

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
A COMPONENT UNIT OF THE STATE OF WEST VIRGINIA AND
WEST VIRGINIA DEPARTMENT OF TRANSPORTATION

AUDITED FINANCIAL STATEMENTS
WITH ADDITIONAL INFORMATION

YEAR ENDED JUNE 30, 2002
AND
INDEPENDENT AUDITORS' REPORTS

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INDEPENDENT AUDITORS' REPORT

Joint Committee on Government and Finance
West Virginia Legislature

We have audited the accompanying financial statements of the governmental activities and each major fund, of the West Virginia Department of Transportation, Division of Highways, as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the West Virginia Department of Transportation, Division of Highways' management. Our responsibility is to express opinions on these financial statements based on our audit.

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

As discussed in Note 1, the financial statements of the West Virginia Department of Transportation, Division of Highways are intended to present the financial position and the changes in financial position of only that portion of the governmental activities and each major fund of the West Virginia Department of Transportation and of the State of West Virginia, that is attributable to the transactions of the Division of Highways. They do not purport to, and do not, present fairly, the financial position of the West Virginia Department of Transportation or the State of West Virginia as of June 30, 2002 and the changes in their financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the West Virginia Department of Transportation, Division of Highways, as of June 30, 2002, and the respective changes in financial position thereof and the respective budgetary comparison for the State Road (General) Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, the West Virginia Department of Transportation, Division of Highways has implemented a new financial reporting model as required by the provisions of Governmental Accounting Standards Board Statement 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as of June 30, 2002.

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The management's discussion and analysis on pages 5 through 15 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 31, 2002 on our consideration of the West Virginia Department of Transportation, Division of Highways' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Suttle & Stalnaker, PLLC

October 31, 2002

MANAGEMENT'S DISCUSSION AND ANALYSIS

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the West Virginia Department of Transportation, Division of Highways (Division) annual financial report presents our discussion and analysis of the Division's financial performance during the fiscal year that ended June 30, 2002. Please read it in conjunction with the Division's financial statements, which immediately follow this section.

FINANCIAL HIGHLIGHTS - PRIMARY GOVERNMENT

Government-Wide:

Net Assets - The assets of the Division exceeded its liabilities at June 30, 2002 by \$5.3 billion (presented as "total net assets"). Of this amount, \$85 million was reported as "unrestricted net assets". Unrestricted net assets represent the amount available to be used to meet the Division's ongoing obligations to citizens and creditors.

Changes in Net Assets - The Division's total net assets at June 30, 2002 decreased by \$42 million (a .79 % decrease) in total net assets from June 30, 2001.

Revenues - Total revenues increased \$53 million or 5.35%. The amount of automobile privilege tax revenue increased by \$25 million or 15.97%.

Expenditures - Total expenditures decreased \$49 million or 4.37%. Expenditures excluding noncapitalized construction expenditures increased by \$6 million or 1.38%.

Fund Highlights:

Government Funds - Fund Balances - As of the close of fiscal year 2002, the Division's governmental funds reported combined total fund equity of \$247 million, an increase of \$46 million in comparison with the prior year. Of this total amount, \$133 million represents the "unreserved fund balances" with substantially all being in the general fund. This is roughly 12.40 % of the total governmental fund expenditures for the year.

Long-term Debt:

The Division's total long-term debt obligations, net of bond premiums, increased by \$92 million (20.24%) during the current fiscal year. The key factor in the increase was the July 2001 sale of \$110 million in Safe Road Bonds.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The Division's basic financial statements are prepared in accordance with accounting principles generally accepted in the United States of America for governmental entities. The Division is an operating unit of the West Virginia Department of Transportation and represents separate funds of the State of West Virginia (the "State") that are not included in the State's general fund. The Division is a legally separate entity defined by the State constitution, and has statutory responsibility for the construction, reconstruction, maintenance, and improvement of all State roads. The basic financial statements include two kinds of financial statements that present different views of the Division - the Government-Wide Financial Statements and the Fund Financial Statements. These financial statements also include the Notes to the Financial Statements that explain some of the information in the financial statements and provide more detail.

Government-wide Statements (reporting the Division as a whole)

The Statement of Net Assets and the Statement of Activities are two financial statements that report information about the Division, as a whole, and about its activities. They are designed to provide readers with a broad overview of the Division's finances, in a manner similar to a private-sector business.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS- CONTINUED

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

The Statement of Activities presents information showing how the Division's net assets changed during the fiscal year 2002. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes, and earned but unused vacation leave) or that resulted in cash flows in previous periods and are recorded as assets or liabilities in the statement of net assets (e.g. cost incurred to purchase or construct capital assets, bond proceeds, and bond issue costs).

The report includes two schedules that reconcile the amounts reported on the governmental fund financial statements (modified accrual accounting) with the governmental activities (accrual accounting) on the appropriate government wide statements. The following summarizes the impact of transitioning from modified accrual to accrual accounting:

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Deferred issue costs are capitalized and amortized as governmental activities, but reported as expenditures in the governmental fund statements.
- Unless due and payable, long-term liabilities, such as bonds, compensated absences, litigation and others only appear as liabilities in the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are recorded as expenditures on the governmental fund statements.
- Bond proceeds, including any premiums on debt issued, result in liabilities on the government-wide statements, but are recorded as other financing sources on the governmental fund statements.
- Certain other outflows represent either increases or decreases in liabilities on the government-wide statements, but are reported as expenditures on the governmental fund statements.

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

Fund Financial Statements (Reporting the Division's Major Funds)

The fund financial statements provide detailed information about the major individual funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the Division uses to keep track of specific sources of funding and spending for a particular purpose. The Division has only one category of funds, Governmental Funds. Governmental funds focus on how money flows into and out of funds and the balances left at year-end that are available for future spending. The governmental fund financial statements provide a detailed short-term view of the Division's general government operations and the basic services it provides. Government Fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the Division's programs. These funds are reported using modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The Governmental funds include:

- The State Road fund, which is the Division's general fund, reflects the ongoing operations of the Division that are financed from the designated tax, license, registration and other fees, as well as the federal share of projects that qualify for federal reimbursement.
- The Capital Projects fund reflects the expenditure of proceeds from bond offerings.
- The Debt Service fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION AS A WHOLE

The Division's net assets decreased by approximately \$42 million or .79%. Prior year information is not available to present a complete comparison to the prior year. In future years, a full comprehensive financial analysis will be presented. The following summarizes the Division's net assets at year end (amounts in thousands).

Net Assets as of June 30, 2002

ASSETS	
Current assets	
Cash and cash equivalents	\$ 201,009
Other assets	157,423
Total current assets	<u>358,432</u>
Non-current assets	
Capital assets, net of accumulated depreciation	
Buildings, furniture and fixtures	39,883
Land and land improvements	17,824
Equipment	49,355
Roads, bridges and right of way	5,280,688
Work in progress	270,790
Total capital assets	<u>5,658,540</u>
Other non-current assets	3,574
Total assets	<u>6,020,546</u>
LIABILITIES	
Current liabilities	
Other current liabilities	113,500
Current maturities of long term obligations	42,107
Total current liabilities	<u>155,607</u>
Non-current liabilities	
Claims and judgments	4,095
Compensated absences	56,222
General obligation bonds	520,955
Total non-current liabilities	<u>581,272</u>
Total liabilities	<u>736,879</u>
NET ASSETS	
Invested in capital assets, net of related debt	5,198,392
Unrestricted	<u>85,275</u>
Total net assets	<u>\$ 5,283,667</u>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
 DIVISION OF HIGHWAYS
 MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION AS A WHOLE - CONTINUED

The largest component (98.38%) of the Division's net assets reflects its investment in capital assets (e.g. land, buildings, equipment, infrastructure and others) less any related debt outstanding (excluding debt proceeds that have yet to be expended for infrastructure construction) that was needed to acquire or construct the assets. The remaining portion, unrestricted net assets, may be used at the Division's discretion.

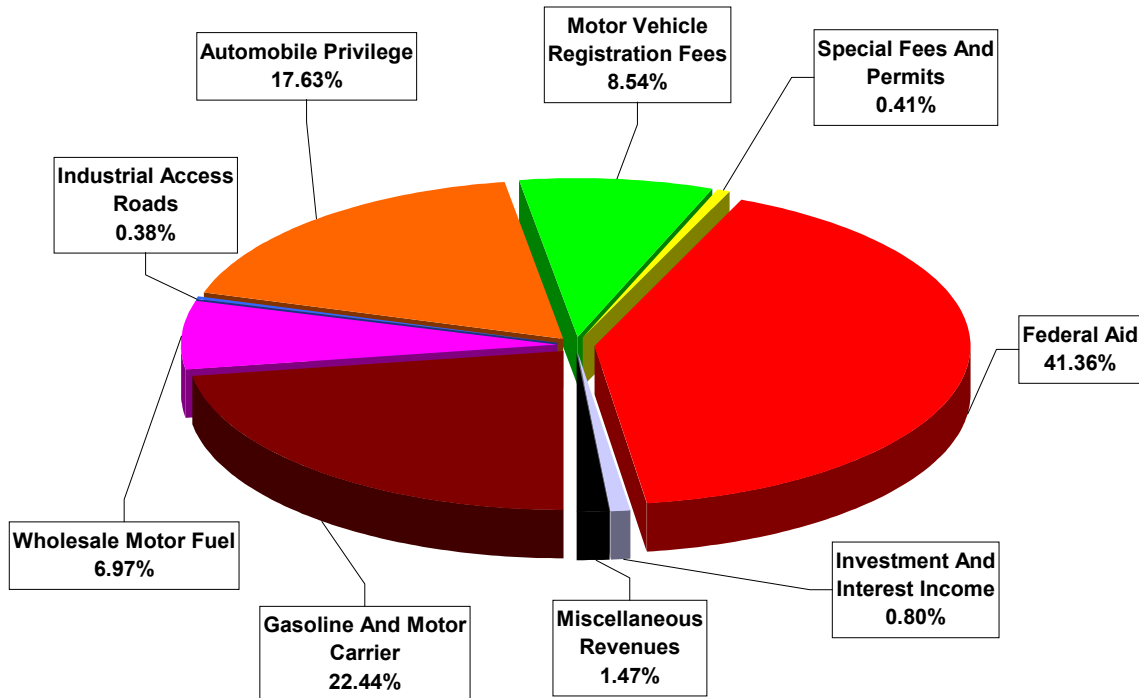
The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the Division's net assets changed during the fiscal year (amounts in thousands):

Revenues	
Taxes	\$ 485,350
Licenses, fees and permits	91,553
Federal aid	433,156
Investment and interest income	8,148
Miscellaneous revenues	15,062
Total revenues	<u>1,033,269</u>
Expenses	
Road maintenance	297,586
Other road operations	649,364
General and administration	85,822
Interest on long-term debt	28,168
Unallocated depreciation	14,022
Total expenses	<u>1,074,962</u>
Change in net assets	(41,693)
Net assets, beginning	<u>5,325,360</u>
Net assets, ending	<u>\$ 5,283,667</u>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION AS A WHOLE - CONTINUED

