



STATE OF WASHINGTON
OFFICE OF FINANCIAL MANAGEMENT

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November 22, 2011

The Honorable Christine Gregoire, Governor
Honorable Members of the Legislature
Citizens of the State
State of Washington
Olympia, Washington 98504

In accordance with Revised Code of Washington 43.88.027, the Office of Financial Management has prepared this Comprehensive Annual Financial Report (CAFR) of the state of Washington for the fiscal year ending June 30, 2011. Full responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal control established for this purpose, rests with the state. Because the cost of internal control should not exceed anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

The State Auditor has issued an unqualified (“clean”) opinion on the Washington State financial statements for the fiscal year ending June 30, 2011. The independent auditor’s report is located at the front of the financial section of this report.

Management’s Discussion and Analysis (MD&A) immediately follows the independent auditor’s report and provides a narrative introduction, overview, and analysis of the basic financial statements. The MD&A complements this letter of transmittal and should be read in conjunction with it.

Following the MD&A are the basic financial statements, including the government-wide financial statements, the fund financial statements, and the notes to the financial statements. The required supplementary information, combining and individual fund financial statements, and the statistical section complete the CAFR.

Profile of Washington State

Washington State was created in 1889 by an enabling act of Congress. The state is located on the Pacific Coast, in the northwestern corner of the continental United States, and comprises 71,303 square miles. Its current population is 6.8 million. Washington is famous for its breathtakingly beautiful scenery and sharp contrasts. On the west side of the state, high mountains rise above coastal waters. The forests of the Olympic Peninsula are among the world’s rainiest places. The state’s coastline has hundreds of bays and inlets that make excellent harbors, while in the eastern part, flat semi-desert land stretches for long distances without a single tree.

Washington's location makes it a gateway for land, sea, and air travel to Alaska and Pacific Rim countries. Ships from all parts of the world dock at Washington ports. Costco Wholesale Corporation, headquartered in Issaquah, operates an international chain of membership warehouses. Microsoft, a leader in the computer software industry, makes its home in Redmond. Major internet retailer, Amazon.com, and worldwide renowned coffee company, Starbucks, are both headquartered in Seattle. The Weyerhaeuser Company, a major producer of wood and related products, is headquartered in Federal Way.

East of the Cascade Mountain range, farmers raise livestock and grow a variety of crops such as wheat, potatoes, and tree fruits. Washington leads the nation in apple and hops production, makes world-class wine, and produces large amounts of lumber, pulp, paper, and other wood products. Western Washington's mild, moist climate makes that region excellent for dairy farming and the production of flower bulbs.

GOVERNMENTAL STRUCTURE

As established in the State Constitution, Washington State has Executive, Legislative, and Judicial branches of government. The Executive Branch has nine elected officials: the Governor, Lieutenant Governor, Secretary of State, State Treasurer, State Auditor, Attorney General, Superintendent of Public Instruction, Insurance Commissioner, and Commissioner of Public Lands. Forty-one agency heads are appointed by, and report to, the Governor. Eighty-six agency heads report to boards appointed, in whole or in part, by the Governor. The Legislative Branch consists of the Senate (with forty-nine members) and the House of Representatives (with ninety-eight members). The Judicial Branch consists of the State Supreme Court, the highest court in the state, which has nine Justices. Every two years, three Justices are elected for six-year terms. A Chief Justice is chosen from among the most senior Justices. The Judicial Branch also includes the state's superior courts, justices of the peace, and such inferior courts as the Legislature may provide.

TYPES OF SERVICES PROVIDED AND REPORTING ENTITY

The state provides a wide range of services that include education, transportation, environmental and natural resource protection, and social and health services.

The accompanying report includes all funds and subsidiary accounts of the primary government, the State of Washington as legally defined, as well as all of its component units. Component units are legally separate entities for which the primary government is financially accountable. The determination of "financial accountability" is based on criteria established in Governmental Accounting Standards Board Statement No. 14. Note 1.A to the financial statements explains more fully which organizations are included in the reporting entity.

