

A REPORT TO THE CITIZENS OF THE COMMONWEALTH

Virginia Financial Perspective

For the Fiscal Year Ended June 30, 2005



Mark R. Warner
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December 15, 2005

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EXECUTIVE SUMMARY – PURPOSE OF THIS REPORT

The purpose of this report is to summarize and simplify the presentation of information contained in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Virginia. The Commonwealth's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and are independently audited by the Auditor of Public Accounts. Much of the information in the audited financial statements is necessarily technical and complex. As a result, the full financial statements may not be particularly useful to the citizens of the Commonwealth who wish to better understand state government finances.

Fourteen years ago, Virginia began issuing simplified financial reports, commonly referred to as *popular reports*. These reports are intended to better inform the public about their government's financial condition, without excessive detail or the use of technical accounting terms.

This report summarizes and explains the information contained in the financial statements for fiscal year 2005, along with other information on the Commonwealth's finances, in easily understood terms. This report represents the ongoing commitment of Commonwealth officials to keep Virginia's citizens informed about state finances, and to be accountable in all respects for the receipt and expenditure of public funds.

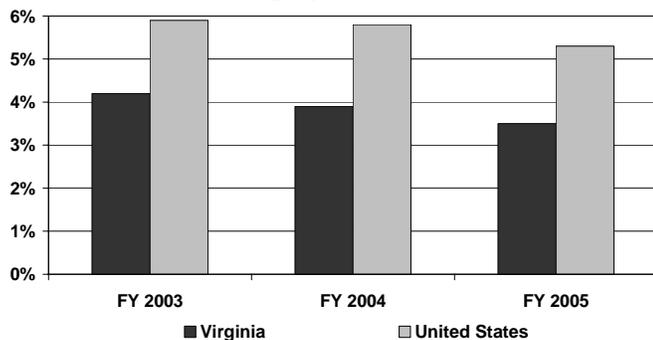
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Virginia's Economy

Each year the CAFR includes a section describing the Commonwealth's economic outlook. For fiscal year (FY) 2005, economists at Virginia Commonwealth University's Center for Urban Development (Center) prepared this economic highlight section. Building upon the growth of FY 2004, FY 2005 has been an excellent year for Virginia's economy. Unemployment continued its downward trend, employment has grown in nearly every industry sector and almost every urban center, real wages and salaries and personal income increased sharply, and the housing and retail markets performed very well.

Employment and income are the two broad economic measures that give the best picture of major developments. Unemployment decreased by 0.4 percent in FY 2005. Persons without work constituted 3.5 percent of the labor force (**Figure 1**).

Figure 1
Unemployment Rate



Source: Bureau of Labor Statistics

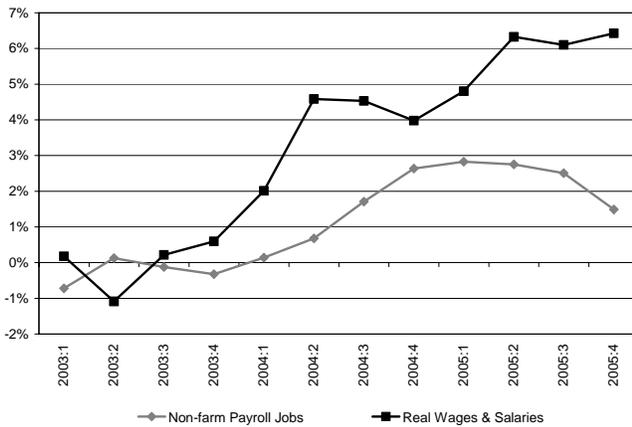
Virginia's unemployment rate was 1.8 percentage points lower than the national average.

Figure 2 shows that Virginia's total non-farm employment in FY 2005 increased by 2.4 percent in comparison to FY 2004. The year-over-year quarterly growth rate in non-farm payroll jobs has been positive for nine of the past twelve quarters. The average year-over-year quarterly growth rate in real wages and salaries reached 5.9 percent in fiscal year 2005, compared to 3.8 percent in fiscal year 2004 and 0.0 percent in fiscal year 2003. With Virginia's relatively low unemployment rate, firms have needed to pay higher salaries in order to attract workers who are in high demand.

Virginia's average pay per job in FY 2005 was \$42,281. This is over \$1,200 more than the national average of \$41,005. Two industries are the main reason that Virginia's workers had a higher pay per job, on average, than the United States as a whole: information, and professional and business services. These two highly sought after industries have been a focus of State and Local economic development efforts for a number of years. The only other industry in which Virginia's wages and salaries per job were higher than the United States in fiscal year 2005 was government.

Virginia's personal income reached approximately \$280 billion in FY 2005. As shown in **Figure 3**, this is an 8.3 percent increase over FY 2004. Total wages and salaries comprised about 58 percent of personal income and increased 8.5 percent during FY 2005. Virginia has outpaced the United States in personal income growth and wage and salary growth in each of the past three fiscal years. After accounting for inflation, Virginia's growth in real personal income (5.5 percent) and real wages and salaries (5.6 percent) surpassed the Nation's growth of 3.7 percent and 3.1 percent, respectively.

Figure 2
Economic Indicator Growth Rates



Source: Bureau of Labor Statistics and Bureau of Economic Analysis

Figure 3
Personal Income

	Annual Growth Rates		
	FY 2002-2003	FY 2003-2004	FY 2004-2005
Virginia Personal Income	3.2%	6.0%	8.3%
Virginia Wages and Salaries	2.2%	6.1%	8.5%
United States Personal Income	2.1%	4.7%	6.5%
United States Wages and Salaries	4.1%	4.0%	6.8%
Inflation, PCE Chain-Type Index	1.8%	2.1%	2.7%
Virginia Real Personal Income	1.4%	3.8%	5.5%
Virginia Real Wages and Salaries	0.4%	4.0%	5.6%
United States Real Personal Income	0.3%	2.6%	3.7%
United States Real Wages and Salaries	-0.4%	1.9%	3.1%

Sources: Bureau of Labor Statistics and Bureau of Economic Analysis

FINANCIAL STATEMENT INFORMATION

This section contains financial statement information for the Commonwealth of Virginia for the fiscal year ending June 30, 2005.

Virginia state government reports on its finances on the basis of a *fiscal year* which starts on July 1 and ends the following June 30. All information presented in this report is for the fiscal year that began on July 1, 2004, and ended on June 30, 2005. This is referred to as fiscal year 2005, or FY 2005.

Virginia's financial information is prepared by the Department of Accounts, an executive branch agency, under the direction of the Governor and the Secretary of Finance. The information is then audited by the Auditor of Public Accounts, who is an official of the legislative branch of government. In this way, the audit process is independent. The financial information for FY 2005 was audited and received an unqualified auditor's opinion.

