Basic Financial Statements

Government of the United States Virgin Islands
Year Ended September 30, 2012

Ernst & Young LLP

Building a better working world

Government of the United States Virgin Islands

Basic Financial Statements

Year Ended September 30, 2012

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Report of Independent Auditors

The Honorable Governor
of the Government of the United States Virgin Islands:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government), as of and for the year ended September 30, 2012, which collectively comprise the Government's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Government's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following component units:

- The Virgin Islands Lottery (V.I. Lottery), a nonmajor enterprise fund, which represents 0.4%, and 2.8%, respectively, of the assets, and revenues/additions of the aggregate remaining fund information, and 7.9%, 3.5%, and 20.7%, respectively, of the assets, net assets, and revenue of the business-type activities. The V.I. Lottery net deficit represents $2.2 million of the $1.4 billion net asset/fund balance of the aggregate remaining fund information.

- The Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), which represents 88.9%, 94.2%, and 41.5%, respectively, of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information.

- The Virgin Islands Housing Authority (VIHA), Virgin Islands Public Television System (VIPTS), Virgin Islands Economic Development Authority (VIEDA), Magens Bay Authority (MBA), Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA), discretely presented component units, which collectively represent 26.2%, 32.9%, and 37.0%, respectively, of the assets, net assets, and revenue of the aggregate discretely presented component units.

These financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based solely on the reports of other auditors.

Except as discussed in the following six paragraphs, 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 *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. The financial statements of Juan F. Luis Hospital and the GERS were not audited in accordance with *Government Auditing Standards*. We were not engaged to perform an audit of the Government's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Government's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

The report of the other auditors on the 2012 financial statements of VIHFA, a discretely presented component unit, was qualified because the auditors were unable to obtain sufficient audit evidence to determine whether assets transferred from Department of Planning and Natural Resources of cash and cash equivalents of $16.2 million, investments of $5.0 million, and capital assets of $31.7 million were fairly stated.

The report of other auditors on the 2012 financial statements of VIPTS, a discretely presented component unit, was qualified because the auditors were unable to obtain sufficient audit evidence to determine whether capital assets of $5.6 million were fairly stated.

The financial statements of WMA and the Virgin Islands Research and Technology Park (RTPark), nonmajor discretely presented component units, have not been audited, and we were not engaged to audit the WMA and RTPark financial statements as part of our audit of the Government's basic financial statements. WMA and RTPark's financial activities are included in the Government's basic financial statements as a discretely presented component units and represents 8%, 14%, and 6% of the assets, net position, and revenues, respectively, of the Government's aggregate discretely presented component units.

The Government did not maintain the requisite documentation to support its accrued retroactive liability of $195.3 million as of September 30, 2012 and for fiscal year 2012. As a result, we were unable to obtain sufficient audit evidence to determine whether adjustments to these balances in the governmental activities were required.

The report of other auditors on the 2012 financial statements of GERS, a fiduciary component unit (pension trust fund), was qualified because GERS maintained investments in a limited partnership valued at $42.8 million whose fair value has been estimated in the absence of a readily determinable fair value. GERS' estimate was based on information provided by the general partner of the limited partnership. The effect on the financial statements as a result of GERS' inability to document its procedures for determining fair value of the investment was not determinable.

The basic financial statements do not include a liability for medical malpractice claims in the reciprocal insurance fund (a non-major enterprise fund) and, accordingly, the Government has not recorded an expense for the current period change in that liability. The Government's records do not permit it, nor is it practical to extend our auditing procedures sufficiently to determine the extent by which the business-type activities, government insurance fund, and aggregate remaining fund information as of and for the year ended September 30, 2012 may have been affected by this condition.

Because of the matters discussed in the preceding two paragraphs of this report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial position of the business-type activities and aggregate remaining fund information as of September 30, 2012. In addition, we do not express an opinion on the changes in financial position of the business-type activities, and aggregate remaining fund information and, where applicable, cash flows for the year ended September 30, 2012.

In our opinion, based on our audit and the reports of other auditors, except for the effect of the adjustments, if any, as might be determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether (1) cash and cash equivalents of $16.2 million, investments of $5.0 million and capital assets of $31.7 million in the financial statements of VIHFA, (2) capital assets of $5.6 million in the financial statements of VIPTS, and (3) unaudited financial statements of WMA and RTPark were fairly stated as described above, and the effect of the adjustments, if any, as might be determined to be necessary, had we been able to obtain sufficient audit evidence to determine whether the retroactive pay liability balance in the governmental activities were fairly stated as described in paragraph seven above, the financial statements referred to previously, present fairly, in all material respects, the respective financial position of the aggregate discretely presented component units, and the governmental activities of the Government of the United States Virgin Islands, as of September 30, 2012, and the respective changes in financial position for the year then ended in conformity with U.S. generally accepted accounting principles.

Finally, in our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund of the Government of the United States Virgin Islands, as of September 30, 2012, and the respective changes in financial position and respective budgetary comparison for the general fund for the year then ended in conformity with U.S. generally accepted accounting principles.

As described more fully in Note 18 to the financial statements, the beginning net assets of the discretely presented component units as of September 30, 2011, was restated by $3.3 million. The previously issued auditor's report dated June 28, 2013, is not to be relied on because the previously issued financial statements were materially misstated and has been replaced by the auditor's report on the restated financial statements herein. Refer to Finding 12-08 in the schedule of findings and questioned costs for the reporting of a material weakness related to the financial reporting of component units.

In accordance with *Government Auditing Standards,* we have also issued our report dated February 7, 2014, on our consideration of the Government'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. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. 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 require that the management's discussion and analysis and the schedules of funding progress and employer distributions listed on pages 6 through 18 and 144 through 146, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting 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, 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 assurance.

Ernst & Young LLP

February 7, 2014

Introduction

The following management's discussion and analysis presents an overview of the financial position and activities of the Government of the United States Virgin Islands (the Government) as of and for the fiscal years ended September 30, 2012 and 2011.

Government-wide Financial Statements

The government-wide financial statements are designed to present an overall picture of the financial position of the Government. These statements consist of the statement of net assets (deficit) and the statement of activities, which are prepared using the economic resources measurement focus and the accrual basis of accounting. This means that current year's revenue and expenses are included regardless of when cash is received or paid, producing a view of financial position and changes in financial position similar to that presented by most private-sector companies.

The statement of net assets (deficit) combines and consolidates the Government's current financial resources with capital assets and long-term obligations.

Both of the above-mentioned financial statements have separate sections for three different types of the Government programs or activities. These three types of activities are as follows:

> ***Governmental Activities –*** The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with the primary government (PG) fall into this category, including general government, public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.
>
> ***Business-Type Activities –*** These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Government include the operations of the (i) unemployment insurance program and (ii) the West Indian Company (WICO). Both of these programs operate with minimal assistance from the governmental activities of the Government.

Discretely Presented Component Units **–** These are operations for which the Government has financial accountability even though they have certain independent qualities as well. For the most part, these entities operate similar to private sector businesses and the business-type activities described above. The Government’s discretely presented component units are presented in two categories, major and nonmajor. This separation is determined by the relative size of the entities’ assets, liabilities, revenue, and expenses in relation to the total of all component units.

Fund Financial Statements

Fund financial statements focus on the most significant (or major) funds of the Government. A fund is a separate accounting entity with a self-balancing set of accounts. The Government uses funds to keep track of sources of funding and spending related to specific activities. The Government uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

A major fund is a fund whose revenue, expenditures or expenses, assets, or liabilities (excluding extraordinary items) are at least 10% of the corresponding totals for all governmental or enterprise funds and at least 5% of the aggregate amount for all governmental and enterprise funds for the same item. The general fund is always considered a major fund. In addition to funds that meet the major fund criteria, any other governmental or enterprise fund that the Government believes is particularly important to the financial statements may be reported as a major fund.

All of the funds of the Government are divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental Funds

Governmental funds are accounted for using the modified accrual basis of accounting, which measures cash and other assets that can be readily converted to cash. The governmental funds statements provide a detailed short-term view of the PG’s general governmental operations and the basic services it provides. The reconciliation following the fund financial statements explains the differences between the governmental activities, reported in the government-wide financial statements, and the governmental funds’ financial statements. The General Fund, the PFA debt service fund and the PFA capital projects fund are reported as major governmental funds.

The General Fund is the PG's primary operating fund. It accounts for all financial resources of the PG, except those required to be accounted for in another fund.

The PFA debt service fund accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by the PFA on behalf of the Government.

The PFA capital projects fund accounts for bond proceeds of debt issued by the PFA on behalf of the Government. The bond proceeds have been designated for certain necessary public safety and capital development projects which are accounted for in this fund.

The governmental fund activities are reported in a separate balance sheet and statement of revenues, expenditures, and changes in fund balances. Additionally, the government presents a reconciliation of the statement of revenues, expenditures, and change in fund balances, to the statement of activities.

Proprietary Funds

Services provided to outside (nongovernmental) customers are reported in enterprise funds. Enterprise funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. These are the same business-type activities reported in the government-wide financial statements.

The West Indian Company (WICO) fund and the Unemployment Insurance Fund are major proprietary funds.

The WICO fund accounts for the activities of WICO, which owns a port facility including a cruise ship pier, and manages a shopping mall complex on the island of St. Thomas.

The Unemployment Insurance Fund is a federally mandated program to manage unemployment insurance.

The proprietary fund activities are reported in a separate statement of net assets (deficit), statement of revenues, expenditures, and changes in fund net assets (deficit) and statement of cash flows.

Fiduciary Funds

The fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets.

Financial Analysis of the Government as a Whole

The PG and its component units continue to experience a downturn in the economy following the economic recession of 2008.

The Government has initiated several actions to offset the negative impact of these financial challenges. The Government continues to promote environmentally safe industries into the USVI. The Government is participating in the American Recovery and Reinvestment Act, obtaining federal grants for energy, health, education and other construction projects, and other federal tax initiatives such as the Making Work Pay and Additional Child tax credits. To improve cash flow, the PG overhauled the property tax assessment and valuation systems of the Territory, proposed increases to locally assessed taxes, initiated tax compliance programs, and enacted expenditure reduction initiatives.

In fiscal year 2012, the Government issued the Series 2012A Working Capital Revenue Bonds in the amount of $142.6 million, to provide working capital for various operating expenses due to deficits. The Government issued the 2011 Property Tax Revenue Anticipation Note in the amount of $13.0 million to pay incentive payments to government employees that elected to retire early under the Economic Stability Act enacted by the Virgin Islands Legislature in 2010. The Government also borrowed $15.1 million from the U.S. Treasury to fund deficits in the Virgin Islands Unemployment Trust Fund.

Financial Analysis of the Primary Government

Total assets of the PG as of September 30, 2012 and 2011, were approximately $1.9 billion and $1.8 billion, respectively. Total liabilities as of September 30, 2012 and 2011, were approximately $3.3 billion and $3.0 billion, respectively.

As of September 30, 2012, the PG net deficit of $1.4 billion consisted of $178.4 million invested in capital assets, net of related debt; $226.9 million restricted by statute or other legal requirements that were not available to finance day-to-day operations of the Government; and an unrestricted net deficit of $1.8 billion. As of September 30, 2011, the PG net deficit of $1.2 billion consisted of $256.9 million invested in capital assets, net of related debt; $218.0 million restricted by statute or other legal requirements that were not available to finance day-to-day operations of the Government; and an unrestricted net deficit of $1.7 billion.

For the fiscal year ended September 30, 2012, the PG earned program and general revenue amounting to $1.2 billion and reported expenses of $1.4 billion, resulting in an increase in net deficit of $167.0 million.

For the fiscal year ended September 30, 2011, the PG earned program and general revenue amounting to $1.2 billion and reported expenses of $1.4 billion, resulting in an increase in net deficit of $218.7 million.

Overall, revenue increased by approximately $40 million in fiscal 2012, when compared to fiscal 2011, mainly due to increases in tax revenues of $96.1 million an increase in charges for services and interest and other of $39.7 million, offset by a decrease in federal grant revenues of $95.8 million. Increases in tax revenues mainly included rum excise taxes (matching funds) of $40.0 million and income taxes of $19.4 million. Expenses decreased in fiscal 2012 by $14.1 million when compared to fiscal 2011, mainly due to decreases in health and education expenses due to budgetary controls and employees electing early retirement.

A summary of net assets (deficit) and changes in net assets (deficit) for the primary government follows:

Net Assets (Deficit) – Primary Government

September 30, 2012 and 2011
(In thousands)

	Governmental activities		Business-type activities		Total	
	2012	**2011**	**2012**	**2011**	**2012**	**2011**
Assets						
Current assets	**$ 984,766**	$ 957,705	**$ 5,793**	$ (4,903)	**$ 990,559**	$ 952,802
Capital assets	**753,059**	749,156	**69,183**	56,006	**822,242**	805,162
Other assets	**41,743**	40,289	**66**	82	**41,809**	40,371
Total assets	**1,779,568**	1,747,150	**75,042**	51,185	**1,854,610**	1,798,335
Liabilities						
Long-term debt outstanding	**2,616,014**	2,422,939	**35,145**	37,539	**2,651,159**	2,460,478
Other liabilities	**500,106**	515,590	**101,255**	55,549	**601,361**	571,139
Total liabilities	**3,116,120**	2,938,529	**136,400**	93,088	**3,252,520**	3,031,617
Net Assets						
Invested in capital assets, net of related debt	**138,617**	223,155	**39,849**	33,830	**178,466**	256,985
Restricted	**221,897**	216,015	**5,098**	2,078	**226,995**	218,093
Unrestricted	**(1,697,066)**	(1,630,549)	**(106,305)**	(77,811)	**(1,803,371)**	(1,708,360)
Total net assets (deficit)	**$ (1,336,552)**	$ (1,191,379)	**$ (61,358)**	$ (41,903)	**$ (1,397,910)**	$ (1,233,282)

Changes in Net Assets (Deficit) - Primary Government

September 30, 2012 and 2011

(In thousands)

	Governmental Activities		Business-type Activities		Total	
	2012	**2011**	**2012**	**2011**	**2012**	**2011**
Revenue:						
Program revenue:						
Charges for services	**$ 38,932**	$ 35,632	**$ 61,144**	$ 50,069	**$ 100,076**	$ 85,701
Operating grants and contributions	**281,100**	377,727	**23,294**	14,701	**304,394**	392,428
Capital grants and contributions	**25,157**	40,688	**7,742**	–	**32,899**	40,688
General revenue:						
Taxes	**780,315**	684,199	**–**	–	**780,315**	684,199
Interest and other	**46,933**	21,652	**142**	81	**47,075**	21,733
Other general revenue	**2,134**	2,124	**–**	–	**2,134**	2,124
Total revenue	**1,174,571**	1,162,022	**92,322**	64,851	**1,266,893**	1,226,873
Expenses:						
General government	**626,050**	498,250	**–**	–	**626,050**	498,250
Public safety	**56,251**	68,166	**–**	–	**56,251**	68,166
Health	**97,590**	143,558	**–**	–	**97,590**	143,558
Public housing and welfare	**138,589**	142,146	**–**	–	**138,589**	142,146
Education	**236,612**	298,610	**–**	–	**236,612**	298,610
Transportation and communication	**54,991**	86,505	**–**	–	**54,991**	86,505
Culture and recreation	**7,356**	12,252	**–**	–	**7,356**	12,252
Interest on long-term debt	**103,005**	99,340	**–**	–	**103,005**	99,340
Unemployment insurance	**–**	–	**57,407**	40,785	**57,407**	40,785
West Indian Company	**–**	–	**8,983**	9,779	**8,983**	9,779
Workmen's compensation	**–**	–	**14,790**	13,223	**14,790**	13,223
VI Lottery	**–**	–	**15,150**	20,256	**15,150**	20,256
Other	**–**	–	**14,747**	12,724	**14,747**	12,724
Total expenses	**1,320,444**	1,348,827	**111,077**	96,767	**1,431,521**	1,445,594
Changes in net assets (deficit) before transfers	**(145,873)**	(186,805)	**(18,755)**	(31,916)	**(164,628)**	(218,721)
Transfers	**700**	700	**(700)**	(700)	**–**	–
	700	700	**(700)**	(700)	**–**	–
Change in net deficit	**(145,173)**	(186,105)	**(19,455)**	(32,616)	**(164,628)**	(218,721)
Net assets (deficit) at beginning of year, as restated	**(1,191,379)**	(1,005,274)	**(41,903)**	(9,287)	**(1,233,282)**	(1,014,561)
Net assets (deficit) at end of year	**$ (1,336,552)**	$ (1,191,379)	**$ (61,358)**	$ (41,903)	**$ (1,397,910)**	$ (1,233,282)

The Virgin Islands Office of Management and Budget of the PG prepares an annual executive budget subject to approval by the Governor and the Legislature of the Virgin Islands. The executive budget is prepared on a budgetary basis similar to the cash basis of accounting. The executive budget includes only those funds that are subject to appropriation by law. More information regarding budgetary procedures is provided in Note 3 of the basic financial statements. A summary of the budgetary report for the General Fund of the PG, included on page 26 of the financial statements, follows:

Revenue and Expenditures – Budget and Actual – Budgetary Basis – General Fund

Year Ended September 30, 2012
(In thousands)

	Original Budget	Amended Budget	Actual	Variance
Total revenues	$ 601,361	$ 601,361	$ 668,812	$ 67,451
Total expenditures	682,710	730,069	784,148	(54,079)
Deficiency of revenues over expenditures	(81,349)	(128,708)	(115,336)	13,372
Other financing sources, net	128,708	128,708	228,131	99,423
Excess (Deficiency) of revenues and net other financing sources over expenditures	$ 47,359	$ –	$ 112,795	$ 112,795

For fiscal 2012, the general fund realized a favorable budgetary variance of $112.80 million mainly due to the general government function of government. The general fund realized a positive revenue variance of $67.4 million due to an increase in tax revenues and federal grants and contributions. The PG realized an unfavorable expenditure variance of $54.1 million due to increases in general government expenditures.

Capital Assets

Capital assets additions during fiscal 2012 amounted to $36.3 million for governmental activities and $17.6 million for business-type activities.

Capital assets additions during fiscal 2011 amounted to $39.5 million for governmental activities and $18.6 million for business-type activities.

The Government's capital assets include land, land improvements, buildings, building improvements, machinery and equipment, infrastructure, construction in progress, and intangibles as follows:

Capital Assets – Primary Government
(In thousands)

	Governmental Activities		Business-type Activities		Total	
	2012	**2011**	**2012**	**2011**	**2012**	**2011**
Land and improvements	**$ 198,342**	$ 198,240	**$ 5,495**	$ 5,495	**$ 203,837**	$ 203,735
Building and improvements	**440,906**	410,954	**67,517**	66,434	**508,423**	477,388
Machinery and equipment	**156,472**	141,198	**11,766**	11,213	**168,238**	152,411
Infrastructure	**240,167**	223,884	**–**	–	**240,167**	223,884
Construction in progress	**102,467**	127,735	**12,303**	5,661	**114,770**	133,396
Intangible	**–**	–	**8,064**	–	**8,064**	–
Total capital assets	**1,138,354**	1,102,011	**105,145**	88,803	**1,243,499**	1,190,814
Less accumulated depreciation	**(385,295)**	(352,855)	**(35,962)**	(32,797)	**(421,257)**	(385,652)
Total capital assets, net	**$ 753,059**	$ 749,156	**$ 69,183**	$ 56,006	**$ 822,242**	$ 805,162

Note 10 provides detailed information regarding the capital assets of the primary government and the component units of the Government.

Debt Administration

The Government issues both general obligation bonds and revenue bonds. The Revised Organic Act [48 U.S.C. Section 1574 (b)(ii)] restricts the principal amount of general obligation debt that the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the U.S. Virgin Islands. Following is a summary of bonds outstanding as of September 30, 2012:

Primary Government – Bonds Payable

(In thousands)

Bonds Payable	Maturity	Rates (%)	Balance
2012 Series A Revenue Bonds	2032	4.00 - 5.00	$ 142,640
2010 Series A & B Revenue Bonds	2029	4.00 - 5.25	399,050
2009 Series A Revenue Bonds (Cruzan)	2039	3.00 - 6.00	38,075
2009 Series A-1, A-2, B & C Revenue and Refunding Bonds	2040	3.00 - 5.00	420,730
2009 Series A Revenue Bonds (Diageo)	2038	6.00 - 6.75	250,000
2006 Series A Revenue Bonds	2029	3.50 - 5.00	211,680
2006 Series A,B,C & D Tobacco Turbo and Capital Appreciation Bonds	2035	6.25 - 7.625	7,290
2004 Series A Revenue Bonds	2025	4.00 - 5.25	71,430
2003 Series A Revenue Bonds	2033	4.00 - 5.25	245,325
2001 Series A Tobacco Bonds	2031	5.00	14,180
1999 Series A Revenue Bonds	2020	4.20 - 6.50	74,165
Subtotal			1,874,565
Plus (less):			
Deferred costs on refundings			(14,126)
Bond premium			35,499
Bond discount			(4,728)
Bond accretion			3,794
Total			$ 1,895,004

Note 11 provides detailed information regarding all bonds of the PG.

In fiscal year 2012, the Government issued the 1) 2012A Working Capital Revenue Bonds in the amount of $142.6 million, to provide working capital for various operating expenses, 2) the 2011 Property Tax Revenue Anticipation Note in the amount of $13.0 million, the proceeds of which was used to pay incentive payments to government employees that elected to retire early under the Economic Stability Act enacted by the Virgin Islands Legislature in 2010, and 3) an additional $1.6 million to a private developer in St. Croix under the 2009A Tax Increment Note. During fiscal year 2012, the Government also borrowed $15.1 million from the U.S. Treasury to fund deficits in the Virgin Islands Unemployment Trust Fund.

In fiscal year 2011, the Government issued the: 1) 2010A Working Capital Notes in the amount of $131.4 million to pay the outstanding balance of the 2009B Working Capital Notes of $6.4 million, and to provide $125.0 million in working capital for various operating expenses, 2) the Series 2011A Gross Receipts Tax Loan Notes in the amount of $32.2 million to upgrade the territory's broadband technology infrastructure and equipment, and 3) an additional $4.0 million to a private developer in St. Croix under the 2009A Tax Increment Note. During fiscal year 2011, the Government also borrowed $10.4 million from the U.S. Treasury to fund deficits in the Virgin Islands Unemployment Trust Fund.

The PG made bond principal payments on all outstanding general and special revenue bonds amounting to $48.6 million during fiscal year 2012, and $25.5 million during fiscal year 2011.

The Government's bonds secured by pledged rum excise taxes (matching funds) carry insured ratings of "BBB" and "BBB-" from Fitch Ratings and "BBB" from Standard & Poor's, respectively as of the date of this report. The Government's bonds secured by gross receipts taxes carry insured ratings of "BBB" and "BBB-"from Fitch Ratings and BBB+ from Standard & Poor's. Bond ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained from the respective rating agency.

Other liabilities of the PG include:

Primary Government – Other Liabilities

September 30, 2012 and 2011
(In millions)

	2012	2011
Accrued compensated absences	$ 73	$ 59
Accrued arbitrage rebates	14	–
Retroactive union arbitration	195	195
Litigation	12	27
Post employment benefits	246	201
Landfill closure and post closure costs	72	72
Worker's compensation	27	20
Total other liabilities	$ 639	$ 574

Economic Condition and Outlook

The PG continues its recovery efforts from the economic recession of 2008 through a combination of revenue initiatives and budgetary restraint on expenditures.

Revenue Initiatives

The PG has implemented several initiatives to create jobs and promote economic growth including: providing economic incentives to attract a major rum distiller (Diageo) and retain another rum distiller (Cruzan Rum), enactment of tax increment financing legislation, implementation of a broadband infrastructure initiative, continued promotion of tourism through national advertising. The PG has also implemented several tax initiatives to promote tax compliance and tax collection. A successful initiative was the "Operation Last Chance" income tax collection initiative. Delinquent taxpayers were provided an amnesty of penalty and interest to become current in tax filings. The PG has also legislated increases in local taxes, including gross receipts taxes, hotel taxes and stamp taxes.

In connection with a real property tax case instituted against the PG in the U.S. District Court of the Virgin Islands, the PG was enjoined from appraising and assessing any real property taxes until it modified its system of appraisal to comply with certain court mandates. The PG retained a consultant to modify its system of appraisal and to perform reassessment of properties. This project was completed in fiscal 2009. The U.S. District Court also required an over-haul of the tax review board responsible for hearing tax assessment reviews. The PG complied with all court orders and in 2013 became current in the issuance of property tax assessments.

The Government is currently in litigation challenging the computation of its corporate franchise tax. Of the four cases brought against the Government, one is currently before the Virgin Islands Territorial Court, and the remaining three cases are on appeal.

Budgetary Control of Expenditures

The PG faces the challenge of carry-forward liabilities from prior fiscal years and the loss of federal grant revenues with the closing of the American Recovery and Reinvestment (ARRA) grant program.

Carry-forward liabilities consist mainly of retroactive salary increases, which accumulated following Hurricanes Hugo, Marilyn and Bertha in the years of 1990 through 1998. At September 30, 2012 and 2011, unpaid retroactive salary increase liabilities amounted to $195.2 million respectively, reported as a liability of the Government within other noncurrent liabilities.

Federal grant program revenues returned to pre-ARRA levels in fiscal year 2012, a reduction of $139.9 million.

The PG faces the challenge of funding pension and other post-employment benefits for retirees. In September 2011, the Department of Interior issued an evaluation report that the Government's pension plan may be unable to fulfill its responsibilities in fourteen to seventeen years. In addition to pension liabilities, the actuarial estimate of post-employment liabilities (mainly health insurance for retirees) was $1.1 billion as of September 30, 2012. The PG has enacted a Pension Reform Joint Task Force to provide recommendations to the Legislature to meet these challenges. Recommendations provided to the Legislature in May 2013 by the Task Force included: (1) increasing retirement age, (2) restructuring of benefits, and (3) no longer allowing retirees to both work and collect benefits from the PG.

Deficit Reduction Measures

In fiscal year 2012, the PG reported an unrestricted net deficit of $1.8 billion. In fiscal year 2011, the PG reported an unrestricted net deficit of $1.7 billion.

The PG has implemented a number of deficit reducing measures including: (i) withholding of local gross receipts taxes on Government invoice payments, (ii) increasing local taxes such as property tax assessments on time-shares, gross receipts taxes and hotel taxes; (iii) exerting greater control of expenditures through the budgetary process, and (iv) increasing collection efforts for amounts due to the PG from taxpayers.

Contacting the Government's Financial Management

This financial report is designed to provide the Government's citizens, taxpayers, customers, and creditors with a general overview of the Government's finances. If you have questions about this report, or need additional financial information, contact the Government of the United States Virgin Islands, Department of Finance, No. 2314 Kronprindsens Gade, St. Thomas, VI 00802.

Government of the United States Virgin Islands

Statement of Net Assets (Deficit)

September 30, 2012

(In thousands)

	Primary Government			
	Governmental Activities	Business-type Activities	Total	Component Units
Assets				
Cash and cash equivalents	$ 159,611	$ 17,834	$ 177,445	$ 82,886
Investments	518,132	2,002	520,134	10,732
Receivables, net	227,561	3,082	230,643	63,856
Internal balances	29,865	(29,865)	–	–
Due from component units	4,380	–	4,380	–
Notes and other receivables	–	–	–	9,077
Due from primary government	–	–	–	34,258
Due from federal government	44,789	2,044	46,833	9,987
Inventories	–	–	–	28,808
Other assets	34	5,599	5,633	58,528
Restricted:				
Cash and cash equivalents	394	5,097	5,491	70,421
Investments	–	–	–	80,971
Other	–	–	–	27,026
Capital assets, net	753,059	69,183	822,242	997,253
Deferred expenses and other assets	41,743	66	41,809	66,983
Total assets	1,779,568	75,042	1,854,610	1,540,786
Liabilities				
Accounts payable and accrued liabilities	79,926	9,418	89,344	146,400
Tax refunds payable	59,560	–	59,560	–
Unemployment insurance benefits	–	35,118	35,118	–
Customer deposits	–	–	–	24,483
Due to primary government	–	–	–	4,380
Due to component units	34,258	–	34,258	–
Due to federal government	–	–	–	5,906
Interest payable	47,047	590	47,637	6,164
Unearned revenue	186,120	1,102	187,222	8,450
Other current liabilities	10,607	–	10,607	27,090
Noncurrent liabilities:				
Due within one year:				
Notes payable	9,810	42,280	52,090	13,051
Bonds payable	49,995	–	49,995	14,015
Other liabilities	22,783	12,747	35,530	590
Due in more than one year:				
Line of credit payable	–	–	–	19,375
Notes payable	181,612	21,231	202,843	53,809
Bonds payable	1,845,009	–	1,845,009	308,457
Other liabilities	589,393	13,914	603,307	80,469
Total liabilities	3,116,120	136,400	3,252,520	712,639

(Continued)

Government of the United States Virgin Islands

Statement of Net Assets (Deficit) (continued)

September 30, 2012
(In thousands)

	Primary Government			
	Governmental Activities	**Business-type Activities**	**Total**	**Component Units**
Net assets (deficit)				
Invested in capital assets, net of related debt	$ 138,617	$ 39,849	$ 178,466	$ 744,100
Restricted for:				
Unemployment insurance	–	3,147	3,147	–
Debt service	221,503	1,951	223,454	–
Capital projects	394	–	394	–
Other purposes	–	–	–	160,823
Unrestricted	(1,697,066)	(106,305)	(1,803,371)	(76,776)
Total net assets (deficit)	$ (1,336,552)	$ (61,358)	$ (1,397,910)	$ 828,147

See accompanying notes.