THE BUDGET CYCLE

Washington enacts budgets for a two-year cycle, beginning on July 1 of each odd-numbered year. By law, the Governor must propose a biennial budget in December, the month before the Legislature convenes in regular session. The biennial budget enacted by the Legislature can be modified in any legislative session through changes to the original appropriations. Since the inception of annual legislative sessions in 1979, it has become common for the Legislature to enact annual revisions to the state's biennial budget. These revisions are referred to as supplemental budgets.

Operating appropriations are generally made at the fund/account and agency level; however, in a few cases, appropriations are made at the fund/account and agency/program level. Operating appropriations cover either the entire biennium or a single fiscal year within the biennium. Capital appropriations are biennial and are generally made at the fund/account, agency, and project level. The legal level of budgetary control is at the fund/account, agency and appropriation level, with administrative controls established at lower levels of detail in certain instances.

Washington State's Economy and Revenue Outlook

SUMMARY

Since the nation's recession began in December 2007, Washington State has lost almost 206,000 jobs, or about 6.9 percent of total nonfarm payroll employment. While the state appeared to lag the nation into this slowdown, local losses accelerated in late 2008 and, for the most part, began to mirror national trends. By June 2009, the nation was officially out of recession and national economic indicators were signaling a recovery in economic output. However, employment was noticeably restrained as employers sought to increase output through productivity gains rather than by hiring additional workers. Employment patterns were inconsistent throughout 2010 as the use of temporary Census workers in the late spring and summer masked the lethargic employment trends in the remainder of the economy. Employment growth turned positive in the last quarter of 2010 and accelerated slowly through 2011. Employment should maintain its positive track through 2012 though at a growth rate less than half the historic norm. Because of Washington's export-dependent economy, and because of the relative strength of the Asian economies and trade, Washington is expected to lead the nation during this recovery and expansion in terms of income growth, thanks to higher average wages in aerospace and software.

It is expected that Washington's recovery and expansion will build upon the diversity of the state's economy, whose elements include a vital export base; the presence of knowledge-based industries such as business, professional, health, and financial services; and an attractive quality of life. All these elements should continue to support population growth.

Washington's nonfarm payroll employment grew by 0.5 percent in fiscal year 2011, compared to the 4.0 percent drop in fiscal year 2010, and the 2.0 percent drop in fiscal year 2009. The aerospace industry was able to maintain relatively steady payrolls despite weakness in the global airline industry, thanks primarily to a long backlog of orders. In addition, the final awarding of the Air Force Tanker contract to Boeing and the Federal Aviation Administration (FAA) certification of the 787 Dreamliner should strengthen payrolls in fiscal year 2011 and beyond. Total manufacturing employment grew 1.3 percent in fiscal year 2011 as production schedules ramped up and a weak dollar gave Washington products an advantage in the international markets.

Washington's unemployment rate eased modestly in fiscal year 2011, as a slow-growing national economy, weak housing markets, and volatile energy costs continued to hamper the labor markets. As the annual unemployment rate eased down to 9.3 percent from 9.8 percent in the previous year, Washington's jobless rate tracked closely with the national average throughout this period.

Personal income grew 4.9 percent in fiscal year 2011, despite the slow pace of hiring and whip-sawed financial markets. Real personal income – after factoring out inflation – grew by 3.1 percent in fiscal year 2011 after falling 2.5 percent in fiscal year 2010. In comparison, real personal income fell 1.1 percent in fiscal year 2009, and grew 4.9 percent in 2008 and 5.9 percent in 2007.

Washington's outlook for fiscal year 2012 is for modest gains in economic growth as the recovery and expansion from the financial crisis and national and international recessions gain a small degree of traction in the local economy. Nonfarm payroll employment in Washington is forecasted to increase in fiscal year 2012 by 1.2 percent. Personal income in fiscal year 2012 is predicted to grow by 3.6 percent in current terms, and by 1.6 percent in real terms.

General Fund-State revenues are forecasted to grow at a 7.1 percent rate in the 2011-13 biennium, compared to the 5.9 percent decrease in the 2009-11 biennium. The slow economy and weak housing markets have had a negative effect on revenue growth. Particularly hard hit have been retail sales and real estate excise taxes.

