

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, 2019. 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, 2019, by \$27.2 billion. Net position of governmental activities increased by \$2.5 billion and net position of business-type activities increased by \$405.5 million. Component units reported an increase in net position of \$1.8 billion from June 30, 2018.

Fund Highlights

At the end of the fiscal year, the Commonwealth's governmental funds reported a combined ending fund balance of \$6.9 billion, an increase of \$1.5 billion in comparison with the prior year. Of this total fund balance, \$298.8 million represents nonspendable fund balance, \$2.8 billion represents restricted fund balance, \$4.0 billion represents committed fund balance, and \$34.0 million represents assigned fund balance. These amounts are offset by a negative \$326.8 million unassigned fund balance. The Enterprise Funds reported net position at June 30, 2019, of \$2.5 billion, an increase of \$403.3 million during the year which is primarily attributable to the Virginia College Savings Plan and the Unemployment Compensation Funds. See page 33 for additional information.

The General Fund recognized higher fund assets and deferred outflows of resources, as well as revenues, expenditures, liabilities and deferred inflows of resources when compared to fiscal year 2018. See page 34 for additional information.

Long-term Debt

The Commonwealth's total debt declined during the fiscal year to \$46.5 billion, a decrease of \$590.8 million, or 1.3 percent. While the Commonwealth issued new debt in the amount of \$801.6 million and \$2.2 billion for the primary government and component units, respectively, the fiscal year 2019 debt issuances were lower than the prior year. The new debt issuances coupled with debt retirements decreased the total debt balances for the primary government and component units to \$16.0 billion and \$30.5 billion, respectively.

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 2019. 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 24 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 results 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 15 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 11 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 26 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 is 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 six 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 two external investment pools; and,
- Agency, which accounts for assets held on behalf of others in 18 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 is 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 net pension liability, other postemployment benefit liability plans, and employer contributions for pension and other postemployment benefit plans, 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 223 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 \$27.2 billion during the fiscal year. The net position of the governmental activities increased \$2.5 billion, or 11.1 percent, primarily due to increases in assets 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 15. Business-type activities had an increase of \$405.5 million, or 19.6 percent, primarily due to increases for the Virginia College Savings Plan and the Unemployment Compensation Funds on page 33. As discussed in Note 2, the government-wide beginning balance was restated for the correction of prior year errors to arrive at a restated beginning balance of \$24.3 billion.

Figure 11
Net Position as of June 30, 2019 and 2018
(Dollars in Thousands)

| | Governmental Activities | | Business-type Activities | | Total | |
|---|-------------------------|---------------------|--------------------------|--------------|---------------|---------------------|
| | 2019 | 2018 as restated | 2019 | 2018 | 2019 | 2018 as restated |
| Current and other assets | \$ 16,163,570 | \$ 13,163,311 | \$ 5,127,572 | \$ 4,907,524 | \$ 21,291,142 | \$ 18,070,835 |
| Capital assets | 33,804,048 | 33,319,215 | 40,516 | 33,795 | 33,844,564 | 33,353,010 |
| Total Assets | 49,967,618 | 46,482,526 | 5,168,088 | 4,941,319 | 55,135,706 | 51,423,845 |
| Deferred outflows of resources | 768,171 | 770,090 | 22,844 | 21,071 | 791,015 | 791,161 |
| Total assets and deferred outflows of resources | 50,735,789 | 47,252,616 | 5,190,932 | 4,962,390 | 55,926,721 | 52,215,006 |
| Long-term liabilities outstanding | 13,673,724 | 13,860,886 | 2,286,386 | 2,444,995 | 15,960,110 | 16,305,881 |
| Other liabilities | 7,826,129 | 6,771,756 | 405,509 | 430,295 | 8,231,638 | 7,202,051 |
| Total Liabilities | 21,499,853 | 20,632,642 | 2,691,895 | 2,875,290 | 24,191,748 | 23,507,932 |
| Deferred inflows of resources | 4,493,029 | 4,349,086 | 27,060 | 20,622 | 4,520,089 | 4,369,708 |
| Total liabilities and deferred inflows of resources | 25,992,882 | 24,981,728 | 2,718,955 | 2,895,912 | 28,711,837 | 27,877,640 |
| Net position: | | | | | | |
| Net investment in capital assets | 26,031,917 | 25,524,252 | 39,998 | 33,795 | 26,071,915 | 25,558,047 |
| Restricted | 2,194,477 | 1,935,406 | 1,485,125 | 1,348,816 | 3,679,602 | 3,284,222 |
| Unrestricted | (3,483,487) | (5,188,770) | 946,854 | 683,867 | (2,536,633) | (4,504,903) |
| Total net position | \$ 24,742,907 | \$ 22,270,888 | \$ 2,471,977 | \$ 2,066,478 | \$ 27,214,884 | \$ 24,337,366 |

