
INTRODUCTORY SECTION

Comptroller's Letter of Transmittal to the Governor
Certificate of Achievement for Excellence in Financial Reporting
Organization of Executive Branch of Government
Organization of Government – Selected Government Officials – Executive Branch
Organization of the Department of Accounts



COMMONWEALTH of VIRGINIA

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COMPTROLLER

Office of the Comptroller

P. O. BOX 1971
RICHMOND, VIRGINIA 23218-1971

December 15, 2014

The Honorable Terence R. McAuliffe
Governor of the Commonwealth of Virginia
State Capitol
Richmond, Virginia 23219

Dear Governor McAuliffe:

It is my pleasure to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2014, in accordance with Section 2.2-813 of the *Code of Virginia*. This report consists of management's representations concerning the Commonwealth of Virginia's finances. Management assumes full responsibility for the completeness and reliability of all information presented. This report reflects my commitment to you, to the citizens of the Commonwealth, and to the financial community to maintain our financial statements in conformance with accounting principles generally accepted in the United States of America (GAAP) as established by the Governmental Accounting Standards Board (GASB). Data presented in this report is believed to be accurate in all material respects, and all disclosures that are necessary to enable the reader to obtain a thorough understanding of the Commonwealth's financial activities have been included.

The 2014 CAFR is presented in three sections. The Introductory Section includes this transmittal letter and organization charts for state government. The Financial Section includes the State Auditor's Report, management's discussion and analysis (MD&A), audited government-wide and fund financial statements and notes thereto, required supplementary information other than MD&A, and the underlying combining and individual fund financial statements and supporting schedules. The Statistical Section sets forth selected unaudited economic, financial trend, and demographic information for the Commonwealth on a multi-year basis.

The Commonwealth's management is responsible for the establishment and maintenance of internal accounting controls that ensure assets are safeguarded and financial transactions are properly recorded and adequately documented. To ensure that the costs of controls do not exceed the benefits obtained, management is required to use cost estimates and judgments to attain reasonable assurance as to the adequacy of such controls. The Commonwealth's established internal controls fulfill these requirements and provide reasonable, but not absolute assurance, that the accompanying financial statements are free of material misstatement.

In accordance with Section 30-133 of the *Code of Virginia*, the Auditor of Public Accounts has audited the Commonwealth's financial statements for the year ended June 30, 2014. The audit was conducted in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards issued by the Comptroller General of the United States. The auditor's opinion is included in the Financial Section of this report. Audit testing for compliance with the Federal Single Audit Act Amendments of 1996 and the related OMB Circular A-133 is performed at the statewide level. The Commonwealth's Single Audit Report will be issued at a later date. I would like to acknowledge the Auditor of Public Accounts' staff for their many contributions to the preparation of this report.

GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, requires that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of MD&A. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. In addition to the financial analysis addressing the Commonwealth's governmental and business-type activities, the MD&A focuses on the Commonwealth's major funds: General, Commonwealth Transportation Special Revenue, Federal Trust Special Revenue, Literary Special Revenue, Virginia Lottery, Virginia College Savings Plan, and Unemployment Compensation. The Commonwealth's MD&A can be found on page 27 immediately following the independent auditor's report.

PROFILE OF THE GOVERNMENT

Reporting Entity

For financial reporting purposes, the Commonwealth's reporting entity consists of (1) the primary government, (2) component unit organizations for which the primary government is financially accountable (blended component units), and (3) other component unit organizations for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete (discrete component units). The funds and accounts of all agencies, boards, commissions, foundations, and authorities that have been identified as part of the primary government or a component unit have been included. Further information can be found in Note 1.B. to the Financial Statements.

Section 2100 of the GASB *Codification of Governmental Accounting and Financial Reporting Standards* describes the criteria for determining which organizations, functions, and activities should be considered part of the Commonwealth for financial reporting purposes. The basic criteria include appointing a voting majority of an organization's governing body, as well as the Commonwealth's ability to impose its will on that organization, or the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Commonwealth. The Commonwealth's discretely presented major component units are the Virginia Housing Development Authority, Virginia Public School Authority, Virginia Resources Authority, and Virginia College Building Authority.