ECONOMIC CONDITION IN FISCAL YEAR 2011

Washington's nonfarm payroll employment grew by 0.5 percent in fiscal year 2011, compared to the 0.6 percent growth in U.S. nonfarm payroll employment. The absolute increase in Washington's nonfarm payroll employment was 13,400 during fiscal year 2011. Personal income in Washington fell behind the U.S. pace: up 4.7 percent compared to a gain of 5.4 percent for the U.S. Because Washington's personal income had not fallen to the same degree as the nation in the previous two years, the rebound effect in Washington would not have been as vigorous as the nation during the subsequent recovery (i.e., the state did not have near as deep a hole from which to extract itself in 2011). Real per capita income grew by 1.9 percent in Washington over the same period, again lagging the nation, which experienced a 2.6 percent gain.

Aerospace employment provided an anchor for Washington's manufacturing sector in fiscal year 2011. While aerospace employment did ratchet down a modest amount in fiscal years 2009 and 2010, fiscal year 2011 saw a return to aerospace employment gains with an additional 1,400 workers, a growth rate of 1.7 percent. The awarding of the Air Force Tanker contract to Boeing, along with the FAA certificate of the 787 Dreamliner, will help add stability to aerospace and other manufacturing employment for the foreseeable future.

Manufacturing employment, other than aerospace, was less vibrant, but still grew by 1.1 percent. Durable manufacturing industries, which had experienced pullbacks in employment in fiscal year 2010, turned up in fiscal year 2011 as the national economy and export market began to strengthen. Nondurable manufacturing employment, which had declined 4.7 percent in fiscal year 2010, eased upward in fiscal year 2011 as demand for processed food and paper products solidified.

Employment in durable manufacturing, other than aerospace, grew by 1.4 percent in fiscal year 2011 (a gain of 1,400 jobs), while employment in durable manufacturing increased by 1.8 percent nationally. Employment patterns in durable manufacturing industries were mixed in Washington during fiscal year 2011. Specifically, employment in lumber and wood products, nonmetallic mineral products, ships and boat building, and other durable goods were all down, while primary metal, fabricated metal, computers, machinery, electrical equipment, and aerospace were all on the plus side of the ledger.

Washington's lumber industry is dependent upon local and national home building trends. The housing market in Washington had begun to soften in fiscal year 2008, and the national markets had been weak since the end of fiscal year 2007. The continued weakness in home building resulted in a 1.4 percent decline in wood products employment in fiscal year 2011. Employment in other transportation equipment (other than aerospace) was also mixed as demand for heavy trucks rebounded thanks to renewed wholesale and other distribution activity while ship and boatbuilding activity continued to soften. As aerospace employment strengthened, employment in primary and fabricated metal products – a major supplier to aerospace – grew by 4.1 percent in fiscal year 2011, despite the more intense use of composite materials in newer aircraft. Machinery manufacturing employment increased 5.3 percent in fiscal year 2011. Computers and electronic products were up 1.4 percent, while employment in other durable manufacturing was down by 1.5 percent.

Nondurable manufacturing employment in Washington increased by 0.8 percent in fiscal year 2011, a gain of about 600 jobs. Nationally, nondurable manufacturing employment declined by 0.8 percent over the same period. In Washington, employment in food manufacturing grew 0.9 percent in fiscal year 2011 as a result of a rebound in the export markets. Printing and paper products employment dropped 2.8 percent in fiscal year 2011 as a result of declining national demand for magazines and newspapers.

Washington's non-manufacturing employment advanced 0.4 percent in fiscal year 2011. Among the major non-manufacturing sectors, construction, financial activities, and government experienced declining payrolls in fiscal year 2011. Construction and financial activities are inexorably linked through the housing market which will be constrained for the foreseeable future. All other major nonfarm services sectors posted payroll gains for fiscal year 2011 with professional and business services outpacing the field with a growth of 3.7 percent.

The construction industry posted a 5.1 percent loss in employment as the housing market remained weak throughout the year. The housing market in fiscal year 2011 was little changed, though continued declines in mortgage interest rates seemed to stem the decline in housing prices somewhat. Weakness in the labor market and in the resumption of home foreclosures continued to be a drag on the housing market and construction sector.