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

An additional portion of the primary government's net position represents restricted net position. These resources are subject to external restrictions or constitutional provisions specifying how they may be used. The remaining balance of negative \$2.5 billion is unrestricted net position (**Figure 11**).

Approximately 55.6 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 2019, program and general revenues exceeded governmental expenses by \$1.6 billion. Program revenues exceeded expenses from business-type activities by \$1.3 billion. The following condensed financial information (**Figure 12**) was derived from the Government-wide Statement of Activities and provides detail regarding the change in net position (see page 42).

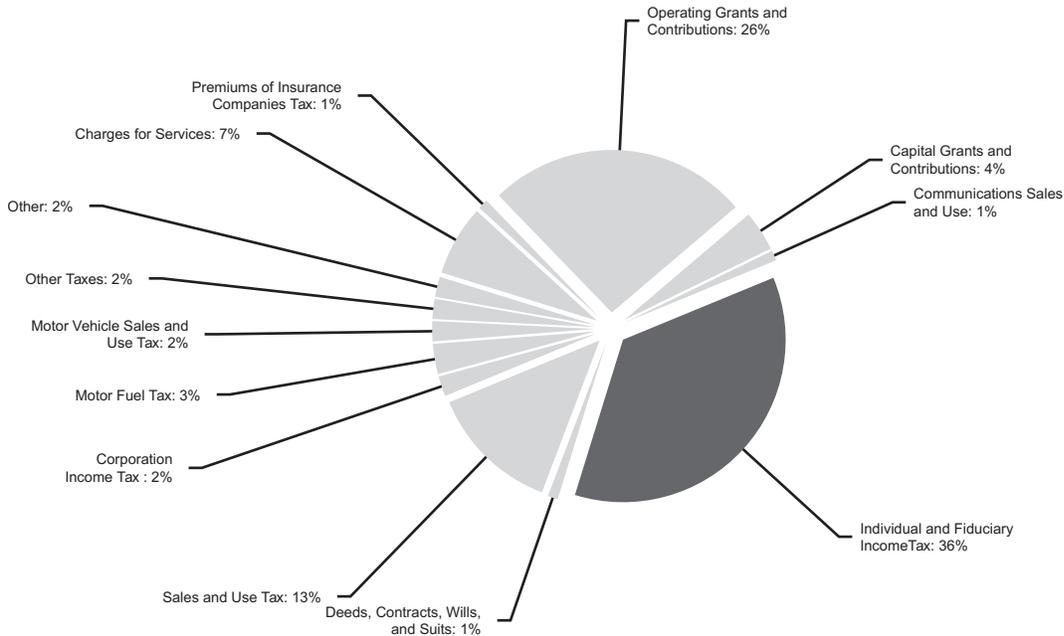
Figure 12
Changes in Net Position for the Fiscal Years Ended June 30, 2019 and 2018
(Dollars in Thousands)