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



Total revenues increased by approximately \$53 million. Total tax revenues increased by approximately \$32 million with the majority of the increase (\$25 million or 78%) due to increases in the privilege tax. Federal aid revenue increased by approximately \$21 million (5.0%). The following summarizes revenues for the year ended June 30, 2002 and June 30, 2001 (amounts in thousands):

	June 30, 2002	June 30, 2001	Increase (decrease)	% Increase
Gasoline and motor carrier road tax	\$ 229,650	\$ 221,757	\$ 7,893	3.56%
Wholesale motor fuel	71,314	71,521	(207)	(.29%)
Industrial access roads	3,914	4,189	(275)	(6.56%)
Automobile privilege	180,472	155,623	24,849	15.97%
Motor vehicle registration fees	87,380	78,745	8,635	10.97%
Special fees and permits	4,173	4,063	110	2.71%
Federal aid	433,156	412,403	20,753	5.03%
Investment and interest income	8,148	13,413	(5,265)	(39.25%)
Miscellaneous revenues	15,062	19,042	(3,980)	(20.90%)
	<u>\$ 1,033,269</u>	<u>\$ 980,756</u>	<u>\$ 52,513</u>	<u>5.35%</u>

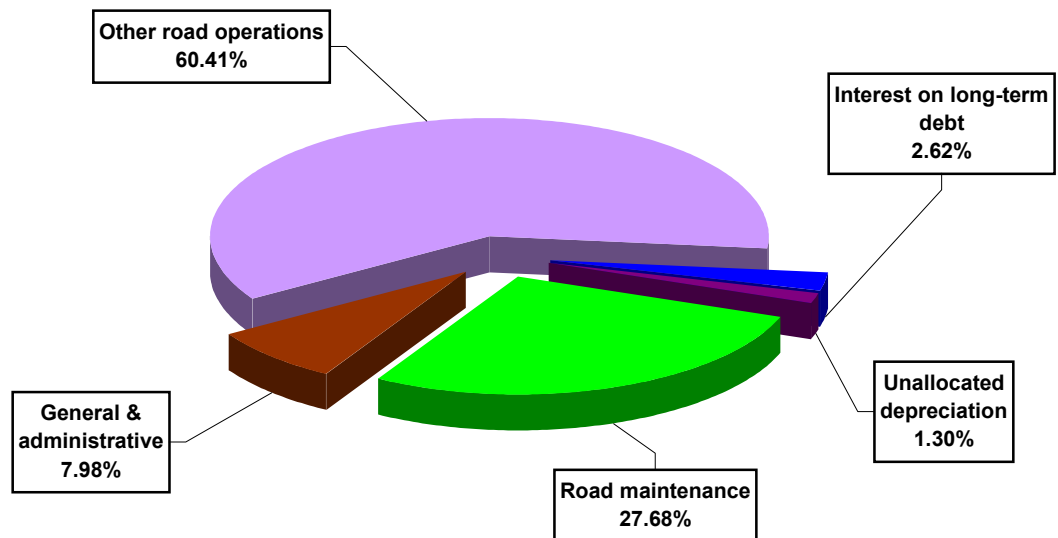
The Division of Highways primary sources of revenue for funding of ongoing administration of the Division, general maintenance and construction of the State Road System and for providing resources to match available Federal funds is derived from fuel taxes, automobile privilege tax, motor vehicle registration and license fees, net of costs incurred to maintain the Department of Motor Vehicles, which collects a majority of these revenues. Over the past several years, the Division of Highways has benefited from the extended strong national and state economies.

FINANCIAL ANALYSIS OF THE DIVISION AS A WHOLE - CONTINUED

Tax collections, especially of privilege tax, exceeded official estimates by a significant amount, allowing the Division to undertake additional projects and expand customer services. Unfortunately, both the state and national economies have slowed dramatically. Through the end of the 2002 fiscal year revenues continued to approximate estimates, but revenue projections through the fiscal year 2006 reflect only minimal growth in collections. As a consequence, many programs that operate from the Division will experience little, if any, increase in the foreseeable future and some programs may be funded at lower levels.

The Division also relies on Federal funds as a source of revenue. The "Transportation Equity Act for the 21st Century" (TEA 21) passed by Congress and signed by the President in 1998, established a new six-year highway transit bill. West Virginia's six-year total will approach \$1.8 billion. The Division expects to receive regular federal funds of \$209 million each fiscal year, compared to \$159 million yearly under previous legislation. Additional special funding is also included. The Division expects to receive a total of \$542 million of added funding over the life of the legislation. The Federal Aid is obtained in the form of reimbursable grants. The recognition of revenue under these grants occurs when expenditures occur on specific projects that have qualified for federal participation. While TEA 21 and special spending authorizations result in funds available for obligation by the Federal Government in specific years, and the Division expects to continue to fully obligate available funds, thus ensuring that all available Federal dollars are received by the Division, the timing of revenue recognition for financial reporting is dependent on the timing of completion of specific construction projects. TEA 21 is due to expire in 2003. The United States Congress is currently working on reauthorization of a new Highway Transit Bill (TEA 3). The results of the reauthorization are yet to be determined.

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



WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION AS A WHOLE - CONTINUED

Total expenditures decreased by approximately \$49 million (4.37%). The following summarizes expenditures for the years ended June 30, 2001 and June 30, 2002 (amounts in thousands):

	June 30, 2002	June 30, 2001	Increase (decrease)	% Increase (decrease)
Road maintenance	\$ 297,586	\$ 307,953	\$ (10,367)	(3.37%)
Other road operations	649,364	708,291	(58,927)	(8.32%)
General and administration	85,822	69,481	16,341	23.52%
Interest on long-term debt	28,168	14,344	13,824	96.37%
Unallocated depreciation	14,022	24,051	(10,029)	(41.70%)
	<u>\$ 1,074,962</u>	<u>\$ 1,124,120</u>	<u>\$ (49,158)</u>	<u>(4.37%)</u>

The significant increase in support and administrative expense is a result of the following:

- Upon retirement, the Division's employees may use accumulated sick leave to purchase health insurance premium at a predetermined number of days per month of coverage or to extend their years of service credits for retirement purposes. The rising cost of premiums has resulted in a change in the actuarial assumptions related to the computation of the liability for this post retirement benefit. As premiums rise employees are more likely to choose to use accumulated sick leave to acquire insurance and less likely to extend service credits. The liability for accrued sick leave to be paid on retirement increased by approximately \$9 million.
- The Division allocates the cost of employee benefits to the various functions (operations, construction, maintenance, etc.) by applying an additive rate to salary amounts charged to those functions. As of the last review of the additive rate the Division had under distributed these costs by approximately \$8 million. The additive rate is adjusted each year to reflect any over or under allocation so that these costs are allocated to the various projects and functions of the Division in succeeding years.

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

The type of routine maintenance expenses incurred is dependent, to a degree, on the level of snow and ice removal that is required in a given year. Operating divisions are allocated amounts for routine maintenance in the Division's annual plan. The State had a mild winter during the year ended June 30, 2002; therefore, the approximately \$12 million reduction in costs were used to perform other routine maintenance functions in the spring. Therefore the decline in maintenance expenditures were not a result of the savings due to the mild winter as those savings were used to perform other routine maintenance functions.

The Division's expenditures for contract paving are more discretionary in nature and the level of contract paving during the year ended June 30, 2002 was approximately \$13 million less than the previous fiscal year. Division management elected to conserve funds by adjusting the level of contract paving that was carried out during the year ended June 30, 2002. This was in response to projected revenues increasing at a slower pace than expenses.

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

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION'S MAJOR FUNDS

As the Division completed the year, the Division reported fund balances of \$247 million. Of this total amount, \$133 million, 53.91%, constitutes unreserved fund balance, which is available for appropriation for the general purposes of the funds. The remainder of fund balance is reserved and is not available for new spending because it has already been dedicated for various commitments, such as capital outlay projects.

State Road Fund

The State Road Fund is the Division's General Fund. At the end of the 2002 fiscal year, unreserved fund balance of the General fund was \$133 million and reserved fund balance was \$30 million. Total fund balance increased slightly during the year primarily due to higher than anticipated tax revenues as discussed above in the financial analysis of the Division as a whole.

Capital Projects Fund

The Capital Projects Fund is used to account for financial resources to be used for road construction or reconstruction financed by the proceeds from the sale of Safe Road Bonds and matching federal highway funds on such projects. At June 30, 2002 the fund balance of the fund represented unexpended bond funds associated with the 2002 bond issue (discussed below). The projects to be constructed from the proceeds of these bonds have been programmed, and where applicable, the federal funds for the projects have been obligated.

Debt Service Fund

The Debt Service Fund accounts for the resources accumulated and payments made for principal and interest on long-term debt of the Division. During the year ended June 30, 2002 this fund was no longer mandated, and the remaining funds of approximately \$132 thousand were transferred to the State Road Fund. Bond principal and interest payments on all outstanding debt are currently being made directly from the State Road Fund.

State Road (General) Fund Budgetary Highlights

Since the Division is dependent on revenues generated from the purchase and use of motor fuel, motor vehicle fees, consumer purchases of motor vehicles and federal funding generated from motor fuel purchases, revenues are affected by state and national economic conditions, world events affecting availability and pricing of motor fuel and fuel consumption rates for motor vehicles. Although average fuel consumption rates for motor vehicles have remained fairly constant over the past several years, any future changes in these rates would have a significant impact on revenue collections without changes to the tax rates or structure. For the sixth straight year, tax and fee revenue collections have increased over the previous year. Although there has been a downward turn to the national economy over the past few years, the effect of low interest rates and moves by major car manufacturers to increase automobile sales have resulted in increases in both privilege tax and motor vehicle registration fees. There has also been limited impact on fuel tax revenues.

The Division's budget included \$611 million in federal aid revenues to be used primarily for design, right-of-way and construction of Corridor D, Corridor H, WV 9 and other major corridors including King Coal Highway, Coalfields Expressway, WV 2, WV 10, and WV 35. As previously discussed the recognition of revenue under these grants occurs when expenditures occur on specific projects that have qualified for federal participation. Since the timing of such expenditures are dependent on variables such as the weather, the existence of differing site conditions that require plan modification, or delays caused by environmental issues or the results of public meetings, expenditures often do not occur as planned. The budgeted amounts for federal aid revenue and expenditures are based on projects that have been approved and estimates of the timing of each phase of the project.

