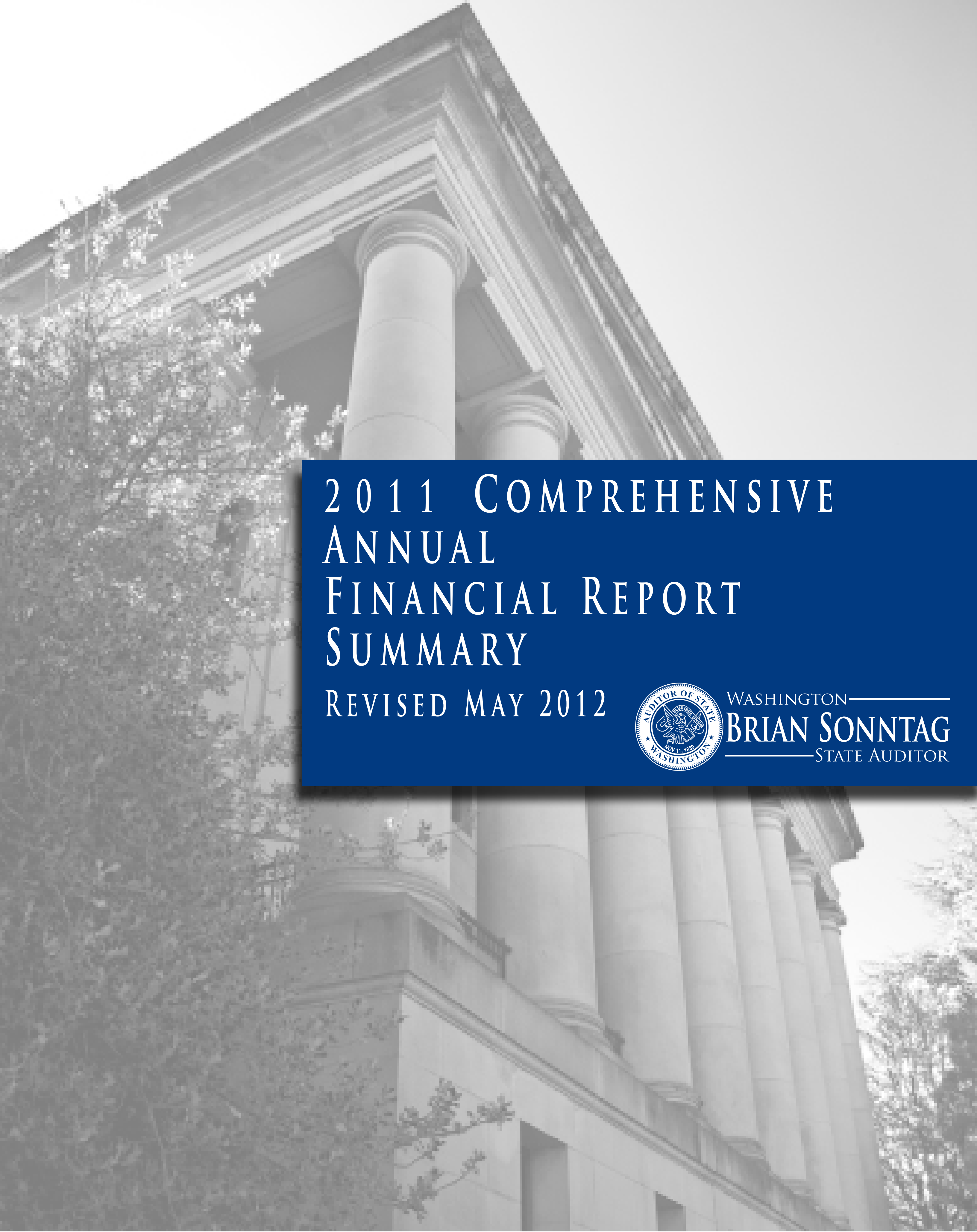


2011 Comprehensive Annual Financial Report Summary

Revised May 2012

Washington
Brian Sonntag
State Auditor

A snapshot of Washington's finances

Each year, as required by law, the state publishes its Combined Annual Financial Report, or CAFR, to provide information on the state's financial position.

