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, 2011. 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 $19.0 billion (reported as net assets). Of this amount, $(8.5) 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 $10.6 billion, an increase of 0.1 percent compared with the prior year.

- The General Fund reported unassigned fund balance (deficit) of $(107.8) million, at the end of fiscal year 2011, or 0.4 percent of total General Fund expenditures.

- The state's capital assets increased by $1.4 billion while total bond debt increased by $488 million during the current fiscal year.

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 B15 - 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 fund balances 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, 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 B21 - 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, the Higher Education Student Services Fund, and the Other Activities 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 - B33 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 B34 and B35 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 B40 - B49 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 B36 and B37 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 B39 - B134 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 B135 - B160 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 181-241 of Comprehensive Annual Financial Report.

STATE OF WASHINGTON
Statement of Net Assets
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
ASSETS						
Current and other assets	$ 17,210	$ 16,915	$ 23,249	$ 22,080	$ 40,459	$ 38,995
Capital assets	32,960	31,247	1,947	2,254	34,907	33,501
Total assets	50,170	48,162	25,196	24,334	75,366	72,496
LIABILITIES						
Current and other liabilities	3,900	3,730	3,109	3,421	7,009	7,151
Long-term liabilities outstanding	21,540	21,234	27,832	27,934	49,372	49,168
Total liabilities	25,440	24,964	30,941	31,355	56,381	56,319
NET ASSETS						
Invested in capital assets, net of related debt	18,723	18,201	718	913	19,441	19,114
Restricted	4,847	5,214	3,199	2,930	8,046	8,144
Unrestricted (deficit)	1,160	(217)	(9,662)	(10,864)	(8,502)	(11,081)
Total net assets	$ 24,730	$ 23,198	$ (5,745)	$ (7,021)	$ 18,985	$ 16,177

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 $19.0 billion at June 30, 2011 as compared to $16.2 billion as reported at June 30, 2010.

The largest portion of the state's net assets (102.4 percent for fiscal year 2011 as compared to 118.2 percent for fiscal year 2010) 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 (42.4 percent for fiscal year 2011 as compared to 50.3 percent for fiscal year 2010) represents resources that are subject to external restrictions on how they may be used. The remaining balance of $(8.5) 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, unrestricted net assets improved from $(217) million deficit in fiscal year 2010 to $1.2 billion in fiscal year 2011. The improvement was a

combination a modest increase in revenues, and the state's ability to curtail spending in response to revenue shortfalls.

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

(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
REVENUES						
Program revenues:						
Charges for services	$ 4,902	$ 4,584	$ 6,466	$ 5,987	$ 11,368	$ 10,571
Operating grants and contributions	12,609	12,193	2,305	2,468	14,914	14,661
Capital grants and contributions	833	939	13	-	846	939
General revenues:						
Taxes	16,166	14,982	174	160	16,340	15,142
Interest and investment earnings (loss)	474	449	1,611	1,743	2,085	2,192
Total Revenues	34,984	33,147	10,569	10,358	45,553	43,505
EXPENSES						
General government	(1,674)	(1,738)	-	-	(1,674)	(1,738)
Education - K-12	(8,055)	(8,468)	-	-	(8,055)	(8,468)
Education - Higher education	(6,257)	(6,051)	-	-	(6,257)	(6,051)
Human services	(13,364)	(12,946)	-	-	(13,364)	(12,946)
Adult corrections	(935)	(938)	-	-	(935)	(938)
Natural resources and recreation	(996)	(1,084)	-	-	(996)	(1,084)
Transportation	(1,981)	(2,073)	-	-	(1,981)	(2,073)
Interest on long-term debt	(882)	(810)	-	-	(882)	(810)
Workers' compensation		-	(1,219)	(4,268)	(1,219)	(4,268)
Unemployment compensation		-	(3,690)	(4,729)	(3,690)	(4,729)
Higher education student services		-	(1,820)	(1,628)	(1,820)	(1,628)
Liquor control		-	(556)	(552)	(556)	(552)
Washington's lottery		-	(393)	(389)	(393)	(389)
Other business-type activities		-	(784)	(345)	(784)	(345)
Total Expenses	(34,144)	(34,108)	(8,462)	(11,911)	(42,606)	(46,019)
Excess (deficiency) of revenues over expenses before contributions to endowments and transfers	840	(961)	2,107	(1,553)	2,947	(2,514)
Contributions to endowments	69	52	-	-	69	52
Transfers	231	252	(231)	(252)	-	-
Special item	-	-	(223)	-	(223)	-
Increase (decrease) in net assets	1,140	(657)	1,653	(1,805)	2,793	(2,462)
Net assets - July 1, as restated	23,590	23,855	(7,398)	(5,216)	16,192	18,639
Net assets - June 30	$ 24,730	$ 23,198	$ (5,745)	$ (7,021)	$ 18,985	$ 16,177

