

MD&A
Management's Discussion and Analysis

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MD&A

Management's Discussion & Analysis

As managers of the state of Washington, we offer this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2010. We present this information in conjunction with the information included in our letter of transmittal, which can be found preceding this narrative, and with the state's financial statements, which follow. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

- Total assets of the state of Washington exceeded its liabilities by \$16.2 billion (reported as net assets). Of this amount, \$(11.1) billion was reported as "unrestricted (deficit) net assets." A negative balance indicates that no funds were available for discretionary purposes.
- The state of Washington's governmental funds reported a combined ending fund balance of \$10.5 billion, an increase of 10 percent compared with the prior year.
- The General Fund reported an unreserved fund balance (deficit) of \$(561) million, at the end of Fiscal Year 2010, or 2.4 percent of total General Fund expenditures.
- The state's capital assets increased by \$1.8 billion while total bond debt increased by \$2.7 billion during the current fiscal year. Of the total bond debt issued, \$1.1 billion was unspent at year end largely related to a June 2010 bond issuance.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the state of Washington's basic financial statements, which include three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The focus is on both the state as a whole (government-wide) and the major individual funds. The dual perspectives allow the reader to address relevant questions, broaden a basis for comparison (year-to-year or government-to-government), and enhance the state's accountability.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the state of Washington's finances, in a manner similar to a private sector business.

Statement of Net Assets. The *Statement of Net Assets* presents information on all of the state of Washington's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the state of Washington is improving or deteriorating.

Statement of Activities. The *Statement of Activities* presents information showing how the state's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). The Statement of Activities is focused on both the gross and net cost of various activities (including governmental, business-type, and component unit). This is intended to summarize and simplify the reader's analysis of the revenues and costs of various state activities and the degree to which activities are subsidized by general revenues.

Both of these government-wide financial statements distinguish functions of the state of Washington that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities).

The governmental activities of the state of Washington include education, human services, transportation, natural resources, adult corrections, and general government.

The business-type activities of the state of Washington include the workers' compensation and unemployment compensation programs, as well as Washington's lottery, liquor control, and various higher education student services such as housing and dining.

The government-wide financial statements can be found on pages B17 through B19 of this report.

FUND FINANCIAL STATEMENTS

A fund is a group of related accounts used to maintain control over resources that are segregated for specific activities or objectives. The state of Washington, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the state can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for four major funds and an aggregate total for all nonmajor funds. The state's major governmental funds are the General Fund, Higher Education Special Revenue Fund, the Motor Vehicle Fund, and the Higher Education Endowment Fund. Individual fund data for the state's nonmajor governmental funds are provided in the form of combining statements elsewhere in this report. The governmental fund financial statements can be found on pages B22 through B25 of this report.

Proprietary Funds. The state of Washington maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Internal service funds represent an accounting device used to accumulate and allocate costs internally among the state of Washington's various

functions. The state of Washington uses internal service funds to account for general services such as motor pool, central stores, data processing services, risk management, employee health insurance, and printing services. Because internal service funds predominately benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary fund financial statements provide the same type of information as the government-wide financial statements, but in greater detail. The proprietary fund financial statements provide separate information for the Workers' Compensation Fund, Unemployment Compensation Fund, and the Higher Education Student Services Fund, which are considered to be major funds, as well as an aggregated total for all nonmajor enterprise funds.

The internal service funds are combined for presentation purposes. Individual fund data for the state's nonmajor proprietary funds are provided in the form of combining statements elsewhere in this report. The proprietary fund financial statements can be found on pages B26 through B31 of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the state of Washington's own programs. Washington's fiduciary funds include state administered pension plans. The accounting used for fiduciary funds is much like that used for proprietary funds. Individual fund data for the state's fiduciary funds are provided in the form of combining statements elsewhere in this report.

The fiduciary fund financial statements can be found on pages B32 through B33 of this report.

Component Units. Component units that are legally separate from the state and primarily serve or benefit those outside the state are discretely presented. They are either financially accountable to the state, or have relationships with the state such that exclusion would cause the state's financial statements to be misleading or incomplete. The state discretely reports one major component unit, the Washington State Public Stadium Authority, and four nonmajor component units.

Refer to Note 1 on pages B38 through B47 for more detailed information. Individual fund data for the state's nonmajor component units are provided in the form of combining statements elsewhere in this report. The component unit financial statements can be found on pages B34 through B35 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages B37 through B132 of this report.

OTHER REQUIRED INFORMATION

In addition to this discussion and analysis, this report also presents required supplementary information on

budgetary comparisons, pension plans and other post-employment benefits, funding progress, and infrastructure assets reported using the modified approach.

