WEST VIRGINIA DEPARTMENT OF TRANSPORTATION
DIVISION OF HIGHWAYS
A Component Unit of the State of West Virginia and
West Virginia Department of Transportation

Audited Financial Statements with Additional Information
For the Year Ended June 30, 2012
And Independent Accountants' Report

Perry & Associates
Certified Public Accountants, A.C

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Perry & Associates

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INDEPENDENT ACCOUNTANTS' REPORT

November 10, 2012

Joint Committee on Government and Finance
West Virginia Legislature

We have audited the accompanying financial statements of the governmental activities and each major fund of the **West Virginia Department of Transportation, Division of Highways** (the Division), a component unit of the State of West Virginia and the West Virginia Department of Transportation, as of and for the year ended June 30, 2012, which collectively comprise the Division's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Division's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities and each major fund of the West Virginia Department of Transportation, Division of Highways as of June 30, 2012, and the respective changes in financial position thereof and the budgetary comparison for the State Road (General) Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 10, 2012, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require this presentation to include *Management's discussion and analysis* to supplement the basic financial statements. Although this information is not part of the basic financial statements, the Governmental Accounting Standards Board considers it essential for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any other assurance.

Respectfully submitted,

Perry & Associates CPA's A.C.

Perry and Associates
Certified Public Accountants, A.C.

MANAGEMENT’S DISCUSSION AND ANALYSIS

This section of the West Virginia Department of Transportation, Division of Highways (Division) annual financial report presents our discussion and analysis of the Division's financial performance during the fiscal year that ended June 30, 2012. This section introduces the basic financial statements and provides an analytical overview of the Division's financial activities. Please read it in conjunction with the Division's financial statements, which immediately follow this section.

FINANCIAL HIGHLIGHTS - PRIMARY GOVERNMENT

Net Assets - The Division's total combined net assets are $7.70 billion as of the close of fiscal year 2012.

Changes in Net Assets - During the year the Divisions' net assets decreased $49 million or .63%. This percentage is a decrease from the prior year, when net assets increased $226 million or 3.00%.

Revenues and Expenses - Total revenues decreased by $478 thousand or .04% Total expenses increased $274 million or 26.51%. There were no significant changes in the programs carried out by the Division during the year.

Governmental Funds - Fund Balances - As of the close of fiscal year 2012, the Division's governmental funds reported combined total fund equity of $40 million, a decrease of $104 million in comparison with the prior year.

Long-term Debt - The Division's total outstanding general obligation bonds, net of bond premiums, decreased by $35 million during the current fiscal year. The Division's total outstanding special obligation notes, net of note premium, decreased by $22 million decreasing total long term debt by 13.38% during the current fiscal year.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The discussion and analysis serves as an introduction to the Division's basic financial statements. The Division's basic financial statements are comprised of three components, government-wide financial statements, fund financial statements, and notes to the financial statements.

Government-wide Statements

Government-wide financial statements provide both long-term and short-term information about the Division's financial condition. Changes in the Division's financial position may be measured over time by increases and decreases in the Statement of Net Assets. Information on how the Division's net assets changed during the fiscal year is presented in the Statement of Activities.

Fund Financial Statements

The fund financial statements focus on the individual parts of the Division, reporting the Division's operations in more detail than the government-wide financial statements. Fund financial statements can include the statements for governmental, proprietary, and fiduciary funds. The Division has only governmental funds.

Notes to the Financial Statements

Notes to the financial statements provide additional information that is essential to the full understanding of the data provided in the government-wide and fund financial statements.

CONDENSED FINANCIAL INFORMATION

Condensed Statement of Net Assets

The following condensed financial information was derived from the government-wide statement of net assets and summarizes the Division's net assets as of June 30, 2012 and 2011 (amounts in thousands).

The largest component of the Division's net assets reflects its investment in capital assets (e.g. land, buildings, equipment, infrastructure and others) less any related debt outstanding (excluding debt proceeds that have yet to be expended for infrastructure construction) that was needed to acquire or construct the assets. The Division uses these capital assets to provide services to the citizens and businesses in the State; consequently, these net assets are not available for future spending. The remaining portion is classified as either restricted or unrestricted net assets. The unrestricted net assets may be used at the Division's discretion. The restricted net assets have constraints as to how these funds may be used. Enabling legislation directs the use of these funds.

Net Assets as of June 30

	2012	2011	% Change
Total current assets	$ 271,231	$ 311,710	-12.99%
Capital assets, net of accumulated depreciation	8,109,900	8,111,197	-0.02%
Other non-current assets	2,050	2,331	-12.05%
Total assets	8,383,181	8,425,238	-0.50%
Total current liabilities	300,105	245,763	22.11%
Long term liabilities	378,118	425,875	-11.21%
Total liabilities	678,223	671,638	0.98%
Invested in capital assets, net of related debt	7,712,955	7,654,175	0.77%
Restricted	17,350	14,584	18.97%
Unrestricted	(25,347)	84,841	-129.88%
Total net assets	$ 7,704,958	$ 7,753,600	-0.63%

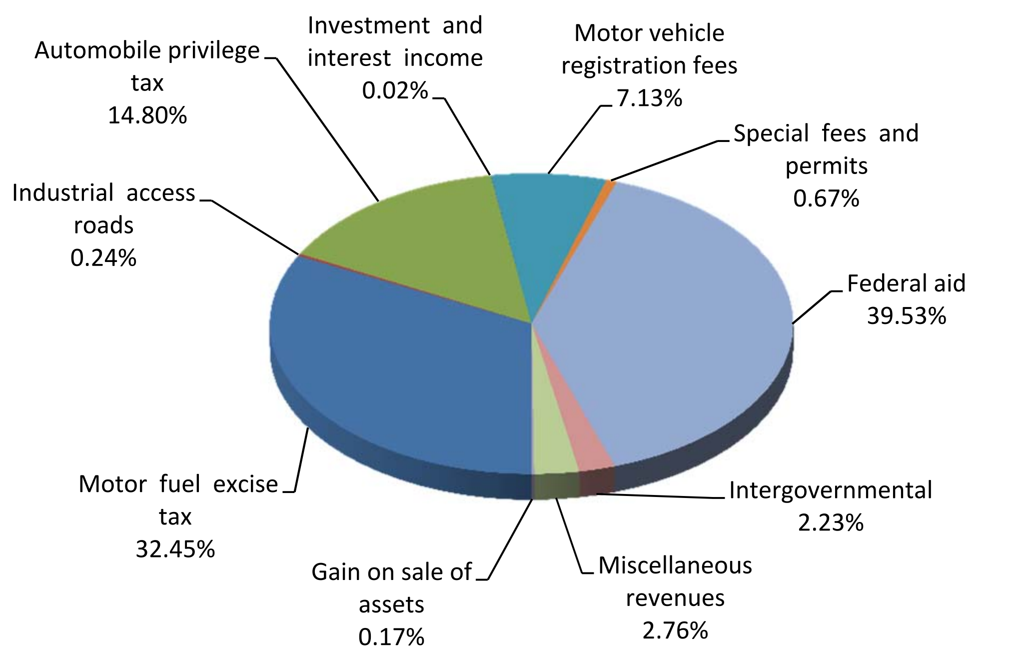
Condensed Statement of Activities

The following condensed financial information was derived from the government-wide statement of activities and reflects how the Division's net assets changed during the fiscal year (amounts in thousands):

	2012	2011	% Change
Revenues			
Taxes	$ 594,871	$ 574,949	3.47%
Investment and interest income	209	517	-59.57%
Intergovernmental	28,078	14,171	98.14%
Miscellaneous revenues	34,695	31,945	8.61%
Gain on sale of assets	2,149	1,673	28.45%
Total general revenues	660,002	623,255	5.90%
Capital grants and contributions	500,814	537,602	-6.84%
Charges for services	98,121	98,558	-0.44%
Total program revenues	598,935	636,160	-5.85%
Total revenues	1,258,937	1,259,415	-0.04%
Expenses			
Road maintenance	491,044	433,905	13.17%
Other road operations	672,251	448,650	49.84%
General and administration	123,397	126,704	-2.61%
Interest on long-term debt	17,136	20,041	-14.50%
Unallocated depreciation	3,751	4,275	-12.26%
Total expenses	1,307,579	1,033,575	26.51%
Change in net assets	(48,642)	225,840	-121.54%
Net assets, beginning	7,753,600	7,527,760	3.00%
Net assets, ending	$ 7,704,958	$ 7,753,600	-0.63%

Over time, increases and decreases in net assets measure whether the Division's financial position is improving or deteriorating. During the fiscal year, the net assets of the governmental activities decreased by $49 million or .63% percent.

The following chart depicts the revenues of the Division for the fiscal year.



Total revenues decreased by approximately $478 thousand. Total tax revenues increased by approximately $20 million. Federal aid revenue decreased by approximately $37 million or 6.88%. The following summarizes revenues for the years ended June 30, 2012 and June 30, 2011 (amounts in thousands):

