

CITY OF VIRGINIA BEACH

DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, VA

Financial Statements

June 30, 2005 and 2004

(With Independent Auditors' Report Thereon)

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

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CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia
Commissioners

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Independent Auditors' Report

The Commissioners
City of Virginia Beach Development Authority

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the City of Virginia Beach Development Authority (the "Authority"), a component unit of the City of Virginia Beach, Virginia, as of and for the years ended June 30, 2005 and 2004, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express opinions on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, and each major fund of the Authority as of June 30, 2005 and 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 19, 2005 on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis on pages 3 through 11 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 this information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Authority's basic financial statements. The information listed as supplementary information in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Virginia Beach, Virginia
August 19, 2005

Cherry. Sakant : *Hallbank, LLP*

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Management's Discussion and Analysis

This section of the City of Virginia Beach Development Authority's (the Authority) annual financial report represents our discussion and analysis of the Authority's financial performance during the fiscal years ended June 30, 2005 and 2004. Please read it in conjunction with the Authority's financial statements and accompanying notes.

FINANCIAL HIGHLIGHTS

- The Authority's governmental net assets decreased by \$12.94 million in fiscal year 2005 and the net results from governmental activities decreased by \$13.24 million from fiscal year 2004. The decreases in net assets and net results from activities are mainly due to the completion and transfer of the 31st Street Project and part of the Town Center Project. The governmental activities revenue increased by \$18.02 million due to increased funding received from the City of Virginia Beach to support the construction of infrastructure in Town Center and the 31st Street Project.
- The Authority's business-type net assets increased by \$5.04 million in fiscal year 2005 and the net results from activities increased by \$5.14 million from fiscal year 2004. The increases in net assets and net results from activities are primarily due to additional non-operating revenue received from the City of Virginia Beach for a portion of the 31st Street Project and the transfer of the Town Center Plaza from the Special Projects Fund. The business-type activities program revenue decreased by \$2.80 million resulting from a decrease in land sales.
- The Authority provided economic development services, as requested by the Virginia Beach City Council, for the 31st Street Project and the Town Center Infrastructure Project that are accounted for in the Authority's Governmental Fund. When projects are complete, the associated costs are capitalized and transferred out of the Governmental Fund. During fiscal year 2005, \$7.5 million of Town Center Infrastructure expenses pertaining to Phase I and II and \$30.25 million of 31st Street Project expenses were removed from the Governmental Fund. The Town Center Plaza and the Authority's portion of the 31st Street Project are now recorded in the Authority's Propriety Fund.
- During fiscal year 2005, the Authority reported two land sales totaling \$0.81 million. The sales, totaling 8.504 acres, included two parcels in Corporate Landing Business Park. These transactions are accounted for in the Authority's Proprietary Fund.
- In May 2005, the Authority acted as the conduit issuer for \$94,900,000 in Series 2005A Public Facility Revenue Bonds and \$9,000,000 in Series 2005B Public Facility Revenue Bonds, at the request of the City of Virginia Beach. The portion attributable to the Authority, \$26.05 million, was used to finance the 9th Street Garage (\$9.22 million) and part of the 31st Street Project (\$12.91 million). The remainder of the bonds will be used to finance part of the Block 10 parking facility located in Town Center (\$3.92 million). A premium on the bonds in the amount of \$.54 million was also used to finance the 9th Street Garage and a premium of \$.17 million will be used to finance part of the Block 10 parking facility.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Management's Discussion and Analysis

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial section of this annual report consists of three parts: management's discussion and analysis (this section), the basic financial statements and the notes to the financial statements, and other supplemental information.

In the past, the primary focus for local government financial statements has been summarized by fund type information on a current financial resource basis. This approach has been modified and the Authority financial statements now present two types of statements, each with a different snapshot of the Authority's finances. The new focus is on both the Authority as a whole (entity-wide) as well as on the individual funds. The entity-wide financial statements provide both long-term and short-term information about the Authority's overall financial status. The fund financial statements, which have been provided in the past, focus on the individual parts of the Authority, reporting the Authority's operations in more detail than the entity-wide statements. Both perspectives (entity-wide and fund) allow the user to address relevant questions, broaden the basis for comparison (year to year or entity to entity) and enhance the Authority's accountability.

ENTITY-WIDE FINANCIAL STATEMENTS

The entity-wide financial statements report information about the Authority as a whole using accounting methods similar to those used by private-sector companies. The focus of the Statement of Net Assets (the "Unrestricted Net Assets") is to report the entity's net assets and how they have changed. Net assets – the difference between assets and liabilities – is one way to measure the Authority's financial health, or financial position. Over time, increases or decreases in an entity's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.

The Statement of Activities is focused on both the gross and net cost of various functions (governmental and business-type), which are supported by program revenues. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid. This statement summarizes and simplifies the user's analysis of the cost of governmental activities and/or subsidy to business-type activities.

In the Statement of Net Assets and the Statement of Activities, the Authority is divided into the following:

Governmental activities – The Authority's special projects are reported here. These activities consist of various economic development projects as requested by the Council of the City of Virginia Beach.

Business-type activities – The Authority's basic operations are reported here as the Authority charges a fee to customers to help cover the cost of certain services it provides.

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Management's Discussion and Analysis

FUND FINANCIAL STATEMENTS

The fund financial statements provide more detailed information about the Authority's significant funds – not the Authority as a whole. Funds are accounting devices that the Authority uses to keep track of specific sources of funding and spending for particular purposes.

The Authority has two types of funds:

Governmental fund – The Special Projects Fund is used to account for the financial resources for the acquisition or construction of ongoing construction projects conducted on behalf of the City of Virginia Beach (the City).

Proprietary fund – The Authority Operations Fund accounts for the activities of the Authority which charges fees for Industrial Revenue Bonds, acquires, develops and resells land, and administers the Economic Development Investment Program (EDIP).

FINANCIAL ANALYSIS OF THE AUTHORITY AS A WHOLE

Net Assets:

The following table reflects the condensed Net Assets of the Authority:

as of June 30, 2005, 2004, and 2003
(in millions)

	Governmental Activities			Business - type Activities			Total		
	2005	2004	2003	2005	2004	2003	2005	2004	2003
Current and other assets	\$ 0.54	0.34	2.36	35.21	41.25	28.36	35.75	41.59	30.72
Capital assets	0.03	12.97	12.68	73.39	36.24	41.05	73.42	49.21	53.73
Total Assets	0.57	13.31	15.04	108.60	77.49	69.41	109.17	90.80	84.45
Current and other liabilities	0.50	0.30	2.33	9.44	6.74	9.00	9.94	7.04	11.33
Long-term liabilities	-	-	-	75.67	52.30	41.86	75.67	52.30	41.86
Total liabilities	0.50	0.30	2.33	85.11	59.04	50.86	85.61	59.34	53.19
Net assets:									
Invested in capital assets, net of related debt	-	-	-	9.97	0.11	1.12	9.97	0.11	1.12
Restricted - other purposes	0.03	12.97	12.67	2.55	1.80	1.24	2.58	14.77	13.91
Unrestricted	0.04	0.04	0.04	10.97	16.54	16.19	11.01	16.58	16.23
Total net assets	\$ 0.07	13.01	12.71	23.49	18.45	18.55	23.56	31.46	31.26

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
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Management's Discussion and Analysis

At June 30, 2005 and 2004, the total assets of the Authority were \$109.17 and \$90.80 million, respectively; total liabilities were \$85.61 and \$59.34 million, respectively, while combined net assets were \$23.56 and \$31.46 million, respectively.

The sale of \$103.9 million in Public Facility Revenue Bonds in May 2005 included \$26.05 million of debt to finance part of the Block 10 public parking facility located in Town Center, part of the 31st Street Project, and the 9th Street Garage, which resulted in an increase in current and other assets, in the form of receivables, capital assets and land, as well as an increase in long-term liabilities in the Authority's financial statements.

Construction in progress grew by \$24.8 million in fiscal year 2005 and \$6.8 million in fiscal year 2004 as a result of costs associated with Town Center Development and the 31st Street Project. A transfer of infrastructure assets totaling \$37.75 million offset the increase in 2005.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
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Management's Discussion and Analysis

Changes in Net Assets:

The following chart shows the revenue and expenses for the current fiscal year:

Table 2
Changes in Net Assets
as of June 30, 2005, 2004, and 2003
(in millions)

	<u>Governmental Activities</u>			<u>Business - type Activities</u>			<u>Total</u>		
	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
Revenue									
Program Revenue:									
Charges for services	\$ -	-	-	2.93	6.87	1.92	2.93	6.87	1.92
Operating grants and contributions	-	-	-	3.51	2.37	0.97	3.51	2.37	0.97
Capital grants and contributions	24.81	6.79	2.68	0.05	0.05	0.05	24.86	6.84	2.73
General Revenue:									
Other	-	-	0.03	0.08	0.03	0.26	0.08	0.03	0.29
Special Items:									
Transfer of assets	-	-	-	1.77	0.03	-	1.77	0.03	-
Contribution from Primary Government	-	-	-	2.57	-	2.50	2.57	-	2.50
Cancellation of interest	-	-	-	-	-	1.23	-	-	1.23
Total revenues	<u>24.81</u>	<u>6.79</u>	<u>2.71</u>	<u>10.91</u>	<u>9.35</u>	<u>6.93</u>	<u>35.72</u>	<u>16.14</u>	<u>9.64</u>
Expenses									
Development Activities	-	-	0.02	-	-	-	-	-	0.02
Authority Operations	-	-	-	5.87	9.45	3.33	5.87	9.45	3.33
Special Items:									
Transfer of infrastructure to City	35.98	6.46	-	-	-	-	35.98	6.46	-
Transfer of assets to Proprietary Fund	1.77	0.03	-	-	-	-	1.77	0.03	-
Total expenses	<u>37.75</u>	<u>6.49</u>	<u>0.02</u>	<u>5.87</u>	<u>9.45</u>	<u>3.33</u>	<u>43.62</u>	<u>15.94</u>	<u>3.35</u>
Change in net assets	\$ (12.94)	0.30	2.69	5.04	(0.10)	3.60	(7.90)	0.20	6.29
Net Assets - Beginning of Year	13.01	12.71	10.02	18.45	18.55	14.95	31.46	31.26	24.97
Net Assets - End of Year	<u>0.07</u>	<u>13.01</u>	<u>12.71</u>	<u>23.49</u>	<u>18.45</u>	<u>18.55</u>	<u>23.56</u>	<u>31.46</u>	<u>31.26</u>

REVENUES

Revenues attributable to governmental activities were in the form of contributions, for economic development projects, from the City of Virginia Beach and investment earnings. For the fiscal years ended June 30, 2005 and 2004, revenues from business-type activities totaled \$10.91 and \$9.35 million, respectively. This included revenue derived from land sales, industrial revenue bond fees, lease income, investment earnings, and support agreement funding from the City of Virginia Beach.