Required supplementary information can be found on pages B133 through B159 of this report.

The combining statements referred to earlier are presented immediately following the required supplementary information. Combining and individual fund statements and schedules can be found on pages 181-231 of the Comprehensive Annual Financial Report.

STATE OF WASHINGTON						
Statement of Net Assets						
<i>(in millions of dollars)</i>						
	Governmental Activities		Business-Type Activities		Total	
	2010	2009	2010	2009	2010	2009
ASSETS						
Current and other assets	\$ 16,915	\$ 15,611	\$ 22,080	\$ 21,027	\$ 38,995	\$ 36,638
Capital assets	31,247	29,558	2,254	2,099	33,501	31,657
Total assets	<u>48,162</u>	<u>45,169</u>	<u>24,334</u>	<u>23,126</u>	<u>72,496</u>	<u>68,295</u>
LIABILITIES						
Current and other liabilities	3,730	3,593	3,421	2,653	7,151	6,246
Long-term liabilities outstanding	21,234	17,721	27,934	25,689	49,168	43,410
Total liabilities	<u>24,964</u>	<u>21,314</u>	<u>31,355</u>	<u>28,342</u>	<u>56,319</u>	<u>49,656</u>
NET ASSETS						
Invested in capital assets, net of related debt	18,201	17,551	913	721	19,114	18,272
Restricted	5,214	4,887	2,930	3,800	8,144	8,687
Unrestricted (deficit)	(217)	1,417	(10,864)	(9,737)	(11,081)	(8,320)
Total net assets	<u>\$ 23,198</u>	<u>\$ 23,855</u>	<u>\$ (7,021)</u>	<u>\$ (5,216)</u>	<u>\$ 16,177</u>	<u>\$ 18,639</u>

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. For the state of Washington, total assets exceed liabilities by \$16.2 billion at June 30, 2010 as compared to \$18.6 billion as reported at June 30, 2009.

The largest portion of the state's net assets (118.2 percent for Fiscal Year 2010 as compared to 98.0 percent for Fiscal Year 2009) reflects its investment in capital assets (e.g., land, buildings, equipment and intangible assets), less any related debt used to acquire those assets that is still outstanding. The state of Washington uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

Although the state of Washington's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

A portion of the state of Washington's net assets (50.3 percent for Fiscal Year 2010 as compared to 46.6 percent for Fiscal Year 2009) represents resources that are subject to external restrictions on how they may be used. The remaining balance of \$(11.1) billion represents unrestricted (deficit) net assets. The state's overall negative balance is caused by deficits in both governmental and business-type activities.

In governmental activities, the deficit is largely related to decreased tax revenues in Fiscal Year 2010. The decline in tax revenues reflects the continued weak economy and the lack of consumer confidence.

In business-type activities, the majority of the deficit is caused by the workers' compensation program that provides time-loss, medical, disability and pension payments to qualifying individuals who sustain work-related injuries or develop occupational diseases as a result of their required work activities.

The main benefit plans of the workers' compensation program are funded on rates that will keep the plans solvent in accordance with recognized actuarial principles.

The supplemental pension cost-of-living adjustments (COLAs) granted for time-loss and disability payments, however, are funded on a pay-as-you-go basis. By statute, the state is only allowed to collect enough revenue to fund the current COLA payments.

As previously mentioned, the state's activities are divided between governmental and business-type. The majority of support for governmental activities comes from taxes and intergovernmental grants, while business-type activities are supported primarily through user charges.