The Commonwealth and its component units provide a wide range of services and funding to its citizens, including elementary, secondary and higher education; health and human services; economic development; environment and natural resources; public safety, corrections, and regulation; transportation; agriculture; and general government services. The financial activities associated with these services are reflected in both summary and detail throughout the CAFR.

Budgetary Control

In addition to the internal controls previously discussed, the Commonwealth maintains budgetary controls to ensure compliance with the legal provisions of the Commonwealth's Appropriation Act, which reflects the General Assembly's approval of a biennial budget. The financial transaction process begins with development and approval of the budget, after which budgetary control is maintained through a formal appropriation and allotment system. The budgeted amounts reflected in the accompanying financial statements represent summaries of agency budgets.

The Commonwealth's budget is prepared principally on a cash basis and represents appropriations as authorized by the General Assembly on a biennial basis at the program level. The Commonwealth monitors spending activity to ensure the expenditures do not exceed the appropriated amounts at the agency level. The State Comptroller maintains a central general ledger that records total appropriations and related expenditures for all agencies and institutions included in the approved budget. Systemic controls are in place to prevent disbursements that exceed authorized appropriations. Additional information regarding the Commonwealth's budgetary process can be found in Note 1.E. to the Financial Statements.

ECONOMIC REVIEW

Local Economy

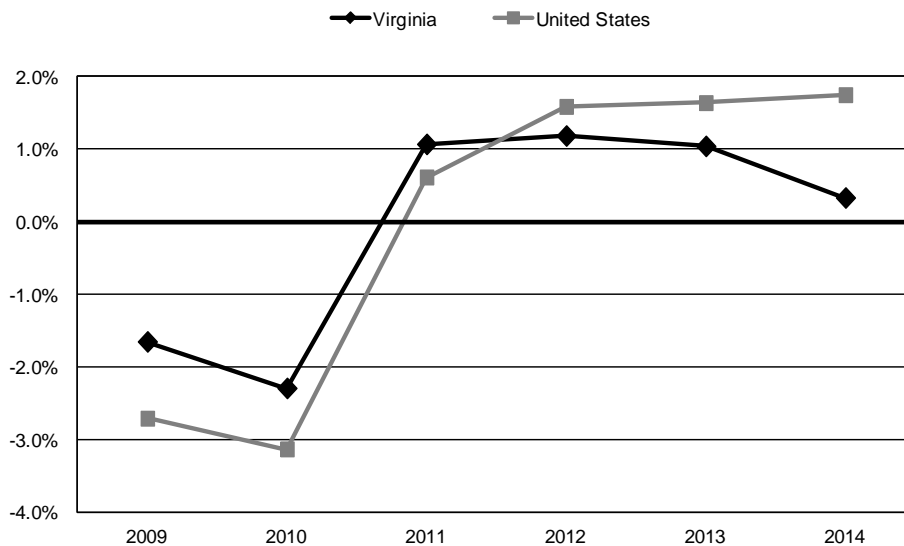
Introduction

This overview of the economy of the Commonwealth of Virginia was prepared by the Center for Urban and Regional Analysis (CURA) at Virginia Commonwealth University. In fiscal year 2014, Virginia's economy continued its recovery from the recession of 2008-10. Yet the pace of recovery, which began to slow in fiscal year 2013, slowed further still in fiscal year 2014. Indicators such as jobs and new housing units, in particular, show that the current expansion, which looked very promising in fiscal years 2011 and 2012, has tapered off and this is cause for concern.

Employment

While the recession experienced between 2008 and 2010 – and the loss of almost 150,000 jobs – is now in the past, the steady increase of around 1.0 percent in employment observed between 2011 and 2013 seems to have slowed down in this past fiscal year. In fiscal year 2014, in fact, Virginia's employment grew only by 0.3 percent, increasing the gap with the national level, where nonfarm payroll employment has increased by 1.7 percent (see **Figure 1**). While this is the fourth consecutive year of job growth in Virginia, it must be noted how in fiscal year 2014 only 12,400 jobs have been added to the economy (compared to nearly 40,000 during fiscal year 2013). This slowdown is troubling, especially when compared with the nation's more robust economic performance over this period. Moreover, uncertainty in the global economy, caused principally by the weakness of the Euro zone and by crises in the Middle East and in West Africa, may portend more trouble ahead for Virginia's economy.