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Management's Discussion and Analysis

EXPENSES

For the fiscal years ended June 30, 2005 and 2004, expenses totaling \$37.75 and \$6.49 million, respectively, were transferred to the City of Virginia Beach and the Authority's Proprietary Fund. These development expenses were related to Town Center infrastructure and the 31st Street Project.

The expenses of the business-type activities included cost of land sold, depreciation/amortization, selling and administrative expenses, and interest on outstanding debt obligations. For the fiscal years ended June 30, 2005 and 2004, these expenses totaled \$5.87 and \$9.45 million, respectively.

FINANCIAL ANALYSIS OF THE AUTHORITY'S FUNDS

The Authority's governmental fund reflects a fund balance of \$43,796 and \$39,329, respectively. The June 30, 2005 and 2004 increases in fund balance of \$4,467 and \$4,340, respectively are primarily the result of interest income associated with a security deposit held on the TPC Golf Course. The activities reflect support from the City of Virginia Beach as well as expenditures on the 31st Street Project and Town Center infrastructure totaling \$24.8 million in fiscal year 2005.

The proprietary fund includes total net assets of \$23.49 and \$18.45 million at June 30, 2005 and 2004, respectively. The June 30, 2005 increase in net assets is attributable to an increase in non-operating revenue from the City of Virginia Beach and the transfer of the Town Center Plaza from the Special Projects Fund. In 2004, the decrease in net assets is attributable to an increase in cost of land sold. In 2005 and 2004, operating revenues from land sales, industrial revenue bond fees, lease income, and miscellaneous revenue totaled \$2.9 and \$6.9 million, respectively, while operating expenses for cost of land and selling and administrative expenses totaled \$3.0 and \$7.0 million, respectively.

CAPITAL ASSETS AND DEBT ADMINISTRATION

CAPITAL ASSETS

As of June 30, 2005 and 2004, the Authority had invested \$73.42 and \$49.21 million (see note 6), respectively, in various capital assets and infrastructure as reflected in the schedule. In 2005, this represents a net increase of \$24.21 million, while 2004 reflects a net decrease of \$4.22 million from the beginning of the fiscal year.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Management's Discussion and Analysis

Table 3
Capital Assets
(in millions)

	Governmental Activities			Business - type Activities			Total		
	2005	2004	2003	2005	2004	2003	2005	2004	2003
Non-depreciable assets:									
Land	\$ -	-	-	14.24	5.38	5.38	14.24	5.38	5.38
Option land and capitalized interest	-	-	-	2.18	3.10	7.10	2.18	3.10	7.10
Construction in progress	0.03	12.98	12.68	-	-	-	0.03	12.98	12.68
Other capital assets:									
Buildings	-	-	-	60.23	29.99	29.63	60.23	29.99	29.63
Accumulated depreciation on other capital assets	-	-	-	(3.26)	(2.24)	(1.36)	(3.26)	(2.24)	(1.36)
Total net capital assets	\$ 0.03	12.98	12.68	73.39	36.23	40.75	73.42	49.21	53.43

Major capital asset additions in fiscal year 2005 included:

- Town Center Project – Phase II infrastructure construction including streets, curbs and gutters, sidewalks, and underground utilities; and construction of a public plaza - \$2,596,118
- Town Center Block 12 – The purchase of part of the Block 12 Parking Garage located in Town Center on July 19, 2004 - \$4,465,983
- Town Center Block 12 Retail Space – The purchase of the Block 12 retail space located in Town Center on October 29, 2004 - \$1,558,179
- 9th Street Garage – The purchase of the 9th Street garage on March 31, 2005 - \$9,750,000
- 31st Street Project – Capital asset addition reflected in the Authority's business-type activities - \$20,357,500

Major capital asset disposals included:

- 31st Street Project – Expenses associated with the acquisition of property for and construction of a public parking facility. The project is a public/private investment involving the City of Virginia Beach, the Development Authority, and a private investor. The City-owned portion of the \$33.1 million asset was removed from the Authority's financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Management's Discussion and Analysis

LONG-TERM DEBT

At June 30, 2005, the Authority had an outstanding loan balance due to the City of Virginia Beach in the amount of \$5.836 million. During fiscal year 2005, twenty percent of the net proceeds from land sales within Corporate Landing (\$158,739) were distributed to the City to reduce the outstanding debt balance.

In May 2005, the Authority acted as the conduit issuer for \$94,900,000 in Series 2005A Public Facility Revenue Bonds and \$9,000,000 in Series 2005B Taxable Public Facility Revenue Bonds, at the request of the City of Virginia Beach. The Series 2005A bonds will mature incrementally between 2006 and 2025 and the Series 2005B will mature incrementally between 2006 and 2016. These bonds have financed or will finance various public facilities, including: the replacement of the Pavilion Theater and the Convention Center, construction of a parking facility for the Virginia Aquarium and Marine Science Center, Open Space site acquisition, construction of an Emergency Communications Operations Center, construction of the 31st Street Parking Garage, acquisition of Town Center's Block 10 garage and the 9th Street Garage, and various City equipment and software. The bonds are a limited obligation of the Authority, payable solely from payments made by the City of Virginia Beach, pursuant to a Support Agreement between the City and the Authority. The portion attributable to the Town Center Block 10 garage (\$3,920,000), the 9th Street Parking Garage (\$9,215,000), and part of the 31st Street Project (\$12,915,000) is presented in the Authority's business-type activity statements, since that portion of the bond issue is for Authority owned assets. The remainder of the bond issue is for City owned assets and thus, not reflected in the Authority's financial statements. The Series 2005A Bonds' interest rates range from 4.0% to 5.0% and the Series 2005B Bonds' interest rates range from 4.75% to 5.0%. For additional analysis related to long-term debt activities of the Authority, see note 8.

ECONOMIC FACTORS

In fiscal year 2005, the Authority located new business and retained and expanded existing industry, continued construction of the Town Center of Virginia Beach, leveraged the City's Economic Development Investment Program Fund and authorized Industrial Development Revenue Bond activity.

During fiscal year 2005, the VBDA and the Department of Economic Development assisted in the location of 52 new companies and the expansion and retention of 42 existing businesses that created new capital investment in excess of \$303 million. These companies and businesses created and retained over 3,500 employment opportunities in Virginia Beach. The VBDA authorized issuance of \$14,210,000 in industrial revenue bond funds and provided EDIP assistance in the amount of \$511,000 during fiscal year 2005.

The VBDA's primary business parks had a considerable amount of the activity in fiscal year 2005. Within these major business/industrial parks, 28 new businesses located and 24 existing Virginia Beach companies expanded or retained their operations.

Development in Town Center continued in both Phases I and II, and Phase III was announced. In fiscal year 2005, Phase I construction included the 21-story, 254,000 square-foot, Class "A" Town Center office tower, 93,000 square feet of additional office and retail space, the 176-room Hilton Garden Inn Hotel, the Towne Bank Building, and a 1,284-space structured parking garage. Phase II included the 90,000 square-foot Dick's Sporting Goods retail location, the 341-unit

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Management's Discussion and Analysis

luxury apartment building ("The Cosmopolitan"), 232,500 square feet of retail and office space, and two structured parking garages with a total of 1,430 parking spaces.

Phase III will include a new, 38-story, 240-room, Westin Hotel and 119 luxury condominiums, 35,000 square feet of retail space, and a structured parking garage with 957 parking spaces. Phase III also includes the construction of an exquisite 84,000 square-foot, 1,200-seat, Performing Arts Center. Completion of Phase III is scheduled for Summer, 2007.

The Virginia Beach Development Authority held its annual workshop on January 10, 2005. The VBDA focused its energy on advancing the Economic Development Strategy, and examined the following topics: redevelopment / land, transportation, incentives, and trends in the workforce.