Government of the United States Virgin Islands

Statement of Activities

Year Ended September 30, 2012

(In thousands)

		Program Revenues			Net Revenue (Expense) and Changes in Net Assets			
					Primary Government			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total	Component Units
Functions:								
Primary government:								
Governmental activities:								
General government	$ 626,050	$ 34,788	$ 90,240	$ 4,846	$ (496,176)	$ –	$ (496,176)	$ –
Public safety	56,251	865	2,375	544	(52,467)	–	(52,467)	–
Health	97,590	585	29,554	–	(67,451)	–	(67,451)	–
Public housing and welfare	138,589	523	87,332	–	(50,734)	–	(50,734)	–
Education	236,612	176	68,382	–	(168,054)	–	(168,054)	–
Transportation and communication	54,991	495	3,064	19,767	(31,665)	–	(31,665)	–
Culture and recreation	7,356	1,500	153	–	(5,703)	–	(5,703)	–
Interest on long-term debt	103,005	–	–	–	(103,005)	–	(103,005)	–
Total governmental activities	1,320,444	38,932	281,100	25,157	(975,255)	–	(975,255)	–
Business-type activities:								
Unemployment insurance	57,407	4,180	20,995	–	–	(32,232)	(32,232)	–
West Indian Company	8,983	8,574	–	40	–	(369)	(369)	–
Workmen’s compensation	14,790	17,576	–	–	–	2,786	2,786	–
VI Lottery	15,150	19,105	–	–	–	3,955	3,955	–
Other	14,747	11,709	2,299	7,702	–	6,963	6,963	–
Total business-type activities	111,077	61,144	23,294	7,742	–	(18,897)	(18,897)	–
Total primary government	$ 1,431,521	$ 100,076	$ 304,394	$ 32,899	(975,255)	(18,897)	(994,152)	–
Component units:								
Virgin Islands Housing Authority	$ 58,654	$ 6,472	$ 39,398	$ 13,113	–	–	–	329
Virgin Islands Port Authority	59,528	47,230	–	5,298	–	–	–	(7,000)
Virgin Islands Water and Power Authority:								
Electric system	363,961	331,414	–	1,951	–	–	–	(30,596)
Water system	25,531	34,624	–	5,947	–	–	–	15,040
Virgin Islands Government Hospital and Health Facilities Corporation:								
Roy L. Schneider Hospital	89,874	56,661	23,310	–	–	–	–	(9,903)
Juan F. Luis Hospital	86,726	48,401	25,611	–	–	–	–	(12,714)
University of the Virgin Islands	80,450	18,676	54,153	3,992	–	–	–	(3,629)
Other component units	68,080	9,744	60,847	17,442	–	–	–	19,953
Total component units	$ 832,804	$ 553,222	$ 203,319	$ 47,743	–	–	–	(28,520)
Total primary government and component units					(975,255)	(18,897)	(994,152)	(28,520)

(continued)

Government of the United States Virgin Islands

Statement of Activities (continued)

Year Ended September 30, 2012
(In thousands)

	Net Revenue (Expense) and Changes in Net Assets			
	Primary Government			
	Governmental Activities	Business-type Activities	Total	Component Units
General revenues:				
Taxes	780,315	–	780,315	–
Interest and other	46,933	142	47,075	33,526
Tobacco settlement rights	2,134	–	2,134	–
Transfers – internal activities of primary government	700	(700)	–	–
Forgiveness of debt	–	–	–	86,301
Total general revenue	830,082	(558)	829,524	119,827
Changes in net assets (deficit)	(145,173)	(19,455)	(167,041)	91,307
Net assets (deficit), beginning of year, as restated	(1,191,379)	(41,903)	(1,233,282)	736,840
Net assets (deficit), end of year	$ (1,336,552)	$ (61,358)	$ (1,397,910)	$ 828,147

See accompanying notes.

Government of the United States Virgin Islands

Balance Sheet – Governmental Funds

September 30, 2012
(In thousands)

	General	PFA Debt Service	PFA Capital Projects	Other Governmental	Total Governmental
Assets					
Cash and cash equivalents	$ 79,525	$ 3,214	$ 24,790	$ 52,476	$ 160,005
Investments	158,064	305,435	49,471	5,161	518,131
Receivables:					
Taxes, net	181,272	44,532	–	–	225,804
Accrued interest and other	19	–	–	137	156
Due from:					
Other funds	17,230	–	24,275	21,192	62,697
Component units, net	4,380	–	–	–	4,380
Federal government	–	–	–	44,789	44,789
Total assets	$ 440,490	$ 353,181	$ 98,536	$ 123,755	$ 1,015,962
Liabilities and Fund Balances					
Accounts payable and accrued liabilities	$ 59,894	$ 326	$ 10	$ 19,696	$ 79,926
Tax refunds payable	59,560	–	–	–	59,560
Due to:					
Other funds	18,376	1,426	–	13,030	32,832
Component units	34,258	–	–	–	34,258
Deferred revenue	240,345	129,926	–	4,886	375,157
Other current liabilities	7,607	–	1,140	1,858	10,605
Total liabilities	420,040	131,678	1,150	39,470	592,338
Fund balances:					
Restricted	–	221,503	97,386	19,557	338,446
Committed	29,099	–	–	20,757	49,856
Assigned	–	–	–	43,971	43,971
Unassigned	(8,649)	–	–	–	(8,649)
Total fund balances	20,450	221,503	97,386	84,285	423,624
Total liabilities and fund balances	$ 440,490	$ 353,181	$ 98,536	$ 123,755	

Amounts reported for governmental activities in the statement of net assets (deficit) are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	753,059
Expenditures identified as related to a future, period recognized as a prepaid asset in the statement of net assets.	34
Deferred bond issue costs are not financial resources and, therefore, are not reported in the funds.	41,743
Other long-term assets, primarily taxes receivable, will not be available to pay for current period expenditures and, therefore, are deferred in the funds	190,637
Interest on long-term debt is not accrued in the funds, but rather is recognized as an expenditure when due.	(47,047)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.	(2,698,602)
Deficit of governmental activities	$ (1,336,552)

See accompanying notes.

Government of the United States Virgin Islands

Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds

Year Ended September 30, 2012
(In thousands)

	General	PFA Debt Service	PFA Capital Projects	Other Governmental	Total Governmental
Revenues:					
Taxes	$ 598,762	$ 221,224	$ 1,847	$ 17,658	$ 839,491
Federal grants and contributions	24,058	–	–	282,202	306,260
Charges for services	22,071	–	–	12,389	34,460
Tobacco settlement rights	–	–	–	2,134	2,134
Interest and other	23,921	3,322	82	19,609	46,934
Total revenues	668,812	224,546	1,929	333,992	1,229,279
Expenditures:					
Current:					
General government	423,956	82	17,573	93,699	535,310
Public safety	51,036	–	–	3,392	54,428
Health	61,835	–	–	34,772	96,607
Public housing and welfare	54,457	–	–	83,765	138,222
Education	165,523	–	–	65,187	230,710
Transportation and communication	20,795	–	–	26,622	47,417
Culture and recreation	6,546	–	–	388	6,934
Capital outlays	7,878	–	13,545	20,474	41,897
Debt service:					
Principal	2,859	49,629	1,554	1,365	55,407
Interest	7,771	94,894	293	771	103,729
Total expenditures	802,656	144,605	32,965	330,435	1,310,661
Excess (deficiency) of revenue over expenditures	(133,844)	79,941	(31,036)	3,557	(81,382)
Other financing sources (uses):					
Bonds issued	130,000	12,640	–	–	142,640
Loans issued	13,000	143	1,525	–	14,668
Bond premiums	–	5,628	–	–	5,628
Bond discounts and issuance costs	–	(3,442)	–	–	(3,442)
Transfers from other funds	100,158	11,240	4,000	8,331	123,729
Transfers to other funds	(15,027)	(99,390)	(4,612)	(4,000)	(123,029)
Total other financing sources (uses), net	228,131	(73,181)	913	4,331	160,194
Net change in fund balances	94,287	6,760	(30,123)	7,888	78,812
Fund balance at beginning of year	(73,837)	214,743	127,509	76,397	344,812
Fund balance at end of year	$ 20,450	$ 221,503	$ 97,386	$ 84,285	$ 423,624

See accompanying notes.

Government of the United States Virgin Islands

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities – Governmental Funds

Year Ended September 30, 2012
(In thousands)

Net change in fund balances – total governmental funds	$	78,812
Government funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current year.		3,935
Tax revenue in the statement of activities, which do not provide current financial resources, are not reported as revenue in the funds.		(59,176)
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of the governmental funds. This is the amount by which debt loan and bond proceeds of $157.3 million exceeded debt repayments of $55.4 million.		(101,901)
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 governmental funds. This is the amount by which the increase in certain liabilities reported in the statement of net assets of the previous year increased expenses reported in the statement of activities that do not require the use of current financial resources.		(57,985)
Some expenses reported as prepaid assets in the statement of net assets in the prior year are recognized as expenses in the current year in the statement of activities.		(4,583)
Bond issue costs are expended in the governmental funds when paid, and are capitalized and amortized in the statement of activities. This is the amount of bond issuance costs amortized in the statement of activities.		1,455
Bond premiums and discounts are reported as other financing sources and uses in the governmental funds when the bonds are issued, and are capitalized and amortized in the government-wide financial statements. This amount represents additional net interest expense reported in the statement of activities related to the amortization of premiums, discounts deferred refunding loss, and accreted interest on capital appreciation bonds during the current year.		(6,455)
Certain interest reported in the statement of activities does not require the use of current financial resources and therefore is not reported as expenditures in the governmental funds. This amount represents the decrease in interest payable reported in the statement of net assets.		725
Change in net assets of governmental activities	$	(145,173)

See accompanying notes.

Government of the United States Virgin Islands

Statement of Revenues and Expenditures – Budget and Actual – Budgetary Basis – General Fund

Year Ended September 30, 2012
(In thousands)

	Original Budget	Amended Budget	Actual	Variance
Revenues:				
Taxes	$ 566,621	$ 566,621	$ 598,762	$ 32,141
Federal grants and contributions	–	–	24,058	24,058
Charges for services	12,425	12,425	22,071	9,646
Interest and other	22,315	22,315	23,921	1,606
Total revenues	601,361	601,361	668,812	67,451
Expenditures:				
Current:				
General government	139,128	185,008	423,956	(238,948)
Public safety	131,664	131,662	51,036	80,626
Health	81,730	81,780	61,835	19,945
Public housing and welfare	62,008	62,008	54,457	7,551
Education	212,005	213,436	165,523	47,913
Transportation and communication	34,402	34,402	20,795	13,607
Culture and recreation	21,773	21,773	6,546	15,227
Total expenditures	682,710	730,069	784,148	(54,079)
Deficiency of revenues over expenditures	(81,349)	(128,708)	(115,336)	13,372
Other financing sources (uses):				
Bonds Issued	–	–	130,000	130,000
Loans Issued	–	–	13,000	13,000
Transfers from other funds	129,900	129,900	100,158	(29,742)
Transfer to other funds	(1,192)	(1,192)	(15,027)	(13,835)
Total other financing sources, net	128,708	128,708	228,131	99,423
Excess (deficiency) of revenues and net other financing sources over expenditures	$ 47,359	$ –	$ 112,795	$ 112,795

See accompanying notes.

Government of the United States Virgin Islands

Statement of Net Assets (Deficit) – Proprietary Funds

September 30, 2012
(In thousands)

	Business-type Activities – Enterprise Funds			
	West Indian Company	Unemployment Insurance	Other Enterprise	Totals
Assets				
Current assets:				
Cash and cash equivalents	$ 1,107	$ 834	$ 15,893	$ 17,834
Investments at fair value	–	–	2,002	2,002
Receivables, net:				
Premiums receivable	–	1,045	–	1,045
Other receivables	749	–	1,288	2,037
Due from:				
Other funds	–	–	739	739
Federal government			2,044	2,044
Other assets	658	–	4,941	5,599
Total current assets	2,514	1,879	26,907	31,300
Noncurrent assets:				
Restricted cash and cash equivalents	1,951	3,146	–	5,097
Capital assets	38,451	–	30,732	69,183
Deferred expenses	66	–	–	66
Total noncurrent assets	40,468	3,146	30,732	74,346
Total assets	42,982	5,025	57,639	105,646
Liabilities				
Current liabilities:				
Accounts payable and accrued liabilities	1,538	590	7,880	10,008
Due to other funds	4,000	–	26,604	30,604
Unemployment insurance benefits	–	35,118	–	35,118
Unearned revenue	–	–	1,102	1,102
Workers compensation	–	–	12,747	12,747
Loan payable to U.S. Treasury	–	41,747	–	41,747
Loans payable related to capital assets	533	–	–	533
Total current liabilities	6,071	77,455	48,333	131,859
Noncurrent liabilities:				
Workers compensation	–	–	13,914	13,914
Loans payable related to capital assets	21,231	–	–	21,231
Total noncurrent liabilities	21,231	–	13,914	35,145
Total liabilities	27,302	77,455	62,247	167,004
Net assets (deficit)				
Invested in capital assets, net of related debt	16,753	–	23,096	39,849
Restricted	1,951	3,146	–	5,097
Unrestricted	(3,024)	(75,576)	(27,704)	(106,304)
Total net assets (deficit)	$ 15,680	$ (72,430)	$ (4,608)	$ (61,358)

See accompanying notes.

Government of the United States Virgin Islands

Statement of Revenues, Expenses, and Changes in Fund Net Assets (Deficit) – Proprietary Funds

Year Ended September 30, 2012
(In thousands)

	Business-type Activities – Enterprise Funds			
	West Indian Company	**Unemployment Insurance**	**Other Enterprise**	**Total**
Operating revenues:				
Charges for services	$ 8,574	$ 4,180	$ 48,390	$ 61,144
Total operating revenues	8,574	4,180	48,390	61,144
Operating expenses:				
Cost of services	5,622	57,386	43,052	106,060
Amortization	–	–	454	454
Depreciation	1,923	–	1,175	3,098
Total operating expenses	7,545	57,386	44,681	109,612
Operating income (loss)	1,029	(53,206)	3,709	(48,468)
Non-operating revenues (expenses):				
Federal grants	40	20,995	10,001	31,036
Interest and other income	32	38	72	142
Interest expense	(1,437)	(21)	(7)	(1,465)
Total non-operating revenues (expenses), net	(1,365)	21,012	10,066	29,713
(Loss) Income before operating transfers	(336)	(32,194)	13,775	(18,755)
Transfers to other funds	(700)	–	–	(700)
Change in net assets	(1,036)	(32,194)	13,775	(19,455)
Net assets at beginning of year	16,716	(40,236)	(18,383)	(41,903)
Net assets (deficit) at end of year	$ 15,680	$ (72,430)	$ (4,608)	$ (61,358)

See accompanying notes.

Government of the United States Virgin Islands

Statement of Cash Flows – Proprietary Funds

Year Ended September 30, 2012

(In thousands)

	Business-type Activities – Enterprise Funds			
	West Indian Company	Unemployment Insurance	Other Enterprise	Total
Cash flows from operating activities				
Receipts from customers and users	$ 8,108	$ 4,282	$ 48,890	$ 61,280
Payments to beneficiaries, suppliers and employees	(5,106)	(37,330)	(29,966)	(72,402)
Net cash provided by (used in) operating activities	3,002	(33,048)	18,924	(11,122)
Cash flows from noncapital financing activities				
Federal grants	40	20,995	10,001	31,036
Net cash provided by noncapital financing activities	40	20,995	10,001	31,036
Cash flows from capital and related financing activities				
Acquisition and construction of capital assets	(2,104)	–	(7,620)	(9,724)
Disposal of capital assets	13	–	762	775
Investment in intangible broadband assets	–	–	(8,064)	(8,064)
Issuance of long-term debt	–	15,126	–	15,126
Principal paid on long-term debt	(493)	–	–	(493)
Interest paid on long-term debt	(1,382)	(21)	(6)	(1,409)
Net cash provided by (used in) capital and related financing activities	(3,966)	15,105	(14,928)	(3,789)
Cash flows from investing activities				
Interest on investments	20	38	71	129
Sale of investments	–	–	376	376
Net cash provided by investing activities	20	38	447	505
Net decrease in cash and cash equivalents	(904)	3,090	14,444	16,630
Cash and cash equivalents at beginning of year	3,962	890	1,449	6,301
Cash and cash equivalents at end of year	$ 3,058	$ 3,980	$ 15,893	$ 22,931
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities				
Operating income (loss)	$ 1,029	$ (53,206)	$ 3,709	$ (48,468)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:				
Provision for doubtful accounts	164	–	–	164
Depreciation and amortization	1,923	–	1,629	3,552
Impairment	92	–	–	92
Change in assets and liabilities:				
Receivables, net	(477)	102	(5)	(380)
Due from federal government	–	–	(2,044)	(2,044)
Unearned revenue	–	–	505	505
Other assets	96	–	(4,783)	(4,687)
Accounts payable and accrued liabilities	175	–	1,539	1,714
Unemployment insurance benefits	–	20,056	–	20,056
Workers compensation	–	–	6,319	6,319
Due to other funds	–	–	12,055	12,055
Net cash provided by (used in) operating activities	$ 3,002	$ (33,048)	$ 18,924	$ (11,122)
Reconciliation of cash and cash equivalents to the statement of net assets				
Cash and cash equivalents – current	$ 1,107	$ 834	$ 15,893	$ 17,834
Cash and cash equivalents – restricted	1,951	3,146	–	5,097
Total cash and cash equivalents at end of year	$ 3,058	$ 3,980	$ 15,893	$ 22,931

See accompanying notes.

Government of the United States Virgin Islands

Statement of Fiduciary Net Assets – Fiduciary Funds

September 30, 2012
(In thousands)

	Pension Trust Fund	Agency Funds
Assets		
Cash and cash equivalents:		
Unrestricted	$ 103,438	$ 6,382
Restricted	14	–
Investments	1,178,880	3,062
Receivables, net:		
Loans and advances	143,806	–
Accrued interest	4,246	–
Other	2,996	–
Other assets	13,292	–
Total assets	1,446,672	9,444
Liabilities		
Accounts payable and accrued liabilities	–	6,382
Cash overdraft with bank	3,505	–
Unsettled securities purchased	2,848	–
Securities lending collateral	128,495	–
Other liabilities	10,486	3,062
Total liabilities	145,334	9,444
Net assets held in trust for employees' pension benefits	$ 1,301,338	$ –

See accompanying notes.

Government of the United States Virgin Islands

Statement of Changes in Fiduciary Net Assets - Fiduciary Funds

Year Ended September 30, 2012
(In thousands)

	Pension Trust Fund
Additions:	
Contributions:	
Employer	$ 66,677
Plan members	37,727
Total contributions	104,404
Investment income:	
Net appreciation of fair value of investments	143,062
Net depreciation of fair value of real estate	(704)
Interest, dividends, and other, net	33,027
Real estate – net rental income	2,761
	178,146
Less investment expense	5,038
Net investment income	173,108
Other income	1,421
Total additions	278,933
Deductions:	
Benefits paid	225,770
Refunds of contributions	7,327
Administrative and operational expenses	18,481
Total deductions	251,578
Change in net assets	27,355
Net assets, beginning of year	1,273,983
Net assets, end of year	$ 1,301,338

See accompanying notes.

1. Summary of Significant Accounting Policies

The Government of the United States Virgin Islands (the Government) is an unincorporated organized territory of the United States of America (United States). The powers of the Government are derived from and set forth in the Revised Organic Act of 1954, as amended. The Government assumes responsibility for public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.

The accompanying basic financial statements of the Government have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as prescribed by the *Governmental Accounting Standards Board* (GASB).

The accompanying basic financial statements have been prepared primarily from accounts maintained by the Department of Finance of the Government. Additional data has been derived from reports prepared by other departments, agencies, and public corporations based on independent or subsidiary accounting systems maintained by them.

Financial Reporting Entity

The Government follows the provisions of GASB Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. These standards require that the Government's financial reporting entity be defined according to specific criteria. According to the standard, for financial reporting purposes, the Government is a primary government (PG). The PG includes all Government departments, agencies, boards, and organizations that are not legally separate. In addition to the PG, the financial reporting entity includes blended and discretely presented component units. Component units include all legally separate organizations for which the Government's elected officials are financially accountable and other organizations for which the nature and significance of their relationship with the Government are such that exclusion would cause the basic financial statements to be misleading or incomplete. The criteria used to define financial accountability include appointment of a voting majority of an organization's governing body and (i) the ability of the PG to impose its will on that organization or (ii) the potential for the organization to provide specific financial benefits to or impose specific financial burdens on the PG.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

The financial statements of the following component units are included in the financial reporting entity either as blended or as discretely presented component units in accordance with GAAP:

(a) Blended Component Units

The following public benefit corporations, while legally separate from the Government, meet the criteria to be reported as part of the PG because they provide services entirely or almost entirely to the Government:

Virgin Islands Public Finance Authority (PFA)

PFA was created as a public corporation and autonomous governmental instrumentality by Act No. 5365, the Government Capital Improvement Act of 1988, with the purpose of aiding the Government in the performance of its fiscal duties and in effectively carrying out its governmental responsibility of raising capital for essential public projects. Under the enabling legislation, PFA has the power, among other matters, to borrow money and issue bonds and to lend the proceeds of its bonds to the Government or any governmental instrumentality. The powers of PFA are exercised by a board of directors consisting of the Governor (Chairperson), the Commissioner of Finance, the Director of the Office of Management and Budget, and two representatives of the private sector appointed by the Governor with the advice and consent of the USVI Legislature (the Legislature). PFA activities are blended within the PG because it is so intertwined with the Government that, in substance, they are the same. The PFA funds are reported as major funds, with the exception of PFA Special Revenue Fund, which is included in the other aggregate remaining fund information.

PFA has a component unit, the West Indian Company (WICO), which is presented as an enterprise fund in the Government's basic financial statements.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(a) Blended Component Units (continued)

Tobacco Settlement Financing Corporation (TSFC)

TSFC was created in September 2001 under Act No. 6428 as a separate and independent corporation of the Government to purchase the rights, title, and interest in tobacco settlement litigation awards and to issue revenue bonds supported by the tobacco settlement rights. The responsibility for the operations of TSFC is vested in a board of directors composed of three Government officials appointed by the Governor and two private citizens. The activities of TSFC are limited to activities conducted on behalf of the Government. The TSFC is reported in the other aggregate fund information.

Complete audited financial statements of the PFA and TSFC blended component units can be obtained directly by contacting their respective administrative offices:

Administrative Offices of Blended Component Units
Virgin Islands Public Finance Authority
32-33 Kongens Gade
St. Thomas, VI 00802

Tobacco Settlement Financing Corporation
32-33 Kongens Gade
St. Thomas, VI 00802

(b) Discretely Presented Component Units

The following component units, consistent with GASB Statements Nos. 14 and 39 are discretely presented in the basic financial statements because of the nature of the services they provide and the Government's ability to impose its will. The component units are reported in a separate column to emphasize that they are legally separate from the PG and governed by separate boards.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Major Component Units

Virgin Islands Housing Authority (VIHA)

VIHA was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act No. 903 on June 18, 1962, with the purpose of providing housing for low and moderate income families residing in the U.S. Virgin Islands. From June 1962 through August 2003, the powers of VIHA were exercised by a board of commissioners consisting of seven members. In August 2003, the U.S. Department of Housing and Urban Development (HUD) determined that because of the severity of compliance violations, VIHA was declared to be in substantial default of its annual contributions contract (ACC) dated July 12, 1996 with HUD. VIHA was placed in receivership and HUD assumed control of all assets, projects, and programs.

The Authority is governed by a board of commissioners which is autonomous to HUD. An executive director is appointed by the Authority's Board to manage the day-to-day operations of the Authority.

Given the nature of VIHA's operations and the significance of its relationship with the Government, management believes that its exclusion from the financial reporting entity would cause the Government's basic financial statements to be incomplete and misleading.

Virgin Islands Port Authority (VIPA)

VIPA was created as a body corporate and politic constituting a public corporation and autonomous government instrumentality by Act No. 2375 on December 23, 1968, with the purposes of owning, operating, and managing all types of air and marine terminals. The powers of VIPA are exercised by a board of governors consisting of the Commissioner of Economic Development and Agriculture (Chairperson), the Attorney General, the Commissioner of Public Works, the Director of the Small Business Development Agency, and five other persons appointed by the Governor with the advice and consent of the Legislature.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Major Component Units (continued)

Virgin Islands Water and Power Authority (WAPA)

WAPA was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act No. 1248 on August 13, 1964, with the purpose of operating the water production and electric generation plants in the U.S. Virgin Islands. The powers of WAPA are exercised by a governing board consisting of nine members, all appointed by the Governor with the advice and consent of the Legislature, from which three are heads of cabinet-level executive departments or agencies and six other persons, who shall not be employees of the Government. WAPA is required by its bond resolutions to maintain separate audited financial statements for each system (the Electric and Water Systems).

Virgin Islands Government Hospital and Health Facilities Corporation (VIGHHFC)

VIGHHFC was created by Act No. 6012 on August 23, 1994 and became active on May 1, 1999, with the purpose of providing healthcare services and hospital facilities to the people of the U. S. Virgin Islands. The powers of VIGHHFC are exercised by a board of directors consisting of 15 members as follows: the Director of the Office of Management and Budget, the Commissioner of Finance, and 13 other members appointed by the Governor with the advice and consent of the Legislature. The VIGHHFC is composed of the Roy L. Schneider Hospital located in St. Thomas and the Juan F. Luis Hospital and Medical Center located in St. Croix. Both entities issue separate audited financial statements. The Roy L. Schneider Hospital's financial statements include its component units: the Myra Keating Smith Community Health Center ("Health Center") of St. John and the Charlotte Kimelman Cancer Institute ("Cancer Institute") on St. Thomas. The Health Center and Cancer Institute are legally separated organizations for which the Roy L. Schneider Hospital is financially accountable. The Juan F. Luis Hospital and Medical Center's financial statements include its component unit: the Virgin Islands Cardiac Center at the Governor Juan F. Luis Hospital and Medical Center Foundation, Inc. (VICC Foundation). VICC Foundation is a legally separate nonprofit corporation for which the Juan F. Luis Hospital and Medical Center is financially accountable.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Major Component Units (continued)

University of the Virgin Islands (the University)

The University was organized as an instrumentality of the Government under Act No. 852 on March 16, 1962, in accordance with Section 16(a) of the Revised Organic Act of 1954, as amended. The purpose of the University is the stimulation and utilization of the intellectual resources of the people of the U.S. Virgin Islands and the development of a center of higher education. The powers of the University are exercised by a board of trustees consisting of 17 members as follows: Chairman of the Board of Education, Commissioner of Education, and the President of the University, all serving as members ex-officio, 9 other members appointed by the Governor with the advice and consent of the Legislature, two other members elected by the board of trustees, one representative of the student body, one alumnus of the University, and another representative of the teaching faculty. The University was not organized as a self-sustaining entity and therefore receives substantial financial and other support from the Government.

The University's financial statements include its component units: The Foundation for the University of the Virgin Islands and The Reichhold Foundation. The Foundation for the University of the Virgin Islands is a not-for-profit corporation whose purpose is to assist and support the University in accomplishing its charitable and educational mission. The Reichhold Foundation is a not-for-profit corporation that supports the arts and provides financial assistance in operating the Reichhold Center for the Arts on St. Thomas.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Nonmajor Component Units

Virgin Islands Economic Development Authority (EDA)

EDA was created by Act No. 6390 on December 21, 2000 as a body corporate and politic constituting a public corporation and semiautonomous instrumentality of the Government. EDA was created as an umbrella authority to assume, integrate, and unify the functions of the Economic Development Commission, the Small Business Development Agency, the Government Development Bank, and the Virgin Islands Industrial Development Park Corporation. The powers of EDA are exercised by a board of directors consisting of the members of the Virgin Islands Economic Development Commission, the Director of the Virgin Islands' Bureau of Internal Revenue, and five members not employed by the Government, but appointed by the Governor with the advice and consent of the Legislature.

Magens Bay Authority (MBA)

MBA was created as a corporate instrumentality by Act No. 2085 on December 20, 1967, with the purpose of acquiring, improving, and operating parks and beaches. The powers of MBA are exercised by a board of directors consisting of the Governor and six members initially appointed by the Governor. The board of directors is responsible for the appointment and reappointment of subsequent board members except that the Governor, with the advice and consent of the Legislature may, by appointment, fill any vacancy on the board of directors remaining unfilled for sixty days.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Nonmajor Component Units (continued)

Virgin Islands Housing Finance Authority (VIHFA)

VIHFA was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government by Act No. 4636 on October 20, 1981, with the purpose of stimulating low and moderate-income housing construction and home ownership through the issuance of revenue bonds to obtain funds to be used for low-interest mortgage loans to qualified purchasers of low and moderate-income housing. On October 31, 2008, VIHFA established the Virgin Islands Housing Management, Inc. (VIHM), a wholly-owned not-for-profit subsidiary for the purpose of managing VIHFA's rental properties. The financial statements of VIHM are separately issued, and not blended into the PG. The powers of VIHFA are exercised by a board of directors consisting of the Commissioner of the Department of Housing, Parks, and Recreation (the Chairman), the Director of the Office of Management and Budget, and three persons not employed by the Government appointed by the Governor with advice and consent of the Legislature.

Virgin Islands Public Television System (VIPTS)

VIPTS was created as a body corporate and politic constituting a public corporation and autonomous instrumentality by Act No. 2364 on November 15, 1968, with the purpose of advancing the general welfare, education, cultural development, and awareness of public affairs of all the population of the U.S. Virgin Islands as well as to provide an effective supplement to the in-school education of children. The powers of VIPTS are exercised by a board of directors consisting of the Commissioner of Education, the Chairman of the Board of Education, three members appointed by the President of the Legislature, and four members, not more than two of whom should be employed by the Government and appointed by the Governor with the advice and consent of the Legislature. In addition, the Director of the Office of Management and Budget, the President of the University of the Virgin Islands, and the General Manager of VIPTS are ex-officio members of the board who are not entitled to vote.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(b) Discretely Presented Component Units (continued)

Nonmajor Component Units (continued)

Virgin Islands Waste Management Authority (VIWMA)

VIWMA was established as a nonprofit, public, autonomous instrumentality of the Government by Act No. 6638 and approved by the Governor of the Virgin Islands on January 23, 2004. VIWMA provides environmentally sound management for the collection and disposal of solid waste in the territory, including operation and closure of landfills and wastewater collection, treatment and disposal. VIWMA is governed by a Board of Directors consisting of seven members.