Virginia accounts for its financial operations in government-wide financial statements and fund financial statements. The government-wide financial statements 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, and are prepared on a full accrual basis of accounting, which means that all revenue and expenditures are reflected even if the cash was not received or paid as of June 30, 2005. The fund statements are divided into three categories, governmental, proprietary, and fiduciary. The governmental funds are reported on a modified accrual basis of accounting which focuses on assets that can readily be converted to cash. The proprietary funds account for activities that operate like private sector business and use the full accrual basis of accounting. The fiduciary funds account for resources held for the benefit of parties outside the government. These also use the full accrual basis of accounting. These fiduciary funds are not included in the government-wide financial statements because they cannot be used to finance the Commonwealth's operations.

Virginia accounts for its revenues and expenditures within various funds. The funds are groups of related accounts that are segregated for specific activities or objectives. The largest fund supporting the operation of state government is the General Fund, which accounts for the majority of receipts from income and sales taxes. Another important fund is the Commonwealth Transportation Fund, which derives its revenues from gasoline taxes, vehicle registration fees, and a portion of sales taxes. The largest fund overall is the Pension Trust Fund, which includes the assets of the state employees' pension system.

Virginia accounts for its revenues and expenditures under two different methods of accounting. The Virginia Constitution and laws passed by the General Assembly require that all accounting be on a *cash basis*. This means that revenue is recognized when cash is received and expenditures are recognized when cash is paid out. Cash basis accounting is simple and easily verified. It is, therefore, the best way to demonstrate that state agencies are complying with laws that govern spending.

The other method of accounting used in Virginia involves the application of *accounting principles generally accepted in the United States of America*, or *GAAP*. GAAP is defined by national standard setting bodies, and is the method of accounting required when Virginia sells bonds. Only financial information prepared on a GAAP basis can be audited in accordance with accepted practice and receive an unqualified opinion from the Auditor of Public Accounts.

Information is presented in this report on the GAAP basis of accounting, and also, for the general fund, on the budgetary (cash) basis. Labels have been used to note which basis of accounting is being shown.

This Popular Report contains information from only selected funds and accounts and does not include all of the State's component units. Component units are legally separate entities that are accountable to the State. Some examples of component units are the public higher education institutions. Only the Statement of Net Assets and Statement of Activities on pages 5 and 6 include all of the State's funds and component units.

The full financial statements of the Commonwealth of Virginia, together with other economic and demographic information, are published in Virginia's Comprehensive Annual Financial Report, or CAFR. Requests for copies of the CAFR should be directed to the address given on the last page of this report.

Commonwealth Statement of Net Assets and Statement of Activities - GAAP Basis

A *Statement of Net Assets* summarizes all of the assets and liabilities with the difference between the two reported as net assets. As of the end of FY 2005, Virginia had Primary Government *assets* (i.e., cash, investments, property and amounts owed to the state) on a GAAP basis of \$26.0 billion, and Component Unit assets of \$29.4 billion. These assets were partially offset by Primary Government liabilities (i.e., amounts owed by the state to others) of \$11.6 billion, and Component Unit liabilities of \$15.1 billion. This left state government with Primary Government net assets (the amount left after liabilities are subtracted from assets) of \$14.3 billion, and Component Unit net assets of \$14.2 billion. **Figure 4** is a condensed Statement of Net Assets for the Commonwealth as of June 30, 2005.

The Statement of Activities (**Figure 5**) summarizes information showing how the State's net assets changed, on a GAAP basis, during the fiscal year. Virginia recognized \$10.9 billion in program revenues and \$16.2 billion in general revenues, which was used to pay for \$25.2 billion of expenses in the primary government. Virginia's component units reported \$6.8 billion of program revenues and \$3.1 billion of general revenues, which was used to pay \$8.3 billion of expenses. Program revenues are receipts that can be identified with specific expenses and are used to pay those expenses.

Although the total equity of Virginia is substantial and confirms the overall financial health of the Commonwealth, it is equally important to look at the financial condition of some of the individual *funds*. Governmental activities represent activities associated with the taxes and fees charged by most state agencies. Business-type activities are those like the State Lottery that operate like a business.

Figure 4
Statement of Net Assets (GAAP Basis)
As of June 30, 2005

(Dollars in Millions)

	Primary Government			Component Units		
	Governmental Activities	Business-type Activities	FY 2005 Total	FY 2004 Total (Informational Only)	FY 2005 Total	FY 2004 Total (Informational Only)
Current and Other Assets	\$ 7,902	\$ 2,878	\$ 10,780	\$ 8,711	\$ 22,190	\$ 19,898
Capital Assets	14,831	339	15,170	14,363	7,168	6,474
Total Assets	<u>22,733</u>	<u>3,217</u>	<u>25,950</u>	<u>23,074</u>	<u>29,358</u>	<u>26,372</u>
Long-term Liabilities	4,773	2,299	7,072	6,473	13,196	11,604
Other Liabilities	4,037	499	4,536	3,865	1,945	2,075
Total Liabilities	<u>8,810</u>	<u>2,798</u>	<u>11,608</u>	<u>10,338</u>	<u>15,141</u>	<u>13,679</u>
Net Assets:						
Invested in Capital Assets,						
Net of Related Debt	11,830	(132)	11,698	11,119	4,596	4,251
Restricted	1,252	600	1,852	1,269	7,840	6,673
Unrestricted	841	(49)	792	348	1,781	1,769
Total Net Assets	<u>\$ 13,923</u>	<u>\$ 419</u>	<u>\$ 14,342</u>	<u>\$ 12,736</u>	<u>\$ 14,217</u>	<u>\$ 12,693</u>

Figure 5
Statement of Activities (GAAP Basis)
 For the Fiscal Year Ended June 30, 2005

(Dollars in Millions)

	Primary Government			Component Units		
	Governmental Activities	Business-type Activities	FY 2005 Total	FY 2004 Total (Informational Only)	FY 2005 Total	FY 2004 Total (Informational Only)
Program Revenues:						
Charges for Services	\$ 2,000	\$ 3,009	\$ 5,009	\$ 4,442	\$ 5,038	\$ 4,651
Operating Grants and Contributions	5,262	19	5,281	5,329	1,531	1,422
Capital Grants and Contributions	578	-	578	734	202	112
	<u>7,840</u>	<u>3,028</u>	<u>10,868</u>	<u>10,505</u>	<u>6,771</u>	<u>6,185</u>
Expenses	22,976	2,270	25,246	23,217	8,329	7,702
Net (Expenses) Revenues	(15,136)	758	(14,378)	(12,712)	(1,558)	(1,517)
General Revenues	16,165	22	16,187	13,897	3,072	2,568
Transfers and Other Items	535	(535)	-	-	-	-
Change in Net Assets	1,564	245	1,809	1,185	1,514	1,051
Net Assets - July 1, as restated	12,359	174	12,533	11,551	12,703	11,642
Net Assets - June 30	<u>\$ 13,923</u>	<u>\$ 419</u>	<u>\$ 14,342</u>	<u>\$ 12,736</u>	<u>\$ 14,217</u>	<u>\$ 12,693</u>

Governmental Activities Revenues

The following is a graphical representation of the Statement of Activities (Figure 5) revenues for governmental activities.