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide users (citizens, taxpayers, customers, clients, investors and creditors) with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the funds it receives. Questions concerning this report or requests for additional information should be directed to Director of Economic Development, Virginia Beach Development Authority, 222 Central Park Avenue, Suite 1000, Virginia Beach, VA 23462, telephone (757) 437-6464, or visit the Authority's website at vbgov.com/dept/econdev.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Statements of Net Assets - Entity-Wide

June 30, 2005 and 2004

	2005			2004		
	Governmental Activities	Business-type Activities	2005 Total	Governmental Activities	Business-type Activities	2004 Total
Assets						
Cash and cash equivalents (note 2)	—	3,138,604	3,138,604	—	2,484,190	2,484,190
Receivables, net (note 4)	23,332	72,537	95,869	—	86,401	86,401
Internal balances (note 5)	—	—	—	(151,353)	151,353	—
Deferred charges	—	650,414	650,414	—	694,397	694,397
Land inventory	—	13,183,346	13,183,346	—	18,590,029	18,590,029
Restricted cash and cash equivalents (notes 2 and 3)	521,617	4,008,470	4,530,087	238,987	3,295,374	3,534,361
Receivables, restricted (note 4)	—	14,159,326	14,159,326	250,000	15,948,481	16,198,481
Capital assets (note 6)						
Land, improvements, and construction in progress	25,623	16,426,802	16,452,425	12,976,338	8,484,058	21,460,396
Other capital assets, net of accumulated depreciation	—	56,962,427	56,962,427	—	27,752,351	27,752,351
Total capital assets	25,623	73,389,229	73,414,852	12,976,338	36,236,409	49,212,747
Total assets	570,572	108,601,926	109,172,498	13,313,972	77,486,634	90,800,606
Liabilities						
Accounts payable and accrued liabilities (note 7)	100,000	1,082,533	1,182,533	100,000	792,365	892,365
Liabilities payable from restricted assets	401,153	4,908,905	5,310,058	198,305	4,363,325	4,561,630
Long-term liabilities (note 8)						
Due within one year	—	3,448,117	3,448,117	—	1,579,125	1,579,125
Due in more than one year	—	75,671,676	75,671,676	—	52,303,019	52,303,019
Total liabilities	501,153	85,111,231	85,612,384	298,305	59,037,834	59,336,139
Net Assets						
Invested in capital assets, net of related debt	—	9,967,759	9,967,759	—	111,119	111,119
Restricted - other purposes (notes 3 and 13)	25,623	2,549,528	2,575,151	12,976,338	1,800,655	14,776,993
Unrestricted	43,796	10,973,408	11,017,204	39,329	16,537,026	16,576,355
Total net assets	69,419	23,490,695	23,560,114	13,015,667	18,448,800	31,464,467

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Statements of Activities - Entity-Wide
Year ended June 30, 2005

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
	Expenses	Charge for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Governmental activities	\$ —	—	—	24,796,485	24,796,485	—	24,796,485
Development Activities							
Business-type activities							
Authority Operations	5,875,066	2,938,726	3,514,524	50,000	—	628,184	628,184
Total	\$ 5,875,066	2,938,726	3,514,524	24,846,485	24,796,485	628,184	25,424,669
General Revenues:					\$ 4,467	71,482	75,949
Unrestricted investment earnings					—	6,379	6,379
Miscellaneous							
Special Items:					(35,981,205)	—	(35,981,205)
Transfer of infrastructure to Primary Government					—	2,569,855	2,569,855
Contribution from Primary Government					(1,765,995)	1,765,995	—
Transfer of fixed assets to Proprietary Fund					(37,742,733)	4,413,711	(33,329,022)
Total general revenues and special items					(12,946,248)	5,041,895	(7,904,353)
Change in net assets					13,015,667	18,448,800	31,464,467
Net assets - beginning of year					69,419	23,490,695	23,560,114
Net assets - end of year					\$	\$	\$

See accompanying notes to financial statements

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Statements of Activities - Entity-Wide

Year ended June 30, 2004

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
	Expenses	Charge for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Governmental activities	\$ —	—	—	6,792,966	6,792,966	—	6,792,966
Development Activities							
Business-type activities							
Authority Operations	9,450,157	6,866,066	2,375,811	50,000	—	(158,280)	(158,280)
Total	\$ 9,450,157	6,866,066	2,375,811	6,842,966	6,792,966	(158,280)	6,634,686
General Revenues:							
Unrestricted investment earnings					\$ 4,340	26,569	30,909
Miscellaneous					—	1,695	1,695
Special Items:							
Transfer of infrastructure to Primary Government					(6,468,941)	—	(6,468,941)
Transfer of fixed assets to Proprietary Fund					(29,786)	29,786	—
Total general revenues and special items					(6,494,387)	58,050	(6,436,337)
Change in net assets					298,579	(100,230)	198,349
Net assets - beginning of year					12,717,088	18,549,030	31,266,118
Net assets - end of year					\$ 13,015,667	18,448,800	31,464,467

See accompanying notes to financial statements

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Balance Sheets - Governmental Fund

Special Projects

June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Assets		
Restricted cash and cash equivalents (notes 2 and 3)	\$ 521,617	238,987
Receivables, intergovernment (note 4)	<u>23,332</u>	<u>250,000</u>
Total assets	\$ <u><u>544,949</u></u>	<u><u>488,987</u></u>
 Liabilities and Fund Balance		
Liabilities (note 7)		
Due to Operating Fund	\$ —	151,353
Accrued liabilities	100,000	100,000
Liabilities payable from restricted assets	<u>401,153</u>	<u>198,305</u>
Total liabilities	<u>501,153</u>	<u>449,658</u>
Fund balance		
Unreserved	<u>43,796</u>	<u>39,329</u>
Total liabilities and fund balance	\$ <u><u>544,949</u></u>	<u><u>488,987</u></u>
 Reconciliation to Statement of Net Assets:		
Ending fund balance	\$ <u>43,796</u>	<u>39,329</u>
Adjustments for the Statement of Net Assets:		
Capital assets used in government activities are not current financial resources and therefore not reported in the governmental fund	<u>25,623</u>	<u>12,976,338</u>
Net Assets of Governmental Activities	\$ <u><u>69,419</u></u>	<u><u>13,015,667</u></u>

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Statements of Revenues, Expenditures, and Changes in Fund Balance - Governmental Fund

Special Projects

Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Revenues		
City Contributions:		
Town Center Infrastructure	\$ 2,594,968	4,794,034
31st Street Project	22,201,517	1,998,932
Interest	<u>4,467</u>	<u>4,340</u>
Total revenues	<u>24,800,952</u>	<u>6,797,306</u>
Expenditures		
Construction:		
31st Street Project	22,201,517	1,998,932
Town Center Infrastructure	<u>2,594,968</u>	<u>4,794,034</u>
Total Expenditures	<u>24,796,485</u>	<u>6,792,966</u>
Excess of revenues over expenditures	4,467	4,340
Fund balance at beginning of year	<u>39,329</u>	<u>34,989</u>
Fund balance at end of year	<u>\$ 43,796</u>	<u>39,329</u>
Reconciliation to Statement of Activities		
Excess of revenues over expenditures	\$ <u>4,467</u>	<u>4,340</u>
Adjustment for the Statement of Activities:		
Transfer of infrastructure to Primary Government	(35,981,205)	(6,468,941)
Transfer of capital assets to Proprietary Fund	(1,765,995)	(29,786)
Governmental funds report capital outlays as expenditures while governmental activities capitalize such costs	<u>24,796,485</u>	<u>6,792,966</u>
Changes in net assets of governmental activities	<u>\$ (12,946,248)</u>	<u>298,579</u>

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Statements of Net Assets - Proprietary Fund

Authority Operations

June 30, 2005 and 2004

	2005	2004
Assets		
Current assets:		
Cash and cash equivalents (note 2)	\$ 3,138,604	2,484,190
Receivables, net (note 4)	72,537	86,401
Internal balances	—	151,353
Total current assets	3,211,141	2,721,944
Noncurrent assets:		
Restricted cash and cash equivalents (notes 2 and 3)	4,008,470	3,295,374
Receivables, restricted (note 4)	14,159,326	15,948,481
Deferred charges (note 1)	650,414	694,397
Land inventory	13,183,346	18,590,029
Capital Assets (note 6)		
Land	16,426,802	8,484,058
Buildings and equipment	60,223,637	29,992,164
Less accumulated depreciation	(3,261,210)	(2,239,813)
Total noncurrent assets	105,390,785	74,764,690
Total assets	108,601,926	77,486,634
Liabilities		
Current liabilities:		
Accounts payable (note 7)	158,281	103,222
Accrued liabilities (note 7)	924,252	689,143
Bonds, notes, and loans payable (note 8)	3,448,117	1,579,125
Total current liabilities	4,530,650	2,371,490
Noncurrent liabilities:		
Liabilities payable from restricted assets	4,908,905	4,363,325
Bonds, notes and loans payable (note 8)	75,671,676	52,303,019
Total liabilities	85,111,231	59,037,834
Net Assets		
Invested in capital assets, net of related debt	9,967,759	111,119
Restricted - other purposes (note 3)	2,549,528	1,800,655
Unrestricted	10,973,408	16,537,026
Total net assets	\$ 23,490,695	18,448,800

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia
Statements of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Fund
Authority Operations
Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Operating Revenues:		
Land sales - Town Center	\$ —	4,097,030
Land sales - other corporate parks	814,720	994,100
Industrial revenue bond fees (note 10)	633,836	472,358
Lease income (notes 9 and 12)	1,490,170	1,302,578
Miscellaneous income	6,379	1,695
Total operating revenues	<u>2,945,105</u>	<u>6,867,761</u>
Operating Expenses:		
Cost of land sold - Town Center	—	4,097,030
Cost of land sold - other corporate parks	534,038	763,969
Selling, general, and other expenses (schedule A)	1,974,013	1,858,486
Garage operations	501,261	270,083
Total operating expenses	<u>3,009,312</u>	<u>6,989,568</u>
Operating income (loss)	<u>(64,207)</u>	<u>(121,807)</u>
Nonoperating Revenue (Expense):		
City of Virginia Beach (schedule E)	5,634,379	2,425,811
Interest income	71,482	26,569
Pass through grant - Governor's Opportunity Fund award	500,000	—
Disbursement of award proceeds	(500,000)	—
Interest expense (note 11)	(2,342,080)	(2,004,395)
31st Street Project marketing	(23,674)	(456,194)
Total nonoperating revenue (expense)	<u>3,340,107</u>	<u>(8,209)</u>
Income (expense) before capital contributions	3,275,900	(130,016)
Town Center Garage	—	29,786
Town Center Plaza	1,765,995	—
Change in net assets	<u>5,041,895</u>	<u>(100,230)</u>
Total net assets at beginning of year	18,448,800	18,549,030
Total net assets at end of year	<u>\$ 23,490,695</u>	<u>18,448,800</u>

