NEW ISSUE – BOOK-ENTRY ONLY **Ratings: see "RATINGS" herein**

DAC Bond

In the opinion of Bond Counsel, under existing statutes, regulations, administrative interpretations and court decisions and subject to conditions described in "TAX MATTERS" herein, interest on the Series 2006 Bonds (a) will not be included in gross income for federal income tax purposes and (b) will not be an "item of tax preference" for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, interest on the Series 2006 Bonds held by certain corporations may be subject to federal income tax under certain circumstances described herein. Under existing law, interest on the Series 2006 Bonds is exempt from personal income taxes imposed by the United States Virgin Islands, by any state, other territory or possession of the United States or any political subdivision thereof, or by the District of Columbia, as described in the section "TAX MATTERS" herein.

$219,490,000
VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY
Revenue Bonds
(Virgin Islands Gross Receipts Taxes Loan Note)
Series 2006

Dated: Date of Delivery **Due:** October 1, as shown on the inside cover

The Series 2006 Bonds (as hereinafter defined) will bear interest at a fixed rate as described herein and are issuable in minimum denominations of $5,000 and integral multiples of $5,000 in excess thereof and will be issued initially as a single registered bond for each maturity registered in the name of Cede & Co., the nominee of The Depository Trust Company ("DTC"), New York, New York. Beneficial ownership interests in the Series 2006 Bonds will be available for purchase in book-entry form only. Except in limited circumstances, purchasers of Series 2006 Bonds will not receive physical delivery of the Series 2006 Bond certificates, as further described herein. Principal of, Redemption Price, if applicable, of, and interest on the Series 2006 Bonds will be paid by the Paying Agent to DTC, who will remit payment to DTC Participants, with such payments to be subsequently disbursed to the beneficial owners of the Series 2006 Bonds, as further described herein. The Series 2006 Bonds will be subject to redemption prior to maturity as described herein. The Bank of New York Trust Company, N.A., located in Jacksonville, Florida, is the Trustee with respect to the Series 2006 Bonds. See "THE SERIES 2006 BONDS."

Interest on the Series 2006 Bonds will be payable semiannually on October 1, and April 1, commencing April 1, 2007.

The Series 2006 Bonds are being issued by the Virgin Islands Public Finance Authority (the "Authority") to (i) refund a portion of the Authority's Revenue Bonds, Series 1999A (Virgin Islands Gross Receipts Taxes Loan Note) (the "Series 1999A Bonds"), (ii) pay the cost of a termination fee in connection with an outstanding swap option agreement, (iii) fund certain necessary public sector capital development projects of the Government of the United States Virgin Islands (the "Government"), (iv) fund the Debt Service Reserve Account in an amount necessary to meet the Debt Service Reserve Requirement, (v) pay the premium in connection with the Series 2006 Bond Insurance Policy, (vi) fund a net payments reserve account for a new swap agreement, and (vii) pay the costs of issuing the Series 2006 Bonds (see "PLAN OF FINANCE"). The Series 2006 Bonds will be issued under and secured by an Indenture of Trust, dated as of November 1, 1999 (as heretofore supplemented and amended, the "Original Indenture"), by and between the Authority and The Bank of New York Trust Company, N.A., as successor trustee (the "Trustee"), and a Seventh Supplemental Indenture of Trust, dated as of September 1, 2006 (the "Seventh Supplemental Indenture" and together with the Original Indenture, the "Indenture"), by and between the Authority and the Trustee. The Trustee will act as Bond Registrar and Paying Agent for the Series 2006 Bonds. The Series 2006 Bonds will be payable from and secured by a pledge of the Trust Estate which includes certain funds established under the Indenture and the 2006 Gross Receipts Taxes Loan Note, Series A (the "Series 2006 Loan Note") issued by the Government of the United States Virgin Islands (the "Government") pursuant to a Loan Agreement, dated as of September 1, 2006 (the "Series 2006 Loan Agreement"), among the Government, the Trustee and the Authority.

THE SERIES 2006 BONDS ARE LIMITED SPECIAL OBLIGATIONS OF THE AUTHORITY PAYABLE FROM AND SECURED BY A PLEDGE OF THE TRUST ESTATE, WHICH INCLUDES CERTAIN FUNDS ESTABLISHED UNDER THE INDENTURE, INCLUDING THE PLEDGED REVENUE ACCOUNT AND THE DEBT SERVICE RESERVE ACCOUNT. THE SERIES 2006 BONDS SHALL UNDER NO CIRCUMSTANCES CONSTITUTE A GENERAL OBLIGATION OF THE AUTHORITY OR OF THE UNITED STATES OF AMERICA. THE AUTHORITY HAS NO TAXING POWER. THE SERIES 2006 LOAN NOTE IS SECURED BY A PLEDGE OF GROSS RECEIPTS TAXES (AS HEREINAFTER DEFINED), IMPOSED AND COLLECTED UNDER THE VIRGIN ISLANDS CODE, AS AMENDED, WHICH PLEDGE SHALL BE SUBJECT TO THE REQUIRED ANNUAL MODERATE INCOME HOUSING FUND DEPOSIT (AS HEREINAFTER DEFINED). THE SERIES 2006 LOAN NOTE WILL CONSTITUTE A GENERAL OBLIGATION OF THE GOVERNMENT FURTHER SECURED BY THE FULL FAITH AND CREDIT AND TAXING POWER OBLIGATION OF THE GOVERNMENT.

As more fully described under "BOND INSURANCE" herein, scheduled payment of the principal of and interest on the Series 2006 Bonds when due will be guaranteed by a municipal bond insurance policy to be issued simultaneously with the delivery of the Series 2006 Bonds by Financial Guaranty Insurance Company.

FGIC

THE PURCHASE AND OWNERSHIP OF THE SERIES 2006 BONDS INVOLVES CERTAIN INVESTMENT RISKS. SEE "BONDOWNER RISKS." INFORMATION CONTAINED ON THIS COVER IS A SUMMARY ONLY. PROSPECTIVE PURCHASERS OF THE SERIES 2006 BONDS ARE ADVISED TO READ THIS OFFICIAL STATEMENT IN ITS ENTIRETY.

Maturity Schedule

(On Inside Cover)

The Series 2006 Bonds are offered, subject to prior sale, when, as and if issued by the Authority and accepted by the Underwriter, subject to the approval of legality by Buchanan Ingersoll & Rooney PC, New York, New York, Bond Counsel, and certain other conditions. Certain legal matters will be passed upon for the Underwriter by its counsel, Duane Morris, LLP, New York, New York. It is expected that the Series 2006 Bonds will be available for delivery to DTC in New York, New York on or about September 28, 2006.

UBS Investment Bank

Dated: September 19, 2006

MATURITY SCHEDULE

$219,490,000
VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY
Revenue Bonds
(Virgin Islands Gross Receipts Taxes Loan Note)
Series 2006

Maturity Date (October 1)	Amount	Interest Rate	Price or Yield
2007	$ 505,000	3.50%	100%
2008	1,490,000	3.50%	3.53%
2009	1,530,000	4.00%	3.55%
2010	1,580,000	4.00%	3.58%
2011	2,705,000	5.00%	3.62%
2012	2,805,000	5.00%	3.66%
2013	2,905,000	5.00%	3.70%
2014	3,015,000	5.00%	3.75%
2015	3,125,000	5.00%	3.80%
2016	3,240,000	5.00%	3.85%
2017	3,360,000	5.00%	3.90%*
2018	3,485,000	5.00%	3.94%*
2019	3,615,000	5.00%	3.98%*
2020	15,865,000	4.00%	4.17%
2021	16,295,000	5.00%	4.06%*
2022	16,895,000	5.00%	4.09%*
2023	17,515,000	5.00%	4.12%*
2024	18,165,000	5.00%	4.14%*
2025	18,840,000	5.00%	4.16%*
2026	19,530,000	5.00%	4.18%*
2027	20,250,000	5.00%	4.20%*
2028	21,000,000	5.00%	4.23%*
2029	21,775,000	4.25%	4.50%

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* Priced to the October 1, 2016 par call date.

VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY

24 Honduras
Frenchtown
St. Thomas, United States Virgin Islands 00802
www.USVIPFA.com
Kent E. Bernier, Sr. Director of Finance and Administration

BOARD OF DIRECTORS

The Honorable Charles W. Turnbull, Governor – Chairman
Bernice A. Turnbull, Commissioner of Finance - Executive Director
Ira R. Mills, Director of the Office of Management and Budget – Secretary
Paul Arnold, St. Croix Representative
Roy Jackson, St. Thomas/St. John Representative

TRUSTEE

The Bank of New York Trust Company, N.A.
Jacksonville, Florida

BOND COUNSEL

Buchanan Ingersoll & Rooney PC
New York, New York

FINANCIAL ADVISOR

Banc of America Securities LLC
New York, New York

UNDERWRITER

UBS Securities LLC
New York, New York

This Official Statement is furnished in connection with the sale of securities as referred to herein and may not be reproduced or be used, in whole or in part, for any other purpose. The information and expressions of opinion herein are subject to change without notice. The delivery of this Official Statement, including the Appendices attached hereto, does not imply that there has not been a change in the affairs of the Authority, the Government or the other matters described herein since the date hereof or that the information herein is correct as of any time subsequent to its date.

No dealer, salesman or any other person has been authorized by the Authority, the Government or the Underwriter to give any information or to make any representation other than as contained in this Official Statement in connection with the offering described herein and, if given, or made, such other information or representation must not be relied upon as having been authorized by the Authority, the Government or the Underwriter. This Official Statement does not constitute an offer of any securities other than those described on the cover page or an offer to sell or a solicitation of any offer to buy, nor shall there be any sale of the Series 2006 Bonds in any jurisdiction in which it is unlawful to make such offer, solicitation or sale.

The information contained in this Official Statement has been obtained from the Authority, the Government and other sources which are believed to be reliable. The Underwriter has reviewed the information in this Official Statement in accordance with, and otherwise has satisfied, its responsibilities under the federal securities laws with respect hereto, but does not guarantee the accuracy or completeness of this Official Statement and it is not to be construed as a representation by the Underwriter or by any of such sources as to information from any other source.

THE SERIES 2006 BONDS HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION, NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR COMPLETENESS OF THIS OFFICIAL STATEMENT. ANY REPRESENTATION TO THE CONTRARY MAY BE A CRIMINAL OFFENSE.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SERIES 2006 BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITER MAY OFFER AND SELL THE SERIES 2006 BONDS TO CERTAIN DEALERS AND DEALER BANKS AND OTHERS AT PRICES LOWER OR YIELDS HIGHER THAN THE PUBLIC OFFERING PRICES OR YIELDS STATED ON THE INSIDE COVER PAGE HEREOF AND SAID PUBLIC OFFERING PRICES OR YIELDS MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITER.

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OFFICIAL STATEMENT

$219,490,000
VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY
Revenue Bonds
(Virgin Islands Gross Receipts Taxes Loan Note)
Series 2006

INTRODUCTION

The purpose of this Official Statement, which includes the cover page, inside front cover page and the appendices, is to furnish certain information concerning the Virgin Islands Public Finance Authority (the "Authority") and the sale and delivery of its Revenue Bonds (Virgin Islands Gross Receipts Taxes Loan Note) Series 2006 (the "Series 2006 Bonds"), in the aggregate principal amount of $219,490,000. The Series 2006 Bonds are being issued pursuant to an Indenture of Trust, dated as of November 1, 1999 (as heretofore supplemented and amended, the "Original Indenture"), by and between the Authority and The Bank of New York Trust Company, N.A., Jacksonville, Florida, as successor trustee (together with any appointed successor trustee, the "Trustee"), as supplemented by a Seventh Supplemental Indenture of Trust, dated as of September 1, 2006 (the "Seventh Supplemental Indenture" and together with the Original Indenture, the "Indenture"), by and between the Authority and the Trustee. The Series 2006 Bonds are being issued pursuant to Sections 1574 through 1574c of the United States Virgin Islands Revised Organic Act of 1954, as amended (48 U.S.C. §§ 1541 *et seq.*) (the "Revised Organic Act"), Title 29 of the Virgin Islands Code, 2002 United States Virgin Islands Act No. 6514, as amended by 2002 United States Virgin Islands Act No. 6533, (collectively with the Revised Organic Act, the "Act"), and Resolution No. 06-007, adopted by the Authority on June 7, 2006 (the "Resolution") and other applicable law. All capitalized terms not defined in this Official Statement have meanings as defined in Appendix A entitled "Glossary of Certain Defined Terms."

The proceeds of the Series 2006 Bonds will be loaned to the Government of the United States Virgin Islands (the "Government") pursuant to the Loan Agreement, dated as of September 1, 2006 (the "Series 2006 Loan Agreement"), by and among the Authority, the Government and the Trustee. Proceeds from the Series 2006 Bonds will be used to: (i) refund a portion of the Authority's Revenue Bonds, Series 1999A (Virgin Islands Gross Receipts Taxes Loan Note) (the "Series 1999A Bonds"), (ii) pay the cost of a termination fee in connection with an outstanding swap option agreement, (iii) fund certain necessary public sector capital development projects of the Government of the United States Virgin Islands (the "Government"), (iv) fund the Debt Service Reserve Account in an amount necessary to meet the Debt Service Reserve Requirement, (v) pay the premium in connection with the Series 2006 Bond Insurance Policy, (vi) fund a net payments reserve account for a new swap agreement, and (vii) pay the costs of issuing the Series 2006 Bonds.

The Series 2006 Bonds are payable from and secured by a pledge of the Trust Estate, which includes certain funds established under the Original Indenture, the Seventh Supplemental Indenture and the 2006 Gross Receipts Taxes Loan Note, Series A issued by the Government pursuant to the Series 2006 Loan Agreement pledged to secure the Series 2006 Bonds (the "Series 2006 Loan Note"). The Series 2006 Loan Note is secured by a pledge of the Gross Receipts Taxes. The Series 2006 Loan Note is further secured by the full faith and credit and taxing power of the Government. The Government is obligated under the Series 2006 Loan Note to make payments to the Authority in amounts sufficient to pay all principal, premium, if any, and interest on the Series 2006 Bonds when due, to cause the amount on deposit in the Debt Service Reserve Account to equal the Debt Service Reserve Requirement pursuant to the terms of the Indenture and to pay all other amounts payable by the Authority under the Series 2006 Bonds or the Indenture. See "SECURITY FOR THE SERIES 2006 BONDS." The Series 2006 Bonds are the sixth series of obligations to be issued under the Original Indenture. The Series 2006 Bonds are being issued on a parity with and shall be entitled to the same benefit and security of the Indenture as the outstanding Series 1999A Bonds and the Authority's Revenue Bonds, Series 2003A (Virgin Islands Gross Receipts Taxes Loan Note) (the "Series 2003A Bonds") and any additional bonds which may hereafter be issued under the Indenture. See

"VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY — Outstanding Indebtedness under the Indenture." The Gross Receipts Taxes over the full term of the Series 2006 Loan Note are anticipated to be sufficient to pay all of the principal of, and premium, if any, and interest on, (i) the Series 2006 Loan Note, (ii) the Gross Receipts Taxes Loan Note (the "Series 1999A Loan Note") issued by the Government pursuant to a Loan Agreement, dated as of November 1, 1999, among the Government, the Trustee and the Authority (the "Series 1999A Loan Agreement") and (iii) the Gross Receipts Taxes Loan Note (the "Series 2003A Loan Note") issued by the Government pursuant to a Loan Agreement, dated as of December 1, 2003, among the Government, the Trustee and the Authority (the "Series 2003A Loan Agreement") and (iv) other Bonds and any other parity indebtedness when due. However, no assurances can be given as to the sufficiency of Gross Receipts Taxes for such purpose. Pursuant to Title 33 of the Virgin Islands Code, Section 43 (the "Gross Receipts Tax Statute"), Gross Receipts Taxes are those revenues received by the Government from the payment by individuals and entities doing business in the United States Virgin Islands (the "Virgin Islands") currently at a tax rate of 4.0% on the gross receipts of such business. The Gross Receipts Tax is broad and extends to most sellers of services and goods. According to the Gross Receipts Tax Statute, "gross receipts" means "all receipts, cash or accrued, of the taxpayer for services or derived from trade, business, commerce or sales, and the value accruing from the sale of tangible personal property or services, or both, including rentals, fees and other involvements, however designated, without any deduction on account of the cost of the property sold, the cost of materials used, labor cost, royalties, taxes, interest or discount paid, and any other expenses whatsoever." Certain businesses are exempt from the application of the Gross Receipts Tax. In Fiscal Year 2005, the Government reported Gross Receipts Taxes deposited with the Collecting Agent (as hereinafter defined) of approximately $125.0 million, such collections constituting approximately 17.8% of the Government's general fund (budgetary basis) revenues. In Fiscal Year 2004, the Government reported Gross Receipts Taxes deposited with the Collecting Agent (as hereinafter defined) of approximately $113.2 million, such collections constituting approximately 18.2% of the Government's general fund (budgetary basis) revenues. In Fiscal Year 2003, the Government reported Gross Receipts Taxes deposited with the Collecting Agent (as hereinafter defined) of approximately $100.9 million, such collections constituting approximately 19.7% of the Government's general fund (budgetary basis) revenues.

The proceeds of the Gross Receipts Taxes are paid to the Virgin Islands Bureau of Internal Revenue (the "BIR") for deposit into the General Fund of the Government; except that the first $250,000 of such tax collected during each Fiscal Year is required to be deposited into the Moderate Income Housing Fund pursuant to Title 33 of the Virgin Islands Code, Section 3027(a)(3) (the "Required Annual Moderate Income Housing Fund Deposit"). Pursuant to authority granted by the United States Virgin Islands Legislature (the "Legislature"), the Government has entered into an agreement with the Authority and The Bank of New York Trust Company, N.A., Jacksonville, Florida, as the special escrow agent (the "Special Escrow Agent"), dated as of November 1, 1999 and amended as of February 28, 2003, and as amended as of September 1, 2006 (collectively, the "Special Escrow Agreement"), providing for the deposit of Gross Receipts Tax collections by the Government in the Special Escrow Account maintained by Banco Popular de Puerto Rico, as the collecting agent (the "Collecting Agent"), as agent of the Special Escrow Agent. See "SECURITY FOR THE SERIES 2006 BONDS" and "GROSS RECEIPTS TAXES."

This Official Statement describes, among other items, the Series 2006 Bonds, the Original Indenture, the Seventh Supplemental Indenture, the Series 2006 Loan Agreement, the Series 2006 Loan Note, the Special Escrow Agreement, the Collecting Agent Agreement (as hereinafter defined), the Gross Receipts Taxes, the Authority, the Government and the Virgin Islands. The descriptions do not purport to be comprehensive or definitive and reference is made to the Original Indenture, the Seventh Supplemental Indenture, the Series 2006 Loan Agreement, the Series 2006 Loan Note, the Special Escrow Agreement and the Collecting Agent Agreement for full and complete statements of the provisions thereof. Copies of the Original Indenture, the Seventh Supplemental Indenture, the Series 2006 Loan Agreement, the Special Escrow Agreement and the Collecting Agent Agreement, including the form of the Series 2006 Bonds and the Series 2006 Loan Note, are available at the offices of the Trustee, 10161 Centurion Parkway, Jacksonville, Florida, 32256 (904-645-1912), and at the offices of the Authority, 24 Honduras, Frenchtown, St. Thomas, United States Virgin Islands 00802 (340-714-1635); Attention: Director of Finance and Administration.

