

County of Hanover, Virginia Management's Discussion and Analysis

As management of the County, we offer readers of the financial statements this narrative overview and analysis of the financial activities of the County for the fiscal year ended June 30, 2011. We encourage readers to consider this discussion and analysis in conjunction with our letter of transmittal in the Introductory Section of this report, and the County's financial statements which follow this discussion and analysis.

Financial Highlights

- The assets of the County exceeded its liabilities at the close of fiscal year 2011 by \$338.7 million (*net assets*). Of this amount, \$60.4 million (*unrestricted net assets*) may be used to meet the County's ongoing obligations to citizens and creditors.
- The County's total net assets increased by \$7.9 million, of which the governmental activities increased by \$5.8 million and business-type activities increased by \$2.1 million.
- As of the close of fiscal year 2011, the County's governmental funds reported combined ending fund balances of \$66.0 million, an increase of \$7.5 million from prior year. Of the \$66.0 million total, 89.7% (\$59.2 million) is available for spending at the County's discretion (sum of *committed*, *assigned* and *unassigned fund balances*), while *unspendable and restricted fund balances* were 10.3% or \$6.8 million of the total.
- The General Fund's unassigned fund balance increased \$0.1 million to \$24.6 million, and remained at 12.6% of total General Fund revenues. This exceeds the County's unassigned fund balance policy minimum of 10% of total General Fund revenues. In addition, the General Fund's assigned fund balance increased \$9.7 million to \$19.6 million. The \$9.7 million increase includes an additional \$6.5 million assigned to education, an additional \$1.6 million assigned to fund subsequent five-year financial plans, \$0.3 million assigned to capital projects, and \$1.3 million for other County services.
- The County's total debt decreased by \$702,000 (0.34%) during fiscal year 2011. Two new debt transactions included (1) the issuance by the County of \$17.8 million of general obligation and refunding bonds to finance the final \$12.3 million of public safety, parks and libraries and school capital projects approved by the County's November 2005 referendum and to refund \$5.5 million of prior general obligation debt at a net present value savings of \$120,375, and (2) the issuance of \$17.3 million of revenue and refunding bonds by the Economic Development Authority of Hanover County to provide \$2.3 million to finance the acquisition of a building to be used by the Community Services Board, the Social Services Department, and the Registrar's Office, to refund \$9.8 million of Utility revenue bonds and to refinance \$5.2 million of Literary Fund (School) loans, for a net present value savings of \$720,000. The bonds are limited obligations of the Authority payable from the payments to be made by the County pursuant to a \$17.9 million support agreement with the Authority, of which \$7.4 million is payable by the General Fund and \$10.6 million is payable by the Public Utilities Fund.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the County's basic financial statements. The County's basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Government-wide financial statements: The *government-wide financial statements* are designed to provide readers with a broad overview of the County's finances, in a manner similar to a private-sector business. The *statement of net assets* presents information on all of the County's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of how the financial position of the County may be changing. Increases in net assets may indicate an improved financial position; however, even decreases in net assets may reflect a changing manner in which the County may have used previously accumulated funds.

The *statement of activities* presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the County which are principally supported by taxes, intergovernmental revenues, and other non-exchange transactions (*governmental activities*) from other activities which are intended to recover all or a significant portion of their costs primarily through user fees charged to external parties (*business-type activities*). The governmental activities of the County include general government administration; judicial administration; public safety; public works; human services; parks, recreation and cultural; community development; education; and interest on long-term debt, as well as the County's self-insurance and fleet management activities. The business-type activities consist of public utilities and the airport.

The government-wide financial statements (Exhibits 1 and 2) include not only the County itself (known as the *primary government*), but also a legally separate school board and a legally separate economic development authority for which the County is financially accountable. Financial information for these *component units* is reported separately from the financial information presented for the primary government itself.

Fund financial statements: A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the County can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

With the exception of *internal service fund* activity, (described under *Proprietary Funds which follows*), **Governmental Funds** are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating the County's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the County's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The County maintains five individual governmental funds. Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund, the County Improvements Fund and the School Improvements Fund; all three of which are considered to be *major funds*. Data from the other two County funds, the Comprehensive Services Fund and the Community Services Fund, are combined into a single, aggregated presentation. Individual fund data for each of these *nonmajor* governmental funds is provided in the form of *combining statements* at Exhibits 16 and 17 of this report. The County adopts an annual appropriated General Fund budget, for which a budgetary comparison statement has been provided to demonstrate compliance with this budget. The governmental fund financial statements can be found at Exhibits 3 through 6 of this report.