Governmental Activities. Governmental activities resulted in an increase in the state of Washington's net assets of $1.1 billion. A number of factors contributed to the increase:

- Tax revenues increased by $1.2 billion in fiscal year 2011 as compared to fiscal year 2010 reflecting sluggish positive growth in the economy. Sales and use taxes reported an increase of $478 million. Sales and use taxes are the main tax revenue for governmental activities. The increase in sales tax is attributable to both a slight increase in taxable sales in fiscal year 2011 and a tax penalty amnesty program in the spring of 2011. Business and occupation tax, the second largest source of tax revenue in governmental activities, increased by $480 million in fiscal year 2011 over 2010. It is a tax on the gross receipts of all businesses operating in Washington. Growth in business and occupation tax revenue in fiscal year 2011 was mainly due to an increase in the tax rate on services which increased from 1.5 percent to 1.8 percent. Business and occupation tax collections were also aided by the tax penalty amnesty program and other legislative changes.

- Operating and capital grants and contributions increased $310 million in fiscal year 2011 as compared to fiscal year 2010. While American Recovery and Reinvestment Act (ARRA) grants contributed $1.6 billion in fiscal year 2011, it was a decrease of $615 million from the level contributed in fiscal year 2010. Offsetting the decrease in ARRA grants were increases in non-ARRA student financial assistance and supplemental nutrition assistance grants.

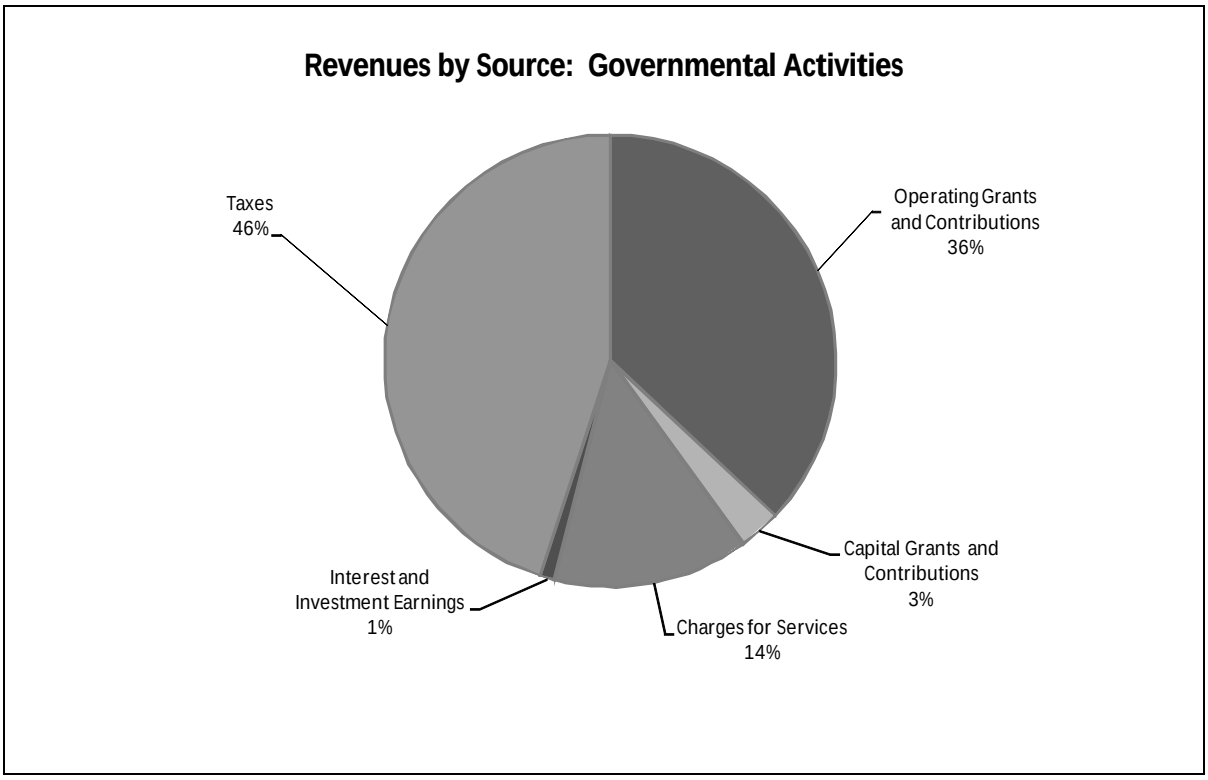
- Expenses grew slightly in fiscal year 2011 as compared to fiscal year 2010. The expenses for human services and education comprised 81.1 percent of the total expenses for governmental activities which is fairly consistent with the 80.5 percent in fiscal year 2010. Human services accounted for the majority of the growth in expenses increasing by $418 million or 3.2 percent in fiscal year 2011 over fiscal year 2010 reflecting the increased number of citizens seeking assistance from state programs and services due to the economic recession.