THE PURCHASE AND OWNERSHIP OF THE SERIES 2006 BONDS INVOLVE INVESTMENT RISKS. PROSPECTIVE PURCHASERS OF THE SERIES 2006 BONDS ARE ADVISED TO READ THIS OFFICIAL STATEMENT IN ITS ENTIRETY. FOR A DISCUSSION OF CERTAIN RISKS RELATING TO THE SERIES 2006 BONDS, SEE "BONDOWNER RISKS" HEREIN.

VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY

Purposes and Powers

The Authority was created in 1988 by United States Virgin Islands Act No. 5365 of the Legislature, as amended, as a public corporation and autonomous governmental instrumentality for the purposes of aiding the Government in the performance of its fiscal duties and in effectively carrying out its governmental responsibility of raising capital for essential public projects. Under its enabling legislation, the Authority is vested with, but not limited to, the following powers: (i) to have perpetual existence as a corporation, (ii) to borrow money and issue bonds, (iii) to lend the proceeds of its bonds or other money to the Government or any agency, authority or instrumentality thereof or private enterprise in the Virgin Islands subject to the approval of the Legislature, (iv) to establish one or more revolving loan funds with the proceeds of bonds issued by the Authority or issued by the Government or any agency, authority or instrumentality thereof, (v) to encourage economic development through the issuance of special obligations issued to finance a project for the benefit of private parties which special obligations are payable out of revenue generated by the involved project and are payable to the Authority by said private party, (vi) to invest its funds and to arrange for the investment of the funds of the Government or any agency, authority or instrumentality thereof, (vii) to enter into contracts and agreements with the government of the United States, the Government and any agency, authority or political subdivision thereof, (viii) to make, modify and repeal by-laws, rules and regulations, (ix) to acquire, sell, lease, mortgage, pledge, dispose of or encumber property or interests therein and (x) to sue and be sued.

Management

The powers of the Authority are exercised by a board of directors (the "Board of Directors") consisting of five members. The Governor of the Virgin Islands (the "Governor"), the Commissioner of Finance, and the Director of the Office of Management and Budget of the Virgin Islands are members and serve ex-officio. The two remaining members are appointed by the Governor with the advice and consent of the Legislature and represent the private sector. Of these two members, one must be a resident of the District of St. Thomas/St. John and one must be a resident of the District of St. Croix. Both must be experienced in the area of municipal finance. The Governor serves as Chairman of the Board of Directors while the Commissioner of Finance serves as the Authority's Executive Director and the Director of the Office of Management and Budget serves as Secretary to the Authority.

Kent E. Bernier, Sr. serves as the Director of Finance and Administration of the Authority and is responsible for the administration and operation of the Authority. The Director of Finance and Administration is appointed by, and serves at the pleasure of, the Board of Directors.

The following is a list of the current Board of Directors with their official posts or, for private sector representatives, their island of residency, and date of expiration of their current terms on the Board of Directors. The Governor of the Virgin Islands, the Commissioner of Finance and the Director of the Office of Management and Budget serve terms which are coincident with their terms in such offices. The Directors who represent the private sector serve 4-year terms.

Name	Government Post or Profession/Residency	Term Expiration
Hon. Charles W. Turnbull, Ph.D., Chairman	Governor of the Virgin Islands	Ex-officio
Bernice A. Turnbull, Executive Director	Commissioner of Finance	Ex-officio
Ira R. Mills, Secretary	Director of the Office of Management and Budget	Ex-officio
Paul Arnold	Human Resources Consultant, St. Croix	2001†
Roy Jackson	Certified Public Accountant, St. Thomas	2001†

† Members serve until the appointment and confirmation of a successor.

Outstanding Indebtedness under the Indenture

Parity Bonds/Subordinate Bonds

The Authority has issued its $299,880,000 Revenue Bonds, Series 1999A and $268,020,000 Revenue Bonds, Series 2003A, a total of $538,710,000 of which is outstanding as of September 10, 2006, including the hereinafter defined Refunded Bonds. Such Series 1999A and Series 2003A Bonds are equally secured and on a parity with and entitled to the same benefits as the Series 2006 Bonds and constitute "Bonds" under the Indenture. See also "Swap Agreements" below for a discussion of the swap entered into by the Authority with respect to a portion of the Series 2006 Bonds.

The Authority also has outstanding as of September 10, 2006 $4,317,275 principal amount of Subordinate Lien Revenue Notes, Series 2005 and $4,000,000 principal amount of Subordinate Lien Revenue Notes, Series 2006.

For a listing of the Authority's other bonds and similar obligations outstanding as of September 10, 2006, see "UNITED STATES VIRGIN ISLANDS – Outstanding Bonds and Similar Obligations."

Swap Agreement

In 2003 the Authority entered into a swap option agreement (the "2003 Swap Agreement") related to certain maturities of its 1999 Bonds, with a view to refunding such maturities in 2010. In exchange for an upfront payment made to the Authority by the provider of the 2003 Swap Agreement in 2003, the Authority agreed to issue a series of bonds in 2010 to refund such maturities of the 1999 Bonds. Because such 1999 Bonds are being refunded upon the issuance of the Series 2006 Bonds, the Authority has decided to terminate the 2003 Swap Agreement, which termination necessitates a payment to the provider of the 2003 Swap Agreement. See "PLAN OF FINANCE – Use of Proceeds of the Series 2006 Bonds."

In conjunction with the Series 2006 Bonds, the Authority will enter into a Swap Agreement with UBS AG (the "Counterparty"), with a notional amount of $219,490,000, maturing on October 1, 2029. The first payment on the swap will occur on October 1, 2007. Under the terms of the Swap Agreement, the Authority will pay a floating rate equivalent to the BMA short-term index and receive from the Counterparty a floating rate equal to 67.03% of the 10-year LIBOR rate.

Audited Financial Statements

Audited financial statements of the Authority for the fiscal year ended September 30, 2005 are available from the Authority, the nationally recognized municipal securities information repositories, and Digital Assurance Certification, L.L.C., the dissemination agent responsible for maintaining Authority and the Government compliance with their respective continuing disclosure agreements for the Series 2006 Bonds. See "CONTINUING DISCLOSURE; DISCLOSURE DISSEMINATION."

Department of the Interior Report

In November 2002, the Office of Inspector General ("OIG") of the United States Department of the Interior ("DOI") issued a report (the "PFA Report") which stated that while the Authority had effectively raised capital through the issuance of bonds, in reference to bonds issued from 1989-1992, it did not effectively manage bond proceeds. The Authority has administrative procedures in place and staff dedicated to project management to ensure timely expenditures of bond proceeds by monitoring the letting of contracts and the processing of requisitions.

PLAN OF FINANCE

Use of Proceeds of the Series 2006 Bonds

Upon delivery of the Series 2006 Bonds, the net proceeds of the Series 2006 Bonds will be loaned to the Government. The Government has covenanted in the Series 2006 Loan Agreement to immediately deposit, or cause the Authority to deposit, all such proceeds into the Funds and Accounts held by the Trustee or the Escrow Agent pursuant to the Indenture or the Escrow Agreement and apply such proceeds in accordance with the Indenture or the Escrow Agreement.

Proceeds of the Series 2006 Bonds will be (i) transferred into the Escrow Fund to be applied to redeem a portion of the Series 1999A Bonds, (ii) applied to pay the costs associated with terminating the 2003 Swap Agreement, (iii) deposited to the Series 2006 Project Subaccount to be applied to the payment of the costs related to the Series 2006 Projects (as described below), (iv) deposited to the Debt Service Reserve Account to meet the Debt Service Reserve Requirement, (v) applied to pay the premium on the 2006 Bond Insurance Policy, (vi) deposited to the Net Payments Reserve Account, and (vii) deposited to the Series 2006 Cost of Issuance Subaccount of the Cost of Issuance Account to pay the costs associated with the issuance of the Series 2006 Bonds.

The Series 1999A Bonds to be redeemed consist of the term bonds due October 1, 2024 and October 1, 2029 ("the Refunded Bonds") at the Principal Amounts, Redemption Dates and Redemption Prices (expressed as a percentage of principal) as detailed below:

Maturity Date	Principal Amount	Redemption Date	Redemption Price
October 1, 2024	$69,015,000	October 1, 2010	101%
October 1, 2029	$93,855,000	October 1, 2010	101%

Pursuant to the terms of an Escrow Trust Agreement (the "Escrow Agreement") to be entered into between the Government, the Authority, and the Trustee, as Trustee and as Escrow Agent (the "Escrow Agent"), the refunding of the Refunded Bonds will be effected by depositing with the Escrow Agent proceeds of the Series 2006 Bonds and certain other moneys which will be used to purchase certain noncallable direct obligations of the United States of America (the "Government Obligations"). The Government Obligations will bear interest at such rates and will be scheduled to mature at such times and in such amounts so that, when paid in accordance with their respective terms and together with certain other available amounts, sufficient moneys will be available to pay the principal or respective redemption prices, as applicable, of, and the interest on, the Refunded Bonds when due on and prior to the respective maturity or redemption dates therefor, as set forth in the table above. Principal of and interest on the Government Obligations will be held in trust in one or more separate accounts of a fund created under the Escrow Agreement (the "Escrow Fund") and used solely for the payment of the interest on and the principal or respective redemption prices, as applicable, of the Refunded Bonds, as set forth above.

Upon issuance of the Series 2006 Bonds and compliance with the requirements of the Indenture with respect to defeasance, the Refunded Bonds will be deemed paid within the meaning of the Indenture and, except for the rights of the holders of the Refunded Bonds to payments from the Escrow Account, the Refunded Bonds will no longer be entitled to any lien, benefit or security under the Indenture and all covenants, agreements and obligations of Authority to the holders of the Refunded Bonds will be discharged and satisfied. The refunding will result in removal of the Refunded Bonds from the Authority and Government financial statements.

The accuracy of the mathematical computations of the adequacy of the principal of and interest on the Government Obligations to provide for the payment when due of the interest on and the principal or respective redemption prices, as applicable, of the Refunded Bonds will be verified at the time of delivery of the Series 2006 Bonds by Causey Demgen & Moore Inc., independent certified public accountants. See "VERIFICATION OF MATHEMATICAL COMPUTATIONS" herein.

The estimated sources and uses of the proceeds of the Series 2006 Bonds and certain other amounts derived from the Indenture are expected to be as follows:

Sources	
Principal Amount of the Series 2006 Bonds	$ 219,490,000.00
Debt Service Account	5,117,296.88
Net Original Issue Premium	11,572,151.35
Total	**$ 236,179,448.23**
Uses	
Series 1999A Bonds Escrow Fund deposit	$ 180,242,465.31
2003 Swap Agreement termination payment	26,910,000.00
Series 2006 Project Subaccount deposit	14,000,000.00
Debt Service Reserve Account deposit	2,863,300.00
Net Payments Reserve Account deposit	2,911,257.43
Series 2006 Cost of Issuance Subaccount(1) deposit	9,252,425.49
Total	**$ 236,179,448.23**

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(1) The Costs of Issuance of the Series 2006 Bonds include legal fees, Trustee fees, financial advisor fees, bond insurance premium, underwriter's discount and other costs incurred in connection with the issuance of the Series 2006 Bonds.

Description of the Series 2006 Capital Projects

The capital projects of the Government to be financed in whole or in part from Series 2006 Bond proceeds are expected to be as follows: (i) construction of a new library on St. Thomas, (ii) construction of Annaly Bay Road, St. Croix and (iii) infrastructure work at Gallows Bay, St. Croix (collectively, the "Series 2006 Capital Projects").

THE SERIES 2006 BONDS

General

The Series 2006 Bonds will be dated the date of delivery thereof, and will bear interest at the rates and will mature on the dates set forth on the inside cover of this Official Statement. For a more complete description of the Series 2006 Bonds and the basic documentation pursuant to which they were issued, see "THE SERIES 2006 BONDS," APPENDIX B — "Summary of Certain Provisions of the Original Indenture and the Seventh Supplemental Indenture " and APPENDIX C "Summary of Certain Provisions of the Series 2006 Loan Agreement." The Series 2006 Bonds are subject to redemption at the times and in the manner set forth below in "THE SERIES 2006 BONDS — Redemption." Pursuant to the Indenture, the Authority has appointed The Bank of New York Trust Company, N.A., Jacksonville, Florida (as successor to The Bank of New York, New York, New York), as Trustee, and as the Paying Agent and Bond Registrar. Interest on the Series 2006 Bonds will be payable to Cede & Co., or such other owner of record as shown in the registration books of the Authority maintained by the Paying Agent as Bond Registrar.

The Series 2006 Bonds will be issued only in fully registered form, in denominations of $5,000 and any integral multiple thereof and shall mature on the dates and in the principal amounts and bear interest at the rates as set forth on the inside cover of this Official Statement. Interest on the Series 2006 Bonds is payable semiannually on October 1 and April 1 of each year commencing April 1, 2007 (each, an "Interest Payment Date") and shall be calculated on the basis of a 360-day year consisting of twelve 30-day months.

Redemption

Optional Redemption

The Series 2006 Bonds maturing on or prior to October 1, 2016 are not subject to optional redemption. The Series 2006 Bonds maturing after October 1, 2016 shall be subject to redemption at the option of the Authority prior to their stated maturity, on or after October 1, 2016, in whole or in part at the principal amount thereof, together with the interest accrued to the date fixed for redemption, at any time from such maturities as the Authority shall determine, and otherwise by lot within a maturity, from any funds available therefore.

Selection; Notice of Redemption

In the event of any redemption of less than all of any Series 2006 Bonds and the Authority does not select the maturities to be so redeemed, or of less than all of the Series 2006 Bonds of the same maturity, portions of the Series 2006 Bonds of such Series and maturity to be redeemed will be selected at random by the Trustee in such manner as the Trustee in its discretion may deem fair and appropriate; provided, however, that the portion of any of the Series 2006 Bonds of a denomination greater than $5,000 to be redeemed shall be in the minimum principal amount of $5,000, or an integral multiple of $5,000 in excess thereof. In selecting portions of such Bonds for redemption, the Trustee shall treat each such Bond as representing that number of Bonds of $5,000 denomination which is obtained by dividing the principal amount of such Bond to be redeemed in part by $5,000 and integral multiples of $5,000 in excess thereof; provided, however, notwithstanding the foregoing, the Trustee shall revise the Bonds or portions thereof to be redeemed as determined by the foregoing, in any manner deemed by the Trustee in its sole judgment to be fair and reasonable, so that no Bond Outstanding following any redemption shall be in a principal amount less than an authorized denomination therefor. Notice of any such redemption will be mailed by the Trustee not more than 60 nor less than 30 days prior to the date fixed for the redemption thereof or such shorter period as shall be acceptable to the Trustee, to each registered holder of the Series 2006 Bonds selected for redemption. The Authority, so long as a book-entry method is used for the Series 2006 Bonds, will send any such notice of redemption only to DTC (see APPENDIX F — "DTC Book-Entry-Only System").

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DEBT SERVICE REQUIREMENTS FOR THE BONDS

The debt service on the Bonds for the annual period ending October 1 in each of the years to maturity is as follows:

Year	Outstanding Bonds Debt Service	Series 2006 Bonds Principal	Series 2006 Bonds Interest	Series 2006 Bonds Total Debt Service	Total Debt Service on the Bonds
2007	$ 28,299,150.00	$ 505,000.00	$ 10,679,775.11	$ 11,184,775.11	$ 39,483,925.11
2008	28,295,593.76	1,490,000.00	10,573,837.50	12,063,837.50	40,359,431.26
2009	28,294,518.76	1,530,000.00	10,521,687.50	12,051,687.50	40,346,206.26
2010	28,294,681.26	1,580,000.00	10,460,487.50	12,040,487.50	40,335,168.76
2011	28,294,756.26	2,705,000.00	10,397,287.50	13,102,287.50	41,397,043.76
2012	28,294,943.76	2,805,000.00	10,262,037.50	13,067,037.50	41,361,981.26
2013	28,297,762.50	2,905,000.00	10,121,787.50	13,026,787.50	41,324,550.00
2014	28,295,868.76	3,015,000.00	9,976,537.50	12,991,537.50	41,287,406.26
2015	28,297,100.00	3,125,000.00	9,825,787.50	12,950,787.50	41,247,887.50
2016	28,297,675.00	3,240,000.00	9,669,537.50	12,909,537.50	41,207,212.50
2017	28,294,893.76	3,360,000.00	9,507,537.50	12,867,537.50	41,162,431.26
2018	28,295,943.76	3,485,000.00	9,339,537.50	12,824,537.50	41,120,481.26
2019	28,297,543.76	3,615,000.00	9,165,287.50	12,780,287.50	41,077,831.26
2020	16,176,300.00	15,865,000.00	8,984,537.50	24,849,537.50	41,025,837.50
2021	16,176,525.00	16,295,000.00	8,349,937.50	24,644,937.50	40,821,462.50
2022	16,176,000.00	16,895,000.00	7,535,187.50	24,430,187.50	40,606,187.50
2023	16,179,750.00	17,515,000.00	6,690,437.50	24,205,437.50	40,385,187.50
2024	16,172,500.00	18,165,000.00	5,814,687.50	23,979,687.50	40,152,187.50
2025	16,174,000.00	18,840,000.00	4,906,437.50	23,746,437.50	39,920,437.50
2026	16,173,000.00	19,530,000.00	3,964,437.50	23,494,437.50	39,667,437.50
2027	16,173,750.00	20,250,000.00	2,987,937.50	23,237,937.50	39,411,687.50
2028	16,175,250.00	21,000,000.00	1,975,437.50	22,975,437.50	39,150,687.50
2029	16,176,500.00	21,775,000.00	925,437.50	22,700,437.50	38,876,937.50
2030	38,531,500.00				38,531,500.00
2031	38,531,500.00				38,531,500.00
2032	38,532,250.00				38,532,250.00
2033	38,529,750.00				38,529,750.00

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SECURITY FOR THE SERIES 2006 BONDS

General

The Series 2006 Bonds are payable from and secured by a pledge of the Trust Estate which includes certain Accounts established under the Indenture and the Series 2006 Loan Note. The Series 2006 Loan Note is secured by a pledge of the Gross Receipts Taxes to the extent hereinafter described, and is a general obligation of the Government further secured by the full faith and credit and taxing power of the Government.

Pursuant to the Indenture, the Trust Estate relating to the Series 2006 Bonds includes: (i) moneys deposited or required to be deposited relating to the Bonds in the Pledged Revenue Account, the Debt Service Account and the Debt Service Reserve Account pursuant to the provisions of the Indenture, including all right, title, and interest in and to the investments held in the Debt Service Account, the Debt Service Reserve Account and any Credit Facility held in a Debt Service Reserve Account pursuant to the provisions of the Indenture; (ii) the Series 1999A Loan Note, the 2003A Loan Note and the Series 2006 Loan Note, and the proceeds and collections therefrom, including all right, title and interest of the Authority in the Revenues, including, but not limited to, the Gross Receipts Taxes;

(iii) all right, title and interest of the Authority in the Series 1999A Loan Agreement, the Series 2003A Loan Agreement and Series 2006 Loan Agreement; (iv) all right, title and interest of the Authority in and to the proceeds of the Series 2006 Bonds, or such other moneys required to be deposited in the Series 2006 Project Subaccount of the Project Account; and (v) any and all other property or security interest therein, of every name and nature from time to time hereafter by delivery or by writing of any kind granted, bargained, sold, conveyed, transferred, mortgaged, pledged and assigned as and for additional security under the Indenture.