For many years, employment growth in the information sector has relied almost exclusively on the strength of software publishing. However, after a run of 27 years, software employment fell 2.6 percent because of restructuring at Microsoft in fiscal year 2010. The sector's employment stabilized in the last half of fiscal year 2010 and began a slow up-turn in fiscal year 2011, growing 1.0 percent.

Both wholesale and retail trade employment increased by 1.0 percent in fiscal year 2011. While this was a welcome turnabout from fiscal year 2010, it was slow relative to what one would expect from an economy in recovery. Professional and business service jobs advanced by 3.7 percent in fiscal year 2011, as the great majority of activities within the sector gained strength over the year. Education and health services reported an increase of 1.5 percent during fiscal year 2011 – the one major sector seemingly unaffected by slumping demand. Leisure and hospitality services recorded a 0.5 percent increase as food and beverage establishments experienced a modest turn-around and as hotels and motels were feeling upbeat about higher occupancy rates. Employment slumped in the public sector as state and local governments continued to be beset with revenue shortfalls resulting in payroll cuts.

ECONOMIC OUTLOOK

The forecast for Washington State for fiscal year 2012 reflects the continuation of slow but steady employment growth at both the state and national levels. According to the September 15, 2011, forecast by the state Economic and Revenue Forecast Council, Washington's nonfarm payroll employment is predicted to increase by 1.2 percent in fiscal year 2012, a bit quicker than that of the nation. Up until the middle of fiscal year 2010, the economic recovery was characterized by an expansion of existing workers' hours rather than new hiring. In addition, an aggressive cycle of productivity gains through the early period of economic recovery had also kept hiring at bay. With the end of the productivity surge in early 2011, employers began to expand their payrolls to increase output. This pattern should hold through fiscal year 2012.

Manufacturing employment in Washington is projected to continue its upward course in fiscal year 2012. The aerospace industry is expected to add another 6,800 workers in fiscal year 2012, and durable manufacturing, aside from the aerospace sector, is expected to grow by 3,900 jobs as business investment and exports boost demand. As a result, primary and fabricated metals, machinery and electrical equipment, computer and electronic products, and other transportation equipment are all expected to solidify their employment base.

The wood products industry was hard hit by both the housing bubble and the slowdown in international trade. But after five years of downward trending employment, the wood products sector should begin to hold its own in fiscal year 2012 as the nation's multi-family market and increased residential remodeling shore up demand for wood products. It is unlikely, however, that any market rebound will result in the recovery of all the wood products jobs that were lost in the recession.

Nondurable manufacturing developments should be a mixed bag in fiscal year 2012. Employment in food manufacturing is forecasted to decline by 3.6 percent, while employment in other nondurable manufacturing sectors will increase. Employment in paper and paper products manufacturing is expected to grow by 1.6 percent in fiscal year 2012, and other nondurable manufacturing should increase by 3.1 percent.

In the non-manufacturing sectors, the strongest employment growth in fiscal year 2012 is predicted to occur in professional and business services (3.8 percent) as business-to-business related activity increases, particularly computer systems design and employment services. Information payrolls are expected to gain 3.1

percent, thanks to the resumption of growth in software publishing that is expected to grow by 6.3 percent in fiscal year 2012. Competition for skilled technical workers kept employment growth stunted in fiscal year 2011, but enhanced compensation packages helped boost employment in the latter stages of the year and should help the sector carry some momentum over the next several years.

Wholesale and retail trade should post moderate job gains of 2.8 percent and 2.4 percent respectively in fiscal year 2012. Increased international trade volumes will help boost demand for wholesale trade activity. Retail payrolls will likely be spurred by both growth in income and overall nonfarm payroll employment.

Education and health service jobs should also post a moderate 2.7 percent gain in fiscal year 2012. Health services have proven to be much less susceptible to economic downturns than other sectors of the economy. The coverage provided by public and private insurers provides the economic buffer for this sector.

Leisure and hospitality jobs are projected to grow 3.0 percent in fiscal year 2012. Travel and eating out activities were put on hold during the recession. Recent gains have been modest because of the slow growth in employment and incomes. Because both overall income and employment are expected to post moderate gains in 2012, so too should the leisure and hospitality sector.

