

- TABLE OF CONTENTS -

INDEPENDENT AUDITOR'S REPORT:

[Auditor's Report on Financial Statements](#)

[Auditor's Report on Compliance and on Internal Control Over Financial Reporting](#)

FINANCIAL STATEMENTS:

[Balance Sheet](#)

[Statement of Support and Revenue, Expenses, and Changes in Fund Balances](#)

[Statement of Cash Flows](#)

[Notes to Financial Statements](#)

SUPPLEMENTARY INFORMATION:

[Schedule of Changes in Fund Balances](#)

AGENCY OFFICIALS

August 13, 1999

The Honorable James S. Gilmore, III
Governor of Virginia

Board of Directors
Innovative Technology Authority

INDEPENDENT AUDITOR'S REPORT

We have audited the balance sheet of the **Innovative Technology Authority** as of June 30, 1999, and the related statements of support and revenue, expenses, and changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As more fully described in Note A, the accompanying financial statements do not include the financial position and the results of operations and cash flows of the Center for Innovative Technology, a component unit of the Innovative Technology Authority.

In our opinion, except for the omission of component unit financial data as described above, the financial statements referred to above present fairly, in all material respects, the financial position of the Innovative Technology Authority as of June 30, 1999, and the results of its operations and cash flows for the year then ended, in conformity with generally accepted accounting principles.

The supplemental schedules of changes in fund balances and expenditure of federal awards are presented for the purpose of additional analysis and is not a required part of the basic financial statements. The information has been audited in connection with the audit of the basic financial statements and, in our opinion, such information is fairly stated in all material respects in relation to the financial statements taken as a whole.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Compliance

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the internal controls over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal controls over financial reporting. Our consideration of the internal controls over financial reporting would not necessarily disclose all matters in the internal controls over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level of risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal controls over financial reporting and its operation that we consider to be material weaknesses.

The “Independent Auditor’s Report on Compliance and on Internal Control Over Financial Reporting” is intended solely for the information and use of the Governor and General Assembly of Virginia, the Innovative Technology Authority Board and Authority management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR OF PUBLIC ACCOUNTS

KKH/kva
kva:46

INNOVATIVE TECHNOLOGY AUTHORITY
BALANCE SHEET
As of June 30, 1999

A S S E T S

Current assets:	
Cash and cash equivalents (Note B)	\$ 1,527,623
Accrued rent and interest receivable and deposits	200,206
Accounts receivable (Net of allowance for doubtful accounts of \$4,840)	<u>36,004</u>
Total current assets	1,763,833
Non-current assets:	
Unamortized bond issuance expense	<u>135,489</u>
Property and equipment:	
Land	7,300,000
Land improvements	627,197
Building (Note C)	24,941,985
Less accumulated depreciation	(3,797,118)
Furniture, fixtures and equipment	2,821,849
Less accumulated depreciation	<u>(1,877,340)</u>
Total property and equipment	<u>30,016,573</u>
Total assets	<u><u>\$ 31,915,895</u></u>

LIABILITIES AND FUND BALANCES

Current liabilities:	
Due to non-profit organization (Note F)	\$ 87,188
Accrued interest payable	148,236
Accounts payable and accrued expenses	182,296
Security deposits	<u>18,179</u>
Total current liabilities	435,899
Long-term liabilities:	
Bonds payable (Note D)	<u>12,195,000</u>
Total liabilities	<u>12,630,899</u>
Fund balance	<u>19,284,996</u>
Total liabilities and fund balances	<u><u>\$ 31,915,895</u></u>

The accompanying Notes to Financial Statements are an integral part of this statement.