THE SERIES 2006 BONDS ARE LIMITED AND SPECIAL OBLIGATIONS OF THE AUTHORITY. PRINCIPAL, PREMIUM, IF ANY, AND INTEREST ON THE SERIES 2006 BONDS ARE PAYABLE FROM THE PROCEEDS OF REPAYMENT OF THE SERIES 2006 LOAN NOTE AND AMOUNTS PLEDGED PURSUANT TO THE INDENTURE AS DESCRIBED HEREIN. THE SERIES 2006 BONDS DO NOT CONSTITUTE A GENERAL OBLIGATION OF THE AUTHORITY OR OF THE UNITED STATES OF AMERICA. THE AUTHORITY HAS NO TAXING POWER.

THE SERIES 2006 LOAN NOTE IS SECURED BY A PLEDGE OF THE GROSS RECEIPTS TAXES SUBJECT TO THE REQUIRED ANNUAL MODERATE INCOME HOUSING FUND DEPOSIT. THE SERIES 2006 LOAN NOTE ALSO IS A GENERAL OBLIGATION OF THE GOVERNMENT. THE SERIES 2006 LOAN NOTE DOES NOT CONSTITUTE A GENERAL OBLIGATION OF THE UNITED STATES OF AMERICA, NOR SHALL THE UNITED STATES OF AMERICA BE LIABLE THEREON.

The Authority shall at all times, to the extent permitted by law, defend, preserve and protect the pledge of the Trust Estate under the Indenture and all rights of the owners of the Series 2006 Bonds (the "Bondowners") under the Indenture against all claims and demands of all third parties. Further, the Authority shall cause the Government to maintain and abide by its covenants contained in the Act, the Series 2006 Loan Agreement and the Special Escrow Agreement not to limit, restrict or in any way impair the imposition, collection, transfer or disbursement of the Gross Receipts Taxes, subject to permitted tax exemptions, until the principal of, and premium, if any, and interest on all the Bonds and any parity indebtedness permitted under the Series 2006 Loan Agreement and the Indenture have been fully paid or discharged. In the event that the Gross Receipts Tax collections during any period of 12 consecutive months are less than 150% of maximum annual debt service on all Outstanding Bonds and any parity indebtedness permitted under the Series 2006 Loan Agreement and the Indenture, the Government has covenanted to use its best efforts to pledge an additional stream of revenues (the "Substitute Revenues") to repay the Series 2006 Loan Note. Any pledge of Substitute Revenues will remain in effect until such time as Gross Receipts Tax collections are increased for a period of at least 12 consecutive months thereafter to an amount that equals or exceeds 150% of maximum annual debt service on all Outstanding Bonds and parity indebtedness permitted under the Series 2006 Loan Agreement and the Indenture. To the extent that Gross Receipts Tax collections and Substitute Revenues, if any, are insufficient to pay amounts due under the Series 2006 Loan Note, as of the date which is 30 days prior to the due date thereof, the Government also has covenanted to fund such deficiency out of any other moneys of the Government legally available therefor by the 15th day prior to such due date.

Series 2006 Loan Note

The Series 2006 Bonds will be secured by the Series 2006 Loan Note issued by the Government pursuant to the Series 2006 Loan Agreement. The Government will be obligated under the Series 2006 Loan Note to make payments to the Authority in amounts sufficient to pay all principal, premium, if any, and interest on the Series 2006 Bonds when due, to make payments to the Debt Service Reserve Account in amounts necessary under the Indenture to replenish the Debt Service Reserve Account in an amount equal to the Debt Service Reserve Requirement and to pay such other amounts as required under the Series 2006 Bonds or pursuant to the terms of the Indenture. Pursuant to the terms of the Series 2006 Loan Agreement, the Government has authorized the issuance of the Series 2006 Loan Note as security for the Series 2006 Bonds. The Series 2006 Loan Note is secured by a pledge of the Gross Receipts Taxes over the full term of the Series 2006 Loan Note, which Gross Receipts Tax collections in each Fiscal Year are anticipated to be in excess of the amount necessary to pay all the principal of, premium, if any, interest on, and such other amounts payable under the Series 2006 Bonds and all other Bonds and other parity indebtedness when due. However, no assurances can be given as to the sufficiency of Gross Receipts Taxes for such purpose. See "GROSS RECEIPTS TAXES."

The pledge of Gross Receipts Taxes securing the Series 2006 Loan Note is subject to the Required Annual Moderate Income Housing Fund Deposit and to any parity indebtedness permitted under the Indenture, including the Series 1999A Bonds and the 2003A Bonds.

Series 2006 Loan Agreement

Under the Series 2006 Loan Agreement, the Authority shall lend to the Government the sum of $219,490,000 as a loan which shall be evidenced by the Series 2006 Loan Note. The Government shall repay the loan to the Authority, pursuant to the Series 2006 Loan Note, in annual installments of principal and semiannual installments of interest corresponding to the requirements of the Seventh Supplemental Indenture. The Series 2006 Loan Note provides for payments of principal according to a maturity schedule corresponding to principal which shall be due and payable on the Series 2006 Bonds and shall bear interest from its dated date payable on dates corresponding to the Interest Payment Dates on the Series 2006 Bonds. The Series 2006 Loan Note may, at the option of the Government, be redeemed, in whole or in part, prior to its maturity at the times, in the manner of, and of the same maturities as an optional redemption of the Series 2006 Bonds and at a redemption price equal to that for optional redemption of such Series 2006 Bonds, pursuant to the terms of the Indenture. In addition, in the event the Series 2006 Bonds are subject to mandatory redemption in whole or in part or in the event the Series 2006 Bonds are tendered by the holders thereof for purchase and are purchased by the Authority for retirement or cancellation then, upon payment of the redemption price or purchase price of such Series 2006 Bonds, the Government shall be deemed to have made a prepayment on the Series 2006 Loan Note, in accordance with the Series 2006 Loan Agreement, in a principal amount equal to the aggregate principal amount of the Series 2006 Bonds so redeemed or purchased. See APPENDIX C – "Summary of Certain Provisions of the Series 2006 Loan Agreement."

To the extent the aggregate amounts transferred from the Special Escrow Account to the Trustee pursuant to the Special Escrow Agreement as of the date which is 30 days prior to the due date of any installment of principal, interest or other amounts payable on the Series 2006 Loan Note, are insufficient to pay those amounts in full, the Trustee shall promptly provide written notification to the Government and the Authority of such deficiency and the Government shall, on or before the date which is 15 days prior to such due date, remit or cause to be remitted to the Trustee, in immediately available funds out of any moneys of the Government legally available therefor, an amount equal to such deficiency.

Special Escrow Agreement and Collecting Agent Agreement

The Special Escrow Agreement provides for the daily deposit of all Gross Receipts Taxes collected on the preceding Business Day by or on behalf of the Government, including all additions to tax, penalties and interest thereon and, to the extent pledged by the Government in accordance with the Series 2006 Loan Agreement, the Substitute Revenues, into the Special Escrow Account maintained by Banco Popular de Puerto Rico, as the Collecting Agent, who will act on behalf of the Special Escrow Agent pursuant to a Collecting Agent Agreement, dated as of November 1, 1999, as amended as of February 28, 2003 and as further amended as of September 1, 2006 (the "Collecting Agent Agreement"), among the Collecting Agent, the Special Escrow Agent and the Government. Within one (1) Business Day of the daily receipt of Gross Receipts Taxes, the Collecting Agent will make daily transfers to the Government until satisfaction of the Required Annual Moderate Income Housing Fund Deposit. Upon satisfaction of the Required Annual Moderate Income Housing Fund Deposit, the Collecting Agent will transfer daily all further amounts deposited in the Special Escrow Account to the Trustee for deposit into the Pledged Revenue Account until the Monthly Transfer Requirement for each calendar month is satisfied. Upon satisfaction of the Monthly Transfer Requirement, any excess Gross Receipts Taxes for such calendar month will be transferred to the Trustee into the Surplus Account until the Swap Agreement Termination Payment Requirement (as defined in the Special Escrow Agreement), if any, related to the Swap Option Agreement is satisfied and thereafter to the Government to be used for any lawful purpose. All Gross Receipts Taxes deposited in the Special Escrow Account maintained by the Collecting Agent are subject to the lien created pursuant to the Indenture. Failure by the Government to deposit Gross Receipts Taxes in the Special Escrow Account due to force majeure (as determined in the reasonable judgment of the Government) is not an Event of Default under the Loan Agreement.

Covenants

So long as the Series 2006 Loan Note remains outstanding, the Government has covenanted in the Series 2006 Loan Agreement, among other things, to take all actions necessary to defend, preserve and protect the pledge of Gross Receipts Taxes, to the extent permitted by law, and take all steps necessary to ensure the receipt of and the maximization of the Gross Receipts Taxes to be received. The Government has further covenanted not to take any action or fail to take any actions that would in any way impair the Government's right to receive the maximum amount of Gross Receipts Taxes to which it may be entitled nor take any action to reduce the rate of Gross Receipts Taxes or to allow waiver of payment of such Gross Receipts Taxes, except for the Government's Economic Development Commission program which grants certain tax exemptions to qualified businesses pursuant to Title 29, Chapters 12 and 13 of the Virgin Islands Code (the "EDC Program") or other similar programs. In furtherance of such covenant, the Series 2006 Loan Agreement provides that the Government may not grant tax exemptions (including pursuant to the EDC Program) if such grants cause or will cause the aggregate of the aggregate Gross Receipts Taxes estimated to be collected in any Fiscal Year of the Government to be less than 150% of the maximum debt service on all Outstanding Bonds and on any parity indebtedness permitted by the Series 2006 Loan Agreement and the Indenture.

In the event that Gross Receipts Tax collections during any period of 12 consecutive months are less than 150% of maximum annual debt service on all Outstanding Bonds and any parity indebtedness permitted by the Series 2006 Loan Agreement and the Indenture, the Government has covenanted to use its best efforts to provide Substitute Revenues in addition thereto and to pledge such Substitute Revenues as additional security for the Series 2006 Loan Note. Any pledge of Substitute Revenues will remain in effect until such time as Gross Receipts Tax collections during any period of at least 12 consecutive months thereafter equal or exceed 150% of maximum annual debt service on all such Outstanding Bonds and parity indebtedness. Further, the Authority has covenanted in the Series 2006 Loan Agreement and the Indenture to use its best efforts to cause the Government to maintain and abide by its covenants contained in the Act, the Series 2006 Loan Agreement and the Special Escrow Agreement not to limit, restrict or in any way impair the imposition, collection, transfer or disbursement of the Gross Receipts Taxes, subject to any permitted tax exemptions, until the principal of, premium, if any, and interest on, and all other amounts due on all the Bonds have been fully paid or discharged.

The Government has covenanted to require the independent certified public accounting firm that has contracted with the Government to perform its annual audit (the "Auditor") to also perform on a quarterly basis certain agreed-upon procedures on Gross Receipts Tax deposits made to the Collecting Agent. As part of its contract, the Auditor delivers an agreed-upon procedures report (the "Report") to the Government, the Authority, the Trustee and the Bond Insurer comparing the Gross Receipts Tax payments documented in the Government's financial management system with the total revenues deposited with the Collecting Agent and the deposit receipts remitted by the Collecting Agent to the Revenue Audit section of the Government's Department of Finance. The Report is required to be delivered within 45 days of the end of each fiscal quarter of the Fiscal Year.

The Authority also has covenanted in the Indenture to at all times, and to the extent permitted by law, defend, preserve and protect the pledge of the Trust Estate and all rights of the Bondowners under the Indenture against all claims and demands of all third parties.

Flow of Funds

The Indenture provides that all Revenues received by the Trustee for the benefit of the Bondowners and any such other revenues as may be received by the Trustee and designated for deposit to the Pledged Revenue Account shall be deposited, upon receipt by the Trustee, to the credit of the Pledged Revenue Account, which is an account held by the Trustee. All amounts in the Pledged Revenue Account shall be transferred daily on or before 5:00 p.m. on each Business Day during each calendar month to Accounts and Subaccounts created pursuant to the Indenture, so long as any of the Series 2006 Bonds remain Outstanding, in the following amounts and in the following order of priority:

(a) to each Interest Subaccount and to any net payment sub-subaccount thereof with respect to any Qualified Swap Agreement in accordance with the Indenture and the applicable Supplemental Indenture, until the aggregate amount on deposit in all existing Interest Subaccounts is equal to the sum of all Required Interest Subaccount Balances (as defined in the Indenture). The Required Interest Subaccount Balance in effect during each calendar month for each Interest Subaccount shall be the greater of (i) the amount determined by multiplying (A) the portion of the Adjusted Debt Service Requirement for the applicable Series of Bonds which constitutes all of the interest accruing or to accrue on such Series of Bonds during the Interest Payment Period ending on the next Interest Payment Date by (B) a fraction, the numerator of which is equal to one (1) plus the number of whole calendar months that have elapsed since the immediately preceding Interest Payment Date (or, in the case of the period prior to the first Interest Payment Date, one (1) plus the number of whole calendar months that have elapsed since the date interest on such Series of Bonds commenced to accrue) and the denominator of which is the number of whole calendar months in such Interest Payment Period, or (ii) the amount specified in the applicable Supplemental Indenture;

(b) to each Principal Subaccount, beginning in the first calendar month specified in the applicable Supplemental Indenture (the "Principal Amortization Start Month"), until the aggregate amount on deposit in all existing Principal Subaccounts is equal to the sum of all Required Principal Subaccount Balances (as defined in the Indenture). The Required Principal Subaccount Balance in effect during each calendar month for each Principal Subaccount shall be the greater of (i) the amount determined by multiplying (A) the principal (including Sinking Fund Installments) on the applicable Series of Bonds due on the next succeeding Principal Payment Date by (B) a fraction, the numerator of which is equal to one (1) plus the number of whole calendar months that have elapsed since the immediately preceding Principal Payment Date (or, in the case of the period prior to the first Principal Payment Date, one (1) plus the number of whole calendar months that have elapsed since the first day of the Principal Amortization Start Month), and the denominator of which is the number of whole calendar months between the immediately preceding Principal Payment Date (or, in the case of the period prior to the first Principal Payment Date, the first day of the Principal Amortization Start Month), and the next succeeding Principal Payment Date, or (ii) the amount specified in the applicable Supplemental Indenture;

(c) to each Credit Subaccount, an amount sufficient to pay any principal or interest then owing to a Credit Provider under the applicable Supplemental Indenture and Credit Agreement by reason of any drawing of amounts under the related Credit Facility for the payment of principal of or interest or premium on any Series A Bonds subject to any required transfer, under other provisions of the Indenture or a Supplemental Indenture;

(d) to the Debt Service Reserve Account, the amount of any transfer required by the Indenture to restore any deficiency in the Debt Service Reserve Account (or to pay any amounts then owing to a Credit Provider pursuant to a Credit Agreement relating to a Debt Service Reserve Account Credit Facility);

(e) to each Redemption Subaccount, the amount of Revenues required to redeem Series A Bonds pursuant to the related Supplemental Indenture;

(f) to each Expense Subaccount, any amounts then due and owing to the Trustee, any Paying Agent, Remarketing Agent, Bond Registrar, Credit Provider, the Special Escrow Agent, the Collecting Agent, or other Fiduciary which are Bond Service Charges or Bond Related Costs for the Series A Bonds, and the Authority's Annual Administrative Fee, which otherwise have not been provided for above;

(g) to each Subaccount of the Rebate Account attributable to a specific Series of Bonds;

(h) to any Swap Provider under any Qualified Swap Agreement, the amounts required to meet the Swap Agreement Termination Payments (as defined in the Special Escrow Agreement) as set forth in such Qualified Swap Agreement; and

(i) except as may be provided in one or more Supplemental Indentures to the contrary, to the Surplus Account for application pursuant to the Indenture.

Debt Service Reserve Account

Net proceeds of the Series 2006 Bonds representing the Debt Service Reserve Requirement relating to the Series 2006 Bonds shall be deposited by the Trustee in the Debt Service Reserve Account. Pursuant to the terms of the Indenture, the Debt Service Reserve Requirement shall mean, as of any date of calculation, an amount equal to the least of (i) the maximum principal (including mandatory Sinking Fund Installments) and interest due on Outstanding Bonds in the then current or any future Bond Year, (ii) 10% of the original aggregate principal amount of the Bonds (net of original issue discount), and (iii) 125% of the average annual principal (including mandatory Sinking Fund Installments) and interest due on the Outstanding Bonds in the then current and each future Bond Year, as specified in the Indenture and each Supplemental Indenture.

A valuation of the Debt Service Reserve Account shall be made on March 1 and September 1 in each year pursuant to the Indenture and at such other times as the Authority shall direct in writing and, in addition, shall be valued at the time of any withdrawal from the Debt Service Reserve Account pursuant to the Indenture. In the event the amount on deposit in such Debt Service Reserve Account is less than the Debt Service Reserve Requirement due to a payment made from such Account to cure an insufficiency of funds on any Interest Payment Date or Principal Payment Date, the Authority shall be required to restore the deficiency caused thereby by transfers of any moneys on deposit in the Surplus Account and to the extent any deficiency exists upon transfer from the Surplus Account, then the Authority shall be required to restore the deficiency by equal monthly transfers of Revenues from the Pledged Revenue Account over a period of twelve calendar months following the month in which the determination of such deficiency was made. The Trustee shall notify the Authority of the amount, if any, of the deficiency or excess in the Debt Service Reserve Account.

The Debt Service Reserve Account has always satisfied the Debt Service Reserve Requirement.

In the event that there are not sufficient amounts on deposit in the Interest Subaccount on an Interest Payment Date to pay amounts due or if there are not sufficient amounts on deposit in the Principal Subaccount on a Principal Payment Date to pay amounts then due, after making the transfers required to be made from the other Accounts and Subaccounts as provided in the Indenture, the Trustee shall transfer amounts on deposit in the Debt Service Reserve Account to the Interest Subaccount or Principal Subaccount, as applicable, in an amount sufficient to make up any such deficiency. The Trustee shall notify the Authority of such transfer at the time of the transfer.

Surplus Available Revenues

To ensure compliance with certain federal tax law requirements with respect to the issuance of long-term working capital financings, upon elimination of the accumulated deficit, on or after October 1, 2007, all Surplus Available Revenues of the Government shall be applied to the retirement of Bonds issued to finance working capital, by purchase, redemption or defeasance.

Limitations on Available Remedies

Upon the occurrence of an Event of Default, the Indenture provides certain remedies available to the Trustee and Bondowners. However, the Indenture does not authorize the Trustee to accelerate payment of the full principal and interest due and payable on the Bonds in the event of the occurrence and continuance of an Event of Default. See APPENDIX B — "Summary of Certain Provisions of the Original Indenture and the Seventh Supplemental Indenture — The Original Indenture — Events of Default," "— Proceedings by Trustee" and "— Rights of Owners."

Additional Bonds

All of the Bonds issued under a Supplemental Indenture shall collectively be a charge and lien upon the Trust Estate as provided in the Indenture and such charge and lien shall be prior to any other charge and lien upon the Trust Estate with the exception of the Required Annual Moderate Income Housing Fund Deposit and any other Bonds or parity indebtedness. Except as permitted in the Indenture, no obligations payable from Revenues or secured by a prior or equal lien on the Trust Estate shall be issued after the date of the Indenture.