As a result of the above items, the original budget was amended. The most significant changes were to decrease anticipated federal aid expenditures by \$30 million.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL ANALYSIS OF THE DIVISION'S MAJOR FUNDS - CONTINUED

Differences between the final budget and actual spending result principally from lower than expected expenditures on construction projects which occurred due to the estimated timing of expenditures on specific projects differing from actual construction schedules (approximately \$87 million), equipment revolving fund purchases that were not completed until the following fiscal year (approximately \$7 million), and the lower than expected maintenance expenditures (approximately \$30 million).

There were no over expenditures by the Division in appropriated funds. In addition, there were no over expenditures in specific budget line items.

Although it is anticipated that revenues will increase slightly in the next fiscal year, the Division's revenue increases are not projected to keep pace with increases in costs related to retirement, health insurance, increased debt service and other increases that are non-discretionary in nature. As a result the Division will be required to reduce expenditures on programs that are discretionary and expenditures in these areas will be managed to ensure that the Division maintains a positive fund balance. The Fiscal 2003 budget reflects a budgeted decline in fund balance of approximately \$38 million. Management is taking all necessary steps to ensure that the fund balance of the Division is maintained at levels that are adequate to ensure the soundness of the Division and is confident that adequate discretionary items exist to permit them to continue to operate in a fiscally sound manner. However, the level of funding available and the increases in non-discretionary spending may impact the Division's ability to achieve all operational objectives.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of June 30, 2002, the Division had invested \$5.7 billion, net of accumulated depreciation, in a range of capital assets (see table below). Depreciation charges for the fiscal year totaled \$239 million.

**Capital Assets as of June 30, 2002
(net of depreciation, amounts in thousands)**

	<u>2002</u>	<u>2001</u>	<u>% Change</u>
Land - non infrastructure	\$ 14,287	\$ 13,386	6.73%
Buildings	39,373	36,828	6.91%
Furniture and fixtures	510	535	(4.67%)
Land improvements - non infrastructure	3,537	2,476	42.85%
Rolling stock	48,309	47,560	1.57%
Shop equipment	375	513	(26.90%)
Scientific equipment	671	626	7.19%
Total capital assets excluding infrastructure	<u>107,062</u>	<u>101,924</u>	5.04%
Land - infrastructure	579,229	521,454	11.08%
Roads	3,871,849	3,828,990	1.12%
Bridges	829,610	704,605	17.74%
Construction in process - roads	228,271	348,094	(34.42%)
Construction in process - bridges	42,519	146,687	(71.01%)
Total infrastructure	<u>5,551,478</u>	<u>5,549,830</u>	.03%
Total capital assets	<u>\$ 5,658,540</u>	<u>\$ 5,651,754</u>	.12%

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
MANAGEMENT'S DISCUSSION AND ANALYSIS

CAPITAL ASSETS AND DEBT ADMINISTRATION - CONTINUED

The limited increase in capital assets, net of depreciation, reflects the nature of the State's road system. While the Division continues to expand the state road system, these expansions are focused primarily on upgrading existing roadways and completion of Appalachian Highway Corridors. While these are significant construction projects, the additions are offset by \$224 million in depreciation on the infrastructure. The Division expended \$246 million dollars during the year ended June 30, 2002 for additions to infrastructure. Of this amount, \$226 million was related to the acquisition of right of way and construction of roads and bridges. Construction costs for completed projects in the amount of \$392 million was reclassified from construction in process to roads and bridges. Major construction expenditures during the year included continued construction related to Corridor H in Randolph and Hardy Counties, Corridor D in Wood County, upgrade of WV 10 in Logan County, upgrade of WV 2 in Brooke County, widening of I-64, and continued environmental studies on various projects in process.

Long-term Debt

The Division has been authorized to issue bonds by constitutional amendments and all bonds are general obligation bonds of the State of West Virginia. All bonds authorized under prior constitutional amendments have been issued. At June 30, 2002 the Division had \$540 million in outstanding bonds. The amount outstanding increased by \$89 million (19.63%) due to the issuance of \$110 million in bonds during the year which was offset by principal payments of \$21 million.

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

Issue	Status of insurance	Bond Rating	Amount (in thousands)
Better Highways 73 - All Bonds maturing on or before June 1, 2006	Not insured	Fitch: AA- Moody's: Aa3 S&P: AA-	\$ 18,660
Safe Roads 98A - All Bonds maturing on or before June 1, 2023	Insured by FGIC	Fitch: AAA Moody's: Aaa S&P: AAA	204,080
Safe Roads 99A - All Bonds maturing on or before June 1, 2007	Not Insured	Fitch: AA- Moody's: Aa3 S&P: AA-	105,020
Safe Roads 00A - All Bonds maturing on or before June 1, 2020	Insured by FGIC	Fitch: AAA Moody's: Aaa S&P: AAA	32,290
Safe Roads 00A - Term Bond maturing on June 1, 2025	Insured by MBIA	Fitch: AAA Moody's: Aaa S&P: AAA	77,710
Safe Roads 01A - Bonds maturing between June 1, 2005 to 2013	Insured by FSA	Fitch: AAA Moody's: Aaa S&P: AAA	93,465
Safe Roads 01A - Bonds maturing between June 1, 2002 to 2004	Not insured	Fitch: AA- Moody's: Aa3 S&P: AA-	8,315
			<u>\$ 539,540</u>

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

BASIC FINANCIAL STATEMENTS

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
 DIVISION OF HIGHWAYS
 STATEMENT OF NET ASSETS
 JUNE 30, 2002
 (amounts expressed in thousands)

ASSETS	<u>Governmental Activities</u>
Current assets	
Cash and cash equivalents	\$ 201,009
Accounts receivable	63,137
Taxes receivable	56,327
Due from other State of West Virginia agencies	5,380
Inventories	30,273
Other assets	2,306
Total current assets	<u>358,432</u>
Non-current assets	
Capital assets, net of accumulated depreciation	
Land - non-infrastructure	14,287
Land improvements	3,537
Buildings	39,373
Furniture and fixtures	510
Rolling stock	48,309
Scientific equipment	671
Shop equipment	375
Roads	3,871,849
Bridges	829,610
Land - infrastructure	579,229
Work in progress	270,790
Total capital assets	<u>5,658,540</u>
Other non-current assets	3,574
Total assets	<u>6,020,546</u>
LIABILITIES	
Current liabilities	
Accounts payable	73,120
Retainages payable	14,770
Accrued payroll and related liabilities	20,337
Due to other State of West Virginia agencies	2,946
Accrued interest payable	2,327
Current maturities of long term obligations	42,107
Total current liabilities	<u>155,607</u>
Non-current liabilities	
Claims and judgements	4,095
Compensated absences	56,222
General obligation bonds	520,955
Total non-current liabilities	<u>581,272</u>
Total liabilities	<u>736,879</u>
NET ASSETS	
Invested in capital assets, net of related debt	5,198,392
Unrestricted	85,275
Total net assets	<u>\$ 5,283,667</u>

The Accompanying Notes Are An Integral
 Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
 DIVISION OF HIGHWAYS
 STATEMENT OF ACTIVITIES
 YEAR ENDED JUNE 30, 2002
 (amounts expressed in thousands)

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Functions/Programs	Expenses	Program Revenues		Net Revenue (Expenses) and Changes in Net Assets
		Charges for Services	Capital Grants and Contributions	
Government activities				
Road maintenance				
Expressway, trunkline & feeder & SLS	\$ 228,449	\$ -	\$ -	(228,449)
Contract paving & secondary roads	41,536	-	-	(41,536)
Small bridge repair & replacement	25,259	-	-	(25,259)
Litter control program	1,595	-	-	(1,595)
Depreciation	747	-	-	(747)
Other road operations				
Interstate highways	54,614	-	55,825	1,211
Appalachian highways	126,317	-	161,088	34,771
Other federal aid programs	199,802	-	216,243	16,441
Non federal aid improvements	41,966	-	-	(41,966)
Industrial access roads	2,224	-	3,914	1,690
Depreciation	224,441	-	-	(224,441)
General and administration				
Support and administrative operations	53,183	4,173	-	(49,010)
Claims	610	-	-	(610)
Costs associated with DMV	32,029	-	-	(32,029)
Interest on long-term debt	28,168	-	-	(28,168)
Unallocated depreciation	14,022	-	-	(14,022)
	<u>1,074,962</u>	<u>4,173</u>	<u>437,070</u>	<u>(633,719)</u>
General revenues				
Taxes:				
Gasoline and motor carrier				229,650
Wholesale motor fuel				71,314
Automobile privilege				180,472
Motor vehicle registration fees				87,380
Investment and interest income				8,148
Miscellaneous revenues				15,062
Total general revenues				<u>592,026</u>
Change in net assets				(41,693)
Net assets, beginning (as restated)				5,325,360
Net assets, ending				<u>\$ 5,283,667</u>

The Accompanying Notes Are An Integral
 Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
 DIVISION OF HIGHWAYS
 BALANCE SHEET - GOVERNMENTAL FUNDS
 JUNE 30, 2002
 (amounts expressed in thousands)

	State Road (General)	Capital Projects	Total Governmental Funds
ASSETS			
Assets			
Cash and cash equivalents	\$ 111,247	\$ 89,762	\$ 201,009
Receivables	61,857	1,280	63,137
Taxes receivable	56,327	-	56,327
Due from other State of West Virginia agencies	5,380	-	5,380
Due from other funds	71	-	71
Inventories	30,273	-	30,273
Other assets	2,306	-	2,306
	<u>\$ 267,461</u>	<u>\$ 91,042</u>	<u>\$ 358,503</u>
LIABILITIES AND FUND BALANCES			
Liabilities			
Accounts payable	\$ 67,422	\$ 5,698	\$ 73,120
Retainages payable	13,180	1,590	14,770
Accrued payroll and related liabilities	20,337	-	20,337
Due to other State of West Virginia agencies	2,946	-	2,946
Due to other funds	-	71	71
	<u>103,885</u>	<u>7,359</u>	<u>111,244</u>
Fund balances			
Reserved for capital projects	-	83,683	83,683
Reserved for inventories	30,273	-	30,273
Unreserved, undesignated	133,303	-	133,303
	<u>163,576</u>	<u>83,683</u>	<u>247,259</u>
	<u>\$ 267,461</u>	<u>\$ 91,042</u>	<u>\$ 358,503</u>

The Accompanying Notes Are An Integral
 Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
 DIVISION OF HIGHWAYS
 RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
 TO THE STATEMENT OF NET ASSETS
 JUNE 30, 2002
 (amounts expressed in thousands)

Total fund balances - governmental funds \$ 247,259

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:

Land - non infrastructure	\$	14,287	
Land improvements- non infrastructure		3,537	
Buildings		39,373	
Furniture and Fixtures		510	
Rolling Stock and Shop Equipment		48,309	
Scientific Equipment		671	
Shop Equipment		375	
Roads		3,871,849	
Bridges		829,610	
Infrastructure Land		579,229	
Work in process		270,790	5,658,540

