954	182,110	-	-	178,954	182,110
Estate	92	149	-	-	92	149
Public Service Corporations	118,849	119,074	-	-	118,849	119,074
Beer and Beverage Excise	42,719	43,050	-	-	42,719	43,050
Wine and Spirits/ABC Liter	26,253	25,620	-	-	26,253	25,620
Bank Stock	19,030	22,581	-	-	19,030	22,581
Other Taxes	112,368	95,415	9,142	9,142	121,510	104,557
Unrestricted Grants and Contributions	48,613	48,730	-	-	48,613	48,730
Investment Earnings	15,970	44,571	1,603	1,735	17,573	46,306
Miscellaneous	205,625	233,716	243	358	205,868	234,074
Total Revenues	34,977,451	33,645,256	3,964,850	4,212,375	38,942,301	37,857,631
Expenses:						
General Government	3,267,325	3,545,550	-	-	3,267,325	3,545,550
Education	9,844,625	9,484,561	-	-	9,844,625	9,484,561
Transportation	4,369,089	4,060,677	-	-	4,369,089	4,060,677
Resources and Economic Development	970,515	1,163,797	-	-	970,515	1,163,797
Individual and Family Services	13,276,897	13,875,427	-	-	13,276,897	13,875,427
Administration of Justice	2,751,111	3,641,626	-	-	2,751,111	3,641,626
Interest and Charges on Long-term Debt	223,584	237,782	-	-	223,584	237,782
Virginia Lottery	-	-	1,299,753	1,281,732	1,299,753	1,281,732
Virginia College Savings Plan	-	-	155,331	110,156	155,331	110,156
Unemployment Compensation	-	-	431,437	535,715	431,437	535,715
Alcoholic Beverage Control	-	-	579,945	595,272	579,945	595,272
Risk Management	-	-	10,240	13,839	10,240	13,839
Local Choice Health Care	-	-	349,910	308,295	349,910	308,295
Route 460 Funding Corporation of Virginia	-	-	13,024	82,257	13,024	82,257
Virginia Industries for the Blind	-	-	42,722	39,198	42,722	39,198
Consolidated Laboratory	-	-	8,630	11,244	8,630	11,244
eVA Procurement System	-	-	22,563	23,739	22,563	23,739
Department of Environmental Quality Title V	-	-	10,444	16,287	10,444	16,287
Wireless E-911	-	-	36,804	46,598	36,804	46,598
Museum and Library Gift Shops	-	-	6,618	7,174	6,618	7,174
Behavioral Health Canteen and Work Activity	-	-	466	442	466	442
Total Expenses	34,703,146	36,009,420	2,967,887	3,071,948	37,671,033	39,081,368
Excess before transfers	274,305	(2,364,164)	996,963	1,140,427	1,271,268	(1,223,737)
Special Item	(134,561)	-	34,437	-	(100,124)	-
Transfers	728,371	723,701	(728,371)	(723,701)	-	-
Increase in net position	868,115	(1,640,463)	303,029	416,726	1,171,144	(1,223,737)
Net position, July 1, as restated	18,568,742	20,209,205	1,076,433	659,707	19,645,175	20,868,912
Net position, June 30	\$ 19,436,857	\$ 18,568,742	\$ 1,379,462	\$ 1,076,433	\$ 20,816,319	\$ 19,645,175

Governmental Activities Revenues

Figure 13 is a graphical representation of the Statement of Activities revenues for governmental activities. Governmental activities revenues increased by \$1.3 billion, or 4.0 percent. The net increase is mainly attributable to increases in the General Fund, which are discussed on page 34.

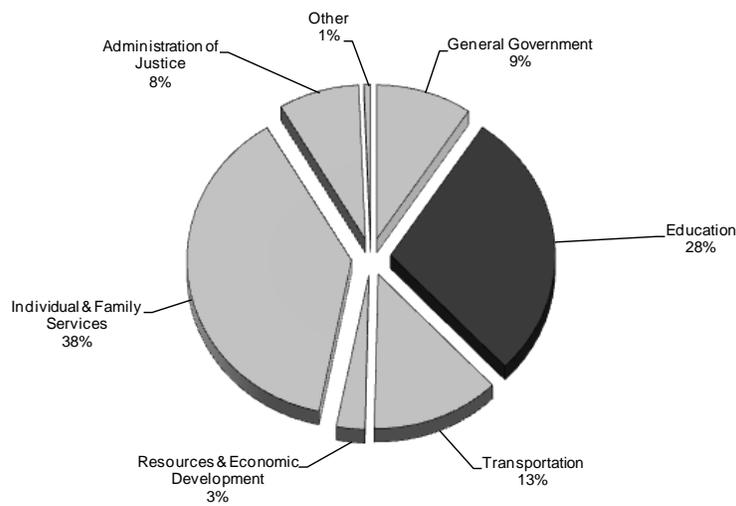
Figure 13
Revenues by Source – Governmental Activities
 Fiscal Year 2015