So long as no Event of Default has occurred and is continuing, the Authority may from time to time enter into a Supplemental Indenture providing for the issuance of Additional Bonds pursuant to the Indenture. Additional Bonds may be issued if the conditions set forth in the Indenture are met, including:

(a) receipt by the Trustee of a certificate of an Independent Verification Analyst stating (i) (A) the actual amount of Gross Receipts Taxes collected by the Government during each of the eighteen (18) calendar months immediately preceding the calendar month in which such Bonds are issued (the "Test Period"); and (B) the actual amount of Gross Receipts Taxes collected by the Government during any twelve (12) consecutive month period within the Test Period in which aggregate collections of the Gross Receipts Taxes were the greatest in actual amount, (ii) the maximum annual Adjusted Debt Service Requirement in the current or any subsequent Bond Year on Outstanding Bonds after giving effect to the issuance of the proposed Additional Bonds; and (iii) that the actual amount of Gross Receipts Taxes collected by the Government during the twelve (12) consecutive calendar month period referred to in (i)(B) above, equal or exceed 150% of the amount of maximum Adjusted Debt Service Requirement on Outstanding Bonds in the current or any subsequent Bond Year after giving effect to the issuance of the proposed Additional Bonds; and

(b) receipt by the Trustee of a certificate of the Director of the Office of Management and Budget of the Government stating (i) the projected amount of Gross Receipts Taxes to be collected during the period of twelve (12) consecutive calendar months immediately following the calendar month in which such proposed Additional Bonds are to be issued; and (ii) that the projected amount of Gross Receipts Taxes to be collected by the Government during the twelve (12) consecutive calendar month period referred to in clause (i) above, equal or exceed 150% of the amount of the maximum annual Adjusted Debt Service Requirement in the current or any subsequent Bond Year on Outstanding Bonds after giving effect to the issuance of the proposed Additional Bonds.

Additional Bonds may be issued for any purpose for which Bonds or other obligations may be issued at or after the date of the Indenture under the Act or as otherwise permitted under the laws of the Virgin Islands. Any such Additional Bonds may bear interest at any rate lawful at the time of the issuance thereof and may mature over any period of time not exceeding the maximum maturity permitted by law and may provide for such other payment terms and conditions as the Authority shall determine in a Supplemental Indenture.

Nothing in the Indenture prevents the Authority or the Government from issuing or creating other bonds, notes or other evidences of indebtedness that are not secured by the Indenture so long as such indebtedness is not secured by a prior or parity pledge of Gross Receipts Taxes.

Amendments

The provisions of the Indenture, the Special Escrow Agreement and the Collecting Agent Agreement may not be amended so as to materially adversely affect the Bondowners without the prior written consent of the holders of at least a majority in the aggregate principal amount of such Bonds then Outstanding. The provisions of the Series 2006 Loan Note and the Series 2006 Loan Agreement may not be amended so as to materially adversely affect the Series 2006 Bondowners without the prior written consent of the holders of at least a majority in principal amount of the Series 2006 Bonds then outstanding.

GROSS RECEIPTS TAXES

General

Pursuant to Title 33 of the Virgin Islands Code, Section 43, individuals and entities doing business in the Virgin Islands are required to pay a tax of 4.0% on the gross receipts of such business (the "Gross Receipts Tax"). The Gross Receipts Tax is broad and extends to most sellers of services and goods. The current number of total Gross Receipts Tax taxpayers is approximately 3,900. For Fiscal Year 2005, the top five taxpayers generated 16.1% of Gross Receipts Tax collections and the top ten taxpayers generated 24.8% of Gross Receipts Tax collections.

General Information Regarding Gross Receipts Taxes
Fiscal Years 2001 - 2005
($000's)

	2001	2002	2003	2004	2005
Gross Receipts Taxes	$99,598	$95,916	$100,918	$113,185	$124,963
Gross Receipts Taxes as Percentage of General Fund (Budgetary Basis) Revenues	18.5%	18.5%	19.7%	18.2%	17.8%

Source: Continuing Disclosure Quarterly Summary reports of the Authority certifying Gross Receipts Taxes Deposited with the Collecting Agent.

In Fiscal Year 2002, the Gross Receipts Taxes decreased by 4.3%. This decrease was primarily attributable to a general decrease in business activity as a result of the general economic decline in the United States and the terrorist attacks in New York City and Washington, D.C. on September 11, 2001.

The proceeds of the Gross Receipts Tax are paid to the BIR for deposit into the General Fund of the Government, subject to the Required Annual Moderate Income Housing Fund Deposit (see "SECURITY FOR THE SERIES 2006 BONDS — Special Escrow Agreement and Collecting Agent Agreement"). "Gross receipts" means "all receipts, cash or accrued, of the taxpayer for services or derived from trade, business, commerce or sales, and the value accruing from the sale of tangible personal property or services, or both, including rentals, fees and other involvements, however designated, without any deduction on account of the cost of the property sold, the cost of materials used, labor cost, royalties, taxes, interest or discount paid, and any other expenses whatsoever."

There is a general exemption from the Gross Receipts Tax for agencies of the Government or the United States federal government, religious, charitable, benevolent or educational organizations when not engaged in the conduct of business pursuits for profit, and transactions involving a charitable or benevolent purpose. Every person, partnership, firm, corporation or association whose gross receipts are less than $150,000 per annum is allowed a maximum $5,000 exemption per month. Exempt businesses include insurance companies, franchised bus operators, costume jewelry manufacturers, some reverse osmosis water production plants, and providers of affordable housing pursuant to an approved Affordable Housing Development Agreement entered into with the Government under the United States Virgin Islands Affordable Housing Program. Additionally, some qualifying businesses are granted exemptions from certain tax liabilities, including Gross Receipts Taxes, pursuant to the EDC Program. See APPENDIX E — "United States Virgin Islands Economic and Demographic Information — Tax Incentives Programs — Economic Development Commission."

Collection of Gross Receipts Taxes

Individuals and entities subject to the Gross Receipts Tax must file a monthly (or annual, under certain circumstances) report with the Director of the BIR declaring the dollar value of the gross receipts received during the calendar month or year (as applicable). Such reports must be accompanied by payment of taxes due on the declared gross receipts to preclude accrual of penalties and interest. Monthly reports and payments are due within thirty (30) calendar days following the last day of the calendar month concerned. All BIR tax collectors who physically handle currency or checks received as payments from taxpayers are required to be bonded. Businesses with annual gross receipts of $120,000 or less do not file monthly, but are required to file an annual report with the Director of the BIR declaring the gross receipts for each calendar month and the total amount of Gross Receipts Taxes for the year. Reports of these entities must be filed within thirty (30) calendar days following the last day of the calendar year concerned. All exempt businesses are also required to file a report with the Director of the BIR.

The Director of the BIR notifies taxpayers of any deficiencies that are due and imposes penalties and interest on such deficiencies. The BIR sends written notices to delinquent taxpayers. Two written notices are sent allowing the taxpayer up to twenty-one (21) days to respond. If a taxpayer fails to respond after the second notice, a third notice is sent and a Taxpayer Delinquent Account is routed to the Delinquent Account and Returns Branch which handles the collections. The BIR employs revenue officers who implement various methods for collecting delinquent taxes, including liens and levies. Liens for taxes owed to the BIR are created in favor of the Government upon all property and rights to property, whether real or personal, belonging to the taxpayers owing such Gross Receipts Taxes. Monetary penalties not to exceed 25% in the aggregate, excluding interest (1% per month), are also imposed on individuals and entities subject to taxation who fail to declare gross receipts or pay the amount of tax due in the time allotted by the statute. The BIR may waive any such monetary penalties upon the taxpayer's satisfactory proof that the taxpayer's failure to file a report or pay any taxes or penalties owed was due to reasonable cause and not due to willful neglect. The BIR may also levy a penalty upon a delinquent taxpayer's property or rights to property.

Pursuant to the Special Escrow Agreement, Gross Receipts Taxes will be deposited daily in the Special Escrow Account maintained by the Collecting Agent, acting on behalf of the Special Escrow Agent. Upon receipt of such collections, the Collecting Agent shall make daily transfers of such collections to the Government until satisfaction of the Required Annual Moderate Income Housing Fund Deposit. All further amounts deposited into the Special Escrow Account shall be transferred daily to the Trustee for deposit into the Pledged Revenue Account established under the Indenture until the amounts transferred to the Trustee for each calendar month satisfy the Monthly Transfer Requirement. Upon satisfaction of the Monthly Transfer Requirement, all excess Gross Receipts Taxes for such calendar month will be transferred to the Government for deposit into the General Fund to be used for any authorized purpose. Pursuant to the Series 2006 Loan Agreement, to the extent the aggregate amounts transferred from the Special Escrow Account to the Trustee as of the 30th day preceding any due date for the payment of principal, interest or other amount payable on the Series 2006 Loan Note are insufficient to make such payment, the Trustee shall promptly provide written notification to the Government and the Authority of such deficiency and the Government shall, on or before the 15th day preceding such due date, remit or cause to be remitted to the Trustee in immediately available funds out of any moneys of the Government legally available therefor an amount equal to such deficiency. See "SECURITY FOR THE SERIES 2006 BONDS — Series 2006 Loan Agreement" and " — Special Escrow Agreement and Collecting Agent Agreement."

Historical Gross Receipts Taxes and Pro Forma Debt Service Coverage

The following table presents Gross Receipts Taxes for Fiscal Years 2001 through 2005. These figures are used to give a pro forma coverage ratio for the Series 1999A Bonds, the Series 2003A Bonds, and the Series 2006 Bonds after defeasance of the Refunded Bonds.

Gross Receipts Taxes
Historical Pro Forma
Debt Service Coverage
Fiscal Years 2001 - 2005
($000's)

	2001	2002	2003	2004	2005
Gross Receipts Taxes(1) Less $250,000 (2)	$99,348	$95,666	$100,668	$112,935	124,713
Maximum Annual Debt Service on the Bonds (3).........................	$41,397	$41,397	$41,397	$41,397	$41,397
Coverage Based on Gross Receipts Taxes......	2.40X	2.31X	2.43X	2.73X	3.01X

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(1) Source: Continuing Disclosure Quarterly Summary reports of the Authority certifying Gross Receipts Taxes Deposited with the Collecting Agent.

(2) Reflects Required Annual Moderate Income Housing Fund Deposit. See "SECURITY FOR THE SERIES 2006 BONDS — Special Escrow Agreement and Collecting Agent Agreement."

(3) Annual debt service based on: (i) the outstanding Series 1999A Bonds and 2003A Bonds after defeasance of the Refunded Bonds and (ii) the Series 2006 Bonds.

BOND INSURANCE

Financial Guaranty has supplied the following information for inclusion in this Official Statement. No representation is made by the Authority, the Government or the Underwriter as to the accuracy or completeness of this information.

Payments Under the Policy

Concurrently with the issuance of the Series 2006 Bonds, Financial Guaranty Insurance Company ("Financial Guaranty") will issue its Municipal Bond New Issue Insurance Policy for the Bonds (the "Policy"). The Policy unconditionally guarantees the payment of that portion of the principal or accreted value (if applicable) of and interest on the Series 2006 Bonds, which has become due for payment, but shall be unpaid by reason of nonpayment by the issuer of the Series 2006 Bonds (the "Issuer"). Financial Guaranty will make such payments to U.S. Bank Trust National Association, or its successor as its agent (the "Fiscal Agent"), on the later of the date on which such principal, accreted value or interest (as applicable) is due or on the business day next following the day on which Financial Guaranty shall have received notice (in accordance with the terms of the Policy) from an owner of Series 2006 Bonds or the trustee or paying agent (if any) of the nonpayment of such amount by the Issuer. The Fiscal Agent will disburse such amount due on any Series 2006 Bond to its owner upon receipt by the Fiscal Agent of evidence satisfactory to the Fiscal Agent of the owner's right to receive payment of the principal, accreted value or interest (as applicable) due for payment and evidence, including any appropriate instruments of assignment, that all of such owner's rights to payment of such principal, accreted value or interest (as applicable) shall be vested in Financial Guaranty. The term "nonpayment" in respect of a Series 2006 Bond includes any payment of principal, accreted value or interest (as applicable) made to an owner of a Series 2006 Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a 'final, nonappealable order of a court having competent jurisdiction.

Once issued, the Policy is non-cancellable by Financial Guaranty. The Policy covers failure to pay principal (or accreted value, if applicable) of the Series 2006 Bonds on their stated maturity dates and their mandatory sinking fund redemption dates, and not on any other date on which the Series 2006 Bonds may have been otherwise called for redemption, accelerated or advanced in maturity. The Policy also covers the failure to pay interest on the stated date for its payment. In the event that payment of the Series 2006 Bonds is accelerated, Financial Guaranty will only be obligated to pay principal (or accreted value, if applicable) and interest in the originally scheduled amounts on the originally scheduled payment dates. Upon such payment, Financial Guaranty will become the owner of the Series 2006 Bond, appurtenant coupon or right to payment of principal or interest on such Series 2006 Bond and will be fully subrogated to all of the Bondholder's rights thereunder.

The Policy does not insure any risk other than Nonpayment by the Issuer, as defined in the Policy. Specifically, the Policy does not cover: (i) payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity; (ii) payment of any redemption, prepayment or acceleration premium; or (iii) nonpayment of principal (or accreted value, if applicable) or interest caused by the insolvency or negligence or any other act or omission of the trustee or paying agent, if any.

As a condition of its commitment to insure Series 2006 Bonds, Financial Guaranty may be granted certain rights under the Series 2006 Bond documentation. The specific rights, if any, granted to Financial Guaranty in connection with its insurance of the Series 2006 Bonds may be set forth in the description of the principal legal documents appearing elsewhere in this Official Statement, and reference should be made thereto.

The Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

Financial Guaranty Insurance Company

Financial Guaranty is a New York stock insurance corporation that writes financial guaranty insurance in respect of public finance and structured finance obligations and other financial obligations, including credit default swaps. Financial Guaranty is licensed to engage in the financial guaranty insurance business in all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the U.S. Virgin Islands and the United Kingdom.

Financial Guaranty is a direct, wholly owned subsidiary of FGIC Corporation, a Delaware corporation. At June 30, 2006, the principal owners of FGIC Corporation and the approximate percentage of its outstanding common stock owned by each were as follows: The PMI Group, Inc. - 42%; affiliates of the Blackstone Group L.P. - 23%; and affiliates of the Cypress Group L.L.C. - 23%. Neither FGIC Corporation nor any of its stockholders or affiliates is obligated to pay any debts of Financial Guaranty or any claims under any insurance policy, including the Policy, issued by Financial Guaranty.

Financial Guaranty is subject to the insurance laws and regulations of the State of New York, where Financial Guaranty is domiciled, including New York's comprehensive financial guaranty insurance law. That law, among other things, limits the business of each financial guaranty insurer to financial guaranty insurance (and related lines); requires that each financial guaranty insurer maintain a minimum surplus to policyholders; establishes limits on the aggregate net amount of exposure that may be retained in respect of a particular issuer or revenue source (known as single risk limits) and on the aggregate net amount of exposure that may be retained in respect of particular types of risk as compared to the policyholders' surplus (known as aggregate risk limits); and establishes contingency, loss and unearned premium reserve requirements. In addition, Financial Guaranty is also subject to the applicable insurance laws and regulations of all other jurisdictions in which it is licensed to transact insurance business. The insurance laws and regulations, as well as the level of supervisory authority that may be exercised by the various insurance regulators, vary by jurisdiction.

At June 30, 2006, Financial Guaranty had net admitted assets of approximately $3.752 billion, total liabilities of approximately $2.616 billion, and total capital and policyholders' surplus of approximately $1.136 billion, determined in accordance with statutory accounting practices ("SAP") prescribed or permitted by insurance regulatory authorities.

The unaudited consolidated financial statements of Financial Guaranty and subsidiaries, on the basis of U.S. generally accepted accounting principles ("GAAP"), as of June 30, 2006 and the audited consolidated financial statements of Financial Guaranty and subsidiaries, on the basis of GAAP, as of December 31, 2005 and 2004, which have been filed with the Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs"), are hereby included by specific reference in this Official Statement. Any statement contained herein under the heading "BOND INSURANCE," or in any documents included by specific reference herein, shall be modified or superseded to the extent required by any statement in any document subsequently filed by Financial Guaranty with such

NRMSIRs, and shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement. All financial statements of Financial Guaranty (if any) included in documents filed by Financial Guaranty with the NRMSIRs subsequent to the date of this Official Statement and prior to the termination of the offering of the Series 2006 Bonds shall be deemed to be included by specific reference into this Official Statement and to be a part hereof from the respective dates of filing of such documents.

The New York State Insurance Department recognizes only SAP for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the New York Insurance Law, and for determining whether its financial condition warrants the payment of a dividend to its stockholders. Although Financial Guaranty prepares both GAAP and SAP financial statements, no consideration is given by the New York State Insurance Department to financial statements prepared in accordance with GAAP in making such determinations. A discussion of the principal differences between SAP and GAAP is contained in the notes to Financial Guaranty's audited SAP financial statements.

Copies of Financial Guaranty's most recently published GAAP and SAP financial statements are available upon request to: Financial Guaranty Insurance Company, 125 Park Avenue, New York, NY 10017, Attention: Corporate Communications Department. Financial Guaranty's telephone number is (212) 312-3000.

Financial Guaranty's Credit Ratings

The financial strength of Financial Guaranty is rated "AAA." by Standard & Poor's, a Division of The McGraw-Hill Companies, Inc., "Aaa" by Moody's Investors Service, and "AAA" by Fitch Ratings. Each rating of Financial Guaranty should be evaluated independently. The ratings reflect the respective ratings agencies' current assessments of the insurance financial strength of Financial Guaranty. Any further explanation of any rating may be obtained only from the applicable rating agency. These ratings are not recommendations to buy, sell or hold the Series 2006 Bonds, and are subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Series 2006 Bonds Financial Guaranty does not guarantee the market price or investment value of the Series 2006 Bonds nor does it guarantee that the ratings on the Series 2006 Bonds will not be revised or withdrawn.

Neither Financial Guaranty nor any of its affiliates accepts any responsibility for the accuracy or completeness of the Official Statement or any information or disclosure that is provided to potential purchasers of the Series 2006 Bonds, or omitted from such disclosure, other than with respect to the accuracy of information with respect to Financial Guaranty or the Policy under the heading "BOND INSURANCE." In addition, Financial Guaranty makes no representation regarding the Series 2006 Bonds or the advisability of investing in the Series 2006 Bonds.

UNITED STATES VIRGIN ISLANDS

General

Under the terms of the Revised Organic Act, the Virgin Islands is an unincorporated territory of the United States with separate executive, legislative and judicial branches of government. The legislative power of the Virgin Islands is vested in the Legislature, a unicameral, popularly elected body consisting of 15 members who serve two-year terms. The Legislature has jurisdiction over "all rightful subjects of legislation" not inconsistent with the laws of the United States made applicable to the Virgin Islands.

Executive power resides with a Governor and a Lieutenant Governor who are elected every four years. The Governor is responsible for execution of local laws, administration of all activities of the executive branch and appointment of department heads and other employees. The current Governor is the Honorable Charles W. Turnbull, who assumed office on January 4, 1999, and the current Lieutenant Governor is the Honorable Vargrave A. Richards, who assumed office on January 6, 2003, both of whose terms expire on the first Monday in January 2007.

Judicial power is vested in the District Court of the Virgin Islands, which has jurisdiction of a District Court of the United States, and in the Superior Court of the Virgin Islands, a court established by local law with jurisdiction over all local matters. Within the District Court there is an appellate division which reviews judgments of the Superior Court. The United States Court of Appeals for the Third Circuit has appellate jurisdiction over the District Court and its appellate division. The judges of the District Court of the Virgin Islands are appointed by the

President of the United States with the advice and consent of the United States Senate and serve for ten years. The Superior Court judges are appointed by the Governor and confirmed by the Legislature and serve for terms of six years.