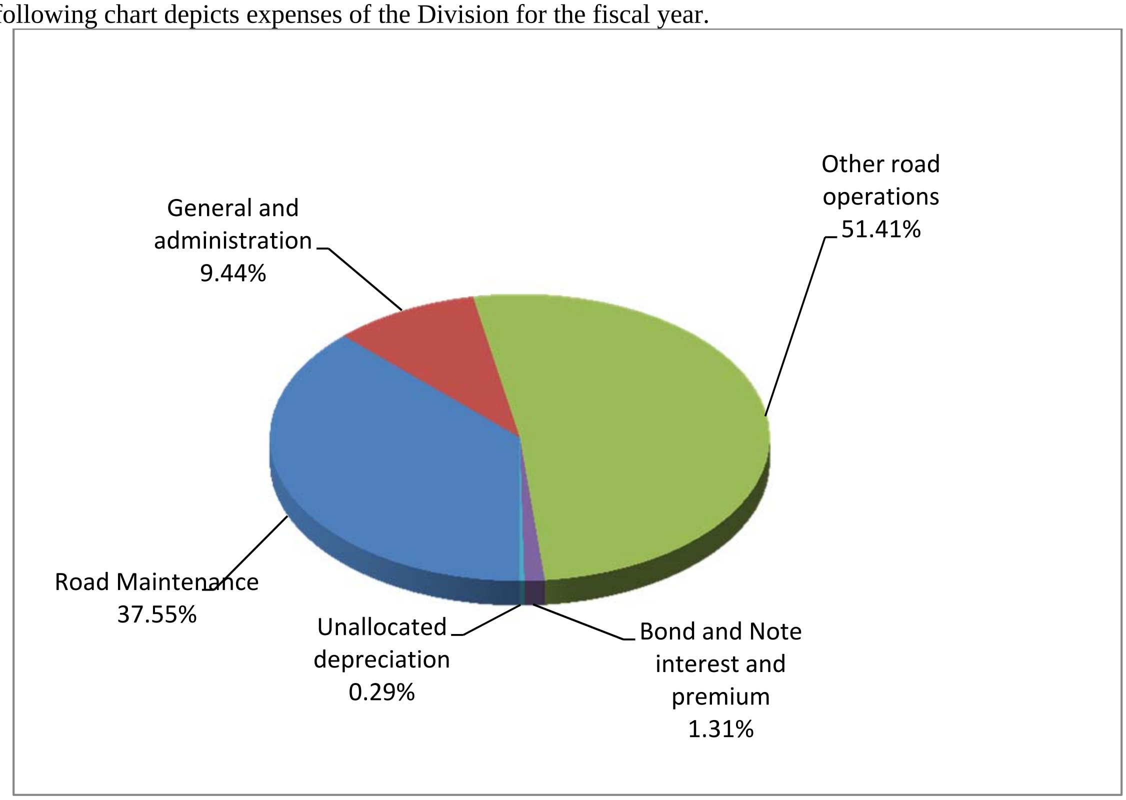
	2012	2011	Increase (Decrease)	% Increase (Decrease)
Motor fuel excise tax	$ 408,571	$ 406,347	$ 2,224	0.55%
Industrial access roads	3,000	3,000	-	0.00%
Automobile privilege tax	186,300	168,602	17,698	10.50%
Motor vehicle registration fees	89,741	91,475	(1,734)	-1.90%
Special fees and permits	8,380	7,083	1,297	18.31%
Federal aid	497,814	534,602	(36,788)	-6.88%
Investment and interest income	209	517	(308)	-59.57%
Intergovernmental	28,078	14,171	13,907	98.14%
Miscellaneous revenues	34,695	31,945	2,750	8.61%
Gain on sale of assets	2,149	1,673	476	28.45%
	$ 1,258,937	$ 1,259,415	$ (478)	-0.04%

The Division's primary sources of revenue for funding of ongoing administration of the Division, general maintenance and construction of the state road system and for providing resources to match available Federal funds are derived from fuel taxes, automobile privilege taxes, motor vehicle registration and license fees, net of costs incurred by the Division of Motor Vehicles in collecting funds for deposit into the State Road Fund.

FY 2012 tax collections reported on a cash basis grew by $2.3 million (0.35%) over FY 2011 tax collections. Motor fuel tax collections were $6.3 million (1.67%) above estimates and $10.7 million (2.69%) higher than FY 2011 collections. Privilege tax collections were $35.1 million (23.28%) above estimates and $13.8 million (8.03%) above FY 2011 collections. Registration fee collections were $1.7 million (1.90%) above estimates and $512 thousand (0.56%) below FY 2011 collections. In FY 2013, motor fuel tax, privilege tax collections and registration fee collections are all projected to be stagnant. As a result, many programs that are operated by the Division will experience little, if any, real growth in the foreseeable future, and it is possible that some programs will be reduced.

The Division also relies on federal funds as a source of revenue. The federal aid is obtained in the form of reimbursable grants. Federal transportation legislation and special spending authorizations provide funds that are available for obligation by the Federal Government in specific years, and the Division expects to continue to fully obligate available funds, thus ensuring that it captures all federal dollars. Revenue under these grants is recognized when expenditures occur on specific projects that have qualified for federal participation. Federal funds received during 2012 were authorized under the Highway Transit Bill, the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) and the American Recovery and Reinvestment Act of 2009.

The following chart depicts expenses of the Division for the fiscal year.



Total expenses increased by approximately $274 million or 26.51%. The following summarizes expenditures for the years ended June 30, 2012 and June 30, 2011 (amounts in thousands):

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Road maintenance	$ 491,044	$ 433,905	$ 57,139	13.17%
Other road operations	672,251	448,650	223,601	49.84%
General and administration	123,397	126,704	(3,307)	-2.61%
Interest on long-term debt	17,136	20,041	(2,905)	-14.50%
Unallocated depreciation	3,751	4,275	(524)	-12.26%
	$ 1,307,579	$ 1,033,575	$ 274,004	26.51%

The maintenance expenses of the Division are comprised primarily of routine maintenance, small bridge repair, and contract paving.

Operating units are allocated yearly amounts for routine maintenance. The type of routine maintenance expenses incurred is dependent, to a degree, on the level of snow removal and ice control (SRIC) that is required in a given year. In FY 2012, the agency continued its core maintenance plan, which emphasizes ditching, mowing, brush-cutting, and patching maintenance activities. County crews concentrate on these activities during all non-SRIC periods. The intent is to improve safety and perform maintenance that will extend the life of the highway system.

Other road operations expenditures reported in the Government-Wide Financial Statements include the total expended for all other road operations and small construction activities that fail to meet the criteria established for capitalization as infrastructure assets. A discussion of the change in actual funds expended is included in the financial analysis of the Division's Fund Financial Statements below.

FINANCIAL ANALYSIS OF THE DIVISION'S MAJOR FUND

At June 30, 2012, the Division reported fund balances of approximately $40 million. Of this total amount ($23) million constitutes unassigned fund balance while $17 million is restricted for various purposes. The remainder of fund balance is nonspendable and is not available for spending because it is comprised of inventories.

State Road Fund

The State Road Fund is the Division's General Fund. At the end of the 2012 fiscal year, unassigned fund balance of the General Fund was ($23) million and nonspendable fund balance was $46 million while the restricted fund balance was $17 million. The total General Fund balance decreased $104 million during the fiscal year primarily due to increased expenditures for road construction, maintenance and rehabilitation projects.

State Road (General) Fund and Budgetary Highlights

The Division is dependent on revenues generated from the purchase and use of motor fuel, motor vehicle fees, privilege tax on consumer purchases of motor vehicles, and federal funding generated from motor fuel purchases. Revenues are affected by state and national economic conditions, world events affecting availability and pricing of motor fuel, and fuel consumption rates for motor vehicles. As fuel consumption is forecast to decrease each year through FY 2018, it is expected to have a significant impact on revenue collections unless there is a corresponding change to the tax rates or structure. Neither Privilege tax collections nor registration fee collections are forecast to increase significantly through FY 2018. The following table summarizes tax and fee collections over the past two years (amounts in thousands):

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Motor fuel excise and wholesale fuel	$ 408,571	$ 406,347	$ 2,224	0.55%
Motor vehicle registration	89,741	91,475	(1,734)	-1.90%
Privilege tax	186,300	168,602	17,698	10.50%
	$ 684,612	$ 666,424	$ 18,188	2.73%

The gasoline and special fuels excise tax was repealed by HB 218 passed during the 2008 Second Legislative Special Session, and the motor fuel excise tax was imposed on motor fuel. The motor fuel excise tax is the combination of a flat 20.5 cents per invoiced gallon rate and a variable sales and use tax rate that is calculated yearly. The variable rate changed on January 1, 2012, when the rate rose from 11.7 cents to 12.9 cents per invoiced gallon.

The Division's federal revenue, on a cash (budgetary) basis for fiscal year 2012 was $449.0 million, used primarily for design, right-of-way and construction of Corridor H, WV 9, US Route 35 and other major corridors including King Coal Highway, WV 10 and all other federal highways. As previously discussed the recognition of revenue under these grants occurs when expenditures occur on specific projects that have qualified for federal participation. The budgeted amounts for federal revenue and expenditures are based on projects that have been approved and estimates of the timing of each phase of the project. Since the timing of such expenditures are dependent on variables such as the weather, the existence of differing site conditions that require plan modification, or delays caused by environmental issues or the results of public meetings, expenditures often do not occur as planned. Federal revenue recognized in the Statement of Activities in each of the last two years is summarized below (amounts in thousands):

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Federal reimbursement-Budgeted funds	$ 467,532	$ 497,783	$ (30,251)	-6.08%
Federal reimbursement-Surface Transportation	27,591	27,577	14	0.05%
Federal reimbursement-Emergency funds	2,691	9,242	(6,551)	-70.88%
	$ 497,814	$ 534,602	$ (36,788)	-6.88%

It is anticipated that state revenues will basically remain unchanged in FY 2013. The Division's revenues are not projected to keep pace with increases in operating costs, and Management has taken steps to maintain a fiscally sound fund equity balance. The approved FY 2013 budget, exclusive of ARRA projects, which are 100% federally-reimbursed is $1.16 billion. If revenues are significantly less than estimated, Management is confident that adequate discretionary expenditure items can be reduced to permit the Division to continue to operate in a fiscally sound manner.

After ten extensions of SAFETEA-LU, a new twenty-seven month federal highway funding authorization has been enacted and designated as Moving Ahead for Progress in the 21st Century Act (MAP-21). MAP-21 provides a simple extension of the current SAFETEA-LU programs and all related provisions through the end of FFY 2012. The effective date for most highway provisions in MAP-21, both funding and changes to policy, is October 1, 2012. West Virginia's FFY 2013 apportionment will be $423.3 million, and its FFY 2014 apportionment will be $426.9 million.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of June 30, 2012 the Division had invested $8.1 billion, net of accumulated depreciation, in a range of capital assets (see note 7 for additional details). Depreciation charges for the fiscal year totaled $314 million.

As the Division continues to expand the state road system, these expansions are focused primarily on upgrading existing roadways and completion of Appalachian Highway Corridors. While these are significant construction projects, the additions are offset by $291 million in depreciation of the infrastructure. The Division expended $313 million dollars during the year ended June 30, 2012 for additions to capital assets. Of this amount, $282 million was related to the acquisition of right of way and construction of roads and bridges. Construction costs for completed projects in the amount of $427 million were reclassified from construction in process to roads and bridges. Major construction expenditures during the year included continued construction related to Corridor H in Hardy and Grant Counties, completion of the Mon/Fayette Expressway in July 2011, widening of I-79 in Harrison County, upgrade of WV Route 9 in the Eastern Panhandle, upgrade of US Route 52 in Mercer County, Coalfields Expressway in Raleigh County, Fairmont Connector, upgrade of existing 2-lane sections of US Route 35 in Putnam and Mason Counties and continued environmental studies on various projects in process.

Long-term Debt

The Division has been authorized to issue bonds by constitutional amendments and all bonds are general obligation bonds of the State of West Virginia. All bonds authorized under prior constitutional amendments have been issued. At June 30, 2012, the Division had $271 million in outstanding bonds. The amount outstanding decreased by $35 million (11.41%) due to net principal payments.