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Statements of Cash Flows - Proprietary Fund

Authority Operations

Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Receipts from customers and users	\$ 3,142,831	7,416,295
EDIP cash receipts	2,092,738	4,263,644
Other operating cash receipts	176,353	15,000
Cash payments to suppliers of goods and services	(1,371,835)	(95,688)
Net EDIP activities	(1,862,250)	(4,844,318)
Other operating cash payments	-	(6,043,438)
Net cash provided (used) by operating activities	<u>2,177,837</u>	<u>711,495</u>
Cash flows from capital and related financing activities:		
Principal Repayment on Long-Term Debt	(1,583,652)	(1,482,463)
Interest Paid on Long-Term Debt	(2,157,588)	(2,055,575)
Capital contributions from City	3,049,059	2,480,168
Acquisition of Capital Assets	(165,625)	-
Sale of Town Center Land	-	983,417
Governor's Opportunity Fund Award	500,000	-
Governor's Opportunity Fund Award	(500,000)	-
31st Street Project	(23,674)	(456,194)
Net cash used by capital and related financing activities	<u>(881,480)</u>	<u>(530,647)</u>
Cash flows from investing activities:		
Interest	71,153	26,578
Net increase (decrease) in cash and cash equivalents	1,367,510	207,426
Cash and cash equivalents at beginning of year	5,779,564	5,572,138
Cash and cash equivalents at end of year	<u>\$ 7,147,074</u>	<u>\$ 5,779,564</u>
Classified as:		
Current assets	\$ 3,138,604	2,484,190
Restricted assets	4,008,470	3,295,374
	<u>\$ 7,147,074</u>	<u>\$ 5,779,564</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income (loss)	\$ (64,207)	(121,807)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization expense	1,065,380	916,130
Changes in assets and liabilities		
Receivables, net	2,441,817	4,227,244
Accounts and other payables	(1,824,191)	(4,910,006)
Accrued expenses	25,000	15,000
Land inventory	534,038	584,934
Net cash provided (used) by operating activities	<u>\$ 2,177,837</u>	<u>711,495</u>
Noncash transactions:		
Public facility revenue bond proceeds receivable from City	\$ 4,087,983	11,800,000
Receivables resulting from deferred land sales	-	851,061
Decrease in Town Center notes payable related to land sales	-	(2,258,430)
Amortization on bond discount/premium	(21,147)	(15,290)
Acquisition of 9th Street Garage with City bond proceeds	(9,750,000)	-
Acquisition of 31st Street Garage with City bond proceeds	(12,915,000)	-
Acquisition of Town Center Land with City bond proceeds	(6,024,162)	-

See accompanying notes to financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

(1) Summary of Significant Accounting Policies

Narrative Profile

The City of Virginia Beach (the City) Development Authority (the Authority) was established by an act of the Virginia General Assembly in 1964 to facilitate expansion of the City's tax base through increased business investment and to create employment opportunities within the City. A commission composed of eleven commissioners appointed by the Virginia Beach City Council governs the Authority.

The Authority is considered a component unit of the City for reporting purposes and, as such, will be a discretely presented component unit in the Comprehensive Annual Financial Report of the City of Virginia Beach. Future funding and ongoing cash flows of the Authority are dependent on the City.

In evaluating how to define the Authority, for financial reporting purposes, management has determined that there are no entities over which the Authority exercises significant influence. Significant influence or accountability is based primarily on operational or financial relationships with the Authority. Since the Authority does not exercise significant influence or accountability over other entities, it has no component units.

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America, as specified by the Governmental Accounting Standards Board (GASB). The more significant of the Authority's accounting policies are described below.

The Authority assists in the business/industry location and retention process by acquiring, developing and reselling land, issuing Industrial Revenue Bonds, and administering the Economic Development Investment Program (EDIP). Beginning in 1995, the Authority's mission was expanded to include facilitating economic development projects for the City in order to contribute to the City's economic growth and financial health. This facilitation has been in the structuring of public-private partnerships between the City and private entities.

(a) Basis of Financial Reporting

In June 1999, the GASB issued statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. This statement known as the "Reporting Model," affects the way the Authority prepares and presents financial information.

GASB Statement No. 34 established new requirements and a new reporting model for the annual financial reports of state and local governments. The Statement was developed to make annual reports easier to understand and more useful to the people who use governmental financial information to make decisions and includes:

Management's Discussion and Analysis – GASB Statement No. 34 requires that financial statements be accompanied by a narrative introduction and analytical overview of the government's financial activities in the form of "management's discussion and analysis" (MD&A). This analysis is similar to analysis the private sector provides in their annual reports.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

Entity-Wide Financial Statements – The reporting model includes financial statements prepared using full accrual accounting for all of the government’s activities. This approach includes not just current assets and liabilities (such as cash and accounts payable) but also capital assets and long-term liabilities (such as buildings and infrastructure, including bridges and roads, and general obligation debt). Accrual accounting also reports all of the revenues and costs of providing services each year, not just those received or paid in the current year or soon thereafter.

Statement of Net Assets – The Statement of Net Assets is designed to display the financial position of the Authority (government and business-type activities). Governments report all capital assets, including infrastructure, in the government-wide statement of net assets and report depreciation expense – the cost of “using up” capital assets – in the statement of activities. The net assets of a government will be broken down into three categories: 1) invested in capital assets, net of related debt; 2) restricted; and 3) unrestricted.

Statement of Activities – The government-wide Statement of Activities reports expenses and revenues in a format that focuses on the cost of each of the government’s functions. The expense of individual functions is compared to the revenues generated directly by the function (for instance, through user charges or intergovernmental grants).

(b) *Entity-Wide and Fund Financial Statements*

The basic financial statements include both entity-wide (based upon the Authority as a whole) and fund financial statements. While the previous model emphasized fund types (the total of all funds of a particular type), in the new reporting model the focus is on either the Authority as a whole or major individual funds (within the fund financial statements). Both the entity-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type. In the entity-wide statement of net assets, both the governmental and business-type activities columns are reflected on a full accrual, and economic resources basis, which incorporates long-term assets and receivables as well as long-term debt and obligations. As a general rule, the effect of interfund activity has been eliminated from the entity-wide financial statements. The restricted cash and cash equivalents is used for specific purposes and capital projects. When both restricted and unrestricted resources are available for use, it is the Authority’s policy to use restricted resources first, then unrestricted resources as they are needed.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. The program revenues must be directly associated with the function or a business-type activity. Program revenues include: 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment; and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. The Authority does not allocate indirect expenses.

(c) *Basis of Accounting*

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet in the fund statements. Long-term assets and long-term liabilities are included in

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

the entity-wide statements. Operating statements of the governmental funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

The entity-wide Statement of Net Assets, Statement of Activities, and Proprietary Fund are accounted for on a flow of economic resources measurement focus. With the measurement focus, all assets and all liabilities associated with the operation of these activities are included on the statement of net assets. Proprietary fund-type operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

The statement of net assets, statement of activities, and financial statements of the Proprietary Fund are presented on the accrual basis of accounting. Under this method of accounting, revenues are recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash. Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Authority Operations fund include the sale of land within Authority corporate parks, administrative fees for the issuance of Industrial Revenue Bonds, and lease income. Operating expenses include the cost of land sold, selling and administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. When both restricted and unrestricted assets are available for use, it is the Authority's policy to apply restricted assets first, then unrestricted assets as needed.

The fund financial statements of the Special Projects Fund are maintained and reported on the modified accrual basis of accounting using the current financial resources measurement focus. Under this method of accounting, revenues are recognized in the period in which they become 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 Authority considers the revenues to be available if they are collected within 45 days of year-end. Expenditures, other than accrued interest on long-term debt, are recorded when the fund liability is incurred.

The Authority reports the following major governmental fund:

The **Special Projects Fund** is used to account for the financial resources for the acquisition or construction of ongoing economic development projects conducted on behalf of the City.

The Authority reports the following major proprietary fund:

The **Authority Operations Fund** accounts for the activities of the Authority which charges fees for Industrial Revenue Bonds, acquires, develops, and resells land, and administers the EDIP.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting* (Statement No. 20), the Authority Operations fund follows all applicable GASB pronouncements as well as all Financial Accounting Standards Board (FASB) pronouncements and predecessor APB Opinions and Accounting Research Bulletins (ARB) issued on or before November 30, 1989. Under paragraph 7 of

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

GASB Statement No. 20, the Authority has elected not to apply FASB pronouncements issued after November 30, 1989.

(d) Capital Assets

All capital assets are stated at cost. Capital assets are defined as assets with initial, individual costs exceeding a \$5,000 threshold. Depreciation is computed on the straight-line method over the following estimated useful lives:

Buildings	40 years
Improvements	5-10 years
Equipment	5-10 years

A full month's depreciation is taken in the month an asset is placed in service unless otherwise stated. The 31st Street Garage was placed into service on June 30, 2005. The fiscal year 2005 depreciation on this asset will be recorded in the subsequent year. When property and equipment are disposed, depreciation is removed from the respective accounts, and the resulting gain or loss is recorded in operations.