| | Governmental Activities | | Business-type Activities | | Total | |
|---|-------------------------|----------------------|--------------------------|---------------------|----------------------|----------------------|
| | 2018 | | 2019 | 2018 | 2018 | |
| | 2019 | as restated | | | 2019 | as restated |
| Revenues: | | | | | | |
| Program Revenues: | | | | | | |
| Charges for Services | \$ 2,796,618 | \$ 2,747,441 | \$ 4,595,496 | \$ 4,393,515 | \$ 7,392,114 | \$ 7,140,956 |
| Operating Grants and Contributions | 10,927,233 | 9,871,386 | 32 | 542 | 10,927,265 | 9,871,928 |
| Capital Grants and Contributions | 1,528,453 | 1,969,604 | — | — | 1,528,453 | 1,969,604 |
| General Revenues: | | | | | | |
| Taxes: | | | | | | |
| Individual and Fiduciary Income | 14,872,136 | 14,117,735 | — | — | 14,872,136 | 14,117,735 |
| Sales and Use | 5,457,799 | 5,266,818 | — | — | 5,457,799 | 5,266,818 |
| Corporation Income | 923,683 | 851,603 | — | — | 923,683 | 851,603 |
| Motor Fuel | 1,083,719 | 1,031,034 | — | — | 1,083,719 | 1,031,034 |
| Motor Vehicle Sales and Use | 971,987 | 935,101 | — | — | 971,987 | 935,101 |
| Communications Sales and Use | 359,011 | 383,221 | — | — | 359,011 | 383,221 |
| Deeds, Contracts, Wills, and Suits | 442,970 | 505,255 | — | — | 442,970 | 505,255 |
| Premiums of Insurance Companies | 554,299 | 516,743 | — | — | 554,299 | 516,743 |
| Alcoholic Beverage Sales | 174,144 | 160,910 | — | — | 174,144 | 160,910 |
| Tobacco Products | 151,287 | 161,273 | — | — | 151,287 | 161,273 |
| Estate | 216 | 454 | — | — | 216 | 454 |
| Public Service Corporations | 111,996 | 112,131 | — | — | 111,996 | 112,131 |
| Beer and Beverage Excise | 41,249 | 41,394 | — | — | 41,249 | 41,394 |
| Wine and Spirits/ABC Liter | 29,484 | 28,946 | — | — | 29,484 | 28,946 |
| Bank Stock | 29,780 | 23,870 | — | — | 29,780 | 23,870 |
| Other Taxes | 518,694 | 133,674 | 9,141 | 9,141 | 527,835 | 142,815 |
| Unrestricted Grants and Contributions | 60,108 | 60,695 | — | — | 60,108 | 60,695 |
| Investment Earnings | 238,588 | 72,286 | 1,841 | 1,151 | 240,429 | 73,437 |
| Miscellaneous | 368,744 | 524,761 | 414 | 265 | 369,158 | 525,026 |
| Total Revenues | 41,642,198 | 39,516,335 | 4,606,924 | 4,404,614 | 46,249,122 | 43,920,949 |
| Expenses: | | | | | | |
| General Government | 3,217,820 | 3,170,832 | — | — | 3,217,820 | 3,170,832 |
| Education | 11,103,677 | 10,730,908 | — | — | 11,103,677 | 10,730,908 |
| Transportation | 4,927,117 | 5,325,640 | — | — | 4,927,117 | 5,325,640 |
| Resources and Economic Development | 1,027,271 | 972,535 | — | — | 1,027,271 | 972,535 |
| Individual and Family Services | 16,566,424 | 15,604,202 | — | — | 16,566,424 | 15,604,202 |
| Administration of Justice | 2,946,304 | 2,995,238 | — | — | 2,946,304 | 2,995,238 |
| Interest and Charges on Long-term Debt | 256,962 | 167,111 | — | — | 256,962 | 167,111 |
| Virginia Lottery | — | — | 1,642,754 | 1,521,006 | 1,642,754 | 1,521,006 |
| Virginia College Savings Plan | — | — | 61,321 | 294,056 | 61,321 | 294,056 |
| Unemployment Compensation | — | — | 273,566 | 323,214 | 273,566 | 323,214 |
| Alcoholic Beverage Control | — | — | 699,242 | 665,811 | 699,242 | 665,811 |
| Risk Management | — | — | 14,894 | 10,461 | 14,894 | 10,461 |
| Local Choice Health Care | — | — | 473,076 | 459,616 | 473,076 | 459,616 |
| Line of Duty | — | — | 17,836 | 18,403 | 17,836 | 18,403 |
| Virginia Industries for the Blind | — | — | 50,158 | 46,397 | 50,158 | 46,397 |
| Consolidated Laboratory | — | — | 10,552 | 10,470 | 10,552 | 10,470 |
| eVA Procurement System | — | — | 20,797 | 20,079 | 20,797 | 20,079 |
| Department of Environmental Quality Title V | — | — | 10,179 | 10,156 | 10,179 | 10,156 |
| Wireless E-911 | — | — | 44,134 | 43,227 | 44,134 | 43,227 |
| Museum and Library Gift Shops | — | — | 7,221 | 7,695 | 7,221 | 7,695 |
| Behavioral Health Canteen and Work Activity | — | — | 299 | 329 | 299 | 329 |
| Total Expenses | 40,045,575 | 38,966,466 | 3,326,029 | 3,430,920 | 43,371,604 | 42,397,386 |
| Excess before transfers | 1,596,623 | 549,869 | 1,280,895 | 973,694 | 2,877,518 | 1,523,563 |
| Transfers | 875,396 | 826,648 | (875,396) | (826,648) | — | — |
| Increase in net position | 2,472,019 | 1,376,517 | 405,499 | 147,046 | 2,877,518 | 1,523,563 |
| Net position, July 1, as restated | 22,270,888 | 20,894,371 | 2,066,478 | 1,919,432 | 24,337,366 | 22,813,803 |
| Net position, June 30 | \$ 24,742,907 | \$ 22,270,888 | \$ 2,471,977 | \$ 2,066,478 | \$ 27,214,884 | \$ 24,337,366 |