The Division has also been authorized to issue revenue notes in the amount of $200 million by constitutional amendment. The Division issued revenue notes in the amount of $76 million in October 2006, $33 million in April 2007, and $77 million during fiscal year 2010. These notes are revenue notes and the debt service payments will be funded through federal aid revenue. At June 30, 2012, the Division had $100 million in outstanding revenue notes. The amount decreased by $22 million (18.26%) due to net principal payments.

The following is a summary of the amounts outstanding, including insured status and bond and note ratings:

Issue	Status of insurance	Bond Rating		Amount (in thousands)	
Safe Roads 01A - All Bonds maturing between June 1, 2007 to 2013	Insured by FGIC	Fitch: Moody's: S&P:	AA+ Aa1 AA	$	1,565
Safe Roads 05A - Bonds maturing on or before June 1, 2025	Insured by FSA	Fitch: Moody's: S&P:	AA+ Aa1 AA		233,895
Safe Roads 10A - Bonds maturing on or before June 1, 2023.	Insured by FSA	Fitch: Moody's: S&P:	AA+ Aa1 AA		35,135
Surface Transportation Improvements Special Obligation Notes (GARVEE 2006A) – Notes maturing on or before June 1, 2016	Not Insured - notes maturing Sept. 1, 2008 Insured by FSA – notes maturing after Sept. 1, 2008	Moody's: S&P:	Aa2 AA		37,545
Surface Transportation Improvements Special Obligation Notes (GARVEE 2007A) – Notes Maturing on or before June 1, 2016	Not Insured - notes maturing Sept. 1, 2008 Insured by FSA – notes maturing after Sept. 1, 2008	Moody's: S&P:	Aa2 AA		16,270
Surface Transportation Improvements Special Obligation Notes (GARVEE 2009A) – Notes Maturing on or before June 1, 2016	Insured by FSA	Moody's: S&P:	Aa2 AA		46,555
				$	370,965

More detailed information regarding capital asset and long-term debt activity is included in the notes 7 and 9, respectively to the financial statements.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the finances of the Division for those with an interest in this organization. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the West Virginia Department of Transportation, Division of Highways at 1900 Kanawha Boulevard, East, Building 5, Room 220, Charleston, West Virginia 25305.

BASIC FINANCIAL STATEMENTS

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
STATEMENT OF NET ASSETS
JUNE 30, 2012
(amounts expressed in thousands)

	Governmental Activities
ASSETS	
Current assets	
Cash and cash equivalents	$ 63,450
Accounts receivable, net	84,676
Taxes receivable	74,865
Due from other State of West Virginia agencies	2,475
Inventories	45,765
Total current assets	271,231
Non-current assets	
Capital assets not being depreciated	
Land - non-infrastructure	23,025
Land - infrastructure	986,302
Construction in progress	795,373
Capital assets net of accumulated depreciation	
Land improvements	7,643
Buildings	87,339
Furniture and fixtures	996
Rolling stock	70,078
Scientific equipment	386
Shop equipment	40
Roads	3,957,162
Bridges	2,181,556
Total capital assets	8,109,900
Other non-current assets	2,050
Total assets	8,383,181
LIABILITIES	
Current liabilities	
Accounts payable	85,082
Retainages payable	4,009
Accrued payroll and related liabilities	20,450
Deferred Revenue	248
Other Post Employment Benefits Liability	118,159
Due to other State of West Virginia agencies	3,692
Accrued interest payable	2,673
Current maturities of long term obligations	65,792
Total current liabilities	300,105
Non-current liabilities	
Claims and judgements	16,100
Compensated absences	16,418
Bonds and notes	345,600
Total non-current liabilities	378,118
Total liabilities	678,223
NET ASSETS	
Invested in capital assets, net of related debt	7,712,955
Restricted	
Coal Resource	4,739
Waste Tire	2,371
Industrial Access	10,240
Unrestricted	(25,347)
Total net assets	$ 7,704,958

The Accompanying Notes Are An Integral Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2012

(amounts expressed in thousands)

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Capital Grants and Contributions	Net Revenue (Expenses) and Changes in Net Assets
Government activities				
Road maintenance				
Expressway, trunkline & feeder & SLS	$ 380,283	$ -	$ -	$ (380,283)
Contract paving & secondary roads	66,721	-	-	(66,721)
Small bridge repair & replacement	22,794	-	-	(22,794)
Litter control program	1,682	-	-	(1,682)
Depreciation	19,564	-	-	(19,564)
Other road operations				
Interstate highways	105,899	-	109,422	3,523
Appalachian highways	51,584	-	82,989	31,405
Other federal aid programs	212,896	-	305,403	92,507
Non federal aid improvements	9,561	-	-	(9,561)
Industrial access roads	1,583	-	3,000	1,417
Depreciation	290,728	-	-	(290,728)
General and administration				
Support and administrative operations	81,441	8,380	-	(73,061)
Claims	6,540	-	-	(6,540)
Costs associated with DMV	33,838	89,741	-	55,903
Costs associated with OAH	1,578	-	-	(1,578)
Interest on long-term debt	17,136	-	-	(17,136)
Unallocated depreciation	3,751	-	-	(3,751)
	$ 1,307,579	$ 98,121	$ 500,814	(708,644)

General revenues	
Taxes:	
Gasoline and motor carrier	408,571
Automobile privilege	186,300
Investment and interest income	209
Intergovernmental	28,078
Miscellaneous revenues	34,695
Gain on Sale of Assets	2,149
Total general revenues	660,002
Change in net assets	(48,642)
Net assets, beginning	7,753,600
Net assets, ending	$ 7,704,958

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
BALANCE SHEET - GOVERNMENTAL FUND
JUNE 30, 2012
(amounts expressed in thousands)

	State Road (General)
ASSETS	
Assets	
Cash and cash equivalents	$ 63,450
Receivables	84,676
Taxes receivable	74,865
Due from other State of West Virginia agencies	2,475
Inventories	45,765
Total assets	$ 271,231
LIABILITIES AND FUND BALANCES	
Liabilities	
Accounts payable	$ 85,082
Retainages payable	4,009
Accrued payroll and related liabilities	20,450
Deferred Revenue	248
Other post employment benefits	118,159
Due to other State of West Virginia agencies	3,692
Total liabilities	231,640
Fund balances	
Nonspendable	
Inventories	45,765
Restricted	
Construction and maintenance of industrial access roads	10,240
Construction and maintenance of coal resource roads	4,739
Waste tire clean up and disposal	2,371
Unassigned	(23,524)
Total fund balances	39,591
Total liabilities and fund balances	$ 271,231

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUND TO THE STATEMENT OF NET ASSETS
JUNE 30, 2012

(amounts expressed in thousands)

Total fund balance - governmental fund		$	39,591
Amounts reported for governmental activities in the statement of net assets are different because:			
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:			
Capital assets not being depreciated			
Land - non-infrastructure	$ 23,025		
Land - infrastructure	986,302		
Construction in progress	795,373		
Capital assets net of accumulated depreciation			
Land improvements	7,643		
Buildings	87,339		
Furniture and fixtures	996		
Rolling stock	70,078		
Scientific equipment	386		
Shop equipment	40		
Roads	3,957,162		
Bridges	2,181,556		8,109,900
Bonds issued by the Division have associated costs that are paid from current available financial resources in the funds. However, these costs are deferred on the statement of net assets.			2,050
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:			
Accrued interest payable	(2,673)		
Claims and judgments	(18,194)		
Compensated absences	(28,771)		
General obligation bonds and revenue notes	(396,945)		(446,583)
Net assets of governmental activities		$	7,704,958

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE - GOVERNMENTAL FUND
YEAR ENDED JUNE 30, 2012
(amounts expressed in thousands)

	State Road (General)
Revenues	
Taxes	
Gasoline and motor carrier	$ 408,571
Automobile privilege	186,300
Industrial access roads	3,000
License, fees and permits	
Motor vehicle registrations and licenses	89,741
Special fees and permits	8,380
Federal aid	
Interstate highways	109,422
Appalachian highways	82,989
Other federal aid programs	305,403
Investment and interest income, net of arbitrage rebate	209
Intergovernmental	28,078
Miscellaneous revenues	34,695
Total revenues	1,256,788
Expenditures	
Current	
Road maintenance	
Expressway, trunkline and feeder, state and local services	380,301
Contract paving and secondary roads	66,721
Small bridge repair and replacement	39,731
Litter control program	1,682
Support and administrative operations	112,652
Division of Motor Vehicles operations	33,838
Office of Administration Hearings operations	1,578
Claims	2,327
Capital outlay and other road operations	
Road construction and other road operations	
Interstate highways	129,221
Appalachian highways	108,798
Other federal aid programs	387,429
Nonfederal aid construction and road operations	19,908
Industrial access roads	1,583
Debt service	
Debt Service Fees	3
Principal	57,290
Interest	20,078
Total expenditures	1,363,140
Excess (deficiency) of revenues over expenditures	(106,352)
Other financing sources (uses)	
Proceeds of sale of assets	2,446
Net change in fund balances	(103,906)
Fund balances, beginning of year	143,497
Fund balances, end of year	$ 39,591

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION
DIVISION OF HIGHWAYS
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - GOVERNMENTAL FUND TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2012
(amounts expressed in thousands)

Net change in fund balance - governmental fund	$	(103,906)
Amounts reported for governmental activities in the statement of activities are different because:		
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation of ($314,043) exceeded capital outlays $313,043 in the current period.		(1,000)
In the statement of activities only the loss on the sale of assets is reported, whereas in the governmental funds, the proceeds from the sale increase financial resources. Thus the change in the net assets differs from the change in fund balance by the undepreciated cost of the assets sold.		(296)
Repayment of bond and note principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of assets.		57,290
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount by which the increase in claims of ($4,214) and the amortization of bond issue cost of ($282), exceed the decrease in interest payable of $438, compensated absences of $541 and the accretion of bond premium of $2,787.		(730)
Change in net assets of governmental activities	$	(48,642)

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION, DIVISION OF HIGHWAYS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
(BUDGETARY BASIS) - STATE ROAD FUND
YEAR ENDED JUNE 30, 2012
(amounts expressed in thousands)