Figure 1
Annual Percentage Change in Nonfarm Payroll Employment
Fiscal Years 2009 - 2014



Source: U. S. Bureau of Labor Statistics

Virginia's lackluster economic performance in fiscal year 2014 is due mostly to employment declines in the Professional and Business Services and the Federal Government sectors, which lost a combined total of roughly 18,000 jobs. **Figure 2** shows changes in Virginia's nonfarm employment by industry for fiscal years 2009 through 2014, along with the employment change between fiscal years 2013 and 2014 for Virginia and the U.S. While it is important that Virginia continued on the trend initiated in fiscal year 2011, and reaffirmed in fiscal years 2012 and 2013, it is undeniable that some economic sectors had a poor performance during fiscal year 2014. Six NAICS industries out of the 15 considered, have lost jobs. This creates uncertainty for the future, especially in traditionally important sectors like Professional and Business Services and Manufacturing. On the other end of the spectrum, some good news came from Wholesale Trade, which continued the employment gains posted in fiscal year 2013, and Educational and Health Services, which added nearly 14,000 jobs on top of the 13,000 added in the previous year.

Figure 2
Nonfarm Payroll Employment
Fiscal Years 2009 - 2014

NAICS Industry*	Virginia Employment (000)						Change, Fiscal Year 2014 over Fiscal Year 2013		
	2009	2010	2011	2012	2013	2014	Virginia		U. S.
							Number (000)	Percent	Percent
Mining and Logging	10.9	10.1	10.7	11.1	10.4	9.9	(0.5)	(4.8)	3.9
Construction	206.2	184.1	181.5	177.3	176.9	178.3	1.4	0.8	3.2
Manufacturing	252.5	233.1	230.0	231.5	231.3	229.9	(1.4)	(0.6)	0.6
Wholesale Trade	116.6	110.0	111.2	111.2	111.5	111.6	0.1	0.1	1.8
Retail Trade	409.3	396.9	400.1	404.6	406.8	412.5	5.7	1.4	2.1
Transportation and Utilities	116.2	112.0	114.2	115.4	116.2	116.0	(0.2)	(0.2)	1.7
Information Services	84.5	77.9	75.0	72.5	71.4	70.6	(0.8)	(1.1)	(0.5)
Financial Activities	184.5	178.1	180.6	185.3	190.8	193.5	2.7	1.4	1.0
Professional and Business Services	649.9	641.3	660.0	673.3	682.3	669.0	(13.3)	(1.9)	3.7
Educational and Health Services	456.9	462.6	472.7	478.9	491.6	505.5	13.9	2.8	1.8
Leisure and Hospitality	345.1	339.6	345.5	354.1	362.8	366.6	3.8	1.0	3.2
Other Services	187.8	184.9	185.8	190.0	193.4	195.6	2.2	1.1	0.6
Federal Government	163.2	171.0	174.6	173.9	175.2	170.9	(4.3)	(2.5)	(2.6)
State Government	153.5	153.1	154.8	157.9	159.4	160.7	1.3	0.8	0.1
Local Government	382.3	379.4	376.3	379.5	375.2	377.0	1.8	0.5	0.3
Total	3,719.4	3,634.1	3,673.0	3,716.5	3,755.2	3,767.6	12.4	0.3	1.7

Source: U. S. Bureau of Labor Statistics; some prior year numbers have been revised to reflect the incorporation of newly available and revised source data

* North American Industry Classification System

Figure 3 shows the annual percentage change in nonfarm employment for 10 of the 11 Metropolitan Statistical Areas (MSAs) in Virginia. The Kingston-Bristol MSA is not included in this table because most of it is located in Tennessee and data for this indicator are not reported separately for the Virginia portion of the MSA. Except for Danville and Lynchburg, all other MSAs added jobs in fiscal year 2014, following on the recovery path that started in fiscal year 2011. Danville's employment losses are disappointing, since the region had grown by 1.1 percent in fiscal year 2011 and by 2.0 percent in fiscal year 2012, but by only 0.3 percent in fiscal year 2013. Following the long-term trend, the Richmond MSA, Northern Virginia MSA and Virginia Beach-Norfolk-Newport News MSA maintain their prominent roles in the economy, accounting for more than 82.0 percent of Virginia's nonfarm payroll employment. All three MSAs experienced growth in fiscal year 2014, adding a total of more than 16,000 jobs (although this increase is much less than the 39,000 jobs added in fiscal year 2013).