Governmental Activities Revenues

Figure 13 is a graphical representation of the Statement of Activities revenues for governmental activities. Governmental activities revenues increased by \$2.1 billion, or 5.4 percent. The net increase is mainly attributable to increases in the General Fund, which are discussed on page 34.

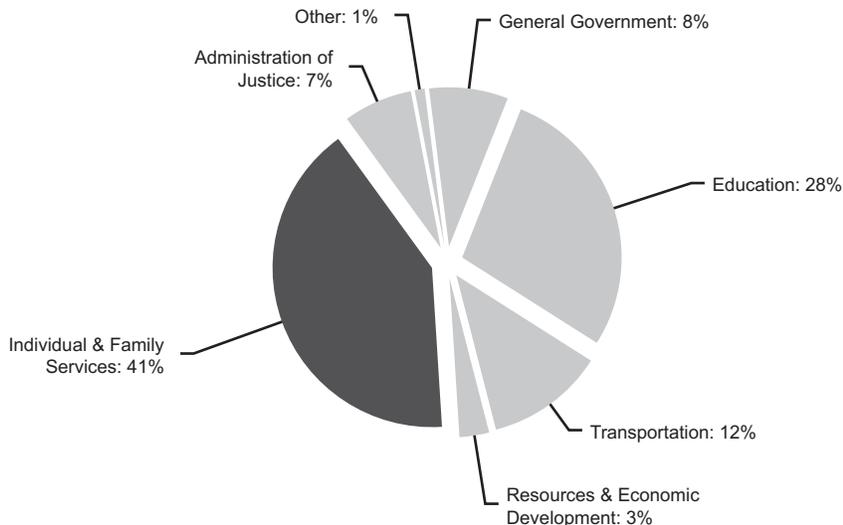
**Figure 13
Revenues by Source – Governmental Activities
Fiscal Year 2019**



Governmental Activities Expenses

Figure 14 is a graphical representation of the Statement of Activities expenses for governmental activities. Governmental activities expenses increased by \$1.1 billion, or 2.8 percent. This change is primarily attributable to increases in all expense types with the exception of transportation and administration of justice. See pages 34 and 35 for additional information.

**Figure 14
Expenses by Type – Governmental Activities
Fiscal Year 2019**



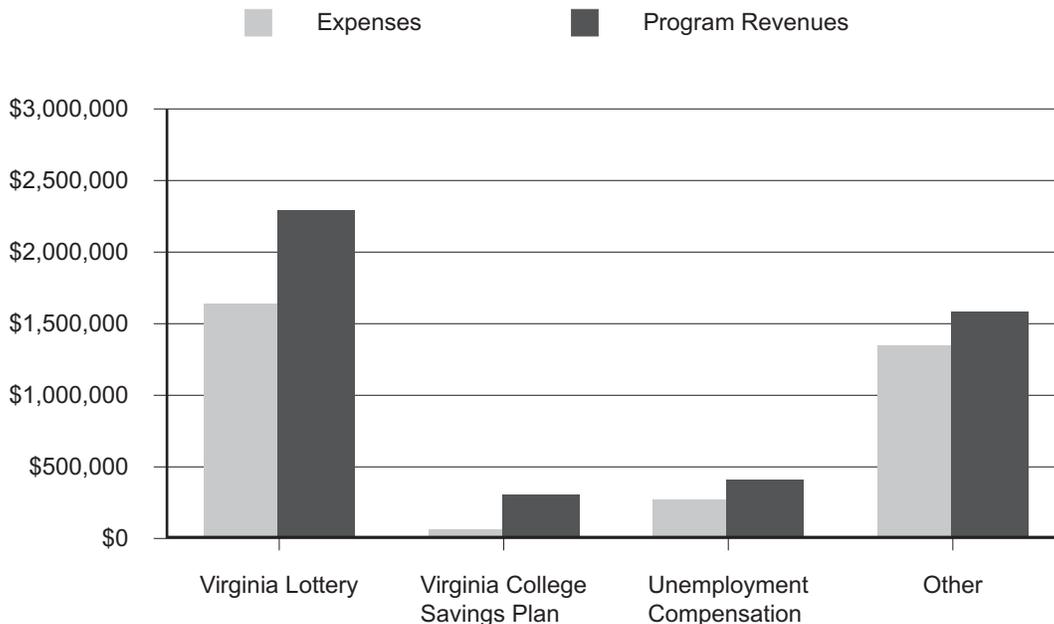
Net Position of Business-type Activities