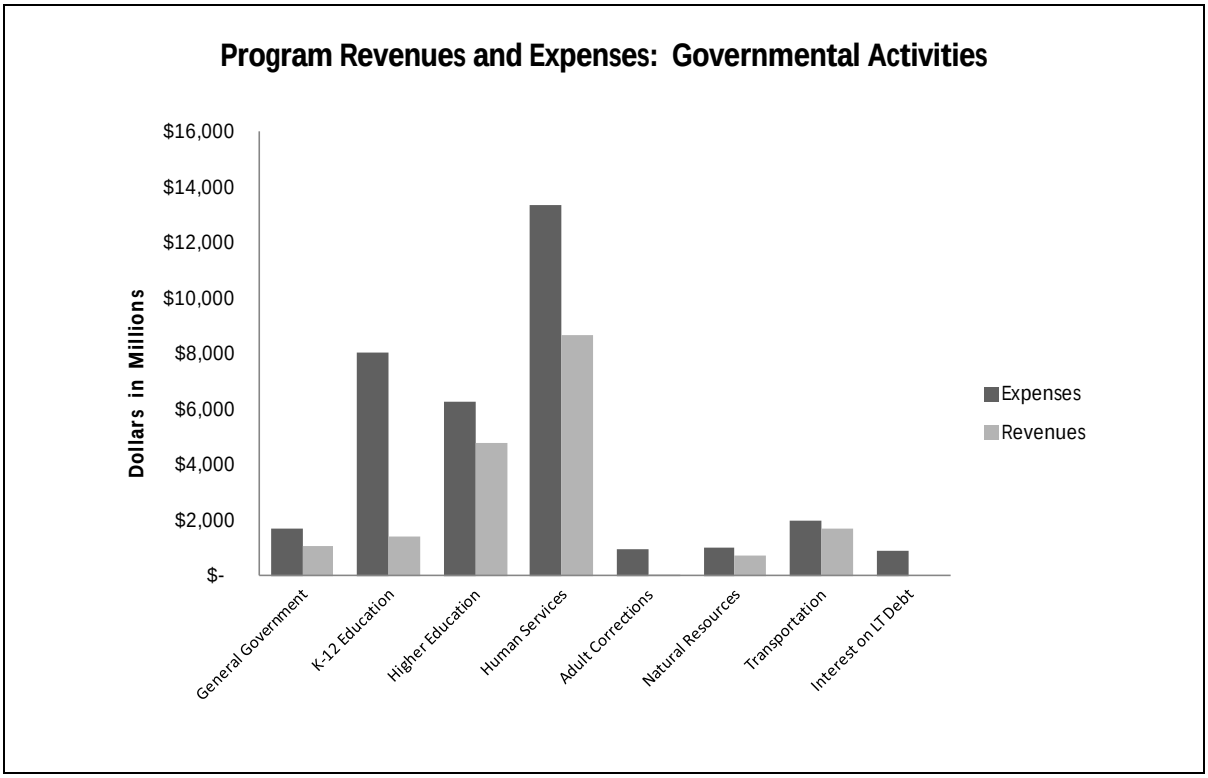
Business-Type Activities. Business-type activities increased the state of Washington's net assets by $1.7 billion which included increases in both the workers' compensation and unemployment compensation activities. Key factors contributing to the operating results of business-type activities are:

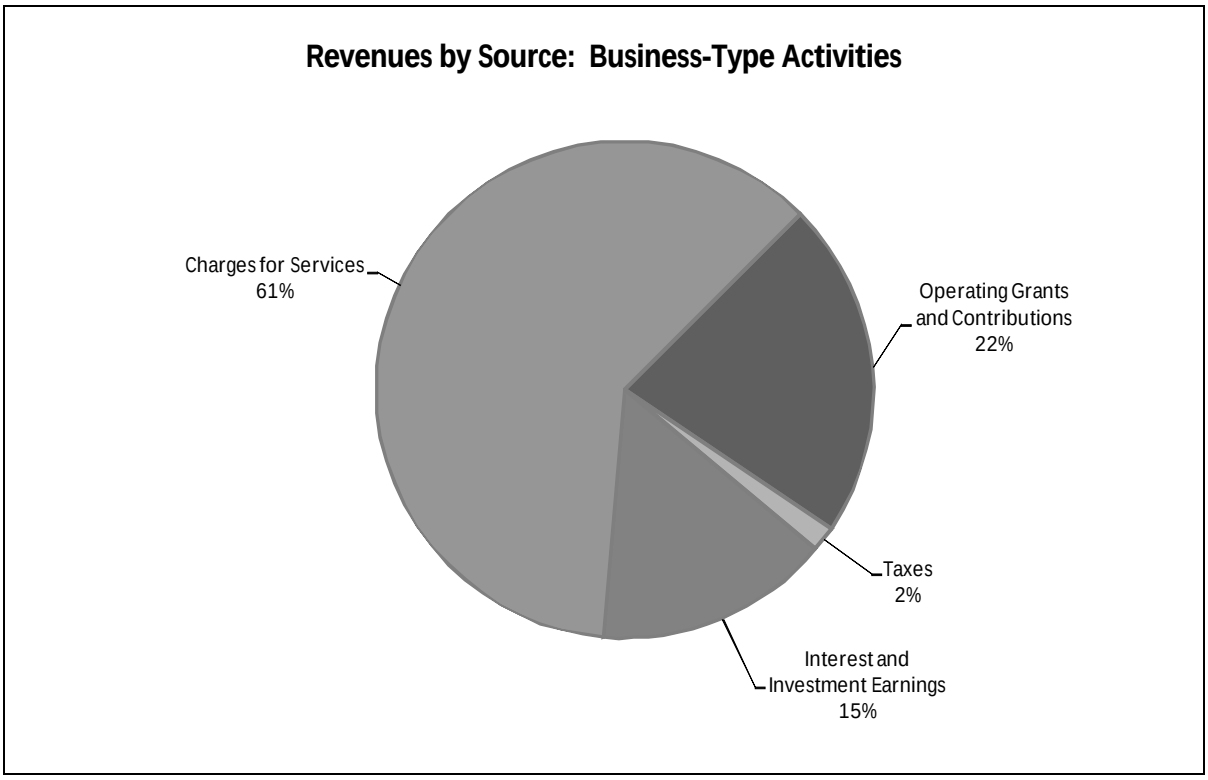
- The increase in net assets in the workers' compensation activity in fiscal year 2011 was $1.8 billion after a decrease of $1.0 billion in fiscal year 2010. A number of factors contributed to the turn around. Premium revenue increased by $256 million as a result of a January 2011 premium rate increase that averaged 12 percent and a slight increase in reported hours worked. Claims costs decreased by $3.1 billion in fiscal year 2011 compared with fiscal year 2010 in large part due to workers' compensation reform legislation. Substitute Senate Bill 5801 and Engrossed House Bill 2123 provided for: (1) the implementation of a single statewide network of health care providers to treat injured workers and expansion of the Centers of Occupational Health and Education, which increases the use of occupational health best practices in treating injured workers; (2) a structured settlement option for injured workers who are age 55 by January 1, 2012; and (3) a one year cost of living adjustment freeze and a one year delay for first-time COLA during fiscal year 2012. Other factors contributing to the decline in claims costs included the use of generic drugs and the low wage rate growth. Nonoperating investment income decreased by $457 million due to lower returns on fixed income securities.