The County maintains two different types of ***Proprietary Funds***: enterprise and internal service. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The County uses enterprise funds to account for its public utilities fund and its airport fund (a nonmajor fund). *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the County's various functions. The County uses internal service funds to account for its fleet management and its healthcare and other postemployment benefit self-insurance activities. Because both of these services predominantly benefit governmental rather than business-type functions, they have been included within *governmental activities* in the government-wide financial statements.

Proprietary funds provide the same type of information as the business-type activities in the government-wide financial statements, only in more detail. Conversely, both internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for the internal service funds is provided in the form of combining statements elsewhere in this report. The proprietary fund financial statements can be found at Exhibits 7 through 9 of this report.

Fiduciary funds are used to account for resources received and held in a fiduciary capacity for the benefit of individuals, private organizations, or other governments. Fiduciary funds are *not* reflected in the government-wide financial statement because the resources of those funds are *not* available to support the County's own programs. However, the County is responsible for ensuring that fiduciary fund assets are used for their intended purposes. The County's fiduciary funds consist of an employee benefit trust fund, the Retiree Medical Benefits Trust Fund, and Agency Funds. The Retiree Medical Benefits Trust Fund is used to account for the receipt and disbursement of employer contributions and assets held in trust to provide healthcare benefits to retirees, and agency funds are used to report resources held in a purely custodial capacity for individuals, private organizations or other governments. The fiduciary fund financial statements can be found at Exhibits 10 and 11 of this report, while individual fund data for the agency funds can be found in the form of combining statements at Exhibits 23 and 24 of this report.

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

Other information: In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the County’s progress in funding its obligations to provide pension and other postemployment benefits to its current and future retirees. This required supplementary information can be found at Exhibit 12 of this report.

The combining statements referred to earlier in connection with nonmajor governmental funds, internal service funds and agency funds, and individual fund statements and schedules are presented immediately following the required supplementary information, at Exhibits 13 through 32 of this report.

This report also contains a statistical section that supplements the basic financial statements by presenting detailed trend information, to assist the users to assess the economic condition of the County. We encourage our readers to review the statistical section, to better understand the County’s operations, services and financial condition.

Finally, this report contains a compliance section, including the County’s Schedule of Expenditures of Federal Awards and related notes, and the independent auditors’ required reports on compliance and internal control.

Financial Analysis of the County as a Whole

Statement of Net Assets

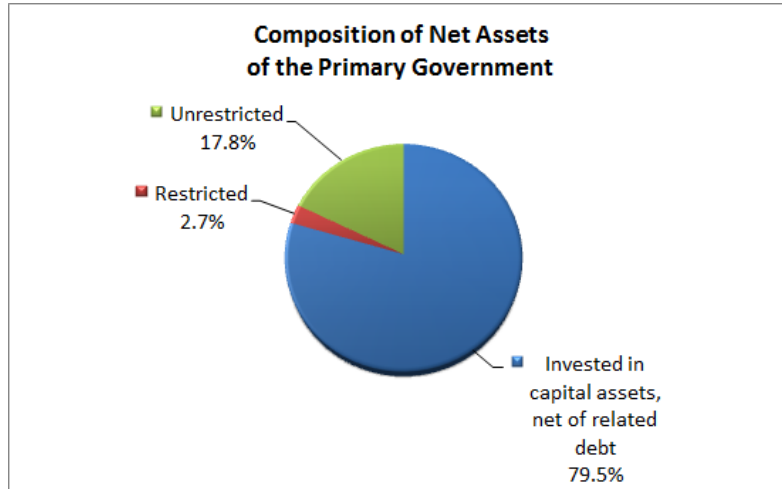
Table 1 summarizes the Statements of Net Assets for the primary government as of June 30, 2011 and 2010:

| Table 1 | County of Hanover, Virginia | | | | | |
|-------------------------------------------------|-----------------------------|----------|-----------------------------|-------|-----------------------------|-------|
| | Summary of Net Assets | | | | | |
| | (\$ in millions) | | | | | |
| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 |
| Current and other assets | \$ 136.4 | \$ 130.0 | 26.1 | 30.7 | 162.5 | 160.7 |
| Capital assets | 243.7 | 242.9 | 211.4 | 207.9 | 455.1 | 450.8 |
| Total assets | 380.1 | 372.9 | 237.5 | 238.6 | 617.6 | 611.5 |
| Long-term liabilities outstanding | 180.5 | 178.9 | 35.0 | 37.5 | 215.5 | 216.4 |
| Other liabilities | 61.5 | 61.7 | 1.9 | 2.6 | 63.4 | 64.3 |
| Total liabilities | 242.0 | 240.6 | 36.9 | 40.1 | 278.9 | 280.7 |
| Net assets: | | | | | | |
| Invested in capital assets, net of related debt | 81.2 | 76.1 | 188.0 | 171.4 | 269.2 | 247.5 |
| Restricted | 5.6 | 6.6 | 3.5 | 3.5 | 9.1 | 10.1 |
| Unrestricted | 51.3 | 49.6 | 9.1 | 23.6 | 60.4 | 73.2 |
| Total net assets | \$ 138.1 | 132.3 | 200.6 | 198.5 | 338.7 | 330.8 |