	Original Budget	Budget Amendments	Final Budget	Actual Amounts	Variance with Final Budget - Positive (Negative)
Revenues					
Taxes					
Gasoline and motor carrier	$ 380,700	$ -	$ 380,700	$ 387,041	$ 6,341
Automobile privilege	151,114	-	151,114	186,293	35,179
Motor vehicle registrations and licenses	90,668	-	90,668	92,269	1,601
Revenue Transfer to Industrial Access Roads	(3,000)	-	(3,000)	(3,000)	-
Federal aid	493,400	45,000	538,400	449,092	(89,308)
Miscellaneous revenues	39,110	15,000	54,110	45,784	(8,326)
	1,151,992	60,000	1,211,992	1,157,479	(54,513)
Expenditures					
Road construction and other road operations					
Interstate highways	150,000	10,000	160,000	128,426	31,574
Appalachian highways	115,000	(5,000)	110,000	87,427	22,573
Other federal aid programs	300,700	58,000	358,700	358,640	60
Nonfederal aid construction	15,000	3,000	18,000	17,230	770
Federal economic stimulus	20,000	-	20,000	18,331	1,669
Road maintenance					
Maintenance	326,096	61,000	387,096	382,568	4,528
Contract paving and secondary roads	45,000	15,000	60,000	60,000	-
Small bridge repair and replacement	30,000	8,000	38,000	35,694	2,306
Litter control program	1,680	-	1,680	1,680	-
Support and administrative operations					
General operations	53,849	3,000	56,849	47,661	9,188
Equipment revolving	15,000	2,500	17,500	12,571	4,929
Inventory revolving	4,000	-	4,000	(482)	4,482
Debt service	49,900	-	49,900	49,755	145
Division of Motor Vehicles operations	40,579	-	40,579	33,469	7,110
Office of Administrative Hearings operations	1,952	-	1,952	1,700	252
Claims - DOH and DMV	2,391	-	2,391	2,327	64
	1,171,147	155,500	1,326,647	1,236,997	89,650
Excess (deficiency) of revenues over expenditures	(19,155)	(95,500)	(114,655)	(79,518)	35,137
Fund balance, beginning of year	125,893	-	125,893	125,893	-
Fund balance, end of year	$ 106,738	$ (95,500)	$ 11,238	$ 46,375	$ 35,137

The Accompanying Notes Are An Integral Part Of These Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION - The accompanying financial statements of the West Virginia Department of Transportation, Division of Highways (the "Division") have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

REPORTING ENTITY - The Division is an operating unit of the West Virginia Department of Transportation and represents separate funds of the State of West Virginia (the "State") that are not included in the State's general fund. The Division is a legally separate entity defined by the State constitution, and has statutory responsibility for the construction, reconstruction, maintenance, and improvement of all State roads. The Division is governed by a commissioner who is appointed by the Governor, but does not have a governing board separate from the State Legislature. The Division is considered a component unit of the State and its financial statements are blended with the financial statements of the primary government in the State's comprehensive annual financial report.

The financial statements of the Division are intended to present the financial position, and the results of operations of only that portion of the financial reporting entity of the West Virginia Department of Transportation and the State of West Virginia, that is attributable to the transactions of the Division. They do not purport to, and do not, present fairly the financial position of the West Virginia Department of Transportation or the State of West Virginia as of June 30, 2012 and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management has considered all potential component units to be included in the Division's reporting entity by applying the criteria set forth in accounting principles generally accepted in the United States of America. These criteria include consideration of organizations for which the Division is financially accountable, or organizations for which the nature and significance of their relationship with the Division are such that exclusion would cause the Division's financial statements to be misleading or incomplete. Since no organizations meet these criteria, the Division has no component units.

The Division of Motor Vehicles is an operating division of the West Virginia Department of Transportation, which collects certain revenues for expenditure by the Division. The expenditures related to the collection of these revenues are recorded in the State Road Fund of the Division.

The Public Service Commission collects revenues from coal companies that are operating trucks with excessive weights. These revenues are deposited into the Coal Resource Fund, which is controlled by the Division.

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS - The government-wide financial statements (the statement of net assets and the statement of activities) report information of all of the activities of the primary government and its component units, if any. For the most part, the effect of interfund activity has been removed from these government-wide statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function, segment or component unit are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function, segment, or component unit. Program revenues include charges to customers who purchase, use or directly benefit from goods or services provided by a given function, segment, or component unit. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function, segment, or component unit. Taxes and other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues. The Division does not allocate general government (indirect) expenses to other functions.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. The government-wide statement of net assets reports $17,350 restricted assets, of which all is restricted by enabling legislation.

When both restricted and unrestricted resources are available for use, generally it is the Division’s policy to use restricted resources first, then unrestricted resources, as they are needed. Separate financial statements are provided for governmental funds, proprietary funds, fiduciary funds and similar component units, and major component units, if applicable. However, the fiduciary funds are not included in the government-wide statements. Major individual governmental funds and major individual enterprise funds, if applicable, are reported as separate columns in the fund financial statements.

MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION –

GOVERNMENT-WIDE FINANCIAL STATEMENTS - The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

GOVERNMENTAL FUND FINANCIAL STATEMENTS - The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Division considers revenues to be available if they are collected within 45 days of the end of the current fiscal year. Principal revenues subject to accrual include gasoline and wholesale fuel taxes, automobile privilege taxes, federal reimbursements and other reimbursements for use of materials and services.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting for the governmental fund financial statements include:

- Employees’ vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at June 30, 2012, has been reported only in the government-wide financial statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- Division employees earn sick leave benefits, which accumulate, but do not vest. When separated from employment with the Division, an employee's sick leave benefits are considered ended and no reimbursement is provided. Any employee who retires, however, may convert any unused accumulated sick leave to increase service credits for retirement purposes. Additionally, certain employees may choose to apply any unused accumulated sick leave to pay a portion of the employee's postemployment health care insurance premium in lieu of increasing their service credits. Those employees cannot split their unused leave between the two options.

- Principal and interest on general long-term debt are recorded as fund liabilities when due or when amounts have been accumulated in the debt service fund for transfer to the fiscal agent or for payment to be made early in the following year.

- Claims and judgments are recorded only when payment is due.

FUND ACCOUNTING - The Division uses funds to report its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate accounting entity with a self-balancing set of accounts. The following summarizes the major governmental fund that is presented in the accompanying financial statements:

- State Road (General) Fund - This fund serves as the Division's general fund and is used to account for all financial resources, except those required to be accounted for in another fund. The State Road Fund is funded primarily by dedicated highway user taxes and fees and matching federal highway funds.

INTERFUND ACTIVITY - As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges from the government's various functions. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned. The Division processes certain routine payments, such as payroll through the State Road Fund and allocates those costs to the other governmental funds based on individual projects charged. The interfund balances at June 30, 2012 generally are a result of these routine payments and transfers. At June 30, 2012 there was no interfund activity.

BUDGETING AND BUDGETARY CONTROL - The Division's expenditures are subject to the legislative budget process of the State, with annual budgets adopted utilizing the cash basis of accounting. The cash basis is modified at year-end to allow for payment of invoices up to 45 days after year-end for goods or services received prior to year-end. Appropriated budgeted expenditures, which lapse 45 days after the end of the fiscal year, are incorporated into the Division's overall financial plan, which includes revenue estimates developed by the Division and the State's executive branch. Expenditures are budgeted using natural categories of activity including specific categories of construction, maintenance, and operations, as well as special items. Any revisions that alter overall budgeted expenditures for an expenditure category must be approved by the State Legislature.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Division's State Road (General) Fund which includes the State Road Fund and A. James Manchin Fund has a legislatively approved budget. However, the Coal Resource Fund, Industrial Access Fund and certain monies reported within the State Road Fund in accordance with accounting principles generally accepted in the United States of America are not considered appropriated funds in accordance with the Division's budgetary reporting policy. Accordingly, these funds have not been reported in the Division's Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual (Budgetary Basis) - State Road Fund. A reconciliation of the excess of revenues over expenditures and other financing uses for the year ended June 30, 2012, on the budgetary basis to the GAAP basis for the State Road fund follows:

Excess of revenues over expenditures - budgetary basis	$	(79,518)
Basis of accounting differences (budgetary to GAAP)		(21,273)
Unbudgeted funds		(5,561)
Deficiency of revenues over expenditures - GAAP basis	$	(106,352)

CASH AND CASH EQUIVALENTS - Cash and cash equivalents are short-term investments with original maturities of 90 days or less. Cash and cash equivalents principally consist of amounts on deposit in the State Treasurer's Office (STO) that are pooled funds managed by the West Virginia Board of Treasury Investments (BTI). Interest income from these investments is prorated to the Division at rates specified by the BTI based on the balance of the Division's deposits maintained in relation to the total deposits of all state agencies participating in the pool. Deposits are available with overnight notice to the BTI.

The STO has statutory responsibility for the daily cash management activities of the State's agencies, departments, boards, and commissions. The STO determines which funds to transfer to the BTI for investment in accordance with the West Virginia Code, policies set by the BTI, and provisions of bond indentures and trust agreements when applicable. The West Virginia Legislature, effective July 8, 2005, established the BTI to manage the short-term operating funds of the State. Prior to this date, the West Virginia Investment Management Board (the "IMB") was responsible for investment of both the short-term and long-term funds. The Legislature declared this transfer to ensure direct governmental oversight of state general and special revenue funds. The IMB continues to manage the retirement funds, the employment security funds, and other assets with longer time horizons.

INVENTORIES - Inventories are stated at weighted average cost generally using the "consumption method" whereby expenditures are recognized in the period in which inventory usage, as opposed to purchase, occurs. The portion of fund balance relating to inventories is reported as "Nonspendable" in the Government Fund Financial Statements.

CAPITAL ASSETS - Capital assets, which include buildings, non-infrastructure land, furniture and fixtures, rolling stock, scientific equipment, shop equipment and infrastructure assets (which are normally immovable and of value only to the Division, such as roads, bridges, and similar items), are reported in the statement of net assets in the government-wide financial statements. Capital assets are defined by the Division as follows:

- Non-infrastructure assets with a useful life of at least three years and:
    - A cost of five thousand dollars or more for machinery, equipment, rolling stock, furniture and fixtures; or
    - An acquisition cost of twenty-five thousand dollars or more for buildings at the date of acquisition; and
- Infrastructure assets with a cost in excess of one million dollars.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Purchased and constructed capital assets are valued at historical cost or estimated historical cost. Donated capital assets are recorded at their fair market value at the date of donation.

The estimates of historical costs of buildings and other improvements were based on values that were compiled in 1983. Buildings and non-infrastructure land have been recorded at cost since 1983. Infrastructure constructed from July 1, 1980 to July 1, 2001 has been recorded at estimated historical cost. The estimated historical cost for years 1980-2001 was based on capital outlay expenditures reported by the West Virginia Department of Transportation in the annual reports for those years, less an amount estimated for the historical cost of the acquisition of land for right-of-way. The Division has not capitalized any infrastructure expenditures for assets constructed prior to July 1, 1980, as permitted by GASB 34. The costs of normal maintenance and repairs that do not add to the asset's value or materially extend an asset's useful life are not capitalized. Interest incurred during construction of capital facilities is not capitalized.