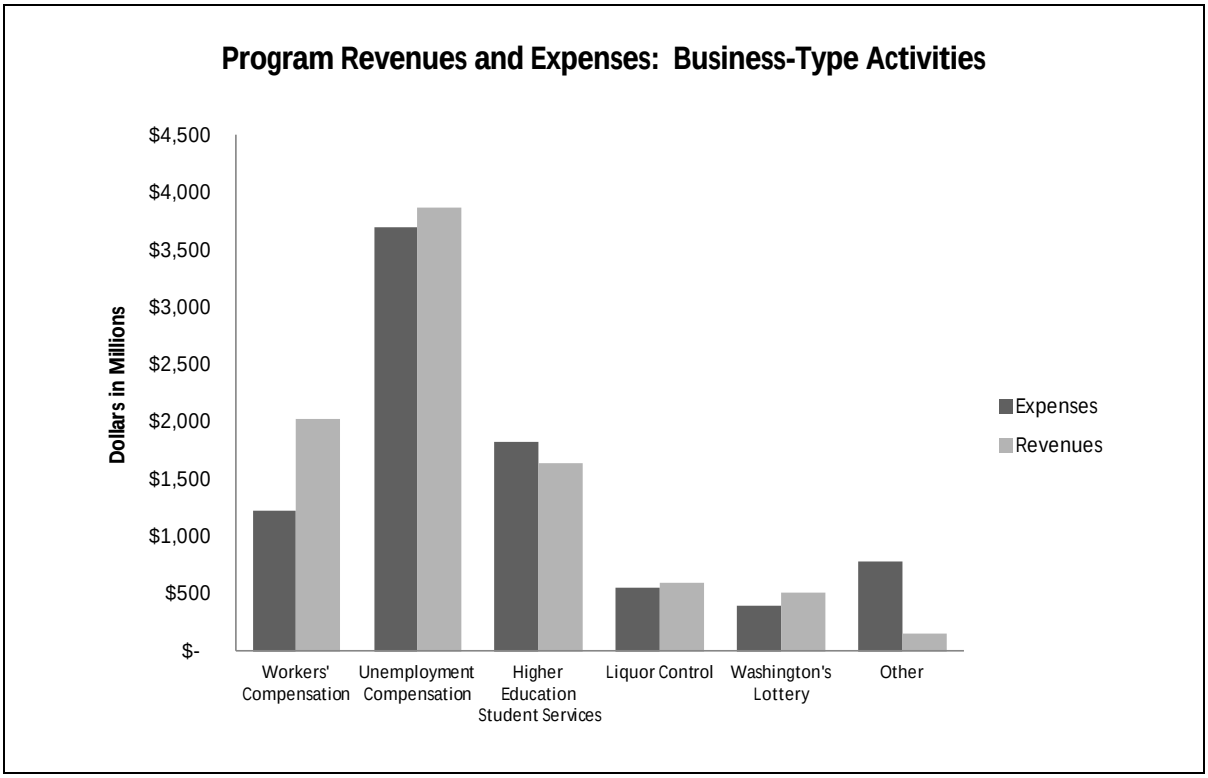
- The unemployment compensation activity reported operating income in fiscal year 2011 of $171 million, compared to a $985 million operating loss in fiscal year 2010. Washington's unemployment insurance program is an experience-based system. Due to the recession, Washington has seen a rise in the number of unemployed starting in 2009. The rise in unemployment has resulted in increased premium charges to employers. Additionally, the taxable wage base increased to $37,300 in 2011 from $36,800 in 2010. Unemployment insurance benefits declined by $1.0 billion in fiscal year 2011 over fiscal year 2010. The decrease in benefit costs was the result of a decline in the number of claims and the duration of claims. While the annualized unemployment rate for the state was 9.3 percent in fiscal year 2011, up from 8.7 percent in fiscal year 2010, the insured rate declined to 3 percent in fiscal year 2011 from 3.75 percent in fiscal year 2010.