Over time, changes in net assets may serve as a useful indicator of a County’s financial position. Of interest, the County’s assets exceeded liabilities by \$338.7 million at the close of fiscal year 2011, representing an increase of \$7.9 million from the net assets at June 30, 2010.

As the following graph shows, by far the largest portion of the County’s net assets (\$269.2 million, 79.5% of total) reflects its investment in capital assets (e.g., land, buildings, machinery, equipment and intangibles); less any related debt used to acquire those assets that is still outstanding. The County uses these capital assets to provide services to citizens, like water and wastewater services, schools, libraries, law enforcement, and fire and emergency medical services. Consequently, these net assets are *not* available for future spending, as capital assets are generally not sold or otherwise disposed of during their useful life.

As also shown, an additional portion of the County's net assets (\$9.1 million, 2.7% of total) represents resources that are subject to external restrictions on how they may be used, including amounts restricted for capital projects, grant programs, debt covenants and postemployment healthcare benefits. The remaining balance of unrestricted net assets (\$60.4 million, 17.8% of total) may be used to meet the County's ongoing obligations to citizens and creditors.



Statement of Activities

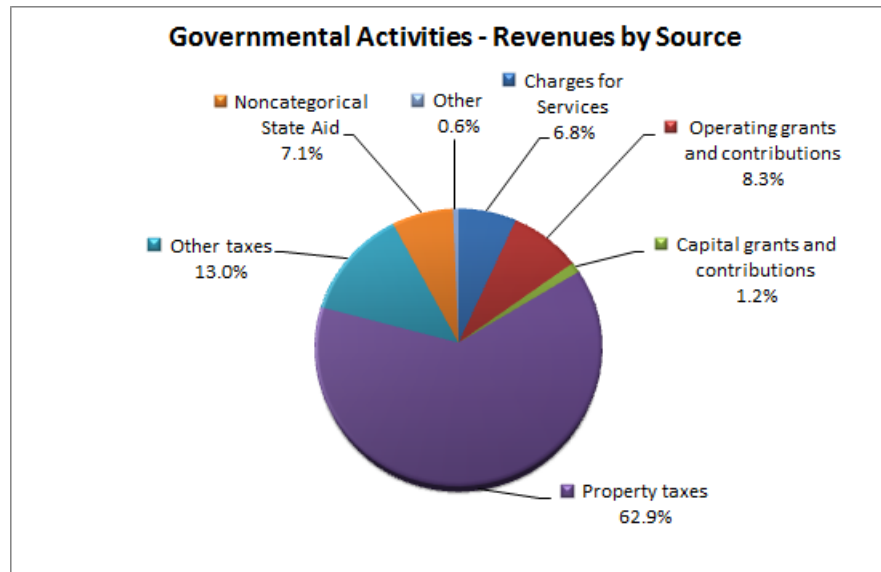
Table 2 summarizes the Statements of Activities of the primary government for the fiscal years ended June 30, 2011 and 2010:

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|-----------------------------------------|-------------------------|--------------|--------------------------|--------------|--------------------------|--------------|
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 |
| Revenues: | | | | | | |
| Program revenues: | | | | | | |
| Charges for services | \$ 13.9 | 12.7 | 22.1 | 21.6 | 36.0 | 34.3 |
| Operating grants and contributions | 17.1 | 16.0 | - | - | 17.1 | 16.0 |
| Capital grants and contributions | 2.5 | 4.5 | 5.3 | 6.0 | 7.8 | 10.5 |
| General revenues: | | | | | | |
| Property taxes | 129.6 | 133.9 | - | - | 129.6 | 133.9 |
| Other taxes | 26.8 | 26.1 | - | - | 26.8 | 26.1 |
| Noncategorical State aid | 14.7 | 14.9 | - | - | 14.7 | 14.9 |
| Grants and contributions | 1.2 | 1.0 | - | - | 1.2 | 1.0 |
| Other | 0.4 | 0.5 | 0.1 | 0.3 | 0.5 | 0.8 |
| Total revenues | 206.2 | 209.6 | 27.5 | 27.9 | 233.7 | 237.5 |
| Expenses: | | | | | | |
| General government | 13.7 | 13.6 | - | - | 13.7 | 13.6 |
| Judicial administration | 4.4 | 4.4 | - | - | 4.4 | 4.4 |
| Public safety | 48.0 | 45.6 | - | - | 48.0 | 45.6 |
| Public works | 9.9 | 11.1 | - | - | 9.9 | 11.1 |
| Human services | 24.2 | 23.9 | - | - | 24.2 | 23.9 |
| Parks, recreation and cultural | 6.4 | 6.5 | - | - | 6.4 | 6.5 |
| Community development | 5.3 | 5.8 | - | - | 5.3 | 5.8 |
| Education | 86.8 | 86.3 | - | - | 86.8 | 86.3 |
| Interest on long-term debt * | 1.5 | 0.8 | - | - | 1.5 | 0.8 |
| Public utilities | - | - | 24.9 | 26.6 | 24.9 | 26.6 |
| Airport | - | - | 0.7 | 0.6 | 0.7 | 0.6 |
| Total expenses | 200.2 | 198.0 | 25.6 | 27.2 | 225.8 | 225.2 |
| Increase in net assets before transfers | 6.0 | 11.6 | 1.9 | 0.7 | 7.9 | 12.3 |
| Transfers | (0.2) | (0.2) | 0.2 | 0.2 | - | - |
| Increase in net assets | 5.8 | 11.4 | 2.1 | 0.9 | 7.9 | 12.3 |
| Net assets - beginning of year | 132.3 | 120.9 | 198.5 | 197.6 | 330.8 | 318.5 |
| Net assets - end of year | \$ 138.1 | 132.3 | 200.6 | 198.5 | 338.7 | 330.8 |

* For business-type activities, interest on long-term debt is included in the functional expense category.

Governmental Activities: As reflected in Table 2, the increase in net assets attributable to the County’s governmental activities totaled \$5.8 million for fiscal year 2011. Generally, net asset changes are the result of the difference between revenues and expenses. Fiscal year 2011 revenues of \$206.2 million represent a decrease of \$3.4 million or 1.7% in comparison to the prior year, while expenses of \$200.2 million represent an increase of \$2.2 million or 1.1% compared to the prior year.

The following chart illustrates the County’s fiscal year 2011 governmental revenues by source as a percentage of total governmental revenues:



Taxes are the largest source of County revenues, totaling \$156.4 million for fiscal year 2011, a decrease of \$3.6 million, or 2.2%, in comparison to fiscal year 2010, primarily due to general property taxes, which fell by \$4.4 million, or 3.3%, largely attributable to lower real property taxes resulting from lower assessed values. This decrease was partially offset by an increase in sales tax revenue of \$0.87 million, or 5.8%. General property taxes totaled \$129.6 million for fiscal year 2011, and represent 82.9% of total taxes and 62.9% of all revenues.

Also in fiscal year 2011, \$33.5 million, or 16.3% of total revenues, consisted of program revenues, including \$13.9 million in charges for services, \$17.1 million of operating grants and contributions, and \$2.5 million of capital grants and contributions. General revenues, including \$14.7 million of noncategorical state aid, unrestricted grants and contributions, and unrestricted investment earnings accounted for the remaining revenues.

As shown in Table 2 (previous page) and Table 3 (following), the total expenses of all the County’s governmental activities for fiscal year 2011 were \$200.2 million, which represents an increase of \$2.2 million, or 1.1% higher than fiscal year 2010, primarily attributable to increased public safety expenses, including an increase of \$0.6 million in the County’s contribution to the Pamunkey Regional Jail due to increased per diem rates, and an increase of \$0.6 million in depreciation expense due to the completion of the County’s new Emergency Communications Center in August 2011, acquisition of emergency communication and dispatch system upgrades and completion of the Ashland and Farrington replacement fire stations in fiscal 2010, and acquisition of replacement fire engine and ambulance vehicles in fiscal years 2010 and 2011. As the following chart indicates, education continues to be the County’s largest program and highest priority, with education expenses totaling \$86.8 million in fiscal year 2011. Public

safety is also a high County priority and the County’s second largest expense, totaling \$48.0 million in fiscal year 2011.