STATE OF WASHINGTON						
Changes in Net Assets						
<i>(in millions of dollars)</i>						
	Governmental Activities		Business-Type Activities		Total	
	2010	2009	2010	2009	2010	2009
REVENUES						
Program revenues:						
Charges for services	\$ 4,584	\$ 4,398	\$ 5,987	\$ 5,640	\$ 10,571	\$ 10,038
Operating grants and contributions	12,193	10,565	2,468	572	14,661	11,137
Capital grants and contributions	939	706	-	-	939	706
General revenues:						
Taxes	14,982	16,001	160	113	15,142	16,114
Interest and investment earnings (loss)	449	(212)	1,743	291	2,192	79
Total Revenues	33,147	31,458	10,358	6,616	43,505	38,074
EXPENSES						
General government	(1,738)	(1,815)	-	-	(1,738)	(1,815)
Education - K-12	(8,468)	(8,549)	-	-	(8,468)	(8,549)
Education - Higher education	(6,051)	(6,044)	-	-	(6,051)	(6,044)
Human services	(12,946)	(12,436)	-	-	(12,946)	(12,436)
Adult corrections	(938)	(1,044)	-	-	(938)	(1,044)
Natural resources and recreation	(1,084)	(1,062)	-	-	(1,084)	(1,062)
Transportation	(2,073)	(1,883)	-	-	(2,073)	(1,883)
Interest on long-term debt	(810)	(728)	-	-	(810)	(728)
Workers' compensation	-	-	(4,268)	(2,544)	(4,268)	(2,544)
Unemployment compensation	-	-	(4,729)	(2,360)	(4,729)	(2,360)
Higher education student services	-	-	(1,628)	(1,502)	(1,628)	(1,502)
Liquor control	-	-	(552)	(540)	(552)	(540)
Washington's lottery	-	-	(389)	(401)	(389)	(401)
Other business-type activities	-	-	(345)	(391)	(345)	(391)
Total Expenses	(34,108)	(33,561)	(11,911)	(7,738)	(46,019)	(41,299)
Excess (deficiency) of revenues over expenses before contributions						
to endowments and transfers	(961)	(2,103)	(1,553)	(1,122)	(2,514)	(3,225)
Contributions to endowments	52	57	-	-	52	57
Transfers	252	(190)	(252)	190	-	-
Increase (decrease) in net assets	(657)	(2,236)	(1,805)	(932)	(2,462)	(3,168)
Net assets - July 1	23,855	26,091	(5,216)	(4,284)	18,639	21,807
Net assets - June 30	\$ 23,198	\$ 23,855	\$ (7,021)	\$ (5,216)	\$ 16,177	\$ 18,639

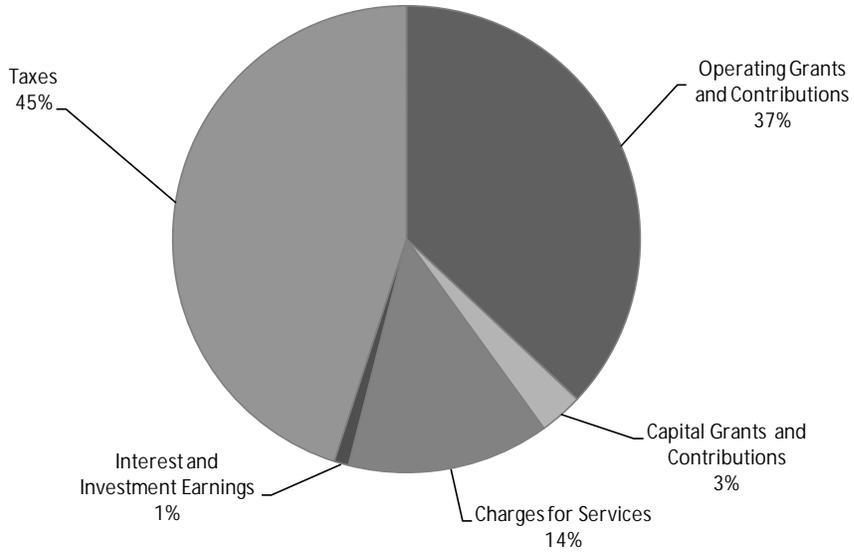
Governmental Activities. Governmental activities resulted in a decrease in the state of Washington's net assets of \$657 million. A number of factors contributed to the decrease:

- Tax revenues decreased \$1.0 billion in Fiscal Year 2010 as compared to Fiscal Year 2009 reflecting the negative impact of the slowing economy and slumping housing markets. While certain tax sources showed moderate increases, sales and use taxes reported a decrease of \$435 million. Sales and use taxes are the main tax revenue for governmental activities. Taxable sales have declined due to reductions in consumer spending power as a result of job losses as well as weak consumer confidence. Real estate excise taxes also declined by \$20 million reflecting the continued decline in real estate throughout Fiscal Year 2010 in spite of record low mortgage rates, declining home prices and the federal government's home-buyers tax credit program.
- Operating and capital grants and contributions increased \$1.9 billion in Fiscal Year 2010 as compared to Fiscal Year 2009. American Recovery and Reinvestment Act grants made up \$1.3 billion of the increase funding expenses in the areas of education, transportation, public health and the environment.
- Expenses grew slightly in spite of the drop in revenues. The expenses for human services and education comprised 80.5 percent of the total expenses for governmental activities which is consistent with the 80.5 percent in Fiscal Year 2009. Human services accounted for the majority of the growth in expenses increasing by \$510 million or 4.1 percent in Fiscal Year 2010 over Fiscal Year 2009 reflecting the increased number of citizens seeking assistance from state programs and services due to the economic recession.