New construction is put into construction in process until completed. At that time the projects are evaluated to determine if they meet the threshold for capitalization. The projects that don't meet the threshold for capitalization are expensed.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

Capital assets are depreciated on the straight-line method over the assets' estimated useful lives. There is no depreciation recorded for land and construction in progress. Generally, estimated useful lives are as follows:

- Machinery and equipment: 5 - 20 years
- Buildings: 40 years
- Furniture and fixtures: 3 - 20 years
- Rolling stock: 3 - 20 years

Scientific equipment: 3 - 25 years
Infrastructure: roads - 30 years
Infrastructure: bridges - 50 years

ACCOUNTS AND TAXES RECEIVABLE - Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts. Governmental fund type receivables consist primarily of amounts due from the Federal government. Interest and investment revenue receivable in all funds consist of revenues due on each investment. Taxes receivable in governmental funds represent taxes subject to accrual, primarily motor fuel excise taxes and automobile privilege taxes, which are collected within forty-five days after year end. The uncollectible amounts are based on collection experience and a review of the status of existing receivables.

OTHER ASSETS - Other assets represent payments that reflect costs applicable to future accounting periods and are recorded as other assets in both government-wide and fund financial statements.

CLAIMS - Claims awarded against the Division in the West Virginia State Court of Claims must be approved and funded by legislative action. Expenditures in the fund financial statements for such claims are recognized to the extent that claims awarded are approved and funded by the Legislature. A liability for unfunded claims is recorded in the government-wide financial statements when management and the Division's legal section determine that it is probable that a loss has occurred and the loss can be reasonably estimated. Such claims are segregated as either tort or contract actions and estimates of loss are based on an analysis of the individual claims and historical experience.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

COMPENSATED ABSENCES - Division employees generally earn vacation and sick leave on a monthly basis. Vacation, up to specific limits, is fully vested when earned, and sick leave, while not vesting to the employee prior to retirement, can be carried over to subsequent periods. During 2008, the legislature passed a bill allowing regular full time employees hired before July 1, 2001, having accumulated at least 65 days of sick leave, to be paid, at their option, for a portion of their unused sick leave, not to exceed the number of sick leave days that would reduce the employee's sick leave balance to less than fifty days. The employee shall be paid at a rate equal to one quarter of their usual rate of daily pay during that calendar year. Expenditures for compensated absences are recognized as incurred in the governmental fund financial statements. The government-wide financial statements present the cost of accumulated compensated absences as a liability.

POSTEMPLOYMENT BENEFITS **–** For employees hired prior to July 1, 2001, any unused sick leave accumulated at employee retirement vests to the employee and may be provided in the form of post-retirement payment of all or a portion of the employee's health insurance premiums, or as service credits for retirement purposes, based on hire dates, periods of service and benefit amendments. To the extent that eligible conversion and retirement benefits are determined, a liability in the governmental fund financial statements has been accrued as a result of the Division's participation on the State's post-employment benefits plan, in accordance with GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions.* See Note 13.

RETIREMENT BENEFITS - The Division's employees are covered by the West Virginia Public Employees Retirement System (PERS), a multi-employer cost-sharing defined benefit pension plan. PERS covers substantially all employees of the Division, with employer contributions prescribed by the State Legislature as a percentage of covered payroll.

PREMIUMS, DISCOUNTS AND ISSUANCE COSTS - In the government-wide financial statements long-term debt and other long-term obligations are presented in the columns for governmental activities. Where material, bond and note premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt. Bonds and notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges in other assets and are amortized over the term of the related debt**.** In the governmental fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

INTERGOVERNMENTAL REVENUE – Intergovernmental revenue represents legally authorized appropriations under West Virginia State Code by the West Virginia Legislature.

NET ASSETS – As required by GASB Statement No. 34, the Division displays net assets in the government-wide financial statements in three components: invested in capital assets, net of related debt; restricted and unrestricted.

INVESTED IN CAPITAL ASSETS – This component of net assets consists primarily of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

RESTRICTED NET ASSETS – Restricted net assets are assets whose use or availability has been restricted and the restrictions limit the Division's ability to use the resources to pay current liabilities. When both restricted and unrestricted resources are available for use, it is the Division's policy to use restricted resources first, then unrestricted resources as needed.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

UNRESTRICTED NET ASSETS – Unrestricted net assets consist of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt." In the governmental environment, net assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints on resources are internal and management can remove or modify them. Such internal designations are not reported on the face of the statement of net assets.

FUND BALANCE – In accordance with GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions* the division has classified in the governmental fund financial statements its fund balances in the following categories: nonspendable, restricted, committed, assigned and unassigned as applicable.

The nonspendable fund balance classification includes amounts that cannot be spent because they are either not in spendable form or legally or contractually required to be maintained intact.

The restricted fund balance classification includes amounts restricted for use to specific purposes including externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; imposed by law through constitutional provisions, or enabling legislation including *legally enforceable* requirement that those resources be used only for the specific purposes stipulated in the legislation. *Legal enforceability* means that a government can be compelled by an external party-such as citizens, public interest groups, or the judiciary-to use resources created by enabling legislation only for the purposes specified by the legislation.

Committed amounts reported in fund balance can only be used for specific purposes pursuant to constraints imposed by formal action of the West Virginia State Legislature. Those committed amounts cannot be used for any other purpose unless the government removes or changes the specified use by taking the same type of action (for example, legislation, resolution, ordinance) it employed to previously commit those amounts. The Division has no committed fund balances at June 30, 2012.

Amounts that are constrained by the Division's *intent* to be used for specific purposes as expressed by the West Virginia State Legislature or budget and or finance officers of the Division to be used for specific purposes, but are neither restricted nor committed, are reported as assigned fund balance. The Division has no assigned fund balances at June 30, 2012.

Unassigned fund balance is the residual classification for the general fund. This classification represents fund balance that has not been assigned to other funds and that has not been restricted, committed, or assigned to specific purposes within the general fund.

The Division first applies restricted resources when an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned and then unassigned amounts when an expenditure is incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.

RECENT STATEMENTS ISSUED BY THE GASB –

The Governmental Accounting Standards Board has issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, effective for fiscal years beginning after December 15, 2011. This statement addresses how to account for and report service concession arrangements (SCAs) by establishing recognition, measurement, and disclosure requirements for SCAs for both transferors and governmental operators. The early adoption of this statement has no impact on the June 30, 2012 financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 61, *The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34*, effective for fiscal years beginning after June 15, 2012. This statement improves financial reporting for a governmental financial reporting entity by improving guidance for including, presenting, and disclosing information about component units and equity interest transactions of the entity. The early adoption of this statement has no impact on the June 30, 2012 financial statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Governmental Accounting Standards Board has also issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, effective for fiscal years beginning after December 15, 2011. The objective of this statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance included in the FASB and AICPA pronouncements issued on or before November 30, 1989. This statement will improve financial reporting by contribution to the GASB's efforts to codify all sources of generally accepted accounting principles for state and local governments so that they derive from a single source. The early adoption of this statement has no impact on the June 30, 2012 financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position – an amendment of GASB Statements No. 3, No. 6, No. 10, No. 15, No. 17, No. 23, No. 25, No. 27, No. 28, No. 31, and No. 33*, effective for fiscal years beginning after December 15, 2011. This statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. The Division has not yet determined the effect that the adoption of GASB Statement No. 63 may have on its financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, effective for fiscal years beginning after December 15, 2012. This statement will improve financial reporting by clarifying the appropriate use of the financial statement elements deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The Division has not yet determined the effect that the adoption of GASB Statement No. 65 may have on its financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 66, *Technical Corrections-2012-an amendment of GASB Statements No.10 and No. 62*, effective for fiscal years beginning after December 15, 2012. This statement will resolve conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting and thereby enhance the usefulness of the financial reports. The Division has not yet determined the effect that the adoption of GASB Statement No. 66 may have on its financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 67, *Financial Reporting for Pension Plans-an amendment of GASB Statement No. 25*, effective for fiscal years beginning after June 15, 2013. This statement will improve financial reporting primarily through enhanced note disclosures and schedules of required supplementary information that will be presented by the pension plans that are within its scope. The Division has not yet determined the effect that the adoption of GASB Statement No. 67 may have on its financial statements.

The Governmental Accounting Standards Board has also issued Statement No. 68, *Accounting and Financial Reporting for Pensions-an amendment of GASB Statement No. 27*, effective for fiscal years beginning after June 15, 2014. This Statement will improve the decision-usefulness of information in employer and governmental nonemployer contributing entity financial reports and will enhance its value for assessing accountability and interperiod equity by requiring recognition of the entire net pension liability and a more comprehensive measure of pension expense. The Division has not yet determined the effect that the adoption of GASB Statement No. 68 may have on its financial statements.

(amounts expressed in thousands)

NOTE 2: CASH AND CASH EQUIVALENTS

The composition of cash and cash equivalents were as follows at June 30:

	Amortized Cost	Estimated Fair Value
Cash on deposit with State Treasurer	$ 20,143	$ 20,143
Cash on deposit with State Treasurer in Debt Service Fund	8	8
Cash on deposit with State Treasurer invested in BTI WV Money Market Pool	37,667	37,667
Cash on deposit with State Treasurer invested in BTI WV Short Term Bond Pool	5,622	5,622
Cash in transit	10	10
	$ 63,450	$ 63,450

West Virginia Board of Treasury Investments (BTI) WV Money Market Pool, WV Government Money Market Pool, and WV Short Term Bond Pool

Cash on deposit with the State Treasurer is a non-safeguarded deposit in accordance with GASB Statement No. 3, *Deposits with Financial Institutions, Investments, (including Repurchase Agreements), and Reverse Repurchase Agreements*. Additionally, such deposits are subject to the following BTI policies and procedures.

The BTI has adopted an investment policy in accordance with the "Uniform Prudent Investor Act." The "prudent investor rule" guides those with responsibility for investing the money for others. Such fiduciaries must act as a prudent person would be expected to act, with discretion and intelligence, to seek reasonable income, preserve capital, and, in general, avoid speculative investments. The BTI's investment policy to invest assets in a manner that strives for maximum safety, provides adequate liquidity to meet all operating requirements, and achieves the highest possible investment return consistent with the primary objectives of safety and liquidity. The BTI recognizes that risk, volatility, and the possibility of loss in purchasing power are present to some degree in all types of investments. Due to the short-term nature of the Consolidated Fund, the BTI believes that it is imperative to review and adjust the investment policy in reaction to interest rate market fluctuations/trends on a regular basis and has adopted a formal review schedule. Investment policies have been established for each investment pool and account of the Consolidated Fund.