Several non-manufacturing sectors are expected to experience job losses. Construction declined by over 69,000 jobs between fiscal year 2008 and fiscal year 2011. Fiscal year 2012 will also be a year of losses in construction jobs though not near the magnitude of the last few years. We expect a drop of 0.5 percent as home-building and commercial building activities struggle with excess inventories of unleased office space and foreclosed homes. Growing demand for rental apartments and residential remodeling should help stem further losses in the last half of fiscal year 2012.

Employment in financial activities will remain slow because of continued difficulties among state chartered banks; many were over-exposed in commercial building loans when the market weakened. Those banks that survived the shake-out have emphasized recapitalizing their balance sheets, which in some ways has been detrimental to small business lending activity. Payrolls are expected to decline by another 0.2 percent in fiscal year 2012.

Federal government payrolls will decline by 1.7 percent in fiscal year 2012 because of the easing of defense-related federal expenditures. State and local government employment will also dip 1.5 percent as slow labor markets and slower than expected consumer spending impede revenue collections.

Washington's personal income is expected to grow by 3.6 percent in fiscal year 2012, a bit slower than the 3.8 percent growth in U.S. personal income for the same period. Employment is expected to gain some traction in fiscal year 2012, and as a result, the wage component of personal income should grow at a 3.5 percent pace. But, because of the slow turnaround in the labor markets and the difficulties among the long-term unemployed, the use of unemployment compensation, an important component of personal income, will actually decline by 13.6 percent in fiscal year 2012. Proprietors' income is projected to grow at a 5.9 percent clip in fiscal year 2012 as entrepreneurs ride the upswing in the economy. Dividends, interest, and rents will grow at a 5.7 percent pace as financial markets extend their recovery.

Major Initiatives

For more than three years, ever since our nation fell into the recession, states have seen their budgets battered by plummeting revenue and rising demand for services. Washington is no exception. Over the past five quarters, starting in September 2010, state General Fund revenue projections for the last biennium and the current biennium have declined by more than \$4.8 billion. The recession and the downward spiral in revenue collections have fundamentally altered Washington's fiscal outlook and forced the state to take dramatic, and often painful, steps to put our state budget on a more sustainable trajectory.

Last year, Governor Gregoire launched her “Transforming Washington’s Budget” initiative. She invited leaders from all walks of life to serve as an advisory board to examine the assumptions underlying the budget and suggest ideas for changing how the state conducts business. The Governor also solicited ideas from the public through a series of hearings and an online forum. Finally, the Governor used the Priorities of Government process and a series of tough questions to identify the most essential state services.

Working in an unprecedented bipartisan spirit, the Governor and the Legislature approved a 2011-13 biennial budget that includes more than \$4.5 billion in reductions as well as major cost-cutting reforms and agency consolidations. However, additional cuts will be needed. Less than three months after the new budget went into effect, the state’s revenue projection for the current biennium was reduced by \$1.4 billion.

TRANSFORMING GOVERNMENT

Lawmakers approved the Governor’s proposal for the state’s most significant agency consolidation in decades, including creation of the Department of Enterprise Services (DES). This consolidation merges the Department of General Administration, Department of Information Services, Department of Personnel, the State Printer and portions of the Office of Financial Management into two agencies. DES will handle facilities and lease management, fleet management, purchasing and contracts, business systems applications, printing, accounting and human resources, which are central services provided to all state agencies. The Office of Financial Management will continue to handle policy, budget, forecasting and labor relations.

The Legislature also approved the creation of the Consolidated Technology Services agency to begin the merger of information technology services managed separately by state agencies.

During the current biennium, this reorganization of state government is expected to save \$18.8 million and employ 83 fewer employees. Future savings will be realized through possible contracting out of certain services and implementation of actions to reduce or eliminate redundant activities.

Pension reform. Governor Gregoire proposed eliminating the automatic annual benefit increases to older pension plans, which have been closed to new members since 1977. While the Legislature approved the automatic increases in 1995 to protect against inflation, the increase itself was not linked to inflation. Without action, underfunding would cause employer pension contribution rates to double in the 2011-13 biennium and remain high for the next 20 years. This created an unfunded liability of \$7 billion.