As an unincorporated territory of the United States, the Virgin Islands is subject to the power of Congress to make rules and regulations respecting the Virgin Islands. In addition, Congress has the power to legislate directly for a territory or to establish the government for such territory subject to congressional control.

Pursuant to the Insular Areas Act of 1982, the OIG of the DOI performs the functions of government comptroller through audits of revenues and receipts and expenditure of funds and property of the Virgin Islands, as well as the other insular areas of Guam, American Samoa, and the Commonwealth of Northern Mariana Islands. In connection therewith, the OIG has issued numerous audit reports over the past several years regarding the Virgin Islands. See "VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY – Department of the Interior Report" and "UNITED STATES VIRGIN ISLANDS — Financial Position of the Government – Other DOI Office of Inspector General Reports."

Residents of the Virgin Islands have been citizens of the United States since 1917. However, apart from express Congressional grants of rights, such as the Bill of Rights in Section 1561 of the Revised Organic Act, residency in the Virgin Islands does not carry with it the full range of rights which accompany citizenship in any of the states. Residents of the Virgin Islands do not have the right to vote in national elections for the President and Vice President of the United States. The Virgin Islands has an elected, non-voting delegate to the United States House of Representatives. The delegate may vote in legislative committees and participate in floor debate but may not vote on the House floor.

Financial Management, Budgeting and Controls

Budgetary Process

The Fiscal Year of the Government begins on October 1 of each year. The Governor is required by law to submit to the Legislature an annual budget of capital improvements and operating expenses for the following Fiscal Year no later than May 30. The annual budget is prepared by the Virgin Islands Office of Management and Budget ("OMB"), working in conjunction with other Government departments and agencies. The Legislature, in its consideration of the budget for each Fiscal Year, may modify or change the Governor's submission. Upon passage by the Legislature, the budget is submitted to the Governor, who may eliminate any item by a line-item veto but not increase or insert any new item in the budget within ten (10) days of passage by the Legislature. The Governor also may veto the budget in its entirety and return it to the Legislature with his objections within ten (10) days of passage by the Legislature. The Legislature may override any veto by the Governor (including any line-item veto) only by a vote of two-thirds of its members. The Legislature is obligated by law to pass a final balanced budget no later than September 30, the last day of the Fiscal Year. Subsequent to enactment of the Government Financial Accountability Act of 1999, 1999 Virgin Islands Act No. 6289, as amended (the "Financial Accountability Act"), supplemental budgetary appropriations bills that are signed into law may be made during the year only with the identification of a specific revenue source to finance them.

If a budget has not been approved before the commencement of any Fiscal Year, then the appropriations for the preceding Fiscal Year, insofar as they may be applicable, are automatically deemed reappropriated item by item. The Fiscal Year 2007 Budget was submitted by the Governor to the Legislature on May 30, 2006, which the Legislature is expected to finalize and pass before September 30, 2006 (see "UNITED STATES VIRGIN ISLANDS — Financial Position of the Government — Proposed Fiscal Year 2007 Budget"). It is currently anticipated that the final Fiscal Year 2007 Budget will be acted upon by the Governor by October 1, 2006. If not enacted by October 1, 2006, the Fiscal Year 2006 Budget would continue to be in effect until the enactment of the Fiscal Year 2007 Budget.

Once the budget is enacted, fiscal control over expenditures made pursuant thereto is exercised by the Governor through the allotment process by the Director of OMB. During any Fiscal Year in which the resources available to the Government are not sufficient to cover the appropriations approved for such year, the Governor, through the Director of OMB, may take administrative measures to reduce expenses. The Governor also may make recommendations to the Legislature for new taxes, or any other necessary action to meet the estimated deficiency. It has been the practice of the Director of OMB, when making funding adjustments, to allot funds in the following order of priority: to the payment of the interest on and amortization requirements for public debt; to the fulfillment of obligations arising out of legally binding contracts, court decisions on eminent domain and certain commitments to protect the name, credit and good faith of the Government, and to current expenditures in the areas of education, protection, health and welfare.

Fund Structure and Accounts

The Government reports its financial position and results of operations in funds and account groups. The Government has established the following fund categories, fund types, account groups:

Governmental Fund Types. Governmental funds are used to account for the general government functions of the Government. The following are the governmental fund types: (i) General Fund -- The general fund is the primary operating fund of the Government. It is used to account for all financial transactions, except those required to be accounted for in another fund; (ii) Special Revenue Funds -- The special revenue funds are used to account for the proceeds of specific revenue sources (other than debt service or capital projects) such as federal grants, that are legally restricted to expenditures for specific purposes; (iii) Debt Service Funds -- The debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs other than long-term debt from the operations of proprietary fund types and discretely presented component units; and (iv) Capital Projects Funds -- The capital projects funds are used to account for the financial resources used for acquisition or construction of major capital facilities not being financed by proprietary fund types and discretely presented component units.

Proprietary Fund Types. Proprietary fund types include the enterprise funds that are used to account for operations that are financed and operated in a manner similar to private business enterprises and where net income and capital maintenance are measured. Costs of providing goods and services to the general public on a continuing basis, including depreciation, are financed or recovered primarily through user charges.

Fiduciary Fund Types. Fiduciary funds are used to account for assets held by the Government in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. The following are the fiduciary fund types: (i) Expendable Trust Funds -- The expendable trust funds are used to account for trusts for which principal and income may be expended for designated purposes; (ii) Pension Trust Fund -- The pension trust fund is used to account for the assets, liabilities, and fund equity held in trust for the public employees' retirement system. It accounts for assets of which the principal may not be spent for general government purposes; and (iii) Agency Funds – The agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

Account Groups. Account groups establish control and accountability over the Government's general long-term obligations. The general long-term debt account group is used to account for long-term obligations of the Government including bonds and notes payable and other long-term liabilities excluding the liabilities of proprietary funds, pension trust fund, and discretely presented component units.

Basis of Accounting

The basis of accounting determines when the Government recognizes revenue and expenditures or expenses and related assets and liabilities. The modified accrual basis of accounting is followed by governmental fund types, expendable trust funds, and agency funds. Under the modified accrual basis of accounting, revenue is recorded when it becomes measurable and available (that is, earned and collected or expected to be collected within the next 120 days) to pay liabilities of the current period. Tax revenue, net of estimated overpayments (refunds), is recorded by the Government as taxpayers earn income (income and unemployment) as sales are made (consumption and use taxes) and as cash is received (miscellaneous taxes).

In applying the modified accrual concept to intergovernmental revenue, there are essentially two types of revenue. For the majority of grants, moneys must be expended by the Government on the specific purpose or project before any amounts will be reimbursed. Revenue is, therefore, recognized as expenditures are incurred. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the modified accrual criteria is met.

Expenditures and related liabilities are recorded in the accounting period in which the liability is incurred, except for: (i) principal payment and interest on long-term obligations, which are recorded when due; and (ii) compensated absences, retroactive union arbitration salary increase, federal funds cost disallowances, and amounts subject to legal claims and judgments under litigation that are recorded in the general long-term debt account group.

The accrual basis of accounting is used by proprietary fund types and the pension trust fund. Under the accrual basis, revenue is recognized when earned and expenses are recorded as liabilities when incurred, without regard to receipt or payment of cash. Employee and employer contributions recorded in the pension trust fund are recognized as revenue in the period in which employee services are performed. The accrual basis is also used by the public university funds, except that depreciation of fixed assets is not recorded as permitted for governmental colleges and universities.

Financial Reporting

The basic financial statements of the Government for Fiscal Years 2002 through 2004 have been audited by KPMG LLP, independent public accountants ("KPMG"), to the extent and for the years indicated in their reports thereon. Such basic financial statements have been included in reliance upon the reports of KPMG. Such reports refer to reports of other auditors with respect to the financial statements of certain funds and component units that are included in the basic financial statements of the Government but that were not audited by KPMG, contain a disclaimer over the balances and transactions of the enterprise fund caused by certain limitations in their audit scope and contain various qualifications. See "FINANCIAL STATEMENTS OF THE GOVERNMENT" and Appendix D hereto. Such basic financial statements are included herein for informational purposes only, and the information contained in these basic financial statements should not be read to in any way modify the description of the security for the Series 2006 Bonds contained herein. In addition, OMB Circular A-133 audit for Fiscal Years 2002, 2003 and 2004 performed by KPMG noted material weaknesses in internal controls over financial reporting based on an audit of the basic financial statements performed in accordance with Government Accounting Standards and events of non-compliance with certain provisions of laws, regulations, contracts and grants that have a direct and material effect on the determination of basic financial statement amounts.

The Government has contracted with KPMG to audit its basic financial statements for Fiscal Years 2003 through 2006. KPMG is in the preliminary phase of the audit for Fiscal Year 2005. The Government expects that, upon completion of the audit of Fiscal Year 2005, adjustments to the unaudited financial statements presented herein will be necessary. The Government can make no assurance that such adjustments will not be material. See "FINANCIAL STATEMENTS OF THE GOVERNMENT."

Revenues of the Government

General

The principal sources of revenues for the Government are: United States federal income taxes (collected locally as Virgin Islands income taxes); Gross Receipts Taxes and other taxes and fees levied by the Government under its own locally applicable internal revenue laws; real property taxes; federal excise taxes imposed on products of the Virgin Islands entering the United States; and other fees and taxes collected by the United States federal government. For a description of the Government's program to provide tax relief and subsidies to certain businesses to promote economic growth, see APPENDIX E — "United States Virgin Islands Economic and Demographic Information — Tax Incentive Programs."

The Revised Organic Act sets forth the taxes imposed by the United States federal government, the proceeds of which are paid into the Treasury of the Virgin Islands, including: customs duties, the United States income tax, any taxes levied by Congress on the inhabitants of the Virgin Islands, and quarantine, passport, immigration and naturalization fees collected in the Virgin Islands. In addition, the Government has the power to impose local taxes which include real property taxes, Gross Receipts Taxes, excise taxes and hotel room taxes. There are no political subdivisions with taxing power in the Virgin Islands.

Unaudited revenues of the General Fund (budgetary basis) for Fiscal Years 2001 to 2005 are presented in the table below.

Components of General Fund (Budgetary Basis) Revenues
For Fiscal Years 2001-2005
Cash Basis
($000's)

	2001		2002		2003		2004		2005	
Income[1]	$ 347,763	64.5%	$ 343,690	66.2%	$ 337,000	65.9%	$384,194	61.8%	$481,953	68.7%
Gross Receipts[2]	99,598	18.5	95,916	18.5	100,918	19.7	113,185	18.2	124,963	17.8
Real Property	50,495	9.4	46,044	8.9	36,510	7.1	77,045	12.4	35,033	5.0
Excise	15,715	2.9	12,802	2.5	13,335	2.6	15,422	2.5	17,947	2.6
Other Taxes[3]	8,921	1.7	8,031	1.5	11,827	2.3	17,854	2.9	20,661	2.9
Total Taxes	**$522,492**	**96.9%**	**$ 506,484**	**97.5%**	**$ 499,389**	**97.5%**	**$607,699**	**97.8%**	**$680,557**	**97.1%**
Other Sources of Revenue [4]	16,542	3.1%	12,873	2.5%	12,858	2.5%	13,786	2.2%	20,529	2.9%
Total Revenue	**$ 539,034**	**100.0%**	**$ 519,357**	**100.0%**	**$ 510,181**	**100.0%**	**$621,485**	**100.0%**	**$ 701,085**	**100.0%**

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(1) Figures do not reflect income tax refunds paid. In Fiscal Year 2001, income tax refunds paid were approximately $54.2 million; in Fiscal Year 2002, income tax refunds paid were approximately $41.3 million; in Fiscal Year 2003, refunds paid were approximately $41.2 million; in Fiscal Year 2004, income tax refunds paid were approximately $59.7 million; and in Fiscal Year 2005, income tax refunds paid were approximately $58.7 million. For the Fiscal Year 2006 period October 1, 2005 through July 31, 2006, income tax refunds paid were approximately $73.9 million. Cumulative unpaid income tax refunds for Fiscal Years 2001 through 2005 total approximately $7.0 million. (Source: Virgin Islands Bureau of Internal Revenue financial management system reports)

(2) Does not reflect Required Annual Moderate Income Housing Fund Deposit. See "SECURITY FOR THE SERIES 2006 BONDS — Special Escrow Agreement and Collecting Agent Agreement."

(3) Other Taxes include stamp taxes, foreign sales corporation franchise taxes, inheritance taxes and corporate franchise taxes.

(4) Other Sources of Revenues include, among other things, licenses, fees and permits, fines, forfeitures, penalties, rents and concessions, customs dues, bank fees and charges, and franchise fees.

Source: United States Virgin Islands Department of Finance unaudited revenue reports; except that, with respect to Gross Receipts Taxes, the Source is the Continuing Disclosure Quarterly Summary reports of the Authority certifying Gross Receipts Taxes Deposited with the Collecting Agent, and except as noted in Footnote (1).

Income Taxes

The principal source of revenue for the Government is income taxes. The Naval Appropriations Act, 1922, and Section 1642 of the Revised Organic Act created a separate tax structure for the Virgin Islands that mirrors the Code. To the extent the tax structure of the Virgin Islands mirrors that of the Code, any changes to federal tax laws may have an impact upon the Government's collections of certain taxes. The Government has the power to impose a territorial income tax. Currently, the Government has imposed a corporate income tax surcharge of 10%.

Income taxes are levied each year for every corporation, partnership, individual, estate or trust that meets the filing requirements of the Code. A United States taxpayer who is a permanent resident of the Virgin Islands satisfies his United States income tax obligations by filing his return with, and paying income taxes to, the Government, even if his income is from non-Virgin Islands sources. A non-resident of the Virgin Islands pays income taxes on his Virgin Islands source income to the Government, and is entitled to a foreign tax credit therefor on his United States federal tax return if the taxpayer is a United States citizen or United States domestic corporation.

Income tax collections increased in Fiscal Years 2004 and 2005 primarily as a result of, among other things, a general increase in the tax base, and as a result of the operations and tax collections from Hovensa.

Gross Receipts Taxes

Individuals and entities doing business in the Virgin Islands are required to pay a tax of 4.0% on the gross receipts of such business, without reduction for cost of goods sold or services or other expenses. Gross Receipts Taxes are pledged under the Series 2006 Loan Agreement for the payment of the Series 2006 Loan Note which secures the Series 2006 Bonds. The Government expects Gross Receipts Taxes to be received in an amount each year sufficient to pay the full amount of principal of, Redemption Premium, if any, interest on and such other amounts due and payable on the Series 1999A Bonds, the Series 2003A Bonds and the Series 2006 Bonds. See "GROSS RECEIPTS TAXES."

Real Property Taxes

Title 33 of the Virgin Islands Code, Section 2301 (the "Real Property Tax Statute") imposes a tax on all real property in the Virgin Islands. The Real Property Tax Statute sets assessed value of real property based upon its actual value and assesses a real property tax levy equal to 1.25% of 60% of assessed valuation on an arrearage basis. The proceeds of this tax are paid into the General Fund, with the exception of the first $1.5 million of such tax collected annually, which must be deposited into the St. John Capital Improvements Fund.

Noncommercial real property is reassessed once every five years and commercial real property every two years. The Virgin Islands Office of the Tax Assessor prepares an annual assessment roll and schedule of collections for each parcel of real property that is used by the Virgin Islands Office of the Tax Assessor's billing agent as the basis for issuing tax bills to all taxpayers in the Virgin Islands.

In connection with a real property tax case instituted against the Government, since 2003 the Government has been enjoined from appraising and assessing any real property in the Virgin Islands until it has modified its system of appraisal to comply with certain court mandates. Currently, the Government is unable to realize any increases in real property tax revenues due to the District Court's order. Property tax values continue at the 1998 assessment level pending the completion of the Government's revaluation project and the District Court's approval of the new valuation system; as a result, property tax revenues have been stagnant. As a result of the real property tax case, the Government has modified its system of appraisal, and the reassessment of commercial property has been completed. The court appointed Special Master is conducting random sampling reviews on the reassessed properties and is expected to present his final formal report in January 2007. The Government is expected to file a motion to lift the injunction on the reassessment of commercial and residential properties in January 2007 and expects that the Special Master's report will certify that the property tax assessment system in the Virgin Islands is credible and reliable. The revaluation is currently showing an average increase of 17% in commercial property values. Revaluation of residential property is currently underway and expected to be completed in December 2006. If the Special Master's report is dismissed or modified by the District Court, this revaluation could change. The Government anticipates that it will issue tax bills at the new assessment value in June 2007 and that it will collect taxes at the new assessment value prior to the end of the 2007 Fiscal Year.

The Government appealed the decision issued in the real property tax case but the U.S. Court of Appeals for the Third Circuit denied the appeal. The Government, through its Delegate to Congress, has proposed a bill in Congress that would repeal those sections of the United States Code, specifically Section 1401 through 1401e of Title 48, which formed the basis for the plaintiffs' actions and the assessment methodology ordered by the District Court. If the proposed bill is enacted the District Court's decision would become moot. The financial impact to the Government if the legislation is not enacted cannot be determined at this time. See "LITIGATION — Real Property Tax Case."

All real property not expressly exempt is subject to the real property tax. Exemptions include (i) property of the United States federal government subject to a $10,000 payment in lieu of real estate taxes, (ii) property of the Government, (iii) property used for religious, educational, literary, scientific and charitable purposes, (iv) property subject to the homestead exemption and (v) property for which exemptions have been granted by the Economic Development Commission (the "Commission" or the "EDC"). See APPENDIX E — "United States Virgin Islands Economic and Demographic Information — Tax Incentive Programs — Economic Development Commission." In 2004, approximately 52% of all real property in the Virgin Islands was exempt from real property taxation, including approximately 2.8% of which is due to EDC exemptions.

The following table presents property taxes, assessed value and exemptions for Virgin Islands real estate for the calendar years 2001 through 2004:

United States Virgin Islands
Property Tax - Assessed Value And Exemptions
2001-2004
(millions)

Year	Total Assessed Value(1)	Local and Federal Government(2)	Other(3)	EDC(4)	Taxed Assessed Value	Levy
2001	$16,614.5	$7,105.2	$1,122.8	$345.7	$8,040.8	$58.6
2002	$16,623.5	$6,993.1	$1,505.1	$365.0	$7,760.3	$58.2
2003	$16,859.1	$6,993.1	$1,498.3	$354.7	$8,013.0	$60.1
2004	$16,487.1	$6,977.9	$1,162.7	$453.5	$7,893.0	$59.2

(1) Pursuant to Act No. 6297 the assessed value of real property is now equal to the actual value of such real property.
(2) Includes a national park on St. John.
(3) Includes exemptions for veterans, non-profit organizations, churches, farms and homesteads, and senior citizens.
(4) EDC Program provides exemptions for 10 to 15 years.

Source: United States Virgin Islands Office of the Tax Assessor.

Delays in the issuance of tax bills since 2000 as a result of the real property tax litigation discussed above, as well as real property taxpayers' failure to pay such tax bills as a result of such case, has negatively impacted the collection of real property taxes since 2000. See "LITIGATION — Real Property Tax Case."