The CAFR is a complex and lengthy document with detailed information on the state's structure, services, finances, trends and nonfinancial data.

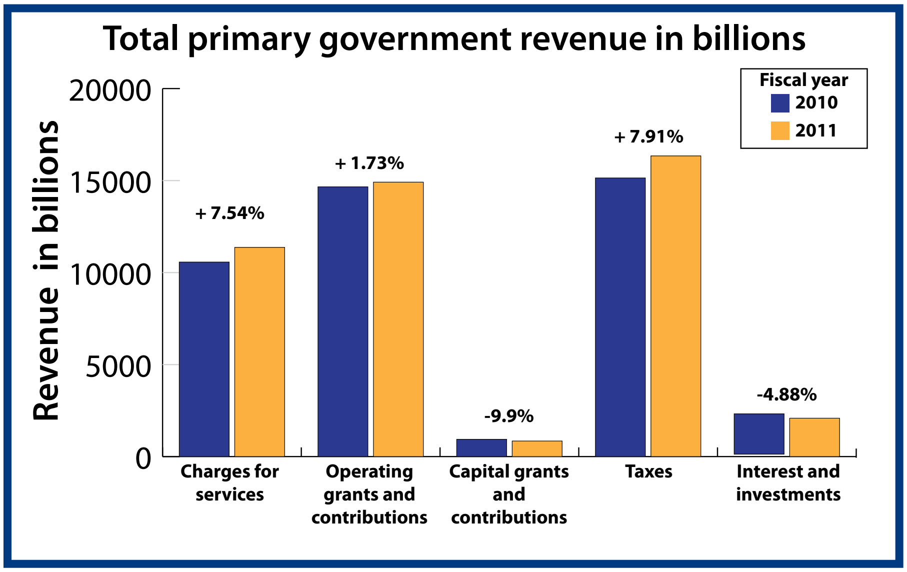
Because it can be difficult for many people to understand, we prepare this CAFR summary, to provide a snapshot of the state's financial position, including revenues and expenditures, cash balances and debt.

The Office of Financial Management prepares the CAFR in accordance with the Governmental Accounting Standards Board, and we perform an independent audit. Our audit of the fiscal year 2011 CAFR resulted in a clean audit opinion, meaning we concluded the financial statements fairly presented the state's financial position.

The full report is available at **http://www.ofm.wa.gov/cafr/default.asp**

Total Government Expenses (in millions)

Expenses	2010	2011	% Change
General Government	$1,738	$1,674	-3.68%
Education - K-12	8,468	8,055	-4.88%
Education - Higher Education	6,051	6,257	3.4%
Human Services	12,946	13,364	3.23%
Adult Corrections	938	935	-0.32%
Natural Resources & Recreation	1,084	996	-8.12%
Transportation	2,073	1,981	-4.44%
Interest on Long-term Debt	810	882	8.89%
Workers' Compensation	4,268	1,219	-71.44%
Unemployment Compensation	4,729	3,690	-21.97%
Higher Education Student Services	1,628	1,820	11.79%
Liquor Control	552	556	0.72%
Washington's Lottery	389	393	1.03%
Other Activities	345	784	127.25%
TOTAL EXPENSES	**$46,019**	**$42,606**	**-7.42%**



Highlights

General fund cash balance

As of June 30, 2011, for the third year in a row, Washington State's general fund had a negative cash balance. State law prohibits individual agencies from incurring cash deficiencies in their allocated funds, unless they are temporary and result from payments under an approved spending plan. However, state law does not prohibit a cash deficit for the state as a whole. State law does require the Governor or Legislature to take steps to address an anticipated cash deficit.

State Treasurer's Ending Fiscal Year Cash Balances (in millions)

Fund Type	2010	2011	% Change
General Fund	($626)	($70)	88.82%
Other Treasury Funds	$3,861	$2,808	-27.27%
Trust Funds	$678	$806	18.88%
TOTAL	$3,913	$3,544	-9.43%

The state's financial statements indicate the general fund has a $30.4 million cash balance. For financial statement reporting, additional accounts are considered to be part of the general fund.