- 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
Taxes 46%
Operating Grants and Contributions 36%
Capital Grants and Contributions 3%
Charges for Services 14%
Interest and Investment Earnings 1%


Program Revenues and Expenses: Governmental Activities
Dollars in Millions
$16,000
$14,000
$12,000
$10,000
$8,000
$6,000
$4,000
$2,000
$-
General Government
K-12 Education
Higher Education
Human Services
Adult Corrections
Natural Resources
Transportation
Interest on LT Debt
Expenses
Revenues


Revenues by Source: Business-Type Activities
Charges for Services
61%
Operating Grants
and Contributions
22%
Taxes
2%
Interest and
Investment Earnings
15%


Program Revenues and Expenses: Business-Type Activities
Dollars in Millions
$4,500
$4,000
$3,500
$3,000
$2,500
$2,000
$1,500
$1,000
$500
$-
Workers' Compensation
Unemployment Compensation
Higher Education Student Services
Liquor Control
Washington's Lottery
Other
Expenses
Revenues

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 fund balances. Such information is useful in assessing the state of Washington's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

Adjustments to Beginning Fund Balances. As described in Note 2 to the financial statements on pages B50 and B51, beginning fund balances of governmental funds were adjusted. To enhance comparability, all amounts presented for fiscal year 2010 in this discussion and analysis were revised, where applicable, to reflect these changes as if the changes had been made in the prior year.

- Net reclassification of $253.9 million from the Nonmajor Governmental Funds to the General Fund related to the implementation of Governmental Accounting Standards Board Statement Number 54.

- Reclassification of the Motor Vehicle Fund from a major fund to a nonmajor governmental fund because it fell below the major fund threshold.

Fund Balances. At June 30, 2011, the state's governmental funds reported combined ending fund balances of $10.6 billion. Of this amount, $3.75 billion or 35.6 percent is nonspendable, either due to its form or legal constraints, and $3.81 billion or 36.1 percent is restricted for specific programs by external constraints, constitutional provisions or contractual obligations. An additional $2.15 billion or 20.4 percent of total fund balance has been committed to specific purposes. Committed amounts cannot be used for any other purpose unless approved by the Legislature. An additional $1.11 billion or 10.6 percent of total fund balance has been assigned to specific purposes by management. The remaining $(282) million or (2.7) percent of fund balance is unassigned.

The General Fund is the chief operating fund of the state of Washington. At the end of fiscal year 2011, total fund balance for the General Fund equaled $1.2 billion, an increase of $585.6 million over fiscal year 2010. Assigned fund balance included $1.1 billion in fiscal year 2011 which is assigned for working capital purposes. This amount relates to certain accrued revenues which are not considered by management to be available for budgetary purposes.

The unassigned fund balance deficit of $(107.8) million in the General Fund indicates that the state has overspent funds available for discretionary purposes. The deficit fund balance in fiscal year 2011 reflects improvement over the $(561) million deficit in fiscal year 2010. The back to back deficits are due to the recessionary economic conditions which have adversely impacted state revenues.

STATE OF WASHINGTON
General Fund
(in millions of dollars)

	Fiscal Year 2011	Fiscal Year 2010	Difference Increase (Decrease)
REVENUES			
Taxes	$ 14,423	$ 13,169	$ 1,254
Federal grants	9,597	9,648	(51)
Investment revenue (loss)	(15)	(7)	(8)
Other	645	563	82
Total	24,650	23,373	1,277
EXPENDITURES			
Human services	13,473	13,238	235
Education	9,211	9,491	(280)
Other	1,519	1,632	(113)
Total	24,203	24,361	(158)
Net transfers in (out)	(215)	(7)	(208)
Other financing sources	354	137	217
Net increase (decrease) in fund balance	$ 586	$ (858)	$ 1,444

Expenditures continue to be concentrated in services and programs most vital to citizens – primarily human services and public education. In fiscal year 2011, the General Fund received $1.2 billion in American Recovery and Reinvestment Act down from $1.7 billion in fiscal year 2010. The majority of the ARRA funding in the General Fund was for human services programs.