INNOVATIVE TECHNOLOGY AUTHORITY
STATEMENT OF SUPPORT AND REVENUE, EXPENSES,
AND CHANGES IN FUND BALANCES
For the Year Ended June 30, 1999

SUPPORT AND REVENUE

Appropriations from the Commonwealth of Virginia	\$ 11,577,237
Interest income	82,536
Lease revenue	1,357,533
Rental income - bonds	1,374,516
Transfer from non-profit organization	270,173
Other income	<u>3,166</u>
Total support and revenue from operations	<u>14,665,161</u>

EXPENSES

Operating:

Distribution to non-profit organization (Note F)	11,577,237
Building operating costs	1,234,152
Other administration	21,401
Interest	931,150
Depreciation	1,144,997
Land project	110,271
Loss on disposal of fixed assets	<u>17,074</u>

Total operating expenses	<u>15,036,282</u>
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Deficiency of support and revenue under operating expenses	(371,121)
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Fund balance, July 1, 1998	<u>19,656,117</u>
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Fund balance at June 30, 1999	<u><u>\$ 19,284,996</u></u>
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The accompanying Notes to Financial Statements are an integral part of this statement.

INNOVATIVE TECHNOLOGY AUTHORITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 1999

Cash flows from operating activities:	
Excess of expenses over support and revenue	\$ (371,121)
Reconciling items:	
Depreciation and amortization	1,144,997
Loss on disposal of fixed assets	17,174
Change in assets and liabilities:	
Decrease in accounts receivable	12,589
Increase in accrued interest receivable	(16,135)
Decrease in unamortized bond issuance expense	9,134
Increase in accounts payable	98,000
Decrease in due to non-profit organization	(17,310)
Decrease in accrued interest payable	(6,520)
Decrease in security deposits	<u>(6,291)</u>
Net cash provided by operating activities	<u>864,517</u>
Cash flows from investing activities:	
Acquisition of short-term investments	<u>974,230</u>
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets - CIT	(270,173)
Acquisition and construction of capital assets - ITA	(245,152)
Cash payment to retire bond indenture	<u>(435,000)</u>
Net cash provided by capital and related financing activities	<u>(950,325)</u>
Net increase in cash and cash equivalents	888,422
Cash and cash equivalents at July 1, 1998	<u>639,201</u>
Cash and cash equivalents at June 30, 1999	<u><u>\$ 1,527,623</u></u>

The accompanying Notes to Financial Statements are an integral part of this statement.

INNOVATIVE TECHNOLOGY AUTHORITY

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 1999

NOTE A – SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: The Innovative Technology Authority (Authority), which was created by the General Assembly in 1984, is a political subdivision of the Commonwealth of Virginia. Its mission is to promote the economic development of the Commonwealth of Virginia through technology. The financial statements of the Authority have been prepared on the accrual basis of accounting.

The Center for Innovative Technology (CIT) is a non-stock, not-for-profit corporation, which acts as the operating arm of the Authority and is a component unit of the Authority. These financial statements do not include the financial position and results of operations and cash flows of CIT. Inclusion of this data is necessary for reporting in conformity with generally accepted accounting principles. Financial statements for CIT may be obtained from CIT.

A separate report is prepared for the Commonwealth of Virginia which includes all agencies, boards, commissions and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. The Authority is a component unit of the Commonwealth of Virginia and is included in the general purpose financial statements of the Commonwealth.

Property and Equipment: Property and equipment are stated at cost at date of acquisition or fair market value at date of donation in the case of gifts. Depreciation is recorded on the straight-line basis over estimated useful lives of the assets ranging from 3 to 40 years.

NOTE B – CASH, CASH EQUIVALENTS AND INVESTMENTS

Certain deposits and investments of the Authority are held by The Bank of New York, as trustee for the Authority. This activity is in accordance with the provisions of the Master Indenture of Trust Agreement between the Authority and the trustee. Cash and cash equivalents represent deposits and short-term investments with maturities of ninety days or less.

Deposits with banks are covered by federal depository insurance or collateralized in accordance with Virginia Security for Public Deposits Act. Under the Act, banks holding public deposits in excess of the amount insured by FDIC must pledge collateral in the amount of 50 percent of excess deposits to a collateral pool in the name of the State Treasury Board.