Interest costs incurred on the note payable to Wachovia Bank for the acquisition of assets are capitalized. The loan and interest charges associated with the asset are secured by a security agreement provided by a developer, which requires the developer to purchase the asset no later than December 2006.

(e) Land Inventory

Land is stated at acquisition cost plus improvements and capitalized interest, if applicable, but not in excess of net realizable value. Capitalized costs of projects are assigned to individual components of the projects based on specific identification. If specific identification is not practicable, capitalized costs are allocated to each parcel benefited, based on relative fair value before construction. As land is sold, all cost associated with that land is charged to cost of land sold.

(f) Miscellaneous

Cash & Cash Equivalents

The Authority has defined cash and cash equivalents to include cash on hand, demand deposits, and cash with fiscal agents. For purposes of the statement of cash flows, all highly liquid debt instruments and certificates of deposit, regardless of maturity date, are grouped into cash and cash equivalents.

Restricted Cash

Restricted cash includes: 1) funds held for procurement of capital assets; 2) option deposits on land; 3) funds for the EDIP; 4) funds for capital and structural improvements and repairs and maintenance to the Social Services facility; 5) funds from corporate park land sales; and 6) funds from various capital projects.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

Accounts Receivables

Where appropriate, trade receivables are shown net of an allowance for doubtful accounts.

Deferred Charges

The Authority Operations Fund deferred charges represent unamortized bond issuance costs incurred in the sale of Revenue Bonds. These costs are amortized using the straight-line method over the life of the related bonds. At June 30, 2005 and 2004, the unamortized bond issuance costs were \$650,414 and \$694,397.

Bond Premiums and Discounts

Bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method, which approximates the effective interest method. Bonds are reported net of the applicable bond premium or discount.

(2) Cash and Cash Equivalents

At June 30, 2005 and 2004, the carrying value of the Authority's deposits with banks and savings institutions were \$7,668,691 and \$6,018,551, respectively and the bank balances were \$7,782,131 and \$5,988,173, respectively. The June 30, 2005 bank balance was fully covered by federal depository insurance or collateralized in accordance with the Virginia Security for Public Deposits Act (the Act). Under the Act, banks holding public deposits in excess of the amounts insured by FDIC must pledge collateral in the amount of 50% of excess deposits to a collateral pool in the name of the State Treasury Board. Savings and loan institutions are required to collateralize 100% of deposits in excess of FDIC limits. The State Treasury Board is responsible for monitoring compliance with the collateralization and reporting requirements of the Act and for notifying local governments of compliance by banks and savings and loans. If any member financial institution fails, the entire collateral becomes available to satisfy the claims of the Authority. If the value of the pool's collateral is inadequate to cover a loss, additional amounts would be assessed on a pro-rata basis to the members (banks and savings and loans) of the pool. Therefore, these deposits are considered collateralized and as a result of this are considered insured.

The Authority's deposits at June 30, 2005 and 2004 are stated as Cash and Cash Equivalents and Restricted Cash and Cash Equivalents with balances of \$3,138,604 and \$4,530,087 and \$2,484,190 and \$3,534,361, respectively.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

The reconciliations of total cash and cash equivalents to the entity-wide financial statements at June 30, 2005 and 2004 are as follows:

	Governmental Activities/Special Projects Fund	Business-type Activities/Authority Operations Fund	Total 2005
Cash and Cash Equivalents- Bank of America	\$ -	3,138,604	3,138,604
Restricted Cash and Cash Equivalents-			
Option Deposits	\$ -	115,000	115,000
Town Center Option Land	-	17,422	17,422
Social Services	-	868,587	868,587
Town Center SunTrust	-	127	127
EDIP	-	1,326,393	1,326,393
EDIP Town Center	377,821	-	377,821
Land Sales/Infrastructure	-	1,680,941	1,680,941
TPC Golf Course	143,796	-	143,796
Total Restricted Cash and Cash Equivalents	\$ 521,617	4,008,470	4,530,087
Total	\$ 521,617	7,147,074	7,668,691

	Governmental Activities/Special Projects Fund	Business-type Activities/Authority Operations Fund	Total 2004
Cash and Cash Equivalents- Bank of America	\$ -	2,484,190	2,484,190
Restricted Cash and Cash Equivalents-			
Option Deposits	\$ -	90,000	90,000
Town Center Option Land	-	17,422	17,422
Social Services	-	754,671	754,671
Town Center SunTrust	-	442,744	442,744
EDIP	-	944,553	944,553
EDIP Town Center	99,658	-	99,658
Land Sales/Infrastructure	-	1,045,984	1,045,984
TPC Golf Course	139,329	-	139,329
Total Restricted Cash and Cash Equivalents	\$ 238,987	3,295,374	3,534,361
Total	\$ 238,987	5,779,564	6,018,551

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

(3) Restricted Cash and Cash Equivalents

The Town Center SunTrust reserve account balances at June 30, 2005 and 2004 were \$127 and \$442,744, respectively. These funds are proceeds from the June 2002 bond sales to purchase the Town Center Garage (Block 4) upon completion (See note 8).

The EDIP accounts were established in February 1994 through funds that the City appropriated from the Capital Improvement Program EDIP Project for economic development activities. This program represents annual funding from the City to the Authority to be used for off-site infrastructure needs for businesses meeting certain criteria. Payments are made out of these accounts to qualifying businesses to fund infrastructure improvements. EDIP cash and cash equivalents at June 30, 2005 and 2004 were \$1,704,214 and \$1,044,211, respectively.

A City Council Ordinance established the TPC Golf Course Project in May 1997. An appropriation of \$4,225,000, for improvements and infrastructure has been received since the project's inception. In fiscal year 2001, the City appropriated \$725,000 for road improvements. In January 1998, an additional \$100,000 option deposit was also received from PGA Tour Properties for an option to develop a second course on an additional 200 acres adjacent to the current project site. A total of \$4,225,000 has been expended to date. The cash account balances, representing interest and the option deposit, at June 30, 2005 and 2004 were \$ 143,796 and \$139,329, respectively.

The Social Services Facility reserve accounts at June 30, 2005 and 2004 were \$868,587 and \$754,671. These funds are reserved for capital and structural improvements, maintenance, and repairs to the facility in accordance with the lease agreement (See note 9).

Option deposits held in escrow are not available for operations. The deposits are normally applied to the sale price of optioned land if the sale is consummated, or forfeited in the event the option holder elects not to exercise the option. In the event the Authority is unable to satisfy its obligations stated in the option agreements, the option deposits would be fully refundable to the option holder. Option deposits were \$115,000 and \$90,000 in the Authority Operations Fund at June 30, 2005 and 2004, respectively.

Under a February 2003 loan modification agreement between the Authority and the City of Virginia Beach, 20% of the net proceeds from land sales within Corporate Landing Business Park and Oceana West Corporate Park are to be paid to the City to reduce the outstanding note balance, while the remaining 80% is to be used by the Authority to fund its infrastructure requirements and strategic land acquisitions. This modification was retroactive to March 22, 2002 and includes the net proceeds from land sales, which occurred between May 2003 and June 2004. At June 30, 2005 and 2004, 80% of the net proceeds, \$1,680,941 and \$1,045,984, respectively, attributable to the sale of property were reserved.

Restricted cash at June 30, 2005 and 2004 included \$17,422 of unexpended loan proceeds from the Town Center property financing.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Notes to Financial Statements

June 30, 2005 and 2004

(4) Receivables

Receivables at June 30, 2005 and 2004 consist of the following:

	Governmental Activities/ Special Projects Fund	Business-type Activities/ Authority Operations Fund	Total 2005
Industrial Revenue Bond fees	\$ -	5,125	5,125
Town Center Garage	-	9,011	9,011
Beach Quarters Inn	-	38,000	38,000
Interest	-	368	368
Due from City of Virginia Beach-Current	23,332	20,033	43,365
Due from City of Virginia Beach-Non-Current	-	9,653,703	9,653,703
Sportsplex	-	72,050	72,050
Land Sales	-	851,061	851,061
EDIP appropriations	-	3,582,512	3,582,512
Gross accounts receivables	\$ 23,332	14,231,863	14,255,195
Less: Allowance for Uncollectibles	-	-	-
Accounts receivable, net	\$ 23,332	14,231,863	14,255,195

The receivable due from the City of Virginia Beach includes the remaining portion of \$11.8 million in bond proceeds from the sale of Public Facility Revenue Bonds in September 2003 as well as \$3.9 million in bond proceeds from the sale of Public Facility Revenue Bonds in May 2005. The proceeds associated with these bond sales are held in the City's SNAP account.

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	Governmental Activities/ Special Projects Fund	Business-type Activities/ Authority Operations Fund	Total 2004
Industrial Revenue Bond fees	\$ -	130	130
Town Center Garage	-	11,933	11,933
Beach Quarters Inn	-	47,500	47,500
Interest	-	39	39
Due from City of Virginia Beach-Current	-	26,799	26,799
Due from City of Virginia Beach-Non-Current	250,000	11,800,000	12,050,000
Land Sales	-	851,061	851,061
Sportsplex	-	30,000	30,000
EDIP appropriations	-	3,267,420	3,267,420
Gross accounts receivables	\$ 250,000	16,034,882	16,284,882
Less: Allowance for Uncollectibles	-	-	-
Accounts receivable, net	\$ 250,000	16,034,882	16,284,882

(5) Internal Balances

At June 30, 2004, an internal balance existed between the Special Projects Fund and the Operations Fund. This balance consists of Town Center infrastructure expenses paid by the Operations Fund in June 2004. There was not an internal balance between the Special Projects Fund and Operations Fund at June 30, 2005.