In addition to the General Fund, the state reports the Higher Education Special Revenue, and the Higher Education Endowment Funds as major governmental funds.

The fund balance of the Higher Education Special Revenue Fund increased by $107 million in fiscal year 2011. Increases in tuition and federal grant revenues offset the increased costs of higher education activities.

The fund balance for the Higher Education Endowment Fund increased by $364 million. Support from donors increased by $17 million over the prior year and investment earnings increased by $89 million over the same period. The increase in donor support comes after four straight years of decreases and reflects slowly improving economic conditions.

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 an increase in net assets of $1.8 billion in fiscal year 2011. Operating revenues increased by $264 million and operating expenses decreased by $3.0 billion as compared to fiscal year 2010. As noted previously, operating revenues increased due to an increase in premium rates and claims expense decreased in large part due to workers' compensation reform legislation. Investment income decreased as compared to fiscal year 2010 due to lower returns on fixed income securities.

- Washington's Unemployment Compensation Fund reported operating income of $171 million. The increase in premium revenue of $304 million in fiscal year 2011 over 2010 was partially offset by a decrease in federal aid of $167 million over the same period. Unemployment benefit claims decreased by $1.0 billion in fiscal year 2011 as compared to 2010. As reported previously, while the unemployment rate in Washington remains high, the insured rate declined in fiscal year 2011.

- The Other Activities Fund was presented as a major proprietary fund for the first time in fiscal year 2011. The major activity in the Other Activities Fund is the state's guaranteed education tuition (GET) program. The GET program reported a net loss of $311 million in fiscal year 2011. While the program continues to attract new enrollments and investment returns are up, tuition rates have been escalating much higher than assumed in prior valuations. Tuition rates for the 2011-2012 school year increased by 19.0 percent exceeding the 7.5 percent assumed in the prior valuation. Tuition growth assumptions have been increased for future years.

- The state's Convention and Trade Center (CTC) which was reported as a nonmajor enterprise fund in prior years, was transferred to a public facilities district (PFD) in fiscal year 2011. The transfer agreement with the PFD required the PFD to provide the state with funds to retire the state's existing debt on the CTC. The transfer resulted in a net loss to the state of $223 million which is reported as a special item.

- The Higher Education Student Services and other nonmajor enterprise funds reported activity generally consistent with prior years.

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 biennium ended June 30, 2011. While there were no significant increases or decreases, changes to estimates are summarized as follows:

- Estimated resources increased by $1.1 billion over the course of the biennium. A decrease of $1.9 billion was reported for taxes reflecting the continued sluggish economy. The decrease in estimated tax revenue was offset by increases to federal grants-in-aid of $1.8 billion and transfers from other funds of $940 million.

- Appropriated expenditure authority increased by $1.8 billion over the course of the biennium ended June 30, 2011. Increases were recorded in human services, education and transfers to other funds of $856 million, $204 million, and $523 million, respectively. The largest decrease was in transportation of $5 million.

The state did not overspend its legal spending authority for the 2009-2011 Biennium. Actual General Fund revenues and expenditures were 96.9 and 96.8 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, 2011, totaled $34.9 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 2011 investment in capital assets, net of current year depreciation, was $1.4 billion, including increases to the state's transportation infrastructure of $1.3 billion. The state's construction in progress includes both new construction and major improvements to state capital facilities and infrastructure. Remaining commitments on these construction projects total $9.1 billion.

The land, buildings, furnishings and equipment (net of accumulated depreciation) of the Convention and Trade Center (CTC) which totaled $410 million were removed from the state records when the CTC was transferred to a public facilities district.

Additional information on the state of Washington's capital assets can be found in Note 6 beginning on page B78 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, state managed airports, and two short rail lines. While the rail lines are reported net of depreciation, the state highway system and state managed 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
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
Land	$ 1,331	$ 1,179	$ 65	$ 143	$ 1,396	$ 1,322
Transportation infrastructure and other assets not depreciated	21,092	19,758	-	-	21,092	19,758
Buildings	7,080	6,926	1,363	1,671	8,443	8,597
Furnishings, equipment and intangible assets	1,368	1,362	144	142	1,512	1,504
Other improvements and infrastructure	1,119	1,157	82	87	1,201	1,244
Construction in progress	970	865	293	211	1,263	1,076
Total	$ 32,960	$ 31,247	$ 1,947	$ 2,254	$ 34,907	$ 33,501

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 B135.