Bonds issued by the Division have associated costs that are paid from current available financial resources in the funds. However, these costs are deferred on the statement of net assets 3,574

Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:

Accrued interest payable		(2,327)	
Claims and judgments		(4,095)	
Compensated absences		(56,222)	
General obligation bonds		(563,062)	(625,706)

Net assets of governmental activities \$ 5,283,667

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
YEAR ENDED JUNE 30, 2002
(amounts expressed in thousands)

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	State Road (General)	Capital Projects	Debt Service	Total Governmental Funds
Revenues				
Taxes				
Gasoline and motor carrier	\$ 229,650	\$ -	\$ -	\$ 229,650
Wholesale motor fuel	71,314	-	-	71,314
Automobile privilege	180,472	-	-	180,472
Industrial access	3,914	-	-	3,914
License, fees and permits				
Motor vehicle registrations and licenses	87,380	-	-	87,380
Special fees and permits	4,173	-	-	4,173
Federal aid				
Interstate highways	55,382	443	-	55,825
Appalachian highways	161,088	-	-	161,088
Other federal aid programs	202,217	14,026	-	216,243
Investment and interest income, net of arbitrage rebate	2,412	5,422	314	8,148
Miscellaneous revenues	15,062	-	-	15,062
	<u>1,013,064</u>	<u>19,891</u>	<u>314</u>	<u>1,033,269</u>
Expenditures				
Current				
Road maintenance				
Expressway, trunkline and feeder, state and	228,456	-	-	228,456
Contract paving and secondary roads	41,536	-	-	41,536
Small bridge repair and replacement	25,603	-	-	25,603
Litter control program	1,595	-	-	1,595
Support and administrative operations	70,927	-	-	70,927
Division of Motor Vehicles operations	32,029	-	-	32,029
Claims	15	-	-	15
Capital outlay				
Road construction				
Interstate highways	66,888	1,104	-	67,992
Appalachian highways	198,175	-	-	198,175
Other federal aid programs	274,354	20,777	-	295,131
Nonfederal aid construction	15,559	71,581	-	87,140
Industrial access road	2,224	-	-	2,224
Debt service	13,814	-	36,976	50,790
	<u>971,175</u>	<u>93,462</u>	<u>36,976</u>	<u>1,101,613</u>
Excess (deficiency) of revenues over expenditures	<u>41,889</u>	<u>(73,571)</u>	<u>(36,662)</u>	<u>(68,344)</u>
Other financing sources (uses)				
Proceeds from issuance of long term debt	-	114,172	-	114,172
Operating transfers in	132	-	35,859	35,991
Operating transfers out	(35,859)	-	(132)	(35,991)
Total other financing sources (uses)	<u>(35,727)</u>	<u>114,172</u>	<u>35,727</u>	<u>114,172</u>
Net change in fund balances	6,162	40,601	(935)	45,828
Fund balances, beginning of year	<u>157,414</u>	<u>43,082</u>	<u>935</u>	<u>201,431</u>
Fund balances, end of year	<u>\$ 163,576</u>	<u>\$ 83,683</u>	<u>\$ -</u>	<u>\$ 247,259</u>

The Accompanying Notes Are An Integral
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS

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RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2002
(amounts expressed in thousands)

Net change in fund balances - total governmental funds \$ 45,828

Amounts reported for governmental activities in the statement of activities
are different because:

Governmental funds report capital outlays as expenditures. However, in the
statement of activities, the cost of those assets is allocated over their
estimated useful lives as depreciation expense. This is the amount by which
capital outlays of \$245,996 exceeded depreciation of (\$239,209) in the
current period. 6,787

Bond proceeds provide current financial resources to governmental funds,
but issuing debt increases long-term liabilities in the statement of net assets.
Repayment of bond principal is an expenditure to governmental funds, but
the repayment reduces long-term liabilities in the statement of net assets.
This is the amount by which proceeds of (\$110,000) exceeded repayments
of \$21,485. (88,515)

Bonds issued at a premium provide current financial resources to
governmental funds, but increase the long-term liabilities in the statement of
net assets. Bond issuance costs are expenditures to governmental funds, but
are deferred assets in the statement of net assets. This is the amount by
which premiums of (\$4,172) exceeded bond issue costs of \$774. (3,398)

Some expenses reported in the statement of activities do not require the use
of current financial resources and therefore are not reported as expenditures
in the governmental funds. This is the amount by which the increase in
compensated absences of (\$8,863), interest payable of (\$347) and
amortization of bond issuance costs of (\$443) exceeded accretion of bond
premiums of \$1,153 and a decrease in accrued claims of \$6,105. (2,395)

Change in net assets of governmental activities \$ (41,693)

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION, DIVISION OF HIGHWAYS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
(BUDGETARY BASIS) - STATE ROAD FUND
YEAR ENDED JUNE 30, 2002
(amounts expressed in thousands)

	Original Budget	Budget Amendments	Final Budget	Actual Amounts	Variance with Final Budget - Positive (Negative)
Revenues					
Taxes					
Gasoline and motor carrier	\$ 226,505	\$ -	\$ 226,505	\$ 228,703	\$ 2,198
Wholesale motor fuel	72,370	-	72,370	72,771	401
Automobile privilege	159,050	-	159,050	171,402	12,352
Motor vehicle registrations and licenses	82,000	-	82,000	85,395	3,395
Federal aid	501,800	-	501,800	388,827	(112,973)
Miscellaneous revenues	15,560	-	15,560	13,174	(2,386)
	<u>1,057,285</u>	<u>-</u>	<u>1,057,285</u>	<u>960,272</u>	<u>(97,013)</u>
Expenditures					
Road construction					
Interstate highways	70,000	4,000	74,000	64,170	9,830
Appalachian highways	250,000	(30,000)	220,000	201,063	18,937
Other federal aid programs	290,700	-	290,700	239,682	51,018
Nonfederal aid construction	20,000	4,000	24,000	16,675	7,325
Road maintenance					
Maintenance	234,000	7,379	241,379	228,936	12,443
Contract paving and secondary roads	50,000	-	50,000	41,572	8,428
Small bridge repair and replacement	36,000	(2,000)	34,000	25,254	8,746
Litter control program	1,600	-	1,600	1,600	-
Support and administrative operations					
General operations	49,101	(5,784)	43,317	41,675	1,642
Equipment revolving	15,000	-	15,000	8,035	6,965
Inventory revolving	2,000	-	2,000	61	1,939
Debt service	50,000	-	50,000	49,446	554
Division of Motor Vehicles operations	35,009	3	35,012	32,029	2,983
Waste tire	3,625	-	3,625	902	2,723
Claims	15	-	15	15	-
	<u>1,107,050</u>	<u>(22,402)</u>	<u>1,084,648</u>	<u>951,115</u>	<u>133,533</u>
Excess (deficiency) of revenues over expenditures	(49,765)	22,402	(27,363)	9,157	36,520
Fund balance, beginning of year	96,835	-	96,835	96,835	-
Fund balance, end of year	<u>\$ 47,070</u>	<u>\$ 22,402</u>	<u>\$ 69,472</u>	<u>\$ 105,992</u>	<u>\$ 36,520</u>

The Accompanying Notes Are An Integral
Part Of These Financial Statements

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION - The accompanying financial statements of the West Virginia Department of Transportation, Division of Highways (the "Division") have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999 the GASB issued Statement 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. This Statement established new financial reporting requirements for state and local governments throughout the United States. It requires new information and restructure much of the information that governments have presented in the past. Comparability with reports issued in prior years is affected.

The Division is required to implement these standards for the fiscal year ending June 30, 2002, which is consistent with the West Virginia Department of Transportation and the State of West Virginia's adoption period. The Division has adopted the provisions of GASB Statement 34 for its fiscal year ended June 30, 2002. With the implementation of GASB Statement 34, the Division has prepared required supplementary information titled *Management's Discussion and Analysis*, which precedes the basic financial statements.

Other GASB Statements are required to be implemented in conjunction with GASB Statement 34. Therefore, the Division has implemented the following GASB Statements in the current fiscal year: Statement 33 - *Accounting and Financial Reporting for Nonexchange Transactions*, Statement 36 - *Recipient Reporting for Certain Shared Nonexchange Revenues*, Statement 37 - *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and Statement 38 - *Certain Financial Statement Note Disclosures*. The accompanying financial statements present the financial position of the Division and the various funds, and the results of operations of the Division and the various funds.

Significant changes required by the implementation of these statements include the presentation of management's discussion and analysis, which precedes the financial statements, and the presentation of accrual based government-wide financial statements, including the recording of infrastructure assets. The following summarizes significant impacts of transitioning to the new reporting model.

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Deferred issue costs are capitalized and amortized as governmental activities, but reported as expenditures in the governmental fund statements.
- Unless due and payable, long-term liabilities, such as bonds, compensated absences, litigation and others only appear as liabilities in the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are recorded as expenditures on the governmental fund statements.
- Bond proceeds, including any premiums on debt issued, result in liabilities on the government-wide statements, but are recorded as other financing sources on the governmental fund statements.
- Certain other outflows represent either increases or decreases in liabilities on the government-wide statements, but are reported as expenditures on the governmental fund statements.

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

The financial statements of the Division are intended to present the financial position, and the results of operations of only that portion of the financial reporting entity of the West Virginia Department of Transportation and the State of West Virginia, that is attributable to the transactions of the Division. They do not purport to, and do not, present fairly the financial position of the West Virginia Department of Transportation or the State of West Virginia as of June 30, 2002 and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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

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

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS - The government-wide financial statements (the statement of net assets and the statement of activities) report information of all of the non-fiduciary activities of the primary government and its component units, if any. For the most part, the effect of interfund activity has been removed from these government-wide statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable. The Division has no component units, fiduciary activities or business type activities; therefore the government-wide financial statements of the Division are composed of all of the governmental activities of the Division.

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

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets.

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION -

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

GOVERNMENTAL FUND FINANCIAL STATEMENTS - The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Division considers revenues to be available if they are collected within 60 days of the end of the current fiscal year. Principal revenues subject to accrual include gasoline and wholesale fuel taxes, automobile privilege taxes, federal reimbursements and other reimbursements for use of materials and services.

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

- Employees' vested annual leave is recorded as an expenditure when utilized. The amount of accumulated annual leave unpaid at June 30, 2002, has been reported only in the government-wide financial statements.
- Division employees earn sick leave benefits, which accumulate, but do not vest. When separated from employment with the Division, an employee's sick leave benefits are considered ended and no reimbursement is provided. However, an employee may convert, at the time of retirement, any unused accumulated sick leave to pay a portion of the employee's post employment health care insurance premium or to increase service credits for retirement purposes. The liability for accumulated sick leave for employees has been recorded only in the government-wide financial statements.
- The Division pays 100% of the health insurance premium for retirees who elected to participate in the health insurance plans prior to July 1, 1988, and 50% of the premium for retirees who elected to participate on or after that date. The liability for accumulated post-retirement health insurance has been reported only in the government-wide financial statements.
- Principal and interest on general long-term debt are recorded as fund liabilities when due or when amounts have been accumulated in the debt service fund for transfer to the fiscal agent or for payment to be made early in the following year.
- Claims and judgments are recorded only when payment is due.