University of the Virgin Islands Research and Technology Park (RTPark)

RTPark was established as a public, autonomous instrumentality of the Government by Act 6502 on February 21, 2002, as amended, by Act 6725, the Protected Cell Amendments Act of 2005. RTPark was organized for internet commerce and technology, providing an enabling environment for research, development, business incubation and technology-driven businesses. RTPark is governed by a Board of Directors consisting of seven members, including the Chairman of the Board of Trustees of the University, the President of the University, two trustees selected from among the Board of Trustees of the University, and three members selected by the Governor.

Complete audited financial statements of the discretely presented component units can be obtained directly by contacting their administrative offices:

Administrative Offices

Virgin Islands Housing Authority
402 Estate Anna's Retreat
PO Box 7668
St. Thomas, VI 00801

Virgin Islands Port Authority
PO Box 301707
St. Thomas, VI 00803

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

Administrative Offices (continued)

Virgin Islands Water and Power Authority
PO Box 1450
St. Thomas, VI 00804

Virgin Islands Government Hospital and Health Facilities Corporation
9048 Sugar Estate
St. Thomas, VI 00802

University of the Virgin Islands
2 John Brewer's Bay
St. Thomas, VI 00802

Virgin Islands Economic Development Authority
Nisky Shopping Center, Suite 620
St. Thomas, VI 00802

Magens Bay Authority
PO Box 10583
St. Thomas, VI 00801

Virgin Islands Housing Finance Authority
3202 Demarara
Frenchtown Plaza, Suite 200
St. Thomas, VI 00802

Virgin Islands Public Television System
PO Box 7879
St. Thomas, VI 00801

Virgin Islands Waste Management Authority
#1 La Grande Princesse, Suite BL1
Christiansted, VI 00820

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

Administrative Offices (continued)

University of the Virgin Islands Research and Technology Park Corporation
RR1 Box 10000
Kingshill, St. Croix, VI 00850-9781

All financial statements of the discretely presented component units have a fiscal year-end of September 30, 2012, except for WAPA and VIHA that have a year-end of June 30, 2012 and December 31, 2011, respectively.

(c) Fiduciary Component Unit

The following public benefit corporation is legally separate from the Government, meets the definition of a blended component unit, and is presented in the fund financial statements along with other fiduciary funds of the Government. Fiduciary funds are not reported in the government-wide financial statements.

Employees' Retirement System of the Government of the Virgin Islands (GERS)

GERS was created as an independent and separate agency of the Government with the purpose of administering the Government's, and component units, cost-sharing, multiple-employer defined-benefit pension plan. GERS was established on October 1, 1959. The responsibility for the operation of GERS is vested in a board of trustees composed of seven members appointed by the Governor with the advice and consent of the Legislature.

Employee and employer contributions to GERS are recognized as additions to net assets held in trust for employees' pension benefits in the period in which employee services are performed, except for contributions pursuant to the Early Retirement Act of 1994, which are recorded as the cash is received. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan, except for benefits pursuant to sections 8(a) and 8(b) of the Early Retirement Act of 1994, which are recorded when the subsidy provided by the Government is receivable and payable.

1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity (continued)

(c) Fiduciary Component Unit (continued)

Complete audited financial statements of this component unit can be obtained directly by contacting their administrative office:

Employees' Retirement System of the Government of the Virgin Islands
3438 Kronprindsens Gade
St. Thomas, Virgin Islands 00802

Government-wide and Fund Financial Statements

The government-wide financial statements (that is, the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the PG and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the PG is reported separately from certain legally separate component units for which the PG is financially accountable. The statement of net assets (deficit) presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets or net deficit. The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include (i) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (ii) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenue.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

1. Summary of Significant Accounting Policies (continued)

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

(a) Government-wide Financial Statements

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue when as all eligibility requirements have been met.

(b) 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. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Government considers most revenue to be available if collected within 90 days of the end of the current fiscal year-end. Specifically, gross receipts taxes, property taxes, and income taxes are considered to be available if collected within 30, 60, and 90 days, respectively, after the end of the current fiscal year-end. Grant revenue is considered to be available if collected within the 12 months after the end of the current fiscal year-end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due.

Income taxes, gross receipts taxes, real property taxes, and grant funding are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period to the extent they are considered available. All other revenue items are considered to be measurable and available only when cash is received by the Government.

(c) Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements

The financial statements of the proprietary funds, fiduciary funds, and discretely presented component units are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

1. Summary of Significant Accounting Policies (continued)

Measurement Focus, Basis of Accounting, and Financial Statement Presentation (continued)

(c) Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements (continued)

Each proprietary fund has the option under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, to elect and apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless these conflict with a GASB pronouncement. The PG and most blended and discretely presented component units have elected not to apply FASB pronouncements issued after November 30, 1989 for its proprietary fund types. VIPA has elected to follow the FASB's pronouncements issued after November 30, 1989.

Proprietary funds distinguish operating revenue and expenses from non-operating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations.

Fund Accounting

The Government reports its financial position and results of operations in funds, which are considered separate accounting entities and discrete presentations of those component units, which are not required to be blended. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions. GASB No. 34, *Basic Financial Statements – and Management's Discussions and Analysis – for State and Local Governments*, establishes criteria (percentage of the assets, liabilities, revenue, or expenditures/expenses of either fund category or the governmental and enterprise funds combined) for the determination of major funds. Indirect costs are automatically allocated and reported in the program expense for each fund. Nonmajor funds are combined in a single column in the fund financial statements. The Government reports the following major funds:

1. Summary of Significant Accounting Policies (continued)

Fund Accounting (continued)

(a) Governmental Funds

The Government reports the following major governmental funds:

- General Fund – The general fund is the Government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

- PFA Debt Service Fund – The PFA debt service fund accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by PFA on behalf of the Government.

- PFA Capital Projects Fund – The PFA capital projects fund accounts for bond proceeds of debt issued by the PFA on behalf of the Government. The bond proceeds have been designated for certain necessary public safety and capital development projects which are accounted for in this fund.

(b) Proprietary Funds

These funds account for those activities for which the intent of management is to recover, primarily through user charges, the cost of providing goods or services to the general public. The government reports the following major proprietary funds:

- West Indian Company – WICO, a component unit of PFA, accounts for the activities of a cruise ship pier and shopping mall complex on the island of St. Thomas.

- Unemployment Insurance Fund – The unemployment insurance fund accounts for the collection of unemployment premiums from employers in the U.S. Virgin Islands, and the payment of unemployment benefits to eligible unemployed recipients.

1. Summary of Significant Accounting Policies (continued)

Fund Accounting (continued)

(c) Fiduciary Funds

Fiduciary funds are used to account for assets held by the Government in a trustee capacity, or as an agent for individuals, private organizations, and other governmental units. The following are the Government's fiduciary funds:

- Pension Trust Fund – The pension trust fund accounts for the activities of GERS, which accumulates resources for pension benefit payments to qualified employees.

- Agency Fund – The agency fund is custodial in nature (assets equal liabilities) and does not involve measurement of the results of operations.

Cash and Cash Equivalents

The Government follows the practice of pooling cash. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing accounts and time deposits with eligible depository institutions.

Cash equivalents of the proprietary funds and discretely presented component units consist of demand accounts, money market accounts, certificates of deposit with maturities of not more than 90 days from the date of acquisition, short-term U.S. government and its agencies' obligations, and repurchase agreements with a U.S. commercial bank maturing within three months and collateralized by U.S. government obligations. Cash and cash equivalents of the discretely presented component units are maintained in separate bank accounts from those of the PG, in their own names. By law, banks, or trust companies designated as depository of public funds of the Government are to maintain corporate surety bond or pledge collateral satisfactory to the Commissioner of Finance to secure all governmental funds deposited.

Investments

The PG and its component units follow the provisions of GASB Statement No. 40, *Deposit and Investment Risk Disclosures, an Amendment of GASB Statement No. 3*. GASB Statement No. 40 establishes and modifies the following disclosure requirements related to investment risks: credit risk (including custodial credit risk and concentrations of credit risk), interest rate risk, and foreign currency risk.

1. Summary of Significant Accounting Policies (continued)

Investment Policies

Investment policies of the PG, its blended component units, major funds, and major component units are as follows:

- ***Primary Government Investment Policies –*** Title 33, Chapter 117 of the Virgin Islands Code (V.I. Code) authorizes the Government to invest in U.S. Government and its agencies' obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. As of September 30, 2011, the General Fund, the Virgin Islands Lottery, a non-major governmental fund, and an agency fund had invested in certificates of deposit with two local banks. Investments are reported at fair value.

- ***PFA Investment Policies*** – Under GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for Most External Investment Pools*, investments of the PFA are reported at fair value. Various bond resolutions of the PFA restrict investments to direct obligations of the U.S. Government, territories, possessions and states, specific bank obligations, investment agreements or similar funding agreements, shares or other interests in mutual funds, trusts or investment companies, corporate commercial paper, and money market portfolios consisting of any of the foregoing. The PFA has retained investment managers and investments are held in trust by a commercial bank on behalf of the PFA. The PFA handles investments for two major governmental funds of the Government: the PFA debt service fund and the PFA capital projects fund.

- ***Tobacco Settlement Financing Corporation Investment Policies –*** Various bond resolutions of this blended component unit restrict investments to direct obligations of the U.S. Government, territories, possessions and states, specific bank obligations, investment agreements or similar funding agreements, shares or other interests in mutual funds, trusts or investment companies, corporate commercial paper, and money market portfolios consisting of any of the foregoing. The PFA has retained investment managers and investments are held in trust by a commercial bank on behalf of the PFA. Investments are reported at fair value in the non-major governmental fund of the Government.

1. Summary of Significant Accounting Policies (continued)

Investment Policies (continued)

- ***West Indian Company Limited Investment Policies* –** This blended business-type major fund of the Government maintains an investment policy that 1) limits investments in bonds to a maximum remaining maturity of 30 years (or estimated average life on mortgage-backed issues), 2) limits fixed income securities to a maximum of 40% and a minimum of 30% of the overall assets of the WICO portfolio, 3) limits corporate bond exposure to 45% of the fixed income portfolio, and 4) has no provision which limits or restricts investments in U.S. Government Treasury or Agency issues. WICO reports investments at fair value.

- ***Pension Trust Fund Investment Policies* –** The board of trustees of GERS have enacted policies that limit investments in certain investment categories and provide requirements for the institutions with which investment transactions may be entered into. Under those policies, GERS may invest in U.S. Government and agencies obligations, bonds or notes of any state, territory or possession of the United States, municipal bonds and obligations, foreign bonds, bonds of domestic railroad corporations, public utility bonds, industrial corporate bonds or trust certificates, common and preferred shares of foreign and domestic corporations, mutual funds, mortgage or personal loans to GERS members or retirees, and mortgage and asset-backed securities. Investments in bonds are subject to rating restrictions of BBB and may not exceed 2% of the portfolio. Investments in stock of a single corporation may not exceed 1% of the market value of the fund, or exceed 1% of the outstanding stock of the corporation. The aggregate amount of investments in stock may not exceed 60% of the market value of total investments of GERS. Investment in foreign stock should be limited to 10% of the market value of the total investments of GERS. Any investment of 20% or more of the aggregate value of the portfolio must be approved by two-thirds of the membership of the board of trustees. The investments are administered by several professional investment managers and are held in trust by a commercial bank on behalf of GERS.

  GERS is authorized to invest in life settlement policy contract investments provided the investment is in a group of life insurance policies, with a minimum number of 100 measured lives; the face value of any single policy investment does not exceed $5.0 million or 2% of the aggregate face value of policy investments, and; the aggregate face value on any individual life does not exceed the greater of $10.0 million or 1% of the aggregate face value of policies purchased as investments by GERS. As of September 30, 2012, GERS had invested $50 million in a limited partnership that purchases senior life insurance policies for individuals age 65 and older with an average life expectancy of 5 to 7 years. The value of the investment, net of returns of capital of $8.2 million, was $53 million at September 30, 2012.

1. Summary of Significant Accounting Policies (continued)

Investment Policies (continued)

Investments in equity securities in the GERS pension trust fund are reported at quoted market values. Shares of mutual funds are reported at the net asset value of shares held by GERS at year-end. Purchases and sales are recorded on a trade-date basis. Realized gains and losses on securities are determined by the average cost method.

In December 4, 2009, GERS executed a loan agreement with Seaborne Virgin Islands, Inc., a seaplane service operating on the islands of St. Croix and St. Thomas. The agreement provided for a first lien term loan of $1.3 million at an initial interest rate of 8.25%, and a senior secured convertible loan of $2 million at an interest rate of 14.5%, secured by real and personal property of Seaborne Airlines, the unconditional guarantee of Coastal Airways, Inc., the parent company of Seaborne, and all of the issued and outstanding stock of Seaborne. On September 20, 2012 the parties agreed to an amendment/modification to the loan agreement and term note and provided for the modification of the convertible note. The original principal indebtedness of the term note was amended and restated to be $2.3 million with an interest rate of 6.25% per annum for the unpaid principal of the term note. The original principal indebtedness of the convertible note was amended and restated to be $1 million. The interest is accrued at the rate of 8.25% per annum payable quarterly in arrears until the maturity date. The note may be prepaid in whole or in part with a prepayment penalty of $300 thousand. As of September 30, 2012, the loan investment was $2.78 million.

On November 2, 2012, GERS extended an additional loan to Seaborne Virgin Islands, Inc., in the amount of $1.5 million as part of a modification agreement of existing loans. The term of the loan is five (5) years, bearing interest in the amount of 6.25%.

On December 8, 2009, GERS executed a loan agreement with Carambola Northwest, LLC (“Carambola’), a condominium, hotel and golf resort on the island of St. Croix. The five year term loan in the amount of $15 million is collateralized with all real property holdings of Carambola, with an interest rate of 10.5% per annum. Carambola subsequently went into default on the loan agreement. On May 11, 2012, GERS exercised its rights under the loan agreement and executed a preliminary Disposition Agreement with Carambola assuming management of the resort complex. As of September 30, 2012, the investment loan balance was $17.6 million, which includes the unpaid principal balance of $14.8 million and $2.8 million in receivables due to GERS.

1. Summary of Significant Accounting Policies (continued)

Investment Policies (continued)

GERS has also invested in a shopping and pier complex on the island of St. Thomas. The property is reported at the fair market value of $66.6 million. GERS owns administrative facilities on the islands of St. Thomas and St. Croix, reported at historical cost, net of accumulated depreciation, in the amount of $29 million.

- ***WAPA and VIPA Investment Policies*** **–** These major component units are authorized under bond resolutions and the V.I. Code to invest in open accounts, time deposits, certificates of deposit, repurchase agreements, guaranteed investment contracts, obligations of the United States government, and obligations of any state within the United States, obligations of international banking institutions, mutual funds, corporate commercial paper, money market accounts and investment pools. Investments are reported at fair value.

- ***The University Investment Policies*** **–** The board of trustees of this major component unit is responsible for the management of the University's investments which consist of U.S. Government securities and securities backed by the U.S. Government or its agencies and instrumentalities, common and preferred stocks, and mutual funds. The University is in the process of finalizing a formal investment policy for review and approval by the board of trustees. The University's component unit Foundation for the University of the Virgin Islands, issued an investment policy in February 2012. The members of the board of trustees of the Reichhold Foundation are responsible for their specific investment policy.

- ***VIGHHFC Investment Policies*** **–** The board of trustees of this major component unit have not developed a formal investment policy. At September 30, 2012, investments consisted of a 40% interest in a U.S. Virgin Islands corporation that provides radiology services at Juan F. Luis Hospital and Medical Center amounting to $375 thousand. The investment in the U.S. Virgin Islands Corporation is accounted for under the equity method.

- ***VIHA Investment Policies*** **–** This major component unit is required by the U.S. Department of Housing and Urban Development ("HUD") to invest excess funds in obligations of the United States, certificates of deposit, or any other federally insured investment. HUD requires that deposits be fully collateralized at all times, and may be held by an unaffiliated bank or trust company for the account of the VIHA.

1. Summary of Significant Accounting Policies (continued)

Receivables

Taxes receivable represent amounts owed by taxpayers for individual and corporate income taxes, gross receipts taxes and real property taxes. Tax revenue is recognized in the governmental fund financial statements when they become both measurable and available based on actual collections during the seven months subsequent to the fiscal year end.

Federal government receivables represent amounts owed to the Government for reimbursement of expenditures incurred pursuant to federally funded programs.

Accounts receivable are reported net of estimated allowances for uncollectible amounts, which are determined, based upon past collection experience and current economic conditions.

Subject to the provisions of the V.I. Code, and subject to rules and regulations prescribed by the board of trustees of GERS, members of GERS have the right to obtain loans from GERS to finance a home, automobile, or other personal needs. The maximum mortgage loan that could be granted to members who have been contributing to GERS for at least five years is $250,000. The interest rate on new first mortgages was 8% and on second mortgages, 9% throughout the year. Members may also borrow up to $50,000 to purchase land.

Members who have contributed to GERS for at least five years can borrow up to $18,000 for the purchase of an automobile. The interest rate offered on auto loans was 8.5% with a maximum term of five years. Active members may also borrow up to 75% of their contributions paid into GERS to a maximum borrowing of $50,000 as a personal loan. The interest rate offered on personal loans was 8% to 8.5% for the year. Retired members may qualify for personal loans up to $10,000 at the same interest rates as active members; however, effective fiscal year 2009, retirees have the option of refinancing their personal loan provided the original amount is paid down by at least 50%.

Member loans in GERS are valued at the outstanding loan principal balance less an allowance for estimated loan losses.

The accounts receivable from non-governmental customers of the discretely presented component units are net of estimated uncollectible amounts. These receivables arise primarily from service charges to users. Accounts receivable from the PG and other component units that arise from service charges do not have significant allowances for uncollectible accounts.

1. Summary of Significant Accounting Policies (continued)

Restricted Assets

Restricted assets in the PG and discretely presented component units are set aside primarily for the payment of bonds, notes, construction funds, unemployment benefits, and other specific purposes.

Capital Assets

Capital assets, which include land, land improvements, buildings, building improvements, machinery and equipment, construction in progress, and infrastructure assets are reported in the applicable governmental, business-type activities, and component unit columns in the government-wide financial statements as well as in the applicable proprietary funds reported in the fund financial statements.

The PG defines capital assets as assets that have an initial, individual cost and useful lives of: (i) $5,000 for personal property with a useful life of five years; (ii) $50,000 for buildings and building improvements with estimated useful lives of 40 and 20 years, respectively; (iii) $100,000 for land improvements with an estimated useful life of 20 years; and (iv) $200,000 for infrastructure with an estimated useful life of 30 years. The value of all land acquired is capitalized.

Capital assets purchased or acquired are carried at historical cost or normal cost. The normal costing method to estimate cost based on replacement cost indexed by a reciprocal factor of the price increase from the appraisal date to the actual or estimated acquisition date was used to estimate the historical cost of certain land, buildings, and building improvements because invoices and similar documentation was no longer available in certain instances. Donated capital assets are recorded at fair value at the time of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest costs are capitalized during the construction period only for business-type activities and proprietary component units. The costs of routine maintenance and repairs that do not add value to the assets or materially extend asset lives are expensed as incurred.

1. Summary of Significant Accounting Policies (continued)

Capital Assets (continued)

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, as well as the proprietary funds and component units' financial statements.

Capital assets of the PG, excluding land and construction in progress, are depreciated on the straight-line method over the assets' estimated useful lives.

The capital assets of the component units are recorded in accordance with the applicable GASB and FASB statements and under their own individual capitalization thresholds. The estimated useful lives of capital assets reported by the component units are (i) 7 to 50 years for buildings and building improvements; (ii) 20 to 40 years for airports and marine terminals; and (iii) 3 to 20 years for vehicles and equipment.

Tax Refunds Payable

During the calendar year, the Government collects individual income taxes through withholdings and payments from taxpayers. As of September 30th, the Government estimates the amount owed to taxpayers for overpayments during the first nine months of the calendar year. These estimated amounts and the actual tax refunds claimed for prior years but not paid at year-end are recorded as tax refunds payable and as a reduction of tax revenue.

Deferred and Unearned Revenue

Deferred revenue at the governmental fund level arises when potential revenue neither meets measurable nor available criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Government has a legal claim to them. In subsequent periods, when the revenue recognition criteria are met, or when the Government has a legal claim to the resources, deferred revenue is reduced from the balance sheet and the revenue is recognized. Unearned revenue at the government-wide and proprietary fund levels arises only when the Government receives resources before it has a legal claim to them or revenue recognition criteria have not been met.

1. Summary of Significant Accounting Policies (continued)

Long-term Liabilities

The liabilities reported in the government-wide financial statements include the Government's bonds, long-term notes, and other long-term liabilities including: compensated absences, retroactive union arbitration salaries, landfill closure and post closure, workers compensation loss claims, postemployment benefit costs, accrued arbitrage rebates, and legal claims. Bond premiums and discounts, losses incurred on bond refundings, and debt issuance costs are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premiums or discounts and deferred refunding losses.

In the fund financial statements, governmental fund types 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 issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Losses incurred on bond refundings are not recognized in the fund financial statements as the corresponding liability for the bonds is only recorded in the government-wide financial statements. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Fund Balance

Fund balances are reported in classifications provided by the Government Accounting Standards Board Statement No. 54, "*Fund Balance Reporting and Governmental Fund Type Definitions*". Statement No. 54 provides a hierarchy of classifications based primarily on the extent to which the Government is bound to honor constraints on the specific purposes for which amounts in funds may be spent. Following are the fund classifications:

- ***Restricted Fund Balance –*** Fund balances constrained by externally imposed constraints such as constitutional provisions, laws and regulations, debt covenants and grantors. The Government's policy is to consider restricted amounts to have been spent when expenditures are incurred for which both restricted and unrestricted fund balances are available.

- ***Committed Fund Balance –*** Fund balances subject to constraints imposed by the Government's highest level of decision making authority including legislation enacted by the Legislature of the Virgin Islands, and resolutions or ordinances enacted by Government elected regulatory boards and authorities. Committed fund balances may be modified or rescinded by enacted legislation, or amendment of resolutions or ordinances.

1. Summary of Significant Accounting Policies (continued)

Fund Balance (continued)

- ***Assigned Fund Balance –*** Fund balances subject to budgetary constraints of the Legislature, the Office of Management and Budget, or authorizing boards of the Government, that are not restricted or committed. Budgetary authority of the Office of Management and Budget is provided by Title 2, Sections 22, 23, 26 and 27 VIC, and Executive Order No. 371-1997. The Government's policy is to expend assigned or committed amounts, before unassigned amounts, when an expenditure is incurred.

- ***Unassigned Fund Balance –*** 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.

- ***Nonspendable Fund Balance –*** The nonspendable fund balance classification includes amounts that cannot be spent because they are either (a) not in spendable form (such as inventories or prepaid amounts), or (b) legally or contractually required to be maintained intact (such as a permanent endowment fund).

Net Assets

Net assets are reported in three categories:

- ***Invested in Capital Assets, Net of Related Debt –*** These consist of capital assets, net of accumulated depreciation and amortization, and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets. Debt pertaining to significant unspent debt proceeds is not included in the calculation of invested in capital assets, net of related debt. The unspent portion of the debt is presented, net of the related debt, as restricted net assets for capital projects.

1. Summary of Significant Accounting Policies (continued)

Net Assets (continued)

- ***Restricted Net Assets* –** These result when constraints placed on net assets' use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

- ***Unrestricted Net Assets* –** These consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

When both restricted and unrestricted resources are available for use, generally it is the Government's policy to use restricted resources first, then the unrestricted resources, as needed.

Compensated Absences

The vacation policy of the Government provides for the accumulation of four, six, or eight hours for each full biweekly pay period depending on the time of entry into government service. At the beginning of each calendar year, vacation leave is limited to 480 hours (60 days). However, the excess of 480 hours is considered by GERS for service credit towards the employees' retirement. This vacation policy does not apply to professional educational personnel of the Virgin Islands Department of Education, who receive compensation during the school breaks. Upon retirement, an employee receives compensation for unused vacation leave at the employee's base pay rate.

Employees accumulate sick leave at a rate of four hours for each full biweekly pay period up to a maximum of 180 days. Separated employees do not receive payment for unused sick leave; therefore, a provision for accumulated sick leave is not required.

Compensated absences accumulation policies for the blended component units and discretely presented component units vary from entity to entity, depending upon negotiated bargaining agreements and other factors agreed upon between the management of these entities and its employees.

1. Summary of Significant Accounting Policies (continued)

Interfund and Intra-entity Transactions

The Government has the following types of transactions among funds:

- ***Interfund Transfers*** **–** Legally required transfers are reported as interfund transfers in (out) when incurred.
- ***Intra-entity Transactions*** **–** These are transactions between the PG and its component units, and among the component units. Transfers between the PG and its blended component units are reported as interfund transfers, except for transfers within the same fund type.

Similarly, receivables and payables between the PG and its blended component units are reported as amounts due from (to) other funds. Transfers between the PG and discretely presented component units (and among those component units) are reported separately as revenue and expenses or expenditures. Amounts owed to and from discretely presented component units by the PG are reported separately from interfund payables and receivables as due from (to) component units, net of allowance for estimated uncollectible amounts.

Risk Management

With some exceptions, the Government does not carry general casualty or liability insurance coverage on its properties or the acts of its employees, relying instead on self-insurance and/or statutory liability limitations. However, as a result of an agreement with the Federal Emergency Management Agency (FEMA), with respect to properties and structures damaged by Hurricane Hugo and repaired with federal disaster assistance funds, the Government has obtained insurance for certain hospitals, schools, and other insurable public buildings that were repaired with such federal assistance. The Government purchases commercial insurance covering physical losses or damages against its property. The limit of liability for all risks, excluding earthquake, windstorm, and flood, is $1 million for each and every occurrence except for windstorm and flood losses, which has a $45 million limit. For physical losses arising from earthquake, the insurance policy has a limit of $100 million for each and every occurrence and in the annual aggregate.

The Government does not maintain accounting records in support of individual claim liabilities or for claims incurred but not reported (IBNR). Accordingly, medical malpractice claims are accounted for on a cash basis. Therefore, the basic financial statements do not include a liability for medical malpractice claims outstanding, including related IBNR, as of September 30, 2012, as required by GAAP.

1. Summary of Significant Accounting Policies (continued)

Future Adoption of Accounting Requirements

GASB has issued the following statements that the Government or its component units have not yet adopted:

Statement Number		Required in Fiscal Year
60	Accounting and Financial Reporting For Service Concession Arrangements	2013
61	The Financial Reporting Entity; Omnibus- An Amendment of GASB Statements No. 14 and 34	2013
62	Codification of Accounting and Financial Reporting Guidance Contained in pre-November 30, 1989 FASB and AICPA Pronouncements	2013
63	Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position	2013
65	Items Previously Reported as Assets and Liabilities	2014
66	Technical Corrections - 2012 - an amendment of GASB Statement No. 10 and No. 62	2014
67	Financial Reporting for Pension Plans	2014
68	Accounting and Financial Reporting for Pensions	2015
69	Government Combinations and Disposals of Government of Government Operations	2015
70	Accounting and Financial Reporting for Nonexchange Financial Guarantees	2014
71	Pension Transition for Contributions Made Subsequent to the Measurement Date	2015

The impact of these statements has not yet been determined by the Government.

2. Component Units

The basic financial statements include the financial statements of the following discretely presented component units:

- Virgin Islands Housing Authority
- Virgin Islands Port Authority
- Virgin Islands Water and Power Authority
- Virgin Islands Government Hospital and Health Facilities Corporation
- University of the Virgin Islands
- Virgin Islands Economic Development Authority
- Magens Bay Authority
- Virgin Islands Housing Finance Authority
- Virgin Islands Public Television System
- Virgin Islands Waste Management Authority
- University of the Virgin Islands Research and Technology Park Corporation

2. Component Units (continued)

Condensed financial information as of September 30, 2012 of all discretely presented component units follows (expressed in thousands):

			Virgin Islands Water and Power Authority		Hospital and Health Facilities Corporation				
Information on net assets	**Virgin Islands Housing Authority**	**Virgin Islands Port Authority**	**Electric System**	**Water System**	**Roy L. Schneider Hospital**	**Juan F. Luis Hospital**	**University of the Virgin Islands**	**Other Entities**	**Total Component Units**
Assets:									
Current assets	$ 15,889	$ 30,512	$ 55,422	$ 7,898	$ 22,987	$ 14,979	$ 15,741	$ 43,215	$ 206,643
Due from primary government	–	–	23,557	3,940	–	–	970	5,791	34,258
Due from federal government	1,774	1,157	–	–	750	295	3,276	2,735	9,987
Restricted assets	5,974	10,850	52,403	11,211	774	547	46,934	49,725	178,418
Capital assets, net	68,778	240,402	292,621	68,541	57,086	39,816	68,454	161,555	997,253
Deferred expenses	–	967	60,966	5,050	–	–	–	–	66,983
Other noncurrent assets	4,744	–	39	38	262	375	11,583	30,203	47,244
Total assets	97,159	283,888	485,008	96,678	81,859	56,012	146,958	293,224	1,540,786
Liabilities:									
Current liabilities	2,916	8,139	98,537	8,666	25,492	42,460	5,346	13,171	204,727
Due to primary government	–	–	–	–	3,730	–	–	650	4,380
Due to federal government	9	–	5,047	–	–	850	–	–	5,906
Bonds payable	–	30,762	270,335	19,225	–	–	–	2,150	322,472
Notes payable	3,155	1,929	11,027	–	–	–	48,917	1,832	66,860
Line of credit payable	–	–	16,875	2,500	–	–	–	–	19,375
Deferred revenue	4	–	–	–	–	–	3,585	4,861	8,450
Other noncurrent liabilities	27,468	–	31,121	6,228	–	–	3,768	11,884	80,469
Total liabilities	33,552	40,830	432,942	36,619	29,222	43,310	61,616	34,548	712,639
Net assets (deficit):									
Invested in capital assets, net of related debt	63,359	209,640	131,726	51,754	57,086	39,765	30,632	160,138	744,100
Restricted	6,189	10,850	27,416	10,209	774	546	39,348	65,491	160,823
Unrestricted (deficit)	(5,941)	22,568	(107,076)	(1,904)	(5,223)	(27,609)	15,362	33,047	(76,776)
Total net assets	$ 63,607	$ 243,058	$ 52,066	$ 60,059	$ 52,637	$ 12,702	$ 85,342	$ 258,676	$ 828,147

2. Component Units (continued)

Information on statements of activities	Expenses	Program revenue: Charges for Services	Program revenue: Operating Grants and Contributions	Program revenue: Capital Grants and Contributions	Total Component Units
Virgin Islands Housing Authority	$ 58,654	$ 6,472	$ 39,398	$ 13,113	$ 329
Virgin Islands Port Authority	59,528	47,230	–	5,298	(7,000)
Virgin Islands Water and Power Authority:					
Electric System	363,961	331,414	–	1,951	(30,596)
Water System	25,531	34,624	–	5,947	15,040
Virgin Islands Government Hospital and Health Facilities Corporation:					
Roy L. Schneider Hospital	89,874	56,661	23,310	–	(9,903)
Juan F. Luis Hospital	86,726	48,401	25,611	–	(12,714)
University of the Virgin Islands	80,450	18,676	54,153	3,992	(3,629)
Other component units	68,080	9,744	60,847	17,442	19,953
Total activities	$ 832,804	$ 553,222	$ 203,319	$ 47,743	(28,520)
General revenue:					
Interest and other					33,526
Forgiveness of debt					86,301
Changes in net assets					91,307
Net assets at beginning of year *(as restated)*					736,840
Net assets at end of year					$ 828,147

The amount due from the PG at September 30, 2012, amounted to approximately $34.2 million. The amount due to the PG amounted to $4.3 million, and was due from Roy L. Schneider Hospital and Waste Management Authority.