The state highway system capital investment in fiscal year 2011 was a net of $1.3 billion to add additional lane miles, replace and build new bridges and highway structures, improve highway safety, increase mobility and extend the life of existing infrastructure. As part of this highway improvement investment, the Washington State Department of Transportation (WSDOT) accomplished a net addition of 89 lane miles and 21 bridges and other highway structures in fiscal year 2011. Amounts spent during fiscal year 2011 to maintain and preserve these infrastructure assets were not significantly different from estimated spending plans according to the biennial budget.

The state highway system, bridges, and state managed airports continue to meet established condition levels. No significant changes in condition levels were noted for pavements or airports. Bridge assessments in fiscal year 2011 included a third condition measurement related to deck surface and resulted in an additional 2.5 percent of bridges in poor condition. 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 2012 through 2015, would commit approximately $6.8 billion for 387 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 2011, the state of Washington had general obligation bond debt outstanding of $16.8 billion, relatively unchanged from fiscal year 2010. This debt is secured by a pledge of the full faith and credit of the state. Additionally, the state had authorized $9.6 billion general obligation debt that remains unissued.

During fiscal year 2011, the state issued general obligation debt, totaling $2.1 billion, for various capital and transportation projects as well as to refund outstanding bones. Bonds totaling $1.9 billion were retired during the year which included $34.0 million in Convention and Trade Center (CTC) bonds that were refunded when the assets and activities of the CTC were transferred by the state to a public facilities district. Washington's refunding activity produced a savings of $155.9 million in future 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, 2011, 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 2008, 2009, and 2010 is $12.2 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, 2011, subject to the constitutional debt limitation is $995 million, or $101 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_cdl2011.pdf.

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, 2011, 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.

STATE OF WASHINGTON
Bond Debt
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total	
	2011	2010	2011	2010	2011	2010
General obligation (GO) bonds	$ 16,750	$ 16,540	$ 18	$ 60	$ 16,768	$ 16,600
Accreted interest on zero interest rate GO bonds	393	367	-	42	393	409
Revenue bonds	740	743	1,423	1,084	2,163	1,827
Total	$ 17,883	$ 17,650	$ 1,441	$ 1,186	$ 19,324	$ 18,836

The state had revenue debt outstanding at June 30, 2011, of $2.2 billion, an increase of $336 million over fiscal year 2010. This increase is 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 B82 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 Outlook. The forecast for Washington for fiscal year 2012 is for continued slow recovery from the recession. That said, in the coming year, legislative leaders and management will be facing a number of challenges.

- Consumer confidence remains low.
- The state's economy will continue to be adversely impacted by the uncertainty plaguing the global economy.
- The November 2011 state's revenue forecast of General Fund state revenue increased the projected revenue shortfall for the 2011 – 2013 biennium to $1.6 billion.

In light of negative revenue projections in both the June and September forecasts, Governor Gregoire announced that she will call legislators in for a special session beginning November 28, 2011, to address the state's budget. On October 27, 2011, Governor Gregoire presented a list of budget reduction alternatives as a starting point to the conversation lawmakers must engage in to resolve the state's budget deficit.

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, 2011, $129 million was transferred to the BSA from the General Fund in accordance with the provisions of the Constitution. Also during fiscal year 2011, Engrossed Substitute House Bill 1086 authorized the transfer of $223 million from the BSA to the General Fund.

The BSA has a fund balance of $564 thousand as of June 30, 2011.

General Election. There were measures on the state's November 8, 2011, general election ballot that addressed state laws related to state expenditures on transportation, requirements for long-term care workers and providers, and the distribution and sale of wine and spirits. These measures, if passed, could impact the state fiscally. Election results are not final or official until certified. By law December 8, 2011, 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, Statewide Accounting, P.O. Box 43113, Olympia, WA 98504-3113.