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

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

- State Road (General) Fund - This fund serves as the Division's general fund and is used to account for all financial resources, except those required to be accounted for in another fund. The State Road Fund is funded primarily by dedicated highway user taxes and fees and matching federal highway funds.
- Capital Projects Fund - This fund accounts for financial resources to be used for road construction or reconstruction financed by proceeds from the sale of the Safe Road Bonds and matching federal highway funds.
- Debt Service Fund - This fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

INTERFUND ACTIVITY - As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges from the government's various functions. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

BUDGETING AND BUDGETARY CONTROL - The Division's expenditures are subject to the legislative budget process of the State, with annual budgets adopted utilizing the cash basis of accounting. The cash basis is modified at year-end to allow for payment of invoices up to 31 days after year-end for goods or services received prior to year-end. Appropriated budgeted expenditures, which lapse 31 days after the end of the fiscal year, are incorporated into the Division's overall financial plan, which includes revenue estimates developed by the Division and the State's executive branch. Expenditures are budgeted using natural categories of activity including specific categories of construction, maintenance, and operations, as well as for special items. Any revisions that alter budgeted expenditures for the expenditure categories for each Division as a whole must be approved by the State Legislature.

The Division's State Road Fund has a legislatively approved budget. However, the capital projects fund, debt service fund, and certain monies reported within the State Road Fund for GAAP purposes, are not considered appropriated funds in accordance with the Division's budgetary reporting policy. Accordingly, these funds have not been reported in the Division's Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual (Budgetary Basis) - State Road Fund. A reconciliation of the excess of revenues over expenditures and other financing uses for the year ended June 30, 2002, on the budgetary basis to the GAAP basis for the State Road Fund follows:

Excess of revenues over expenditures - budgetary basis	\$ 9,157
Basis of accounting differences (budgetary to GAAP)	(6,502)
Appropriated debt service	36,662
Unbudgeted funds	<u>2,572</u>
 Excess of revenues over expenditures - GAAP basis.	 <u>\$ 41,889</u>

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

CASH AND CASH EQUIVALENTS - Cash and cash equivalents are short-term investments with original maturities of 90 days or less. Cash and Cash equivalents principally consist of amounts on deposit in the State Treasurer's Office (STO) that are pooled funds managed by the West Virginia Investment Management Board (IMB). In addition, the Division makes interest-earning deposits in certain investment pools maintained by the IMB that are available to the Division with overnight notice. Interest income from these investments is prorated to the Division at rates specified by the IMB based on the balance of the Division's deposits maintained in relation to the total deposits of all state agencies participating in the pool. Because these deposits are held in the IMB investment pools, no other disclosures related to safekeeping, credit or market risk, or GASB 3 risk are required. However, market risk exists as the value of the investment pools underlying investment assets may decline because of an increase in interest rates or a decline in stock prices. The carrying value of the deposits reflected in the financial statements approximates fair value and approximates the value of the shares in the external investment pool.

The STO has statutory responsibility for the daily cash management activities of the State's agencies, departments, boards, and commissions. The STO determines which funds to transfer to the IMB for investment in accordance with the West Virginia Code, policies set by the IMB, and provisions of bond indentures and trust agreements when applicable. The IMB is governed by a thirteen-member Board of Trustees. The Governor, the State Auditor and the State Treasurer are members of the Board and the other members are appointed by the Governor. The Board was formed in 1997 to serve as the Trustee to hold certain public pension funds and insurance funds, as well as to provide prudent fiscal administration, investment, and management of the Consolidated Pension Fund and the State's operating funds.

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

CAPITAL ASSETS - Capital assets, which include buildings, non-infrastructure land, furniture and fixtures, rolling stock, scientific equipment, shop equipment and infrastructure assets (which are normally immovable and of value only to the division, such as roads, bridges, and similar items), are reported in the statement of net assets in the government-wide financial statements. Capital assets are defined by the Division as non-infrastructure assets which have a cost of five thousand dollars or more for machinery, equipment, rolling stock, furniture and fixtures; twenty-five thousand dollars or more for buildings at the date of acquisition and have an expected useful life of three or more years; and infrastructure assets with a cost in excess of one million dollars. Purchased and constructed capital assets are valued at historical cost or estimated historical cost. Donated fixed assets are recorded at their fair market value at the date of donation.

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

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (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.

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

- Machinery and Equipment: 5 - 20 years
- Buildings: 40 years
- Furniture and Fixtures: 3 - 20 years
- Rolling stock: 1 - 20 years
- Scientific equipment: 2 - 25 years
- Infrastructure: Roads - 30 years
- Infrastructure: Bridges - 50 years

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

OTHER ASSETS - Other assets represent payments that reflect costs applicable to future accounting periods and are recorded as other assets in both government-wide and fund financial statements. They are composed primarily of amounts on deposit with West Virginia Workers' Compensation Fund.

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

COMPENSATED ABSENCES - Division employees generally earn vacation and sick leave on a monthly basis. Vacation, up to specific limits, is fully vested when earned, and sick leave, while not vesting to the employee prior to retirement, can be carried over to subsequent periods. Any unused vacation and sick leave accumulated at employee retirement vests to the employee and may be provided in the form of post-retirement payment of all or a portion of the employee's health insurance premiums, or as service credits for retirement purposes. The Division pays 100% of the health insurance premium for retirees who elected to participate in the health insurance plans prior to July 1, 1988, and 50% of the premium for retirees who elected to participate on or after that date. Expenditures for vacation, sick leave, and post retirement health insurance premiums are recognized as incurred in the governmental fund financial statements. The government-wide financial statements present the cost of accumulated vacation leave, sick leave and post-retirement health insurance as a liability.

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

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

ARBITRAGE REBATE LIABILITY - The capital project fund accounts for arbitrage rebate payable, if any, as a liability of the fund. The change in the obligation is recorded as an adjustment to current year interest revenue.

NOTE 2 - ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2002 consisted of the following:

Federal aid billed and not paid	\$ 2,316
Federal aid earned but not billed	<u>55,143</u>
Total federal aid receivable	57,459
Other receivables	<u>8,178</u>
Combined total receivables	65,637
Less: allowance for uncollectibles	<u>2,500</u>
Net accounts receivable	<u><u>\$ 63,137</u></u>

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

NOTE 3 - TAXES RECEIVABLE

Taxes receivable at June 30, 2002 consisted of the following:

Automobile privilege taxes	\$ 28,582
Gasoline and motor fuel taxes	<u>27,745</u>
	<u><u>\$ 56,327</u></u>

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 4 - DUE FROM/TO OTHER STATE OF WEST VIRGINIA AGENCIES

Amounts due from other State of West Virginia agencies at June 30, 2002 consisted of the following:

The Department of Administration	\$	114
Bureau of Employment Programs		64
Office of Emergency Services		4,727
The Department of Transportation		237
The Governor's Office		48
West Virginia State Police		40
West Virginia Building Commission		28
Adjutant Generals Office		94
Other agencies		<u>28</u>
	<u>\$</u>	<u>5,380</u>

Amounts due to other State of West Virginia agencies at June 30, 2002 consisted of the following:

The Department of Administration	\$	336
Bureau of Employment Programs		2,358
The Department of Tax and Revenue		9
Division of Environmental Protection		27
Department of Natural Resources		51
Division of Corrections		138
Division of Culture and History		23
Other agencies		<u>4</u>
	<u>\$</u>	<u>2,946</u>

NOTE 5 - INTERFUND TRANSFERS

A summary of interfund transfers for the fiscal year ended June 30, 2002 follows:

Transfers From (Out)	Transfers To (In)	For Purpose	Amount
State Road Fund	Debt Service Fund	To transfer amounts necessary to meet debt service requirements on the Divisions General Obligation Bonds	\$ 35,859
Debt Service Fund	State Road Fund	To transfer funds in excess of those required to meet debt service requirements to the State Road fund	<u>132</u>
			<u>\$ 35,991</u>

West Virginia Department of Transportation,
Division of Highways
Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 6 - INVENTORIES

Inventories at June 30, 2002 consisted of the following:

Materials and supplies	\$	19,710
Equipment repair parts		9,351
Gas and lubrication supplies		<u>1,212</u>
	\$	<u>30,273</u>

During the fiscal year management adjusted its capitalization policy related to certain items that are carried in material and supplies inventory to eliminate the stocking of certain items at organizations below the District level. The result of this change was an adjustment of approximately \$2,289 to reflect such items carried below the district organization level as an expenditure.

NOTE 7 - CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2002, was as follows:

	Balance <u>July 1, 2001</u>	<u>Increases</u>	<u>Decreases</u>	Balance <u>June 30, 2002</u>
Capital assets not being depreciated:				
Land - non infrastructure	\$ 13,387	\$ 900	\$ -	\$ 14,287
Land - infrastructure	521,454	57,775	-	579,229
Construction-in-progress - roads	348,094	127,172	246,995	228,271
Construction-in-progress - bridges	<u>146,687</u>	<u>41,143</u>	<u>145,311</u>	<u>42,519</u>
Total capital assets not being depreciated	<u>1,029,622</u>	<u>226,990</u>	<u>392,306</u>	<u>864,306</u>
Capital assets being depreciated:				
Buildings	59,103	4,365	49	63,419
Furniture and fixtures	3,406	197	48	3,555
Land improvements - non infrastructure	3,204	1,286	-	4,490
Rolling stock	161,645	12,951	3,365	171,231
Shop equipment	3,013	48	17	3,044
Scientific equipment	1,826	159	23	1,962
Infrastructure - roads	5,877,066	246,994	-	6,124,060
Infrastructure - bridges	<u>869,941</u>	<u>145,312</u>	<u>-</u>	<u>1,015,253</u>
Total capital assets being depreciated	<u>6,979,204</u>	<u>411,312</u>	<u>3,502</u>	<u>7,387,014</u>
Less accumulated depreciation:				
Buildings and improvements	22,275	1,820	49	24,046
Furniture and fixtures	2,871	222	48	3,045
Land improvements - non infrastructure	728	225	-	953
Rolling stock	114,085	12,202	3,365	122,922
Shop equipment	2,500	186	17	2,669
Scientific equipment	1,200	114	23	1,291
Infrastructure - roads	2,048,076	204,135	-	2,252,211
Infrastructure - bridges	<u>165,337</u>	<u>20,306</u>	<u>-</u>	<u>185,643</u>
Total accumulated depreciation	<u>2,357,072</u>	<u>239,210</u>	<u>3,502</u>	<u>2,592,780</u>
Total capital assets being depreciated, net	<u>4,622,132</u>	<u>172,102</u>	<u>-</u>	<u>4,794,234</u>
Governmental activities capital assets, net	<u>\$ 5,651,754</u>	<u>\$ 399,092</u>	<u>\$ 392,306</u>	<u>\$ 5,658,540</u>

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 7 - CAPITAL ASSETS (Continued)

Current year depreciation totaling \$239,210 was allocated as a separate line item in the statement of activities under the major functions of the Division of Maintenance and Improvements. The remaining unallocated depreciation expense is included as a separate line item in the statement of activities. Infrastructure depreciation is primarily related to construction type activities; depreciation of shop and rolling stock assets is primarily related to maintenance type activities; and depreciation of buildings and improvements and furniture and fixtures support all of the various activities of the Division.