Since the State Treasurer pools treasury funds, a liability in the general fund has been established to report the amount due to other treasury funds with positive cash balances.

At the end of the 2011 legislative session it was anticipated that the supplemental budget would result in a balanced budget for fiscal year 2011. However the June 2011 revenue forecast projected a further slowdown in taxable activity. The resulting call to agency heads to curtail discretionary spending was insufficient to prevent the deficiency. The general fund cash deficit has continued to grow after fiscal year end. A special session of the Legislature in late 2011 made some cuts to state operations, but not enough to fill the budget shortfall. The Legislature's 2012 session begins January 9.

Tax revenues

Tax revenues increased $1.2 billion or 8 percent in fiscal year 2011 from fiscal year 2010. Moderate increases in sales and business and occupation tax revenues were due to a slight increase in taxable sales largely due to an increase in the business and occupation tax rate on services and a tax penalty amnesty program first proposed by our Office.

Debt burden

At the end of fiscal year 2011, the state had general obligation debt outstanding of $16.8 billion, an increase of 1 percent over fiscal year 2010.

The state has pledged its full faith, credit and taxing power to repay this debt. The Constitution of the State of Washington limits the amount of state debt that may be incurred by restricting the amount of general state revenues that may be allocated to pay principal and interest on the debt. The state has not exceeded its constitutional debt limit, but is approaching it. At June 30, 2011 the State Treasurer estimated it could support an additional general obligation bond issue of $1,424,677,986 before reaching the limit. This borrowing capacity has decreased over the past three years because the state is borrowing more money each year and the limit is tied to state revenues, which have not been growing as fast as the rate of borrowing.

Estimated Available Debt Capacity		
June 30, 2009	June 30, 2010	June 30, 2011
$3,069,991,031	$2,385,147,761	$1,424,677,986

The State Treasurer's report on the *Certification of the Debt Limitation of the State of Washington Fiscal Year 2011* can be found at **http://www.tre.wa.gov/documents/debt_cdl2011.pdf**

The state's total debt per capita at June 30, 2011 is $2,879. The ratio of total debt to personal income is 6.79 percent. Standard and Poor's has described the state's tax-supported debt burden as moderately high.

Bond ratings

On June 30, 2011, the state's general obligation debt was rated Aa1 by Moody's Investor Services, AA+ by Standard & Poor's Rating Group and AA+ by Fitch Ratings. Bond ratings are an important measure of the state's economic strength and accountability. They determine how much the state pays in interest when it borrows money.

Workers' Compensation

Workers' compensation activities reported a gain of $1.8 billion in fiscal year 2011 versus a loss of $1 billion in fiscal year 2010. Premium revenues increased $257 million largely due to rate increases effective in January 2011. Claims expenses decreased $3 billion mainly due to the effect of workers' compensation reform legislation and the expectation of lower future claims costs. The reforms created a structured settlement option, a statewide medical provider network, expanded the Centers of Occupation Health and Education, temporarily froze cost-of-living increases and made other changes designed to reduce the system's overall costs.

The Workers' Compensation Program claims and claims adjustment liabilities were $23 billion as of June 30, 2011. Only $11.3 billion is funded by long-term investments leaving an unfunded liability of $11.7 billion for supplemental pension cost-of-living increases (COLAs). These COLAs are provided to injured workers and their dependents who receive disability payments. The state cannot save money in a fund to pay for these costs as state law requires this program to be operated on a pay-as-you-go basis. This will put pressure on the Department to raise employer and employee premium rates or to revamp benefits.