The Legislature approved the Governor’s proposal to end future automatic benefit increases, which will reduce the unfunded liability in the closed plans by more than 50 percent. This saves taxpayers \$344 million in the current budget and \$7.6 billion over the next 25 years.

Debt reform. Washington’s debt burden has grown steadily over the past two decades. During the 1989-91 biennium, the state’s debt payments for general obligation bonds totaled less than \$500 million - about 3.7 percent of General Fund spending. During the 2009-11 biennium, general obligation debt payments totaled nearly \$1.8 billion - about 6 percent of General Fund spending.

Under a bipartisan agreement that Governor Gregoire helped broker, starting in fiscal year 2016, the State Finance Committee will gradually lower the state debt limit from 8.75 percent to 7.75 percent by fiscal year 2022. The committee may adjust the working debt limit due to extraordinary economic conditions, and is authorized to delay or reduce bond issuance to not exceed the recommended working debt limit.

The agreement also sets up a commission to examine the state’s use of debt, make recommendations on debt policy and debt limitations, and determine whether a constitutional change is needed. The commission’s report is due later this year.

EDUCATION

Early Learning. Washington has increased the number of children who can benefit from the state's preschool program for at-risk children. This early investment gives young children the skills they need to succeed in school and life. A new early learning assessment of developing skills will help early learning and kindergarten teachers to identify what help children need when they come to school. Through a public-private partnership, the state is expanding early learning support for our youngest children (up to 3 years old) through more home visitations.

Launch Year. The Legislature approved the Governor's "Launch Year" legislation, which addresses gaps in one of the key transition points of a student's academic journey. The legislation provides students certainty that the advanced coursework they take in high school will count toward the achievement of a technical certificate or academic degree.

Higher Education Funding Task Force. Lawmakers also took action on several recommendations from the Higher Education Funding Task Force, which the Governor appointed last year. The state will renew its commitment to higher education by providing for sustainable, long-term funding that links tuition and state support and gives higher education governing boards the ability to manage their institutions' budgets. Legislation also strengthens accountability and performance measures, and it creates an endowment to help low- and middle-income Washington students earn a bachelor's degree.

Department of Education. The Governor will continue her work with legislators and stakeholders to fashion a truly student-focused education system and introduce new legislation in 2012. Her goal is to build a unified strategic plan and governance structure that pull together planning, expertise and resources to create prioritized and coordinated learning opportunities.

The Governor proposed creating a state Department of Education to focus on student achievement by providing a seamless, state-level education system from early learning through career preparation and training. Authority now held by eight agencies with 14 major education plans would be consolidated in a single, cohesive, cabinet-level department.

HEALTH CARE AND HUMAN SERVICES

Health Insurance Exchange. With legislation requested by Governor Gregoire, Washington becomes one of the first states in the nation to implement a health insurance exchange in advance of the 2014 federal deadline. The Affordable Care Act requires a health insurance exchange to be established in each state, either by the federal government or the state. Exchanges are consumer-friendly marketplaces where individuals and small employers can shop for insurance coverage. Low-income residents will also be able to access subsidized coverage through the exchange.

Health Care Authority. Lawmakers approved Governor Gregoire's proposal to merge the state's two largest purchasers of health care: the Medicaid program and the Health Care Authority. Together, these agencies purchase health care for more than 1.6 million Washington residents. The power made possible through their combined leverage will align other state health care purchasing as well as facilitate coordination with other health care payers and providers to reform the health care system to benefit all consumers.

A key theme in the Governor's approach to high-quality care is evidence-based medicine - focusing on health care that is proven to work and eliminating the 30 percent of health care costs that studies show do not contribute to meaningful care. Washington was the first to establish a Health Technologies Assessment program, which now contributes more than \$31 million in annual cost avoidance.

Licensing Adult Family Homes. The Governor proposed adopting a user-pay approach to help cover the cost of licensing and regulating the adult family home industry. Today, fees cover only 6 percent of those

costs - the rest is subsidized by the state. While the Governor proposed an almost entirely fee-supported system, the budget includes a fee structure that recovers 39 percent of the licensing and oversight costs in fiscal year 2012 and 60 percent in fiscal year 2013. Taxpayers will save \$2.9 million in the current biennium and \$3.6 million per biennium thereafter.