A summary of depreciation on each capital asset type follows:

<u>Asset Type</u>	<u>Depreciation</u>
Buildings and improvements	\$ 1,820
Furniture and fixtures	12,202
Rolling stock	186
Land improvements	225
Shop equipment	222
Scientific equipment	114
Infrastructure - roads	204,135
Infrastructure - bridges	20,306
Total depreciation expense	<u>\$ 239,210</u>

NOTE 8 - RETAINAGES PAYABLE

The Division has entered into an arrangement with the West Virginia Investment Management Board whereby amounts retained from payments to contractors may, at the option of the contractor, be deposited in an interest bearing account in the contractor's name. Retainage payments are made to the contractor when contracts are satisfactorily completed. The funds on deposit in these accounts are not reported as assets of the Division. At June 30, 2002, retainages payable on contracts had been reduced by these amounts on deposit in such accounts by approximately \$13,006.

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 9 - LONG-TERM OBLIGATIONS

Long-term obligations at June 30, 2002, and changes for the fiscal year then ended are as follows:

	Issue Date	Interest Rates	Maturity Through	Beginning Balance	Additions	Reductions	Ending Balance
General Obligation Bonds Payable From Tax Revenue:							
Better Highway Bonds	1973	5.625% -6.10% 4.30%-	02/01/2006	\$ 30,620	\$ -	\$ 11,960	\$ 18,660
Safe Road Bonds	1998	5.25% 4.30%-	06/01/2023	204,080	-	-	204,080
Safe Road Bonds	1999	5.75% 5.50%-	06/01/2017	106,325	-	1,305	105,020
Safe Road Bonds	2000	5.75% 3.50%-	06/01/2025	110,000	-	-	110,000
Safe Road Bonds	2001	5.50%	06/01/2013	-	110,000	8,220	101,780
Total General Obligation Bonds				451,025	110,000	21,485	539,540
Bond Premium				<u>1,271</u>	<u>4,172</u>	<u>1,153</u>	<u>4,290</u>
Total general obligation bonds payable net of premium				<u>452,296</u>	<u>114,172</u>	<u>22,638</u>	<u>543,830</u>
Claims and judgments				11,200	595	6,700	5,095
Compensated absences				65,269	9,185	-	74,454
Other long-term				<u>320</u>	-	<u>320</u>	-
Total long-term obligations				<u>\$ 529,085</u>	<u>\$ 123,952</u>	<u>\$ 29,658</u>	<u>\$ 623,379</u>

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

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 9 - LONG-TERM DEBT OBLIGATIONS (Continued)

Debt service expenditures for debt service funds included interest of \$28,168 for the year ended June 30, 2002. Total debt service costs, exclusive of coupon redemption costs, for each of the next five years and thereafter, on general obligation bonds payable and liquidated through debt service funds, are as follows:

	2003	2004	2005	2006	2007	2008- 2012	2013- 2017	2018- 2022	2023- 2025	Total
General obligation bonds payable from tax revenue:										
Better highway bonds	\$ 8,933	\$ 6,360	\$ 3,909	\$ 1,567	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 20,769
Safe road bonds	<u>41,063</u>	<u>43,638</u>	<u>46,087</u>	<u>48,431</u>	<u>49,997</u>	<u>249,986</u>	<u>173,087</u>	<u>117,601</u>	<u>70,556</u>	<u>840,446</u>
Total general obligation bonds	49,996	49,998	49,996	49,998	49,997	249,986	173,087	117,601	70,556	861,215
Less: interest	<u>27,956</u>	<u>26,928</u>	<u>25,781</u>	<u>24,628</u>	<u>23,532</u>	<u>96,036</u>	<u>57,837</u>	<u>31,671</u>	<u>7,306</u>	<u>321,675</u>
Total principal	22,040	23,070	24,215	25,370	26,465	153,950	115,250	85,930	63,250	539,540
Bond premium	<u>835</u>	<u>675</u>	<u>563</u>	<u>475</u>	<u>400</u>	<u>1,137</u>	<u>205</u>	<u>-</u>	<u>-</u>	<u>4,290</u>
Total principal and bond premium	<u>\$ 22,875</u>	<u>\$ 23,745</u>	<u>\$ 24,778</u>	<u>\$ 25,845</u>	<u>\$ 26,865</u>	<u>\$ 155,087</u>	<u>\$ 115,455</u>	<u>\$ 85,930</u>	<u>\$ 63,250</u>	<u>\$ 543,830</u>

The portion of long-term and short-term compensated absences, claims payable, and general obligation bonds are as follows:

	Compensated <u>Absences</u>	Claims and <u>Judgments</u>	General Obligation <u>Bonds and Premium</u>	<u>Total</u>
Short-term liability	\$ 18,232	\$ 1,000	\$ 22,875	\$ 42,107
Long-term liability	<u>56,222</u>	<u>4,095</u>	<u>520,955</u>	<u>581,272</u>
	<u>\$ 74,454</u>	<u>\$ 5,095</u>	<u>\$ 543,830</u>	<u>\$ 623,379</u>

During the year ended June 30, 1972, the State was authorized by constitutional amendment to issue \$500,000 of general obligation bonds to fund highway and road construction projects known as Better Highway Bonds. During the year ended June 30, 1997, the State was authorized by constitutional amendment to issue \$550,000 of general obligation bonds to fund highway and road construction projects known as Safe Road Bonds. These bonds will be repaid from revenues of the State Road Fund. Safe Road Bonds of \$220,000 were issued during July 1998; \$110,000 were issued during July 1999; \$110,000 were issued during July 2000; and an additional \$110,000 were issued during July 2001.

The Division's Safe Road Bonds are subject to the arbitrage rebate provisions of the Internal Revenue Code, which requires 90% of interest earnings in excess of interest expended to be paid to the Internal Revenue Service. The Division has no arbitrage rebate liability as of June 30, 2002.

West Virginia Department of Transportation,
 Division of Highways
 Notes to the Financial Statements
 Year Ended June 30, 2002
 (amounts expressed in thousands)

NOTE 9 - LONG-TERM DEBT OBLIGATIONS (Continued)

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

	<u>Year Ended</u> <u>June 30, 2002</u>	<u>Year Ended</u> <u>June 30, 2001</u>	<u>Year Ended</u> <u>June 30, 2000</u>
Estimated claims liability, July 1, 2001	\$ 11,200	\$ 9,300	\$ 11,020
Additions for claims incurred during the year	2,787	1,585	1,905
Changes in estimates for claims of prior periods	(8,877)	415	(3,485)
Payments on claims	<u>(15)</u>	<u>(100)</u>	<u>(140)</u>
Estimated claims liability, June 30, 2001	<u>\$ 5,095</u>	<u>\$ 11,200</u>	<u>\$ 9,300</u>

At June 30, 2002, approximately \$15,250 of tort claims and \$2,567 of construction claims, including non-incremental claims, were pending against the Division in the West Virginia State Court of Claims. With respect to these claims, the Division has an estimated obligation of \$4,500, recorded in the government-wide Statement of Net Assets, based on management's evaluation of the nature of such claims and consideration of historical loss experience for the respective types of action. Such claims will be recognized primarily as expenditures of the State Road Fund if, and when, they are approved for payment by the Legislature in accordance with legal statutes. Also included in claims are claims that have been settled in the court of claims and approved for payment through legislative action. These amounts total approximately \$595. During the normal course of operations, the Division may become subject to other litigation. Accordingly, no provision has been made in the financial statements for liabilities, if any, from such litigation.

The Division's obligation for accrued vacation leave time includes leave time and related costs expected to be paid to employees in the future and is determined using wage levels in effect at the date the obligation is calculated. Also included in this amount is the Division's unfunded obligation of approximately \$3,783 arising in connection with legislation to fund portions of employee post retirement health insurance costs for retired employees. These liabilities are generally liquidated by the State Road Fund.

Upon retirement, an employee may apply unused sick leave or annual leave, or both to reduce their future insurance premiums paid to the West Virginia Public Employees Insurance Agency or to obtain a greater benefit under the West Virginia Public Employees Retirement System. These liabilities are generally liquidated by the State Road Fund.

West Virginia Department of Transportation,
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Notes to the Financial Statements
Year Ended June 30, 2002
(amounts expressed in thousands)

NOTE 10 - TRANSACTIONS WITH THE STATE OF WEST VIRGINIA

The Division leases from the Department of Administration substantially all of State Office Building No. 5 and a portion of State Office Building No. 3 which are owned by the State Building Commission. The Division may be released from its obligation only at the option of the lessor. The Division is obligated under these operating leases, which expire December 31, 2002 for rental payments of approximately \$1,796 annually. Management expects the leases to be renewed upon expiration.

During the year ended June 30, 2002 the Division incurred payroll related expenditures of approximately \$22,261 for employee health insurance benefits and approximately \$8,682 for employee workers' compensation benefits, which are paid into funds administered by the West Virginia Public Employees Insurance Agency and Workers' Compensation Fund, respectively.

Monies were paid from the State Road Fund to the Department of Military Affairs and Public Safety, Division of Public Safety for various services performed. These expenditures, which were authorized by the Legislature, amounted to approximately \$5,466 during the year ended June 30, 2002.

NOTE 11 - COMMITMENTS AND CONTINGENCIES

The amount of unexpended balances of highway design and construction contracts entered into by the Division with various contractors approximated \$507,817 at June 30, 2002.

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

During the year ended June 30, 1989, the Division in-substance defeased Huntington Bridge Revenue Bonds dated January 1, 1965, by authorizing the West Virginia Municipal Bond Commission (MBC), the bond fiscal agent, to purchase U.S. government securities which will mature on dates to coincide with the remaining principal and interest payments. At June 30, 2002, \$2,295 of these bonds were outstanding and are considered defeased. Accordingly, the assets and liability for these defeased bonds have been excluded from the Division's financial statements.