Governmental Activities Expenses

The following is a graphical representation of the Statement of Activities (Figure 5) expenses for governmental activities.

Figure 6
Revenues by Source – Governmental Activities
FY 2005

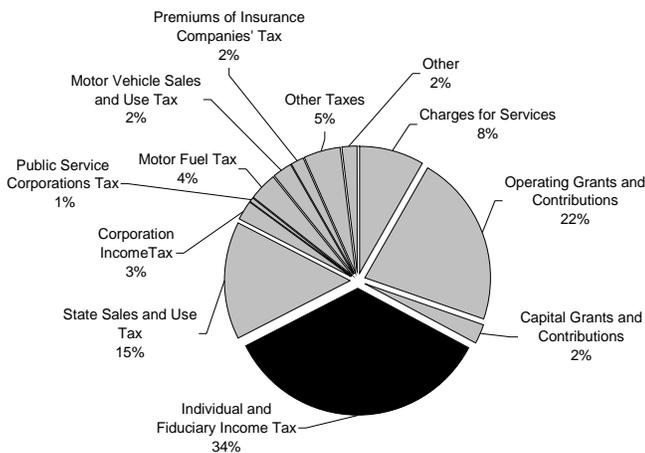
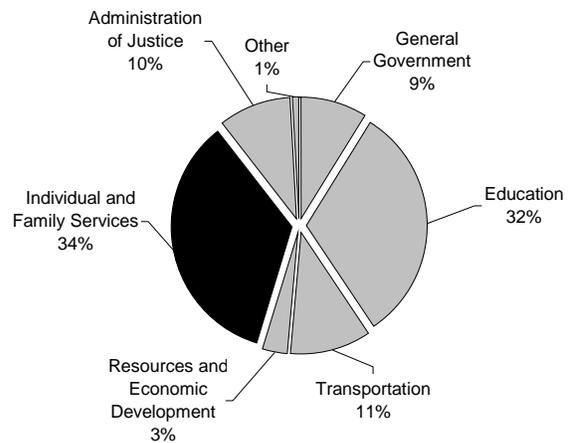


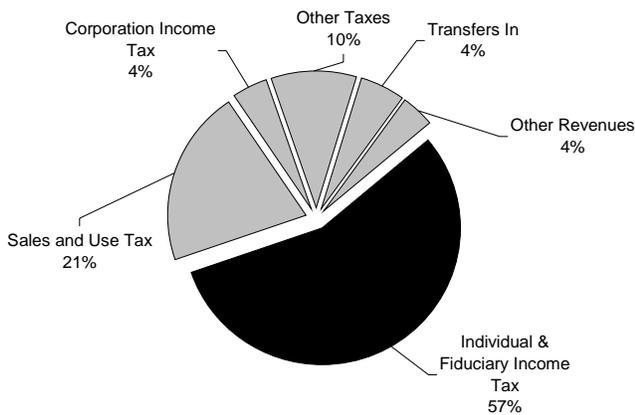
Figure 7
Expenses by Type – Governmental Activities
FY 2005



General Fund – Cash Basis

During FY 2005 the General Fund received \$14.8 billion in resources. **Figure 8** illustrates the various revenue sources. Individual and fiduciary income taxes accounted for 56.5 percent of the total resources of the General Fund, while sales and use taxes made up 21 percent. These revenues plus other revenues totaled \$14.1 billion, or 95.7 percent of General Fund resources. The remaining resources totaling \$636 million came through transfers from other funds, including alcoholic beverage sales and lottery profits.

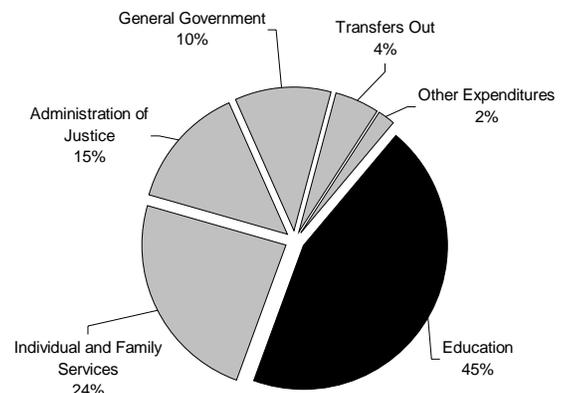
Figure 8
General Fund Revenue
FY 2005, Cash Basis



Revenues (not including transfers) increased by \$2.1 billion from FY 2004. This increase is attributable to the net effect of changes in all sources of revenue.

General Fund disbursements, including transfers, for FY 2005 (**Figure 9**) totaled \$14.0 billion. Expenditures totaled \$13.4 billion and transfers to other funds were \$642 million. Education accounted for 45 percent of General Fund spending, including direct state aid for primary and secondary schools and General Fund expenditures to support state colleges and universities. Support for social services, Medicaid, public health, and mental health consumed 24 percent of the General Fund. Public safety consumed 15 percent. Just 10 percent was used to support the administration of general governmental operations, which included 62 percent, or \$907.3 million, for payments to localities to offset state-mandated reductions in local personal property tax rates (i.e., car tax).

Figure 9
General Fund Disbursements
FY 2005, Cash Basis



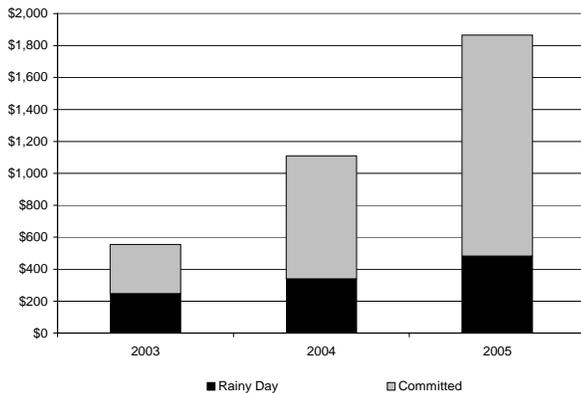
Expenditures (not including transfers) increased by \$1.6 billion over the prior year. The increase is due to the net effect of changes in all uses of General Fund resources.

General Fund revenues and net transfers exceeded expenditures by \$756 million on the cash basis. In other words, the General Fund had an operating gain for the year on the cash basis.