Excise Tax

Individuals and entities doing business in the Virgin Islands are required to pay an excise tax on all articles, goods, merchandise or commodities brought into the Virgin Islands for any business or personal use or purpose, based on the volume or value of each such article, good, merchandise or commodity. The tax covers most articles, goods, merchandise and commodities. Items specifically exempt from such excise tax include educational materials, nutritive foodstuffs, coal, fuel oil and liquid gas, molasses used for the production of rum and for agricultural purposes, animal feed, poultry feeds and commercial fertilizers, motor vehicles requiring licensing of highway use, items for sale to the United States federal government, the Government or an instrumentality of either one, items imported or manufactured in the Virgin Islands which are exported to purchasers who take delivery and actual possession outside of the Virgin Islands, as well as paper, plastics, glass or wooden materials and supplies used to package foodstuffs grown, processed, bottled or produced in the Virgin Islands, spirits, perfumes, toilet waters, bath salts, tapestry, hand-woven fabrics, handmade carpets, sweaters, shawls, scarves and ties. An exemption also is extended to franchised bus operators, costume jewelry manufacturers, EDC beneficiaries, certain film-making and other related professional equipment and licensed insurers.

There is a general exemption from the excise tax for agencies of the Government or the United States federal government, religious, charitable, benevolent or educational organizations when not engaged in the conduct of business pursuits for profit, and transactions involving a charitable or benevolent purpose.

Other Taxes

These taxes include stamp taxes, foreign sales corporation franchise taxes, inheritance taxes and corporate franchise taxes. This category increased significantly during the period from Fiscal Year 2001 to Fiscal Year 2005, primarily due to an increase in stamp taxes (approximately $9.2 million in Fiscal Year 2001 to approximately $18.6 million in Fiscal Year 2005).

There are currently four cases challenging the Government's computation of its corporate franchise taxes. See "LITIGATION — Franchise Tax Litigation Cases."

Other Revenue Sources

Other sources of General Fund revenues include, among other things, licensing fees, franchise taxes, transfer taxes, permitting fees, fines, forfeitures, penalties, custom dues and miscellaneous service charges.

Additional Revenues of the Government

In addition to the taxes and other revenues discussed above which comprise the primary General Fund revenues, there are additional taxes, fees and charges imposed by the Government which are dedicated for specific purposes.

Transportation Trust Fund Revenues

General. The Transportation Trust Fund ("TTF") was created to secure the payment of principal of, redemption premium, if any, and interest on bonds issued by the Authority to finance maintenance, improvement, repair and construction of the road and highway system. Prior to the creation of the TTF, motor fuel and highway users' taxes and traffic law violation fines were deposited into the Road Fund and driver's license and motor vehicle registration fees were deposited into the General Fund. There are currently no outstanding bonds secured by the TTF for the purpose of financing highway projects. It is anticipated that the Legislature will continue its practice of appropriating in each Fiscal Year the estimated TTF revenues to the General Fund. Any amounts remaining in the TTF following such appropriation are deposited into the Road Fund.

The following is a description of the taxes, fees and fines designated for deposit in the TTF.

Motor Fuel Taxes. A tax of 14 cents is levied on each gallon of gasoline and diesel fuel manufactured, sold, or consumed or otherwise disposed of in the Virgin Islands. The following are exempt from motor fuel taxes: (i) the Government; (ii) fuel used for fueling of aircraft, motorboats, yachts or any other motor vehicle not operating or intended for operation upon the public highway; and (iii) fuel used for industrial or other purposes not connected with the fueling of motor vehicles. Motor fuel taxes are collected throughout the Fiscal Year and are transferred directly to the TTF.

Highway Users' Tax. Before registering a motor vehicle in the Virgin Islands for the first time, every person, is required to pay a highway users' tax on the unladen weight of said vehicle at the rate of 11 cents per pound, provided that the minimum highway users' tax for any vehicle is $25.00. The following are exempted from such tax: (i) those motor vehicles to be used as either a taxicab or a bus under a franchise granted by the Governor; (ii) up to two motor vehicles used by non-profit corporations; (iii) Government vehicles subsequently sold to individuals; and (iv) vehicles belonging to individuals transferred for military duty. Highway users' taxes are collected by the BIR and are deposited daily into the TTF.

Motor Vehicle Registration Fees and Driver's License Fees. Every motor vehicle must be registered annually with the Government and an annual fee for said registration must be paid. Every three years, operators of both public and private use vehicles must renew their licenses and pay the required fee. The aforementioned registration and license fees range in unit value but have remained constant, with minor adjustments, since 1983. Registration and licensing fees are collected throughout the Fiscal Year by the Department of Police and are deposited daily in the TTF.

Traffic Law Violation Fines. The Government collects fines for traffic law violations. Traffic law violation fines are collected throughout the Fiscal Year by the Superior Court and are deposited daily to the TTF.

The following sets forth total TTF revenues for Fiscal Years 2001 through 2005:

Transportation Trust Fund Revenues
Fiscal Years 2001-2005
Cash Basis
($000's)

2001	2002	2003	2004	2005
$13,258	$13,609	$14,746	$16,003	$17,071

Source: United States Virgin Islands Department of Finance unaudited revenue reports.

Matching Fund Revenues

General. The Secretary of the United States Department of the Treasury (the "Secretary of the Treasury") is directed to make certain transfers to the Government of certain excise taxes imposed and collected under the Code in any Fiscal Year on certain products produced in the Virgin Islands and exported to the United States mainland from the Virgin Islands. Rum is the principal article presently produced in the Virgin Islands and exported to the United States which is subject to federal excise tax that qualifies for transfer to the Government under the applicable provisions of the Revised Organic Act and the Code. The term "Matching Fund Revenues" is used to denote these payments. The federal excise tax on rum exports from the Virgin Islands to the United States currently accounts for all of the Matching Fund Revenues.

The amount required to be remitted to the Government by the Secretary of the Treasury pursuant to the applicable excise tax transfer provisions is limited to an amount no greater than the total amount of local duties, taxes and fees collected by the Government in the applicable Fiscal Year.

In 1976, Section 1574a of the Revised Organic Act was enacted, in part, to authorize the Government, under certain conditions, to issue bonds secured by Matching Fund Revenues to be received by the Government. Until 1978, the Code provided that the Secretary of the Treasury would determine the amount of excise taxes imposed and collected during the calendar quarter and transfer such amounts, on a quarterly basis, to a designated Government fund, to be expended as determined by the Legislature. Section 1645 of the Revised Organic Act, enacted in 1978, changed the manner in which Matching Fund Revenues were paid. Under Section 1645, the Governor, with the concurrence of OMB, estimates the amount of federal excise taxes to be collected in the ensuing Fiscal Year. The DOI makes a prepayment of estimated Matching Fund Revenues for a Fiscal Year, which commences on October 1, prior to September 30 of the immediately preceding Fiscal Year to the designated Government fund. This prepayment is subject to subsequent adjustment for the amount of revenue actually collected by the Government and the actual amount of the above described federal excise taxes collected by the Department of Treasury during such Fiscal Year. Such adjustments are made to the advances received for the requested prepayments for the second succeeding Fiscal Year. Adjustment payments may also be made during the current Fiscal Year.

The federal excise tax rate and the rate at which such excise taxes are eligible to be transferred back to the Government (the "Cover Over Rate") are set by Congress and codified in Sections 5001(a)(1) and 7652(f) of the Code. The federal excise tax on distilled spirits produced in, or imported into the United States has over the years ranged from $10.50 per proof gallon to $13.50 per proof gallon. Until 1984, the entire amount of such excise tax qualified for transfer to the Government. As part of the Deficit Reduction Act of 1984, Congress increased the federal excise tax on distilled spirits from $10.50 per proof gallon to $12.50 per proof gallon, but capped the Cover Over Rate at $10.50 per proof gallon. As part of the Omnibus Budget Reconciliation Act of 1990, Congress increased the federal excise tax rate on distilled spirits to $13.50 per proof gallon, but maintained the cap on the Cover Over Rate at $10.50. As part of the Omnibus Budget Reconciliation Act of 1993, Congress increased the Cover Over Rate, through September 30, 1998, from $10.50 per proof gallon to $11.30 per proof gallon. As part of the Tax Relief Extension Act of 1999, Congress increased the Cover Over Rate to $13.25 per proof gallon from July 1, 1999 through December 31, 2001. As part of the Job Creation and Worker Assistance Act of 2002, Congress extended the $13.25 per proof gallon Cover Over Rate from January 1, 2002 through December 31, 2003. As part of the Working Families Tax Relief Act of 2004, Congress extended the $13.25 per proof gallon Cover Over Rate from January 1, 2004 through December 31, 2005. Congress is currently considering legislation which would extend the $13.25 per proof gallon Cover Over Rate from January 1, 2006 through December 31, 2007.

The rate of reimbursement is subject to change by Congress and no assurances can be given as to how or whether the Congress might change the Cover Over Rate.

Prior Pledge. Matching Fund Revenues are currently pledged as security for payments due under the Matching Fund Loan Notes that secure the 1998 Bonds and the 2004A Bonds (the "Matching Fund Bonds"). See "UNITED STATES VIRGIN ISLANDS—Outstanding Indebtedness of the Government." Matching Fund Revenues are not pledged under the Indenture. After payment of the annual debt service requirement of the Matching Fund Bonds, a portion of the excess Matching Fund Revenues may be deposited in the General Fund.

The following is a summary of the advances, adjustments and actual earnings of Matching Fund Revenues, as well as surplus Matching Fund Revenues after payment of debt service on the Matching Fund Bonds, for Fiscal Years 2001 through 2005.

Matching Fund Revenues
Fiscal Years 2001 – 2005
($000's)

	2001	2002	2003	2004	2005
Projected Excise Tax Revenues for Current Fiscal Year	$67,611	$60,121	$70,397	$65,849	$66,961
Plus/Minus Payment Adjustment for 2 Fiscal Years Prior	7,505(1)	(1,749)(2)	481(3)	(2,752)(4)	(3,326)(5)
Actual Advance Received for Current Fiscal Year	$75,116	$58,372	$70,878	$63,097	$63,635
Actual Earnings for Current Fiscal Year	68,092	60,337	64,103	75,001	75,126
Estimated Adjustment for 2 Fiscal Years Later	481	216	(6,294)	9,152	8,165

	2001	2002	2003	2004	2005
Actual Advance Received	$75,116	$58,372	$70,878	$63,097	$63,635
Less: Matching Fund Bonds Debt Service	40,055	40,054	40,049	40,062	41,666
Surplus After Payment of Debt Service	$35,061	$18,318	$30,829	$23,035	$21,969

(1) Adjustment for earnings vs advance for Fiscal Year 1999
(2) Adjustment for earnings vs advance for Fiscal Year 2000
(3) Adjustment for earnings vs advance for Fiscal Year 2001
(4) Adjustment for earnings vs advance for Fiscal Year 2002 and 2003. 2002 advance was calculated as $63,089 instead of $60,121 making a difference of 2,968.
(5) Adjustment to 2004 of $2,968, representing a 2002 adjustment and ($6,294) representing a 2003 adjustment.

Source: United States Virgin Islands Office of Management and Budget.

Hotel Occupancy Taxes

Pursuant to Title 33 of the Virgin Islands Code, Section 54, hotel guests in the Virgin Islands are required to pay a hotel tax of 8% of the gross room rate or rental. The hotelkeeper or innkeeper is responsible for collecting, reporting and remitting such revenues to the Government. All hotel room tax revenues are deposited into the Tourism Advertising Revolving Fund. The following table represents hotel occupancy tax collections for Fiscal Years 2001 through 2005.

Hotel Occupancy Tax Revenues
Fiscal Years 2001 – 2005
Cash Basis
($000's)

2001	2002	2003	2004	2005
$13,648	$12,198	$13,872	$14,777	$16,624

Source: United States Virgin Islands Department of Finance unaudited revenue reports.

Expenditures of the Government

A significant portion of the Government's expenditures consist of appropriations for the administration and operation of the Government's institutions and facilities (such as educational facilities, the Legislature, the Superior Court and correctional facilities) and for the operation of the Government's departments and agencies (such as the Department of Tourism, the Virgin Islands Police Department, Housing, Parks and Recreation, Economic Development, Agriculture, Human Services, Department of Planning and Natural Resources, and general administration).

Expenditures also are required under legally binding contractual agreements that the Government has previously made or existing statutes which have continuing applicability. Contractually required expenditures include amounts for debt service payments. Expenditure totals also include amounts from the General Fund contributed to the University of the Virgin Islands, interfund transfers for special projects, and operating and capital funding for other semi-autonomous authorities.

Financial Position of the Government

The following discussion of the financial position of the Government is based on financial information included in the audited basic financial statements for Fiscal Years 2002 through 2004 and unaudited financial reports prepared by the Department of Finance (on a non-GAAP basis) for Fiscal Year 2005. The audited basic financial statements for Fiscal Year 2005 are expected to be available in the first quarter of 2007. The Government expects that, upon completion of the audit of Fiscal Year 2005, adjustments to the unaudited financial statements presented herein will be necessary. The Government can make no assurance that such adjustments will not be material. See "UNITED STATES VIRGIN ISLANDS — Financial Management, Budgeting and Controls — Financial Reporting" and "FINANCIAL STATEMENTS OF THE GOVERNMENT." The basic financial statements of the Government for the Fiscal Years ended September 30, 2002, 2003, and 2004 appended hereto as Appendix D as part of this Official Statement, have been audited by KPMG to the extent and for the years indicated in their reports thereon. Such basic financial statements have been included in reliance upon the reports of KPMG. Such reports refer to reports of other auditors with respect to the financial statements of certain funds and component units that are included in the basic financial statements of the Government but that were not audited by KPMG, contain a disclaimer over the balances and transactions of the enterprise fund caused by certain limitations in their audit scope and contain various qualifications. See "FINANCIAL STATEMENTS OF THE GOVERNMENT" and Appendix D hereto. Such basic financial statements are included herein for informational purposes only, and the information contained in these basic financial statements should not be read to in any way modify the description of the security for the Series 2006 Bonds contained herein. In addition, OMB Circular A-133 audit for Fiscal Years 2002, 2003 and 2004 performed by KPMG noted material weaknesses in internal controls over financial reporting based on an audit of the basic financial statements performed in accordance with Government Accounting Standards and events of non-compliance with certain provisions of laws, regulations, contracts and grants that have a direct and material effect on the determination of basic financial statement amounts.

General

The following sets forth statements of revenues, expenditures and changes in fund balance for Fiscal Years 2002 through 2004, and the statement of revenues and expenditures for Fiscal Year 2005. The statements of revenues expenditures and changes in fund balances for Fiscal Years 2002 through 2004 have been derived from the audited financial statements of the Government and should be read in conjunction with the notes accompanying the corresponding table in the Government's Fiscal Years 2002 through 2004 financial statements (see Appendix D hereto). The statements of revenues and expenditures of Fiscal Years 2005 is based on unaudited data provided by the Government for the general fund (budgetary basis). Revenues for Fiscal Year 2005 have been posted on a cash receipt basis and payables for such years, with respect to a portion of expenditures, have been based upon invoice receipt; consequently the information presented for Fiscal Year 2005 is on a non-GAAP basis.

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Government of the Virgin Islands
Statement of Revenues, Expenditures and Changes in Fund Balances
General Fund and Debt Service Fund
For Fiscal Years 2002-2004
($000's)

	2002	2003	2004
Revenues:			
Taxes	$ 524,969	$ 562,813	$ 612,258
Federal grants and contributions	-	2,921	3,651
Charges for services	4,923	19,907	21,424
Interest and other	29,123	30,282	47,657
Total revenues	$ 559,015	$ 615,923	$ 684,990
Expenditures:			
General government	$ 266,409	$ 254,110	$ 246,658
Public safety	37,718	42,291	40,954
Health	67,150	70,106	70,808
Public housing and welfare	30,178	31,935	31,231
Education	136,784	149,538	149,077
Transportation and communication	37,090	23,193	29,950
Culture and recreation	6,759	5,554	6,203
Debt Service			
Principal	15,935	19,030	120,570
Interest	46,369	46,286	50,155
Bond issuance costs	-	1,625	13,033
Total Expenditures	$ 644,392	$ 643,668	$ 758,639
Excess (deficiency) of revenue over (under) expenditures	$ (85,377)	$ (27,745)	$ (73,649)
Other financing sources (uses):			
Bond Anticipation note issued	$ -	$ 100,000	$ -
Bonds issued	-	2,345	126,520
Transfers from other funds	99,326	101,550	87,302
Transfers to other funds	(93,699)	(98,649)	(91,155)
Premium on bonds issued	-	1,516	2,830
Total other financing Sources (uses), net	5,627	106,762	125,497
Net change in fund balances	$ (79,750)	$ 79,017	$ 51,848
Fund balances (deficits)			
Beginning of fiscal year	$ 190,199	$ 110,449	$ 189,466
End of fiscal year	$ 110,449	$ 189,466	$ 241,314

Source: Statement of Revenues, Expenditures and Changes in Fund Balances, Governmental Funds of the audited financial statements of the Government.

Government of the Virgin Islands
General Fund (Budgetary Basis)
(Unaudited) Revenues and Expenditures
For Fiscal Year 2005
($000's)

	2005
Revenues[1]:	
Taxes	$ 680,328
Other Sources of Revenue[2]	20,529
Matching Fund Contribution	17,828
Transportation Trust Fund Contribution	13,000
Other Contributions[3]	18,264
Total Revenues	$ 749,949
Expenditures[4]:	
General Government	$ 320,822
Public Safety	40,740
Health and Welfare	103,880
Education	147,968
Sanitation	16,635
Transportation	14,031
Culture and Recreation	5,364
Debt Service[5]	41,371
Total Expenditures	$690,811

1 Source: United States Virgin Islands Department of Finance Unaudited General Fund Statement of Revenues.

2 Includes licenses, fees and permits, fines, forfeitures, penalties, customs dues, and other fees and charges.

3 Includes amounts relating to WICO payment-in-lieu-of taxes, 2003 BAN Loan, Insurance Guaranty Fund, Caribbean Basin Initiative, Certificate of Title Fund, and Lottery contribution.

4 Source: United States Virgin Islands Department of Finance Expenditure Report.

5 Represents the Series 1999A Bonds, the Series 2003A Bonds and the Government's General Obligation Bonds, 1999 Series A.

Preliminary Fiscal Year 2005 Results

Based upon preliminary Fiscal Year 2005 results (budgetary basis), gross revenues in Fiscal Year 2005 were approximately $750 million and gross expenditures were approximately $691 million, resulting in a projected $59 million surplus for the year.

Proposed Fiscal Year 2007 Budget

In May 2006, the Governor submitted to the Legislature a proposed balanced budget for Fiscal Year 2007 with total revenues and expenditures of the general fund (budgetary basis) net of operating transfers equal to approximately $749 million. The Government's ability to achieve Fiscal Year 2007 actual results consistent with the proposed budget will be dependent upon certain events, including, but not limited to, approval by the Governor of the Legislature's spending plan and expenditure initiatives. The Legislature expects to finalize the Fiscal Year 2007 Budget by September 30, 2006. It is anticipated that the final Fiscal Year 2007 Budget will be acted upon by the Governor by October 1, 2006. The Fiscal Year 2006 Budget continues to be in effect until the enactment of the Fiscal Year 2007 Budget.