3. Stewardship, Compliance, and Accountability

Budgetary Process and Control

The V.I. Code requires the Governor to submit an annual balanced executive budget to be adopted by the Legislature for the ensuing fiscal year. The Governor is required by law to submit to the Legislature the annual balanced executive budget no later than May 30. The annual balanced executive budget is prepared on a GAAP basis, except for encumbrances, which are reported as expenditures for budget reporting purposes, by the Virgin Islands Office of Management and Budget (OMB) working in conjunction with other Government offices and

3. Stewardship, Compliance, and Accountability (continued)

Budgetary Process and Control (continued)

agencies. If the annual executive budget has not been approved before the commencement of any fiscal year, then the appropriations for the preceding fiscal year, insofar as they may be applicable, are automatically deemed re-appropriated item by item. The annual balanced executive budget, which includes those funds of the Government subject to appropriation pursuant to law, is composed of all proposed expenditures and estimated revenue for the Government. The Legislature enacts the annual executive budget through passage of lump-sum appropriations for each department. The Legislature may add, change, or delete any items in the annual executive budget proposed by the Governor. Upon passage by the Legislature, the annual executive budget is submitted to the Governor, who may veto the budget partially or in its entirety and return it to the Legislature with his objections. A veto by the Governor can be overridden only by a two-thirds majority of all members of the Legislature. The Legislature is obligated by law to pass a final annual executive budget no later than September 30, the last day of the fiscal year. Supplemental budgetary appropriations bills that are signed into law may be created during the year without the identification of a specific revenue source to finance them. In August 1999, the Legislature enacted the Financial Accountability Act (Act No. 6289). The purpose of the Financial Accountability Act is to require by law that the budget of the Government be balanced each year, and the appropriations in each fiscal year not exceed a verifiable revenue source.

Once the budget has been enacted, fiscal control over expenditures made pursuant thereto is exercised by the Governor through the Director of OMB. During any fiscal year in which the resources available to the Government are not sufficient to cover the appropriations approved for such year, the Governor, through the Director of OMB, may take administrative measures to reduce expenditures. The Governor may also make recommendations to the Legislature for new taxes or any other necessary action to meet the estimated deficiency.

Budgetary control is exercised at the department level through an allotment process. Encumbrances and expenditures cannot exceed total allotment amounts. The Government's department heads may make transfers of appropriations within the department. Appropriation transfers between departments and supplemental appropriations require executive and legislative branch approval. Unencumbered and unexpended appropriations, not designated, lapse at fiscal year-end. Also, encumbrances are established at fiscal year-end to pay certain expenditures for travel and utility costs payable against current year appropriation authority, but to be expended in the subsequent year.

3. Stewardship, Compliance, and Accountability (continued)

Budget/GAAP Reconciliation

The following schedule presents a comparison of the general fund legally adopted budget with actual data on a budgetary basis. Because accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of timing and entity difference in the excess (deficiency) of revenue and net other financing sources over expenditures for the year ended September 30, 2012 is presented below (expressed in thousands):

Excess of revenues and net other financing sources over expenditures	$	112,795
Entity difference – deficiency of revenues and net other financing over expenditures – activities with budgets not legally adopted		(18,508)
Excess of revenues and net other financing sources over expenditures – GAAP basis (net change in fund balance)	$	94,287

Controls over spending in special revenue funds and non-appropriated funds are maintained at the Department of Finance by use of budgets and available resources (revenues). The Government makes appropriations to authorize expenditures for various capital projects. Budgets for capital projects normally remain available until completion of the project unless modified or rescinded.

4. Cash and Cash Equivalents

Primary Government

At September 30, 2012, the PG reported $177.4 million in unrestricted cash and cash equivalents, and $5.4 million in restricted cash and cash equivalents. All of the PG's bank balances were fully collateralized.

Pension Trust Fund

GERS considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents. At September 30, 2012, GERS held $103.4 million in cash and cash equivalents consisting of: $62.7 million in money market accounts and $26.2 million in operational accounts and $14.5 million in certificates of deposits with maturity time less than 90 days.

4. Cash and Cash Equivalents (continued)

Component Units

At September 30, 2012, discretely component units held $82.8 million in unrestricted cash and cash equivalents and $70.4 million in restricted cash and cash equivalents, of which $792 thousand was not insured, bonded or collateralized as required for public funds of the Government.

5. Investments

Primary Government Investments

Following is a summary of the investments of the PG, categorized by investment type and maturity as of September 30, 2012:

Primary Government Investments
(in thousands)

	Fair Value	Maturity (in years) Less Than 1 Year	1 to 5 Years	Over 5 Years
Investments with contractual maturities				
Certificates of Deposit	$ 8,024	$ 8,024	$ –	$ –
Portfolio investments				
Commercial Paper	39,547	39,142	–	405
U.S. Government Agencies & Notes	38,456	18,629	19,827	–
Total investments with contractual maturities	86,027	$ 65,795	$ 19,827	$ 405
Investments without contractual maturities				
Money Market & Mutual Funds	434,107			
Total Primary Government Investments	$ 520,134			

5. Investments (continued)

Primary Government Investments (continued)

Interest-Rate Risk – Interest-rate risk represents the exposure to fair value losses arising from increasing interest rates. The PG does not have a formal investment policy that limits investment maturities as a means of managing such exposure. As a means of keeping the interest-rate risk low, virtually all investments held by the PG are short-term in nature.

Credit Risk – The authorizing legislation of the PG does not limit investments by credit rating categories. Authorizing legislation does limit the investment choices of the PG to direct obligations or obligations guaranteed by the United States, obligations of states, territories, possessions and commonwealths of the United States, obligations of international banking institutions, repurchase agreements, investment contracts, certificates of deposit, guaranteed investment contracts, shares in mutual funds, investment companies, corporate commercial paper, money market portfolio investments, and investment pools.

At September 30, 2012, the PG's investments in money market funds were rated AAAm by Standard & Poor's, and Aaa-mf by Moody's Investor Service; PG's investment in commercial securities were rated A- by Standard & Poor's, and A2 by Moody's Investor Services; and the PG's investment in U.S. government agencies were rated AA+ by Standard & Poor's and Aaa by Moody's Investor Services.

Concentration of Credit Risk – The PG places no limit on the amount that may be invested in one issuer. At September 30, 2012, more than 90% of the PG's investments were invested in: Goldman Financial Square Money Market #524 (50.15%), Federated Government Obligation #5 (14.72%), Goldman Financial Securities Money Market #474 (7.54%), Invesco Treasury #1930 (7.26%), and Goldman Financial Square Money Market #465 (3.78%).

Custodial Credit Risk – The PG does not have a custodial risk policy. This is the risk that the PG will not be able to recover the value of its investments that are in the possession of an outside party. At September 30, 2012, $520.0 million of investments were held in the name of The Bank of New York Trust Company, N.A, as trustee for the Government.

5. Investments (continued)

Pension Trust Fund Investments

Following is a summary of pension trust fund investments as of September 30, 2012:

Pension Trust Fund Investments
(In thousands)

		Maturity (in years)				
	Fair Value	**Less Than 1 Year**	**1 to 5 Years**	**6 to 10 Years**	**More Than 10 Years**	**No Stated Maturity**
Investments with contractual maturities						
US government and agency obligations	13,375	$ 3,327	$ 3,263	$ 3,291	$ 3,494	$ –
US Treasury notes	13,097	–	–	1,997	11,100	–
US Treasury bonds	41,208	–	20,989	20,219	–	–
Municipals	5,744	–	828	574	4,342	–
Mutual Funds	151,795	–	–	–	–	151,795
Corporate obligations	62,577	2,520	25,530	24,972	9,555	–
Foreign bonds	3,092	257	1,210	1,625	–	–
Government obligations - foreign	8,598	–	3,141	1,706	3,751	–
Mortgage and asset backed securities	84,001	–	14,952	3,190	65,859	–
Investment loan	32,570	–	32,570	–	–	–
Total investments with contractual maturities	416,057	$ 6,104	$ 102,483	$ 57,574	$ 98,101	$ 151,795
Investments without contractual maturities						
Equity Securities						
Common stocks - U.S.	434,558					
Common stocks - foreign	42,257					
Real Estate Investments						
Real estate investment trusts	6,172					
Havensight Mall - US Virgin Islands	66,600					
GERS Complex - US Virgin Islands	29,000					
Limited partnership	55,741					
Securities lending short-term collateral investment pool	128,495					
Total pension fund investments	$ 1,178,880					

5. Investments (continued)

Pension Trust Fund Investments (continued)

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. GERS does not have a specific policy to manage interest rate risk, but requires investment managers to diversify by issue, maturity, sector, coupon, and geography. Investment managers retained by GERS follow specific investment guidelines and are evaluated against specific market benchmarks that represent their investment style. Any exemption from general guidelines requires approval from GERS' board of trustees.

Credit Risk – GERS investment policy is designed to minimize credit risk by restricting authorized investments to only those investments permitted by statute, subject to certain additional limitations. These additional limitations consist of prohibitions against investments in derivative securities, options, futures or short positions. GERS investment policy allows investments in mortgage pass-through securities.

5. Investments (continued)

Pension Trust Fund Investments (continued)

The credit ratings of GERS debt and equity securities include:

Pension Trust Fund Investment Credit Ratings
(in thousands)

		Credit Ratings	
	Fair Value	**Standard & Poor**	**Moody's**
US government and agency obligations	$ 8,635	AA+	Aaa
US government and agency obligations	997	AA	Aa2
US government and agency obligations	1,019	AA-	Aa1
US government and agency obligations	2,724	Not Rated	Not Rated
US Treasury notes	13,097	AA+	Aaa
US Treasury bonds	41,208	AA+	Aaa
Corporate obligations	61,475	BB+ to AAA	BA3 to Aaa
Corporate obligations	1,102	Not Rated	Not Rated
Foreign bonds and government obligations	10,740	AAA	Aaa
Foreign bonds and government obligations	693	A-	A3
Foreign bonds and government obligations	257	Not Rated	Baa1
Municipals	4,295	A- to AA+	A1 to Aaa
Municipals	1,449	B- to BB+	B3
Mortgage and asset backed securities	67,968	A- to AAA	A3 to Aaa
Mortgage and asset backed securities	1,282	B to BBB+	B3 to Baa1
Mortgage and asset backed securities	734	CC to CCC	Caa3 to Caa1
Mortgage and asset backed securities	14,017	Not Rated	Not Rated
Common stocks- US	434,558	Not Rated	Not Rated
Common stocks - foreign	42,257	Not Rated	Not Rated
Real estate investment trust	2,814	Not Rated	Not Rated
Real estate investment trust	3,358	Not Rated	Not Rated
Real estate holdings - US Virgin Islands	95,600	Not Rated	Not Rated
Investment loans	32,570	Not Rated	Not Rated
Limited partnership	55,741	Not Rated	Not Rated
Securities lending short-term collateral investment pool	128,495	Not Rated	Not Rated
Mutual funds	151,795	Not Rated	Not Rated
Total investments	$ 1,178,880		

5. Investments (continued)

Pension Trust Fund Investments (continued)

Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of a depository financial institution or other counterparty, GERS will not be able to recover the value of an investment or collateral securities that are in the possession of an outside party. With the exception of underlying securities on loans secured by non-cash collateral amounting to $11.9 million, the entire investment portfolio of GERS was held with a single third-party custodian as of September 30, 2012. Cash collateral held for securities lending transactions is invested in a collective investment pool maintained by the securities lending agent.

Foreign Currency Risk – Foreign currency risk is the risk of holding investments in foreign currencies and the risk that those foreign currencies may devalue. GERS has no general investment policy with respect to foreign currency risk.

As of September 30, 2012, $54.0 million of GERS' portfolio was held in foreign cash equivalents and investments, with $22.0 million held in Euro currency, $10.7 million held in pound sterling, $4.8 million held in Australian dollars, $4.7 million held in Swiss francs, $4.0 million held in Japanese yen, $2.5 million held in Hong Kong dollars, $1.3 million held in Norwegian krone, $1.3 million in Egyptian pound, and $2.1 million in other currencies. GERS entered into various forward currency exchange contracts to manage exposure to changes in foreign currency exchange rates, and to facilitate the settlement of foreign security transactions. Risks associated with foreign exchange contracts include the movement in the value of foreign currency relative to the U.S. dollar and the ability of the counterparty to perform in accordance with the terms of the contract. Changes in the market value of open and closed forward contracts are recorded with interest, dividends, and other income or losses reported at fair value. During the fiscal year ended September 30, 2012, GERS reported $11.6 million in forward currency purchases, $11.5 million in forward currency sales, and a foreign exchange loss of $1.3 million.

5. Investments (continued)

Pension Trust Fund Investments (continued)

Securities Lending Transactions **–**The Government's statutes permit GERS to participate in securities lending transactions, and GERS has, via a securities lending authorization agreement (the Agreement), authorized State Street Bank and Trust Company (the Custodian) to lend its securities to broker-dealers and banks pursuant to a form of loan agreement. Lent securities are collateralized with cash, securities issued or guaranteed by the U.S. government, or irrevocable bank letters of credit. GERS does not have the ability to pledge or sell collateral securities delivered absent a borrower default. No restrictions were imposed during 2012 as to the amount of loans the Custodian can make on behalf of GERS. Under the terms of the Agreement the Custodian must indemnify the Government for losses attributable to violations by the Custodian under the "standard of care" clause described in the Agreement. There were neither such violations during fiscal years 2012 or 2011, nor losses resulting from the default of the borrowers or the Custodian.

Loans are generally terminable on demand. The collateral received shall, in the case of loaned securities denominated in U.S. dollars or whose primary trading market is located in the U.S. or sovereign debt issued by foreign governments, have a market value of 102% of the market value of the security for domestic borrowers and 105% for foreign borrowers at the inception of the securities lending transaction. Such collateral should be kept at a minimum of 100% of the market value of the security for all borrowers throughout the outstanding period of the transaction. At September 30, 2012, approximately $138.7 million of U.S. government and agency securities, fixed income, and equity corporate securities were on loan. The cash collateral received with a corresponding liability of an equal amount is recorded in the statement of fiduciary net assets. The cash collateral received on each loan was invested, together with the cash collateral of other lenders, in a collective investment pool. As of September 30, 2012, such investment pool had a weighted average maturity of 45 days and an average expected maturity of 104 days. Because the loans were terminable on demand, their duration did not generally match the duration of the investments made with cash collateral.

5. Investments (continued)

Component Unit Investments

Following is a summary of component unit investments and maturities as of September 30, 2012:

Component Unit Investments
(in thousands)

		Maturity (in years)			
	Fair Value	Less Than 1 Year	1 to 5 Years	6 to 10 Years	Over 10 Years
Investments with contractual maturities					
Certificates of deposit	$ 10,846	$ 10,579	$ 267	$ –	$ –
Mortgage backed securites	2,976	–	–	–	2,976
Corporate bonds	5,450	–	822	956	3,672
Guaranteed investment contracts	143				143
U.S. Government agencies and notes	40,277	34,227	4,657	–	1,393
Total investments with contractual maturities	59,692	$ 44,806	$ 5,746	$ 956	$ 8,184
Investments without contractual maturities					
Common stock	5,685				
Mutual funds	6,758				
Other investments	19,568				
Total component unit investments	$ 91,703				

5. Investments (continued)

Component Unit Investments (continued)

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The component units of the Government have not established formal policies which limit investment maturities as a means of managing such exposure and have some exposure to interest rate risk.

Credit Risk – The authorizing legislation of the component units does not limit investments by credit rating categories. Authorizing legislation limits the investment choices of the component units, as described in Note 1. At September 30, 2012, the University of the Virgin Islands' investments includes corporate bonds with ratings of A- to BBB by Standard & Poor's.

Custodial Credit Risk – The component units of the Government do not have custodial credit risk policies. This is the risk that the component unit will not be able to recover the value of its investments that are held in the possession of an outside party.

6. Receivables

Primary Government Receivables

Receivables for governmental funds at September 30, 2012 consist of the following (expressed in thousands):

	General	PFA Debt Service	Total
Income taxes	$ 196,788	$ –	$ 196,788
Real property taxes	188,220	–	188,220
Hotel occupancy taxes	472	–	472
Excise taxes	1,784	–	1,784
Gross receipts taxes	–	128,587	128,587
Tax receivables	387,264	128,587	515,851
Less allowance for doubtful accounts	(205,992)	(84,055)	(290,047)
Net tax receivables	$ 181,272	$ 44,532	225,804
Other long-term receivables – Tobacco settlement rights			1,757
Total receivables reported in the statement of net assets (deficit)			$ 227,561

6. Receivables (continued)

Primary Government Receivables (continued)

Tax Receivables

The Naval Appropriations Act created a separate tax structure for the U.S. Virgin Islands that mirrors the Internal Revenue Code of 1986, as amended. Income taxes are due from every corporation, partnership, individual, association, estate, or trust that meets the filing requirements of the U.S. Internal Revenue Code. A U.S. taxpayer who is a permanent resident of the U.S. Virgin Islands satisfies his Virgin Islands income tax obligations by filing his return with and paying income taxes to the Government. Virgin Islands residents are taxed by the Virgin Islands on their world-wide income. A nonresident of the U.S. Virgin Islands pays income taxes on his U.S. Virgin Islands source income to the Government. The revenue is recognized in the general fund in the fiscal period for which the income tax return was filed. The revenue from income tax withholding and estimated payments are recognized in the general fund as collected, net of estimated tax refunds.

Corporate income taxes are due by the 15th day of the third month following the close of the fiscal year and become delinquent if not paid on or before the due date.

Partnership and trust income taxes are due by April 15 of the following year for which the income tax was levied. Trust income taxes must be paid by the tax filing date.

Property taxes are assessed each calendar year on all taxable real property located in the U.S. Virgin Islands. The receivable is recognized, net of estimated uncollectable amounts, in the general fund in the fiscal period for which the tax was assessed. The revenue is recognized in the general fund in the fiscal period for which the property tax is levied, provided the tax is collected within 60 days subsequent to fiscal year-end, unless the facts justify a period greater than 60 days. Receivables recognized before that period are recorded as deferred revenues.

The Office of the Tax Assessor is responsible for the assessment of all taxable real property. Noncommercial real property subject to taxation is reassessed once every five years and commercial real property subject to taxation is reassessed biannually. The Tax Assessor prepares an annual assessment roll and schedule of collections for each parcel of real property that is used by The Office of the Tax Collector, as the basis for issuing tax bills to all taxpayers in the U.S. Virgin Islands.

Property taxes are to be levied by May 15 of each year in the name of the record owner on January 15 of the same year. The taxes are due on June 30 and become delinquent if not paid by August 31.

6. Receivables (continued)

Primary Government Receivables (continued)

Tax Receivables (continued)

For businesses with gross receipts of $120,000 per annum or less, gross receipts taxes are levied on an annual basis based on the amount of gross receipts in excess of $9,000 per month. Businesses with annual gross receipts greater than $120,000, but less than $225,000, are levied on a monthly basis, based on the amount of gross receipts in excess of $9,000 per month. Businesses with annual gross receipts of more than $225,000 are levied on a monthly basis, based on all gross receipts, with no $9,000 per month exemption.

Gross receipts tax assessment rates, applied to taxable gross receipts, were as follows:

October 1, 2010 through April 30, 2011:	4.0%
June 1, 2011 through February 28, 2012:	4.5%
March 1, 2012 and thereafter:	5.0%

Monthly gross receipts tax filings are due within 30 calendar days following the last day of the calendar month collected. Annual gross receipts tax filings are due within 30 calendar days following the last day of the calendar year.

Other Receivables

In addition to tax receivables, the PG receives tobacco settlement right payments in connection with a Master Settlement Agreement entered into with certain participating cigarette manufacturers. Under the terms of the agreement, the U.S. Virgin Islands receives .0173593% of annual payments made under the agreement. As of September 30, 2012, the PG reported a receivable of $1.6 million for tobacco settlement right payments.

On November 14, 2011, the PG entered into a loan agreement on behalf of GERS in the amount of $13 million, at an interest rate of 4.91% and a maturity date of December 15, 2016. The security for the loan was pledged property tax receipts for tax years prior to, and including, 2005. At September 30, 2012, the outstanding balance of the loan was $10.1 million, and pledged property tax receipts were sufficient to meet debt service payments.

Component Unit and Pension Trust Fund Receivables

Component unit receivables at September 30, 2012, consist of the following (expressed in thousands):

Utility service charges	$	21,787
Port fees		2,997
Students		2,368
Patients		27,859
Other		8,845
Total	$	63,856

Loans and advances receivable, net at September 30, 2012, consist of the following (expressed in thousands):

		Fiduciary Funds Pension Trust
Mortgage loans	$	7,739
Personal loans		136,699
Other loans and advances		135
Subtotal		144,573
Less allowance for uncollectible accounts		(767)
Loans and advances receivable, net	$	143,806

7. Deferred Revenue

The components of deferred revenue for the general fund as of September 30, 2012 consist of the following (expressed in thousands):

Property tax	$ 83,688
Matching excise tax	84,328
Income tax	72,329
	$240,345

8. Interfund Transactions

Interfund transfers for the year ended September 30, 2012 consisted of the following (expressed in thousands):

Transfers to	General	PFA Debt Service	PFA Capital Projects	West Indian	Nonmajor Governmental	Total
General	$ –	$ 95,458	$ 4,000	$ 700	$ –	$ 100,158
PFA Debt Service	11,240	–	–	–	–	11,240
PFA capital projects	–	–	–	–	4,000	4,000
Nonmajor governmental	3,787	3,932	612	–	–	8,331
West Indian Company	–	–	–	–	–	–
Total	$ 15,027	$ 99,390	$ 4,612	$ 700	$ 4,000	$ 123,729
Transfer from						
General	$ –	$ 11,240	$ –	$ –	$ 3,787	$ 15,027
PFA Debt Service	95,458	–	–	–	3,932	99,390
PFA Capital Projects	4,000	–	–	–	612	4,612
Nonmajor governmental	–	–	4,000	–	–	4,000
West Indian Company	700	–	–	–	–	700
Total	$ 100,158	$ 11,240	$ 4,000	$ –	$ 8,331	$ 123,729

Interfund transfers constitute the transfer of resources from the fund that receives the resources to the fund that utilizes them. The most significant transfers to the general fund from other governmental funds included a $95.5 million transfer from the PFA Debt Service Fund (a major governmental fund) representing gross receipt tax revenue in excess of bond debt service requirements, and a $4 million transfer from the PFA Capital Projects Fund, representing reprogrammed investment income.

8. Interfund Transactions (continued)

Significant transfers made from the General Fund include a transfer of $11.2 million to the PFA Debt Service Fund representing matching funds received during the year utilized for debt service requirements, a transfer of $2 million to the St. Croix Capital Improvement Fund (a non-major governmental fund) and a transfer of $1.0 million to the Crisis Intervention Fund (a non-major governmental fund).

Significant transfers from the PFA Debt Service Fund included a transfer of $3.9 million to the PFA Operating Fund (a non-major governmental fund), representing interest earned from unexpended bond proceeds.

Due From/To Other Funds

The following table summarizes interfund receivables and payables at September 30, 2012 (expressed in thousands):

Due from other funds	General	PFA Debt Service	PFA Capital Projects	Nonmajor Governmental	West Indian Company	Nonmajor Enterprise	Total
General	$ –	$ –	$ –	$ 13,030	$ 4,000	$ 200	$ 17,230
PFA Debt Service	–	–	–	–	–	–	–
PFA capital projects	–	–	–	–	–	24,275	24,275
Nonmajor governmental	17,637	1,426	–	–	–	2,129	21,192
Total Governmental Funds	17,637	1,426	–	13,030	4,000	26,604	62,697
Nonmajor enterprise	739	–	–	–	–	–	739
Total Enterprise Funds	739	–	–	–	–	–	739
Total	$ 18,376	$ 1,426	$ –	$ 13,030	$ 4,000	$ 26,604	$ 63,436
Due to other funds							
General	$ –	$ –	$ –	$ 17,637	$ –	$ 739	$ 18,376
PFA Debt Service	–	–	–	1,426	–	–	1,426
Nonmajor governmental	13,030	–	–	–	–	–	13,030
Total Governmental Funds	13,030	–	–	19,063	–	739	32,832
West Indian Company	4,000	–	–	–	–	–	4,000
Nonmajor enterprise	200	–	24,275	2,129	–	–	26,604
Total Enterprise Funds	4,200	–	24,275	2,129	–	–	30,604
Total	$ 17,230	$ –	$ 24,275	$ 21,192	$ –	$ 739	$ 63,436

8. Interfund Transactions (continued)

Due From/To Other Funds (continued)

The due from (to) other funds includes the following amounts due from the general fund: $4.9 million due to the emergency molasses fund (a non-major governmental fund) for unpaid appropriations, $1.1 million due to the elected governor retirement fund, and $4.8 million due to the PFA special revenue fund for unpaid matching funds. The due to the General Fund is mainly composed of $9.8 million due from the District Street Lighting Fund (a non-major governmental fund) and $2.7 million owed from the bond proceeds fund (a non-major governmental fund) to the general fund.

The due to other governmental funds includes $6.0 million due to the St. Croix Capital Improvement Fund from the General Fund for capital improvement projects, $862.6 thousand due from the Virgin Islands Lottery to the Pharmaceutical Assistance to the Aged Fund and $946.4 thousand due from the Virgin Islands Lottery to the VI Educational Initiative Fund consisting primarily of 15% of revenue derived from lottery games under contract between the Virgin Islands Lottery and private contractors be transferred to these funds. Contributions from the Virgin Islands Lottery (a non-major enterprise fund) amounted to $3.2 million, which represented contributions to the VI Educational Initiative Fund (a non-major governmental fund) of $1.6 million and a contribution to the Pharmaceutical Assistance to the Aged Fund (a non-major governmental fund) of $1.6 million.

The due to PFA Capital Projects funds includes $23.9 million due from the Virgin Islands Next Generation Network (viNGN), a non-major business-type fund in connection with start-up costs in connection with the broadband project.