Figure 10 shows the General Fund balance - cash basis - at the end of each year since 2003. The rebound of Virginia's economy and an overall increase in tax revenue collections that resulted from tax reform legislation increased the balance to \$554.8 million in FY 2003 and \$1,109.6 million in FY 2004. The General Fund balance showed an increase in FY 2005 to \$1,865.3 million due to the continuing rebound.

Figure 10
General Fund Balance - Cash Basis
Highlighting the Available Fund Balance

(Dollars in Millions)



These balances are made up of “committed” funds and the “rainy day” fund.

Balances are “committed” if there are plans in place for their use.

The "rainy day" fund, or Revenue Stabilization Fund, is required by an amendment to the State Constitution, which was approved by the voters on November 7, 1992. The rainy day fund is reported as a reserved portion of the General Fund. The General Assembly is required to appropriate additional reserves to this fund when revenue collections are strong compared to the average for the previous six years. This reserved portion of the General Fund balance can only be used if state revenues decline sharply from the previous year.

The total amount reserved in the Revenue Stabilization Fund for FY 2005 is \$664.2 million. It is made up of \$79.9 million from 1993 collections, \$66.6 million from 1995 collections, \$58.3 from 1996 collections, \$123.8 million from 1997 collections, \$194.1 million from 1998 collections, \$103.3 million from 1999 collections, \$187.1 million from FY 2000 collections, and \$162.9 million in interest. Transfers of \$467.7 and \$247.5 million were made from the Revenue Stabilization Fund into the General Fund in FY 2004 and FY 2003,

respectively as prescribed by the state budget. Collections for FY 1994, FY 2001, and FY 2002 did not require a contribution. While a contribution was not required based on FY 2003 collections, a transfer of \$87 million was made during FY 2004 in advance of the required deposit date based on increased FY 2004 General Fund collections. A contribution of \$316.4 million of the \$664.2 million reserved amount will be required based on FY 2004 collections.

General Fund - GAAP Basis

During FY 2005 the General Fund received \$14.9 billion in resources. **Figure 11** illustrates the various revenue sources. Individual and fiduciary income taxes accounted for 56.1 percent of the resources, while sales and use taxes made up 21.1 percent. These revenues plus other revenues totaled \$14.2 billion, or 95.7 percent. The remaining monies totaling \$636.3 million came through transfers from other funds, including alcoholic beverage sales and lottery profits.

Revenues (not including transfers) increased by \$2.3 billion from FY 2004. This increase is attributable to the net effect of changes in all line items.

General Fund disbursements, including transfers, for FY 2005 (**Figure 12**) totaled \$14.1 billion. Expenditures totaled \$13.4 billion and transfers to other funds were \$638.9 million. Education accounted for 44.5 percent including direct state aid for primary and secondary schools and General Fund transfers to support state colleges and universities. Support for social services, Medicaid, public health, and mental health consumed 23.8 percent of the General Fund. Public safety disbursed 14.7 percent, while only 10.5 percent was used to support the administration of general governmental operations.

Expenditures (not including transfers) increased by \$1.6 billion over the prior year. The increase is due to the net effect of changes in all line items.

General Fund revenues and net transfers exceeded expenditures by \$783.0 million on the GAAP basis of accounting. In other words, the General Fund had an operating gain for the year on the GAAP basis of accounting.

Figure 11
General Fund Revenue
FY 2005, GAAP Basis

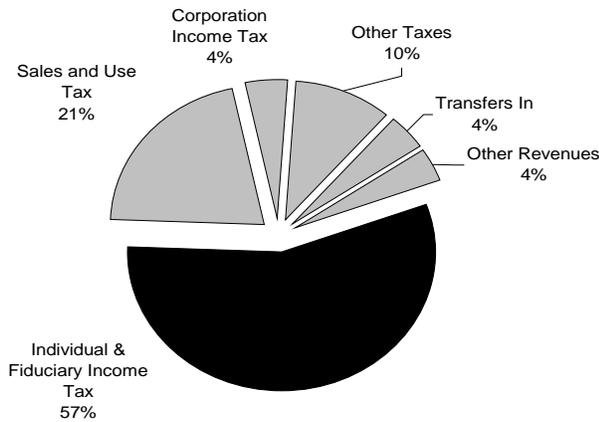
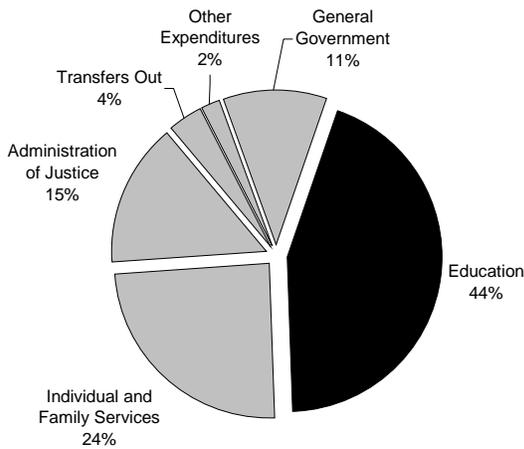


Figure 12
General Fund Disbursements
FY 2005, GAAP Basis



GAAP accounting requires that Virginia recognize certain assets and liabilities that are not recognized on the cash basis of accounting. Overall, the additional liabilities recognized under GAAP exceeded the additional assets, reducing fund balance to a greater degree than is recognized on a cash basis of accounting. Several future liabilities are particularly significant. One is for *estimated tax refunds due* of \$262.7 million, which is an estimate of the state income taxes withheld during FY 2005 that will eventually be refunded. Another is for *tax refunds payable* on returns filed in FY 2005 and paid during the months of July and August following year end close of \$213.7 million. The third item is an amount of estimated *Medicaid claims payable* of \$186.7 million, which represents medical services rendered in prior years that will not be paid for until FY 2006. These amounts are summarized in **Figure 13** that compares the General Fund on a cash and GAAP basis of accounting.

Figure 13
Analysis of General Fund Balance
Cash Basis versus GAAP Basis
For Fiscal Years Ended June 30, 2005 and 2004

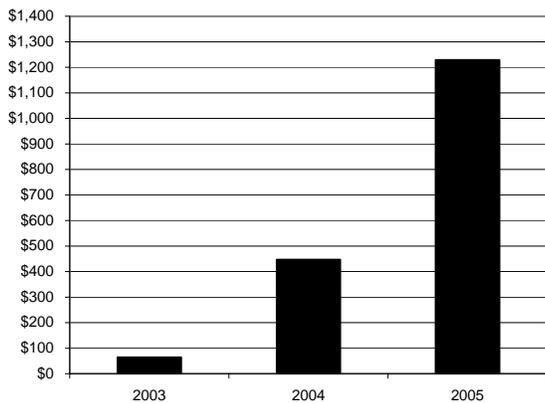
(Dollars in Millions)