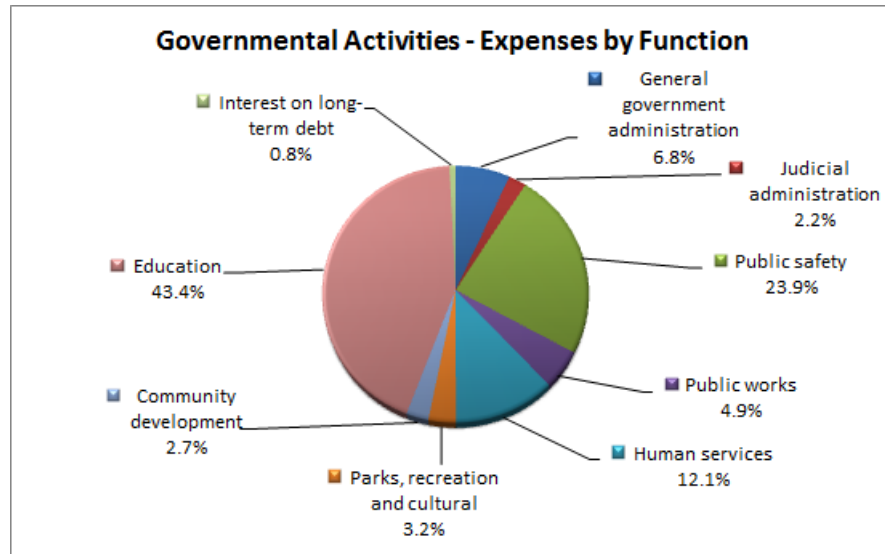


Table 3 presents the total cost of the County’s governmental activities by function, as well as the net cost of each function (total cost less fees generated by each function and program-specific intergovernmental aid):

| Functions/Programs | Total Cost of Services | | Net Cost of Services | |
|--------------------------------|---------------------------|-----------------|-------------------------|-----------------|
| | 2011 | 2010 | 2011 | 2010 |
| General government | \$ 13.7 | \$ 13.6 | \$ 10.8 | \$ 11.1 |
| Judicial administration | 4.4 | 4.4 | 1.8 | 1.6 |
| Public safety | 48.0 | 45.6 | 38.8 | 37.4 |
| Public works | 9.9 | 11.1 | 6.9 | 6.3 |
| Human services | 24.2 | 23.9 | 10.6 | 11.0 |
| Parks, recreation and cultural | 6.4 | 6.5 | 5.6 | 5.9 |
| Community development | 5.3 | 5.8 | 4.5 | 5.0 |
| Education | 86.8 | 86.3 | 86.2 | 85.7 |
| Interest on long-term debt | 1.5 | 0.8 | 1.5 | 0.8 |
| Total | \$ 200.2 | \$ 198.0 | \$ 166.7 | \$ 164.8 |

A portion of the \$200.2 million cost of the County’s governmental activities was paid by those who directly benefited from the programs (i.e., charges for services of \$13.9 million), and other governments and organizations that subsidized certain programs (i.e., operating and capital grants and contributions of \$19.6 million). These combined program revenues of \$33.5 million reduced the total fiscal year 2011 cost of services from \$200.2 million to the net cost of services of \$166.7 million. The net cost of services was covered by the County’s general revenues, consisting primarily of taxes and state aid.

Business-type Activities: Table 2 also summarizes the business-type activities. The County’s business-type activities consist of its Public Utilities water and wastewater treatment services and its airport

activities. The increase in the net assets attributable to the County's business-type activities totaled \$2.1 million for fiscal year 2011, consisting of a \$1.9 million increase attributable to Public Utilities water and wastewater treatment activities, and a \$0.2 million increase attributable to airport activities.

Public Utilities revenues totaled \$26.8 million, of which \$22.0 million, or 82.0%, was generated from charges for services and user fees, up from 77.3% last year, due primarily to lower capital contributions in 2011. Nonoperating capacity fee revenue increased to \$3.6 million from \$2.7 million last year, due to completion of existing projects and new construction. Public Utilities expenses totaled \$24.9 million, compared to \$26.6 million for fiscal year 2010, a decrease of \$1.7 million, or 6.4%. This decrease was primarily due to favorable water and sewer cost of service adjustments received in 2011.

Airport operating revenues totaled \$178,000 in fiscal year 2011, compared to \$171,000 last year, primarily due to increased rental revenue on existing airport facilities. The airport's nonoperating revenues totaled \$622,000 in fiscal year 2011, compared to \$27,000 in fiscal year 2010, primarily due to nonrecurring Federal Airport Improvement Program grant revenue received in 2011 for land acquisition and improvements. Airport nonoperating expenses were \$82,000 and 85,000 in fiscal year 2011 and 2010, respectively.

Financial Analysis of the County's Funds

As noted earlier, the County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds: The focus of the County's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the County's financing requirements. In addition, the County's *fund balance classifications* are useful to identify the extent to which the County's fund balances are constrained and how binding those constraints are.