West Virginia Department of Transportation,
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NOTE 12 - RETIREMENT PLAN

PLAN DESCRIPTION - The Division contributes to the West Virginia Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan administered by the West Virginia Consolidated Public Retirement Board. Chapter 5, Article 10 of the West Virginia State Code assigns the authority to establish and amend benefit provisions to the PERS Board of Trustees. Employees who retire at or after age 55 and have completed 25 years of credited service are eligible for retirement benefits as established by State statute. Retirement benefits are payable monthly for life, in the form of a straight-line annuity equal to two percent of the employee's final average salary, multiplied by the number of years of the employee's credited service at the time of retirement. PERS also provides deferred retirement, early retirement, death, and disability benefits to plan members and beneficiaries. The West Virginia Consolidated Public Retirement Board issues a publicly available financial report that includes financial statements and required supplementary information for PERS. That report may be obtained by writing to the West Virginia Consolidated Public Retirement Board, 1900 Kanawha Boulevard East, Building Five, Charleston, West Virginia 25305 or by calling (304) 558-3570.

FUNDING POLICY - The PERS funding policy has been established by action of the State Legislature. State statute requires that plan participants contribute 4.5% of compensation. The current combined contribution rate is 14% of annual covered payroll, including the Division's contribution of 9.5% which is established by PERS. The Division's contributions to PERS for the years ended June 30, 2002, 2001, and 2000 were \$15,717, \$15,275, and \$14,489, respectively, equal to the required contributions for each year.

NOTE 13 - RISK MANAGEMENT

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

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

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

West Virginia Department of Transportation,
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Notes to the Financial Statements
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(amounts expressed in thousands)

NOTE 14 - IMPACT OF FLOODS

In May and July of 2001 and May of 2002, the State of West Virginia experienced significant flooding. The Division incurred significant expenditures related to emergency work as a result of these floods. The Division worked to recover from these floods, which occurred in southern West Virginia, and to complete work associated with previous disaster projects, which were in process but not completed in prior years. The Division recognizes it is extremely important for local economies to have transportation access restored immediately. During the fiscal year the Division incurred expenditures of approximately \$31,700 on roads deemed eligible for Federal Emergency Management Assistance (FEMA), and \$17,200 on roads deemed eligible for FHWA assistance, to repair and restore damaged roadways to operation. The Division was reimbursed for \$19,500 of expenditures on FEMA routes and \$8,100 on FHWA routes. The unreimbursed expenditures are reflected within the road fund balances.

COMPLIANCE AND INTERNAL CONTROL REPORT

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON
AN AUDIT OF GENERAL PURPOSE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS*

Joint Committee on Government and Finance
West Virginia Legislature

We have audited the financial statements of the West Virginia Department of Transportation, Division of Highways as of and for the year ended June 30, 2002, and have issued our report thereon dated October 31, 2002. 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.

Compliance

As part of obtaining reasonable assurance about whether the West Virginia Department of Transportation, Division of Highways' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 instances of noncompliance that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings as items 2002-2 through 2002-8. Additionally, we noted certain immaterial instances of noncompliance that we have reported to management of the West Virginia Department of Transportation, Division of Highways, and the Joint Committee on Government and Finance in a separate letter dated October 31, 2002.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the West Virginia Department of Transportation, Division of Highways' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the West Virginia Department of Transportation, Division of Highways' ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying schedule of findings as items 2002-1 through 2002-8.

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A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the West Virginia Department of Transportation, Division of Highways, and the Joint Committee on Government and Finance in a separate letter dated October 31, 2002.

This report is intended solely for the information of the West Virginia Legislature, the Division's management, 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.

Suttle & Stalnaker, PLLC

October 31, 2002

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-1	Information Systems Controls
Criteria:	The management of the Division is responsible for establishing and maintaining adequate information systems internal controls.
Condition:	<p>The Division operates a wide variety of computer applications, many of which affect federal and state programs' data. During our review of the information systems controls we noted the following:</p> <ul style="list-style-type: none">• There are no formal policies and procedures for review and monitoring of the user account access maintenance. (Also noted in prior year)• There are no formal policies and procedures for review and monitoring various information system security reports such as the "failed access report." (Also noted in prior year)• There are no policies and procedures in place for conducting periodic intrusion testing of the various computer systems maintained by the Division.
Context:	Information systems controls potentially can affect all federal and state programs and are critical to the daily operations of the Division.
Cause:	Policies and procedures have not been adequately updated and information system controls have not been monitored by the Division.
Effect:	Unauthorized access to critical information systems may occur and not be detected.
Recommendation:	We recommend that the Division strengthen their policies and procedures related to information systems controls and ensure that controls are operating as designed. In addition, the Division should work with the Information System and Controls Department of the State of West Virginia to ensure that periodic intrusion testing is conducted for all significant systems utilized by the Division. Further, the internal audit group of the Division should consider designing audit procedures for the monitoring and review of information system controls.
Management Response:	<i>Agree. We have made progress toward some of the specific items noted with this recommendation. We have established formal network logon/password policies and we have electronically interfaced the monthly mainframe report of terminated personnel with the PC network user accounts system to automate account deletions. Also, we have cooperated fully with the Information Services and Communications Division in the statewide initiative to perform periodic intrusion detection. The first test resulted in no unknown or unacceptable accesses from outside the DOT computer network. We will continue to cooperate with IS&C on this and all other security policies and programs.</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
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YEAR ENDED JUNE 30, 2002

2002-2	Accounts Receivable Collection and Financial Reporting
Criteria:	Article V of the Constitution of West Virginia states in part that, “the legislative, executive and judicial departments shall be separate and distinct, so that neither shall exercise the powers properly belonging to either of the others.” Furthermore, Article 10, Section 6 of the Constitution of West Virginia states in part that, “credit of the state shall not be granted to, or in aid of any county, city, township, corporation or person; nor shall the state ever assume, or become responsible for the debts or liabilities of any county, city, township, corporation or person.” Furthermore, the Division’s accounts receivable policies and procedures state that entities with past due balances will have credit discontinued until the account is brought current.
Condition:	We noted that management of the Division has extended credit to other entities, including State agencies and political subdivisions that have accounts receivable balances that are past due. Thus, the Division significantly decreases their ability to collect these balances through the regular collection process. Furthermore, the Division does not have policies and procedures for analyzing and adjusting on a monthly basis the allowance for doubtful accounts as reported in the Division’s financial statements.
Context:	The total allowance for doubtful accounts as of June 30, 2002 was approximately \$2.5 million. The total accounts receivable for this category of transactions as of June 30, 2002 was approximately \$8.2 million.
Cause:	Management of the Division has extended credit to entities, including other State agencies and political subdivisions of the State that have accounts receivable balances that are past due. Furthermore, the Division does not have policies and procedures for analyzing and adjusting on a monthly basis the allowance for doubtful accounts as reported in the Division’s financial statements.
Effect:	The extension of credit to other State agencies and political subdivisions could be construed as the Division appropriating funds, thus usurping the constitutional authority of the legislature. Also, the net realizable value of accounts receivable may be overstated on financial reports prepared by the Division.
Recommendation:	We recommend that the Division suspend the extension of credit to entities, including other State agencies and political subdivisions with past due balances until the account is brought current. Also we recommend that the Division evaluate accounts with balances outstanding to identify any other State agencies or political subdivisions that should not be granted credit due to a history of late payment. In addition, the Division should review its policies and procedures to determine if changes are needed and should develop policies and procedures for analyzing the amount reported in the allowance for doubtful accounts in the Division’s financial statements.
Management Response:	<i>The Division of Highways agrees with the recommendation that a policy be developed to analyze the allowance accounts for Accounts Receivable. The Accounts Receivable Supervisor is preparing an analytical spreadsheet with historical information to better support making adjustments to our allowance accounts. We will incorporate the policy dealing with the allowance account into the existing collection policy for the Accounts Receivable Section. We also offer the following comments:</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-2

Accounts Receivable Collection and Financial Reporting (Continued)

Management Response:
(Continued)

1. *The Division of Highways does cease credit extension for entities that have past due balances. For hauling permit and escort services accounts through our Enforcement Division, and our "SS" accounts (bid letting and specs) no further charges are allowed until the balance is paid in full. Trucks often have to wait at the state line because we will not issue permits or provide escorts on an overdue account. When entities that have leases with Property Management for sign (logo) rental or property rentals become delinquent, they are noticed that their lease will be cancelled or their signs removed. If payment is not received, these actions are taken.*
2. *In the case of governmental entities, the situation is more complicated. The Division aggressively employs every legal recourse available to collect debts from entities such as County Commissions, Public Service Divisions, Towns, School Boards, Prisons, and State Agencies. We have a record of taking many of these entities to the Court of Claims for Collection, where we have been overwhelmingly successful. However this is often a more complex situation than can be dealt with a simple refusal of services. For example, we have had Emergency Services Organizations with an outstanding balance need gasoline for an ambulance or a school board for its busses. Often in rural areas we are the only source for gasoline in emergency situations. During the past several years the number of governmental entities obtaining gasoline from the Division of Highways has significantly decreased. It has been our goal to eliminate this service completely, but emergency situations arise where this is impossible. We receive calls from members of the legislature requesting the Division's services for their constituency in dire circumstances such as water hauling during a drought or assistance from flood damage. Some of these situations are on an emergency status from the Governor's Office and some are not. The Division of Highways asserts that government must provide for its citizens particularly in exigent circumstances. The Division has responded to these requests with this premise rather than a strictly financial one. The Division seeks guidance from the Legislature for handling matters such as these and requests for services to governmental entities from the Governor's Office on a non-emergency basis to entities indebted to the Division. The Division is currently carrying balances for many government entities for water emergency services.*
3. *The Division does not agree that the extension of credit to entities with outstanding balances "significantly decreases their ability to collect these balances through the regular collection process". There are two applicable time periods for the collection of debts. We have 2 years to collect non-contractual debts and 10 years to collect debts incurred by contract. The Statute of Limitations begins to run when the debt is incurred or the contract is signed. Therefore subsequent debts have no effect on collecting a prior debt that has a different Statute of Limitations. During the applicable time period Accounts Receivable, The Claims Division, and ultimately the Legal Division work systematically to obtain payment. Prior to the Statute of Limitations expiring, the debt is referred to the Legal Division where a determination is made whether to file a lawsuit. Many factors are considered primarily being if the entity has sufficient funds or assets to satisfy a judgment. If it appears feasible to file a lawsuit, a case is filed in Circuit Court or a claim in the Court of Claims. When the Division receives a judgment, every means available to execute the judgment is pursued.*