Figure 3
Nonfarm Payroll Employment in Virginia's MSAs
Fiscal Years 2009 - 2014

Area	Percent Change					
	2009	2010	2011	2012	2013	2014
Virginia	(1.4)	(2.3)	1.1	1.2	1.0	0.3
Metropolitan areas^(a)						
Blacksburg-Christiansburg-Radford	(0.6)	(3.7)	0.9	2.5	1.8	1.8
Charlottesville	(1.6)	(1.9)	0.7	2.0	1.4	0.5
Danville	(1.4)	(4.0)	1.1	2.0	0.3	(1.8)
Harrisonburg	(1.7)	(1.7)	1.9	0.8	0.9	0.7
Lynchburg	(1.5)	(4.1)	(0.6)	(0.8)	0.3	(0.5)
Northern Virginia	(0.8)	(0.7)	2.0	1.9	1.4	0.4
Richmond	(1.9)	(3.1)	0.8	1.9	1.8	1.5
Roanoke	(2.2)	(2.8)	0.3	1.0	0.9	0.1
Virginia Beach-Norfolk-New port News ^(b)	(2.3)	(2.5)	0.1	0.6	1.1	0.2
Winchester ^(c)	(3.5)	(2.6)	3.1	2.7	1.9	2.2

Source: U. S. Bureau of Labor Statistics; some prior year numbers have been revised to reflect the incorporation of newly available and revised source data

(a) Excludes Kingsport-Bristol MSA, most of which is located in Tennessee

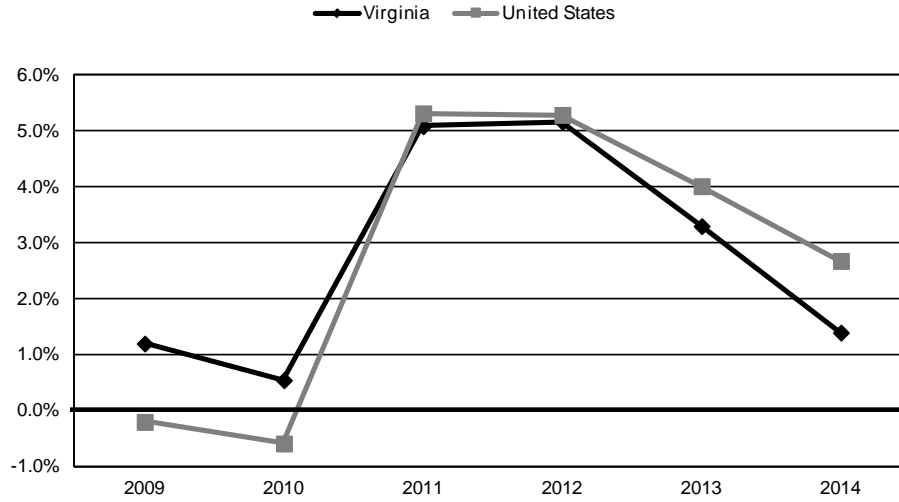
(b) Includes portion in North Carolina

(c) Includes portion in West Virginia

Personal Income

Personal income is an important indicator of the health of Virginia's economy because most state government revenues – income taxes and retail sales taxes in particular – are directly or indirectly related to personal income. As shown in **Figure 4**, the remarkable post-recession growth of fiscal years 2011, 2012 and, to a lesser extent, 2013, has moderated significantly in fiscal year 2014. Although the growth rate has slowed down both at the state and national level, the gap between Virginia and the rest of the country is widening – while average personal income in the U.S. has grown by 2.7 percent, Virginia residents have experienced an increase of just 1.4 percent.