Net position of business-type activities increased by \$405.5 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 \$2.3 billion, an increase of \$153.7 million over the prior year. Net income was \$653.5 million, an increase of \$33.2 million (5.4 percent) from fiscal year 2018. Sales of scratch games increased by \$37.3 million (3.1 percent) and online sales increased by \$116.5 million (12.2 percent). Additionally, there is an increase of \$121.8 million (8.0 percent) in total expenses, primarily attributable to the cost of prizes.
- Virginia College Savings Plan's net position increased by \$244.8 million (31.2 percent) during the fiscal year as a result of total revenues exceeding expenses incurred.
- Unemployment Compensation Fund net position increased by \$135.9 million during fiscal year 2019, as a result of a decrease in benefit claims and operating revenue exceeding operating expenses.

Over the one-year period from July 1, 2018, to June 30, 2019, the unemployment rate declined from 3.3 percent to 2.9 percent. Additionally, there were approximately 14,212 fewer initial unemployment claims filed than in the previous year. These declines were accompanied by a decrease in the average benefit duration from 15.6 weeks to 14.4 weeks in fiscal year 2019. These decreases were offset by an increase in the average weekly benefit amounts from approximately \$299.8 million to \$304.7 million in fiscal year 2019. These multiple influences led to a decrease in the total benefit payments of \$49.6 million over the prior year.

Figure 15
Business-type Activities
Program Revenues and Expenses
Fiscal Year 2019
(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 \$6.9 billion, including a negative unassigned fund balance of \$326.8 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 \$1.6 billion, an increase of \$759.2 million in comparison with the prior year. Of this total fund balance, \$102.7 million represents nonspendable fund balance, \$669.5 million represents restricted fund balance, and \$1.1 billion represents committed fund balance. These amounts are offset by a negative \$264.2 million unassigned fund balance.

Fiscal year 2019 General Fund revenues were 3.5 percent, or \$756.5 million, higher than fiscal year 2018 revenues. This revenue change results from increases of \$1.1 billion primarily attributable to individual and fiduciary income taxes (\$694.9 million), interest, dividends, and rents (\$138.8 million), sales and use taxes (\$116.4 million), corporation income taxes (\$44.5 million), premiums of insurance companies taxes (\$43.1 million), and alcoholic beverage sales tax (\$13.2 million), offset by decreases of \$326.9 million primarily attributable to other revenue predominantly related to prior year expenditures refunded in the current fiscal year (\$260.6 million), communications sales and use taxes (\$23.7 million), sales of property and commodities (\$20.8 million), and tobacco product taxes (\$10.3 million).

Fiscal year 2019 expenditures increased by 2.0 percent, or \$433.2 million, when compared to fiscal year 2018. This was primarily attributable to increases in education and administration of justice expenditures of \$339.4 million and \$39.7 million, respectively. Net other financing sources and uses increased by \$90.9 million, which is primarily due to higher transfers in from nongeneral funds and a decrease in transfers out to nongeneral funds.