9. Restricted Assets

Primary Government

Restricted assets of proprietary funds and business-type activities as of September 30, 2012 include cash and cash equivalents as follows (expressed in thousands):

Restricted Assets – Proprietary Funds and Business-type Activities

Unemployment insurance funds	$	3,146
WICO debt service funds		1,951
Total restricted assets of proprietary funds and business-type activities	$	5,097

9. Restricted Assets (continued)

Component Units

Restricted assets of component units include cash and cash equivalents, investments, and receivables as follows (expressed in thousands):

Restricted Assets – Component Units

Cash and cash equivalents:		
Debt service and sinking fund requirements	$	19,744
Endowment funds		14,382
HUD project funds		5,973
Revolving loan funds		16,474
Construction funds		845
Renewal and replacement funds		4,697
Other		8,306
Total cash and cash equivalents		70,421
Investments:		
Debt service and sinking fund requirements		27,485
Construction funds		12,467
Endowment funds		28,165
Renewal and replacement funds		4,807
Revolving loan funds		5,009
Other		3,038
Total investments		80,971
Other:		
Pledged funds		27,026
Total restricted assets of component units	$	178,418

10. Capital Assets

Primary Government

The capital assets activity for the governmental activities for the year ended September 30, 2012, is summarized as follows (expressed in thousands):

	Beginning Balance	Additions	Transfers	Disposals	Ending Balance
Capital assets not being depreciated:					
Land	$ 192,937	$ 100	$ –	$ –	$ 193,037
Construction in progress	127,735	30,838	(56,106)	–	102,467
Total capital assets not being depreciated	320,672	30,938	(56,106)	–	295,504
Capital assets being depreciated:					
Land improvements	5,305	–	–	–	5,305
Infrastructure	223,884	554	15,729	–	240,167
Buildings and improvements	410,952	1,223	28,731	–	440,906
Machinery and equipment	141,198	3,628	11,646	–	156,472
Total capital assets being depreciated	781,339	5,405	56,106	–	842,850
Less accumulated depreciation for:					
Land improvements	(3,414)	(189)			(3,603)
Infrastructure	(67,448)	(7,714)		–	(75,162)
Buildings and improvements	(174,086)	(12,629)	–	–	(186,715)
Machinery and equipment	(107,907)	(11,908)	–	–	(119,815)
Total accumulated depreciation	(352,855)	(32,440)	–	–	(385,295)
Total capital assets being depreciated, net	428,484	(27,035)	56,106	–	1,228,145
Governmental activities capital assets, net	$ 749,156	$ 3,903	$ –	$ –	$ 753,059

10. Capital Assets (continued)

Primary Government (continued)

Capital assets activity for the business-type activities for the year ended September 30, 2012, is summarized as follows (expressed in thousands):

	Beginning Balance	Additions	Transfers	Disposals	Ending Balance
Capital assets not being depreciated:					
Land	$ 5,147	$ –	$ –	$ –	$ 5,147
Construction in progress	5,660	7,640	(997)	–	12,303
Total capital assets not being depreciated	10,807	7,640	(997)	–	17,450
Capital assets being depreciated and amortized:					
Land improvements	348	–	–	–	348
Buildings and improvements	66,434	235	997	(149)	67,517
Machinery and equipment	11,214	1,683	–	(1,131)	11,766
Intangible	–	8,064	–	–	8,064
Total capital assets being depreciated	77,996	9,982	997	(1,280)	87,695
Less accumulated depreciation and amortization for:					
Land improvements	(341)	–	–	–	(341)
Buildings and improvements	(23,781)	(1,984)	–	102	(25,663)
Machinery and equipment	(8,675)	(1,114)	–	285	(9,504)
Intangible	–	(454)	–	–	(454)
Total accumulated depreciation and amortization	(32,797)	(3,552)	–	387	(35,962)
Total capital assets being depreciated and amortized, net	45,199	6,430	997	893	51,733
Business-type activities capital assets, net	$ 56,006	$ 14,070	$ –	$ 893	$ 69,183

10. Capital Assets (continued)

Primary Government (continued)

Depreciation expense was charged to functions/programs of the PG for the year ended September 30, 2012 as follows (expressed in thousands):

Governmental activities:		
General government	$	15,369
Public safety		1,823
Health		982
Education		5,902
Public Housing and Welfare		367
Culture and recreation		423
Transportation and communication		7,574
Total depreciation expense – governmental activities	$	32,440
Business-type activities:		
WICO – depreciation	$	1,923
Other enterprise funds – depreciation		1,629
Total depreciation – business-type activities	$	3,552

10. Capital Assets (continued)

Component Units

The capital assets activity for the discretely presented component units for the year ended September 30, 2012 is summarized as follows (expressed in thousands):

	Beginning Balance *(As Restated)*	Additions	Transfers	Disposal	Ending Balance
Capital assets not being depreciated:					
Land	$ 92,272	$ 688	$ 2,268	$ 37	$ 95,191
Construction in progress	45,254	44,344	(42,115)	1,166	46,317
Total capital assets not being depreciated	137,526	45,032	(39,847)	1,203	141,508
Capital assets being depreciated:					
Buildings and improvements	1,572,102	34,853	25,899	804	1,632,050
Airport and marine terminal facilities	140,693	12	7,634	–	148,339
Personal property and equipment	205,596	34,774	4,880	1,422	243,828
Intangible assets	2,604	–	–	694	1,910
Total capital assets being depreciated	1,920,995	69,639	38,413	2,920	2,026,127
Less accumulated depreciation:					
Buildings and improvements	(895,393)	(51,730)	36	601	(946,486)
Airport and marine terminal facilities	(101,577)	(7,268)	–	–	(108,845)
Personal property and equipment	(100,520)	(15,606)	–	1,350	(114,776)
Intangible assets	(275)	–	–	–	(275)
Total accumulated depreciation	(1,097,765)	(74,604)	36	1,951	(1,170,382)
Total capital assets being depreciated, net	823,230	(4,965)	38,449	4,871	855,745
Component unit capital assets, net	$ 960,756	$ 40,067	$ (1,398)	$ 6,074	$ 997,253

10. Capital Assets (continued)

Component Units (continued)

Depreciation expense charged by each component unit for the year ended September 30, 2012 was as follows (expressed in thousands):

Virgin Islands Housing Authority	$	5,568
Virgin Islands Port Authority		20,444
Virgin Islands Water and Power Authority:		
Electric System		23,117
Water System		4,123
Virgin Islands Government Hospital and Health Facilities Corporation:		
Roy L. Schneider Hospital		4,837
Juan F. Luis Hospital		3,724
University of the Virgin Islands		2,804
Other component units		9,987
Total depreciation expense– component units	$	74,604

11. Long-Term Liabilities

The change in long-term bonds and loans for governmental activities was as follows for the year ended September 30, 2012 (expressed in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year	Amounts Due Thereafter
Governmental activities:						
Bonds payable:						
2012 Series A Revenue Bonds	$ -	$ 142,640	$ -	$ 142,640	$ -	$ 142,640
2010 Series A & B Revenue Bonds	399,050	-	-	399,050	1,990	397,060
2009 Series A Revenue Bonds (Cruzan)	38,640	–	(565)	38,075	585	37,490
2009 Series A-1, A-2, B & C Revenue and Refunding Bonds	450,380	–	(29,650)	420,730	24,145	396,585
2009 Series A Revenue Bonds (Diageo)	250,000	–	–	250,000	–	250,000
2006 Series A Revenue Bonds	214,385	–	(2,705)	211,680	2,805	208,875
2006 Series A Tobacco Bonds	7,290	–	–	7,290	–	7,290
2004 Series A Revenue Bonds	75,235	–	(3,805)	71,430	3,995	67,435
2003 Series A Revenue Bonds	248,960	–	(3,635)	245,325	3,815	241,510
2001 Series A Tobacco Bonds	15,545	–	(1,365)	14,180	1,335	12,845
1999 Series A Revenue Bonds	81,115	–	(6,950)	74,165	7,395	66,770
Total bonds payable	1,780,600	142,640	(48,675)	1,874,565	46,065	1,828,500
Plus (less):						
Deferred losses on refundings	(14,980)	–	854	(14,126)	(854)	(13,272)
Bonds premium	31,341	5,628	(1,470)	35,499	1,727	33,772
Bonds discount	(5,465)	–	737	(4,728)	(737)	(3,991)
Bonds accretion	3,087	707	–	3,794	3,794	–
Total bonds payable, net	1,794,583	148,975	(48,554)	1,895,004	49,995	1,845,009
Loans payable:						
Series 2011 B Note	–	13,000	(2,859)	10,141	178	9,963
Series 2011 A Note	32,235	–	(2,320)	29,915	5,818	24,097
Series 2010 A Working Capital Notes	131,400	–	–	131,400	–	131,400
Series 2009 A Tax Increment Notes	14,031	1,669	–	15,700	2,175	13,525
Series 2009 Note	5,820	–	(1,554)	4,266	1,639	2,627
Total loans payable	183,486	14,669	(6,733)	191,422	9,810	181,612
Total governmental bonds and loans	$ 1,978,069	$ 163,644	$ (55,287)	$ 2,086,426	$ 59,805	$ 2,026,621

11. Long-Term Liabilities (continued)

The change in other long-term liabilities for governmental activities was as follows for the year ended September 30, 2012 (expressed in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year	Due Thereafter
Other liabilities:						
Accrued compensated absences	$ 58,589	$ 14,281	$ –	$ 72,870	$ 8,115	$ 64,755
Retroactive union arbitration	195,286	–	–	195,286	–	195,286
Litigation	27,263	1,252	(15,607)	12,908	1,033	11,875
Landfill closure and postclosure costs	71,630	768	–	72,398	–	72,398
Accrued arbitrage rebate	–	13,635	–	13,635	13,635	–
Post employment benefit	201,423	43,656	–	245,079	–	245,079
Total other liabilities	$ 554,191	$ 73,592	$ (15,607)	$ 612,176	$ 22,783	$ 589,393

Accrued compensated absences, retroactive union arbitration, litigation, landfill closure and post-closure costs, accrued arbitrage rebates and post-employment benefits to retirees such as health insurance, are generally expected to be liquidated with resources derived from the general fund.

Changes in long-term liabilities for business-type activities were as follows for the year ended September 30, 2012 (expressed in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year	Amounts Due Thereafter
Business-type activities:						
Workers compensation claims	$ 20,342	$ 21,474	$ (15,155)	$ 26,661	$ 12,747	$ 13,914
Loan payable - US Treasury	26,621	15,835	(709)	41,747	41,747	–
Note payable - WICO	22,257	–	(493)	21,764	533	21,231
Total business-type activities	$ 69,220	$ 37,309	$ (16,357)	$ 90,172	$ 55,027	$ 35,145

11. Long-Term Liabilities (continued)

Debt Margin

Pursuant to 48 U.S.C. Section 1574(b)(i) of the Revised Organic Act, the Government may issue revenue bonds for public improvements or undertakings authorized by an act of the Legislature, without limitation as to principal amount. Such revenue bonds are payable solely from the revenue directly derived from and attributable to such public improvements or undertakings. Pursuant to 48 U.S.C. Section 1574(b)(ii), the Government is authorized to issue general obligation bonds for any public purpose provided that no such indebtedness is in excess of 10% of the aggregate assessed valuation of the taxable real property in the U.S. Virgin Islands. In addition, pursuant to 48 U.S.C. Section 1574(a) (Public Law 94-932), the U.S. Virgin Islands is authorized to cause to be issued bonds or other obligations in anticipation of the matching funds to be received from the federal government pursuant to 26 U.S.C. Section 7652(b)(3). There is no legal limit on the value of bonds that the Government may issue pursuant to 48 U.S.C. Section 1574(a). The Legislature of the U.S. Virgin Islands must authorize all bond issuances. PFA is authorized to issue bonds for the purpose of financing any project or for the purpose authorized by the Legislature. Given that PFA's powers to issue bonds are derived from 48 U.S.C. Section 1574(b), the bonds issued by PFA are subject to the limitations of said 48 U.S.C. Section 1574(b).

On August 23, 1999, the Legislature amended the V.I. Code to add a Mandatory Balanced Budget Provision. Such provisions, specifically Title 2 of the V.I. Code Section 256, provide that the amount of debt of the Government existing on October 1, 2000 shall be the debt limit of the Government, exclusive of bond principal and interest that may become due. The debt limit specified under Title 2 of the V.I. Code Section 256 does not include bonds authorized by law for which a specific source of revenue is identified and committed to retiring those bonds. As used in Title 2 of the V.I. Code Section 256, the term "debt" means the total accumulated unpaid obligations that are due and payable, including unpaid income tax refunds, amounts owed to vendors, and current year unpaid debt service obligations, if any. As used in the statute, the term "debt" does not include that portion of principal or interest on bonds that is not yet due and payable.

11. Long-Term Liabilities (continued)

Bonds Payable

Bonds payable outstanding at September 30, 2012 are comprised of the following (thousands):

Bonds Payable	Maturity	Rates (%)	Balance
2012 Series A Revenue Bonds	2032	4.00 - 5.00	$ 142,640
2010 Series A & B Revenue Bonds	2029	4.00 - 5.25	399,050
2009 Series A Revenue Bonds (Cruzan)	2039	3.00 - 6.00	38,075
2009 Series A-1, A-2, B & C Revenue and Refunding Bonds	2040	3.00 - 5.00	420,730
2009 Series A Revenue Bonds (Diageo)	2038	6.00 - 6.75	250,000
2006 Series A Revenue Bonds	2029	3.50 - 5.00	211,680
2006 Series A, B, C & D Tobacco Turbo and Capital Appreciation Bonds	2035	6.25 - 7.625	7,290
2004 Series A Revenue Bonds	2025	4.00 - 5.25	71,430
2003 Series A Revenue Bonds	2033	4.00 - 5.25	245,325
2001 Series A Tobacco Bonds	2031	5.00	14,180
1999 Series A Revenue Bonds	2020	4.20 - 6.50	74,165
Subtotal			1,874,565
Plus (less):			
Deferred costs on refundings			(14,126)
Bonds premium			35,499
Bonds discount			(4,728)
Bonds accretion			3,794
Total			$ 1,895,004

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

On September 1, 2012, the Public Finance Authority ("PFA") issued the 2012 Series A (Working Capital) Revenue Bonds, the proceeds of which amounted to $142.6 million. The Government has pledged matching funds, described below, for the timely payment of the principal and interest on the 2012 Series A Revenue Bonds. The 2012 Series A Bonds bear interest at rates ranging from 4.00% to 5.00%, and mature from 2014 to 2032. The bonds were issued to: (i) provide working capital to the PG to finance various operating expenses, (ii) fund the debt service requirements of the bond issuance, and (iii) pay the costs of issuing the bonds.

The 2012 Series A Bonds maturing on October 1, in the years 2022, 2027, and 2032 are subject to mandatory sinking fund redemptions at a redemption price equal to 100% of the principal amount thereof, plus interest accrued to the date of redemption.

The matching funds pledged for the payment of the bonds consist of annual advance payments received from the U.S. Department of the Treasury of excise taxes imposed and collected under the Internal Revenue laws of the United States on rum products produced in the U.S. Virgin Islands and exported to the United States from the Virgin Islands.

The amount required to be remitted to the Government by the U.S. Department of the Treasury is an amount no greater than the total amount of local revenue (primarily taxes) collected by the Government in each fiscal year. As a result, the term "matching fund revenue" is used to denote these payments.

Amounts to be received by the Government from federal rum excise tax are deposited directly into trust accounts in accordance with the Indenture of Trust for bond debt service payments. The amounts to be received are subject to adjustment for the amount of local revenue actually collected by the U.S. Department of the Treasury during such year. Prepayments of matching fund revenue are recorded as deferred revenue in the accompanying statement of net assets, and recognized as income in the subsequent fiscal year.

The rate of federal rum excise tax is determined by Congress. In November 1999, Congress increased the federal rum excise tax rate from $10.50 to $13.25 per proof gallon. Since then, Congress has extended the higher rate seven times. Under the American Taxpayer Relief Act of 2012, it will be in effect through December 31, 2013.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

On July 8, 2010, the Public Finance Authority ("PFA") issued the 2010 Series A and B Revenue Bonds, the proceeds of which amounted to $399.05 million. The Government has pledged matching funds, described below, for the timely payment of the principal and interest on the 2010 Series A and B Revenue Bonds. The 2010 Series A Bonds, amounting to $305 million, bear interest at rates ranging from 4.00% to 5.00% mature from 2012 to 2029. The 2010 Series B Bonds, amounting to $94.05 million, bear interest at rates ranging from 5.00% to 5.25% and mature from 2025 to 2029.

The bonds were issued to: (i) provide working capital to the PG to finance various operating expenses, (ii) refinance a portion of the outstanding Series 2009 B1 and B2 Notes, (iii) fund the debt service requirements of the bond issuance, and (iv) pay the costs of issuing the bonds.

The 2010 Series A Bonds maturing on October 1, in the years 2020, 2025, and 2029 are subject to mandatory sinking fund redemptions at a redemption price equal to 100% of the principal amount thereof, plus interest accrued to the date of redemption.

The 2010 Series B Bonds maturing on October 1, in the years 2025 and 2029 are subject to mandatory sinking fund redemptions at a redemption price equal to 100% of the principal amount thereof, plus interest accrued to the date of redemption

On December 17, 2009, PFA issued the 2009 Series A Revenue Bonds (the "Cruzan Bonds") amounting to $39.19 million. The Government has pledged matching funds generated from the sale of Cruzan rum products for the timely payment of the principal and interest of the Cruzan Bonds. The Cruzan Bonds bear interest at rates ranging from 3.00% to 6.00% and mature from 2010 to 2039. The proceeds of the Cruzan Bonds were used to: (i) finance the costs of a wastewater treatment facility and renovations at the Cruzan VIRIL, Ltd. ("Cruzan") rum distillery on the island of St. Croix, (ii) fund debt service reserve accounts and (iii) pay the costs of issuing the bonds. The bonds maturing October 1, 2039 are subject to mandatory sinking fund redemptions beginning October 1, 2020, at a redemption price equal to 100% of the principal amount plus interest accrued to the date of redemption.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

In association with the issuance of the Cruzan Bonds, the Government entered into an agreement with Cruzan on October 6, 2009, to provide marketing support payments, production incentive payments, continuation of molasses subsidies and other tax incentives to retain Cruzan as part of the rum industry in the U.S. Virgin Islands. Marketing and incentive payments to Cruzan amounted to $33.5 million, $54.7 million, $40.2 million and $3.9 million for the years ended September 30, 2012, 2011, 2010 and 2009.

On October 1, 2009, PFA issued the 2009 Series A-1, A-2, B and C Revenue and Refunding Bonds, the proceeds of which amounted to $458.84 million. The Government has pledged matching funds for the timely payment of principal and interest on the 2009 Series A-1, A-2, B and C Revenue and Refunding Bonds. The 2009 Series A-1 Bonds amounted to $86.35 million. The 2009 Series A-1 Bonds bear interest at rates ranging from 3.00% to 5.00% and mature from 2010 to 2039. The Series A-1 Bonds were issued to: (i) fund certain capital projects, (ii) fund debt service reserve accounts, and (iii) pay certain costs of issuing the bonds.

The 2009 Series A-2 Bonds amounted to $8.65 million. The 2009 Series A-2 Bonds bear an interest rate of 3.00% and mature from 2010 to 2011. The Series A-2 Bonds were issued to: (i) fund certain capital projects, (ii) fund debt service reserve accounts and (iii) pay certain costs of issuing the bonds.

The 2009 Series B Bonds amounted to $266.33 million, bear an interest rate of 5.00%, and mature from 2010 to 2025. The 2009 Series B Bonds were issued to: (i) current refund the 1998 Series A Bonds, (ii) fund debt service reserve accounts, and (iii) pay certain costs of issuing the bonds.

The 2009 Series C Bonds amounted to $97.51 million, bear an interest rate of 5.00% and mature from 2010 to 2022. The 2009 Series C Bonds were issued to: (i) current refund the 1998 Series E Revenue and Refunding Bonds, (ii) fund debt service reserve accounts and (iii) pay certain costs of issuing the bonds.

The current refunding of the 1998 Series A and E Bonds, on October 28, 2009, was made in order to obtain lower interest rates. The economic gain obtained by this current refunding is the difference between the present value of old debt service requirements and the new debt service.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

This refunding resulted in a debt service saving of approximately $35.9 million and an economic gain of approximately $35.6 million.

The 2009 Series A-1, B and C Bonds are subject to mandatory sinking fund installment redemptions beginning October 1, 2020 at a redemption price equal to 100% of the principal amount, plus interest accrued, to the date of redemption.

On July 9, 2009, PFA issued the 2009 Series A Bonds (the “Diageo Bonds”) amounting to $250 million. The Diageo Bonds mature from 2013 to 2038 at interest rates ranging from 6.00% to 6.75%. The proceeds of the bonds were issued to: (i) provide a grant to Diageo USVI, Inc. (the producer of Captain Morgan rum products) to construct a rum distillery and warehouse on the island of St. Croix, (ii) to redeem the Subordinated Revenue Bond Anticipation Notes Series 2009A issued to finance preliminary costs of the Diageo construction project, (iii) to fund debt service reserve accounts, and (iv) to finance capitalized interest and costs associated with the issuance of the bonds.

The PG has pledged matching funds generated from the sale of Captain Morgan rum products for the timely payment of the principal and interest on the Diageo Bonds. The Diageo Bonds maturing on or after October 1, 2020 are subject to optional redemption on or after October 1, 2019, at a redemption price equal to 100% of the principal amount thereof, plus interest accrued to the date of redemption.

In association with the issuance of the Diageo Bonds, the Government entered into an agreement with Diageo USVI, Inc. on June 17, 2008, to provide marketing support payments, production incentive payments, continuation of molasses subsidies and other tax incentives to attract Diageo USVI, Inc. as part of the rum industry in the U.S. Virgin Islands. Marketing and incentive payments to Diageo USVI, Inc. amounted to $23.1million for the year ended September 30, 2012.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

On September 28, 2006, PFA issued the 2006 Series Gross Receipts Revenue Bonds ("2006 Series Bonds"), the proceeds of which amounted to $219.5 million. The Government has pledged gross receipts tax revenues for the timely payment of the principal and interest on the 2006 Series Bonds. The 2006 Series Bonds bear interest at 3.50% to 5.00% and mature from 2007 to 2029. The proceeds of the bonds were issued to: (i) advance refund a portion of the Series 1999A Revenue Bonds, (ii) pay the cost of a termination fee in connection with an outstanding swap option agreement, (iii) fund certain capital projects, (iv) fund debt service reserve accounts, (v) pay certain costs of issuing the Series 2006 Bonds, and (vi) fund a net payment reserve account for a new swap agreement in connection with the refunding. The 2006 Series Bonds maturing on or before October 1, 2016 are not subject to optional redemption.

The advance refunding of the 2020 through 2029 maturities of the 1999 Series A Bonds was made in order to obtain lower interest rates. The economic gain obtained by this advance refunding is the difference between the present value of old debt service requirements and the new debt service. This refunding resulted in a debt service saving of approximately $40.8 million and an economic gain of approximately $25.6 million.

The proceeds of the 2006 Series Bonds related to the refunding were placed in a trust account to provide for all future debt service payments on the 2020 through 2029 maturities of the 1999 Series A Bonds. Approximately $180 million in funds were deposited into the Escrow Fund accounts. At September 30, 2011, $162.9 million of defeased 1999 Bonds remained outstanding.

On March 15, 2006, the Tobacco Settlement Financing Corporation ("TSFC") issued the 2006 Tobacco Settlement Asset-Backed Bonds, Subordinated Series 2006 A, B, C & D Turbo and Capital Appreciation Bonds amounting to $48.1 million, with an issue value of $7.3 million (net of accretion of $40.8 million). The bonds are secured and payable from collections including all Tobacco Settlement Revenues to be received by TSFC, reserves, amounts held in other accounts established by the indenture and TSFC's rights under the purchase agreement. The proceeds have been used for the purpose of (i) financing several capital hospital and health development projects for the benefit of the Virgin Islands and its residents, (ii) pay certain costs of issuance relating to the Series 2006 Bonds, and (iii) fund operating costs.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

Interest on the Series 2006 Tobacco Settlement Asset-Backed Bonds is not paid currently, but accretes from the date of delivery, compounded every May 15 and November 15, commencing May 15, 2006 through the final maturity date of May 15, 2035. Interest yields on the Bonds range from 6.25% to 7.63%. The series are subject to early redemption at accreted value beginning May 15, 2023, provided that the 2001 Tobacco Settlement Asset-Backed Series A Bonds have been paid in full.

On December 1, 2004, PFA issued the 2004 Series A Bonds, the proceeds of which amounted to $94 million. The Government has pledged the Matching Fund Revenues to the timely payment of principal and interest on the 2004 Series A Bonds. The bonds bear interest at 4.00% to 5.25% and mature from 2005 to 2025. The proceeds of the bonds were issued to: (i) finance the planning, development, constructing, renovating, and equipping of wastewater treatment facilities and collection systems on St. Thomas and St. Croix, (ii) finance the repairs, renovations, and construction of solid waste facilities in the Territory, (iii) finance the repair and construction of public roads in the Territory, (iv) provide start-up capital for the Virgin Islands Waste Management Authority, (v) fund the Series 2004A Senior Lien Debt Service Reserve Subaccount, and (vi) pay certain costs of issuing the Series 2004A Bonds. The Series 2004A Bonds are not subject to optional redemption prior to October 1, 2014.

On December 17, 2003, PFA issued the Series 2003A Revenue Bonds, the proceeds of which amounted to approximately $268 million. The bonds were issued to: (i) repay the Government outstanding Revenue Bond Anticipation Notes, Series 2003, (ii) fund certain necessary public safety and other public sector capital development projects, (iii) fund debt service accounts for the bond issuance, and (iv) to pay certain costs of issuing the bonds. The Government has pledged gross receipts taxes for the timely payment of the principal and interest on the Series 2003A Revenue Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. The Series 2003A Revenue Bonds are not subject to optional redemption prior to October 1, 2014.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

On November 20, 2001, TSFC issued the 2001 Tobacco Settlement Asset-Backed Series A Bonds amounting to $23.7 million of the aggregate principal. The proceeds were used for the purpose of (i) purchasing all rights, title, and interest in certain litigation awards under the master settlement agreement (MSA) entered into by participating cigarette manufacturers, (ii) issuance of Tobacco Settlement Asset-Backed Bonds to pay the purchase price for the rights, and (iii) to provide funds for hospital and healthcare projects in the U.S. Virgin Islands.

Interest on the 2001 bonds is payable semiannually each May and November 15 for the term bonds amounting to $15.5 million and convertible capital appreciation bonds amounting to $8.2 million, with a nominal value of $6.2 million.

The convertible capital appreciation bonds accrete interest prior to November 15, 2007 and accrue interest subsequent to that date. Interest on the capital appreciation bonds will compound on May 15th and November 15th.

The 2001 Series A Tobacco Bonds payable at September 30, 2012 amounted to $14.2 million. Under early redemption provisions, any MSA payments exceeding annual debt service requirements of the 2001 Series A Tobacco Bonds must be applied to early redemption of principal. MSA payments and interest earnings on the trust funds during the year ended September 30, 2012, resulted in early redemption of $100 thousand during fiscal year 2012.

On November 16, 1999, PFA issued the 1999 Series A Revenue Bonds amounting to $299.9 million. These bonds were issued to (i) pay certain working capital obligations of the Government, (ii) repay the Government outstanding tax and revenue anticipation notes, (iii) fund the Series debt service accounts, and (iv) finance certain costs of issuing the bonds.

On September 28, 2006, PFA advance refunded a portion of the 1999 Bonds with maturity dates of October 1, 2020 to October 1, 2029 totaling $162.9 million. The proceeds of the refunding were placed in a trust account to provide for all future debt service payments on the 2020 through 2029 maturities of the bonds. Approximately $180 million was deposited with the refunding bond escrow agent to fund the Escrow Fund accounts. At September 30, 2012, $162.9 million of the defeased 1999 Series A Revenue Bonds remain outstanding.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

The Government has pledged gross receipts taxes for the timely payment of the principal and interest on the 1999 Series A Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. Gross receipts revenue amounted to $152.8 million for the year ended September 30, 2012.

On May 1, 1998, PFA issued the 1998 Series A and B Bonds to advance refund previously issued bonds to obtain lower interest rates. The proceeds of the 1998 Series A and B Bonds were placed in an irrevocable trust account to provide for all future debt service payments on the Highway Revenue Bonds Series 1989, Series 1991, Series 1992, Series 1993, and Series 1994 Bonds. At September 30, 2012, $100.3 million of the above-mentioned defeased bonds were outstanding.

On June 15, 1992, PFA issued the Series 1992 Revenue Bonds. The proceeds of the Series 1992 Revenue Bonds were placed in an irrevocable trust to provide for all future debt service payments on the Series 1989 Revenue Bonds. At September 30, 2012, $100.7 million of defeased bonds were outstanding. Assets held by irrevocable trusts for refunding of prior outstanding debt and the corresponding liabilities are not included in the Government's basic financial statements.

11. Long-Term Liabilities (continued)

Bonds Payable (continued)

Governmental Activities – Bonds

	Revenue Bonds Series 1999 A		Tobacco Bonds Series 2001 A		Revenue Bonds Series 2003 A		Revenue Bonds Series 2004 A		Revenue Bonds Series 2006	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Maturity Year:										
2013	$ 7,395	$ 4,485	$ 1,335	$ 706	$ 3,815	$ 12,262	$ 3,995	$ 3,619	$ 2,805	$ 10,192
2014	7,865	4,057	1,405	642	4,010	12,066	4,195	3,414	2,905	10,049
2015	8,365	3,546	–	572	4,210	11,860	4,405	3,199	3,015	9,901
2016	8,900	2,885	–	572	4,420	11,639	4,625	2,967	3,125	9,747
2017	9,465	2,215	–	572	4,655	11,401	4,865	2,718	3,240	9,588
2018 - 2022	32,175	3,245	3,395	2,690	27,195	52,970	28,440	9,373	42,620	44,361
2023 - 2027	–	–	–	2,011	34,945	45,057	20,905	1,684	90,945	26,638
2028 - 2032	–	–	8,045	1,609	90,430	32,898	–	–	63,025	4,395
2032 - 2037	–	–	–	–	71,645	3,626	–	–	–	–
Total	$ 74,165	$ 20,433	$ 14,180	$ 9,374	$ 245,325	$ 193,779	$ 71,430	$ 26,974	$ 211,680	$ 124,871

	Tobacco Bonds Series 2006		Revenue Bonds Series 2009 A (Diageo)		Revenue Bonds Series 2009 A-1		Revenue Bonds Series 2009 B		Revenue Bonds Series 2009 C	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Maturity Year:										
2013	$ –	$ –	$ –	$ 16,703	$ 1,550	$ 3,928	$ 15,920	$ 11,986	$ 6,675	$ 4,316
2014	–	–	4,040	16,581	1,600	3,881	16,740	11,170	7,015	3,974
2015	–	–	4,290	16,331	1,650	3,830	17,600	10,311	7,210	3,618
2016	–	–	4,575	16,049	1,705	3,773	18,505	9,410	7,745	3,244
2017	–	–	4,890	15,729	1,770	3,710	19,450	8,460	8,040	2,850
2018 - 2022	–	–	30,075	73,033	10,040	17,358	113,285	26,272	45,205	7,762
2023 - 2027	–	–	41,930	61,175	12,685	14,712	46,185	5,170	7,770	194
2028 - 2032	–	–	58,440	44,668	16,255	11,145	–	–	–	–
2032 - 2037	48,145	–	81,815	21,282	20,865	6,529	–	–	–	–
2038 - 2042	–	–	19,945	673	15,265	1,170	–	–	–	–
Less unamortized discount	(40,855)	–	–	–	–	–	–	–	–	–
Total	$ 7,290	$ –	$ 250,000	$ 282,224	$ 83,385	$ 70,036	$ 247,685	$ 82,779	$ 89,660	$ 25,958

	Revenue Bonds Series 2009 A (Cruzan)		Revenue Bonds Series 2010 A		Revenue Bonds Series 2010 B		Revenue Bonds Series 2012 A		Total Government Activities	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Maturity Year:										
2013	$ 585	$ 2,209	$ 1,990	$ 15,148	$ –	$ 4,833	$ –	$ 3,874	$ 46,065	$ 94,261
2014	605	2,186	2,065	15,067	–	4,833	–	7,044	$ 52,445	$ 94,964
2015	640	2,155	2,155	14,983	–	4,833	800	7,028	$ 54,340	$ 92,167
2016	670	2,122	2,270	14,882	–	4,833	825	6,995	$ 57,365	$ 89,118
2017	705	2,087	2,395	14,766	–	4,834	850	6,962	$ 60,325	$ 85,892
2018 - 2022	4,125	9,836	14,050	71,849	1,050	24,101	5,100	34,240	$ 356,755	$ 377,090
2023 - 2027	5,530	8,434	133,360	55,969	50,270	18,713	7,050	32,924	$ 451,575	$ 272,681
2028 - 2032	7,470	6,498	146,715	11,248	42,730	3,444	85,080	27,134	$ 518,190	$ 143,039
2032 - 2037	10,075	3,885	–	–	–	–	42,935	1,073	$ 275,480	$ 36,395
2038 - 2042	7,670	708	–	–	–	–	–	–	$ 42,880	$ 2,551
Less unamortized discount	–	–	–	–	–	–	–	–	(40,855)	–
	$ 38,075	$ 40,120	$ 305,000	$ 213,912	$ 94,050	$ 70,424	$ 142,640	$ 127,274	$ 1,874,565	$ 1,288,158

11. Long-Term Liabilities (continued)

Conduit Debt

In March 2007, the PFA issued private activity bonds, the Refinery Facilities Senior Secured Tax-Exempt Revenue Bonds (HOVENSA Refinery), the “Series 2007 Tax-Exempt Bonds”, amounting to $104.1 million, to finance modifications to diesel and gasoline desulfurization units for a refinery on the island of St. Croix. The bonds have an interest rate of 4.70% and are limited obligations of PFA, payable solely from, and secured by, a pledge and assignment of the amounts payable under a loan agreement between PFA and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the repayment of the bonds. The bonds are not reported as liabilities in the Government’s basic financial statements. The amount outstanding of $104.1 million was subsequently defeased by HOVENSA under a buy-back option offered to bondholders in January 2012.