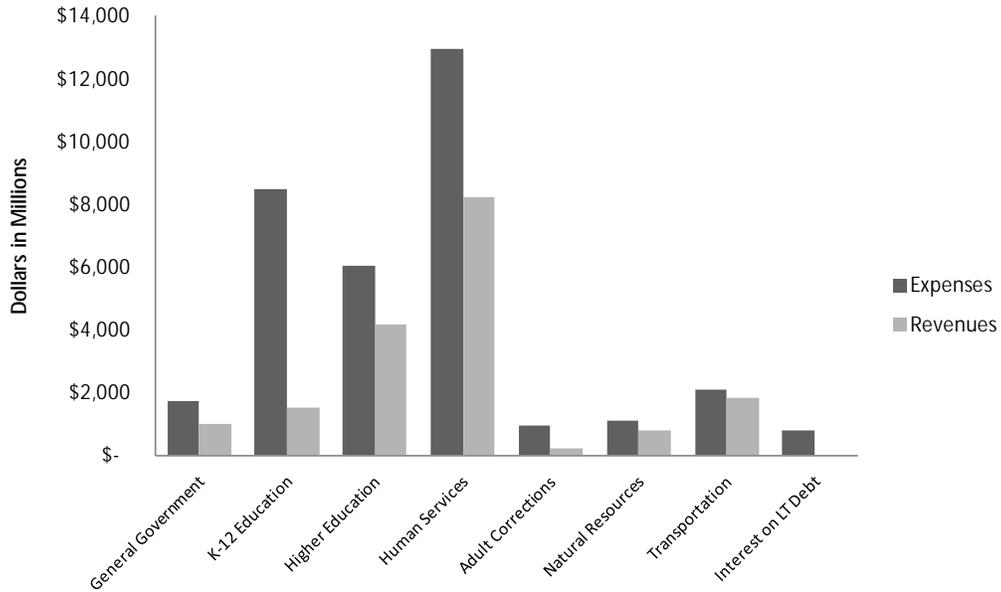
Business-Type Activities. Business-type activities decreased the state of Washington's net assets by \$1.8 billion which included losses in both the workers' compensation and unemployment compensation activities. Key factors contributing to the operating results of business-type activities are:

- The decrease in net assets in the workers' compensation activity in Fiscal Year 2010 was \$598 million more than the decrease in Fiscal Year 2009. A number of factors contributed to the increased loss including a decrease in premium revenue of \$97 million which resulted from a 5.2 percent decline in the number of reported hours worked reflecting the current recessionary stress on the job market. Claims costs increased by \$1.8 billion or 82.1 percent in Fiscal Year 2010 compared with Fiscal Year 2009. The increase in claims costs is attributable to increases in forecasted future wage inflation, an increase in the number of pensions granted for permanent disability, and increases in the duration of time-loss claims affecting both current and prior year claims. Nonoperating investment income increased by \$1.2 billion due to improvements in the financial markets.
- The unemployment compensation activity reported a Fiscal Year 2010 operating loss of \$985 million, compared to a \$789 million operating loss in Fiscal Year 2009. Washington's unemployment insurance program is an experience-based system. Since Washington had relatively low unemployment until Fiscal Year 2009, unemployment premium revenue had been declining. Fiscal Year 2010 premium revenues reflected the first increase since Fiscal Year 2005. This increase combined with an increase in federal aid of \$1.9 billion, which included American Recovery and Reinvestment Act funding, fell short of covering the increase in unemployment insurance benefits which rose by \$2.4 billion over Fiscal Year 2009. The increase in benefit costs was the result of increases in the number of claims and the duration of claims. The annualized unemployment rate for the state was 9.2 percent in Fiscal Year 2010, up from 7.3 percent in Fiscal Year 2009, a 26 percent increase.
- The higher education student services activity reported relatively proportional increases in both expenses and charges for services when compared to the prior year. Additionally, both liquor control and Washington's lottery activities reported operating revenues and expenses consistent with the prior year.