	Governmental Activities/ Special Projects Fund	Business-type Activities/ Authority Operations Fund	Total 2004
Due from Special Projects Fund	\$ -	151,353	151,353
Due to Operation Fund	(151,353)	-	(151,353)
Internal Service Balances, Net	\$ (151,353)	151,353	-

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June 30, 2005 and 2004

(6) Capital Assets

The following schedules summarize the capital assets of the Authority as of June 30, 2005 and 2004:

	Balance June 30, 2004	Increase	Decrease	Balance June 30, 2005
Governmental Activities/ Special Projects Fund:				
Non-depreciable assets:				
Construction in progress	\$ 12,976,338	24,797,635	(37,748,350)	25,623
Business-Type Activities/Authority Operations Fund:				
Non-depreciable assets:				
Land	\$ 5,385,850	8,856,722	-	14,242,572
Option land/capitalized interest	3,098,208	110,935	(1,024,913)	2,184,230
Total non-depreciable assets	8,484,058	8,967,657	(1,024,913)	16,426,802
Depreciable Assets:				
Buildings	29,992,164	30,231,473	-	60,223,637
Total depreciable assets	29,992,164	30,231,473	-	60,223,637
Less Accumulated Depreciation for:				
Buildings	(2,239,813)	(1,021,397)	-	(3,261,210)
Total accumulated depreciation	(2,239,813)	(1,021,397)	-	(3,261,210)
Capital Assets, Net	\$ 36,236,409	38,177,733	(1,024,913)	73,389,229

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Notes to Financial Statements

June 30, 2005 and 2004

	Balance June 30, 2003	Increase	Decrease	Balance June 30, 2004
Governmental Activities/ Special Projects Fund:				
Non-depreciable assets:				
Construction in progress	\$ 12,682,099	6,792,966	(6,498,727)	12,976,338
Business-Type Activities/Authority Operations Fund:				
Non-depreciable assets:				
Land	\$ 5,385,850	-	-	5,385,850
Option land/capitalized interest	7,098,803	96,435	(4,097,030)	3,098,208
Total non-depreciable assets	<u>12,484,653</u>	<u>96,435</u>	<u>(4,097,030)</u>	<u>8,484,058</u>
Depreciable Assets:				
Buildings	29,628,833	363,331	-	29,992,164
Total depreciable assets	<u>29,628,833</u>	<u>363,331</u>	<u>-</u>	<u>29,992,164</u>
Less Accumulated Depreciation for:				
Buildings	(1,367,667)	(872,146)	-	(2,239,813)
Total accumulated depreciation	<u>(1,367,667)</u>	<u>(872,146)</u>	<u>-</u>	<u>(2,239,813)</u>
Capital Assets, Net	\$ <u>40,745,819</u>	<u>(412,380)</u>	<u>(4,097,030)</u>	<u>36,236,409</u>

At June 30, 2005 and 2004, depreciation expense related to capital assets was \$1,021,397 and \$872,146, respectively, and charged to Authority Operations.

In fiscal year 2005, the Authority reclassified land valued in the amount of \$4,872,645 that is located on Atlantic Avenue and 31st Street in Virginia Beach. The land, which was part of the Authority's land inventory in prior years, is now classified as a capital asset on the Authority's books. This reclassification occurred because the land is now under a ninety-nine year lease and not available for sale to other parties.

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Notes to Financial Statements

June 30, 2005 and 2004

(7) Accounts Payable and Accrued Liabilities

Accounts payables and accrued liabilities at June 30, 2005 and 2004 consist of the following:

	Governmental Activities/ Special Projects Fund	Business-type Activities/ Authority Operations Fund	Total 2005
Accounts payable	\$ -	61,231	61,231
Accounts payable-EDIP	401,153	4,908,905	5,310,058
Total accounts payable	<u>401,153</u>	<u>4,970,136</u>	<u>5,371,289</u>
Accrued interest	-	809,252	809,252
Options deposits	-	115,000	115,000
Security deposit	100,000	-	100,000
Total accrued liabilities	<u>100,000</u>	<u>924,252</u>	<u>1,024,252</u>
Due to other governments	-	97,050	97,050
Accounts payable and accrued liabilities \$	<u>501,153</u>	<u>5,991,438</u>	<u>6,492,591</u>

	Governmental Activities/ Special Projects Fund	Business-type Activities/ Authority Operations Fund	Total 2004
Accounts payable	\$ -	25,722	25,722
Accounts payable-EDIP	198,305	4,363,325	4,561,630
Total accounts payable	<u>198,305</u>	<u>4,389,047</u>	<u>4,587,352</u>
Accrued interest	-	599,143	599,143
Options deposits	-	90,000	90,000
Security deposit	100,000	-	100,000
Total accrued liabilities	<u>100,000</u>	<u>689,143</u>	<u>789,143</u>
Due to other governments	-	77,500	77,500
Accounts payable and accrued liabilities \$	<u>298,305</u>	<u>5,155,690</u>	<u>5,453,995</u>

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

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Notes to Financial Statements

June 30, 2005 and 2004

(8) Long-Term Debt

(a) Revenue Bonds

The Authority issues revenues bonds from time to time for the purpose of financing capital improvements and new projects. In February 1998, the Authority issued \$9,800,000 of Series 1998 Lease Revenue Bonds. The purpose of the bonds was to purchase a new building (Social Services Facility) from the City of Virginia Beach. The Series 1998 Lease Revenue Bonds' interest rates ranged from 4.3% to 5.0%. The principal is paid annually and interest is paid semi-annually with rental payments received from the City (see note 9) with final payment due December 2017.

In June 2002, the Authority issued two series of Public Facility Revenue Bonds totaling \$23,855,000. Series 2002A Public Facility Revenue Bonds were issued in the amount of \$20,815,000, while Series 2002B Taxable Public Facility Revenue Bonds were issued in the amount of \$3,040,000. The purpose of the Series 2002 Bonds was to finance the acquisition of a public parking facility and the land for a public plaza in the Town Center development in the City. The Bonds' interest rates ranged from 4.0% to 5.375% for Series 2002A and 4.57% to 5.75% for Series 2002B. The principal and interest is paid annually with payments received from the City pursuant to a support agreement dated June 1, 2002. The final payments on Series 2002A and 2002B are due August 2022 and August 2012.

In September 2003, the Authority acted as the conduit issuer for \$165,000,000 in Public Facility Revenue Bonds, at the request of the City of Virginia Beach. The funding from these bonds will finance various public facilities, including the replacement of the Pavilion Theater and the Convention Center, construction of a parking facility for the Virginia Aquarium and Marine Science Center, Open Space site acquisition, construction of an Emergency Communications Operation Center, construction of the 31st Street Parking Garage, construction of the Town Center's Blocks 10 and 12 garages, and various City equipment and software. The Authority and the City entered into a support agreement, dated September 1, 2003, whereby the City supports all Authority financial obligations (principal and interest payments) with regard to the bonds. The source of the City's support for the Town Center Public Parking garage portion of this issue is the CBD-South Tax Increment Financing District. The portion attributable to the Town Center Block 10 and 12 garages, \$11,800,000, is presented in business-type activity statements. The Bonds' interest rates ranged from 3.0% to 5.25%, and the final payment is due December 2023.

In May of 2005, the Authority acted as the conduit issuer for \$94,900,000 in Series 2005A Public Facility Revenue Bonds and \$9,000,000 in Series 2005B Taxable Public Facility Revenue Bonds. The Authority's financial statements only reflect \$17,050,000 in Series 2005A Public Facility Revenue Bonds and \$9,000,000 in Series 2005B Taxable Public Facility Revenue Bonds. In fiscal year 2005, \$22,130,000 in bond proceeds were used to purchase a portion of the 31st Street Project and the 9th Street Garage. The Authority will use the remaining bond proceeds in the amount of \$3,920,000 to purchase part of the Block 10 garage located in Town Center. The City's share of the bond proceeds will be used to finance various public facilities, including the replacement of the Pavilion Theater and the Convention Center, construction of a parking facility for the Virginia Aquarium and Marine Science Center, Open Space site acquisition, construction of an Emergency Communications Operation Center, and various City equipment and software. The Authority and the

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June 30, 2005 and 2004

City entered into a support agreement, dated September 1, 2003, whereby the City supports all Authority financial obligations (principal and interest payments) with regard to the bonds. The source of the City's support for the Town Center Public Parking garage portion of these issues is the CBD-South Tax Increment Financing District. The Authority's bond proceeds are presented in the business-type activity statements. The Bonds' interest rates ranged from 4.0% to 5.0% for Series 2005A and 4.75% to 5.0% for Series 2005B. The final payments on Series 2005A and 2005B are due May 2025.

(b) Notes Payable – Town Center

On, March 6, 2000, the Authority and Town Center Associates, L.L.C. entered into an agreement for the development of the Town Center. Financing for the purchase of the land for future phases beyond Phase I of this project was obtained from First Union National Bank/Wachovia in the amount of \$5,500,000. Total advances on this loan may not exceed \$11,135,000, to include accrued interest through December 2006. The loan agreement was signed on June 8, 2000 and calls for semiannual interest payments starting November 30, 2000, with all principal and interest due December 1, 2006. Under the terms of this agreement, the Authority is not required to make any principal or interest payments on this loan until the final due date of December 2006; and the intention is to not make principal or interest payments, except to the extent funds are available from the sale of this land. To date, \$884,101 has been added to the original principal of the loan in the form of interest. As of June 30, 2005, the outstanding balance is \$3,283,558. The interest rate is the LIBOR rate plus 0.42%. The loan is secured by a surety agreement provided by Town Center Associates, L.L.C. that requires Town Center Associates, L.L.C. to purchase the land no later than September 2006.