Prevention of Future Operating Deficits

In previous Fiscal Years, the last of which was Fiscal Year 2003, the Government experienced recurring operating deficits in its General Fund resulting from the structural imbalances, including a large public sector payroll, the nature of a three-island economy and a narrow private sector base. This condition was severely exacerbated by three billion dollars worth of damage caused by three major hurricanes since 1989 and by federal tax cuts which are mirrored in the Virgin Islands tax code. Various measures have been enacted by the Legislature and various programs have been initiated by the Executive Branch in an effort to combat the effects of these two factors. In addition to various initiatives to spur the economic activity of the territory, the Government has adopted a new building code to mitigate future hurricane damage. In addition, the Government is implementing its Enterprise Resource Planning System in order to address financial control issues. Further, to mitigate future deficits, the Government established a revenue stabilization fund in Fiscal Year 2006 with a $1 million appropriation. The 2007 Executive Budget proposes a contribution of an additional $5 million to the revenue stabilization fund. See "UNITED STATES VIRGIN ISLANDS — Financial Position of the Government – Financial Reporting and Financial Management System Improvements," and "UNITED STATES VIRGIN ISLANDS —Financial Position of the Government – Private Sector Industry Initiatives."

Federal Oversight of Certain Government Programs

Department of Education "High Risk" Grantee Designation. In 1999, the United States Department of Education ("DOE") designated certain Government departments receiving federal grants, including the Virgin Islands Department of Health and the Virgin Islands Department of Education, to be "high risk" grantees. As a result of high-risk designation, the DOE may impose certain special conditions or restrictions on its grants, including payment of a grant on a reimbursement basis. The DOE cited the cause of the "high risk" designation to be primarily the failure of the Government (as of that time) to conduct timely single audits since Fiscal Year 1994 in contravention of the Single Audit Act and findings by the OIG in the DOI Report regarding improper administration of funds received by the Government's agencies.

The Virgin Islands entered into a three-year compliance agreement (the "Compliance Agreement") in September 2002 with the DOE whereby the DOE will continuously monitor the Virgin Islands' compliance with the DOE's requirements and, if the Virgin Islands is compliant, will continue to provide grants until the expiration of this compliance agreement. To monitor and ensure compliance, the Governor created a committee comprised of the heads of the various entities identified in the compliance agreement including the Office of Management and Budget, Department of Property and Procurement, Department of Finance, Department of Justice and Department of Education. Upon expiration, the DOE can decide to certify compliance and continue to provide grants on an ongoing basis or, if non-compliant, terminate such grants or select an independent third-party overseer of grant administration. The DOE has confirmed its intention to continue to provide federal education assistance through existing grants, however, the DOE has imposed additional reporting requirements such as detailing grant expenditures, and updating progress toward completion of outstanding single audit compliance efforts.

The terms of the Compliance Agreement ended in 2005. In September 2005, DOE imposed special conditions to be included with all pending and subsequent grants to be awarded to the Virgin Islands, including the Virgin Islands Department of Education, Virgin Islands Department of Health, and Virgin Islands Department of

Human Services. One of the key special conditions required the Virgin Islands to select a third-party fiduciary agent acceptable to DOE to handle certain administrative activities related to DOE grants covered by the Compliance Agreement. The Virgin Islands, through its procurement process, selected the consulting firm of Alvarez & Marsal Public Sector Services, LLC, ("Alvarez") to serve as such third-party fiduciary. DOE has approved the selection of Alvarez to serve in such capacity. The Virgin Islands and Alvarez have executed a contract, dated August 25, 2006, pursuant to which Alvarez shall act as third-party fiduciary agent. DOE has approved said contract. With the execution of the contract providing for Alvarez's services as third-party fiduciary, the Virgin Islands is eligible for pending and future grant awards form DOE.

Additional Expenditures. As a result of a 1986 consent order issued by the Virgin Islands District Court, the Government was required to and did expend approximately $2.0 million to ameliorate the deteriorating conditions of the prisons on the Virgin Islands. On March 23, 2006 the Government was held in contempt of court by a Federal Judge for failure to comply with this consent order. A Special Master has been appointed by order of the court. Pursuant to the March 23, 2006 contempt order, the Government has deposited $100,000 with the District Court to be applied to the cost of consultants and experts retained by the Special Master. The Government shall, as ordered by the District Court, deposit such additional monies as required by the Court to cover the cost of such consultants and experts. At this time, the Government cannot give any further quantification as to any fines or penalties to which it may be subject as a result of the contempt order.

The Government has, since 1985, been subject to a consent decree, issued by the Virgin Islands District Court, governing the operation of its wastewater treatment plants ("WWTPs"). The consent decree was amended in 1996 and further modified in 2002 (the "Amended Consent Decree") to establish deadlines for the construction of new secondary treatment facilities, including the replacement of the existing St. Croix and Airport Lagoon ("Charlotte Amalie") WWTPs. The construction of the new St. Croix and Charlotte Amalie WWTPs commenced in April of 2005. Currently, both plants are approximately 80% complete and are expected to be substantially completed and ready to receive water in November 2006. The Amended Consent Decree also establishes certain interim deadlines and performance standards which must be met by the Government pending completion of the new facilities. In addition, the Amended Consent Decree establishes stipulated penalties for violation of any of the deadlines or performance standards set forth in the Amended Consent Decree. The stipulated penalties for each day of violation of each interim deadline or performance standard range from $500 per day to $5,000 per day.

Other DOI Office of Inspector General Reports

Pursuant to its duties as government comptroller of the Virgin Islands (see "UNITED STATES VIRGIN ISLANDS — General"), the OIG of the DOI has issued numerous audit reports over the past several years, which have included claims of, among other things, ineffective revenue collection efforts, noncompetitive bidding and ineffective administration of contracts, and lack of oversight for use of federal funds. The Government has agreed with some of the findings of the audits and has disputed other findings. Government implementation of the various recommendations of the OIG included within these reports are in various stages of implementation.

In March 2002, the OIG delivered a report regarding "Management Challenges for Insular Area Governments, An Opportunity for Improvements." This report was intended to identify what the OIG believed to be the major management challenges for the insular area governments, including the Government. This report noted that the Government continues to face severe financial difficulties. Audits of the Government conducted by the OIG since Fiscal Year 1999 have disclosed weaknesses in the financial and operational activities of various Virgin Islands services, departments and agencies. This report also stated that the Government's lack of adequate audit resolution and implementation of recommendations contributed to the existence of long-standing financial management deficiencies. As a result, the OIG stated that its audit reports often disclose problems that are identical or at least similar to ones that had been disclosed by prior audit reports. The Government has taken steps to improve its financial management systems. Since October 2003, the Office of Management and Budget has been working with OIG to resolve and close outstanding recommendations made in audit reports issued by OIG. As of July 2006, this effort has resulted in the resolution and closure of 215 recommendations from more than 50 audit reports issued since 1991. To date, 59 recommendations remain outstanding. Of said 59 recommendations, 12 require legislative action and have been submitted to the Legislature of the Virgin Islands. The Office of Management and Budget is continuing to work with OIG to resolve and close the remaining 47. See "Financial Position of the Government — Financial Reporting and Financial Management System Improvements" below.

Financial Reporting and Financial Management System Improvements

In recognition of the importance of financial reporting and the need to accurately and timely monitor its financial position, the Government has made significant strides in improving its financial monitoring and transparency. As of the beginning of Fiscal Year 1999, the Government's most recent independent audit of its financial statements was for Fiscal Year 1994. This was in contravention of the Single Audit Act and the Government was in jeopardy of losing its future federal funding. Accordingly, completion of audited financial statements was given high priority. As of June 2006, the Government has completed audits for eight fiscal years (namely Fiscal Years 1995, 1998, 1999, 2000, 2001, 2002, 2003 and 2004). The audit for 2005 is expected to be completed on or before March 31, 2007.

The Government has enhanced, and continues to enhance, the computerization of key departments (such as the BIR, Department of Finance, Department of Education, and Department of Property and Procurement) to better manage both Government receivables and payables and to avoid interest charges and penalties. The Government also has invested approximately $9.0 million to date to automate the billing and collection system for income, corporate, excise and gross receipts taxes and has brought a new processing system on-line. Additionally, the Government has implemented a management and reorganization plan at the BIR to increase and improve the BIR's tax audits and to generally improve the timeliness and effectiveness of tax collections as well as to reduce tax refund liabilities. The new financial management systems of the BIR allow much more accurate and timely identification and categorization of delinquent tax receivables, which permits the Government to deploy its collection efforts more efficiently with maximum impact.

Private Sector Industry Initiatives

In order to decrease the dependence on public sector employment in the Virgin Islands, the Government recognizes the need to stimulate private industry to generate other employment opportunities and increased economic activity. Since 1999, the Government has significantly increased its marketing efforts and focus of its EDC Program to bring additional businesses to the Virgin Islands. In addition to the long-term effect on employment and revenues to the Virgin Islands that these businesses create, the impact of this new investment is also reflected immediately in the substantial increase in income tax revenues that result as of the relocation of the principals of the EDC beneficiaries to the Virgin Islands. The Government has granted benefits to a wide variety of businesses, with a specific focus on financial services companies, and tourism- and medical technology-based enterprises. Legislation has been adopted that would qualify the marine industry for tax benefits by the Commission in an attempt to revitalize this industry.

The Government also has assisted various of the Virgin Islands' large private sector businesses to expand either facilities or production, creating both construction activity as well as increased employment opportunities. The Government issued industrial development bonds on behalf of Hovensa L.L.C. ("Hovensa"), the Territory's largest real property taxpayer, for a portion of the funding for an approximately $615.0 million coker that was constructed beginning in 2000 and placed into service in 2002 that allows the refinery to process a wider range of petroleum sources. To further improve its production output, Hovensa is completing a desulphurization project and has commenced a second clean fuels program. In April 2004, the Authority issued $50,660,000 of industrial development bonds on behalf of Hovensa to reimburse Hovensa for certain costs of completing the coker and related facilities. The Authority has approved a tentative $110 million private activity bond issue in connection with expenditures for solid waste and sewage facilities for the Hovensa Plant. In 2002, the Government worked with Virgin Islands Rum Industries Limited ("VIRIL"), the rum production company that generates all of the Matching Fund Revenues, and the federal Environmental Protection Agency to negotiate an effluent discharge agreement that permits VIRIL to increase production by up to 20% to better meet currently unsatisfied demand. The Government is currently studying possible treatment technologies which would enable VIRIL to further expand its production (and the Government to further increase its Matching Fund Revenues).

Recognizing the importance of tourism to the economy of the Virgin Islands, the Government has undertaken several projects to better facilitate and encourage visitor arrivals, including: improvement of the Red Hook Ferry Terminal; revitalization of the Frederiksted, St. Croix waterfront; development of the Crowne Bay Cruise Ship Terminal and retail center; development of a commercial port at Enighed Pond in St. John; redevelopment of the Kings Alley Hotel and Retail Walk in downtown Christiansted; and a new St. Croix Conference Center and Hotel. Other private sector projects recently completed or currently in progress that the Government has encouraged include: the expansion and refurbishment of the Ritz-Carlton Hotel and Timeshare; construction of the Sapphire Beach Recreational Center; construction of the Marriott timeshare development in St.

Thomas; the new Yacht Haven Marina and Hotel; and the proposed development by the Pequot Tribal Nation of a beachfront hotel, casino and marina. See APPENDIX E— "United States Virgin Islands Economic and Demographic Information—Construction and Real Estate" and "—Capital Program."

The Government also is involved in the coordination and facilitation of two housing development projects in St. Thomas/St. John ($77.0 million) and St. Croix ($50.3 million). Funding for these projects is expected to come from the developers and homeowners as well as federal programs. The Governor submitted and received Senate approval to authorize the establishment of two technology parks to be operated by a newly created Research and Technology Park Corporation in conjunction with the University of the Virgin Islands. The purpose of these parks is to position the Virgin Islands in the rapidly expanding area of electronic commerce and intellectual property.

The Government is also involved with the construction of two specialized hospital facilities. The St. Croix Cardiac Care Center is expected to cost approximately $10 million and is scheduled to be completed in the next two and a half years. The St. Thomas Cancer Center was completed in March 2006 at a cost of $18 million.

Outstanding Indebtedness of the Government

General Obligation Debt

The Revised Organic Act restricts the principal amount of general obligation debt which the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the Virgin Islands. As of September 10, 2006, the Government has approximately $550,847,000* of general obligation debt outstanding. Such amount is within the statutory debt limitation established under the Revised Organic Act.

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* This total includes $162,870,000 of the Series 1999A Bonds which will be refunded using the proceeds of the Series 2006 Bonds, but does not include the Series 2006 Bonds.

Outstanding Bonds and Similar Obligations

Outlined in the tables below are the general obligations of the Government issued either by the Government or the Authority, and the revenue obligations of the Government, outstanding as of September 10, 2006:

Summary of Outstanding General Obligations

Issuer	Issue Description	Outstanding Amount	Security
United States Virgin Islands	General Obligation Bonds, 1999 Series A (the "General Obligation Bonds")	$3,820,000*	General obligation of the Government
Virgin Islands Public Finance Authority	Revenue Bonds, Series 1999A (Virgin Islands Gross Receipts Taxes Loan Note)**	$273,565,000	Gross Receipts Taxes Loan Note payable by the Government and general obligation of the Government
Virgin Islands Public Finance Authority	Revenue Bonds, Series 2003A (Virgin Islands Gross Receipts Taxes Loan Note)	$265,145,000	Gross Receipts Taxes Loan Note payable by the Government and general obligation of the Government
Virgin Islands Public Finance Authority	Subordinate Lien Revenue Notes, Series 2005 (Virgin Islands Gross Receipts Taxes Loan Note) (the "2005 Subordinate Lien Revenue Notes")	$4,317,275	Gross Receipts Taxes Loan Note payable by the Government and general obligation of the Government
Virgin Islands Public Finance Authority	Subordinate Lien Revenue Notes, Series 2006 (Virgin Islands Gross Receipts Taxes Loan Note) (the "2006 Subordinate Lien Revenue Notes")	$4,000,000	Gross Receipts Taxes Loan Note payable by the Government and general obligation of the Government

Summary of Outstanding Revenue Obligations

Issuer	Issue Description	Outstanding Amount	Security
Virgin Islands Public Finance Authority	Revenue and Refunding Bonds (Virgin Islands Matching Fund Loan Notes) 1998 Series A, B, C, D and E (the "1998 Bonds")	$445,025,000	Matching Fund Loan Notes payable by the Government
Virgin Islands Public Finance Authority	Revenue Bonds (Federal Highway Reimbursement Anticipation Loan Note), Series 2002 (the "2002 Bonds")	$12,940,000	Federal Highway Administration, monies derived from the United States federal government
Virgin Islands Public Finance Authority	Revenue Bonds, Series 2004A (Virgin Islands Matching Fund Loan Note) (the "2004A Bonds")	$91,705,000	Matching Fund Loan Notes payable by the Government

*Source: United States Virgin Islands Department of Finance. The remaining figures in this table are per the trustee for the Bond Issues.
**A portion of the Series 1999A Revenue Bonds in the aggregate principal amount of $162,870,000 are being refunded from a portion of the proceeds of the Series 2006 Bonds.

In addition, the Government and the Authority have issued Refinery Facilities Senior Secured Tax-Exempt Revenue Bonds (Hovensa Refinery) (the "Hovensa Bonds") on behalf of Hovensa for construction of a coker. The Hovensa Bonds are solely secured by, and paid from, revenues of Hovensa.

The 1998 Bonds, the 2002 Bonds and the 2004A Bonds are each a special limited obligation of the Authority secured by revenues of the Authority that are different and separate from the Gross Receipts Taxes and the Loan Notes pledged as part of the Trust Estate. The General Obligation Bonds are direct and general obligations of the Government and do not have recourse to the Gross Receipts Tax. Such outstanding bonds (and the Hovensa Bonds) do not constitute the "Bonds" under the Indenture. No recourse may be had for the payment of the 1998 Bonds, the 2002 Bonds, the 2004A Bonds or the Hovensa Bonds against the general funds of the Authority, the Government's general funds or the Gross Receipts Taxes that secure the Series 1999A Bonds, the Series 2003A Bonds, the Swap Agreement, the Series 2006 Bonds the 2005 Subordinate Lien Revenue Notes, the 2006 Subordinate Lien Revenue Notes or any future Bonds issued under the Indenture.

The Authority is considering funding a portion of the Government's unfunded pension liability through the issuance of up to $500 million in bonds. No bonds have been authorized by the Legislature, which must do so to permit their issuance. See "VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY – Other Factors – Government Employees Retirement System".

Other Factors

Labor Relations

There are 13 distinct labor organizations subject to 28 collective bargaining agreements and a total of 28 pay plans currently in place for Governmental employees. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and non-professional workers, in different departments throughout Government represented by different unions. Of the approximately 9,735 workers in the executive branch of the Government, approximately 8,000 belong to unions.

Currently, the Government has contractual obligations to various local labor unions relating to executive branch Government workers for retroactive salary increases aggregating approximately $394.0 million accruing from Fiscal Years 1992 through 2005. Although the Government has a footnote on its balance sheet equal to the above-mentioned retroactive salary increases, as of the present date, all of the salary increases incorporated in the current union contract are reflected in the current salary rates for the individual union members. While negotiated contract provisions requiring appropriation of funds do not become binding under Virgin Islands law until there is such an appropriation, salary increase provisions of negotiated contracts remain on the Government's balance sheet, thus accruing retroactive amounts to be paid at a future date when there is a respective appropriation.

As a result of the Government's inability to implement negotiated contract salary increases with various unions by the negotiated contracts' effective dates, certain unions and their members have periodically staged strikes and/or job work actions against the Government. The job actions moderately interrupted the operations of the Government and had a mild financial impact (e.g., overtime pay to auxiliary personnel, loss of instruction to students, legal fees and associated costs). However, the Government has been successful in obtaining permanent injunctions against such work actions, which has served as strong deterrents for future strikes and/or job actions. To date, 14 contracts with the various unions are current, and 14 have expired, but have been extended on a day-to-day basis.

Government Employees Retirement System

The Employees' Retirement System of the Government of the Virgin Islands (known as GERS) requires that benefits promised under the law to members of the Virgin Islands Employees Retirement System be funded on an "actuarial reserve" basis. As of September 30, 2004, the net assets of GERS were approximately $1.35 billion. The audit reports of GERS for its 2004 fiscal year was qualified since (i) the effects of such adjustments, if any, with respect to cash overdraft with the Department of Finance in the approximate amount of $10.5 million; (ii) the effects of not accruing contributions pursuant to the Early Retirement Act of 1994; (iii) the effects of not having performed a recent valuation of the real estate investment in the GERS complex related to the portion of the St. Thomas building held for lease; and (iv) the effects of not recognizing the appreciation in value of the GERS investment in Havensight Mall in the then current fiscal year.

According to an Actuarial Evaluation, dated as of September 30, 2003 (the "Actuarial Evaluation"), as of September 2003, the number of contributing members was approximately 10,037, the number of retirees was 5,900 and the number of surviving beneficiaries was 193. The total liability for future benefits to pensioners and beneficiaries was $1,969 million. The valuation of the assets in the GERS was an estimate predicated upon the book value of such assets on a date certain. For the period ended September 30, 2003, benefits paid to retirees was approximately $129.7 million. Employee and employer contributions rates to the system were as follows:

	Employee Contribution Rate
Members of the Legislature	9.0%
All other regular employees	8.0
Public Safety employees	10.0
Hazardous duty employees who elect early retirement system	10.0
Judges	11.0

Source: Government Employees Retirement System

The actuarial position suggests the amount which, when added to the total of employee contributions, would be sufficient to meet the actuarial costs. According to GERS, as of September 30, 2003 current employer contributions were 14.5% of membership payroll.