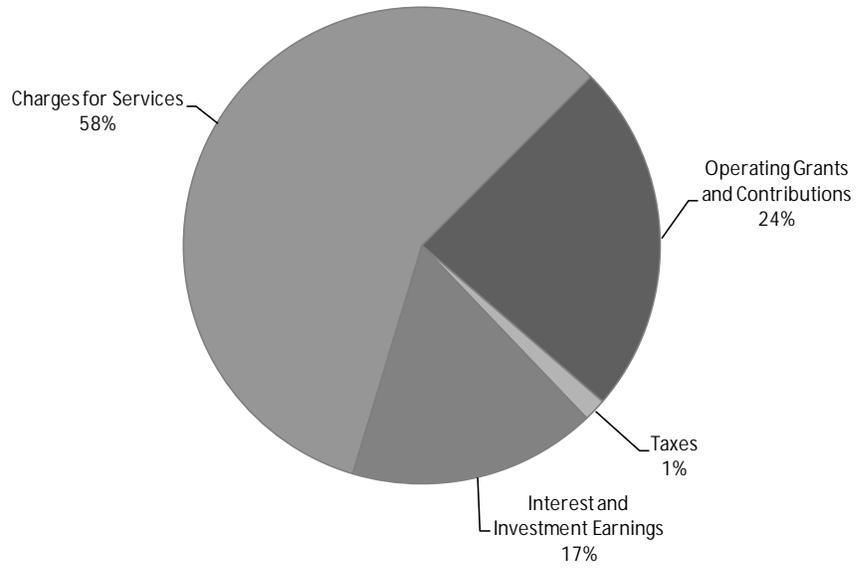
Revenues by Source: Governmental Activities



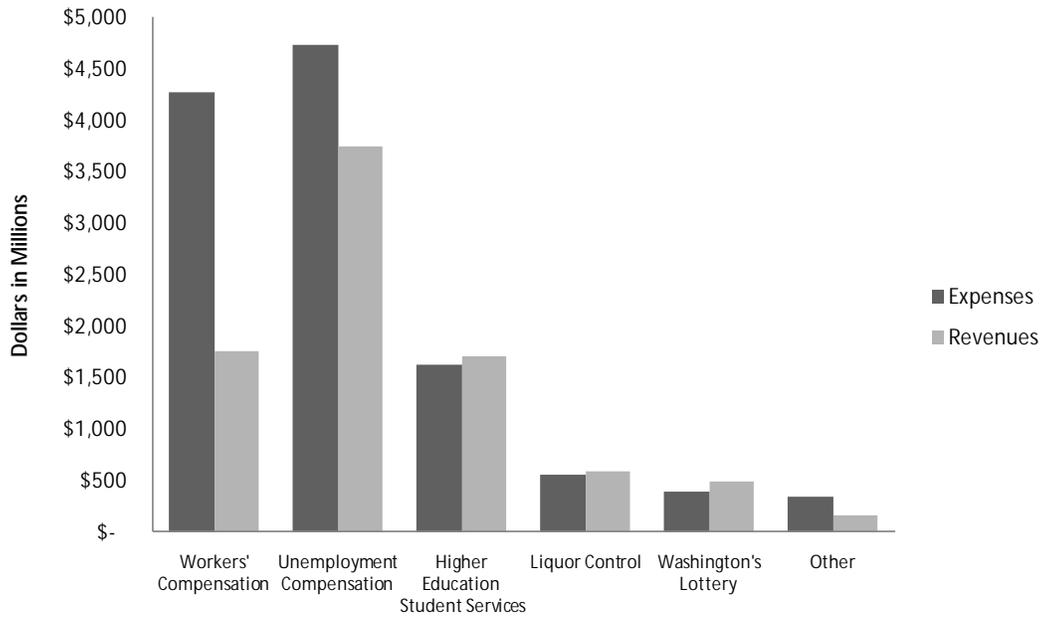
Program Revenues and Expenses: Governmental Activities



Revenues by Source: Business-Type Activities



Program Revenues and Expenses: Business-Type Activities



Financial Analysis of the Government's Funds

As noted earlier, the state of Washington uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. As previously discussed, the focus of the state of Washington's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the state of Washington's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the chief operating fund of the state of Washington. Due to statutory changes, several related accounts were added to the General Fund during Fiscal Year 2010 to improve budget transparency.

At the end of Fiscal Year 2010, total fund balance for the General Fund equaled \$379 million, a decrease of \$783 million from Fiscal Year 2009. Unreserved fund balance included \$864 million designated for working capital purposes. This amount relates to certain accrued revenues and is not considered by management to be available to spend.

The remaining unreserved fund balance deficit of \$(561) million indicates that the state has overspent funds available for discretionary purposes. The deficit fund balance reflects the Fiscal Year 2010 decrease of \$783 million which followed the \$757 million decrease in Fiscal Year 2009. The back to back decreases are due to the recessionary economic conditions.

The increase in General Fund revenues and expenditures is largely attributable to the consolidation of the related accounts. Consistent with Fiscal Year 2009, revenues did not keep pace with the demand for services.