An independent actuary hired by the State Auditor's Office reviewed the Workers' Compensation Fund and had the following assessments and opinions:

- The reported loss and loss adjustment expense reserves are reasonable.
- Contingency reserves increased during the fiscal year ended June 30, 2011 largely as a result of workers' compensation reforms enacted in 2011. However, the contingency reserves remain at historically low levels and below the Department's target. The contingency reserve is the difference between a fund's total assets and its total liabilities.
- Considering the 2012 premium rate changes, and assuming the Department will continue raising rates in 2013 and beyond consistent with long-term averages, it is unlikely the contingency reserve will remain above zero (or remain solvent, as explained in the State Auditor's Office Workers Compensation Report for Fiscal Year ending 2011 **http://www.sao.wa.gov/auditreports/auditreportfiles/ar1006968.pdf**) in the combined accident and medical aid funds over the long-term.
- The 2012 premium rate increase for the Accident Fund is more than needed to allow the fund to break even during calendar year 2012. The 2012 rate increase for the Medical Aid Fund is less than needed to allow the fund to break even during calendar year 2012. However on a combined basis the rate changes are within a reasonable range to allow the funds to break even in 2012.

Unemployment Compensation

Unemployment compensation activity reported operating income of $171 million in fiscal year 2011 versus a loss of $985 million in fiscal year 2010. Un-

employment premium revenues collected from employers rose approximately $300 million and benefits paid decreased about $1 billion from the prior fiscal year. This billion dollar reduction in benefits reflects a decrease in the number and duration of claims, the end of a federal supplemental payment and some claimants exhausted benefits.

The Unemployment Trust Fund has a cash balance of $2.554 billion at June 30, 2011. According to Standard & Poor's, most states do not have a positive balance in their unemployment fund and Washington state has sufficient cash to fund benefits for 15 months.

Budget Stabilization Account

The state's Budget Stabilization Account (rainy day fund) had a balance of $564,000 as of June 30, 2011. On November 8, 2011, voters approved a constitutional amendment to require the transfer of additional funds to the budget stabilization account if the state experiences "extraordinary revenue growth."

The table below shows the decline in the Budget Stabilization Account in recent years.

Budget Stabilization Account (rainy day fund) balance at fiscal year end (in millions)				
2011	**2010**	**2009**	**2008**	**2007**
$ .564	$95	$21.40	$302.70	$226.90

State pension plans

Two of the state's closed pension plans, PERS 1 for retired state employees and TRS 1 for retired teachers, have significant unfunded liabilities. That means the state does not have money set aside to pay the promised retirement benefits to retirees in those two systems. This situation was caused by continuous underfunding and recent investment losses.

As of June 30, 2010, the unfunded liability for PERS 1 was $3.2 billion and TRS 1 was $1.4 billion. The liabilities decreased by $963 million in PERS 1 and $1.264 billion in TRS 1 from the prior year primarily due to a 2011 legislative change that eliminated the automatic annual benefit increase for PERS 1 and TRS 1 retirees and beneficiaries.

The state is the defendant in lawsuits related to the elimination of automatic annual benefit increases and gain sharing. If these benefits were restored, the State Actuary estimates the 2010 funded status of PERS 1 would fall from 74 percent to 63 percent and the funded status of TRS 1 would fall from 84 percent to 70 percent.

Regardless, increases in future contributions will be needed to maintain sufficient assets to pay these benefits in the future. The remaining state retirement plans are fully funded and healthy.

Post-employment benefits

The state administers a post-employment benefit plan of subsidized medical, dental, life and long-term disability insurance to employees who elect to continue coverage and pay the administratively established premiums at the time they retire. The plan had an unfunded liability of $3.5 billion as of January 1, 2011.

Risk Management Fund

The Risk Management Fund has $96 million in cash and investments to pay for future estimated claims of approximately $703 million as of June 30, 2011. This fund pays tort claims, judgments, and settlements against the state. State law limits accumulating funds in the Self-Insurance Liability Program to 50 percent of total outstanding and actuarially determined claims.