	<u>FY 2005</u>	<u>FY 2004</u>
Fund Balance, Cash Basis	<u>\$ 1,865.3</u>	<u>\$ 1,109.6</u>
ADD:		
Sales Taxes Receivable	149.5	111.3
Other Taxes Receivable	345.5	295.1
Other Receivables	77.0	73.0
Inventory	43.9	46.5
Other Accrued Items	8.4	(6.7)
Total to be Added	<u>624.3</u>	<u>519.2</u>
LESS:		
Tax Refunds Payable	213.7	231.4
Estimated Tax Refunds Due	262.7	231.4
Medicaid Claims Payable	186.7	170.6
Sales Taxes Due to Localities	181.3	160.8
Other Accrued Items	416.2	388.4
Total to be Subtracted	<u>1,260.6</u>	<u>1,182.6</u>
Difference	<u>(636.3)</u>	<u>(663.4)</u>
Fund Balance, GAAP Basis	<u>\$ 1,229.0</u>	<u>\$ 446.2</u>

General fund revenues exceeded net transfers and expenditures by \$783.0 million on the GAAP basis. Fund balance increased to \$1,229.0 million, compared to a balance of \$446.2 million in FY 2004 (**Figure 14**). The increase in the General Fund GAAP basis balance from FY 2004 to FY 2005 is due to a rebounding economy and an overall increase in tax revenue collections that resulted from tax reform legislation.

Figure 14
General Fund Balance - GAAP Basis

(Dollars in Millions)



Commonwealth Transportation Fund - GAAP Basis

The Commonwealth Transportation Fund pays for the construction and maintenance of state highways. The fund also provides monies for other modes of transportation including rail, bus, aviation and seaports.

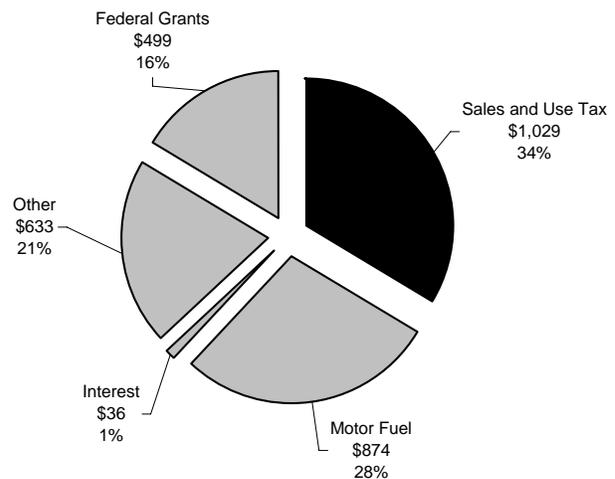
The size of this fund reflects the fact that Virginia is one of only a few states that includes essentially all roads within the state highway system. Virginia has approximately 69,054 miles of state roads.

The Commonwealth Transportation Fund (**Figure 15**) is classified as a *special revenue fund* because revenues of the fund come from various taxes and fees that are restricted for use in the support of transportation programs.

These revenue sources include the tax on motor fuel, vehicle registration and titling fees, and driver licensing fees. Also, since 1986, one half cent of the state's sales tax is deposited into this fund.

During FY 2005, the Commonwealth Transportation Fund had revenues and other receipts of \$3.5 billion and expenditures and other uses of \$3.4 billion on a GAAP basis. At the end of FY 2005, the fund had a balance of \$1.4 billion measured on a GAAP basis.

Figure 15
Commonwealth Transportation Fund Revenue Sources FY 2005, GAAP Basis
(Dollars in Millions)



Highway construction projects often require several years to complete. State revenues contribute approximately 75.7 percent of the funding for these projects. The federal government provides 20.2 percent, and 4.1 percent comes from bond proceeds. Local governments also contribute to the cost of highway construction.

College Savings Plan Fund - GAAP Basis

Proprietary Fund

The Virginia College Savings Plan (VCSP) Fund administers the Virginia Prepaid Education Program that locks in future tuition costs for minors from birth through the ninth grade. The fund accounts for the actuarially determined contributions and payments for approved expenses, and is classified as a proprietary fund. VCSP had current assets of \$171.2 million plus noncurrent assets such as investments and receivables of \$1.2 billion. These assets were held to satisfy current liabilities of \$71.5 million and long-term liabilities of \$1.4 billion. Invested in capital assets, net of related debt is \$120,000 and total unrestricted net assets were a negative \$60.4 million as of June 30, 2005.

Private Purpose Fund

VCSP also administers two other plans, the Virginia Education Savings Trust and College America. These plans are voluntary, non-guaranteed, higher educational investment programs. They are classified as a private purpose fund because the monies solely benefit individuals.

Total assets in the VCSP private purpose fund totaled \$11.6 billion as of June 30, 2005, and included \$11.3 billion of mutual fund investments. The net assets held in trust as of June 30, 2005, were also \$11.6 billion.

For FY 2005, VCSP reported additions of \$4.6 billion, which is primarily composed of contributions from plan participants in the amount of \$3.8 billion. Deductions for FY 2005 totaled \$582.4 million, including \$213.6 million in tuition benefits paid and \$359.7 million in redeemed shares.

The University of Virginia Component Unit Fund - GAAP Basis

The University of Virginia (the University) is the Commonwealth's largest institution of higher education. It is comprised of the graduate and undergraduate university facilities in Charlottesville, Virginia, a separate four-year college in Wise, Virginia, and one teaching hospital. In FY 2005, the University had total program revenues of \$1.9 billion and general revenues of \$619.1 million. Revenues are derived from numerous sources including student tuition and fees, contracts, grants, private gifts, and sales and services through the hospital and auxiliary enterprises. For the same period, the University reported expenses of \$2.1 billion, and showed a net increase in assets of \$428.2 million.

As of June 30, 2005, the University had total assets of \$6.3 billion, which included \$406.7 million of restricted assets and \$1.7 billion of capital assets. For the same period, liabilities totaled \$1.4 billion, of which \$777.6 million was classified as long-term liabilities. The University had \$4.9 billion in net assets as of June 30, 2005.

Pension Trust Fund - GAAP Basis

The Commonwealth maintains a number of funds that are managed for the benefit of various groups and institutions. The largest of these is the pension trust fund for state and certain local employees. This fund ended FY 2005 with a total equity of \$44.1 billion. During FY 2005 the fund received \$1.6 billion in contributions and earned \$4.7 billion on investment holdings. The increase in net assets after the payment of retirement benefits, refunds and operating costs was \$4.1 billion (**Figure 16**).

On November 5, 1996, Virginia voters approved an amendment to the Constitution of Virginia which provided that funds of the Virginia Retirement System are trust funds held separate from other state funds. This amendment safeguards the trust funds from being used for any purpose other than paying benefits to members and beneficiaries. The amendment does not change the way the System is funded or organized.