STATE OF WASHINGTON			
General Fund			
<i>(in millions of dollars)</i>			
	Fiscal Year		Difference Increase (Decrease)
	2010	2009	
REVENUES			
Taxes	\$13,169	\$12,791	\$ 378
Federal grants	9,648	8,311	1,337
Investment revenue (loss)	(9)	64	(73)
Other	567	421	146
Total	23,375	21,587	1,788
EXPENDITURES			
Human services	13,209	11,912	1,297
Education	9,243	9,044	199
Other	1,331	1,223	108
Total	23,783	22,179	1,604
Net transfers in (out)	(379)	(192)	(187)
Other financing sources	4	27	(23)
Net increase (decrease) in fund balance	\$ (783)	\$ (757)	\$ (26)

Expenditures continue to be concentrated in services and programs most vital to citizens – primarily human services and public education. In Fiscal Year 2010, the General Fund received \$1.7 billion in American Recovery and Reinvestment Act funding predominately for human services and public education programs up from \$927 million in Fiscal Year 2009.

In addition to the General Fund, the state reports the Higher Education Special Revenue, the Motor Vehicle

Special Revenue and the Higher Education Endowment Funds as major governmental funds.

The fund balance of the Higher Education Special Revenue Fund increased by \$114 million in Fiscal Year 2010. Increases in tuition and federal grant revenues offset the increased costs of higher education activities.

The fund balance of the Motor Vehicle Special Revenue Fund increased by \$1.2 billion. The majority of this

increase is due to June bond sale proceeds intended for expenditure on construction projects during the summer months. The state issued \$1.7 billion in federal Build America Bond bonds in Fiscal Year 2010 accelerating a portion of the planned Fiscal Year 2011 borrowings to take advantage of exceptionally low interest rates.

The fund balance for the Higher Education Endowment Fund increased by \$251 million. While support from donors was consistent with the prior year, investment earnings of \$270 million in Fiscal Year 2010 compared with investment losses of \$474 million in Fiscal Year 2009 reflected improvement in the financial markets. The increase in investment earnings supported the increased use of funds to support donor specified activities.

The fund balance for nonmajor governmental funds increased by \$186 million. The largest factor contributing to the increase is bond sale proceeds on hand at year end to cover construction projects in progress.

Proprietary Funds. The state of Washington's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

- The Workers' Compensation Fund reported a loss of \$1.0 billion in Fiscal Year 2010. Operating revenues decreased by \$101 million and operating expenses increased by \$1.7 billion as compared to Fiscal Year 2009. As noted previously, operating revenues were down due to a reduction in reported worker hours reflecting the sluggish job market and claims were up due to increases in forecasted future wage inflation, an increase in the number of pensions granted for permanent disability, and increases in the duration of time-loss claims affecting both current and prior year claims. The negative changes were partially offset by an increase in investment income of \$1.2 billion.
- Washington's average unemployment rate increased markedly in Fiscal Year 2010, as the continued slow national economy and weak housing markets took their toll on the labor markets. Despite an increase in federal aid of \$1.9 billion, which included American Recovery and Reinvestment Act funding, the Unemployment Compensation Fund incurred a loss of \$870 million.
- Activity for the various nonmajor proprietary funds resulted in a net increase to net assets of \$18 million. The overall increase was reduced by the \$20 million loss reported by the state's guaranteed college tuition (GET) program which is included in the Other Activities Fund. This GET loss was smaller than the \$340 million loss reported in Fiscal Year 2009. The losses are primarily due to lower than projected investment earnings combined with higher than projected tuition increases. The GET program is continuing to proceed cautiously.

General Fund Budgetary Highlights

Differences between the original budget of the General Fund and the final amended budget reflect adjustments related to changes in the state's economy during the year ended June 30, 2010. While there were no significant increases or decreases, changes to estimates are summarized as follows:

- Estimated resources increased by \$950 million over the course of the first fiscal year. A decrease of \$911 million was reported for taxes in recognition of the continued sluggish economy. The decrease in estimated tax revenue was offset by increases to federal grants-in-aid of \$1.3 billion.
- Appropriated expenditure authority increased by \$1.2 billion over the course of the Fiscal Year ended June 30, 2010. Increases were recorded in human services, natural resources and recreation, education and capital outlays of \$1.2 billion, \$90 million, \$57 million, and \$29 million, respectively. The largest decrease was in transfers to other funds of \$171 million.