Tort payouts and defense costs for the last five fiscal years (expressed in millions)					
	2011	**2010**	**2009**	**2008**	**2007**
Tort payouts	$74	$47	$53	$45	$36
Defense costs	$37	$28	$19	$20	$17
Total	$111	$75	$72	$65	$53

American Recovery and Reinvestment Act

Washington has used federal grant money from the American Recovery and Reinvestment Act to avoid making significant service and workforce cuts, to modernize the state's infrastructure, to enhance energy independence, to support educational system needs, to increase access to health care and to provide tax relief. For the fiscal year ended June 30, 2011, the federal government had granted more than $1.6 billion in Recovery Act money to the state. As a condition to accepting this grant money, the state has agreed to maintain certain programs even after federal funding for the program has ended. Most Recovery Act funding ended during the fiscal year, however Washington will receive additional money in the future for projects previously obligated.

Guaranteed Education Tuition (GET) Program

The GET program, administered by the Higher Education Coordinating Board, was established in 1998 to make higher education more affordable and accessible. An independent actuarial valuation of the program disclosed that program assets fell short of the present value of obligations for future payments by $570 million, or 21 percent of total obligations, at June 30, 2011. However, the State Actuary completed a solvency analysis of the program earlier in 2011 to review the risk and the potential amount of a future state contribution. As part of that analysis, it produced a solvency report card using various funding models and concluded the risk of state contributions is low. The full report can be found at **http://osa.leg.wa.gov/Actuarial_Services/Publications/PDF_Docs/Pension_Studies/11GETSolvAn.pdf**

GET Program obligations, assets and reserves/deficits for the last five fiscal years (in millions)				
Fiscal year ended June 30	Present value of obligations for future payments	Program assets	Reserve/(deficit)	Reserve/(deficit) as a percentage of total obligations
2011	$2,730.70	$2,160.60	$(570.10)	(21%)
2010	$1,853.40	$1,597.70	$(255.70)	(14%)
2009	$1,492.10	$1,256.40	$(235.70)	(16%)
2008	$1,104	$1,208.50	$104.50	10%
2007	$930.40	$1,091.80	$161.40	18%

Trends and ratios

Key financial ratios point to a decline in the state's financial condition.

The continuing services ratio focuses on the government's ability to provide ongoing general services with unrestricted net assets. As shown in the chart below, this ratio significantly declined from 2007 through 2010, it improved slightly in 2011.

The debt to asset ratio focuses on government services and structures that are financed through borrowing and other long-term obligations. As shown in the chart below, the state increased the amount of debt used to finance its assets from 2007 to 2011.

Continuing Service Ratio percentage of expenses in millions			
Fiscal year ended June 30	Unrestricted Net Assets (deficit)	Expenses	Ratio
2011	$1,160	$34,144	3.40%
2010	$(217)	$34,108	-.64%
2009	$1,417	$33,561	4.22%
2008	$3,544	$30,543	11.60%
2007	$4,269	$28,048	15.22%

Debt to Asset Ratio in millions			
Fiscal year ended June 30	Total liabilities	Total assets	Ratio
2011	$25,440	$50,170	50.708%
2010	$24,964	$48,162	51.833%
2009	$21,314	$45,169	47.187%
2008	$21,215	$47,312	44.841%
2007	$18,299	$43,829	41.751%

Visit the Office of Financial Management website to view the full [Comprehensive Annual Financial Report].

State law requires the Auditor's Office to publish an annual report by December 31 of each year. This report fulfills that requirement. The law also requires that we report on any appeals to bills for audits of local governments. We did not receive any appeals in 2011.

Contact information

Headquarters
(360) 902-0370

Website
www.sao.wa.gov

Twitter tag
@WAStateAuditor

State Auditor Brian Sonntag, CGFM

(360) 902-0361

Brian.Sonntag@sao.wa.gov

Chuck Pfeil, CPA
Director of State and Local Audit
(360) 902-0366
Chuck.Pfeil@sao.wa.gov

Mindy Chambers
Director of Communications
(360) 902-0091
Mindy.Chambers@sao.wa.gov

To request public records from the State Auditor's Office:

Mary Leider
Public Records Officer
(360) 725-5617
PublicRecords@sao.wa.gov

Americans with Disabilities

In accordance with the Americans with Disabilities Act, this document will be made available in alternate formats. Please call (360) 902-0370 for more information.