Figure 16

Statement of Changes in Plan Net Assets Pension Trust Fund - GAAP Basis For the Fiscal Year Ended June 30, 2005

(Dollars in Thousands)

Additions:	
Contributions	\$ 1,605,574
Investment Income:	
Interest, Dividends, and Other	
Investment Income	4,964,527
Less Investment Expenses	245,715
Net Investment Income	4,718,812
Other Revenue	743
Total Additions	6,325,129
Deductions:	
Retirement Benefits	1,945,718
Refunds to Former Members	84,739
Retiree Health Insurance Credits	68,966
Insurance Premiums and Claims	97,041
Administrative Expenses	20,405
Other Expenses	26,284
Total Deductions	2,243,153
Net Increase (Decrease)	4,081,976
Net Assets, July 1	40,043,807
Net Assets, June 30	\$ 44,125,783

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

Virtually all pension systems experience some gap between the amount that has been contributed and the amount that will be required to honor all promised benefits to both current and future retirees. This gap arises when benefits are added to the plan, and can also be produced by differences between the assumptions that are made in financing the trust fund and actual experience.

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

Employer contributions made for FY 2005 totaled \$197.5 million. This was less than the actuarially determined Annual Required Contribution of \$291.5 million, but did meet statutory requirements. The State has elected to allow employer contributions to include an annual amount that would phase in automatic cost of living adjustment funding requirements over a five-year period ending with FY 2005. When compared to other plans similar to Virginia's, the funding statistics indicate that Virginia's plans are adequately funded and financially sound. The pension obligation is included in the calculations of future state contribution rates so that a portion of this obligation is paid off each year.

Alcoholic Beverage Control Fund - GAAP Basis

The ABC fund accounts for the receipts and disbursements from the sale of alcoholic beverages. In FY 2005, ABC profits of \$100.9 million were distributed to the General Fund to use for current operations and for alcohol treatment and rehabilitation programs. Total ABC operating income for FY 2005 was \$100.7 million on \$450.1 million in total sales.

State Lottery Fund - GAAP Basis

The lottery fund (**Figure 17**) accounts for all receipts and disbursements from the sale of lottery tickets for various games.

During FY 2005, the Lottery had revenues of \$1.3 billion and expenses, including lottery prize payments, of \$907.1 million. Non-operating income for the year, including interest earnings, was \$6.5 million. During FY 2005, \$432.8 million was transferred out to be spent for public education as required by law.

Figure 17
Revenues, Expenses and Changes in Fund Net Assets
State Lottery - GAAP Basis
 For the Fiscal Year Ended June 30, 2005

(Dollars in Thousands)

Operating Revenues:	
Charges for Sales and Services	\$ 1,333,946
Total Operating Revenue	<u>1,333,946</u>
Operating Expenses:	
Personal Services	18,580
Contractual Services	29,193
Supplies and Materials	1,741
Depreciation	5,489
Lottery Prize Expense	850,222
Other Expenses	1,836
Total Operating Expenses	<u>907,061</u>
Operating Income	<u>426,885</u>
Nonoperating Revenues:	
Interest, Dividends, and Rents	6,489
Other	<u>(721)</u>
Total Nonoperating Revenues	<u>5,768</u>
Income Before Transfers and Changes	432,653
Operating Transfers Out	<u>(432,832)</u>
Change in Net Assets	(179)
Total Net Assets, July 1	<u>(2,309)</u>
Total Net Assets, June 30	<u>\$ (2,488)</u>

Risk Management (Self-Insurance) Program - GAAP Basis

The Commonwealth is self-insured for workers' compensation, property damage, general (tort) liability, medical malpractice and automobile insurance coverage. At the end of FY 2005, the self-insurance program had cash and other assets of \$114.0 million, while the estimated liability for claims payable was \$243.2 million. The program had additional liabilities of \$66.2 million, which resulted in a GAAP deficit balance of \$195.4 million.

The self-insurance program remains solvent because additional cash is constantly being provided from premiums paid by state agencies.

Debt Administration

The total outstanding debt on the books of the Commonwealth as of the end of FY 2005 was \$20.3 billion (**Figure 18**). Debt on the books of the Commonwealth can be classified into three categories:

- 1) general obligation bonds of Virginia taxpayers,
- 2) limited obligations, which may use tax revenue to pay principal and interest (Other Tax Supported); and
- 3) debt issued by state-created authorities and institutions of higher education, which is not an obligation of Virginia taxpayers and does not use tax revenues (Non-Tax Supported).

As illustrated in **Figure 18**, a total of \$954.0 million, or 4.7 percent of all debt, is a general obligation of Virginia taxpayers and supported by a pledge of all tax revenues and other monies of the Commonwealth. This kind of pledge is also referred to as "full faith and credit" debt. General obligation debt is issued as provided for in the State Constitution.

The next category of debt, limited obligations which may use tax revenue, does not carry the "full faith and credit" of the Commonwealth, but does use certain tax revenues, in whole or in part, to pay principal and interest. Examples of other tax supported debt include certain bonds issued by the Virginia Port Authority to improve Virginia ports, most highway construction bonds, bonds issued to construct state office buildings, hospitals and prisons, and capital leases and installment purchase contracts entered into by state agencies and institutions of higher education. A total of \$4.9 billion

of this type of tax supported debt was outstanding at the end of FY 2005. This is 24.2 percent of all debt on the books of the Commonwealth.

law to issue bonds to finance programs considered to provide a benefit to the public. Total debt in this category at the end of FY 2005 was \$14.4 billion.

Non-tax Supported Debt makes up 71.1 percent of all debt in the Commonwealth. The majority of this debt is issued by various authorities that are created under state

Figure 18
State Debt/Obligations
Tax Supported and Non-Tax Supported
As of June 30, 2005

<i>(Dollars in Thousands)</i>	Total	Percent of Total
Tax-Supported Debt/Obligations		
General Obligation Bonds		
Public Facilities Bonds	\$ 520,655	2.5%
Parking Facilities Bonds	11,040	0.1%
Transportation Facilities Bonds	125,337	0.6%
Higher Education Bonds	296,963	1.5%
Total General Obligation Bonds	<u>953,995</u>	<u>4.7%</u>
Other Tax-Supported Debt/Obligations		
Transportation	1,041,397	5.1%
Virginia Port Authority	265,518	1.3%
Virginia Public Building Authority	1,142,070	5.6%
Innovative Technology Authority	8,635	0.0%
Virginia College Building Authority	641,450	3.2%
Long-term Capital Lease Payable	180,071	0.9%
Compensated Absences Obligations	501,385	2.5%
Pension Liability Obligations	860,432	4.3%
Biotechnology Research Park	54,605	0.3%
Regional Jail Construction	15,030	0.1%
Installment Purchase	109,661	0.5%
Other Long-term Debt/Obligations	77,016	0.4%
Total Other	<u>4,897,270</u>	<u>24.2%</u>
Total Tax-Supported Debt/Obligations	<u>5,851,265</u>	<u>28.9%</u>
Non-Tax Supported Debt/Obligations		
Higher Education	546,062	2.7%
Virginia Housing Development Authority	4,627,186	22.8%
Pocahontas Parkway Association	463,357	2.3%
Virginia Public School Authority	2,449,447	12.1%
Virginia Resources Authority	1,286,295	6.3%
Other Long-term Debt/Obligations	5,045,132	24.9%
Total Non-Tax Supported Debt/Obligations	<u>14,417,479</u>	<u>71.1%</u>
Total Commonwealth Debt/Obligations	<u>\$ 20,268,744</u>	<u>100.0%</u>