WV Money Market Pool

Credit risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The BTI"s WV Money Market pool has been rated AAAm by Standard & Poor's. A fund rated "AAAm" has extremely strong capacity to maintain principal stability and to limit exposure to principal losses due to credit, market, and/or liquidity risks. "AAAm" is the highest principal stability fund rating assigned by Standard & Poor's. Neither the BTI itself nor any of the other Consolidated Fund pools or accounts has been rated for credit risk by any organization.

NOTE 2: CASH AND CASH EQUIVALENTS (Continued)

The BTI limits the exposure to credit risk in the WV Money Market Pool by requiring all corporate bonds to be rated AA- by Standard & Poor's (or its equivalent) or higher. Commercial paper must be rated at least A-1 by Standard & Poor's and P-1 by Moody's. The pool must have at least 15% of its assets in U.S. Treasury issues. The following table provides information on the credit ratings of the WV Money Market Pool's investments (in thousands):

Security Type	Credit Rating Moody's	Credit Rating S&P	Carrying Value	Percent of Pool Assets
Commercial paper	P-1	A-1	$ 853,470	30.62%
Corporate bonds and notes	Aa2	AA-	15,000	.54
	Aa3	AA-	13,000	.47
	Aa3	A+	8,000	.29
Total corporate bonds and notes			36,000	1.30
U.S. agency bonds	Aaa	AA+	189,691	6.80
U.S. Treasury notes*	Aaa	AA+	330,865	11.87
U.S. Treasury bills*	Aaa	AA+	237,978	8.54
Negotiable Certificates of deposit	P-1	A-1	110,000	3.95
U.S. agency discount notes	P-1	A-1+	738,706	26.50
Money market funds	Aaa	AAAm	200,054	7.18
Repurchase agreements (underlying securities):				
U.S. Treasury notes *	Aaa	AAA	90,204	3.24
			$ 2,786,968	100.00%

*U.S. Treasury issues are explicitly guaranteed by the United States government and are not subject to credit risk.

At June 30, 2012, the WV Money Market Pool investments had a total carrying value of $2,786,968 of which the Division's ownership represents 1.35%.

WV Short Term Bond Pool

Credit risk – The BTI limits the exposure to credit risk in the WV Short Term Bond Pool by requiring all corporate bonds to be rated A by Standard & Poor's (or its equivalent) or higher. Commercial paper must be rated at least A-1 by Standard & Poor's and P-1 by Moody's. The following table provides information on the credit ratings of the WV Short Term Bond Pool's investments (in thousands):

(amounts expressed in thousands)

NOTE 2: CASH AND CASH EQUIVALENTS (Continued)

Security Type		Credit Rating: Moody's	Credit Rating: S&P	Carrying Value	Percent of Pool Assets
Corporate asset backed securities		Aaa	AAA	$ 95,628	18.99 %
		Aaa	NR*	38,524	7.64
		NR	AA+	3,900	0.77
	**	B1	CCC	896	0.18
	**	B3	BB	311	0.06
	**	B3	BBB-	53	0.01
	**	B3	CCC	280	0.06
	**	Caa2	CCC	186	0.04
	**	Caa3	CCC	243	0.05
	**	Caa3	D	26	0.01
	**	Ca	CCC	586	0.12
		NR	NR	3,786	0.75
Total corporate asset backed securities				144,419	28.68
Corporate bonds and notes		Aa2	AA+	9,025	1.79
		Aa3	AA-	15,666	3.11
		Aa3	A	23,032	4.57
		A1	AA	12,145	2.41
		A1	A+	30,684	6.09
		A2	A	39,064	7.76
		A3	A-	7,755	1.54
		A3	BBB+	3,006	0.6
		Baa1	A-	4,162	0.83
		Baa2	A-	6,709	1.33
Total corporate bonds and notes				151,248	30.03
U.S. agency bonds		Aaa	AA+	45,024	8.94
U.S. Treasury notes***		Aaa	AA+	44,251	8.79
U.S. agency mortgage backed securities****		Aaa	AA+	77,065	15.30
Money market funds		Aaa	AAAm	41,610	8.26
				$ 503,617	100.00 %

* NR = Not Rated

** These securities were not in compliance with BTI Investment Policy at June 30, 2012. The securities were in compliance when originally acquired, but were subsequently downgraded. BTI management and its investment advisors have determined that it is in the best interests of the participants to hold the securities for optimal outcome.

*** U.S. Treasury issues are explicitly guaranteed by the United States government and are not subject to credit risk.

**** U.S. agency mortgage backed securities are issued by the Government National Mortgage Association and are explicitly guaranteed by the United States government and are not subject to credit risk.

NOTE 2: CASH AND CASH EQUIVALENTS (Continued)

At June 30, 2012, the Division's ownership represents 1.12% of these amounts held by BTI.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. All BTI Consolidated Fund pools and accounts are subject to interest rate risk.

The overall weighted average maturity of the investments of the WV Money Market Pool cannot exceed 60 days. Maximum maturity of individual securities cannot exceed 397 days from date of purchase, except for government floating rate notes, which can be up to 731 days. The following table provides information on the weighted average maturities for the various asset types in the WV Money Market Pool:

Security Type	Carrying Value (In Thousands)	WAM (Days)
Repurchase agreements	$ 90,204	3
U.S. Treasury notes	330,865	122
U.S. Treasury bills	237,978	37
Commercial paper	853,470	35
Certificates of deposit	110,000	10
U.S. agency discount notes	738,706	44
Corporate bonds and notes	36,000	48
U.S. agency bonds/notes	189,691	68
Money market funds	200,054	1
	$ 2,786,968	46

The overall effective duration of the investments of the WV Short Term Bond Pool cannot exceed 731 days. Maximum effective duration of individual securities cannot exceed 1,827 days (five years) from date of purchase. The following table provides information on the effective duration for the various asset types in the WV Short Term Bond Pool:

NOTE 2: CASH AND CASH EQUIVALENTS (Continued)

Security Type		Carrying Value (In Thousands)	Effective Duration (Days)
U.S. Treasury bonds/notes	$	44,251	366
Corporate notes		151,248	242
Corporate asset backed securities		144,419	250
U.S. agency bonds/notes		45,024	23
U.S. agency mortgage backed securities		77,065	13
Money market fund		41,610	1
	$	503,617	180

Other Investment Risks

Other risks of investing can include concentration of credit risk, custodial credit risk, and foreign currency risk. None of the BTI's Consolidated Fund's investment pools or accounts is exposed to these risks as described below.

Concentration of credit risk is the risk of loss attributed to the magnitude of a BTI Consolidated Fund Pool or account's investment in a single corporate issuer. The BTI investment policy prohibits those pools and accounts permitted to hold corporate securities from investing more than 5% of their assets in any one corporate name or one corporate issue.

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the BTI will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Repurchase agreements are required to be collateralized by at least 102% of their value, and the collateral is held in the name of the BTI. The BTI or its agent does not release cash or securities until the counterparty delivers its side of the transaction.

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. None of the Consolidated Fund's investment pools or accounts holds interests in foreign currency or interests valued in foreign currency.

Deposits

Custodial credit risk of deposits is the risk that in the event of failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. Deposits include nonnegotiable certificates of deposit. The BTI does not have a deposit policy for custodial credit risk.

(amounts expressed in thousands)

NOTE 3: ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2012 consisted of the following:

Federal aid billed and not paid	$	5,226
Federal aid earned but not billed		67,911
Total federal aid receivable		73,137
Other receivables		12,031
Combined total receivables		85,168
Less: allowance for uncollectibles		(492)
Net accounts receivable	$	84,676

Accounts receivable representing federal aid earned but not billed relate principally to the Federal Highway Administration's (FHWA) participating share of expenditures on highway projects.

NOTE 4: TAXES RECEIVABLE

Taxes receivable at June 30, 2012 consisted of the following:

Automobile privilege taxes	$	16,468
Motor fuel excise taxes		55,532
Registration fees		2,865
Total taxes receivable	$	74,865

(amounts expressed in thousands)

NOTE 5: DUE FROM/TO OTHER STATE OF WEST VIRGINIA AGENCIES

Amounts due from other State of West Virginia agencies at June 30, 2012 consisted of the following:

The Department of Motor Vehicles	$	1,960
Other agencies		515
Total amounts due from other State of West Virginia agencies	$	2,475

Amounts due to other State of West Virginia agencies at June 30, 2012 consisted of the following:

Public Employees Insurance Agency	$	1,920
Public Empoyee's Reitrement		1,677
Other agencies		95
Total amounts due to other State of West Virginia agencies	$	3,692

NOTE 6: INVENTORIES

Inventories at June 30, 2012 consisted of the following:

Materials and supplies	$	32,740
Equipment repair parts		9,341
Gas and lubrication supplies		3,684
Total inventories	$	45,765

(amounts expressed in thousands)

NOTE 7: CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2012, was as follows:

	July 1, 2011	Increases	Decreases	June 30, 2012
Capital assets not being depreciated:				
Land - non infrastructure	$ 19,680	$ 3,345	$ -	$ 23,025
Land - infrastructure	956,518	29,784	-	986,302
Construction-in-progress - buildings	14,487	7,617	11,181	10,923
Construction-in-progress - land improvements	402	1,352	796	958
Construction-in-progress - roads	756,402	129,813	300,964	585,251
Construction-in-progress - bridges	201,549	122,773	126,081	198,241
Total capital assets not being depreciated	1,949,038	294,684	439,022	1,804,700
Capital assets being depreciated:				
Buildings	124,999	11,181	135	136,045
Furniture and fixtures	4,637	64	213	4,488
Land improvements - non infrastructure	11,365	796	-	12,161
Rolling stock	241,189	18,284	15,246	244,227
Shop equipment	3,057	-	-	3,057
Scientific equipment	2,873	11	-	2,884
Infrastructure - roads	8,128,408	300,964	-	8,429,372
Infrastructure - bridges	2,602,262	126,081	-	2,728,343
Total capital assets being depreciated	11,118,790	457,381	15,594	11,560,577
Less accumulated depreciation:				
Buildings	45,830	2,985	109	48,706
Furniture and fixtures	3,498	198	204	3,492
Land improvements - non infrastructure	3,950	568	-	4,518
Rolling stock	169,752	19,381	14,984	174,149
Shop equipment	3,004	13	-	3,017
Scientific equipment	2,328	170	-	2,498
Infrastructure - roads	4,227,535	244,675	-	4,472,210
Infrastructure - bridges	500,734	46,053	-	546,787
Total accumulated depreciation	4,956,631	314,043	15,297	5,255,377
Total capital assets being depreciated, net	6,162,159	143,338	297	6,305,200
Governmental activities capital assets, net	$ 8,111,197	$ 438,022	$ 439,319	$ 8,109,900

(amounts expressed in thousands)

NOTE 7: CAPITAL ASSETS (Continued)

Current year depreciation totaling $310,292 was allocated as separate line items in the statement of activities under the major functions of the Division of Maintenance and Improvements. The remaining $3,751 unallocated depreciation expense is included as a separate line item in the statement of activities. Infrastructure depreciation is primarily related to construction type activities; depreciation of shop and rolling stock assets is primarily related to maintenance type activities; and depreciation of buildings and improvements and furniture and fixtures support all of the various activities of the Division.