Governmental Activities Expenses

Figure 14 is a graphical representation of the Statement of Activities expenses for governmental activities. Governmental activities expenses decreased by \$1.3 billion, or 3.6 percent. This change is primarily attributable to decreases in all expense types with the exception of Education and Transportation. See pages 34 and 35 for additional information.

Figure 14
Expenses by Type – Governmental Activities
 Fiscal Year 2015



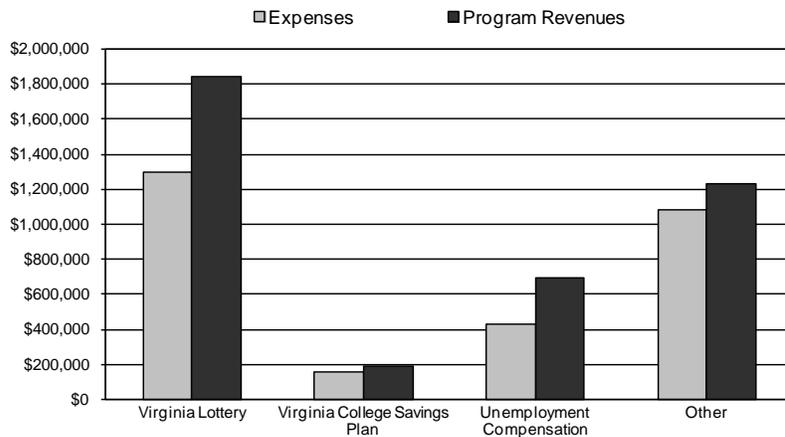
Net Position of Business-type Activities

Net position of business-type activities increased by \$303.0 million during the fiscal year. As shown in **Figure 15**, highlights of the changes in net position for the major enterprise funds were as follows:

- Lottery sales were \$1.8 billion, an increase of \$33.1 million over the prior year. Net income was \$545.5 million, a decrease of \$621,623 (0.1 percent) from fiscal year 2014. Sales of scratch games increased by \$29.9 million (3.0 percent) and online sales increased by \$3.2 million (0.4 percent). This is offset by an increase of \$33.4 million (2.6 percent) in total expenses, primarily attributable to the cost of prizes and claims.
- Virginia College Savings Plan's net position increased by \$32.2 million (6.3 percent) during the fiscal year. Although the investment income decreased from the prior year, total revenues still exceeded the increased expenses incurred during fiscal year 2015.
- Unemployment Compensation Fund net position increased by \$259.1 million during fiscal year 2015, primarily as a result of a decrease in benefit claims. Operating expenses decreased by \$104.3 million. These factors combined give the Trust Fund the large increase.

Over the one year period from July 1, 2014, to June 30, 2015, the unemployment rate declined from 5.2 percent to 4.9 percent. Additionally, there were approximately 51,270 fewer initial unemployment claims filed than in the previous year. These declines were accompanied by decreases in the average weekly benefit amounts from approximately \$290.9 to \$290.0 in fiscal year 2015 and decreases in the average benefit duration from 16.3 weeks to 16.0 weeks in fiscal year 2015. These multiple influences led to a decrease in the total benefit payments of \$104.3 million over the prior year.

Figure 15
Business-type Activities
Program Revenues and Expenses
 Fiscal Year 2015
 (Dollars in Thousands)



Fund Statements Financial Analysis

As of the end of the fiscal year, the primary government's governmental funds reported combined ending fund balances of \$4.3 billion, including a negative unassigned fund balance of \$713.1 million indicating that restricted and committed amounts exceed the available modified accrual basis fund balance. The remainder of fund balance is nonspendable, restricted or committed to indicate that it is not available for new spending.