Figure 4
Percentage Change in Personal Income
 Fiscal Years 2009 - 2014

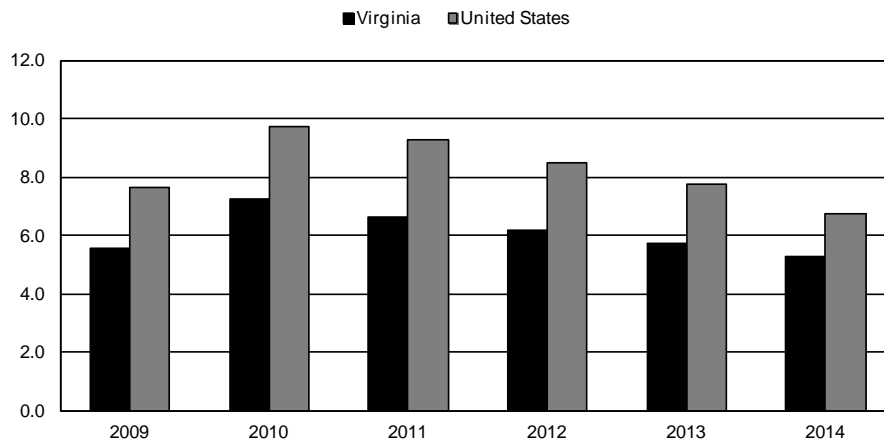


Source: U.S. Bureau of Economic Analysis, Regional Economic Information System

Unemployment

The unemployment rate, both at the state and national levels, continues its post-recession decline of 0.5 percentage points each year for fiscal years 2011 to 2013. In fiscal year 2014, the unemployment rate in Virginia declined to 5.2 percent, significantly lower than the 6.8 percent observed nationally. Although these values are still far from the low unemployment rates of the pre-recession period (in fiscal year 2007, the rates were 3.0 percent in Virginia and 4.5 percent in the U.S. overall), this decline seems consistent with a generally recovering economy. (Note, however, that we did not analyze labor force participation rates, which might complicate this generally positive picture.)

Figure 5
Civilian Unemployment Rate
 Fiscal Years 2009 - 2014



Source: U.S. Bureau of Labor Statistics

Figure 6 shows unemployment rates for each of Virginia's MSAs over the last six fiscal years. Each MSA has posted steady decreases in unemployment since 2011, with Northern Virginia (4.3 percent) and Charlottesville (4.4 percent) currently performing the best.

Figure 6
Civilian Unemployment Rate for Virginia's MSAs
 Fiscal years 2009 – 2014

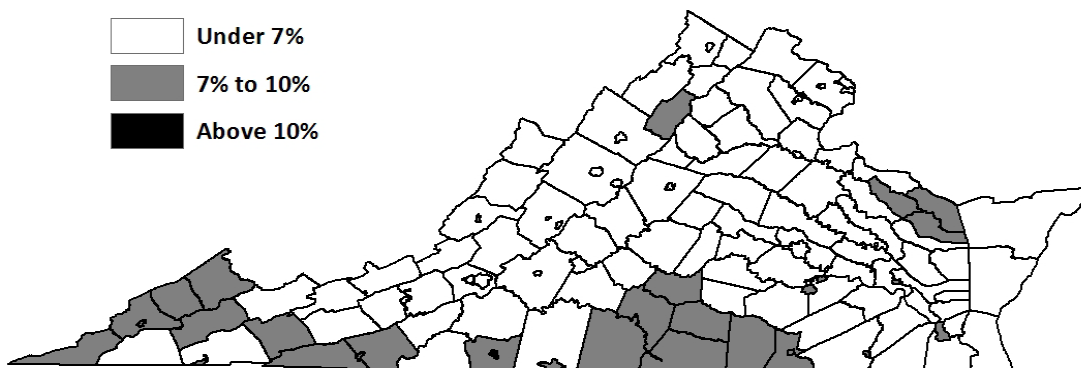
Area	Unemployment Rate (Percent)					
	2009	2010	2011	2012	2013	2014
Virginia	5.6	7.3	6.7	6.2	5.8	5.2
Metropolitan areas						
Blacksburg-Christiansburg-Radford	7.0	8.8	7.6	6.7	6.5	5.6
Charlottesville	4.7	6.2	5.6	5.3	4.8	4.4
Danville	10.4	12.3	10.7	9.1	8.3	7.4
Harrisonburg	5.2	6.9	6.6	6.2	5.7	5.1
Kingsport-Bristol*	7.2	9.5	8.8	7.9	7.4	6.7
Lynchburg	6.1	8.1	7.6	7.1	6.6	5.9
Northern Virginia*	4.2	5.5	5.0	4.7	4.5	4.3
Richmond	6.1	8.2	7.5	6.8	6.2	5.6
Roanoke	5.7	7.9	7.1	6.4	6.0	5.5
Virginia Beach-Norfolk-Newport News*	5.7	7.5	7.2	6.9	6.3	5.8
Winchester*	6.4	7.8	6.8	6.2	5.4	4.8