As of the end of fiscal year 2011, the County's governmental funds reported combined ending fund balances of \$66.0 million (Exhibit 3), as compared to \$58.5 million at June 30, 2010, an increase of \$7.5 million. Of the \$66.0 million fiscal year 2011 fund balance, \$144,000 is classified as *nonspendable* because it is invested in inventories and therefore is not in spendable form, \$6.6 million (10.0%) is classified as *restricted* to indicate that it can only be spent for specific purposes as stipulated by external resource providers (for example, through debt covenants, grant agreements, or by laws or regulations of other governments), \$2.5 million is classified as *committed* to indicate that it has been set aside for specific purposes by resolution of the County's Board of Supervisors, \$32.1 million is *assigned* to indicate that county administration has identified specific purposes for the use of those funds, and the remaining \$24.6 million is *unassigned*. Unassigned fund balances are technically available for any purpose, but are maintained at targeted levels in accordance with sound financial management practices.

The General Fund is the primary operating fund of the County (Exhibits 3 through 6). The General Fund's fund balance increased \$9.8 million (25.9%) during fiscal year 2011, to \$47.3 million, of which \$2.5 million is restricted, \$19.6 million is assigned and \$24.6 million is unassigned. As one measure of the General Fund's liquidity, it is useful to compare the total of the County's committed, assigned and unassigned fund balances to total fund revenues. At the end of fiscal year 2011, the General Fund's committed, assigned and unassigned fund balances of \$46.6 million represents 23.9% of total General Fund revenues of \$195.0 million. In addition General Fund's unassigned fund balance totaled \$24.6 million, up from \$24.5 million at the end of fiscal year 2010, which represents 12.6% of total General Fund revenues in both years, and continues to exceed the 10% minimum set by the County's fund balance

policy. The \$9.8 million fiscal year 2011 increase in the General Fund's fund balance resulted from General Fund revenues of \$195.0 million less expenditures of \$175.7 million and other financing uses of \$9.5 million, and was primarily the result of across-the-board expenditure savings as shown on Exhibit 6 to the financial statements.

The fund balance in the County Improvements Fund (Exhibit 4) increased by \$3.6 million to \$15.1 million during fiscal year 2011 primarily as a result of bond proceeds authorized in the 2005 referendum and other financing sources received in advance of related County capital expenditures.

The fund balance in the School Improvements Fund (Exhibit 4) decreased by \$5.9 million to \$2.8 million during fiscal year 2011, primarily as a result of completion of school capital projects for which funding had been received in prior years.

Proprietary funds: The County's proprietary funds financial statements provide the same type of information presented in the business-type activities on the government-wide financial statements, as their basis of accounting is the same, but in more detail. Factors relating to the financial position and results of operations of the County's Public Utilities System and Airport have been addressed in the discussion of the County's business-type activities.

General Fund Budgetary Highlights

General Fund budget amendments resulted in an increase of \$2.5 million or 1.2% between the originally-adopted fiscal year 2011 budget appropriation for expenditures and transfers out and the final budget, with \$2.1 million of the increase resulting from reappropriation of fiscal year 2010 budget commitments for completion of ongoing projects in fiscal year 2011. Significant reappropriations included:

- \$328,000 for Data Center energy efficient modifications, of which \$312,000 was funded by the American Recovery and Reinvestment Act;
- \$99,000 for Information Technology contingencies;
- \$97,000 for replacement boilers for Judicial Administration buildings;
- \$241,000 for Facilities Management to fund anticipated increases in electrical rates and to fund upgrades to the County phone system;
- \$116,000 for Emergency Communications to continue regional interoperability studies funded by grant revenue;
- \$103,000 for GIS, primarily for data enhancement to the GIS website.

The remaining \$300,000 in budget amendments were funded by various revenue sources or unassigned fund balance. Significant amendments included:

- \$160,000 for firefighter salaries, funded by the Federal SAFER grant;
- \$102,000 for Emergency Communications expenditures related to the award of a Virginia Interoperability Grant to identify and resolve issues related to regional interoperability.

Capital Assets and Debt Administration

Capital assets: The County's investment in capital assets as of June 30, 2011, totals \$455.2 million, net of accumulated depreciation. This represents an increase of \$4.4 million, or 0.9% over fiscal year 2010. Capital assets, net of accumulated depreciation, are illustrated in the following table:

| | (\$ in millions) | | | |
|-----------------------------------|------------------|---------------|-------------------|-------|
| | Governmental | Business-type | Totals at June 30 | |
| | Activities | Activities | 2011 | 2010 |
| Land | \$ 8.8 | 10.9 | 19.7 | 19.1 |
| Intangible assets | 0.7 | - | 0.7 | 0.5 |
| Buildings | 168.8 | 59.9 | 228.7 | 236.2 |
| Improvements other than buildings | 6.4 | 134.8 | 141.2 | 129.8 |
| Machinery and equipment | 24.1 | 2.4 | 26.5 | 17.7 |
| Infrastructure | 15.0 | - | 15.0 | 16.0 |
| Construction in progress | 19.9 | 3.5 | 23.4 | 31.5 |
| Total | \$ 243.7 | 211.5 | 455.2 | 450.8 |