A summary of depreciation on each capital asset type follows:

Asset Type	Depreciation
Buildings and improvements	$ 2,985
Furniture and fixtures	198
Land improvements	568
Total unallocated	3,751
Rolling stock	19,381
Shop equipment	13
Scientific equipment	170
Total road maintenance	19,564
Infrastructure - roads	244,675
Infrastructure - bridges	46,053
Total other road operations	290,728
Total depreciation expense	$ 314,043

NOTE 8: RETAINAGES PAYABLE

Retainages payable includes funds withheld from payments to consulting firms and construction contractors. Retainage payments are made to the consultants and contractors when work is satisfactorily completed. The Division has entered into an arrangement with the BTI whereby amounts retained from payments to construction contractors may, at the option of the contractor, be deposited in an interest bearing account in the contractor's name. The funds on deposit in these accounts are not reported as assets of the Division. At June 30, 2012, retainages payable included $0 that was on deposit at BTI for construction contractors.

(amounts expressed in thousands)

NOTE 9: LONG-TERM OBLIGATIONS

Long-term obligations at June 30, 2012, and changes for the fiscal year then ended are as follows:

	Issue Date	Interest Rates	Maturity Through	Beginning Balance	Additions	Reductions	Ending Balance
General obligation bonds payable from tax revenue							
Safe road bonds	2001	3.50% - 5.50%	06/01/2013	$ 13,890	$ -	$ 12,325	$ 1,565
Safe road bonds	2005	3.00% - 5.00%	06/01/2025	256,435	-	22,540	233,895
Safe road bonds	2010	4.00%	06/01/2023	35,135	-	-	35,135
Total general obligation bonds				305,460	-	34,865	270,595
Bond premium				23,670	-	1,768	21,902
Total general obligation bonds payable net of premium				329,130	-	36,633	292,497
Revenue notes payable from federal aid revenue:							
Surface transportation improvements special notes (Garvee 2006A)	2006	3.75% - 5.00%	06/01/2016	45,915	-	8,370	37,545
Surface transportation improvements special notes (Garvee 2007A)	2007	4.00% - 5.00%	06/01/2016	19,900	-	3,630	16,270
Surface transportation improvements special notes (Garvee 2009A)	2009	3.75% - 5.00%	06/01/2016	56,980	-	10,425	46,555
Total revenue notes payable				122,795	-	22,425	100,370
Bond premium				5,097	-	1,019	4,078
Total general obligation notes payable net of premium				127,892	-	23,444	104,448
Claims and judgments				13,981	4,213	-	18,194
Compensated absences				29,312	426	967	28,771
Total long-term obligations				$ 500,315	$ 4,639	$ 61,044	$ 443,910

(amounts expressed in thousands)

NOTE 9: LONG-TERM OBLIGATIONS (Continued)

General obligation bond issues are authorized by constitutional amendments and are general obligations of the State of West Virginia. Legislation implementing the amendments requires that debt service on the bonds be paid from the State Road Fund and, to the extent that there are insufficient funds therein, from a levy of an annual state tax. All bonds authorized under prior constitutional amendments have been issued and include amounts outstanding above.

Surface Transportation Improvement Special Obligation Notes are authorized under Chapter 17, Article 17A of the Code of West Virginia, 1931, as amended. The Code provides for the issuance of special obligation notes to facilitate the construction of highways, secondary roads and bridges to be funded wholly or in part by federal dollars and in anticipation of reimbursement from such sources. The federal legislation that enables reimbursement of such costs is included in Title 23, Section 122. The Memorandum of Agreement executed between the Federal Highway Administration and the Division of Highways documents the procedures for managing the stewardship and oversight of highway projects that are financed with the proceeds of these notes.

Debt service expenditures included interest of $20,078 for the year ended June 30, 2012. Total debt service costs, exclusive of coupon redemption costs, for each of the next five years and thereafter, on general obligation bonds payable and revenue notes payable liquidated through debt service funds, are as follows:

	2013	2014	2015	2016	2017	2018-2022	2023-2025	Total
General obligation bonds payable from tax revenue:								
Safe road bonds	$ 38,403	$ 36,757	$ 36,765	$ 36,765	$ 23,301	$ 116,108	$ 70,231	$ 358,330
Less: interest	13,173	11,917	10,675	9,370	8,001	28,178	6,421	87,735
Total principal	25,230	24,840	26,090	27,395	15,300	87,930	63,810	270,595
Bond premium	1,726	1,721	1,721	1,721	1,721	8,604	4,688	21,902
Total principal and bond premium	$ 26,956	$ 26,561	$ 27,811	$ 29,116	$ 17,021	$ 96,534	$ 68,498	$ 292,497
Revenue notes payable from federal aid revenue:								
Surface transportation special obligation notes	$ 27,547	$ 27,519	$ 27,504	$ 27,499	$ -	$ -	$ -	$ 110,069
Less: interest	4,177	3,044	1,854	624	-	-	-	9,699
Total principal	23,370	24,475	25,650	26,875	-	-	-	100,370
Note premium	1,019	1,019	1,020	1,020	-	-	-	4,078
Total principal and note premium	$ 24,389	$ 25,494	$ 26,670	$ 27,895	$ -	$ -	$ -	$ 104,448

(amounts expressed in thousands)

NOTE 9: LONG-TERM OBLIGATIONS (Continued)

During the year ended June 30, 1997, the State was authorized by constitutional amendment to issue $550,000 of general obligation bonds to fund highway and road construction projects known as Safe Road Bonds. These bonds will be repaid from revenues of the State Road Fund. Safe Road Bonds of $220,000 were issued during July 1998; $110,000 were issued during July 1999; $110,000 were issued during July 2000; and an additional $110,000 were issued during July 2001.

In 2005, the State refinanced part of the above mentioned bonds in the amount of $321,405. These bonds will be repaid from revenues of the State Road Fund through the year 2025. The refinancing was to advance-refund $319,860 of outstanding 1998, 1999 and 2000 Series bonds. The net proceeds of $351,405 (after payment of $1,606 in underwriting fees, insurance, and other issuance costs) were used to purchase U.S. Government State and Local Government Series securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refinanced portions of the 1998, 1999, and 2000 Series bonds. The defeased bonds were called on June 1, 2010 and are no longer outstanding.

During the year ended June 30, 2007, the State was authorized by constitutional amendment to issue $200,000 of Surface Transportation Improvements Special Obligation Notes (Garvee Notes) to fund highway and road construction projects. These notes will be repaid from future federal highway revenues. Garvee Notes of $76,000 were issued during October 2006 and $33,000 were issued during April 2007. The Division sold $76,835 of additional Garvee notes during the fiscal year ending June 30, 2009.

The Division issued on behalf of the State of West Virginia, $35,135 in General Obligation State Road Refunding Bonds, Series 2010A on July 22, 2010, resulting in proceeds of $38,048. This bond issue refunds Series 1998 and Series 2001 General Obligation State Road Bonds with cumulative outstanding principal of $37,730, and will result in a net present value savings of $4,265 over the life of the bond issue. The bonds that were refunded were called on June 1, 2011 and are no longer outstanding.

Long term obligations for compensated absences, claims payable, and general obligation bonds are as follows:

	Compensated Absences	Claims and Judgments	Obligation Bonds and Revenue Notes and Premium	Total
Current liabilities	$ 12,353	$ 2,094	$ 51,345	$ 65,792
Long-term liabiities	16,418	16,100	345,600	378,118
	$ 28,771	$ 18,194	$ 396,945	$ 443,910

(amounts expressed in thousands)

NOTE 9: LONG-TERM OBLIGATIONS (Continued)

The following summarizes the estimated claims liability for the current year and that of the preceding two years.

	June 30, 2012	June 30, 2011	June 30, 2010
Estimated claims liability, July 1	$ 13,981	$ 18,485	$ 7,809
Additions for claims incurred during the year	2,094	2,391	1,564
Changes in estimates for claims of prior periods	4,510	(5,331)	9,621
Payments on claims	(2,391)	(1,564)	(509)
Estimated claims liability, June 30	$ 18,194	$ 13,981	$ 18,485

At June 30, 2012, approximately $13,000 of tort claims and $3,100 in environmental claims were pending against the Division in the West Virginia State Court of Claims. With respect to these claims, the Division has an estimated obligation of $16,100 recorded in the government-wide Statement of Net Assets, based on management's evaluation of the nature of such claims and consideration of historical loss experience for the respective types of action. Such claims will be recognized primarily as expenditures of the State Road Fund if, and when, they are approved for payment by the Legislature in accordance with legal statutes. Also included in claims are claims that have been settled in the court of claims and approved for payment through legislative action. These amounts total approximately $2,094. During the normal course of operations, the Division may become subject to other litigation. No provision has been made in the financial statements for liabilities, if any, from such litigation.

The Division's obligation for accrued vacation leave time includes leave time and related costs expected to be paid to employees in the future and are determined using wage levels in effect at the date the obligation is calculated. Upon retirement, an employee may apply unused sick leave to reduce their future insurance premiums paid to the West Virginia Public Employees Insurance Agency or apply unused sick leave or annual leave or both to obtain a greater benefit under the West Virginia Public Employees Retirement System.

NOTE 10: RELATED PARTY TRANSACTIONS WITH THE STATE OF WEST VIRGINIA

The Division enters into certain transactions with various agencies of the State of West Virginia. The following summarizes the nature and terms of the most significant transactions:

- The Division leases from the Department of Administration substantially all of State Office Building No. 5 and a portion of State Office Building No. 3 which are owned by the State Building Commission. The Division may be released from its obligation only at the option of the lessor. The Division is obligated under these operating leases, which expire June 30, 2013 for rental payments of approximately $2.0 million annually. Management expects the leases to be renewed upon expiration.

- The Division’s employees participate in various benefit plans offered by the State of West Virginia. Employer contributions to these plans are mandatory. During the year ended June 30, 2012 the Division incurred payroll related expenditures of approximately $25,814 for employee health insurance benefits provided through the West Virginia Public Employees Insurance Agency and approximately $26,024 in employer matching contributions to the State Public Retirement System.