(c) Notes Payable – City of Virginia Beach

On February 25, 2003, the Virginia Beach City Council approved a restructuring proposal for the outstanding debt between the City and the Authority. Under this restructuring accrued interest in the amount of \$1,235,331 was canceled and the remaining debt was separated into two non-interest bearing notes. Note 1, in the original principal amount of \$4,830,936, is secured by a first lien on the 31st Street property. Note 2, in the original principal amount of \$1,425,201, is secured by a first lien on Corporate Landing and Oceana West Corporate Parks.

The following covenants will be in effect while the loan is outstanding: 1) The Authority will incur no additional debt without City approval; 2) All net proceeds from the sale or ground lease of the 31st Street property will be paid to the City when received; 3) 20% of the net proceeds generated from all land sales in Corporate Landing and Oceana West will be used to reduce the outstanding debt; and 4) The remaining net proceeds (80%) from land sales in Corporate Landing and Oceana West will be used by the Authority to fund its infrastructure requirements and strategic land acquisitions.

The modifications to the outstanding debt were made retroactive to March 22, 2002, the date of the satisfaction of the Bank of America loan. Twenty percent of the net proceeds from all land sales, within Corporate Landing and Oceana West, have been distributed to the City to reduce the outstanding debt balance. As of June 30, 2005, the outstanding debt balance was \$5,835,902.

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Notes to Financial Statements

June 30, 2005 and 2004

Long-term debt activities for the year ended June 30, 2005 and 2004 were as follows:

	<u>Balance June 30, 2004</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance June 30, 2005</u>	<u>Amounts Due Within One Year</u>
Business-type activities/Authority					
Operations Fund					
Bonds and notes payable:					
Lease revenue bonds-Social Services	\$ 7,695,000	-	(400,000)	7,295,000	420,000
Public facility revenue bonds	35,655,000	26,050,000	-	61,705,000	890,000
Notes payable-Town Center Option Land	4,219,006	106,466	(1,041,913)	3,283,559	2,028,221
Notes payable-City of Virginia Beach	5,994,641	-	(158,739)	5,835,902	109,896
	<u>53,563,647</u>	<u>26,156,466</u>	<u>(1,600,652)</u>	<u>78,119,461</u>	<u>3,448,117</u>
Add: Bond premium	510,945	702,983	(33,983)	1,179,945	-
Less: Bond discount	(192,448)	-	12,835	(179,613)	-
Business- Type Activities/Authority					
Long-Term Debt	\$ <u>53,882,144</u>	<u>26,859,449</u>	<u>(1,621,800)</u>	<u>79,119,793</u>	<u>3,448,117</u>

	<u>Balance June 30, 2003</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance June 30, 2004</u>	<u>Amounts Due Within One Year</u>
Business-type activities/Authority					
Operations Fund					
Bonds and notes payable:					
Lease revenue bonds-Social Services	\$ 8,080,000	-	(385,000)	7,695,000	400,000
Public facility revenue bonds	23,855,000	11,800,000	-	35,655,000	-
Notes payable-Town Center Option Land	7,358,878	101,975	(3,241,847)	4,219,006	1,020,059
Notes payable-City of Virginia Beach	6,108,687	-	(114,046)	5,994,641	159,066
	<u>45,402,565</u>	<u>11,901,975</u>	<u>(3,740,893)</u>	<u>53,563,647</u>	<u>1,579,125</u>
Add: Bond premium	539,070	-	(28,125)	510,945	-
Less: Bond discount	(205,283)	-	12,835	(192,448)	-
Business- Type Activities/Authority					
Long-Term Debt	\$ <u>45,736,352</u>	<u>11,901,975</u>	<u>(3,756,183)</u>	<u>53,882,144</u>	<u>1,579,125</u>

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Notes to Financial Statements

June 30, 2005 and 2004

The requirements to amortize all long-term bonds and notes payable as of June 30, 2005, including interest payments of \$39,924,082 are summarized as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 3,448,117	3,394,946
2007	3,243,573	3,333,391
2008	2,478,066	3,251,408
2009	2,773,066	3,157,581
2010	2,440,000	3,044,552
2011-2015	20,381,639	13,107,732
2016-2020	22,135,000	8,287,594
2021-2025	21,220,000	2,346,878
	<u>\$ 78,119,461</u>	<u>39,924,082</u>

(9) Operating Leases

In February 1998, the Authority purchased a new building (Social Services Facility) from the City, which was placed in service on May 1, 1998. The Authority entered into a 20-year operating lease with the City. The City pays basic rent equal to the amounts required to pay the principal and interest of the Lease Revenue Bonds Series 1998 (see note 8) and additional rent equal to one-eighth of one percent of the outstanding principal balance of the bonds. In addition, \$50,000 is paid semi-annually and placed in a reserve to be used as needed for capital and structural improvements, maintenance and repair of the facility (see note 3).

The following schedule shows the composition of the Authority's investment in property under operating leases:

	<u>2005</u>	<u>2004</u>
Social Services Facility (including land)	\$ 9,497,137	9,497,137
Less accumulated depreciation	(1,264,079)	(1,089,151)
Net investment on property held for lease	<u>\$ 8,233,058</u>	<u>8,407,986</u>

Minimum future rental income on operating leases as of June 30, 2005 are as follows: 2006, \$860,670; 2007, \$856,731; 2008, \$857,012; 2009, \$861,297; 2010, \$859,086; 2011-2015, \$4,294,822; 2016-2017, \$2,528,954.

(10) Industrial Revenue Bonds

Periodically, the Authority has issued Industrial Revenue Bonds to provide financial assistance to private-sector entities for the acquisition and construction of industrial and commercial facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities transfers to the private-sector entity served by the bond issuance. The Authority is

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Notes to Financial Statements

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never obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements.

As of June 30, 2005 and 2004, there were 72 and 83 series of Industrial Revenue Bonds outstanding, respectively. The bonds had an aggregate principal amount payable of \$356,673,817 and \$374,630,069, respectively.

(11) Interest Cost

The Authority capitalizes interest cost related to construction in progress. The following is a summary of interest cost incurred during 2005 and 2004:

	<u>2005</u>	<u>2004</u>
Interest cost capitalized	\$ 110,935	96,435
Interest cost charged to income	<u>2,342,080</u>	<u>2,004,395</u>
Total interest cost incurred	\$ <u>2,453,015</u>	<u>2,100,830</u>

(12) Lease Income

Lease income as reflected in the statements of revenues, expenses, and changes in net assets was \$1,490,170 and \$1,302,578, respectively for the years ended June 30, 2005 and 2004. The following is a detailed list of the revenue earned:

	<u>2005</u>	<u>2004</u>
Social Services Facility	\$ 858,833	861,224
Sportsplex ground rent	60,000	60,000
Amphitheater ground rent	128,291	118,166
TPC Golf Course ground rent	69,863	69,438
Beach Quarters Inn	114,000	114,000
Town Center Garage	126,834	79,750
9th Street Garage	132,349	—
	\$ <u>1,490,170</u>	<u>1,302,578</u>

(a) Social Services Facility

In 1998, the Authority entered into a 20-year operating lease with the City. The City pays basic rent equal to the amounts required to pay the principal and interest of the Lease Revenue Bonds Series 1998 (see note 7) and additional rent equal to one-eighth of one percent of the outstanding principal balance of the bonds. In addition, \$50,000 is paid semi-annually and placed in a reserve to be used as needed for capital and structural improvements, maintenance, and repair of the facility (see note 3).

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June 30, 2005 and 2004

(b) Sportsplex Ground Rent

In 1997, the Authority executed a ground lease with the City for the Sportsplex and a stadium operating and use agreement with a private entity. A termination agreement was executed in fiscal year 2001. Under the terms of this agreement, \$300,000 was due to the Authority if a new operator was not found by July 15, 2001. In October 2001, the Authority entered into a five-year joint use agreement with a new operator, for \$60,000 per year to be secured by a \$300,000 letter of credit. When the operator was unable to obtain a letter of credit, the agreement was assigned to another operator with a secured letter of credit. The new operator agreed to pay the Authority \$60,000 per year, however during fiscal year 2005, the rent was not paid in full. In June 2005, a new operator paid the Authority \$17,950 as a partial rental payment; the remainder of the back rent owed to the Authority (\$72,050) was paid to the City in July of 2005. City Council approved the assignment of the remaining term of the lease to a new operator in September of 2005.

(c) Amphitheater

The Amphitheater Lease Agreement provides that Cellar Door Venues, Inc. (Cellar Door) will pay the Authority rent having three components: ground rent, basic rent, and supplemental rent. Ground rent is the sum of \$120,000 offset and reduced by the total amount of Amphitheater leasehold (real estate) taxes paid to the City during the calendar year. In addition, Cellar Door pays basic rent to the Authority in an amount equal to 10% of adjusted ticket revenues (offset by admissions taxes paid to City), 5% of adjusted sponsorship revenues, and 5% of adjusted parking revenues paid during the year. Minimum basic rent is \$610,000 annually (before reduction of admissions taxes, parking and sponsorship revenues) until the City recovers its investment, after which time the Authority may retain an administrative fee. Section 3.2 of the Amphitheater Coordination Agreement provides that the Authority shall remit to the City an amount equal to all rent actually received from Cellar Door under the Lease Agreement. The term of the lease is 30 years.