Major capital asset activity during fiscal year 2011 included the following:

- The completion costs of the County's emergency communication and dispatch system upgrades totaling \$10.7 million, funded primarily through the 2005 bond referendum.
- The completion costs of several of the County's park improvement projects totaling \$3.6 million, funded primarily through the 2005 bond referendum.
- The costs of fire apparatus, ambulance and landfill equipment replacement, technology infrastructure, stormwater mitigation and facility renovations totaling \$1.5 million, funded through general revenues.
- The costs of completed and in-progress water and wastewater infrastructure projects reported in the Public Utilities Fund totaling \$11.7 million, funded by water and sewer user fees and capacity fees.
- Developers' contributions of water and wastewater lines totaled \$0.7 million, and developers' conveyance or purchase of drainage, stormwater and access easements totaled \$0.2 million.
- The costs of school facility improvements and equipment acquisition by the School Component Unit totaled \$13.9 million, funded primarily by the 2005 bond referendum, and general revenues.

Additional information on the County's capital assets and capital commitments can be found in notes IV.C and V.C to the financial statements.

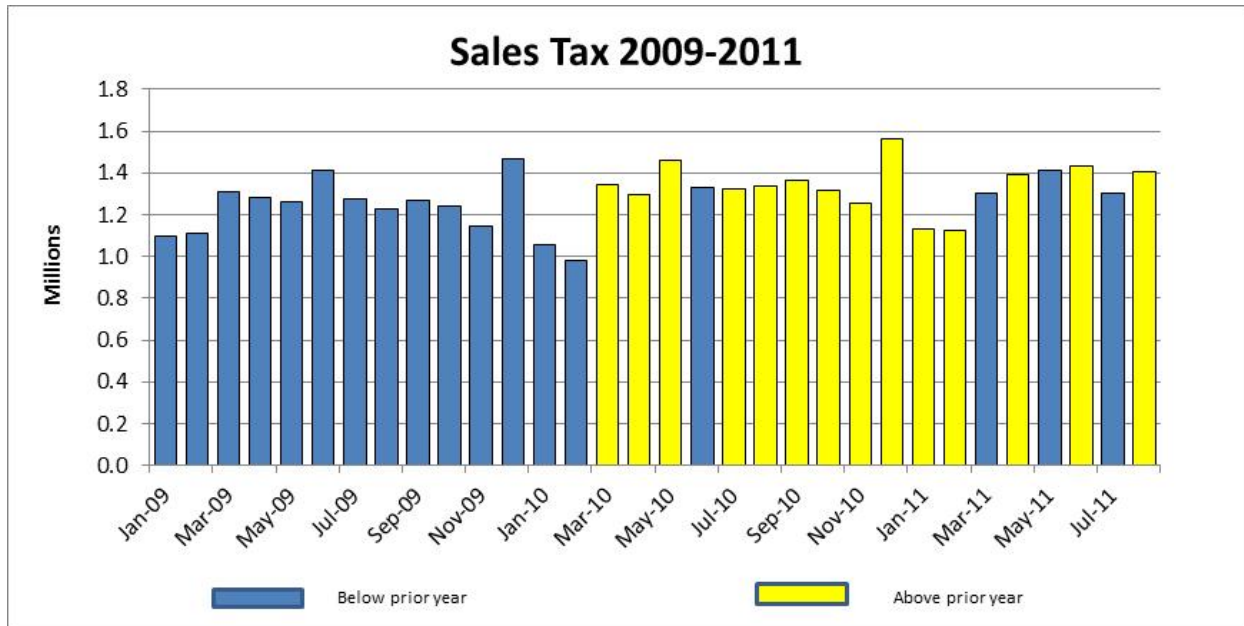
Long-term debt: In the Commonwealth of Virginia, there is no State statute that limits the amount of general obligation debt a County may issue. However, with limited exceptions as described under General Obligation Bonds in Note IV.E to the accompanying financial statements, general obligation bonded indebtedness must be approved by voter referendum prior to issuance. In addition, the County's Board of Supervisors and revenue bond covenants have established limits and coverage requirements with respect to long-term debt, and the County is in compliance with all debt policy limits and debt coverage requirements at June 30, 2011. The following table illustrates the County's outstanding debt at June 30, 2011:

| | (\$ in millions) | | |
|---------------------------|----------------------------|-----------------------------|-------|
| | Governmental Activities | Business-type Activities | Total |
| General obligation bonds | \$ 162.5 | - | 162.5 |
| Revenue bonds | - | 21.9 | 21.9 |
| Support agreement | 7.3 | 10.6 | 17.9 |
| Capital lease obligations | 2.7 | - | 2.7 |
| Total | \$ 172.5 | 32.5 | 205.0 |

Additional information on the County's long-term debt can be found under *Financial Highlights* on the first page of this Management's Discussion and Analysis, and in Note IV.E to the financial statements.