Budget Highlights

The General Fund began the year with an original revenue budget that was \$895.3 million, or 4.3 percent, higher than the final fiscal year 2018 revenue budget. Additionally, the final revenue budget was slightly higher (\$274.2 million or 1.3 percent) than the original budget. The change between the original and final budget was primarily attributable to increases in the final budget for individual and fiduciary income taxes of \$237.8 million, corporation income taxes of \$100.2 million, and sales and use taxes of \$47.0 million. This was offset by decreases in the final budget for communications sales and use taxes of \$28.5 million, deeds, contracts, wills, and suits taxes of \$29.9 million, tobacco products taxes of \$19.2 million, and other revenue primarily related to prior year expenditures refunded in the current fiscal year of \$70.3 million. Total actual General Fund revenues were higher than final budgeted revenues by \$787.6 million due to stronger actual than anticipated collections.

Total final budget expenditures were higher than original budget expenditures by \$410.2 million, or 1.8 percent. This increase was primarily attributable to budgeted expenditures for individual and family services of \$197.5 million, education of \$118.8 million, and administration of justice of \$44.1 million.

The Commonwealth spent less than planned so actual expenditures were \$508.1 million, or 2.2 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.

Virginia economic growth remained at a moderate pace in fiscal year 2019. Employment growth slowed slightly compared to the year before but was enough to put continued pressure on state labor markets. The state unemployment rate has recovered what it had lost during the recession and all areas of the state experienced unemployment rate improvements. Virginia housing market performance saw existing home sales and building permits issuance decrease while home price growth slowed. The state continued to trail the nation in growth on most major economic indicators such as employment, personal income, new housing permits, and housing prices. During fiscal year 2019, 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 2018 collections by \$1.1 billion (7.9 percent) and \$118.6 million (3.4 percent), respectively. The individual income tax collections were more than the estimated revenue by \$804.9 million (5.6 percent) and the retail sales taxes were less than the estimated revenue by \$10.7 million (0.3 percent).

The fiscal year 2019 revenue collections exceeded fiscal year 2018 and exceeded the fiscal year 2019 collections estimate. Based on the most recent General Fund revenue estimate, the fiscal year 2020 revenue is projected to increase 1.2 percent over the fiscal year 2019 revenue collections. This planned increase is a result of continued growth in individual income taxes and retail sales taxes. The Governor will release his amendments to the 2019-2020 biennial budget on December 17, 2019.

Major Special Revenue Fund Highlights

The Commonwealth Transportation Fund ended the fiscal year with a fund balance of \$2.9 billion. Approximately \$6.5 billion is contractually committed for various highways, public transportation, and rail preservation projects; \$978.0 million for individual contracts awarded with a contract value of \$1.0 million or more for operational and tolling services, facilities, and other non-highway construction-type contracts (see Note 22). Additionally, revenues decreased \$54.7 million, or 0.9 percent, and expenditures decreased \$568.4 million, or 9.3 percent. The revenue decrease was primarily due to decreases in other revenue of \$432.4 million, or 74.0 percent, offset by increases in tax collections of \$122.1 million, or 3.3 percent, and in federal income of \$122.9 million, or 12.8 percent. Expenditures decreased mainly for highway maintenance, acquisition, and construction.

The Federal Trust Fund balance increased by \$20.1 million, or 18.7 percent, primarily due to an increase in Federal Grants and Contracts revenue of approximately \$1.3 billion, or 14.0 percent, and a decrease in other revenue of \$229.0 million, or 98.0 percent, offset by a significant increase in expenditures of \$1.0 billion. This change in the Federal Grants and Contracts revenue was mainly attributed to an increase in Medicaid funding (\$1.0 billion). The remaining difference is distributed over many other federal programs. The Other revenue decrease is associated with timing of Medicaid Rebate collections. Expenditures increased primarily due to Medicaid spending. Net other financing sources and uses experienced an increase of \$6.8 million, or 44.9 percent, primarily attributable to lower transfers out to other funds.

The Literary Fund ending balance increased by \$16.8 million, or 1,623.1 percent. Additionally, while expenditures exceeded net receipts by \$115.2 million in fiscal year 2019, this is a significant improvement over the fiscal year 2018 operating results. The loans of \$189.9 million owed to the Virginia Public School Authority (major component unit) decreased by \$6.4 million, or 3.2 percent, and the transfers from other funds decreased by \$47.2 million, or 26.3 percent.