(d) TPC Golf Course

In 1997, the Authority and TPC of Virginia Beach, L.L.C. (TPC) executed a sublease agreement, which ends in October 2037. The basic rent is offset and reduced by the total amount of taxes paid by TPC or TPC's concessionaires to the City during the calendar year.

(e) Beach Quarters Inn

In June 2002, as part of the amended and restated 31st Street Project Development Agreement and other documents, the Authority agreed to purchase the property and building improvements, at 300 Atlantic Avenue, known as Beach Quarters Inn. The purchase of this property occurred in October 2002. In addition, the Authority executed a lease agreement with Beach Quarters Inn, L.C. The initial lease term is for one-year beginning October 1, 2002 and includes up to nine (9) additional one-year terms. The rent is \$114,000 per annum, paid in equal installments in June, July and August.

(f) Town Center

As part of the Town Center Phase I Development Agreement, the Developer has the right to lease 178 of the parking spaces in the Town Center Garage (Block 4) to tenants in the office tower. The Master Agreement pertaining to this lease arrangement was executed in December 2002. All revenue

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

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collected for the reserved spaces is to be forwarded to the Authority to defray the operating costs of the Garage.

(g) 9th Street Garage

On March 31, 2005, the Authority used proceeds from Public Facility Revenue Bonds to purchase the 9th Street Parking Garage for \$9,750,000. The garage consists of 664 spaces, however, only 610 spaces are available for public parking. The remaining 54 spaces are under a long-term lease agreement that was signed prior to the Authority's purchase of the garage.

(13) Advances from City of Virginia Beach

Advances from the City of Virginia Beach represent funds that have been provided, by the City, to the Authority for the construction of capital projects. When construction is complete, the capital asset reverts back to the City. During fiscal year 2005, the City had advanced funding for the following capital projects:

31st Street – The project is the result of a public/private investment partnership agreement between the City, the Authority and the Thirty-First Street, L.C. In fiscal year 2005, the project was completed and a portion of the asset was transferred to the City.

Town Center infrastructure – The project is the result of a public/private investment partnership agreement between the City, the Authority, and Town Center Associates, L.L.C. Advances from the City as of June 30, 2005 and 2004 were \$25,623 and \$4,927,587, respectively. During fiscal year 2005 and 2004, infrastructure assets in the amount of \$5,730,936 and \$6,468,942 were completed and transferred to the City. Also during fiscal year 2005, the Town Center Plaza was completed for \$1,765,994, and in fiscal year 2004, \$363,331 of expenditures related to the Block 4 parking garage were capitalized. These assets were then transferred to the Authority's Proprietary Fund. The costs for this project include infrastructure for streets, curbs and gutters, sidewalks and underground utilities. The total funding currently available for Phase I of the project is \$6,385,000, of which \$5,000,000 is funded through the Authority's EDIP program and the City's CIP Program funds \$1,385,000. Funding available for Phase II, as of June 30, 2005 includes \$4,000,000, funded from the Authority's EDIP program and \$3,700,000 from the City's CIP Program. Additional funding includes \$1 million from the EDIP program in fiscal year 2006.

As of June 30, 2005, the Authority was responsible for \$700,000 to \$1,000,000 of financial commitments related to ongoing projects.

(14) Subsequent Events

(a) Sportsplex

In fiscal year 2006, the Sportsplex use agreement was reassigned to the new Mariners ownership group. Two \$30,000 payments are due each year (one in the fall and one in the spring) for the rental of the facility. The Authority received a payment of \$72,050 in July 2005 that fully satisfies the receivable that was due for the rental of the Sportsplex.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Schedule of Selling, General, and Other Expenses – Authority Operations

Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Selling expenses:		
Sales commissions	\$ 21,024	—
Total selling expenses	<u>21,024</u>	<u>—</u>
General expenses:		
Leases	474,503	366,100
Depreciation	1,021,397	872,146
Amphitheater box seating	25,500	23,000
Independent audit fees	10,800	10,480
Amortization	43,983	43,983
Insurance	2,398	2,754
Equipment under \$5,000	—	3,759
Gifts and donations	14,500	10,000
Leasehold Improvements	27,828	9,803
Bank Charges	—	(1,595)
Other	636	4,195
Total general expenses	<u>1,621,545</u>	<u>1,344,625</u>
Other expenses:		
City of Virginia Beach escrow deposit refund - BQI	—	300,000
Town Center Infrastructure	210,119	99,658
Architecture and engineering	71,620	64,751
Park maintenance – Corporate Landing	22,527	26,372
Utilities – Corporate Landing fountain	2,785	3,427
Miscellaneous	24,393	19,653
Total other expenses	<u>331,444</u>	<u>513,861</u>
Total selling, general, and other expenses	<u>\$ 1,974,013</u>	<u>1,858,486</u>

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Schedule of Land Inventory

Years ended June 30, 2005 and 2004

Description:	<u>2005</u>	<u>2004</u>
Oceana West Corporate Park – beginning inventory July 1	\$ 1,913,239	2,413,478
Current – cost of sales	<u>—</u>	<u>(500,239)</u>
Oceana West Corporate Park – ending inventory June 30	<u>1,913,239</u>	<u>1,913,239</u>
Corporate Landing Office Park – beginning inventory July 1	11,603,840	11,603,840
Current – cost of sales	<u>(534,038)</u>	<u>—</u>
Corporate Landing Office Park – ending inventory June 30	<u>11,069,802</u>	<u>11,603,840</u>
Hunt Club 2 – beginning inventory July 1	200,305	285,000
Adjustment – net realizable value	—	566
Current – cost of sales	<u>—</u>	<u>(85,261)</u>
Hunt Club 2 – ending inventory June 30	<u>200,305</u>	<u>200,305</u>
Oceanfront – beginning inventory July 1	4,872,645	4,872,645
Transfer – 31st Street Project land to capital assets	<u>(4,872,645)</u>	<u>—</u>
Oceanfront – ending inventory June 30	<u>—</u>	<u>4,872,645</u>
Total ending inventory	<u>\$ 13,183,346</u>	<u>18,590,029</u>

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
Component Unit of the City of Virginia Beach, Virginia

Schedule of Construction in Progress

Year ended June 30, 2005

	<u>31st Street</u>	<u>Town Center Infrastructure</u>	<u>Total</u>
Expended during the year ended June 30:			
2000	\$ 2,822,915	—	2,822,915
2001	2,610,818	3,095,062	5,705,880
2002	514,015	956,014	1,470,029
2003	102,070	2,581,205	2,683,275
2004	1,998,933	(1,704,696)	294,237
2005	<u>(8,048,751)</u>	<u>(4,901,962)</u>	<u>(12,950,713)</u>
	\$ <u>—</u>	<u>25,623</u>	<u>25,623</u>

In fiscal year 2005, the 31st Street Project was completed and a portion of the asset totaling \$9,892,768 was transferred to the City. The remaining portion of the asset in the amount of \$23,207,500 is part of the fiscal year 2005 increase in capital assets on the Authority's financial statements.

In fiscal year 2005 and 2004, \$5,730,936 and \$6,468,942 of costs associated with Town Center Phase I and II were capitalized and transferred to the City, and \$1,765,994 and \$363,331 of costs were capitalized and are part of the fiscal year 2005 increase in capital assets on the Authority's financial statements.

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY

Component Unit of the City of Virginia Beach, Virginia

Schedule of EDIP Accounts Payable

June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Balance Forward	\$ 4,561,630	4,237,695
Funding sources:		
EDIP City Appropriation - fiscal year	1,407,830	1,485,050
Town Center City Appropriation - fiscal year	1,000,000	1,000,000
Reimbursement for account payable accruals	99,658	2,220,922
Reimbursement for Construction Management/Design Expenses	186,770	333,545
Reclassification of infrastructure reimbursements	—	99,658
Interest Earned - fiscal year - checking	1,954	1,891
Total Funding Available	<u>7,257,842</u>	<u>9,378,761</u>
Expenses:		
EDIP Awards paid	(860,943)	(1,350,900)
Engineering Studies	(3,262)	(10,410)
Town Center Expenditures	(908,606)	(3,455,821)
Total Expenditures	<u>(1,772,811)</u>	<u>(4,817,131)</u>
Net transfer of Town Center EDIP Funding	<u>(174,973)</u>	—
Total Accounts Payable - Economic Development Program Fund	<u>\$ 5,310,058</u>	<u>4,561,630</u>

CITY OF VIRGINIA BEACH DEVELOPMENT AUTHORITY
 Component Unit of the City of Virginia Beach, Virginia
 Schedule of Nonoperating Revenue from City of Virginia Beach
 Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Central Business District-South payment of debt service for Town Center Note and Public Facility Revenue Bonds	\$ 2,389,284	1,688,720
Option Release Payment	165,625	—
Partial Payment for 31st Street Project	2,569,855	—
Virginia Beach Amphitheater Capital Improvement Program	50,000	50,000
Town Center Garage - Special Service District	435,941	234,840
31st Street DFU fees	—	300,000
31st Street Project Marketing Program	23,674	152,251
Total Nonoperating revenue from City of Virginia Beach	\$ <u>5,634,379</u>	<u>2,425,811</u>



Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters in Accordance With *Government Auditing Standards*

The Commissioners
City of Virginia Beach Development Authority

We have audited the basic financial statements of the City of Virginia Beach Development Authority (the "Authority") as of and for the years ended June 30, 2005 and 2004, and have issued our report thereon dated August 19, 2005. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's 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 an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud 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. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Commissioners, City Council, and Authority and City management and is not intended to be and should not be used by anyone other than these specified parties.

Virginia Beach, Virginia
August 19, 2005

Cherry, Bekaert & Holland, LLP