The state did not overspend its legal spending authority for the Fiscal Year 2010, the first year of the 2009-2011 Biennium. Actual General Fund revenues and expenditures were 48 and 49 percent of final budgeted revenues and appropriations, respectively, for the 2009-2011 Biennium.

Capital Assets, Infrastructure, Bond Debt Administration, and Economic Factors

Capital Assets. The state of Washington's investment in capital assets for its governmental and business-type activities as of June 30, 2010 amounted to \$33.5 billion (net of accumulated depreciation). This investment in capital assets includes land, infrastructure, museum and historical collections, buildings and other improvements, furnishings, equipment, and intangibles, as well as construction in progress.

Washington's Fiscal Year 2010 investment in capital assets, net of current year depreciation, was \$1.8 billion, including increases to the state's transportation infrastructure of \$1.4 billion and buildings of \$558 million. The state's construction in progress includes both new construction and major improvements to state and common school capital facilities, transportation projects and assistance to local governments for public works capital projects.

Remaining commitments on these construction projects total \$5.3 billion.

Additional information on the state of Washington's capital assets can be found in Note 6 beginning on page B76 of this report.

Infrastructure. The state of Washington first reported infrastructure under the requirements of the

Governmental Accounting Standards Board (GASB) Statement No. 34 in Fiscal Year 2002. Transportation infrastructure reported includes the state highway system, emergency airports, and two short rail lines. While the rail lines are reported net of depreciation, the state highway system and emergency airports are reported using the modified approach. Under the modified approach, rather than recording depreciation, asset condition is reported.

STATE OF WASHINGTON						
Capital Assets - Net of Depreciation						
<i>(in millions of dollars)</i>						
	Governmental Activities		Business-Type Activities		Total	
	2010	2009	2010	2009	2010	2009
Land	\$ 1,179	\$ 1,130	\$ 143	\$ 142	\$ 1,322	\$ 1,272
Transportation infrastructure and other assets not depreciated	19,758	18,328	-	-	19,758	18,328
Buildings	6,926	6,473	1,671	1,566	8,597	8,039
Furnishings, equipment and intangible assets	1,362	1,377	142	150	1,504	1,527
Other improvements and infrastructure	1,157	1,065	87	88	1,244	1,153
Construction in progress	865	1,185	211	153	1,076	1,338
Total	\$ 31,247	\$ 29,558	\$ 2,254	\$ 2,099	\$ 33,501	\$ 31,657

The condition of these assets, along with the rating scales for pavement, bridges, rest areas, and airports, and additional detail comparing planned-to-actual preservation and maintenance spending are available in the required supplementary information beginning on page B151.

The state highway system capital investment in Fiscal Year 2010 was a net of \$1.4 billion to add additional lane miles, replace and build new bridges and highway structures, improve highway safety, increase mobility and preservation activities that extend the life of the system. Of this investment, \$150.5 million was funded by the federal American Recovery and Reinvestment Act. The Washington State Department of Transportation (WSDOT) accomplished a net addition of 106 lane miles and 23 bridges and other highway structures in Fiscal Year 2010. Amounts spent during Fiscal Year 2010 to maintain and preserve these infrastructure assets were not significantly different from estimated spending plans according to the biennial budget.

The state highway system and emergency airports continue to meet established condition levels. No significant changes in condition levels were noted for pavements or bridges. Detailed information about targeted and actual condition levels for roads, bridges, rest areas, and airports can be found in the required supplementary information section of this report.

The safety of bridge structures is ensured through meticulous inspections and rating of the primary components of bridges by the WSDOT Bridge Preservation Office or local agency staff. The condition of all bridge decks, superstructures and substructures are rated based on these inspections.

The WSDOT's planned highway infrastructure projects for the next four years, Fiscal Years 2011 through 2014, would commit approximately \$3.7 billion for 448 projects. These projects are either already in progress or are expected to commence within the next four years.

Bond Debt. At the end of Fiscal Year 2010, the state of Washington had general obligation bond debt outstanding of \$16.6 billion, an increase of 18 percent over Fiscal Year 2009. This debt is secured by a pledge of the full faith and credit of the state. Additionally, the state had authorized \$9.5 billion general obligation debt that remains unissued.

During Fiscal Year 2010, the state issued general obligation debt, totaling \$3.9 billion, for various capital and transportation projects. The state took advantage of historically low interest rates and the federal Build America Bonds program to lock in long-term borrowing costs at unprecedented lows. Two Build America Bonds sales during Fiscal Year 2010 provided \$1.6 billion to finance transportation projects at the lowest net effective true

interest cost in state history. Washington also capitalized on strong demand for Washington debt to refund outstanding bonds for a savings of \$70.4 million in debt service costs.