General Fund Highlights

At the end of the fiscal year, the General Fund reported a combined ending fund balance of \$848.4 million, an increase of \$218.7 million in comparison with the prior year. Of this total fund balance, \$120.0 million represents nonspendable fund balance, \$1.1 billion represents restricted fund balance, and \$295.7 million represents committed fund balance. These amounts are offset by a negative \$653.4 million unassigned fund balance.

Fiscal year 2015 General Fund revenues were 3.5 percent, or \$642.6 million, higher than fiscal year 2014 revenues. This revenue change results from increases of \$762.2 million primarily attributable to individual and fiduciary income taxes (\$590.0 million), sales and use taxes (\$94.4 million), deeds, contracts, wills and suits taxes (\$35.4 million) and corporation income taxes (\$22.4 million) offset by decreases of \$119.6 million primarily attributable to interest, dividends, and rents (\$50.3 million), other revenue primarily relating to expenditure recoveries from prior years (\$34.9 million), and premiums of insurance companies taxes (\$14.0 million).

Fiscal year 2015 expenditures increased by 2.6 percent, or \$483.4 million, when compared to fiscal year 2014. This was primarily attributable to increases in individual and family services, education, general government, and administration of justice expenditures of \$262.4 million, \$161.6 million, \$30.2 million, and \$24.6 million, respectively. Net other financing sources and uses increased by \$67.8 million, which is primarily due to lower transfers out to and higher transfers in from nongeneral funds.

Budget Highlights

The General Fund began the year with an original revenue budget that was \$943.0 million, or 5.2 percent, higher than the final fiscal year 2014 revenue budget. Additionally, the final revenue budget was slightly lower (\$624.4 million or 3.3 percent) than the original budget. The change between the original and final budget was primarily attributable to decreases in the final budget for individual and fiduciary income taxes of \$533.6 million and other revenue primarily relating to expenditure recoveries from prior years of \$80.4 million due to revised economic forecasts. This was offset by increases in the final budget for premiums of insurance companies taxes of \$29.6 million and corporation income taxes of \$24.3 million. Total actual General Fund revenues were higher than final budgeted revenues by \$531.1 million due to stronger than anticipated collections.

Total final budget expenditures were lower than original budget expenditures by \$560.8 million, or 2.8 percent. This decrease was primarily attributable to budgeted expenditures for general government of \$561.4 million, individual and family services of \$96.0 million, and education of \$22.4 million, offset in part by increases in resources and economic development of \$56.8 million and administration of justice of \$52.7 million.

The Commonwealth spent less than planned so actual expenditures were \$272.3 million, or 1.4 percent, lower than final budget expenditures.

Budget Outlook

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

While some of the conditions left by the financial and economic downturn experienced between 2008 and 2010 are still visible in certain sectors, Virginia's economy continued to recover, however, at a slower rate than the national level. Data regarding the primary economic indicators – jobs and new housing units provide some improvement. The unemployment rate has decreased from the previous fiscal year while housing indicators show mixed results. During fiscal year 2015 the two General Fund revenue sources most closely tied to current economic activity – individual income taxes and retail sales taxes – experienced increases when compared to the 2014 collections by \$1.1 billion (9.6 percent) and \$169.0 million (5.5 percent), respectively. The individual income tax collections and retail sales taxes were more than the estimated revenue by \$512.4 million (4.3 percent) and \$17.6 million (0.5 percent), respectively. These increases resulted in a strong performance during the second half of the fiscal year.

Although the fiscal year 2015 revenue collections compared to fiscal year 2014 showed improvements over the estimate, the fiscal year 2016 General Fund Revenue estimate calls for a decline of 0.1 percent when compared to the fiscal year 2015 collections. This planned reduction reflects continued uncertainty related to federal spending cuts and concerns in the global market. The Governor will release his amendments to the 2016-2017 biennial budget on December 17, 2015.

Major Special Revenue Fund Highlights

The Commonwealth Transportation Fund ended the fiscal year with a fund balance of \$2.3 billion. Approximately \$3.9 billion is contractually committed for various highways, public transportation, and rail preservation projects (see Note 20). Additionally, revenues and expenditures increased \$434.1 million, or 8.7 percent, and \$284.1 million, or 5.5 percent, respectively. The revenue increase was primarily due to increases in tax collection of \$332.4 million or 11.2 percent and in other revenue of \$68.5 million or 49.7 percent. Expenditures increased mainly for highway maintenance, acquisition, and construction.