The Authority's cash and cash equivalents are categorized below to give an indication of the level of credit risk assumed by the Authority at June 30, 1999. Credit risk is the risk that the Authority may not be able to obtain possession of its investment instrument or collateral at maturity. Risk category 1 includes investments which are insured or registered or for which the securities are held by the Authority or its safekeeping agent in

the Authority's name. Risk category 2 includes uninsured or unregistered investments for which the securities are held by the broker's or dealer's trust department or safekeeping department in the Authority's name. Risk category 3 includes uninsured or unregistered investments for which the securities are held by the broker or dealer, or by its trust department or safekeeping department but not in the Authority's name. There were no investments in risk categories 2 and 3. The Local Government Investment Pool is not categorized into one of these risk categories since the Authority's equity in this pool does not consist of identifiable securities.

	Category 1	Market Value
Cash and cash equivalents:		
Deposits	<u>\$ 154,692</u>	\$ 154,692
Local Government Investment Pool		<u>1,372,931</u>
Total cash and cash equivalents		<u>\$ 1,527,623</u>

NOTE C – BUILDINGS

The Authority issued Taxable Lease Revenue Bonds (Virginia Department of Economic Development Project) on March 1, 1989. The Authority leased a building to the Department of Economic Development, now the Virginia Economic Development Partnership (the Partnership), pursuant to a lease agreement dated February 1, 1989, and a Memorandum of Lease dated March 1, 1989. The lease provided for rental payments by the Department equal to the sum of the debt service on the bonds and the fees and expenses of the trustee of the bond issue and reimbursement of operating costs.

On May 1, 1997, the Authority and Partnership terminated the lease agreement. The Authority assumed ownership of the building and recorded it at \$11,800,000, the principal amount remaining on the outstanding capital lease receivable and corresponding bonds payable. The Partnership paid interest costs through June 30, 1997. As described in Note D, on May 1, 1997, the Authority advance refunded \$11.2 million of the assumed bonds.

NOTE D – BONDS PAYABLE

The Authority issued \$12,455,000 of Taxable Lease Revenue Refunding Bonds on May 1, 1997, pursuant to a Master Indenture of Trust and First Supplemental Indenture of Trust between the Authority and Signet Trust Company, Richmond, Virginia, as Trustee (since transferred to the Bank of New York). The Series 1997 Bonds were issued by the Authority to advance refund \$11,200,000 of outstanding 1989 Taxable Revenue Lease Bonds, Series 1989.

The following amortization schedule illustrates the Authority's principal and interest requirements for the Series 1997 Bonds.

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2000	\$ 540,000	\$ 889,414	\$ 1,429,414
2001	535,000	853,288	1,388,288
2002	530,000	816,801	1,346,801
2003	625,000	780,337	1,405,337
2004	620,000	736,587	1,356,587
2005	710,000	692,691	1,402,691
2006	700,000	641,855	1,341,855
2007	790,000	591,525	1,381,525
2008-2014	<u>7,145,000</u>	<u>2,279,080</u>	<u>9,424,080</u>
Total	<u>\$ 12,195,000</u>	<u>\$ 8,281,578</u>	<u>\$ 20,476,578</u>

NOTE E – PRIOR YEAR DEFEASANCE OF DEBT

In prior years, the Authority defeased certain taxable lease revenue bonds totaling \$11.2 million by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds were not included in the Authority's financial statements. On May 1, 1999, the defeased bonds were called and redeemed, and are no longer payable.

NOTE F – DISTRIBUTION TO A NON-PROFIT ORGANIZATION

The distribution to non-profit organization represents appropriations transferred to the Center for Innovative Technology (CIT). CIT is a nonstock corporation created by the Authority, as provided by Section 9-263 of the Code of Virginia, to carry out the purpose for which the Authority was created.

NOTE G – Year 2000 READINESS EFFORT

In March, 1999 a team was formed to address the total Year 2000 effort including information systems, facilities & embedded technologies, data exchange, supply chain and telecommunications. A project plan has been established to ensure that all milestones are tracked and met.

INFORMATION SYSTEMS - All user machines have been serviced to address any deficiencies. In the area of user machines and software, CIT has reached 100 percent compliancy. In the area of server hardware and software, one server operating system needs to be serviced and one software

program needs to be upgraded. Once these two issues have been addressed, all areas of information systems will be compliant. This will occur no later than August 31, 1999.

A contingency plan will be prepared to address network accessibility, availability and to ensure that the accounting system is intact. The contingency plan will be available no later than November 30, 1999.