In April 2004, the PFA issued private activity bonds, the Refinery Facilities Senior Secured Tax-Exempt Revenue Bonds (HOVENSA Refinery), the “Series 2004 Tax-Exempt Bonds”, amounting to $50.6 million, to finance construction of a delayed coking unit for a refinery on the island of St. Croix. The bonds have an interest rate of 5.875% and are limited obligations of PFA, payable solely from, and secured by, a pledge and assignment of the amounts payable under a loan agreement between PFA and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the repayment of the bonds. The bonds are not reported as liabilities in the Government’s basic financial statements. The amount outstanding of $50.6 million was defeased by HOVENSA under a buy-back option offered to bondholders in January 2012.

In December 2003, the PFA issued private activity bonds, the Refinery Facilities Senior Secured Tax-Exempt Revenue Bonds (HOVENSA Refinery), the “Series 2003 Tax-Exempt Bonds”, amounting to $74.2 million, to finance the costs of a Clean Fuels Program for a refinery on the island of St. Croix. The Clean Fuels Program consists of three major projects to comply with regulatory standards for low sulfur gasoline. The Clean Fuels Program is a federally mandated program effective January 2004. The bonds have an interest rate of 6.125% and are limited obligations of PFA, payable solely from, and secured by, a pledge and assignment of the amounts payable under a loan agreement between PFA and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the repayment of the bonds. The bonds are not reported as liabilities in the Government’s basic financial statements. The amount outstanding of $74.2 million was subsequently defeased by HOVENSA under a buy-back option offered in January 2012.

11. Long-Term Liabilities (continued)

Conduit Debt (continued)

In November 2002, the PFA and the PG issued private activity bonds, the Refinery Facilities Revenue Bonds (HOVENSA Coker Project), the "Series 2002 Tax-Exempt Bonds", amounting to $63.8 million and $63 million respectively ($126.8 million in total) to finance costs of construction of a coker plant for a refinery on the island of St. Croix. The bonds have an interest rate of 6.50% and are limited obligations of PFA and the PG, payable solely from and are secured by, a pledge and assignment of the amounts payable under a loan agreement between PFA, PG and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the repayment of the bonds. The bonds are not reported as liabilities in the Government's basic financial statements. The amount outstanding of $126.8 million was subsequently defeased by HOVENSA under a buy-back option offered to bondholders in January 2012.

Notes Payable

On November 14, 2011, PFA entered into the 2011 Property Tax Revenue Anticipation Note (the "Series 2011B Note") in the amount of $13 million. The proceeds were used to pay incentive payments to government employees who elected to retire early under Act No. 7261 the "Economic Stability Act", as amended by Acts No. 7270 and 7307. The Series 2011B Note is a general obligation of the PG, secured by a first priority lien on real property taxes levied for tax years up to and including tax year 2005. Also, the PG has pledged a third subordinate lien on the gross receipts taxes, along with all fines, interest, penalties and other charges related to gross receipts taxes. Interest on the Series 2011B Note accrues monthly at the rate of 4.91% until the Series 2011 B Note reaches maturity on December 15, 2016. On that date, the Series 2011 B Note will convert to a two year term loan. As of September 30, 2012, the outstanding amount of the Series 2011B Note was $10.1 million.

11. Long-Term Liabilities (continued)

Notes Payable (continued)

Debt service requirements for the Series 2011B Note at September 30, 2012 was as follows (expressed in thousands):

Year	Principal	Interest
2013	$ –	$ 488
2014	–	488
2015	–	489
2016	–	490
2017	10,141	112
	$ 10,141	$ 2,067

On April 29, 2011, PFA entered into the Subordinate Lien Revenue Bond Anticipation Notes (the "Series 2011A Notes"), in the amount of $32.2 million, for the purpose of upgrading the broadband infrastructure, equipment and technology in the U.S. Virgin Islands. The Series 2011 A Notes are a general obligation of the PG, secured by gross receipts taxes. Interest on the Series 2011A Notes accrued quarterly at the rate of 4.75% until the Notes reached maturity on April 29, 2012. On that date the Notes were converted to a term loan with Banco Popular de Puerto Rico in the amount of $32.2 million at an interest rate of 6.25% for sixty (60) months. As of September 30, 2012, the outstanding amount on the Series 2011A Notes was $29.9 million.

Debt service requirements for the Series 2011A Notes at September 30, 2012 are as follows (expressed in thousands):

Year	Principal	Interest
2013	$ 5,818	$ 1,705
2014	6,193	1,331
2015	6,591	932
2016	7,015	508
2017	4,298	90
	$ 29,915	$ 4,566

11. Long-Term Liabilities (continued)

Notes Payable (continued)

On November 4, 2010, PFA entered into the Subordinated Lien Revenue Bond Anticipation Notes (the "Series 2010A Notes"), which modified and amended the Series 2009B Notes, extending the maturity date to October 1, 2013, with a maximum amount of $78.84 million from the Agent Lender and $52.56 million from the Syndicate Lender. The Series 2010A Notes are a general obligation of the PG, secured by gross receipts taxes and, commencing October 1, 2012, a set-aside amount equal to four percent (4%) of matching fund revenues. The Series 2010A Notes accrue interest at a rate of 400 points above the 90-day LIBOR rate, not to be less than a minimum rate of 5.50%, with interest payments due on the first business day of the month.

Debt service requirements for the Series 2010A Notes at September 30, 2012 are as follows (expressed in thousands):

Year	Principal
2013	$ –
2014	131,400
	$ 131,400

On September 25, 2009, PFA entered into the Tax Increment Revenue Bond Anticipation Note Purchase Agreement (the "Agreement") with a local bank. Under the terms of the Agreement, the bank will purchase up to $15.7 million in federally taxable Bond Anticipation Notes (the "Series 2009A Notes"). The purpose of the Series 2009A Notes is to provide a loan to the PG (the "Series 2009A Tax Increment Revenue Loan Note") to finance the developmental costs of a shopping complex on the island of St. Croix. The Series 2009A Notes have a term of three years, maturing on October 1, 2012, with interest of 300 points above the J.P. Morgan Chase Prime Rate or 6.25%, whichever is higher. On October 1, 2012, the Series 2009A Notes will convert to a term loan with payments in twenty quarterly payments (five years), based on a twenty-five (25) year amortization schedule, with a final payment on October 1, 2018. Under the terms of the Agreement, PFA may issue Tax Increment Revenue Bonds to defease the debt prior to that date. On October 1, 2012, PFA paid $2 million of the outstanding debt. As of September 30, 2012, PFA had sold $15.7 million in Series 2009A Notes.

11. Long-Term Liabilities (continued)

Notes Payable (continued)

The proceeds were used to: (i) fund a capitalized interest account and (ii) fund the first phase of the development of the shopping center complex. The debt is a special limited obligation of the PG, secured by Tax Incremental Financing ("TIF") revenues. TIF revenues consist of 100% of the incremental property taxes and 90% of the incremental gross receipts taxes, derived from the development project.

Debt service requirements for the Series 2009A Notes at September 30, 2012, were as follows (expressed in thousands):

Year	Principal
2007	
2013	$ 2,175
2014	245
2015	261
2016	275
2017	295
2018	12,449
	$ 15,700

On September 18, 2009, PFA issued the Subordinated Lien Revenue Bond Anticipation Notes (Series 2009B Notes) in two series: the Series 2009 B-1 Notes in the aggregate amount of $150 million with the agent lender First Bank of Puerto Rico and the Series B-2 Notes in the aggregate amount of $100 million with the syndicate lender Banco Popular de Puerto Rico. The purpose of the Notes was to provide working capital to the PG for operating expenses and to pay the costs of the issuances. As of September 30, 2010, $6.4 million of the credit facility remained outstanding. On November 4, 2010, this amount was defeased with the issuance of the Series 2010A Notes.

11. Long-Term Liabilities (continued)

Notes Payable (continued)

In August 2009, the territory reserve balance of the Unemployment Trust Fund (UTF) became inadequate to cover expenditures for unemployment compensation (UC) benefits. UC benefits are an entitlement program administered through the U.S. Treasury, and the PG is legally liable to pay benefits even if the UTF becomes insolvent. As of September 30, 2012, the PG had borrowed $42.4 million from the U.S. Treasury, of which $709 thousand was repaid through FUTA credit reductions. The outstanding UTF loan balance at September 30, 2012 was $41.7 million.

The American Recovery and Reinvestment Act of 2009 (P.L. 111-5 Section 2004) temporarily waived interest payments on UTF loans through September 30, 2011. Beginning in 2012, the loan became subject to interest at a federal rate of 2.943% and the PG paid $1.07 million in interest on the loan during fiscal year 2012.

On February 12, 2009, PFA issued the Subordinate Lien Revenue Bond Anticipation Notes ("Series 2009 Notes"), in the amount of $8 million. The Government has pledged gross receipts taxes for the timely payment of the Series 2009 Notes. The Series 2009 Notes initially had an interest rate of 4.75% and a due date of February 1, 2010. PFA elected a conversion of the Series 2009 Notes to term notes with principal and interest payable semi-annually on February 1 and August 1, at an interest rate of 5.40% and a maturity date of August 1, 2015. The proceeds of the Series 2009 Notes were issued: (i) to finance the purchase and installation of 911 emergency communication equipment for the Virgin Islands Police Department and (ii) to pay certain costs of issuing the Series 2009 Notes.

Debt service requirements for the Series 2009 Notes at September 30, 2012, were as follows (expressed in thousands):

Year	Principal	Interest
2013	1,638	208
2014	1,728	119
2015	900	24
Total	$ 4,266	$ 351

11. Long-Term Liabilities (continued)

Notes Payable (continued)

On June 1, 2008, WICO refinanced its outstanding notes payable and obtained an additional $2.3 million in financing for infrastructure improvements. The consolidated notes amounted to $23.6 million, to be repaid in 120 consecutive monthly installments of $154,953 at a fixed interest rate of 6.2%, plus a final payment of the balance of principal, plus any unpaid interest, in 2018. The notes may be prepaid, in whole, or in part, at any time without penalty.

WICO has pledged all leases and revenues to secure the notes, and may not declare dividends, or issue additional equity interests without lender approval.

As of September 30, 2012, WICO was in compliance with note covenants requiring certain minimum operating revenue thresholds, and the maintenance of a debt service reserve account equal to one year's debt service payments.

Debt service requirements for the WICO loan at September 30, 2012, were as follows (expressed in thousands):

Year:	Principal
2013	533
2014	567
2015	603
2016	641
2017	683
2018	18,737
Total	$ 21,764

11. Long-Term Liabilities (continued)

Fiduciary Funds – Notes Payable

On October 2, 2006, GERS entered into a loan agreement with Banco Popular de Puerto Rico to provide working capital and to pay issuance and closing costs associated with the agreement. The line of credit is a revolving credit facility with a maximum principal amount of $25 million, which accrues interest at a fixed interest rate of 6.25% calculated on a 360-day basis and is due and payable quarterly, commencing on the first day of the fourth calendar month following the closing of the loan. The line of credit facility is available to GERS for a period up to three years, subject to annual renewals. At any time that an event of default occurs, the loan will bear interest at a rate equal to 3% above a variable interest rate based on the bank's transfer rate. The bank retains a certificate of deposit in the amount of $20 million as security on the loan agreement. As of November 5, 2011, GERS cancelled the line of credit facility.

Standby Credit Facility

On October 9, 2010, PFA entered into a standby credit facility ("credit facility") with Banco Popular de Puerto Rico in an aggregate principal amount of up to $45 million. The purpose of the credit facility is to provide financial liquidity for payments required under Chapter 10 of Title 22 of the VIC upon the failure of a Virgin Islands insurance carrier. Under that legislation, the Virgin Islands Insurance Guaranty Fund is to maintain a minimum balance of $50 million for claimant payments. The credit facility is secured and payable from gross receipts taxes. The credit facility will terminate once the Virgin Islands Insurance Guaranty Fund has been restored to an amount of $50 million. The initial term of the credit facility is three (3) years at an interest rate on drawn funds equal to the 90-Day LIBOR plus 400 basis points with a minimum rate of 5.50%, payable quarterly in advance, with an option to extend the credit facility for an additional three (3) year term. The credit facility is subject to: (i) an issuance fee of one-hundred seventy-five (175) basis points annually, payable quarterly in advance, on the outstanding amount of the credit facility for the principal not drawn upon, (ii) a fee upon each draw of twenty-five (25) basis points, and (iii) extension fees to be negotiated with Banco Popular de Puerto Rico, should the credit facility be extended. As of September 30, 2012, no draws have been made on the credit facility, and the amount in the Virgin Islands Insurance Guaranty fund was $18.8 million.

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable

Bonds payable of discretely presented component units are those liabilities that are paid out of resources pledged by such entities. Bonds payable, outstanding at September 30, 2012, are as follows (expressed in thousands):

Bonds Payable	Maturity	Interest Rates (%)	Balance
Virgin Islands Water and Power			
Authority (Electric System)			
Revenue bonds of 2012	2025	4.00 - 6.06	$ 69,145
Revenue bonds of 2010	2033	4.00 - 6.85	80,910
Revenue bonds of 2007	2031	4.50 - 5.00	57,585
Revenue bonds of 2003	2023	4.00 – 5.00	58,175
Virgin Islands Water and Power			
Authority (Water System)			
Revenue bonds of 1998	2017	5.00 - 5.5	19,335
Virgin Islands Port Authority			
Series A Revenue bonds of 2003	2023	5.00 – 5.25	18,005
Series B Revenue bonds of 2003	2015	3.73 – 5.43	5,035
Series C Revenue bonds of 2003	2023	4.40	7,634
Virgin Islands Housing Finance			
Authority:			
Revenue bonds of 1998	2028	4.10 – 5.25	1,255
Revenue bonds of 1995	2025	5.50 – 6.50	895
Subtotal			$ 317,974
Plus unamortized premium			4,697
Less unamortized discount			(109)
Less deferred costs on debt refunding			(90)
Bonds payable, net			$ 322,472
Less amount due within one year			(14,015)
Bonds payable, due in more than one year			$ 308,457

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

Following is a schedule of changes in bonds payable, loans payable and other long-term liabilities for discretely presented component units for fiscal year ended September 30, 2012 (expressed in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year	Amounts Due Thereafter
Bonds payable:						
University of the Virgin Islands	$ –	$ –	$ –	$ –	$ –	$ –
Virgin Islands Water and Power Authority:						
Electric System	226,101	69,160	(24,926)	270,335	6,925	263,410
Water System	21,592	–	(2,367)	19,225	2,815	16,410
Virgin Islands Port Authority	32,836	–	(2,074)	30,762	2,125	28,637
Virgin Islands Housing Finance Authority	2,410	–	(260)	2,150	2,150	–
Total bonds payable, net	282,939	69,160	(29,627)	322,472	14,015	308,457
Notes payable:						
Virgin Islands Economic Development Authority	473	–	(56)	417	24	393
Virgin Islands Water and Power Authority:						
Electric System	36,520	–	(25,493)	11,027	7,594	3,433
Virgin Islands Housing Authority	–	3,155	–	3,155	1,704	1,451
Virgin Islands Port Authority	1,515	3,453	(3,039)	1,929	1,929	–
Virgin Islands Housing Finance Authority	1,526	–	(111)	1,415	77	1,338
University of the Virgin Islands	39,062	11,093	(1,238)	48,917	1,723	47,194
Total loans payable	79,096	17,701	(29,937)	66,860	13,051	53,809
Line of credit payable:						
Virgin Islands Water and Power Authority:						
Electric System	23,000	–	(6,125)	16,875	–	16,875
Water System	2,500	–	–	2,500	–	2,500
Total line of credit payable	$ 25,500	$ –	$ (6,125)	$ 19,375	$ –	$ 19,375
Other long-term liabilities:						
University of the Virgin Islands	$ 5,298	$ –	$ (1,530)	$ 3,768	$ –	$ 3,768
Virgin Islands Housing Authority	6,865	21,139	–	28,004	539	27,465
Virgin Islands Water and Power Authority:						
Electric System	23,570	7,551	–	31,121	–	31,121
Water System	5,371	857	–	6,228	–	6,228
Economic Development Authority	234	1,014	–	1,248	–	1,248
Juan F. Luis Hospital	51	–	–	51	51	–
Virgin Islands Housing Finance Authority	8,148	2,491	–	10,639	–	10,639
Total other long-term liabilities	$ 49,537	$ 33,052	$ (1,530)	$ 81,059	$ 590	$ 80,469

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

In June 2011, the University of the Virgin Islands entered into two capital project loan agreements (loan agreements) in the amounts of $44 million and $16 million, with Rice Capital Access Program, LLC. The purpose of the capital project loans was to: (i) advance refund the University's 1999 Series A Bonds and 2004 Series A Bonds, and (ii) to pay for construction costs of a 100 bed student residence facility and other construction improvement costs of facilities on the St. Thomas and St. Croix campuses. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old outstanding bonds of approximately $4.5 million and an economic gain of $6.8 million.

In May 2012, the Electric System of WAPA issued the: (i) 2012A Electric System Revenues Refunding Bonds amounting to $17.3 million; (ii) the 2012 B Electric System Subordinated Revenue Bonds amounting to $19.7 million; and (iii) the 2012C Electric System Subordinated Revenue Bonds amounting to $32.1 million. The proceeds of the Series 2012A Bonds were used to refund the Electric System Revenue Refunding Bonds, Series 1998 and pay certain costs of issuances of the Series 2012A Bonds. The proceeds of the Series 2012B Bonds were used to refinance a portion of the Electric System Term Loan, make a deposit into the Subordinated Debt Service Reserve Fund sufficient to satisfy the Series 2012B Subordinated Debt Service Fund Requirement and pay certain costs of issuance of the Series 2012B Bonds. The proceeds of the Series 2012C Bonds were used to refinance all or a portion of the Electric System Working Capital Lines of Credit and Overdraft Credit Facility, make a deposit into the Series 2012C Subordinated Debt Service Reserve Fund sufficient to satisfy the Subordinated Debt Service Reserve Fund Requirement and pay certain costs of issuance of the Series 2012C Bonds.

In March 2010, the Electric System issued the $39 million 2010A Electric System Revenue Refunding Bonds; the $9 million 2010B Electric System Revenue Bonds; and the $37 million 2010C Electric System Revenue Refunding Bonds. The proceeds of the Series 2010A Bonds were used to: i) refund a portion of the Electric System Revenue Refunding Bonds, Series 1998, and ii) pay certain costs of issuance of the Series 2010A Bonds. The proceeds of the Series 2010B and 2010C Bonds were used to: i) finance certain capital expenditures temporarily funded through draws on a line of credit ($9 million) and, ii) to make certain deposits into the Debt Service Revenue Fund sufficient to satisfy the Debt Service Reserve Fund requirement. The proceeds of the three series were also used to pay certain costs of issuance of the 2010A, 2010B, and 2010C Revenue and Refunding Bonds.

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

In June 2007, the Electric System issued the $57.6 million 2007A Electric System Subordinated Revenue Bonds, to pay certain costs of issuance of the bonds, to finance the costs of certain capital improvements, refinance capital improvements funded through draws on a Line of Credit and to reinstall a $10 million Line of Credit.

In June 2003, the Electric System issued the Electric System Revenue Bonds, Series 2003, amounting to $69.9 million. The proceeds from the bonds were used to finance capital improvements, repay $18 million of then outstanding lines-of-credit, cover underwriters' costs, and establish a debt service fund. The Series 2003 Bonds maturing on or after July 1, 2023 are subject to redemption prior to their stated maturity date, at the option of the Electric System, on or after July 1, 2013, as a whole or in part at any time, at a redemption price equal to the principal amount thereof plus accrued interest thereon to the date fixed for redemption.

In June 1998, the Electric System issued $110.9 million of 1998 Series A Electric System Revenue and Refunding Bonds. The proceeds from the bonds, and approximately $14 million in funds from the existing debt service and debt service funds, were used to repay outstanding line-of-credit balances, to provide for approximately $30 million in funds for the construction of certain capital projects, and to pay underwriters discount and issuance costs of approximately $1.7 million. The remaining proceeds were used to purchase direct obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining $69 million principal amount of the 1991 Series A Electric System Revenue Bonds.

Under the terms of the Bond Resolution relating to the Electric System Revenue and Refunding Bonds, payment of the principal and interest is secured by an irrevocable lien on the Electric System's net revenue, (exclusive of any funds that may be established pursuant to the Bond Resolution for certain specified purposes), including the investments and income, if any, thereof.

Under the General Resolution, the Authority is required to maintain a Debt Service coverage ratio at least equal to 1.25 times (125%) the principal of and interest on all Outstanding Senior Bonds for the current and each future fiscal year (the Senior Coverage).

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

Under the Electric System Subordinated Revenue Bond Resolution, adopted by the Authority on May 17, 2007, as amended and supplemented (the Subordinated Bond Resolution), the Authority must satisfy the Debt Service coverage ratio of the General Resolution for the Senior Bonds, must maintain a Subordinated Debt Service coverage ratio at least equal to 1.15 times (115%) the principal of and interest on all Outstanding Bonds (the Senior and Subordinate Coverage) and all Outstanding Subordinated Bonds for the current and each future fiscal year, and must maintain at least 1.0 times (100%) the Maximum Aggregate Debt Service for each such fiscal year (total debt coverage).

For the year ended June 30, 2012, the Authority's debt coverage ratio was 193% for senior coverage, 157% for senior and subordinate coverage and 102% for total debt coverage. Section 606(2) of the Subordinated Bond Resolutions provides that if the Authority fails to achieve the required coverage ratios, then the Authority must "take whatever steps it can to produce the amount of net electric revenues required in the following year". Section 701(3) of the Subordinated Bond Resolutions further provides that if the covenant default continues for 60 days after notice of default without the Authority proceeding with diligence to cure the default. The Authority believes it is taking such steps currently to ensure future compliance with required debt coverage ratios.

The Electric System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the Electric System was damaged, destroyed, taken, or condemned, or (ii) any for-profit nongovernmental investor shall acquire an ownership interest in some or all of the assets of the Electric System.

In December 1998, the Water System of WAPA issued the 1998 Water System Revenue and Refunding Bonds amounting to $44.2 million. The proceeds from the bonds were used to repay the 1990 Series A Water System Revenue Bonds at a redemption price of 100% and to refund the 1992 Series B Water System Revenue Bonds, repay outstanding lines of credit balances, pay underwriters' costs, provide funding for a Renewal and Replacement Reserve Fund, and to purchase obligations of the United States Government, which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining principal amount of the 1992 Series B Bonds.

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

Payment of principal and interest of the 1998 Series Bonds is secured by an irrevocable lien on the Water System's net revenues (exclusive of any funds that may be established pursuant to the Bond Resolution for certain other specified purposes) and funds established under the Bond Resolution, including investment securities. To provide additional security, the Water System has conveyed to the bond trustee, a subordinate lien and security interest in the Water System's General Fund. The Water System is also required to make deposits in a debt service reserve fund in accordance with the Bond Resolution.

The Bond Resolution contains certain restrictions and commitments, including the Water System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net water revenue, as defined, that will be at least 125% of aggregate annual principal and interest payments. The Water System's net water revenue for the fiscal years ended June 30, 2012 and 2011 was 42% and 118% of the aggregate debt service as defined in the Bond Resolution. Section 606(2) of the Bond Resolution provides that if the Authority fails to achieve the 125% coverage, the Authority must "take whatever steps it can to produce the amount of net water revenue required in the following fiscal year". Section 701(3) of the Bond Resolution defines this as a condition of default unless the Authority is proceeding with diligence to cure such default. The management of the Water System advises it is taking necessary steps to ensure future compliance with debt coverage ratios.

The 1998 Series Bonds maturing on or after July 1, 2010 are subject to redemption prior to their stated maturity date, at the option of the Water System, as a whole or in part at any time, at a redemption price of 101% through June 30, 2010 and 100% thereafter. The Water System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the water system shall be damaged, destroyed, taken, or condemned or (ii) any for-profit non-governmental investor shall acquire an ownership interest in some or all assets of the Water System.

In January 2003, VIPA issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable) with principal amounts of approximately $18 million and $17.4 million, respectively. VIPA is using the proceeds of the bonds to finance the dredging, rehabilitation, and construction of berthing piers for cruise and seagoing vessels at Crown Bay in St. Thomas, and the construction of a mixed used commercial facility.

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

In October 2003, VIPA issued the Marine Revenue Bonds Series 2003C (non-AMT), with an authorized principal amount not to exceed approximately $10.8 million. VIPA used the proceeds of the bonds to finance the completion of several projects of rehabilitation and construction of berthing piers and dredging for cruise and seagoing vessels at Crown Bay on the island of St. Thomas, and the construction at Red Hook, Enighed Pond, Gallows Bay Dock, and dredging of the Charlotte Amalie Harbor.

The bonds' indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance, and other costs as specified in the corresponding bond indentures. The bonds' indentures also specify certain debt service coverage requirements determined from net available revenue (as defined) of the Authority's Marine Division. The provisions of each of the bonds' indentures require that rates and fees charged for the use of each facility should be sufficient to generate enough revenue to pay all operation and maintenance expenses, exclusive of depreciation and certain noncash charges, of the respective facilities, plus: (i) at least 125% of the principal and interest and redemption account sinking fund deposit requirement of each of the bonds becoming due during such year; (ii) the amount of the debt service reserve fund deposit requirement for such period; (iii) the deposit required to the Renewal and Replacement Fund; and (iv) the amount of the capital improvements appropriations for such period.

For the year ending September 30, 2012, VIPA did not comply with the requirement to issue the audited financial statements within 150 days after year-end. However, as per the Authority's bond indenture, this noncompliance event does not constitute an event of default until the Trustee sends a notification of failure and such failure continues for 90 days. VIPA did receive notification from its Trustee, but noncompliance was covered within the 90 days.

In August 1998, VIHFA issued the 1998 Revenue Bonds Series A in the amount of $3 million, and on March 1, 1995, VIHFA issued the 1995 Revenue Bonds Series A in the amount of $6.2 million, for the purpose of building single-family housing. The indenture agreements for the bonds require the VIHFA to deposit with the trustee the full amount of the bond proceeds, to purchase Government National Mortgage Association (GNMA) certificates. The servicer is obligated to pay the principal and interest due on the GNMA certificates to the trustee in an amount equal to the scheduled principal and interest payments of the underlying mortgages. All mortgage loans issued by the VIHFA must be originated by the participants and secured by a first priority mortgage lien on the applicable single-family residences.

11. Long-Term Liabilities (continued)

Component Units – Bonds Payable (continued)

Fixed maturities required to pay principal and interest on discretely presented component units' bonds payable with fixed maturities at September 30, 2012 are as follows (expressed in thousands):

Year	Principal	Interest	Total
2013	$ 15,070	$ 15,198	$ 30,268
2014	15,713	14,546	30,259
2015	16,417	13,852	30,269
2016	17,172	13,091	30,263
2017	18,008	12,255	30,263
2018 – 2022	91,765	47,514	139,279
2023 – 2027	73,499	26,333	99,832
2028 – 2032	59,060	9,108	68,168
2033 – 2037	11,270	1,019	12,289
Total	317,974	$ 152,916	$ 470,890
Plus unamortized premium	4,697		
Less unamortized discount	(109)		
Less deferred costs on debt refunding and reacquisition	(90)		
Bonds payable, net	$ 322,472		

12. General Tax Revenue

For the year ended September 30, 2012, general tax revenue of the PG consisted of the following (expressed in thousands):

	General	PFA Debt Service	PFA Capital Projects	Other Governmental	Total
Income taxes	$ 311,157	$ –	$ –	$ –	$ 311,157
Real property taxes	89,681	–	–	10,232	99,913
Gross receipts taxes	6,876	147,473	1,847	250	156,446
Excise taxes rum products	118,149	73,751	–	3,500	195,400
Other taxes	72,899	–	–	3,676	76,575
Tax revenue	$ 598,762	$ 221,224	$ 1,847	$ 17,658	839,491
Tax revenue not recognized on the full accrual basis					(59,176)
Total tax revenue - government-wide					$ 780,315

13. Governmental Fund Balances

For the year ended September 30, 2011, the PG implemented Statement No. 54 of the Governmental Accounting Standards Board, *"Fund Balance Reporting and Governmental Fund Type Definitions."* This Statement establishes criteria for classifying fund balances into specifically defined classifications and clarifies definitions for governmental fund types. The classifications reported by the PG include: nonspendable fund balance, restricted fund balance, committed fund balance, assigned fund balance, and unassigned fund balance.