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, 2019, amounts to \$33.8 billion (net of accumulated depreciation totaling \$14.9 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 offset by increases in total liabilities and deferred inflows of resources resulted in an increase in net position of the governmental activities of \$2.5 billion, or 11.1 percent. The increase in the primary government's net investment in capital assets was primarily attributable to increases in infrastructure of \$530.3 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 14, Capital Assets.

Figure 16
Capital Assets as of June 30, 2019
(Net of Depreciation)
(Dollars in Thousands)

| | Governmental Activities | Business-type Activities | Total |
|--------------------------|----------------------------|-----------------------------|----------------------|
| Land | \$ 3,455,082 | \$ 1,874 | \$ 3,456,956 |
| Buildings | 2,734,880 | 9,923 | 2,744,803 |
| Equipment | 513,794 | 15,052 | 528,846 |
| Water Rights/Easements | 105,526 | — | 105,526 |
| Infrastructure | 22,734,396 | — | 22,734,396 |
| Software | 490,031 | 4,654 | 494,685 |
| Construction-in-Progress | 3,770,339 | 9,013 | 3,779,352 |
| Total | <u>\$ 33,804,048</u> | <u>\$ 40,516</u> | <u>\$ 33,844,564</u> |

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 \$46.5 billion, including total tax-supported debt of \$21.7 billion and total debt not supported by taxes of \$24.8 billion. Bonds backed by the full faith and credit of the government and tax-supported total \$1.3 billion. Debt is considered tax-supported if Commonwealth tax revenues are used or pledged for debt service payments. An additional \$926.5 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 2019, the Commonwealth issued \$3.0 billion of new debt for various projects. Of this new debt, \$801.6 million was for the primary government and \$2.2 billion for the component units. Additional information on the Commonwealth's outstanding debt can be found in Note 28, Long-Term Liabilities, as well as in the Debt Schedules beginning on page 300. The Commonwealth maintains a "triple A" bond rating for general obligation debt from the three rating agencies: Moody's Investors Service, S & P Global Ratings, and Fitch Ratings.

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, are limited to 30.0 percent of 1.15 times the annual tax revenues for fiscal year 2019. 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 2017, 2018, and 2019. 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 2017, 2018, and 2019. The current debt limitation for the Commonwealth is shown below for the 9(a), 9 (b), and 9(c) general obligation bond issues. These limits significantly exceed the Commonwealth's outstanding general obligation debt.

Figure 17
Debt Issuance Margin and Outstanding Debt as of June 30, 2019
General Obligation Bonds
(Dollars in Thousands)

| | Debt Issuance Margin | Outstanding Debt | | | |
|--------------------------|----------------------|-------------------------|--------------------------|------------|-----------------|
| | | Primary Government | | | Component Units |
| | | Governmental Activities | Business-type Activities | Total | |
| General obligation bonds | | | | | |
| 9(a) | \$ 6,802,826 | \$ — | \$ — | \$ — | \$ — |
| 9(b) | 21,108,294 | 401,873 | — | 401,873 | — |
| 9(c) | 20,602,433 | 14,628 | — | 14,628 | 893,106 |
| Total | | \$ 416,501 | \$ — | \$ 416,501 | \$ 893,106 |

Economic Factors and Review

During fiscal year 2019, the Commonwealth's economy continued to improve at a similar pace as the prior year. The Commonwealth experienced a lower job growth rate than at the national level (0.9 percent at the state level versus 1.7 percent nationally). Personal income growth reached 4.9 percent during fiscal year 2019, compared to 4.1 percent in fiscal year 2018. However, it lagged behind the national level (5.1 percent), as it has for past several fiscal years. Unemployment in the Commonwealth and at the national level continued to improve during the fiscal year, reaching 2.9 percent and 3.8 percent, respectively. During fiscal year 2019, total taxable sales growth in the Commonwealth mirrored fiscal year 2018, remaining at 1.9 percent. Economic indicators show that during fiscal year 2019, the housing market in the Commonwealth experienced a 1.0 percent decrease compared to an increase of 1.7 percent in fiscal year 2018. Additionally, housing prices in the Commonwealth again showed a positive change for fiscal year 2019, with an increase of approximately 4.4 percent, compared to just over 5.7 percent at the national level. Many major economic indicators show that the Commonwealth's growth was moderately slow during the fiscal year as it has been during most of the economic expansion. The Commonwealth continues to fall behind the nation in most areas, which reflects its reliance on the slower growing federal employment and other less unstable industries.

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.