The largest of these authorities is the Virginia Housing Development Authority, which has \$4.6 billion in debt outstanding secured by various mortgages. Other issuers include the Virginia Public School Authority, Pocahontas Parkway Association, and the Virginia Resources Authority. Colleges and teaching hospitals also issue bonds secured only by fees paid for services. These bonds do not use state taxes to pay principal and interest.

In each case, the debt of these authorities is secured only by the revenues of the issuing body. No tax revenues are used to support this debt and it is not considered a legal obligation of the Commonwealth. However, \$1.3 billion of the total carries a “moral obligation” promise by the Commonwealth to consider funding any deficiencies in debt service reserves from tax revenues. To date, no such deficiencies have occurred.

Figure 19 summarizes the outstanding debt owed by the Commonwealth in all categories over three fiscal years. **Figure 20** shows the ratio of general obligation debt per person and **Figure 21** shows the percentage of governmental expenditures used to pay governmental bonds.

Figure 19
Categories of Debt
(Dollars in Millions)

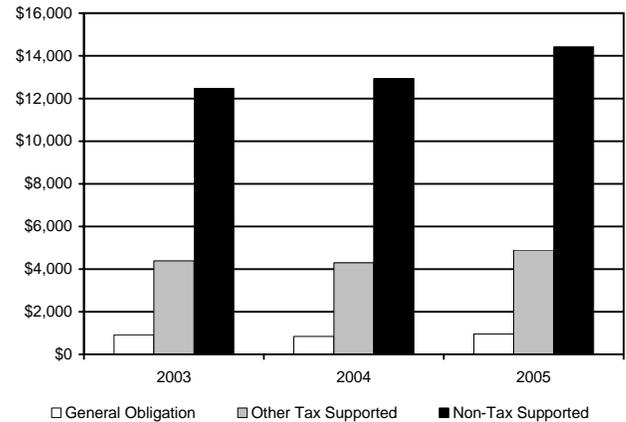


Figure 20
Ratio of General Obligation Debt Per Capita
(Amounts in Thousands, Except for Per Capita)

For the Fiscal Year Ended June 30,	Population (1)	General Obligation Debt (2)	General Long-term Debt Per Capita
2005	7,512	\$ 953,995	\$ 127
2004	7,432	834,832	112
2003	7,275	917,078	126

- (1) Population figure for 2005 is estimated.
- (2) Includes 9(a), 9(b) and 9(c) debt, net of unamortized premiums, discounts, deferral on debt defeasance, and bond anticipation notes payable.

Figure 21
Percentage of Annual Debt Service Expenditures for Governmental Debt to Total Expenditures – All Governmental Fund Types
(Dollars in Thousands)

For the Fiscal Year Ended June 30,	Debt Service (1)	Total Expenditures (2)	Percentage
2005	\$ 414,035	\$ 23,670,765	1.75
2004	421,927	21,769,073	1.94
2003	375,993	21,134,149	1.78

- (1) Includes principal and interest payments related to general bonded debt reflected in the governmental activities column of the Government-wide Statement of Net Assets. The principal outstanding at June 30, 2005 was \$3.6 billion.
- (2) Includes General, Special Revenue, Debt Service, Capital Projects, and Permanent Funds.

Source: Department of Accounts

OTHER INFORMATION

The following section discusses other information which may be of interest to the reader. The remaining information was reported in the State Comptroller's "Report on Statewide Financial Management and Compliance for the Quarter Ended June 30, 2005." This information is not included in the audited financial statements.

Prompt Payment

State government places a significant emphasis on ensuring that vendors doing business with state agencies are paid within the time specified in the purchase contract. Payment performance is monitored monthly and payments that are overdue more than seven days entitle vendors to collect interest. Agencies must achieve a 95 percent compliance rate with all payment provisions in order to be considered in compliance with the Virginia Prompt Payment Act.

Figure 22 shows that for FY 2005, the state made 98.8 percent of its payments on time, and that 97.4 percent of the dollars owed were paid in compliance with prompt payment requirements. The state paid out \$17,576 in interest on late payments during FY 2005, an increase of \$5,300 from FY 2004, on total vendor payments of \$5.2 billion.

Figure 22
Statewide Prompt Payment Statistics
 For FY 2005

Number of Late Payments	30,806
Total Number of Payments	2,611,448
Late Dollars (in Thousands)	\$ 131,531
Total Dollars (in Thousands)	\$ 5,225,630
Interest Paid	\$ 17,576
Percent of Payments in Compliance	98.8%
Percent of Dollars in Compliance	97.4%

E-Commerce and Payment Systems

Virginia actively pursues administrative efficiencies and cost savings by promoting use of automated payment systems by state agencies. To reduce the number of state issued checks, Virginia uses Financial Electronic Data Interchange (EDI), also known as electronic banking, and Payroll Direct Deposit. To consolidate payments for low dollar purchases the state uses the Small Purchase Charge Card.

Electronic Data Interchange

Over 175,000 payments totaling \$20.0 billion were made in FY 2005 using EDI. This helped to avoid the issuance of over 292,000 checks. Electronic payments were made to nearly 29,500 grantees, vendors and localities.

Direct Deposit

Further efforts to reduce the amount of resources consumed are made by using electronic systems for payroll payments. These include the elimination of paychecks for Commonwealth employees who are paid through direct deposit to their bank accounts. As of June 30, 2005, 89.6 percent of salaried employees and 58.9 percent of wage employees took part in Direct Deposit.

Payline

Payline, the Commonwealth's electronic pay stub system, provides secure internet access for employee payroll information. Payline allows for the elimination of costly printing and distribution of earnings notices for employees on direct deposit. During FY 2005, the printing of nearly 237,000 earnings notices was avoided through the Payline earnings notice print opt-out program.