ECONOMIC DEVELOPMENT

Creating Jobs. Through the transportation and capital budgets, nearly 45,000 jobs will be created in Washington to help get people back to work.

Workers' Compensation. The Governor and the Legislature negotiated what will be the largest reform ever to the state's 100-year-old workers' compensation system. That system faced troubling trends that would lead to double-digit rate increases and seriously undermine its long-term viability. The reforms, which are projected to save the system about \$900 million over the next four years, will get injured workers back on the job as quickly and safely as possible, prevent double-digit rate increases and protect the long-term financial integrity of the system.

Unemployment Insurance. The rates that businesses pay into the unemployment insurance trust fund are based on a set formula. Because of the high demand for benefits in a down economy, Washington businesses, on the cusp of recovery, were facing an average 36 percent increase in unemployment insurance rates. As Governor Gregoire requested, the first piece of legislation delivered to her desk this year was a rate reduction to help more than 65,000 small businesses avoid the costly increase. Those savings allow businesses to begin hiring and start growing. The rate reduction saves \$300 million in the first year, with an additional \$50 million expected in later years.

Tax Amnesty. In December 2010, at the Governor's request, the Legislature unanimously enacted the state's first-ever amnesty program for businesses that owe back taxes. Under the amnesty program, the state waived penalties and interest for qualifying businesses that paid agreed-upon taxes. The program helped businesses to quickly resolve old tax issues and provided the state with sorely needed revenue. During the three-month amnesty window, nearly 8,900 businesses paid \$343 million in back taxes - \$282 million to the state and \$61 million to local governments.

ENVIRONMENT AND ENERGY

TransAlta. Taking a significant step to reduce harmful green-house gas emissions, Governor Gregoire signed legislation to phase out coal-fired energy production at the TransAlta power plant. The legislation solidifies into law a collaborative agreement to close TransAlta's two coal boilers, the first in 2020 and the second in 2025. The agreement provides a path to cleaner power while allowing the time necessary to provide stability to the electrical grid and to the community.

Oil Spill Response. Washington became the first in the nation to pass significant legislation addressing oil spill response when the Governor signed House Bill 1186. The legislation greatly advances protection of Washington's environment, economy and cultural resources from the impacts of a potential major oil spill — and ensures that Washington has the best tools and equipment to mount an aggressive, rapid and well-coordinated response in the event of a major spill in Puget Sound and other waters of our state.

State Parks Discover Pass. At the Governor's urging, the Legislature approved a new approach to funding state parks. Sales of the newly created Discover Pass, along with the current opt-out vehicle registration donation program, will fully replace General Fund support of the state parks system in four years. This shift in funding is projected to save \$789 million over the next 10 years and preserve Washington's natural treasures.

TRANSPORTATION

Governor Gregoire signed a transportation budget that will invest \$5.6 billion in more than 800 projects across the state. This budget reflects \$20 million in savings from recently negotiated contracts with ferry employees and \$4.1 million in savings in ferry system administrative costs.

Even with these reforms and savings, critical transportation needs remain unfunded as voter-approved transportation revenue packages end. The Governor formed the transportation advisory group “Connecting Washington” to develop a 10-year strategy for funding the state’s transportation system. The group’s recommendations will be ready for presentation to the Legislature and the public in 2012.

Awards and Acknowledgements

The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Washington State for its CAFR for the fiscal year that ended June 30, 2010. The Certificate of Achievement is a prestigious national award, recognizing conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized CAFR, with contents conforming to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. Washington State has received a Certificate of Achievement for the last twenty-four years. The Office of Financial Management considers this report to be in conformity with the Certificate of Achievement Program requirements, and will submit it to the GFOA.

The preparation of this report could not have been accomplished without the professionalism and dedication demonstrated by the financial and management personnel of each state agency and institution of higher education and the Office of Financial Management. This CAFR reflects the Governor’s commitment to the Legislature, the citizens of Washington State, and the financial community to maintain financial statements in conformance with the highest standards of financial accountability.

Sincerely,

/ s /

Marty Brown
Director