The Federal Trust Fund balance decreased by \$19.8 million, or 14.7 percent primarily due to a significant decrease in fines and forfeitures of \$89.4 million, or 93.7 percent, and a decrease in other revenue of \$32.1 million or 22.4 percent, offset by an increase in Federal Grants and Contracts revenue of approximately \$25.3 million and a decrease in expenditures of \$60.1 million. This change in the Federal Grants and Contracts revenue was mainly attributed to an increase in Medicaid funding (\$156.8 million), child and family assistance (\$61.8 million), and public safety (\$12.7 million), offset by decreases of American Recovery and Reinvestment Act revenue (\$21.6 million), unemployment insurance (\$78.8 million), food and home energy assistance programs (\$97.4 million), and education grants (\$28.5 million). The remaining difference is distributed over many other federal programs. Net other financing sources and uses decreased by \$10.9 million, or 89.4 percent primarily attributable to lower transfers in from other funds.

The Literary Fund ended the year with a deficit net position of \$37.5 million and a fund balance decrease of \$51.0 million, or 378.2 percent. These decreases resulted from both operating results and accruals. The net disbursements exceeded net receipts by \$63.4 million, offset by a cash transfer in of \$12.4 million representing unclaimed prizes from the Virginia Lottery (major enterprise). Additionally, loans of \$185.9 million owed to the Virginia Public School Authority (major component unit) exceeded the cash and accrued receivables at year end.

Capital Asset and Long-term Debt

Capital Assets. The primary government's investment in capital assets for its governmental and business-type activities as of June 30, 2015, amounts to \$29.4 billion (net of accumulated depreciation totaling \$16.4 billion). This investment in capital assets includes land, buildings, improvements, equipment, infrastructure, construction-in-progress, and intangible assets including water rights, easements, and software. Infrastructure assets are items that are normally immovable such as roads, bridges, drainage systems, and other similar assets. As noted on page 30, increases in capital assets and deferred outflows of resources offset by increases in total liabilities and deferred inflows of resources resulted in an increase in net position of the governmental activities of \$868.1 million, or 4.7 percent. The increase in the primary government's net investment in capital assets was primarily attributable to increases in infrastructure of \$1.2 billion offset by decreases in construction-in-progress of \$90.5 million. These changes are primarily attributable to transportation. The primary government reports equipment with a value of \$50,000 or greater and an expected useful life of two or more years. The primary government capitalizes all land, buildings, infrastructure, and intangible assets that have a cost or value greater than \$100,000 and an expected useful life of two or more years. Additional information on the primary government's capital assets can be found in Note 12, Capital Assets.

Figure 16
Capital Assets as of June 30, 2015
(Net of Depreciation)
(Dollars in Thousands)

	Governmental Activities	Business-type Activities	Total
Land	\$ 2,935,504	\$ 1,977	\$ 2,937,481
Buildings	2,619,679	17,638	2,637,317
Equipment	485,154	12,149	497,303
Water Rights/Easements	69,770	-	69,770
Infrastructure	18,974,616	-	18,974,616
Software	244,070	3,861	247,931
Construction-in-Progress	4,019,090	4,602	4,023,692
Total	\$ 29,347,883	\$ 40,227	\$ 29,388,110

Long-term Debt. The Commonwealth is prohibited from issuing general obligation bonds for operating purposes. At the end of the current fiscal year, the Commonwealth had total debt outstanding of \$41.9 billion, including total tax-supported debt of \$19.8 billion and total debt not supported by taxes of \$22.2 billion. Bonds backed by the full faith and credit of the government and tax-supported total \$1.6 billion. Debt is considered tax-supported if Commonwealth tax revenues are used or pledged for debt service payments. An additional \$877.9 million is considered moral obligation debt which is not tax-supported. The Commonwealth has no direct or indirect pledge of tax revenues to fund reserve deficiencies. However, in some cases, the Commonwealth has made a moral obligation pledge to consider funding deficiencies in debt service reserves that may occur. The remainder of the Commonwealth's debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

During fiscal year 2015, the Commonwealth issued \$6.4 billion of new debt for various projects. Of this new debt, \$1.4 billion was for the primary government and \$5.0 billion for the component units. Additional information on the Commonwealth's outstanding debt can be found in Note 26, "Long-Term Liabilities," as well as in the section entitled "Debt Schedules." The Commonwealth maintains a "triple A" bond rating for general obligation debt from the three rating agencies: Moody's Investors Service; Standard & Poor's Ratings Group, a division of The McGraw Hill Companies, Inc.; and Fitch, Inc.