Source: U.S. Bureau of Labor Statistics; some prior year numbers have been revised to reflect the incorporation of newly available and revised source data

* Includes only the portion of the MSA located in Virginia

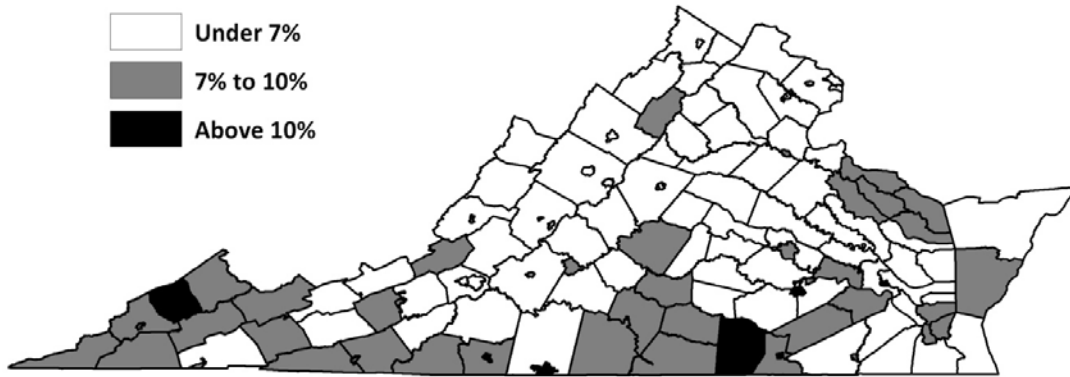
In **Figure 7a**, each of Virginia's localities (95 counties and 39 independent cities) is color coded according to its unemployment rate. Three categories are represented on the map: unemployment rates that are under 7.0 percent, 7.0 to 10.0 percent, and above 10.0 percent. For fiscal year 2014 almost all jurisdictions with an employment rate above the state average (5.2 percent) are located in the South Central and Southwestern parts of the Commonwealth. However, a comparison of fiscal year 2014 with fiscal year 2013 (shown in **Figure 7b**), indicates that several localities improved their performance over the course of the year. (Note, again, that we did not analyze changes in labor force participation rates.)

Figure 7a
Unemployment Rate by Locality
 Fiscal Year 2014



Source: Virginia Employment Commission

Figure 7b
Unemployment Rate by Locality
 Fiscal Year 2013

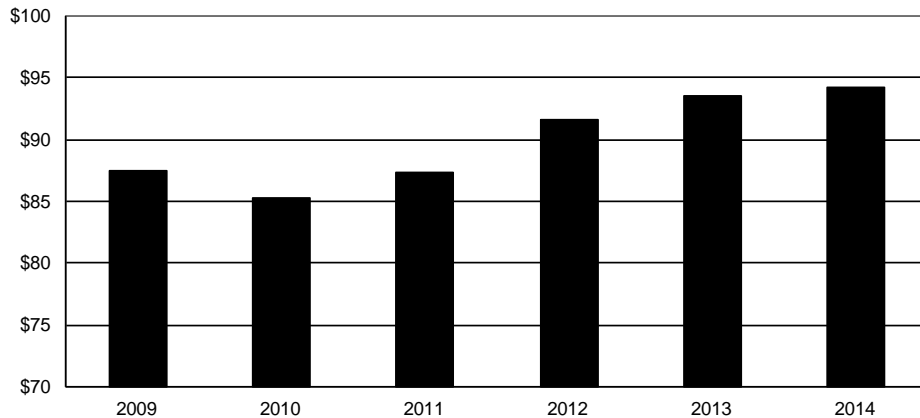


Source: Virginia Employment Commission

Taxable Sales

Since current data on retail sales are not produced for states, this report follows the approach used in previous reports and presents information on taxable sales. These data are used as a proxy for retail sales, even though they do not include motor vehicle and motor fuel sales. (Unlike the Census Bureau’s data on retail sales, however, taxable sales data includes sales at restaurants and lodging places.) **Figure 8** shows that in fiscal year 2014, taxable sales in Virginia continued to increase, albeit at a slower pace than what was observed for the period 2011 through 2013. During fiscal year 2014, Virginia had taxable sales of more than \$94.0 billion.