FACILITIES AND EMBEDDED TECHNOLOGIES - Equipment for the head quarters office located in Herndon, Virginia consists of fire alarm control panel, pre-action fire alarm panel, access control system, energy management system, cable elevators, hydraulic elevators, UPS systems, and site scan system.

All systems, with the exception of the site scan system, have been tested and have been found compliant. Each system contains a documented survey to confirm compliancy. The site scan system has been ordered and will be installed no later than September 15, 1999.

CIT also has eight (8) regional offices located throughout the Commonwealth of Virginia. All offices are housed in leased facilities. In an effort to ensure that all regional offices are in facilities that have made provisions for Year 2000 compliancy, letters were sent to each landlord. To date, all have been received.

A contingency plan has been prepared by building management that covers each identified area. Building management will also supply a list of contacts as well as a personnel policy to ensure the safety and security of the CIT building. These lists will be available no later than November 30, 1999.

DATA EXCHANGE – The payroll vendor, ADP, and the payroll software used at CIT have been identified as being Year 2000 compliant.

A contingency plan will be written and in place no later than October 31, 1999.

SUPPLY CHAIN - Mission-critical supply chain vendors including banks, utility companies, service providers, suppliers and benefits and welfare administrators have been identified and contacted.

An evaluation will be conducted no later than August 30, 1999 to ensure that CIT has compliancy information for each identified vendor. For those vendors who have not responded, a follow-up phone call will be conducted.

A contingency plan will be established addressing the possible problems with financial providers to ensure that CIT can continue to access funds to pay vendors and employees. The anticipated deadline of completion for this document is October 31, 1999.

TELECOMMUNICATIONS – Critical telecommunications equipment has been inventoried and includes as telephone equipment, fax equipment and the postage machine.

Equipment was tested by advancing dates to the Year 2000 and checking to ensure that all equipment functioned properly with the date change.

A contingency plan will be prepared in the event of phone outages. The milestone date of August 31, 1999 has been set for this plan.

In order to address cost issues for replacement of equipment in order to reach full Year 2000 compliancy, funding has been set aside to accomplish these needs. For fiscal year 2000, Innovative Technology Authority was granted \$105,000 for this effort. These funds will be spent on any necessary equipment and software replacement and upgrades, as well as funding for analysis software or vendors to assist in performing verification.

INNOVATIVE TECHNOLOGY AUTHORITY
SCHEDULE OF CHANGES IN FUND BALANCES
For the Year Ended June 30, 1999

INVESTMENT IN PROPERTY AND EQUIPMENT

Fund balance at beginning of year	\$18,033,418
Transfer from undesignated - debt retirement	435,000
Transfer from undesignated - equipment purchases	287,488
Transfer to undesignated - loss on asset disposal	(17,174)
Transfer from building project	227,837
Depreciation and amortization	<u>(1,144,997)</u>
Fund balance at end of year	<u>17,821,572</u>

DESIGNATED TO BUILDING PROJECT

Fund balance at beginning of year	745,423
Transfer from undesignated fund - investment earnings	72,651
Transfer to undesignated for expenditures	(133)
Transfer to investment in property and equipment	<u>(227,837)</u>
Fund balance at end of year	<u>590,104</u>

DESIGNATED TO LAND PROJECT

Fund balance at beginning of year	672,545
Transfer to undesignated for expenditures	<u>(110,271)</u>
Fund balance at end of year	<u>562,274</u>

UNDESIGNATED

Fund balance at beginning of year	204,731
Deficiency of support and revenue under expenses	(371,121)
Depreciation, and amortization	1,144,997
Transfer to investment in property and equipment - equipment purchases	(287,488)
Transfer from undesignated - loss on asset disposal	17,174
Transfer to investment in property and equipment - debt retirement	(435,000)
Transfers to building project - investment earnings	(72,651)
Transfers from building project for expenditures	133
Transfers from land project for expenditures	<u>110,271</u>
Fund balance at end of year	<u>311,046</u>
Total fund balances	<u><u>\$ 19,284,996</u></u>

INNOVATIVE TECHNOLOGY AUTHORITY

Herndon, Virginia

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