State statutes limit the amount of general obligation debt the Commonwealth may issue for each specific type of debt. The 9(a) bonds, which may be issued to fund the defense of the Commonwealth; to meet casual deficits in revenue or in anticipation of the collection of revenues; or to redeem previous debt obligations, and are limited to 30.0 percent of 1.15 times the annual tax revenues for fiscal year 2015. The 9(b) bonds, which have been authorized by the citizens of Virginia through bond referenda to finance capital projects, are limited to 1.15 times the average of selected tax revenues for fiscal years 2013, 2014, and 2015. The 9(c) bonds, which have been issued to finance capital projects that will generate revenue upon their completion, are limited to 1.15 times the average of selected tax revenues for fiscal years 2013, 2014, and 2015. The current debt limitation for the Commonwealth is \$5.8 billion, \$17.6 billion, and \$17.3 billion, respectively, for the 9(a), 9(b), and 9(c) general obligation bond issues. These limits significantly exceed the Commonwealth's outstanding general obligation debt. Currently, there is no 9(a) debt outstanding.

Figure 17
Outstanding Debt as of June 30, 2015
General Obligation Bonds
(Dollars in Thousands)

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
General obligation bonds				
9(b)	\$ 642,181	\$ -	\$ 642,181	\$ -
9(c)	33,190	-	33,190	936,857
Total	<u>\$ 675,371</u>	<u>\$ -</u>	<u>\$ 675,371</u>	<u>\$ 936,857</u>

New Accounting Standard

The Commonwealth implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68*, during fiscal year 2015. The new GASB reporting requirements impact the measurement and recognition of pension-related liabilities, deferred outflows of resources, deferred inflows of resources and pension-related expenses in the Commonwealth's financial statements. As a result of these statements, the beginning net position has been restated for the primary government and component units by \$2.5 billion and \$1.7 billion, respectively, as further discussed in Note 2, "Restatement of Beginning Balances." The following amounts are reported for Net Pension Liability, Deferred Outflows of Resources and Deferred Inflows of Resources in the Commonwealth's financial statements.

	<u>Primary Government</u>	<u>Component Units</u>
Net Pension Liability	\$ 4.3 billion	\$ 2.5 billion
Deferred Outflows of Resources	438.8 million	252.5 million
Deferred Inflows of Resources	768.7 million	473.1 million

While the above amounts are reported for the first time in fiscal year 2015, it is important to note that the Net Pension Obligation was previously reported in both the financial statements and notes to the financial statements. Further, the Unfunded Actuarially Accrued Liability amounts were previously reported in the notes to the financial statements and Required Supplementary Information. Additional information can be found in Note 13, Deferred Inflows and Deferred Outflows of Resources, and Note 15, Retirement and Pension Systems.

Economic Factors and Review

During fiscal year 2015, the Commonwealth's economy saw continued improvement, although at a slower rate than at the national level. The Commonwealth experienced a lower job growth rate than at the national level (0.8 percent at the state level versus 2.2 percent nationally), widening the gap between the Commonwealth's job growth rate and that of the nation during the last fiscal year. Personal income growth reached 3.9 percent during fiscal year 2015, compared to 1.3 percent in fiscal year 2014. This is the highest rate in the last three fiscal years. Unemployment in the Commonwealth and at the national level continued to decline during the fiscal year, reaching 4.9 percent and 5.7 percent, respectively. Total taxable sales in the Commonwealth experienced a considerable increase of 3.9 percent over fiscal year 2014. Economic indicators show that during fiscal year 2015, the housing market in the Commonwealth continued to decline while the national level experienced a slight increase. Additionally, housing prices in the Commonwealth again showed a positive change for fiscal year 2015, with an increase of approximately 2.5 percent, compared to just over 5.0 percent at the national level. Fiscal year 2015 indicates that the Commonwealth's economy will continue to improve; however, because of its dependence on federal government spending measures, the Commonwealth's economy may experience some economic unpredictability in the coming fiscal year.

Requests for Information

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

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