The PG utilizes the classification of: (i) nonspendable fund balance to report prepaid expenses, (ii) restricted fund balance to report debt service accounts, (iii) committed fund balance to report fund balances restricted by grantors, external parties, regulations and litigation, (iv) assigned fund balances to report those funds assigned by the legislature, boards and authorities of the PG, and (v) unassigned fund balances of the General Fund.

The PG's policy is to expend unassigned fund balances before assigned, committed or restricted balances.

13. Governmental Fund Balances (continued)

Following is a detail of the aggregated fund balances presented in the Balance Sheet – Governmental Funds as of September 30, 2012:

	General	PFA Debt Service	PFA Capital Projects	Other Governmental	Total
Fund balances:					
Restricted for:					
Debt Service	$ –	$ 221,503	$ –	$ –	$ 221,503
Capital Projects	–	–	97,386	–	97,386
General Government	–	–	–	20,560	20,560
Public Safety	–	–	–	(4,599)	(4,599)
Health	–	–	–	3,721	3,721
Public Housing and Welfare	–	–	–	5,827	5,827
Education	–	–	–	(9,587)	(9,587)
Transportation and Communication	–	–	–	3,627	3,627
Culture and Recreation	–	–	–	8	8
Total Restricted	–	221,503	97,386	19,557	338,446
Committed to:					
General Government	28,416	–	–	12,066	40,482
Public Housing and Welfare	–	–	–	152	152
Transportation and Communication	–	–	–	8,186	8,186
Culture and Recreation	683	–	–	353	1,036
Total Committed:	29,099	–	–	20,757	49,856
Assigned to:					
General Government	–	–	–	45,859	45,859
Public Safety	–	–	–	208	208
Health	–	–	–	(752)	(752)
Public Housing and Welfare	–	–	–	1,619	1,619
Education	–	–	–	(8,463)	(8,463)
Transportation and Communication	–	–	–	5,358	5,358
Culture and Recreation	–	–	–	142	142
Total Assigned	–	–	–	43,971	43,971
Unassigned	(8,649)	–	–	–	(8,649)
Total Fund Balances	$ 20,450	$ 221,503	$ 97,386	$ 84,285	$ 423,624

The assigned fund balance includes approximately $74.3 million in unexpended encumbrances. Encumbrances are utilized to determine commitments related to unperformed (executor) contracts for goods and services, and to prevent the over-spending of an appropriation.

14. Commitments and Contingencies

Primary Government

Collective Bargaining Agreements

The current labor relations environment of the Government is defined by 13 distinct labor organizations subject to approximately 26 collective bargaining agreements. Fourteen bargaining units are without collective bargaining agreements. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and nonprofessional workers in different departments throughout the Government, represented by different unions. Of the approximately 9,600 government workers, including employees of the executive branch of the Government, approximately 7,200 belong to unions. The present collective bargaining statute requires binding arbitration for certain classified employees in the event of an impasse during salary negotiations between the Government and any union. Under this process, each side chooses an arbitrator and a third impartial arbitrator is selected by the chosen arbitrators. The arbitration panel investigates and reviews the issues in dispute and renders a final and binding decision. For other classified employees, the Government must decide to go to impasse or to enjoin any strike.

As of September 30, 2012, the Government has contractual liabilities for retroactive union arbitration salary increases estimated at $195.2 million accruing from fiscal years 1993 through 2012, as established by the Virgin Islands Retroactive Wage Commission.

Under Title 24, Section 374(h) of the Virgin Islands Code, the PG may not make any payments of retroactive salaries until there is an appropriation of funds by the Legislature.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Federal Assistance Programs

The Government receives financial assistance from the federal government in the form of loans, grants, and entitlements. Loans received are described in Note 11. Monetary and nonmonetary federal financial assistance to governmental funds amounted to approximately \$209.4 million and \$52.3 million, respectively, for the year ended September 30, 2012.

In February 2009, the federal government passed the American Recovery and Reinvestment Act ("ARRA") to create jobs and stimulate the economy. Under Title I, Section 1001(b) of ARRA, the federal government acknowledged that certain refundable tax credits authorized by the Act imposed an economic hardship on United States territories that operate under "mirror" income tax systems. To alleviate this economic hardship, Congress provided for federal loss reimbursements to the mirrored system territories. During fiscal years 2009, 2010, and 2011, the PG received \$23.4 million, \$21.1 million and \$7.7 million in loss reimbursements for the Making Work Pay refundable tax credit. During fiscal year 2011 and 2012, the PG received \$18.6 and \$5.1 million in loss reimbursements of the Additional Child Tax refundable tax credit.

Receipt of grants and loss reimbursements is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under OMB Circular A-133. Disallowances as a result of these audits may become liabilities of the Government.

Management of the Government believes that the future outcome of any changes in federal financial assistance programs will not have a material adverse effect on the basic financial statements.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Compliance Agreement U.S. Department of Education

On September 23, 2002, the Government entered into a three-year compliance agreement with the U.S. Department of Education requiring that the Government develop integrated and systemic solutions to problems in managing its federally funded education programs. The compliance agreement focuses on the areas of program design and evaluation, financial management, human capital, and property management and procurement. The compliance agreement expired on September 23, 2005. The Government had not fully complied with all terms and conditions of the compliance agreement. The U.S. Department of Education subsequently implemented a special condition for the Government to designate a third-party fiduciary to administer U.S. Department of Education grants.

On August 22, 2006, the PG entered into a contract with a third-party fiduciary to administer U.S. Department of Education grants, effective October 1, 2006. The terms and conditions of the original compliance agreement have been extended until the Government is in full compliance with the agreement.

Legal Proceedings and Litigation Claims

The Government is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Title 33, Section 3411(c) of the V.I. Code, no judgment shall be awarded against the Government in excess of $25,000 for tort claims filed under Government statutes. In cases involving several survivors, each award must be construed separately for purposes of applying the limitation upon recovery imposed by the Tort Claims Act. Under Title 27, Section 166(e) of the V.I. Code, the Government's waiver of immunity is expanded to $250,000 for medical malpractice actions, including actions for wrongful death based on malpractice. Under certain circumstances, as provided in Title 33, Section 3414 of the V.I. Code, the Government may assume the payment of a judgment entered against an officer or employee who acted reasonably and within the scope of his employment. The Government may pay up to a maximum amount of $100,000 of the settlement. With respect to pending and threatened litigation, the Government has accrued a provision for legal claims and judgments of approximately $12.9 million for awarded and anticipated unfavorable judgments as of September 30, 2012. Management believes that any liability in excess of amounts recorded will not have a material effect on the basic financial statements.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Legal Proceedings and Litigation Claims (continued)

Changes in the reported provision for legal claims since October 1, 2010, resulted from the following activity (expressed in thousands):

	Beginning Balance at October 1, 2010	New Claims	Claim Payments and Changes in Estimates	Ending Balance at September 30, 2011
Provision for legal claims	$ 20,804	$ 20,995	$ (14,536)	$ 27,263

	Beginning Balance at October 1, 2011	New Claims	Claim Payments and Changes in Estimates	Ending Balance at September 30, 2012
Provision for legal claims	$ 27,263	$ 1,252	$ (15,607)	$ 12,908

The breakdown of the provision for legal claims at September 30, 2012 is as follows (expressed in thousands):

Governmental activities	
Current portion of provision for legal claims	$ 1,033
Long-term portion of provision for legal claims	11,875
	$ 12,908

14. Commitments and Contingencies (continued)

Primary Government (continued)

Property Tax Assessments

As of September 2002, the Government was a defendant in a lawsuit regarding the assessment of property taxes. Under the lawsuit, taxpayers asserted that properties should be assessed at actual value in accordance with the Organic Act of 1933. The U.S. District Court agreed with the plaintiffs and, in May 2003, imposed an injunction on the collection of real property taxes at values higher than the 1998 assessed value. The Government complied with the Court order to develop a plan to implement the new valuation method. In February 2007, the 2005 property tax assessments, based on 1998 assessment levels, were issued. In August 2008, the 2006 property tax assessments, based at actual value in accordance with the Organic Act of 1933, were issued. In September 2008, the 2006 property tax bills were rescinded by court order. In May 2009, the Government received court approval to reissue the 2006 property tax assessments; however, that approval was rescinded in June 2009. The Government subsequently issued the 2006, 2007 and 2008, 2009 property tax assessments, based on 1998 assessment levels, in April 2010, February 2011, August 2011, and February 2012 respectively. The 2010, 2011 and 2012 property tax assessments were issued in June 2012, February 2013 and July 2013 at the 2008 assessment levels.

Landfill Closure and Post-Closure Costs

Federal laws and regulations, including the Clean Air Act, 42 U.S.C. § 7401 *et seq*. ("CAA"), and regulations promulgated thereunder, including the federal standards set forth in 40 C.F.R. Part 62, Subpart GGG ("Federal Plan"), and the National Emission Standards for Hazardous Air Pollutants for Municipal Landfill Maximum Achievable Control Technology, set forth in 40 C.F.R. Part 63, Subpart AAAA ("Landfill MACT"), and the Solid Waste Disposal Act, 42 U.S.C. § 6901 *et seq*. ("RCRA"), and regulations promulgated thereunder, including federal municipal solid waste landfill operating, closure, and post-closure criteria set forth in 40 C.F.R. Part 258, and three EPA administrative orders issued pursuant to RCRA § 7003(a), 42 U.S.C. § 6973(a), and Territorial laws and regulations, including V.I. Code Title 19, Chapter 56 (Solid and Hazardous Waste Management), Title 12, Chapter 9 (Air Pollution Control), and Title 12, Chapter 21 (Virgin Islands Coastal Zone Management), and regulations promulgated thereunder, require the Government to construct and operate certain environmental control systems and otherwise comply with certain requirements during operation of each of its landfill sites, properly close the site (including placement of a final landfill cover) when the landfill (or portion thereof) stops accepting waste, and perform certain post-closure maintenance and monitoring functions at the site for 30 years following closure. Compliance costs during the operational phase will be paid prior to closure.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Landfill Closure and Post-Closure Costs (continued)

Although closure and post-closure costs will be paid only near or after the date that the landfill stops accepting waste, the Government reports a portion of these closure and post-closure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The $72.3 million reported as landfill compliance, closure, and post-closure care liability at September 30, 2012, represents the cumulative amount reported to date based on the use of the estimated capacity of each landfill. The Government will recognize the remaining estimated cost of closure and post-closure care as the remaining estimated capacities are filled. These amounts are based on what it would cost to perform all closure and post-closure care as of September 30, 2012.

The estimated used capacity and expected closure of each of the Government landfills is as follows:

Landfill	Estimated used capacity	Estimated closure date
Bovoni	66%	2020
Angilla	100%	Closed
Susannaberg	100%	Closed

The actual cost to perform closure and post-closure may be higher due to inflation, changes in technology, or changes in regulations. The Government is required by state and federal laws and regulations to make annual contributions to a trust to finance closure and post-closure care. The Government began making annual contributions to a trust in fiscal year 2007 to finance closure and post-closure costs. The Government expects that future inflation costs will be paid from interest earnings on these annual contributions and other financing measures. However, if interest earnings and financing measures should prove to be inadequate, or additional post-closure care requirements are determined due to changes in technology or applicable laws or regulations, these costs may need to be covered by charges to future landfill users.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Wastewater Treatment Plant Consent Decree

Since 1985, the Government has been subject to a consent decree issued by the Virgin Islands District Court, governing the operation of its wastewater treatment plants. The consent decree was amended in 1996 and further modified with the 2002 Stipulation to the Amended Consent Decree (the Stipulation) to establish deadlines for the construction of new secondary treatment facilities, including the replacement of the existing St. Croix and Airport Lagoon (Charlotte Amalie) wastewater treatment plants. The Stipulation requires that the new St. Croix wastewater treatment plants be completed by the end of 2006 and the new Charlotte Amalie wastewater treatment plants be completed by the end of 2007. The cost of both facilities is estimated at approximately $50 million. The Stipulation also establishes certain interim deadlines and performance standards that must be met by the Government pending completion of the new facilities. In addition, the Stipulation establishes specified penalties for violation of any of the deadlines or performance standards set forth therein. As of the date of the basic financial statements, the Government is current on all of its outstanding obligations pursuant to the stipulation. In January 2004, the Government's Legislature authorized the creation of the Virgin Islands Waste Management Authority (WMA) for the purpose of meeting environmental requirements of waste treatment in the U.S. Virgin Islands. On December 2004, the PFA issued revenue bonds amounting to $94 million for the purpose of constructing and rehabilitating wastewater treatment plants noted above.

Memorandum of Understanding - EPA

On August 21, 2002, the Government and the United States Environmental Protection Agency (EPA) entered into a memorandum of understanding documenting the EPA's agreement to support the renewal of the Territorial Pollutant Discharge Elimination System permit for its St. Croix distillery operations provided that the Government make certain funding available to (1) conduct treatability studies regarding the Virgin Islands Rum Industries, Ltd. effluent and the means to mitigate its potential environmental effects in the vicinity of the discharge, (2) identify practicable, available, reliable, and cost-effective potential mitigation measures, and (3) implement (or assist in the implementation of) such mitigation measures in the event such measures are determined by the V.I. Department of Planning and Natural Resources after consultation with EPA to be necessary and appropriate.

14. Commitments and Contingencies (continued)

Primary Government (continued)

Memorandum of Understanding – EPA (continued)

Pursuant to the memorandum of understanding, the Government's obligation to fund such activities is limited to $6 million in the aggregate, commencing on October 13, 2003. In June 2004, the Government entered into a three year contract with a locally licensed environmental consulting firm to facilitate the Government's commitments with the memorandum of understanding with the EPA.

Workers' Compensation Liability

The Government is exposed to risk of loss related to workers' compensation claims. The Government is self-insured for this risk. Self-insured risk liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend upon such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

Changes in the claims liability amount in fiscal year 2012, as recorded in the Government Insurance Fund was as follows (expressed in thousands):

	2011	2012
Claims payable - October 1	$ 17,899	**$ 20,342**
Incurred claims and changes in estimates	11,094	**10,878**
Payments for claims and adjustments expenses	(8,651)	**(4,559)**
Claims payable - September 30	$ 20,342	**$ 26,661**

The Government continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

14. Commitments and Contingencies (continued)

Component Units

In September 1989, WAPA Electric facilities were damaged by Hurricane Hugo. WAPA reconstructed the facilities with proceeds from insurance and FEMA. Subsequent to the receipt of funds, FEMA de-obligated approximately $7.9 million in questioned costs. Approximately $2.6 million of these questioned costs related to an oil spill that was subsequently settled with FEMA. During 1998, WAPA submitted a second appeal for $4.4 million of the remaining questioned costs, and agreed to refund approximately $900 thousand of questioned costs to FEMA. During 1999, FEMA denied the second appeal and formally closed the disaster claim. WAPA has recorded a liability for $5.0 million related to the questioned costs. FEMA has not made a formal request for repayment of the funds.

In September 2005, WAPA Electric facilities were damaged by Tropical Storm Jeanne. Damages amounted to $1.3 million, and FEMA has determined that $438 thousand is eligible for reimbursement. WAPA has reported a receivable of $438 thousand as of June 30, 2012.

In October 2008, WAPA Electric facilities on the island of St. Croix were damaged by Hurricane Omar. WAPA has expended $2.7 million for storm cleanup and system restoration as of June 2010. The territory was declared a federal disaster after the hurricane and is eligible for reimbursement of 75% of what was expended according to the category of the damage. WAPA Electric has recorded a receivable from FEMA through the Office of Management and Budget – Public Assistance (OMB-PA) amounting to approximately $2.3 million.

In August 2010, WAPA Electric facilities were damaged by Hurricane Earl. WAPA has expended over $2 million for storm clean-up and restoration, which was completed in October 2010. The territory was declared a Federal disaster area after the Hurricane and is eligible for reimbursement of 75% - 80% of what was expended according to the category damage. WAPA recorded a receivable of $1.0 million from FEMA through the Virgin Islands Territorial Emergency Management Agency (VITEMA) Public Assistance Program as of June 30, 2012.

On September 30, 2011, WAPA Electric entered into a Memorandum of Agreement (MOA) with viNGN, Inc., a Virgin Islands corporation and wholly owned subsidiary of the PFA. The MOA terms call for WAPA Electric to provide in-kind contributions in connection with a federal grant received by viNGN, Inc. The in-kind contributions consist of the use of certain facilities, equipment and communications infrastructure. The total in-kind match value budgeted by WAPA was $15.2 million. The term of the MOA is twenty-five (25) years upon execution, with two additional twenty-five (25) year terms unless either party provides a written notice of non-renewal not less than twelve (12) months, but no sooner than twenty-four (24) months prior to the expiration of the original term or any additional term.

14. Commitments and Contingencies (continued)

Component Units (continued)

In 2002, the Federal Aviation Administration (FAA) conducted an on-site wildlife evaluation of the Anguilla Landfill, which is located next to the St. Croix airport. The FAA determined that the landfill posed an environmental and navigational threat to the airport due to flocks of birds that reside in the landfill area. The FAA may require VIPA to repay $9.3 million in federal grants and has refused further discretionary grants for the airport until VIPA shows progress toward closing the landfill. The landfill is now under the jurisdiction of the WMA. VIPA negotiated a remediation plan with FAA to close the landfill by December 2009, and subsequently WMA received an extension on the closure date to January 31, 2012. WMA has subsequently entered into a consent decree, extending the closure date to the year 2020, while diverting incoming solid waste to a newly constructed transfer station. Under the consent decree, WMA must pay penalties of $50 thousand in installment of $12.5 thousand over the next four years.

The Governor Juan F. Luis Hospital and Medical Center owns a 40% interest in a radiology practice that operates within the hospital. The radiology practice pays rent to the hospital and the hospital pays for services to hospital patients. As of September 30, 2012 and 2011, the hospital owed the radiology practice $6.6 million and $5.5 million respectively. As a result of the unpaid service fees, the hospital incurred an impairment loss of $2.4 million in its investment in the radiology practice.

WAPA, VIPA, and other discretely presented component units are presently a defendant or codefendant in various lawsuits. The financial managers of the component units have advised the PG that any adverse outcome involving a material claim is expected to be substantially covered by insurance. Government property is exempt from lien, levy, or sale as a result of any judgment under the Virgin Islands Code.

15. Retirement Systems

Plan Description

GERS is the administrator of a cost-sharing, multiple-employer, defined-benefit pension plan established as of October 1, 1959 by the Government to provide retirement, death, and disability benefits to its employees. The following description of the plan is provided for general information purposes only. Refer to the actual text of the retirement law in the V.I. Code, Title 3, Chapter 27 for more complete information. Regular employees are eligible for a full-service retirement annuity when they have completed 30 years of credited service or have attained the age of 60 with at least 10 years of credited service. Members who are considered "safety employees," as defined in the V.I. Code, are eligible for full retirement benefits when they have earned at least 20 years of government service or have reached the age of 55 with at least 10 years of credited service. Regular employees who have attained the age of 50 with at least 10 years of credited service can elect to retire early with a reduced benefit. Senators and members of the Legislature may receive a retirement annuity when they have attained the age of 50 and upon the completion of 6 years of credited service as a member of the Legislature.

Funding Policy

The monthly annuity benefit payment is determined by applying a stipulated benefit ratio to the member's average compensation. Average compensation is determined by averaging the five highest years of salary the member earned within the last ten years of service, subject to the maximum salary limitation in effect during such service. The maximum annual salary that can be used in this computation is $65,000, except for senators and judges, whose annual salary is used. The board of trustees of GERS may set cost-of-living increases for annuitants and pensioners and determine when the annuity should be paid on the basis of the most recent actuarial valuation and the Consumer Price Index.

15. Retirement Systems (continued)

Funding Policy (continued)

GERS is a blended component unit included in the financial reporting entity and is presented as a pension trust fund of the PG. GERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Employees' Retirement System of the Government of the Virgin Islands, 3438 Kronprindsens Gade, St. Thomas, Virgin Islands 00802.

Contributions to GERS are made by the Government and the members. Government and members contributions are not actuarially determined but are set by statute. The Government and members' contributions together with the income of GERS should be sufficient to provide an adequate actuarially determined reserve for the benefits prescribed by the VI Code.

The contributions required to fund GERS on an "actuarial reserve basis" are calculated periodically by the GERS actuarial consultant. The actuarial valuation as of September 30, 2012, indicates that the current combined statutory employer and employee contribution rates are not sufficient to meet the cost of the pension trust fund on an actuarial basis, as required by law.

The Government's required contribution for the year ended September 30, 2012 was 17.5% of the member's annual salary. Since April 1, 1991, required member contributions are 8% of annual salary for regular employees, 9% for senators, 11% for judges, and 10% for safety (hazardous employees) and eligible employees under Act 5226. Prior to June 29, 2000, member contributions were refundable without interest upon withdrawal from employment before retirement. Effective November 2, 2005, legislation was passed that provided for annual interest on refunded contributions of not less than 2%, nor more than 4%, per annum. GERS Board of Trustees approved a 2% effective annual interest rate on refunded contributions effective July 1, 2009. The Government's estimated annual required contributions (based on a fiscal year 2006 actuarial valuation), actual contributions made, and percentage contributed to the plan for the years ended September 30, 2012, 2011, and 2010 were as follows (expressed in thousands):

	Contractually Required Contributions	Contributions Made	Percentage Contributed
2010	$ 77,005	$ 77,005	100%
2011	$ 80,850	$ 80,850	100%
2012	$ 66,677	$ 66,677	100%

15. Retirement Systems (continued)

Funding Policy (continued)

In August 1994, legislation providing an early retirement incentive was passed. The legislation was subsequently amended on October 13, 1994, December 30, 1994, and December 5, 1995. Among other matters, the legislation allows a member of GERS who has a combined aggregate number of years of credited service plus number of years of age, equal to at least 75 years as of the date of the legislation, to retire without reduction of annuity. Members, who have attained the age of 50 with at least 10 but less than 30 years of credited service, may add an additional 3 years to their age for this computation. Members with 30 years of service or who can retire without penalty under the V.I. Code shall have their average compensation increased by 4 percentage points.

For each employee electing to retire pursuant to Section 8(a) of the Early Retirement Act of 1994 (the Act), the Government contributes to GERS, on a quarterly basis, an amount equal to the employer and employee contributions that would have been made until the employee reached the age of 62 had the employee not elected to retire under this provision.

For employees electing to retire under Section 8(b) of the Act, the Government contributes to GERS a sum equal to the additional contribution the employer and employee would have made had the employee received a salary 4% higher during the three years used to compute the employee's average compensation figure, plus a sum of $5,000. Based on this calculation, the amount due to GERS was $26.9 million as of September 30, 2012, of which $26.9 million had been remitted to GERS.

The actuaries of GERS have determined that the specific funding provided under the Act is inadequate to cover the costs of the program. GERS is seeking to recover any unfunded costs of the program under a newly enacted provision of the retirement law, which provides that the Government will compensate GERS for the costs of any special early retirement program.

15. Retirement Systems (continued)

Funding Policy (continued)

The University has two retirement plans in which all eligible employees are required to participate, the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) and GERS. The TIAA-CREF is a defined-contribution pension plan covering participating, full-time faculty members and other exempt employees, under which the contributions, including employees' contributions, are used to purchase annuities. There are no unfunded past service costs, and vested benefits are equal to the annuities purchased under TIAA-CREF. As of September 30, 2012, 235 faculty members and other employees were TIAA-CREF participants. The number of active participants from the University participating in GERS as of September 30, 2012 was 249. Total contributions made by the University to TIAA-CREF and GERS participant accounts amounted to $4.1 million and $1.3 million, respectively.

Postemployment Benefits

In addition to the pension benefits described in Note 15, the Government provides other postemployment benefits (OPEB) of healthcare, prescription, dental and life insurance coverage. These benefits are provided in accordance with Title 3, Chapter 25, Subchapter VIII of the VI Code as part of a cost-sharing, multiple employer defined benefit OPEB plan, in which all component units of the PG participate and contribute. All employees who retire from government service after attaining age 55 with at least 30 years of service; except for policemen and firemen who can retire with at least 20 years of service, are eligible for these benefits.

Based on census data included in the October 1, 2011 actuarial valuation of OPEB, approximately 9,655 active employees, 6,837 service retirees, 1,845 spouses of service retirees covered for medical and dental benefits, 118 disability retirees, 52 spouses of disability retirees, and 175 deferred vested (i.e., non-retired employees who have already terminated employment with the PG, but who are eligible for medical and life insurance benefits when they subsequently reach the qualifying age) meet the eligibility requirements of OPEB.

15. Retirement Systems (continued)

Postemployment Benefits (continued)

Healthcare, prescription and dental insurance is provided through negotiated contracts with private insurance companies. Participants in the plan may elect coverage for their spouses and dependent children. Participants are required to contribute 35% of medical, prescription and dental premiums. Effective October 1, 2012, separate medical premiums for non-Medicare retirees and Medicare retirees are being used to determine contribution requirements, instead of a premium blended with active costs. Retirees of UVI that participate in the 403(b) retirement plan may obtain coverage on a fully contributory basis. Life insurance is offered to retirees on a fully contributory basis.

The contribution requirements of plan members and the PG are legislated within the Virgin Islands Code, and may be amended, by the Virgin Islands Legislature. The plan is a non-funded pay-as-you-go plan, and expenditures are paid as they become due. For the years ended September 30, 2012 and 2011, the Legislature budgeted, and paid, $22.3 million for retiree health insurance payments.

The PG's postemployment benefit cost is calculated on the annual required contribution of the PG, an amount actuarially determined. The first actuarial valuation was prepared as of October 1, 2007, in accordance with provisions of GASB Statement 45, *"Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions"*, and has been updated by the actuarial consultant on October 1, 2009 and October 1, 2011. Prior to the implementation of GASB Statement 45, the PG did not report an OPEB obligation.

The annual required contribution 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 over a period not to exceed an open thirty (30) year period.

15. Retirement Systems (continued)

Postemployment Benefits (continued)

The following table shows the components of the PG's annual postemployment benefits cost for the fiscal year ended September 30, 2012, and the changes in the net estimated obligation for future payments of benefits:

Annual OPEB Cost and Net Postemployment Benefit Obligation

In thousands		
Annual required contribution	$	80,492
Interest on underfunded OPEB obligation		7,553
Adjustment to underfunded OPEB obligation		(7,723)
Annual OPEB cost		80,322
Employer contributions		(36,666)
Change in the net OPEB obligation	$	43,656
Net OPEB obligation - beginning of year	$	201,423
Change in the net OPEB obligation		43,656
Net OPEB obligation - end of year	$	245,079

Actuarial Accrued Liability and Funding Status

In thousands	
Actuarial Valuation Date	October 1, 2011
Actuarial Accrued Liability (AAL)	$1,133,327
Unfunded AAL	$1,133,327
Funded Ratio	0%

15. Retirement Systems (continued)

Postemployment Benefits (continued)

The PG's obligation to provide health insurance to retirees is an unfunded plan. The actuarial valuation of the amount required to fund the plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Estimated annual required contributions are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members), and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the PG and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short term volatility in actuarial accrued liabilities, and the actuarial value of assets, consistent with the long-term perspective of the calculations. In the first actuarial valuation dated October 1, 2007, liabilities at October 1, 2008 were rolled back to October 1, 2007. In subsequent valuation reports, actual benefit payments were used for the fiscal years ending September 30, 2009 through 2012.

Covered health care and dental care expenses were assumed to increase in future years based on the claims experience for fiscal years 2011 and 2012, and a trend assumption beginning at 8.5% for pre-Medicare retirees, 7.0% for post-Medicare retirees, and 7.5% for dental for fiscal year 2012 grading down to an ultimate rate of 4.5% in fiscal year 2022.

The entry age normal actuarial cost method with costs on a level percentage of payroll basis was used to determine the annual required cost of OPEB benefits to retirees. Amortization is over an open thirty (30) year period as a level percentage of payroll. Payroll growth is assumed to be 3% per year for purposes of amortization.

This method is consistent with the cost method used by GERS and typically produces the most level annual required contribution each subsequent year as a percentage of payroll. The normal cost was rolled back using the ultimate trend rate. A discount rate of 3.75% per annum was used, compounded annually. The valuation assumed that the annual unit cost per covered individual (i.e., retiree or spouse) for medical, prescription drugs and dental care for the fiscal year ending September 30, 2012 was $7,395, $1,257 and $199 for retirees under age 65; and $1,558, $1,714 and $199 for retirees over age 65. The normal cost reflects the average age of the covered population and is based on claims experience for fiscal year ending September 30, 2012.

15. Retirement Systems (continued)

Postemployment Benefits (continued)

Combined experience and a combined cost were used for the pre-65 and post-65 populations. A composite cost was developed for retirees and spouses by combining their claim experience. Dependent children claims were included in developing the composite retiree and spouse cost. Costs were trended forward to fiscal year 2012 and adjusted to reflect the anticipated lag in claim payment.

16. Liquidity

Governmental Activities

At September 30, 2012, the Government reported an unrestricted net deficit in governmental activities amounting to $1.6 billion. The net deficit resulted from: 1) the 2008 financial markets collapse and subsequent recession resulting in a reduction in income tax revenue and increase in unemployment, 2) the delay in the issuance of property taxes due to a class action lawsuit, 3) increases in costs of operations, and 4) the negative effect of certain Internal Revenue Service regulations resulting in a reduction of economic development companies operating in the Territory. Following is a summary of the Government's unrestricted net deficit for governmental activities for fiscal years 2007 through 2012:

Governmental Activities Unrestricted Net Deficit
(In thousands, as restated)

Fiscal Year	Governmental Unrestricted Net Deficit	(Increase)
2007	$ (335,924)	$ (29,457)
2008	(513,201)	(177,277)
2009	(1,110,871)	(597,670)
2010	(1,408,601)	(297,730)
2011	(1,630,549)	(221,948)
2012	(1,697,066)	(66,517)

16. Liquidity (continued)

Governmental Activities (continued)

The Government has initiated specific actions to improve its liquidity and future cash flows. The Government established the Office of Economic Opportunity to pursue grants through the American Recovery and Reinvestment Act of 2009, to generate jobs, to promote energy efficient appliances and automobiles, and to improve infrastructure. The Government has successfully attracted a rum producer (Captain Morgan) and retained an existing rum producer (Cruzan Rum) within the Territory. The Government has imposed budgetary restraints, including incentives for early retirement of government workers, salary reductions, personnel reductions and budgetary cut-backs for the entire government. The Government has also legislated increases in local taxes such as the gross receipts taxes and hotel taxes. The Government has met certain District Court requirements in connection with a taxpayer class-action lawsuit, allowing the issuance of 2007 and 2008 property tax assessments in fiscal year 2011, the release of 2009 and 2010 property tax assessments in fiscal year 2012, and the release of 2011 and 2012 property tax assessments in fiscal year 2013.