Figure 8
Taxable Sales in Virginia
 Fiscal Years 2009 - 2014
 (Billions of Dollars)

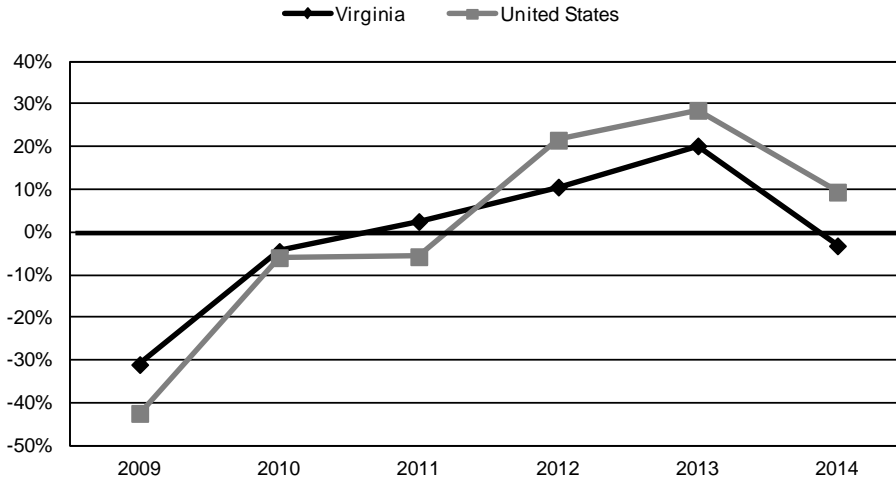


Source: Weldon Cooper Center for Public Service, University of Virginia. Originally from the Virginia Department of Taxation.

Housing Market

After three fiscal years of annual increases in new housing construction – from 2.5 percent in 2011 to 20.3 percent in 2013 – Virginia suffered a decline of 3.1 percent in new housing units authorized for construction in fiscal year 2014 (see **Figure 9**). At the national level, by contrast, building permits increased by almost 10.0 percent during the same period; this is also a decrease since fiscal year 2013, but less severe than that experienced in Virginia.

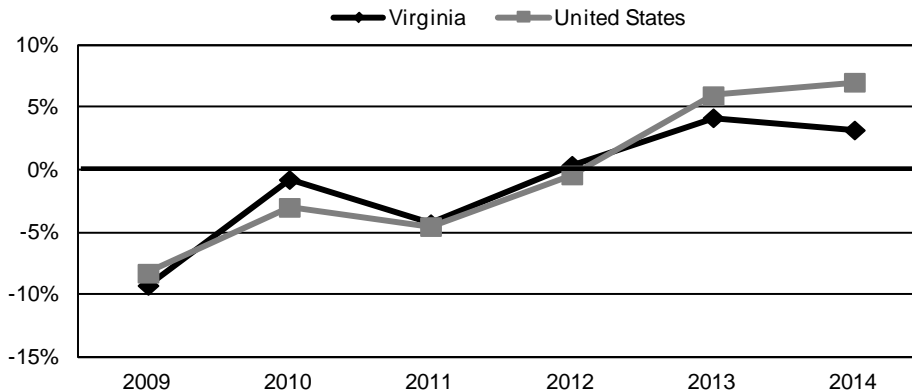
Figure 9
New Privately Owned Housing Units Authorized
Annual Percentage Change
Fiscal Years 2009 - 2014



Source: U.S. Census Bureau

Another indicator for understanding Virginia's housing market is the percentage change in housing prices published by the Federal Housing Finance Agency. Consistent with the national data, **Figure 10** shows a positive change for this indicator in Virginia for fiscal year 2014, with an increase of 3.2 percent (almost one percentage point less than the previous fiscal year's increase). This result is consistent with a recovery trend that began in fiscal year 2011.