General obligation debt is subject to the constitutional limitation as prescribed by the State Constitution. The aggregate debt contracted by the state as of June 30, 2010, does not exceed that amount for which payments of principal and interest in any fiscal year would require the state to expend more than 9 percent of the arithmetic mean of its general state revenues for the three immediately preceding fiscal years. The arithmetic mean

of its general state revenues for Fiscal Years 2007, 2008, and 2009 is \$12.5 billion. The debt service limitation, 9 percent of this mean, is \$1.1 billion. The state's maximum annual debt service as of June 30, 2010 subject to the constitutional debt limitation is \$971.3 million, or \$155.4 million less than the debt service limitation.

For further information on the debt limit, refer to the Certification of the Debt Limitation of the State of Washington, available from the Office of the State Treasurer or at: http://www.tre.wa.gov/documents/debt_cdl2010.pdf.

STATE OF WASHINGTON						
Bond Debt						
<i>(in millions of dollars)</i>						
	Governmental		Business-Type		Total	
	Activities		Activities			
	2010	2009	2010	2009	2010	2009
General obligation (GO) bonds	\$ 16,540	\$ 14,049	\$ 60	\$ 69	\$ 16,600	\$ 14,118
Accreted interest on zero						
interest rate GO bonds	367	328	42	38	409	366
Revenue bonds	743	616	1,084	1,074	1,827	1,690
Total	<u>\$ 17,650</u>	<u>\$ 14,993</u>	<u>\$ 1,186</u>	<u>\$ 1,181</u>	<u>\$ 18,836</u>	<u>\$ 16,174</u>

By statutory provision, the State Finance Committee (SFC) is authorized to supervise and control the issuance of all state bonds, notes, or other evidences of indebtedness.

The SFC is composed of the Governor, Lieutenant Governor, and State Treasurer, the latter serving as chairman.

As of June 30, 2010, the state of Washington's general obligation debt was rated Aa1 by Moody's Investor Service, AA+ by Standard & Poor's Rating Group (S & P), and AA+ by Fitch Ratings.

The state had revenue debt outstanding at June 30, 2010, of \$1.8 billion, an increase of \$137 million over Fiscal Year 2009. This increase is primarily related to revenue bonds issued by state colleges and universities. This debt is not supported or intended to be supported by the full faith and credit of the state. Revenue bond debt is generally secured by specific sources of revenue. The exception is the University of Washington who issues general revenue bonds that are payable from general revenues of the university.

Additional information on the state's bond debt obligations is presented in Note 7 beginning on page B80 of this report.

Additional information on the state's legal debt limit is presented in the statistical section on page 266 of the Comprehensive Annual Financial Report.

Conditions with Expected Future Impact

Economic Factors. The forecast for Washington for Fiscal Year 2011 is for a slow to moderate recovery from the recession. That said, in the coming year, legislative leaders and management will be facing a number of challenges.

- Employment is projected to begin rebounding in Fiscal Year 2011, although construction employment is not expected to show signs of recovery until the second half of Fiscal Year 2011.
- The economic recovery is expected to be slow by historical standards.
- Following September 2011 forecast projections of reduced state revenues, Governor Gregoire called for across the board cuts in the General Fund of 6.3 percent effective October 1, 2011.

Rainy Day Account. In November 2007, Washington State voters ratified Engrossed Substitute Senate Joint Resolution 8206, amending the state's Constitution and establishing the Budget Stabilization Account (BSA). The Constitution details a limited number of circumstances under which funds can be appropriated from the BSA, one of which is a favorable vote of at least three-fifths of the members of each house of the Legislature.

On June 30, 2010, \$119 million was transferred to the BSA from the General Fund in accordance with the provisions of the Constitution. Also during Fiscal Year 2010, Engrossed Substitute House Bill 6444 authorized the transfer of \$45 million from the BSA to the General Fund.

The BSA has a fund balance of \$95 million as of June 30, 2010.

November 2, 2010 General Election. There were measures on the state's November 2, 2010 general election ballot that addressed state laws related to state operations, state imposed taxes and fees, and the calculation of the

state debt limitation. These measures, if passed, could fiscally impact the state. Election results are not final or official until certified. By law, December 2, 2010 is the last day for the Office of the Secretary of State to certify General Election returns. Information is posted as available on the Secretary of State's website at <http://www.sos.wa.gov>.

Requests for Information

This financial report is designed to provide a general overview of the state of Washington's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of Financial Management, Accounting Division, P.O. Box 43113, Olympia, WA 98504-3113.