General Fund

At September 30, 2012, the Government reported a fund balance in the General Fund of $20.4 million. This fund balance represents an increase in the General Fund balance of $94.2 million from the 2011 fiscal year, mainly due to the issuance of working capital loans to offset deficits resulting from a decrease in tax revenue and expenditures exceeding revenues. Following is a summary of the General Fund balance for fiscal years 2012 and 2011:

General Fund Unreserved Fund Balance (Deficit)
(In thousands)

Fiscal Year	Committed	Unassigned	Total
2011	$29,571	$(103,408)	$(73,837)
2012	$29,099	$ (8,649)	$ 20,450

17. Fund and Net Assets Deficit

The following non-major funds have a fund or net assets deficit as of September 30, 2012 (in thousands):

Governmental Funds		
RURAL LIBRARY EXTENSION	$	(572)
EMPLOYMENT SECURITY ADMINISTRATION		(2,369)
FEDERALLY AIDED EDUCATION PROGRAM		(10,362)
SPECIAL FEDERAL GRANT TO EDUCATION		(794)
AIR & WATER POLLUTION CONTROL		(6,494)
VI PLANNING BOARD PROJECTS		(2,996)
HIGHWAY SAFETY		(4,536)
VIRGIN ISLANDS ENERGY OFFICE		(3,657)
VIRGIN ISLANDS NATIONAL GUARD FEDERAL AND STATE AGREEMENT		(3,033)
FOOD STAMP WELFARE		(2,707)
FEDERAL PROGRAMS/DEPARTMENT CONSTRUCTION		(3,876)
FEDERAL AIDED COMMUNITY ACTION AGENCY		(185)
COMMISSION ON AGING		(21)
ELEMENTARY/SECONDARY EDUCATION		(19)
JOB TRAINING PARTNERSHIP ACT OF 1983-1984		(8,818)
CIVIL DEFENSE PROTECTION		(954)
HEALTH INFORMATION COUNCIL ASSISTANCE		(18)
DRUG EDUCATION TRAINING PROGRAM		(123)
FEDERAL HEALTH PROGRAM NOT ON FEDERAL LETTER OF CREDIT SYSTEM		(450)

Proprietary Funds		
BUREAU OF MOTOR VEHCILES	$	(3,657)
GOVERNMENT INSURANCE		(29,032)
HOUSING CONSTRUCTION REVOLVING		(3,004)
EMERGENCY HOUSING FUND		(82)
VIRGIN ISLANDS LOTTERY		(1,687)
CONSUMER PROTECTION FUND		(200)
VIRGIN ISLANDS HOUSING FINANCE AUTHORITY		(3,000)
FREDERIKSTED SMALL BUSINESS FUND		(47)
Proprietary Fund Net Asset Deficits	$	(40,709)

17. Fund and Net Assets Deficit (continued)

Governmental Funds		
WATER & ELECTRIC SYSTEM PROJECTS	$	(1,698)
RURAL COMMUNITY FIRE PROTECTION PROGRAM		(182)
DISTRICT POTABLE WATER FUND		(1,151)
PATERNITY AND CHILD SUPPORT		(11,893)
DISTRICT STREET LIGHT FUND		(2,721)
VI LAW ENFORCEMENT		(4,980)
FORENSIC SCIENCE		(74)
VOCATIONAL REHABILITATION		(1,848)
HURRICAN HUGO INSURANCE CLAIMS		(3,908)
VI ARMY NATIONAL GUARD		(2,266)
EMERGENCY DROUGHT RELIEF		(178)
OUTDOOR RECREATION PROGRAM		(40)
NARCOTICS STRIKE FORCE FORFEITURE		(3)
SMALL BUSINESS DEVELOPMENT ADMINISTRATION MANAGERIAL AND TECHNICAL ASSISTANCE		(8)
FEDERAL GRANTS FOR ALL AGENCIES EXCEPT DEPT OF EDUCATION		(615)
JUVENILE DETENTION CENTER FUND NON-LAPSING		(14)
VI EDUCATION INITIATIVE FUND NON LAPSING		(4,652)
SECTION 12 BOND PROCEEDS		(31,497)
ROAD FUND		(6,330)
PFA/OFFICE OF ECONOMIC OPPORTUNITY		(1,180)
MAJOR REPAIR AND IMPROVEMENT		(58)

Governmental Funds		
BOATING SAFETY PROGRAM	$	(578)
STATE FISCAL STABILIZATION FUND		(5,000)
DEPT OF EDUCATION FEDERAL GRANTS EXCEPT ARRA		(2,088)
Total Fund Deficit	$	(129,951)

18. Restatement of Component Units

Virgin Islands Housing Authority (VIHA)

During the audit of fiscal year 2012, VIHA restated the 2011 audited financial statements due to the fact that the Authority's previously issued financial statements did not included a liability for postemployment benefits other than pensions (OPEB) in accordance with GASB No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local governmental employers. As a result, VIHA's net assets as of September 30, 2011 were adjusted by $18.6 million.

Virgin Islands Housing Finance Authority (VIHFA)

During the audit of fiscal year 2012, VIHFA restated the 2011 audited financial statements due to the fact that the Authority's previously issued financial statements did not include the Virgin Islands Housing Management, Inc. (VIHM), a wholly-owned not for profit-entity. As a result, VIHFA's net assets as of September 30, 2011 were adjusted by $14.1 million.

18. Restatement of Component Units (continued)

Component Units

Beginning net assets of five discretely presented component units were restated to correct account balances reported in prior years as follows (expressed in thousands):

	Beginning Net Assets		
Component Unit	**As Previously Reported**	**Adjustments**	**As Restated**
Virgin Islands Housing Authority	$ 81,727	$ (18,632)	$ 63,095
Virgin Housing Finance Authority	83,012	14,151	97,163
Magens Bay Authority	15,557	154	15,711
Virgin Islands Public Television Station	8,071	129	8,200
Public University	81,062	858	81,920
Other component units	470,751	–	470,751
Net Assets	$ 740,180	$ (3,340)	$ 736,840

19. Subsequent Events

Primary Government

On November 20, 2012, PFA issued the Series 2012 Revenue Refunding Bonds consisting of the Series 2012 A Bonds ("Series 2012A Refinancing Bonds") amounting to $197.1 million and the Series 2012 B Bonds (Series 2012B Broadband Project Bonds") amounting to $31.7 million. The Government has pledged gross receipts taxes for the timely payment of the Series 2012A & 2012B Bonds. The Series 2012A Bonds bear interest at rates from 2.25% to 5.00% and mature from 2017 to 2032. The Series 2012B Bonds bear interest at 5.25% and mature in 2027. The Series 2012A Bonds were issued to: (i) refund the outstanding Series 1999A Bonds, (ii) refund the outstanding Series 2010A Notes, (iii) to pay certain costs of issuing the bonds and (iv) to fund certain debt service accounts in connection with the issuance of the bonds. The Series 2012B Bonds were issued to: (i) refinance the Series 2011A Note, which financed certain broadband projects in the Territory, (ii) pay the costs of issuing the bonds, and (iii) to fund certain debt service accounts in connection with the issuance of the bonds.

19. Subsequent Events (continued)

Primary Government (continued)

On December 19, 2012, PFA issued the Series 2012C Revenue Bonds ("Series 2012C Capital Projects Bonds") amounting to $35.1 million. The Government has pledged gross receipts taxes for the timely payment of the Series 2012C Bonds. The Series 2012 C Bonds bear interest at rates from 3.00% to 5.00% and mature from 2017 to 2042. The Series 2012C Bonds were issued to: (i) finance certain capital projects, (ii) fund capital interest on a portion of the Series 2012C Bonds, and (iii) to pay the costs of issuing the bonds.

On February 12, 2013, Moody's Investors Service withdrew the ratings on the U.S. Virgin Islands general obligation gross receipts tax debt, issued through PFA, due to the lack of sufficient financial and operating information, and the late issuance of the 2010 audited financial statements. On August 29, 2013 Fitch downgraded the U.S. Virgin Islands matching fund bonds from a BBB rating to a BBB- rating.

On May 14, 2013, PFA issued the Series 2013A Subordinate Lien Revenue Note ("Series 2013A Note") amounting to $7.6 million. The Government has pledged gross receipts taxes for the timely payment of the Series 2013A Note. The Series 2013A Note bears interest at the 90 day Libor rate plus 375 points to be paid in thirty-six (36) monthly payments. The Series 2013A Note was issued to: (i) finance the acquisition of a fleet of police vehicles for the PG, and (ii) to fund certain costs of issuing the Series 2013A Note.

On May 15, 2013, the Pension Reform Joint Task Force, authorized by Executive Order 458-2012, presented its recommendations in response to the September 27, 2011 evaluation report of the Office of the Inspector General, U.S. Department of Interior on the administrative functions of the Government Employees Retirement System. The Department of Interior report had concluded that, due to insufficient contribution levels, and an unbalanced ratio of active to retired members, the retirement system of the U.S. Virgin Islands may default within 14 to 19 years. The Pension Reform Joint Task Force recommended: (i) changes to retirement age, (ii) suspension of cost-of-living adjustments, and (iii) the elimination of the ability of retirees to both work for the PG and collect pension payments.

19. Subsequent Events (continued)

Primary Government (continued)

On August 22, 2013, PFA issued the Series 2013B Subordinate Lien Revenue Anticipation Note ("Series 2013B Note") amounting to $40 million. The Government has pledged gross receipts taxes for the timely payment of the Series 2013B Note. The Series 2013B Note bears interest at 6.0% and requires payment in full by September 30th of each fiscal year under the redemption provisions of the Note. The Series 2013B Note was issued to: (i) finance a settlement with the Internal Revenue Service in connection with an audit of the Series 2006 Bonds, (ii) to finance certain operating expenses of the PG, and (iii) to fund certain costs of issuing the Series 2013B Note. On September 30, 2013, the Series 2013B Note was redeemed in full. On October 16, 2013, PFA issued the Series 2013B-2 draw in the amount of $20 million in accordance with the terms of the Series 2013B Note. The Series 2013B-2 Draw was issued to: (i) finance certain operating expenses of the PG, and (ii) to pay the costs of the issuance of the Series 2013B-2 Draw.

On September 19, 2013, PFA issued the Series 2013A Matching Fund Bonds ("Series 2013A Bonds") amounting to $36 million. The Government has pledged matching funds for the timely payment of the Series 2013A Bonds. The Series 2013A Bonds bear interest at rates from 5.00% to 5.25% and mature from 2018 to 2024. The Series 2013A Bonds were issued to: (i) refund portions of the Series 2004A Bonds, Series 2009A-1 Bonds and Series 2009B Bonds, (ii) fund certain debt service reserves in connection with the issuance of the Series 2013A Bonds, and (iii) to pay the costs of issuing the bonds.

On September 30, 2013, the PG received the fiscal year 2014 advance rum excise tax payment (matching funds) from the Department of Interior. The advance payment was computed on a base rate of $10.50 per proof gallon of rum, resulting in a $71 million decrease from the projected advance payment of rum excise taxes. The current rate is $13.25 per proof gallon and is scheduled to expire on December 31, 2013. The Department of Interior noted that the extension of the $13.25 per proof gallon excise tax may be delayed due to Congressional budget hearings.

19. Subsequent Events (continued)

Primary Government (continued)

On October 17, 2013, PFA issued the Series 2013 B Revenue Refunding Bonds ("Series 2013B Bonds") amounting to $51.4 million. The Government has pledged matching funds for the timely payment of the Series 2013B Bonds. The Series 2013B Bonds bear interest at rates from 3.00% to 5.00% and mature from 2015 to 2024. The Series 2013B Bonds were issued to: (i) refund portions of the Series 2004A Bonds, (ii) fund certain debt service reserves in connection with the issuance of the Series 2013B Bonds, and (iii) to pay the costs of issuing the bonds.

On October 18, 2013, WICO entered into a refinancing loan agreement with Banco Popular de Puerto Rico amounting to $28.5 million ("WICO loan"). Under the terms of the refinancing agreement WICO pledged: (i) operating revenues arising from the ship's agent business, and (ii) real property and improvements referred to as the "WICO Dock" including bulkhead and wharf, warehouses, office buildings, maintenance buildings and other facilities. The purpose of the WICO loan is to: (i) repay the existing loan with the bank amounting to $21.2 million, (ii) finance the construction and expansion of the WICO Dock and ship berthing facilities to accommodate larger cruise ships, and (iii) to fund costs associated with the issuance of the WICO loan. The WICO loan bears interest at 6.18%, and requires only interest payments during the first twelve months from the date of closing on the loan. Thereafter, the loan shall be repaid in fifty-nine (59) monthly installment payments of $187 thousand, with a sixtieth (60), final payment of outstanding principal.

Component Units

On November 15, 2012, WAPA Electric filed a petition with the Public Service Commission (PSC), seeking an additional $18 million increase in base electric rates. Base electric rates are the portion of a customer's bill that covers infrastructure costs to operate and maintain power plants. Public hearings on the rate increase request continued through September 2013.

On May 23, 2013 the Virgin Islands Housing Finance Authority sold Government National Mortgage Association (GNMA) Certificates, which were collateral for the 1995 and 1998 bonds, and used the proceeds for the defeasement of the bonds.

19. Subsequent Events (continued)

Component Units (continued)

On July 26, 2013, WAPA Electric signed an $86 million agreement with global energy company, the Vitol Group, for the building of storage terminal facilities, and the upgrading of WAPA Electric turbines to allow the use of liquefied petroleum gas. The conversion to petroleum gas is projected to be implemented in October 2014.

On December 13, 2013, WAPA Electric was awarded a $13 million low-interest rate loan from the United States Department of Agriculture Rural Utilities Service Program. The purpose of the loan is to fund the replacement of all electric meters in the Territory with digital meters that automatically report electricity usage to the WAPA offices. The loan bears interest rates of 3% to 4% and has a fifteen (15) year term.

Pension Trust Fund

On November 2, 2012, GERS entered into a loan agreement with Seaborne Virgin Islands, Inc. ("Seaborne"), a seaplane operator in the Territory, in the amount of $1.5 million as part of a modification agreement of existing loans. The loan term is five (5) years with an interest rate of 6.25% per annum. The loan is payable in twenty (20) quarterly installments of principal in the amount of $75 thousand each, plus interest, with the entire balance due with the 20th payment. Effective for payments due June 15, 2013 and thereafter, Seaborne failed to make payments of principal and interest and has been notified that is was in default. In accordance with the Loan Agreement, Seaborne had until July 15, 2013 to cure the default, but failed to do so. Top senior management of the company is being replaced and the company is undergoing a restructuring. No additional funds have been committed by GERS and the future of GERS' involvement in this investment has not yet been determined as of the date of this report.

Effective January 1, 2013, the Board of GERS suspended cost-of-living adjustment increases for retirees.

Required Supplementary Information

Required Supplementary Information (other than MD&A)

Government of U.S. Virgin Islands

Schedules of Funding Progress

September 30, 2012

Employees Retirement System of the Government of the U.S. Virgin Islands

Actuarial valuation Date	(a) Actuarial value of assets	(b) Unfunded actuarial accrued liability (UAAL)	(c) Actuarial accrued liability (a) + (b)	(d) Funded Ratio (a)/(c)	(e) Annual covered payroll	UAAL as a percentage of covered payroll (b)/(e)
Pension Plan						
2010(*)	1,505,970,212	1,513,059,673	3,019,029,885	49.88%	440,026,457	343.86%
2011(**)	1,448,926,591	1,719,110,906	3,168,037,497	45.74%	403,473,988	426.08%
2012(***)	1,327,038,907	1,603,758,454	3,168,037,497	45.28%	381,012,309	420.92%

(*) Estimated based on the financial information provided as of September 30, 2010, for the actuarial value of assets. For the unfunded actuarial accrued liability (UAAL) amount was projected from the last completed actuarial valuation as of October 1, 2006, assuming that actual experience during the October 1, 2006 to September 30, 2010, matched that assumed by the actuarial assumptions.

(**) Estimated based on the financial information provided as of September 30, 2011, for the actuarial value of assets. For the unfunded actuarial accrued liability (UAAL) amount was projected from the last completed actuarial valuation as of October 1, 2006, assuming that actual experience during the October 1, 2006 to September 30, 2011, matched that assumed by the actuarial assumptions.

(***) Based on the financial information as of September 30, 2012 and the actuarial accrued liability was projected from the October 1, 2011 actuarial valuation assuming that actual experience during the October 1, 2011 to September 30, 2012 matched that assumed by the actuarial assumptions.

Actuarial valuation -September 30, 2006 and thereafter:

Actuarial accrued liability determined under the Entry Age Normal Method.

Required Supplementary Information (other than MD&A)

Government of United States Virgin Islands

Schedules of Funding Progress (continued)

Postemployment Benefits Other Than Pensions

Actuarial valuation Date	(a) Actuarial value of assets	(b) Unfunded actuarial accrued liability (UAAL)	(c) Actuarial accrued liability (a) + (b)	(d) Funded Ratio (a)/(c)	(e) Annual covered payroll	UAAL as a percentage of covered payroll (b)/(e)
10/1/2007	$ –	$976,455,000	$976,455,000	–	N/A	N/A
10/1/2009	$ –	$1,069,997,000	$1069,997,000	–	$418,467,000	255.59%
10/1/2011	$ –	$1,133,327,000	$1,133,327,000	–	$403,389,000	280.95%

Required Supplementary Information (other than MD&A)

Employees' Retirement System of the Government of U.S. Virgin Islands

Schedule of Employer Contributions

September 30, 2012

	Annual required contributions	Contributions made	Percentage contributed
Year ended September 30,			
2008*	$ 138,488,871	$ 75,871,146	54.79%
2009*	147,490,851	80,177,004	52.35%
2010*	157,817,709	77,004,630	48.79%
2011*	162,841,336	80,849,762	49.65%
2012	178,644,349	66,677,154	37.32%

* Estimated based on Fiscal Year 2006 actuarial valuation.

Other Report

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Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Honorable Governor
of the Government of the United States Virgin Islands:

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government) as of and for the year ended September 30, 2012, which collectively comprise the Government's basic financial statements, and have issued our report thereon dated February 7, 2014.

Our report was modified to include a reference to other auditors and the restatement of the net assets of the aggregate discreetly presented component units. We expressed a qualified opinion on the financial statements of the governmental activities and aggregate discretely presented component units opinion units based on the circumstances noted in paragraphs four to seven of our report. In addition, we expressed a disclaimer of opinion on the financial statements of the aggregate remaining fund information and business type activities opinion units based on the circumstances described in paragraphs eight and nine of our report.

Except as described above, we conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the Tobacco Settlement Financing Corporation (TSFC), Virgin Islands Housing Authority (VIHA), Virgin Islands Public Television System (VIPTS), Virgin Islands Lottery (V.I. Lottery), Virgin Islands Economic Development Authority (VIEDA), Magens Bay Authority (MBA), Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), Employees' Retirement System of the Government of the Virgin Islands (GERS), and the Virgin Islands Housing Finance Authority (VIHFA), as described in our report on the Government's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the Juan Luis Hospital and Medical Center and GERS were not audited in accordance with *Government Auditing Standards*.

Internal Control over Financial Reporting

Management of the Government is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Government's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Government's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Government'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 and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. We consider the items 12-01 through 12-08 to be material weaknesses.

Financial Statements Findings

Finding Number 12-01

Topic
Data Collection Form and Single Audit reporting package not submitted on time.

Category
Internal Control / Compliance

Criteria
OMB Circular, Subpart C, Section .320 (a) General establishes that the audit shall be completed and the data collection form described in paragraph (b) of this section and reporting package described in paragraph (c) of this section shall be submitted within the earlier of 30 days after receipt of the auditor's report(s), or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audit. Unless restricted by law or regulation, the auditee shall make copies available for public inspection. (b) Data Collection. (1) The auditee shall submit a data collection form which states whether the audit was completed in accordance with this part and provides information about the auditee, its Federal programs, and the results of the audit. The form shall be approved by OMB, available from the Federal clearinghouse designated by OMB, and include data elements similar to those presented in this paragraph. A senior level representative of the auditee (e.g., State controller, director of finance, chief executive officer, or chief financial officer) shall sign a statement to be included as part of the form certifying that: the auditee complied with the requirements of this part, the form was prepared in accordance with this part (and the instructions accompanying the form), and the information included in the form, in its entirety, are accurate and complete.

Condition
The Data Collection Form (DCF) and the Single Audit reporting package were not submitted within nine months after the end of the audit period.

Questioned Costs
None.

Underlying Cause
Information needed to complete the Single Audit was not available for examination within the required period.

Effects
The lack of appropriate procedures to ensure a complete reporting package and data collection form submission may cause delays in the audit process thus affecting future grant awards.

Recommendation
The Government should improve the procedures to ensure that the OMB Circular A-133 reporting package, including a complete and accurate schedule of expenditures of federal awards, is available for examination by the external auditors with sufficient time to complete and issue the reporting package within the required period.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Finding Number: 12-02

Primary Agencies/Departments Affected: Department of Finance (DOF), Internal Revenue Bureau (IRB), Lieutenant Governors Office (LGO)

Topic
The Government's lack of control over the income, excise, property and sales tax revenues processes led to significant audit adjustments being recorded in the financial statements. Due to the nature and magnitude of this control deficiency, such control deficiency is considered to be a material weakness.

Category
Internal Control

Criteria
A sound system of internal controls is essential in enabling the Government to prepare timely and accurate financial statements by helping ensure that all financial transactions are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
Management's calculation of its tax revenues processes were not properly performed, resulting in significant audit adjustments. The following items resulted in audit adjustments which could have been prevented had Management implemented sound internal controls over its tax revenue recognition processes: (a) Management used an inappropriate date on the report used to calculate the income tax receivable causing an understatements of revenues, and (b) the calculation for property tax receivables was not properly calculated and thus significant audit adjustments were proposed in order to correctly present these accounts.

Questioned Costs
Not applicable.

Underlying Cause
The Government's tax revenue process has grown in complexity. Additionally, supervisory review of the tax revenue process was not effective in all instances.

Effect
The lack of supervisory review led to significant adjustments in the Government's financial statements.

Recommendation
The governmental finance department should be more closely involved in the monitoring and review of the tax revenues processes. Management should consider performing these controls on a quarterly basis in order to detect and correct errors on a timely basis, while enhancing the Government's knowledge over its financial condition.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Finding Number: 12-03

Primary Agencies/Departments Affected: Department of Finance (DOF), Property and Procurement (P&P), Department of Public Works (DPW), Public Finance Authority (PFA)

Topic
The Government's lack of control over its capital assets process led to significant adjustments in the financial statements.

Category
Internal Control

Criteria
A sound system of internal controls is essential in enabling the Government to prepare timely and accurate financial statements by helping ensure that all financial transactions are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
During our review of capital asset accounts, we noted projects capitalized in the incorrect asset class. We also noted transfers of assets from construction in progress included as an addition instead of as a transfer from construction in progress, creating a duplicate addition.

Questioned Costs
Not applicable.

Underlying Cause
There is a lack of timely coordination between the Department of Finance, the Department of Property and Procurement,V.I. Public Finance Authority, and the Department of Public Works.

Effect
The lack of supervisory review and coordination between the mentioned departments led to significant audit adjustments in the Government's financial statements.

Recommendation
The Government should implement a formal procedure of reviewing the status of construction in progress accounts and capital assets activity on at least a quarterly basis that may require impairment.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Finding Number: 12-04

Primary Agency/Department Affected: Department of Finance (DOF)

Topic
The Government's lack of control over the accounts payable reconciliations process led to significant adjustments in the financial statements. Due to the nature and magnitude of this control deficiency, such control deficiency is considered to be a material weakness.

Category
Internal Control

Criteria
A fundamental element of a sound system of internal controls is an effective accounts payable reconciliations process. Such process is essential in enabling entities to prevent and detect errors on a timely basis. This effective process helps ensure that all accounts payable reconciliations are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
Lack of controls over the accounts payable ERP module and accounts payable reconciliations has made it difficult for the Government to establish its accounts payable subledger. Management establishes its accounts payable subledger through a manually intensive process. This resulted in audit significant adjustments in the Government's financial statements.

Questioned Costs
Not applicable.

Underlying Cause
The Government's financial statements have grown in complexity. Additionally, supervisory review of the accounts payable reconciliation process was not effective in all instances.

Effect
The lack of supervisory review led to significant adjustments in the Government's financial statements. This resulted in a material misstatement of the financial statements.

Recommendation
The Government's management should be more closely involved in the monitoring and review of the financial statement close process. Management should consider performing this process on a quarterly basis in order to detect and correct errors on a timely basis, while enhancing the Government's knowledge over its financial condition. In addition, Management should consider establishing procedures to reduce manual efforts by utilizing its ERP Accounts Payable module more effectively.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Finding Number: 12-05

Primary Agencies/Departments Affected: Department of Finance (DOF)

Topic
The Government's lack of control over its retroactive pay liability has affected the auditor's ability to opine on certain affected opinion units. This has resulted in a modification of the audit opinion for the last four years. For the last four years, we encountered calculation errors that were significant in the retroactive pay liability calculation. The calculation errors have not been remediated as of the date of this report.

Category
Internal Control

Criteria
A fundamental element of a sound system of internal controls is an effective liability calculation process. Such process is essential in enabling organization to prevent and detect errors on a timely basis. This effective process helps ensure that all liability transactions are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
The Government was not able to substantiate its calculation of the retroactive pay liability, which resulted in a qualification of the opinion of governmental activities in the Government's basic financial statements.

Questioned Costs
Not applicable.

Underlying Cause
Supervisory review of this liability calculation process was not effective. As a result, supporting documentation for calculation was not sufficiently adequate to support Management's assertions.

Effect
The Government was not able to support its calculation for this liability, which resulted in a qualification of the audit opinion of governmental activities in the Government's basic financial statements.

Recommendation
The Government's management should establish controls over the review of this calculation process and effective procedures to document their support of this liability.

Management's Response
The Government concurs with the auditor's findings and recommendations.

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Finding Number: 12-06

Primary Agencies/Departments Affected: Department of Finance (DOF)

Topic
Performance and review of the bank reconciliation process has not been timely performed.

Category
Internal Control

Criteria
Performance and review of bank reconciliations should be performed within a reasonable period after month-end.

Condition Found
During our audit, we noted that bank reconciliations were not being performed and reviewed within a reasonable period. Most bank reconciliations were completed, reviewed and approved after 365 days.

Questioned Costs
Not applicable.

Underlying Cause
The Government has numerous bank accounts and its process for performing bank reconciliations is, for the most part, performed manually.

Effect
The lack of timely performance and review of bank reconciliations led to adjustments not identified on a timely basis. This could also result in a misstatement due to error or fraud. In addition, this has prevented the Government from performing monthly closing procedures, which is necessary for timely financial reporting.

Recommendation
The Government should automate its bank reconciliation process and consolidate unnecessary bank accounts. This will allow for the Government's personnel to be more efficient and effective in detecting errors and provide the Government more timely and accurate financial information.

Management's Response
While the Government concurs with the auditor's findings and recommendations as of September 30, 2012, significant progress regarding bank reconciliations was made subsequently. At September 30, 2013, 31 out of 32 bank accounts had been reconciled and substantial work completed in relation to the remaining bank account.

Finding Number: 12-07

Primary Agencies/Departments Affected: Department of Finance (DOF), Department of Health (DOH)

Topic
The Government's lack of control over its liability estimation process for medical malpractice claims led to an error in the financial statements, which could not be quantified by management.

Category
Internal Control

Criteria
A fundamental element of a sound system of internal controls is an effective liability estimation process. Such process is essential in enabling entities to prevent and detect errors on a timely basis. This effective process helps ensure that all liability estimation transactions are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
The Government did not establish a liability for medical malpractice claims.

Questioned Costs
Not applicable.

Underlying Cause
The Government's financial statements have grown in complexity. An evaluation of the malpractice liability was not performed for fiscal year 2012.

Effect
The Government was not able to quantify this liability, which resulted in a disclaimer in the audit opinion of the business-type activities and aggregate remaining fund information.

Recommendation
The Government's management should establish controls over the review its claims data process which will allow them to provide the data necessary to their actuary for the estimation of this liability.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Finding Number: 12-08

Primary Agency/Department Affected: Department of Finance (DOF)

Topic
The Government's lack of control over transactions with its component units led to significant adjustments in the financial statements. Due to the nature and magnitude of this control deficiency, such control deficiency is considered to be a material weakness.

Category
Internal Control

Criteria
A sound system of internal controls is essential in enabling the Government to prepare timely and accurate financial statements by helping ensure that all financial transactions are properly recorded, appropriately supported, and subjected to supervisory review.

Condition Found
Lack of review of classification and reporting of transactions with component units led to errors, resulting in significant audit adjustments.

Questioned Costs
Not applicable.

Underlying Cause
The Government does not have an effective process to review the classification and reporting of transactions between component units and the Government.

Effect
This control deficiency led to significant adjustments in the Government's financial statements. This resulted in a material misstatement of the financial statements, some of which related to prior periods.

Recommendation
The Government's management should be more closely involved in the monitoring and review of the transactions with its component units, in order to detect and correct errors on a timely basis, while enhancing the Government's knowledge over its financial condition.

Management's Response
The Government concurs with the auditor's findings and recommendations.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Government's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on 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 such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Government's responses to the findings identified in our audit are described above. We did not audit the Government's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the Honorable Governor of the United States Virgin Islands, management, others within the entity, Federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

February 7, 2014

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