Small Purchase Charge Card Program

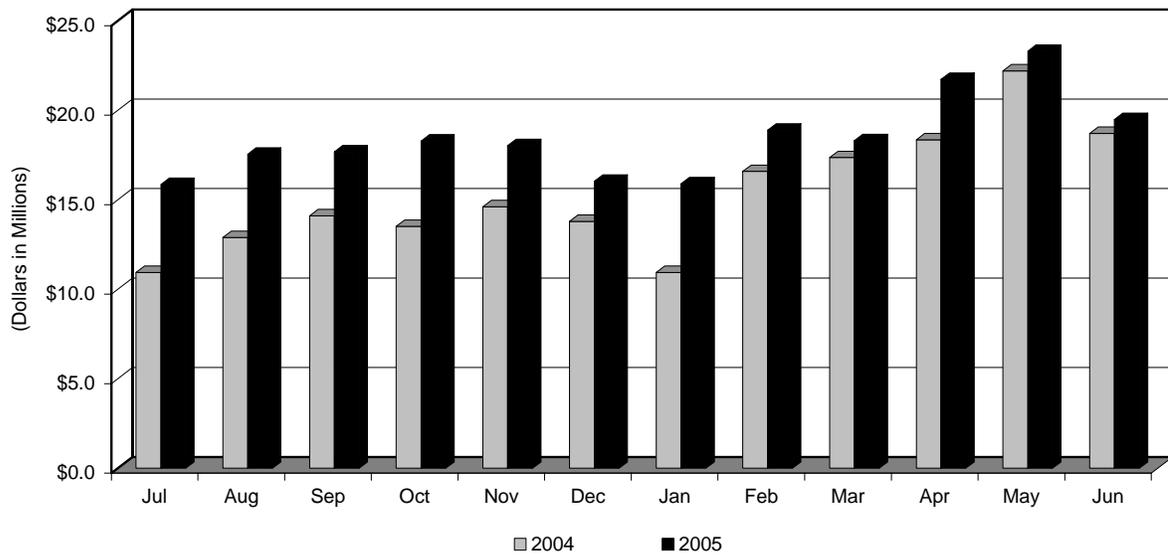
Also in FY 2005, approximately \$221.0 million in purchases were made using the small purchase charge card and newly available increased limit charge card programs. This helped to avoid printing nearly 470,000

checks. As of June 30, 2005, 198 agencies were using 10,192 cards (**Figure 23**). **Figure 24** compares charge activity for FY 2005 to activity for FY 2004.

Figure 23
Small Purchase Charge Card Program

<u>Charge Card Activity</u>	<u>Quarter Ended June 30, 2005</u>	<u>Fiscal Year 2005 to Date</u>	<u>Comparative Fiscal Year 2004 to Date</u>
Amount of Charges	\$ 64,556,247	\$ 221,035,843	\$ 184,037,843
Estimated Number of Checks Avoided	133,359	507,326	469,278
Total Number of Participating Agencies		198	182
Total Number of Cards Outstanding		10,192	9,597

Figure 24
Charge Amount Comparison
FY 2004 – FY 2005



Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) recognized the Commonwealth through its Award for Outstanding Achievement in Popular Annual Financial Reporting for the fiscal year ended June 30, 2004. This is a prestigious national award, recognizing conformance with the highest standards for preparation of state and local government popular reports.

In order to receive an Award for Outstanding Achievement in Popular Annual Financial Reporting, a government unit must publish a Popular Annual Financial Report whose contents conform to program standards of creativity, presentation, reader appeal, and understandability. The award is valid for a period of one year only. The Commonwealth has received this award for the last ten consecutive years (fiscal years 1995-2004). It is expected that the current report continues to conform to the Popular Annual Financial Reporting requirements.

Award for Outstanding Achievement in Popular Annual Financial Reporting

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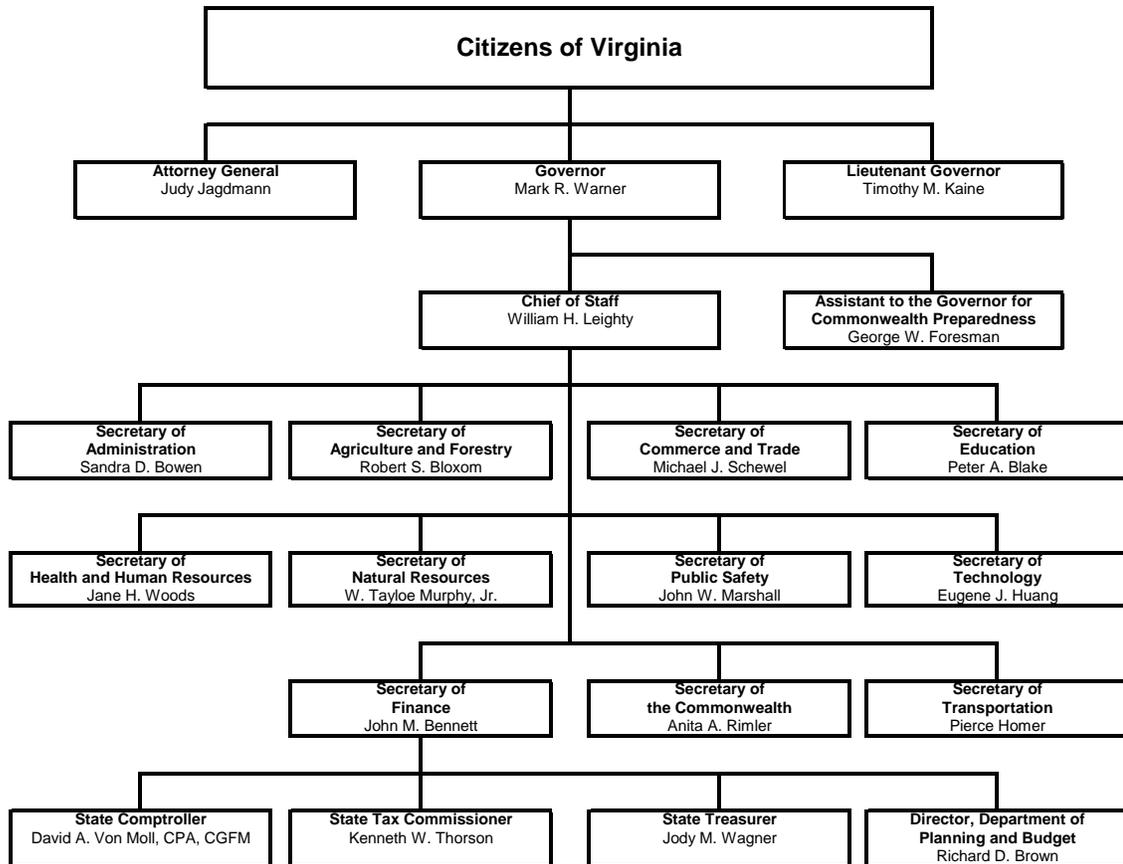
**for the Fiscal Year Ended
June 30, 2004**



Nancy L. Ziehl
President

Jeffrey L. Esalt
Executive Director

**Organization of Government
Selected Government Officials - Executive Branch**





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