Figure 10
Percentage Change in Housing Prices
Fiscal Years 2009 – 2014



Source: Federal Housing Finance Agency

Conclusion

Fiscal year 2014, overall, can be considered as a year of ambivalent results. While there is an overall consolidation of the post-recession recovery that started in fiscal year 2010 and gathered some momentum in fiscal year 2011, some indicators show an alarming slowdown. This appears to be largely the result of spending reductions at the federal government level, but it may also be the result of some lingering effects of the recession, as well as global economic uncertainty marked by the weakness of the Euro zone and crises in the Middle East and in parts of Africa. Virginia's recovery from the recession has slowed, and this is reflected especially in the employment and personal income indicators. Thus, the optimism expressed in the fiscal year 2013 overview has given way to moderate concern.

MAJOR INITIATIVES

The CAFR has received unqualified audit opinions from fiscal year 1986 through fiscal year 2013. During this period, the Commonwealth has also received the Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting. While we are very proud of these unqualified audit opinions and awards, we must be mindful of the fact that they are not automatic. The successes of the State Comptroller's office are directly attributable not only to the professionalism, experience and integrity of the State Comptroller's technical and accounting personnel, but also to the professionalism, experience and integrity of the financial and accounting personnel throughout the Commonwealth. These major initiatives will support efforts to continue our legacy of quality financial management.

Long-term Financial Planning

In 1992, an amendment to the Constitution of Virginia required the establishment of a Revenue Stabilization Fund. Annually, revenue collections are evaluated to determine whether deposits are required to the Fund. Withdrawals can only occur if the general fund revenues appropriated exceed the revised general fund revenue forecast by more than 2.0 percent of the certified tax revenues collected in the most recently ended fiscal year. Additionally, a withdrawal from the Fund cannot compensate for more than one-half of the difference between the general fund appropriations and revised estimate nor can it exceed more than one-half of the Fund balance. Further, pursuant to the constitutional amendment of Article X, Section 8, effective January 1, 2011, the amount on deposit cannot exceed 15.0 percent of the Commonwealth's average annual tax revenues derived from taxes on income and retail sales for the preceding three fiscal years. This is an increase of the previous limit of 10.0 percent.

Enterprise Application Project

The Cardinal Project represents a shared vision between the offices of the Secretary of Transportation, Secretary of Finance and the Virginia Information Technologies Agency to replace the Commonwealth's financial system (CARS) and the Virginia Department of Transportation's (VDOT) financial system with a modern, enterprise-wide financial system (base financial system). The base financial system will provide a solid foundation for the Commonwealth to expand system functionality and facilitate better integration of key administrative systems across the state. This foundation will enable the Commonwealth to re-engineer activities to include taking advantage of shared services, increasing functionality for better fiscal management, and reducing redundant agency financial systems and related cost. The Cardinal project will implement the base financial system in three phases. The first phase implemented VDOT's planned functionality on December 5, 2011, and the second phase implemented the Commonwealth's base financial system at the Department of Accounts (DOA) on October 1, 2012. The current phase of the project includes rolling Cardinal out to all other state agencies, at which time CARS will be retired. The remaining agencies have been divided into two waves, and the first wave was successfully implemented on October 1, 2014. The second wave is currently planned for February 1, 2016, with CARS being retired effective July 1, 2016. I, as State Comptroller, chair the Cardinal Steering Committee, and DOA has assigned full-time resources to this project.

AWARDS AND ACKNOWLEDGMENTS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded the Certificate of Achievement for Excellence in Financial Reporting to the Commonwealth for its CAFR for the fiscal year ended June 30, 2013. The Certificate of Achievement is a prestigious national award that recognizes conformance with the highest standards for preparation of state and local government financial reports. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report that conforms to program standards. Such reports must satisfy both accounting principles generally accepted in the United States of America and all applicable legal requirements.

A Certificate of Achievement is valid for a period of one year. The Commonwealth has received a Certificate of Achievement for the last 28 consecutive years (fiscal years 1986-2013). I believe that this year's report continues to conform to the Certificate of Achievement program requirements and we are submitting it to GFOA.

This report could not have been prepared without the full cooperation of all state agencies within the Executive Branch, the Legislature, the Judiciary, the Component Units, and especially the dedication and professionalism of the financial reporting staff in the Department of Accounts.

Respectfully submitted,

David A. Von Moll
Comptroller of the Commonwealth of Virginia



Government Finance Officers Association

**Certificate of
Achievement
for Excellence
in Financial
Reporting**

Presented to

Commonwealth of Virginia

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended

June 30, 2013

Executive Director/CEO