NOTE 11: COMMITMENTS AND CONTINGENCIES

The amount of unexpended balances of highway design and construction contracts entered into by the Division with various contractors approximated $583,291 at June 30, 2012.

The Division participates in several federal programs which are subject to audit by the federal awarding agency. Any disallowed claims, including amounts already collected by the Division, may constitute a liability to the federal awarding agency of the applicable funds. The amount, if any, of expenditures that may be disallowed by the federal awarding agency cannot be determined at this time. The Division expects such amounts, if any, to be immaterial to the financial position of the Division. The Division records these disallowed costs in the period the audit is finalized.

Based on the Division's Inspection Program the Division has reviewed the information on obsolete and deficient bridges. The Division is concerned about safety and tries to prioritize bridges for repair and replacement based on engineering assessments. The Division’s long range plans to address this issue will be impacted by actions that may be taken by both the federal and state government, including funding levels provided for this purpose.

Various legal proceedings and claims related to condemnation and eminent domain cases are pending against the Division. At June 30, 2012, there were approximately 439 open cases. These cases involve the acquisitions of properties by the Division for right of way purposes. The Division has paid the applicable courts on behalf of the land grantors, estimated fair values of the properties acquired. The open cases may result in condemnation commissioners or jury verdicts awarding amounts in excess of the previously paid estimated fair value amounts. In these situations, the excess award amount plus a statutory interest rate of 10% would be paid to the grantor. The interest amount would be calculated on the excess award amount from the date of the petition filing to the date of the excess payment amount to the court. Several of these cases relate to condemnations from the 1960s and 1970s. There is no estimate available as to the amount of monies needed to resolve these cases. Management is of the opinion that any liability resulting from these claims would have no adverse effect on the financial position of the Division.

NOTE 12: RETIREMENT PLAN

PLAN DESCRIPTION - The Division contributes to the West Virginia Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan administered by the West Virginia Consolidated Public Retirement Board. Chapter 5, Article 10 of the West Virginia State Code assigns the authority to establish and amend benefit provisions to the PERS Board of Trustees. Employees who retire at or after age 55 and have completed 25 years of credited service are eligible for retirement benefits as established by State statute. Retirement benefits are payable monthly for life, in the form of a straight-line annuity equal to two percent of the employee's final average salary, multiplied by the number of years of the employee's credited service at the time of retirement. PERS also provides deferred retirement, early retirement, death, and disability benefits to plan members and beneficiaries. The West Virginia Consolidated Public Retirement Board issues a publicly available financial report that includes financial statements and required supplementary information for PERS. That report may be obtained by writing to the West Virginia Consolidated Public Retirement Board, 4101 MacCorkle Avenue S.E., Charleston, West Virginia 25304-1636 or by calling (304) 558-3570.

FUNDING POLICY - The PERS funding policy has been established by action of the State Legislature. State statute requires that plan participants contribute 4.5% of compensation. The current combined contribution rate is 19% of annual covered payroll, including the Division's contribution of 14.5% which is established by PERS. The Division's contributions to PERS for the years ended June 30, 2012, 2011, and 2010 were $26,024, $22,213, and $18,040, respectively, equal to the required contributions for each year.

NOTE 13: OTHER-POST EMPLOYMENT BENEFITS

The Division participates in the West Virginia Other Postemployment Benefit Plan (OPEB) of the West Virginia Retiree Health Benefit Trust Fund (RHBTF), a cost sharing multiple-employer defined benefit postemployment healthcare plan administered by the West Virginia Public Employee Insurance Agency (WVPEIA). The OPEB Plan, established in accordance with GASB Statement No. 45, provides retiree post-employment health care benefits for participating state and local government employers. The provisions of the Code of West Virginia, 1931, as amended (the Code), assigns the authority to establish and amend benefit plans to the WVPEIA Board of Trustees. The WVPEIA issues a publicly available financial report that includes financial statements and required supplementary information for the OPEB Plan. That report may be obtained by writing to West Virginia Public Employees Insurance Agency, 601 57th Street, Charleston, WV 25304 or by calling 1-888-680-7342.

The Code requires the RHBTF to bill the participating employers 100% of the Annual Required Contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) of the plan over a period not to exceed thirty years. State of West Virginia plan employers are billed per active health policy per month.

The OPEB Plan costs are accrued based upon invoices received from PEIA based upon actuarially determined amounts. The ARC rate is nine hundred sixty one dollars per employee per month for the year ending June 30, 2012. The Division's ARC was $33,557, $39,946 and $30,555 and the Division has paid premiums of $8,541, $8,230 and $ 7,516 which represent 25.4%, 20.6% and 24.6% of the ARC, respectively, for the years ending June 30, 2012, 2011, and 2010. At June 30, 2012, the liability related to OPEB costs was $118,159.

NOTE 14: RISK MANAGEMENT

The Division is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and life coverage; and natural disasters. The State of West Virginia established the Board of Risk and Insurance Management (BRIM) and the Public Employees Insurance Agency (PEIA), to account for and finance uninsured risks of losses for state agencies, institutions of higher education, and component units.

BRIM is a public entity risk pool that provides coverage for general, property, medical malpractice, and automobile liability. PEIA is also a public entity risk pool and provides coverage for employee and dependent health, life and prescription drug insurance. The Division retains the risk of loss on certain tort and contractor claims in excess of the amount insured or covered by BRIM's insurance carrier. Other than the amounts disclosed in Note 9, amounts of settlements have not exceeded insurance coverage in the past three years. The Division has evaluated this potential risk of loss as discussed in Note 9. BrickStreet Insurance, a private mutual insurance company, provided coverage for work related accidents.

Through its participation in the PEIA, the Division has obtained health coverage for its employees. In exchange for payment of premiums to PEIA, the Division has transferred its risks related to health coverage. PEIA issues publicly available financial reports that include financial statements and required supplementary information, these reports may be obtained by writing to PEIA.

American Zurich Insurance Company provides workers compensation coverage to all West Virginia state agencies. Payments for coverage are made directly to the West Virginia State Insurance Commission who in turn purchases the workers' compensation coverage on behalf of all West Virginia state agencies. Nearly every employer in the state who has a payroll must have coverage.

In exchange for premiums, the Division transfers its risk of loss related to employee injuries to American Zurich Insurance Company.

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INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

November 10, 2012

Joint Committee on Government and Finance
West Virginia Legislature

To the Members of the Joint Committee:

We have audited the financial statements of the governmental activities and each major fund of the **West Virginia Department of Transportation, Division of Highways** (the Division), a component unit of the State of West Virginia and the West Virginia Department of Transportation, as of and for the year ended June 30, 2012, which collectively comprise the Division's financial statements and have issued our report thereon dated November 10, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Division's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of opining on the effectiveness of the Division's internal control over financial reporting. Accordingly, we have not opined on the effectiveness of the Division's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. Therefore, we cannot assure that we have identified all deficiencies, significant deficiencies or material weaknesses. However, as described in the accompanying schedule of audit findings and responses we identified a certain deficiency in internal control over financial reporting, that we consider a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, when performing their assigned functions, to prevent, or detect and timely correct misstatements. A *material weakness* is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that material financial statement misstatements will not be prevented, or detected and timely corrected. We consider finding 2012-001 described in the accompanying schedule of audit findings and responses to be a material weakness.

Joint Committee on Government and Finance
West Virginia Legislature
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Required by *Government Auditing*
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Compliance and Other Matters

As part of reasonably assuring whether the Division's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express an opinion. The results of our tests disclosed no instances of noncompliance or other matters we must report under *Government Auditing Standards*.

We did note certain matters not requiring inclusion in this report that we reported to the Division's management in a separate letter dated November 10, 2012.

The Division's response to the finding identified in our audit is described in the accompanying schedule of audit findings and responses. We did not audit the Division's response and, accordingly, we express no opinion on it.

We intend this report solely for the information and use of management of the Division, the Joint Committee on Government and Finance of the West Virginia Legislature and others within the Division. We intend it for no one other than these specified parties.

Respectfully submitted,

Perry & Associates CPA's A.C.

Perry and Associates
Certified Public Accountants, A.C.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

FINDING NUMBER 2012-001

Material Weakness

Financial Reporting of Capital Assets

Criteria:
Expenditures for infrastructure assets are required by accounting principles generally accepted in the United States of America to be capitalized in the Government-wide Financial Statements and depreciated over their estimated useful lives.

Condition:
The Division's process for identifying expenditures for infrastructure assets that meets its established capitalization policy is dependent on several criteria, including the project completion date as reported in the project management system and the type of project. We noted the Division does not have effective controls established to ensure the project completion date entered into the project management system is accurate, nor is there an adequate process that reviews the type of project and whether it should be capitalized or expensed or make sure all costs related to a project are capitalized.

Cause:
The Division has not established effective procedures to ensure that the project completion date used to evaluate and determine the capitalization of expenditures is accurate. A review process is not in place to ensure maintenance projects are not included in WIP or capitalized when the project is completed. In addition, no review process is in place to ensure all costs related to a project are capitalized upon completion.

Effect:
Without proper monitoring, errors in the reported balances for capital assets and expenses in the Division's Government-wide Financial Statements could occur without being detected by management. In 2012, the Division adjusted infrastructure for the following: a reduction in current year work in process expenses of $101,422,064, a reduction of capitalized assets of $21,704,750 and an increase of $66,788,347 in expenses removed from work in process. These adjustments were made to eliminate projects from WIP that were actually maintenance and repair, projects, to capitalize expenses that should have been previously capitalized, or remove assets that were under the capitalization threshold.

Recommendation:
We recommend that management establish procedures to ensure that the project completion date in the project management system is accurate and a review process is established that will 1) capitalized all costs related to a project and 2) ensure maintenance projects are not capitalized. Establishing the procedures will help to ensure that capitalized expenditures and related depreciation expenses are complete and accurate. The Division should consider changes in the supervisory review procedures to ensure that infrastructure items are appropriately identified and capitalized in a timely manner.

Management's Response – DOT Finance & Administration Division with the assistance of the Program, Planning and Administration Division will develop procedures and criteria to ensure the project completion dates are reasonably accurate and all significant expenses associated with true infrastructure projects are capitalized and that the related depreciation expenses are complete and accurate. As a part of this effort, there will be a joint review of the capitalized expenditures by the aforementioned Division managers.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS

SCHEDULE OF PRIOR AUDIT FINDINGS
JUNE 30, 2012

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***
2011-001	Recognition of taxes receivable for leased vehicles not in accordance with GAAP	Yes	
2011-002	Lack of controls in capital asset reporting	No	Repeat as finding 2012-001