Economic Factors and Next Year's Budgets and Rates

Although with a more modest impact than most of the U.S., during fiscal year 2011 and into 2012, Hanover County has continued to experience, and continues to proactively respond to the effects of the national recession. Throughout fiscal year 2011, the County's unemployment rate continued to show modest but steady improvement over the prior year. In September 2011, the County's unemployment rate was 6.0%, which was 0.2% improved (lower) than the same month a year ago, and which continues to compare favorably to the State's average unemployment rate of 6.4% and the national average rate of 8.8%. Throughout fiscal year 2011, real estate assessment values continued a general decline nationwide. For the four quarters ended June 30, 2011, the Federal Housing Finance Agency's purchase-only house price index, calculated using home sales price information from Fannie Mae- and Freddie Mac-acquired mortgages fell 5.9% for the U.S. and 5.0% for Virginia. In addition, by a measure of total assessed value of real estate, Hanover has fared better in comparison to its regional triple AAA rated peers, experiencing a small increase in its total assessed value of all real estate of 0.9% in fiscal year 2010, compared to drops of 3.8% to 8.1% reported by neighboring triple AAA rated counties. Nevertheless, Hanover has shared in the decline in total real estate assessed valuations in fiscal 2011 and expects to again in 2012, but with comparatively modest declines of 2.2% and 5.4%, respectively. Sales tax revenues have offset a portion of this decline, with actual and expected increases of 5.8% and 3.0% in fiscal years 2011 and 2012, respectively. Indicative of the continuing positive trend in sales tax revenue, the following chart shows that sales tax receipts have exceeded the same-month receipts in the prior year in fourteen of the most recent eighteen months. Personal property tax revenues are also expected to offset a portion of the decline in real property tax revenues, with fiscal year 2012's personal property tax expected to increase by 0.8% over fiscal year 2011 actual revenues due to higher than anticipated new vehicle purchases and moderate vehicle depreciation. State and Federal revenues are budgeted to remain substantially the same in fiscal year 2012. With these factors in mind, net of the use of \$9.0 million of prior year fund balance, the County's adopted fiscal year 2012 General Fund budget was set at \$193.7 million, a decrease of \$0.6 million or 0.3% in comparison to the fiscal year 2011 figure of \$194.3 million. In addition, the County closely monitors and forecasts its revenues on a continual basis, and incorporates any significant changes in its current and subsequent year's budget plans in order to mitigate their impact and maintain the County's sound financial condition.



The County recognizes the value of properly illustrating year-end assignments of fund balance. Accordingly, at June 30, 2011, the County has assigned \$4.4 million of fund balance in its General Fund to fund a portion of the fiscal year 2011 adopted General Fund budget. In this manner, the County is able to utilize and reinvest all or portions of positive budget-to-actual variances at the end of the current fiscal year as a source of funding for the succeeding fiscal year’s budget, while also meeting the County’s fund balance policy and assigning amounts as deemed necessary to meet future needs. Accordingly, the County has assigned an additional \$15.2 million to meet other specifically identified future needs, including \$7.5 million to fund future school budgets, \$0.6 million for public safety, \$5.4 million to fund a portion of the County’s subsequent five-year financial plans, \$0.3 million to fund capital projects, and \$1.4 million to fund other specific purposes. In fiscal year 2010 and prior years, by formal resolution, the Board of Supervisors also committed another \$2.0 million for future school needs and \$0.5 million for economic development, which remains on hand at the end of fiscal year 2011 to fund those additional future needs. All commitments and assignments of fund balance are illustrated in footnote V.B to the accompanying financial statements.

All County general property tax rates remained unchanged for calendar year 2011. In fiscal year 2012, Public Utilities’ user fee increases included a 3.0% rate increase for water, and a 2.0% increase for sewer.

Requests for Information

This financial report is designed to provide a general overview of the County’s finances for all those with an interest in the County’s financial condition and operations. Questions concerning any of the information provided in this report, or requests for additional financial information should be addressed to the Director of Finance and Management Services, County of Hanover, P.O. Box 470, Hanover, VA 23069.