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-3	Independent Engineer's Cost Estimate
Criteria:	Section 157-1-7.7b of the Code of State Rules requires the director of the division initiating the request for service to be responsible for preparing an independent engineer's cost estimate prior to the receipt of the fee proposal from the consultant.
Condition:	As noted in the prior year, we noted several instances in which the engineer's cost estimate was not prepared by the Division until after the consultant's price proposal was received.
Context:	Total expenditures for architectural and engineering services were approximately \$75.3 million for the year ended June 30, 2002.
Cause:	Due to staff and time limitations, the Division has been unable to prepare the independent engineer's cost estimate prior to receipt of the fee proposal from the consultant.
Effect:	The Division is in noncompliance with the Code of State Rules and cost estimates prepared by the Division risk being influenced by submitted proposals.
Recommendation:	We recommend that the Division devote the necessary resources to ensure that the Code of State Rules and its policies and procedures are followed and cost estimates are prepared in a timely manner.
Management Response:	<i>As noted in our response to the 2001 audit, West Virginia Division of Highways has undertaken various actions to address this issue. The Division feels that the actions taken this past year will ensure that future cost estimates will be prepared in a timely manner.</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
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YEAR ENDED JUNE 30, 2002

2002-4	Procurement of Architectural and Engineering Services
Criteria:	Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: "The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities." Further, Section 157-1-7.3bb of the Code of State Rules requires the selection committee for the procurement of architectural and engineering services to consist of the Secretary of Transportation, the Commissioner of Highways, the State Highway Engineer and the next lower level of management below the State Highway Engineer under whose direction the work will be performed.
Condition:	We noted the following during our review of documentation related to the procurement of architectural and engineering services: <ul style="list-style-type: none">• The Consulting Services Section of the Engineering Division did not have a Consultant Confidential Qualification Questionnaire on file for one of the projects tested. (Also noted in prior year)• The Consulting Services Section of the Engineering Division did not have a Consultant Cost Accounting Information Statement on file for one of the projects selected for review.• For several of the projects reviewed, the reasons for why a vendor was selected and the interviews of consultants were not documented. (Also noted in prior year)
Context:	Total expenditures for architectural and engineering services were \$75.3 million for the year ended June 30, 2002.
Cause:	The Division was unable to locate some of the documentation and policies and procedures of the Division do not clearly specify the documentation which should be maintained.
Effect:	The Division was unable to provide supporting documentation related to compliance with the West Virginia State Code.
Recommendation:	We recommend that the Division strengthen their policies and procedures regarding required documentation for the procurement of architectural and engineering services.
Management Response:	<i>As noted in our response to the 2001 audit, West Virginia Division of Highways has undertaken various actions to address this issue. The Division feels that the actions taken this past year will ensure that the required documentation will be maintained in the project files.</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-5	Davis Bacon Compliance
Criteria:	The management of the Division is required to ensure that contractors and subcontractors are paying employees the prevailing wage rates as established by the Department of Labor for the locality at the time of the construction payroll.
Condition:	<p>The Division obtains certified payrolls from the contractors/subcontractors and is required to perform prevailing wage inspections and issue reports on their findings. During our review of this process we noted the following:</p> <ul style="list-style-type: none">• One project had been active for greater than one year and only had three inspections performed, of which the last inspection was performed in August of 2001. Further, the February inspection on one of these projects was not completed until May of 2002. (District 3)• One project that was active for over one year had not been inspected since March of 2001. (District 4)• All contractor payrolls for the items selected were properly submitted; however, neither the Labor Interviews nor the Compliance Inspections were provided. (District 7)
Context:	Total disbursements for construction-related activities were approximately \$453.8 million for the year ended June 30, 2002.
Cause:	Policies and procedures have not been adequately developed to provide district workers with clear and concise direction regarding the frequency and timing of the prevailing wage inspection reports.
Effect:	Documentation of the prevailing wage monitoring was not consistent and the Division may be in non-compliance with the requirements of WV State Code and the Davis Bacon Act.
Recommendation:	We recommend that the Division strengthen their policies and procedures related to the monitoring of prevailing wage and ensure that controls are operating as designed. The policies and procedures at a minimum should include the frequency and time requirements for performing the prevailing wage monitoring. Further, the internal audit group of the Division should consider designing audit procedures for the monitoring and review of the prevailing wage inspection reports.
Management Response:	<p><i>West Virginia Division of Highways agrees with the recommendation. A memorandum from the Deputy State Highway Engineer - Development will be sent to Contract Administration Division and all Districts. The memorandum will provide direction to all Districts regarding the frequency and timing of the prevailing wage/EEO reports.</i></p> <p><i>The procedures compliance section of Transportation Auditing currently performs reviews of compliance with Davis Bacon during the course of their work on specific construction contracts. The Internal Audit section of Transportation Auditing is currently in the process of performing audit procedures in the Contract Administration area. Davis Bacon Compliance is included within the scope of that ongoing audit.</i></p>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
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YEAR ENDED JUNE 30, 2002

2002-6	Evaluation of Consultant's Work
Criteria:	Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: "The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities." Further, Section 157-1-7.10 of the Code of State Rules requires upon completion or performance termination of the consultant's work, the responsible Division will prepare a report recording its evaluation of the consultant's efforts. A copy shall be sent to the consultant for review and comment and any written comments received shall be attached to the final report. All consultants with active contracts shall be evaluated in March of each year on each active project."
Condition:	We noted the following during our review of the Division's evaluation of consultants' work: <ul style="list-style-type: none">• The Consulting Services Section of the Engineering Division did not have timely periodic evaluations of consultant's efforts on file for two projects.• The March annual consultant evaluations could not be located for five of the active projects reviewed.
Context:	Total expenditures for architectural and engineering services were \$75.3 million for the year ended June 30, 2002.
Cause:	The Division indicated that evaluations are performed at the preliminary field review, final field review, and final grade review and that these evaluations may be retained by the project manager in the project files. As of the date of fieldwork, these evaluations had not been provided.
Effect:	The Division was unable to provide supporting documentation related to compliance with the West Virginia State Code.
Recommendation:	We recommend that the Division strengthen their policies and procedures regarding required documentation for the evaluation of consultants.
Management Response:	<i>West Virginia Division of Highways agrees with the recommendation. A memorandum from the Deputy State Highway Engineer - Development will be sent to all Divisions and Districts involved with Consultants. This memorandum will emphasize the need to perform the required evaluations in a timely fashion. Each Division/District will be instructed to take any necessary action to ensure that the required documentation will be contained in the project files as required by Chapter 5A, Article 8, Section 9, of the West Virginia Code.</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
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YEAR ENDED JUNE 30, 2002

2002-7	Level of Subcontract/Subconsulting Work
Criteria:	Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: "The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities." Further, the policies and procedures of the Division require the prime contractor/consultant to perform at least 51% of any contracted service.
Condition:	The Consulting Services Section of the Engineering Division reviews the contractors/consultant's cost proposals for the amount of subcontract/subconsulting work proposed; however, the Division has not established procedures to ensure that the contractor/consultant maintains the required 51%.
Context:	Total expenditures for contracted/consulted work was approximately \$75.3 million for the year ended June 30, 2002.
Cause:	The Division has not established controls to monitor the contractors/consultants compliance with the required 51% rule.
Effect:	The Division could be contracting with a certain contractor/consultant for specific qualifications but a majority of the services could be provided by an under qualified subcontractor/subconsultant without the Division's approval.
Recommendation:	We recommend that the Division develop controls for monitoring the contractor/subcontractor's compliance with the 51% rule.
Management Response:	<i>West Virginia Division of Highways agrees with the recommendation. A memorandum from the Deputy State Highway Engineer - Development will be sent to all Divisions and Districts involved with the Consultants. This memorandum will emphasize the procedures to be followed regarding the monitoring of Consultant's compliance with the 51% rule, as required by Chapter 5A, Article 8, Section 9, of the West Virginia Code.</i>

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-8

Contractor Awarded Projects Documentation

Criteria:

Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: “(b) The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency’s activities. Section 157-3-4.1 of the Code of State Rules requires all Bidders on projects let to contract by the Division shall be prequalified as provided for by rules or regulations, or both, of the commissioner. A Certificate of Qualification will be issued by the commissioner fixing the amount of incomplete work a contractor may have under contract at any one time and the type of work for which the contractor is qualified.

To obtain a Certificate of Qualification, the contractor must file a Contractor’s Prequalification Statement containing the information as required based on the category of work for which prequalification is being requested.”

Further, the 1980 Division of Highways Construction Manual Addendum #120 “Finalization Procedures”, page 6, step 7, requires the following authorized documentation: “(g) To Date Quantity Validation Report signed by the Project/Resurfacing Section and District Finals Section reviewers.” In addition, Section 157-3-5.6 of the Code of State Rules requires: “the contractor shall be required, in addition to any other form of insurance or bonds required under the terms of the contract and specifications, to procure and maintain during the life of the contract the following types of insurance in the amounts set forth.”

Condition:

The Department requires contractors to submit Prequalification Statements 15 days prior to the bid “letting” date. These statements serve to qualify a contractor for the type of work the contractor may be awarded and fixes the amount of incomplete work a contractor may have under contract at any one time. We noted that one contractor award did not submit a Prequalification Statement.

The “To Date Quantity Validation Reports” are used in the “finalization” process for the contractors final payment and show the amount of material approved and used for the project. We noted two instances in which there were no authorizing signatures at the project level on the “To Date Quantity Validation Reports.”

In addition, we noted one instance in which the Division did not have an insurance certificate for a contractor on a specific project

Context:

Total expenditures for construction related activities were approximately \$453.8 million for the year ended June 30, 2002. The period for which there was no liability insurance certificate was from February 12, 2001 through the completion of the project on October 3, 2001.

Cause:

The Division indicated that the prequalification statements had been discarded and that they were unsure of why the “To Date Quantity Validation Reports” were not authorized and why the insurance certificate could not be located.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,
DIVISION OF HIGHWAYS
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2002

2002-8

Contractor Awarded Projects Documentation (Continued)

Effect:

Without the Prequalification statement, the Division could not ascertain whether the contractor was qualified for the awarded project.

Without the signatures on the "To Date Quantity Validation Reports," the Division could not determine whether the quantity amounts on this report were checked/correct at the project level; this is one step of the "finalization" procedures that must take place in order to process the final payment to the contractor.

Without an insurance certificate, the Division could not satisfy itself as to the contractor being insured for the various liability coverages defined in Section 157-3-5.6 of the West Virginia Code.

Recommendation:

We recommend that the Division strengthen their policies and procedures over the retention of significant documents on contractor awarded projects.

Management Response:

West Virginia Division of Highways agrees with the recommendation. A memorandum from the Deputy State Highway Engineer - Development will be sent to all Divisions and Districts involved with Contractors. This memorandum will emphasize that all documentation related to the award of construction contracts must be placed in the project files. Each Division/District will be instructed to take any necessary action to ensure that project files are maintained and contain all documentation required by Chapter 5A, Article 8, Section 9.