According to the Actuarial Evaluation, the statutory government and member contribution rates were not sufficient to meet the cost of the GERS. To meet the full actuarial cost (including the system's current cost and the amount necessary to amortize the unfunded actuarial liability over 30 years from October 2, 2003), the contribution rates would have to be increased such that, in total, an additional 17.5% of payroll contribution or $59.3 million would be necessary each year from some combination of member and/or Government sources. As of September 30, 2003, GERS' unfunded actuarial accrued liability was approximately $922.0 million.

The Government, acting as custodian, is responsible for the collection and disbursement of all loan repayments, employee contributions, and employer contributions. Such amounts are deposited by the Government into a special account of the Special Revenue Fund held by the Government. Funds deposited in such accounts are legally restricted to expenditure for specified purposes.

A provision of the Virgin Islands Code (Section 718 of Title 3 of the Virgin Islands Code, 2005 United States Virgin Islands Act No. 6794) prohibits GERS from providing any increases in benefits to members or beneficiaries of GERS, unless the Government has identified a specific funding source and concurrently makes a provision for the funding of all future benefit improvements on a sound actuarial basis in the annual budget of the Government.

Insurance

The Government's enterprise fund provides workmen's compensation for public and private individuals. The Government does not carry general liability insurance coverage on its properties or for the acts of its employees, relying instead on self-insurance and statutory liability limitations. However, as a result of an agreement with FEMA with respect to properties and structures damaged by Hurricane Hugo and repaired with federal disaster assistance, the Government has obtained insurance for hospitals, schools and other insurable public buildings that were repaired with such federal assistance. The Government currently maintains a blanket insurance policy (the "Policy") covering buildings and structures set forth in a related schedule of values totaling approximately $919.3 million. Such schedule of values sets forth the value of each building and/or structure covered by the Policy, as well as contents, computer and software receivables, valuable paper and equipment. The Policy has a loss limit of $100.0 million for each and every occurrence, with a per occurrence sublimit of $45.0 million in respect to windstorm and $45.0 million in the annual aggregate in respect to flood, and $100 million in the annual aggregate for earthquake. There can be no assurance that the Government will not suffer a casualty or liability loss beyond the Policy limits of coverage or the limits of its self-insurance capabilities.

BONDOWNER RISKS

THE PURCHASE AND OWNERSHIP OF THE SERIES 2006 BONDS MAY INVOLVE INVESTMENT RISKS. PROSPECTIVE PURCHASERS OF THE SERIES 2006 BONDS ARE URGED TO READ THIS OFFICIAL STATEMENT IN ITS ENTIRETY. THIS SECTION ENTITLED "BONDOWNER RISKS" DOES NOT PURPORT TO PROVIDE INVESTORS WITH A COMPREHENSIVE ENUMERATION OF ALL POSSIBLE INVESTMENT RISKS. THE FACTORS SET FORTH BELOW, AMONG OTHERS, MAY AFFECT THE SECURITY FOR THE SERIES 2006 BONDS. IN ADDITION TO POSSIBLE ADVERSE AFFECTS ON SECURITY FOR THE SERIES 2006 BONDS, PURCHASERS SHOULD BE AWARE THAT THESE FACTORS, AMONG OTHERS, MAY ADVERSELY AFFECT THE MARKET PRICE OF THE SERIES 2006 BONDS IN THE SECONDARY MARKET.

Risks to Gross Receipts Taxes

Economic Factors

The number of businesses operating in the Virgin Islands will impact the Government's collections of Gross Receipts Taxes. Any substantial decrease in business enterprises may have an adverse impact upon the amount of Gross Receipts Tax revenues. While there are numerous public and private sector projects in various stages of development which are expected to stimulate economic activity in the Virgin Islands, no assurances can be given that any of these projects will be completed, or, if completed, result in the projected economic activity.

Hurricanes

The potential for hurricanes poses a risk to the collection of Gross Receipts Taxes. Significant damage from a hurricane could result in a loss of business enterprises and a decrease in tourism and other economic activity which could have an adverse effect on Gross Receipts Taxes Revenues. Three major hurricanes have struck the Virgin Islands since 1989 causing in excess of three billion dollars worth of damage however, it should be noted that in the aftermath of the previous hurricanes which have hit the Virgin Islands since 1989 Gross Receipt Tax Revenues have not declined. See — GROSS RECEIPTS TAXES.

Economic Development Commission

The Government offers various tax incentives that promote industrial and economic development in the Virgin Islands. The EDC provides qualifying businesses various benefits including up to a 100% Gross Receipts Tax exemption. Additionally, the EDC Program allows some qualifying investors to receive limited extensions or renewals of tax benefits. Currently, 112 enterprises are operating with incentive benefits granted pursuant to the EDC Program, 80 enterprises have been approved for benefits but are not yet in operation and an additional 29 enterprises are awaiting final certification to the Commission. Investors receiving tax benefits under this program include hotels and other tourism-related businesses, goods-producing enterprises and businesses serving customers outside the Territory. Granting of Commission benefits could have a material adverse affect on Gross Receipts Taxes available to make payments in connection with the Series 2006 Loan Note (see "SECURITY FOR THE SERIES 2006 BONDS — Series 2006 Loan Note" and "—Covenants"). See APPENDIX E — "United States Virgin Islands Economic and Demographic Information — Tax Incentives Programs — Economic Development Commission."

Government's Financial Condition

Accumulated and Recurring Operating Deficits

The Government faces certain potential claims against the General Fund which are not recorded in the General Fund because such liabilities do not meet the definition of a fund liability but are reflected in the Government's General Long-Term Debt Account Group. The most significant of these claims is the Government's contractual liability to various local labor unions for retroactive salary increases and current pay-rate increases. See "UNITED STATES VIRGIN ISLANDS — Other Factors — Labor Relations."

A second potential claim is that the Government's and member contribution rates in connection with the Government Employees Retirement System are not sufficient to meet the cost of funding the Government Employees Retirement System. See "UNITED STATES VIRGIN ISLANDS — Government Employees Retirement System. Such amount was estimated by the actuaries of the Government Employee Retirement System to be $922 million as of September 30, 2003.

Further, a significant source of tax revenue for the Government is derived from its two largest non-tourist industries - Hovensa, the Territory's largest real property taxpayer, and VIRIL, the rum production company that generates all of the excess Matching Fund Revenues. Factors negatively impacting either of these companies could result in an adverse impact on the Government's income tax and real property tax revenue, and Matching Fund Revenues respectively. See "UNITED STATES VIRGIN ISLANDS — Additional Revenues of the Government — Matching Fund Revenues" and "UNITED STATES VIRGIN ISLANDS — Revenues of the Government — Income Taxes." and "— Property Taxes".

Audited Financial Statements

The basic financial statements of the Government for the Fiscal Years ended September 30, 2002, 2003 and 2004 appended hereto as Appendix D as part of this Official Statement, have been audited by KPMG to the extent and for the years indicated in their reports thereon. Such basic financial statements have been included in reliance upon the reports of KPMG. Such reports refer to reports of other auditors with respect to the financial statements of certain funds and component units that are included in the basic financial statements of the Government but that were not audited by KPMG, contain a disclaimer over the balances and transactions of the enterprise fund caused by certain limitations in their audit scope and contain various qualifications. See "FINANCIAL STATEMENTS OF THE GOVERNMENT" and Appendix D hereto. Such basic financial statements are included herein for informational purposes only, and the information contained in these basic financial statements should not be read to in any way modify the description of the security for the Series 2006 Bonds contained herein.

Federally-Disciplined Programs

The Government is subject to a compliance agreement with the DOE and consent decrees requiring expenditures for its prisons and WWTPs which may impact the financial condition of the Virgin Islands. See "UNITED STATES VIRGIN ISLANDS — Financial Position of the Government — Federally-Disciplined Programs."

Federal Bankruptcy Code Presently Inapplicable

The Bankruptcy Reform Act of 1978, Title 11, United States Code, as amended (the "Federal Bankruptcy Code"), provides a codified regime for the reorganization, liquidation or debt adjustment of various types of insolvent debtors. Generally, only a "person" or a "municipality" may be debtor in a case under the Federal Bankruptcy Code. The term "person" includes individuals, partnerships and corporations, but does *not* include any "governmental unit." For purposes of the Federal Bankruptcy Code, a governmental unit which cannot file for protection under the Federal Bankruptcy Code, would be (i) a Territory, such as the Government, or (ii) an instrumentality of a Territory, such as the Authority. The term "municipality" is defined to mean a political subdivision or public agency or instrumentality of a State. Therefore, neither the Government nor the Authority may be a debtor in a case under the Federal Bankruptcy Code. Consequently, no Bondowner would be able to avail itself of Federal Bankruptcy Code provisions protecting rights of creditors since the Government and the Authority are both "governmental units" and neither of them is a "person" or a "municipality" for purposes thereof. Since neither the Authority nor the Government is subject to the Federal Bankruptcy Code, there can be no assurance as to how the pledge of Gross Receipts Taxes would be treated by a court of law in the event of an insolvency or other inability to pay debt by the Government or the Authority.

Limitation of Remedies

The Indenture does not provide for acceleration of the Bonds, including the Series 2006 Bonds, if an Event of Default occurs and is continuing.

Tax-Exempt Status of the Series 2006 Bonds

The tax-exempt status of the Series 2006 Bonds is based on the continued compliance by the Authority and the Government with certain covenants relating generally to restriction on use of the facilities financed with the Series 2006 Bonds, and the use and investment of the proceeds of the Series 2006 Bonds. Failure to comply with such covenants could cause interest on the Series 2006 Bonds to become subject to federal income taxation retroactive to the date of the issue of the Series 2006 Bonds. The Series 2006 Bonds are not subject to mandatory redemption or acceleration in such case, nor is any provision made for stepped-up interest.

Continuing Disclosure

As of the date hereof, the Government has not provided the required annual financial information on a timely basis under its continuing disclosure certificate for the Series 1999A Bonds and the 2003A Bonds, primarily because the Government audits have not been updated in time. However, they have established procedures to assure compliance in connection with the issuance of the Series 2006 Bonds. The Government and Authority have provided the required quarterly financial information on a timely basis. See "CONTINUING DISCLOSURE; DISCLOSURE DISSEMINATION".

LITIGATION

There is no pending litigation concerning the Series 2006 Bonds being offered or any of the documents under which the Series 2006 Bonds are being offered.

Outlined below are the significant litigation cases and tax case which impact the Government. Despite the Government's involvement with the claims outlined below, the Government does not believe that any of these claims or actions will have a material adverse affect on the amounts of the Government's funds available for the payment of the Government's obligations in connection with the Series 1999A Bonds, the Series 2003A Bonds or the Series 2006 Bonds.

The Authority is not a party to any other litigation, claims or actions that would, individually or in the aggregate, have a material adverse affect on its existence.

Franchise Tax Litigation Cases

There are currently four Virgin Islands cases challenging the Government's computation of its corporate franchise tax (the "Franchise Tax Litigation Cases"). The Franchise Tax Litigation Cases involve a dispute over the definition of the term "capital stock used in conducting business in the Virgin Islands," as found in Title 13 Virgin Islands Code Section 531(a)(the "Franchise Tax Statute"). The Government's position is that the Franchise Tax Statute taxes the amount paid to a corporation by shareholders for the issuance of shares, and any amount allocated to par value and paid in capital upon a subsequent reorganization. The plaintiff taxpayers (including certain domestic Virgin Islands corporations and foreign corporations doing business in the Virgin Islands) argue that the tax is calculated only on the par value of the stock. The issues presented in the Franchise Tax Litigation Cases relate only to domestic and foreign corporations doing business in the Virgin Islands.

During Fiscal Year 2002, the Government collected approximately $1,329,000 in franchise taxes from domestic and foreign corporations doing business in the Virgin Islands. If the tax base during Fiscal Year 2002 had reflected only the "par value" of each company's stock, as urged by the plaintiffs taxpayers, the franchise tax collected from Virgin Islands domestic and foreign corporations during Fiscal Year 2002 could have been as low as approximately $478,000, representing a decrease of $851,000.

Virgin Islands law imposes a six-year statute of limitation on tax refund claims against the Government. Applying the Fiscal Year 2002 figures to the six years preceding Fiscal Year 2002, the Government, if the plaintiffs prevail in the Franchise Tax Litigation Cases, may be liable, with respect to Virgin Islands domestic and foreign corporations, to pay franchise tax refunds of approximately $5,100,000 for overpayment claims covering the past six years. The approximately $5,100,000 potential liability figure is based upon the assumption that: (i) the average number of domestic and foreign corporations in existence during the six fiscal years preceding Fiscal Year 2002 approximates the number of said corporations that were in existence in Fiscal Year 2002; (ii) the Fiscal Year 2002 collection levels apply to each of the six years preceding Fiscal Year 2002; and (iii) all corporations claiming a franchise tax refund have commenced the appropriate actions. It is unlikely that all of the aforementioned conditions shall apply.

The Government previously appealed three of the Franchise Tax Litigation Cases to the United States Court of Appeals for the Third Circuit, On appeal the Third Circuit Court of Appeals remanded the cases to the Superior Court of the Virgin Islands. On remand, the Superior Court ruled against the Government in each of the three cases. In one of the cases, Miller Properties, the Government intends to file another appeal to the Third Circuit Court of Appeal. The Government expects that a favorable ruling on such appeal would overrule the adverse decisions rendered in the other two cases. The fourth Franchise Tax Litigation Case is currently before the Superior

Court pending a decision by the Court. A favorable ruling on the appeal before the Third Circuit Court of Appeal in the Miller Properties case would have a binding effect on the fourth case. The Government has determined that in the event the plaintiffs prevail in the Franchise Tax Litigation Cases, the Government could be liable to pay franchise tax refunds up to $5,100,000.

Real Property Tax Case

In addition to the Franchise Tax Litigation Cases, there is a consolidated real property tax case that may have a fiscal impact on the Government. In a decision issued on May 12, 2003 in Berne Corp v. Government of the Virgin Islands, 2003 WL 21078073 (D. Virgin Islands) (the "Berne Decision"), a consolidated case representing eight actions and 21 plaintiffs, the District Court of the Virgin Islands issued a permanent injunction enjoining the Government from appraising and assessing any real property in the Virgin Islands until the Government has modified its system of appraisal to comply with certain District Court mandates. Specifically, the order issued by the Berne Court enjoined the Government from assessing any and all real property in the Virgin Islands until: (1) the Virgin Islands' "property tax system has been certified as reliably and credibly assessing and taxing all real property on its actual value," (2) "the Board of Tax Review consistently holds hearings and reaches determinations on appeals within sixty (60) days," and (3) "the Department of Finance consistently remits any refunds awarded by the Board decision within thirty (30) days[.]"

Further, the order issued under the Berne Decision enjoined the Government from (1) issuing "any property tax bills for tax year 2002 and beyond" and (2) making any "further effort to collect any tax bills already issued for any property, commercial or otherwise, for tax years 1999, 2000, and 2001" unless and until "the Legislature amends 33 V.I.C. § 2402 to provide for the retroactive adjustment of the bills on all classes of property for 1999, 2000, 2001, 2003, 2004, and for a reasonable time thereafter until a fair and equitable system capable of reliably and credibly assessing all real property at actual value is in place." The Berne injunctions had the potential of depriving the Government of over $50,000,000 in tax dollars annually.

In response to the Berne Decision, the Virgin Islands Legislature enacted Act No. 6586, which, among other things, amended 33 V.I.C. § 2402 to provide that:

> [T]he Tax Assessor may issue tax bills and collect taxes at the 1998 assessment level, for all classes of real property, including commercial and non commercial real property, for the tax years 1999, 2000, 2001, 2002, 2003, and 2004, before the revision of the property tax and [resolution of] the Property Tax Litigation, provided that the tax due shall be subject to adjustment for each year according to the assessed value based on the new system implemented. The taxpayer shall be entitled to a credit applied to his subsequent years' tax bills or a refund for any over-payment that may have accrued as the result of the payment of any of his tax bills for any year from 1999 until the new system is implemented.

The Government enacted Act No. 6586 for the purpose of satisfying the conditions set out in the Berne Decision to lift the ban on the issuance and collection of the Government's 2002 real property tax bills and the collection of delinquent real property taxes from prior years. The Government used the 1998 assessment level as the basis for tax collection under Act No. 6586 as required by the District Court.

On August 13, 2003, the District Court entered an order permitting the Government to issue and collect from non-plaintiff taxpayers its 2002 real property taxes based on the 1998 assessments and to collect from non-plaintiff taxpayers delinquent real property taxes for prior years, also based on the 1998 assessments. Following the District Court's August 13, 2003 order, the Governor issued Executive Orders authorizing the issuance of the Government's 2002 real property tax bills and providing that such bills shall be due and payable by October 31, 2003.

The Government appealed the Berne Decision to the U.S. Court of Appeals for the Third Circuit. In a decision issued in June 2004, the Third Circuit Court of Appeals upheld the Berne decision against the Government. Given the adverse decision against the Government, the Government's use of the assessment methodology ordered by the District Court could result in either an increase or decrease in taxes in each individual case. Accordingly, the financial impact to the Government of an adverse decision cannot be determined at this time.

Through its Delegate to Congress, the Government has proposed a bill in Congress that would repeal those sections of the United States Code, specifically Section 1401 through 1401e of Title 48, which formed the basis for the plaintiffs' actions in the Berne case and the assessment methodology ordered by the District Court. The

Government anticipates that action will be taken on the proposed bill within the calendar year. If the proposed bill is enacted into law, the Berne decision will become moot.

United States Department of Justice Investigation of Potential Clean Water Act Violations by the Government of the Virgin Islands

The Environmental Crimes Section of the U.S. Department of Justice is investigating whether the Government of the Virgin Islands has violated the Clean Water Act ("CWA") as a result of its operation of the Virgin Islands' wastewater system. The focus of the investigation involves alleged bypasses of untreated wastewater at the three major pump stations on St. Croix during the period 2001 though 2005. It is the position of the Government that there was no material violation of the CWA during this period and that any alleged bypasses were permissible under its CWA permit and/or court orders. Nevertheless, if the Government is determined to have violated the CWA, the Government may face fines of up to $15 - $30 million. However, the amount of fines imposed on persons determined to have violated the CWA typically is significantly less than the total potential fines.

TAX MATTERS

The Code establishes certain requirements which must be met at and subsequent to the issuance and delivery of the Series 2006 Bonds in order that interest on the Series 2006 Bonds will be and remain excludable from gross income for federal income tax purposes. Included among these continuing requirements are certain restrictions and prohibitions on the use of bond proceeds, restrictions on the investment of bond proceeds and other moneys or properties, and the rebate to the United States of certain earnings in respect of investments. Failure to comply with the continuing requirements may cause the interest on the Series 2006 Bonds to be includible in gross income for federal income tax purposes retroactive to the date of their issuance irrespective of the date on which such non-compliance occurs. The Authority and the Government have covenanted to comply in the Indenture, the Series 2006 Loan Agreement and the documents relating to federal tax matters delivered at the time of delivery of the Series 2006 Bonds (the "Tax Certificates") with certain procedures, and have made certain representations and certifications, designed to assure satisfaction of the requirements of the Code.

In the opinion of Buchanan Ingersoll & Rooney PC, New York, New York, Bond Counsel, and subject to the limitations set forth in the immediately succeeding paragraph, under the existing statutes, regulations, administrative interpretations and court decisions as of the date of such opinion, the interest on the Series 2006 Bonds will not be included in gross income for federal income tax purposes pursuant to Section 103 of the Code. Furthermore, Bond Counsel is of the opinion that interest on the Series 2006 Bonds is not a specific "item of tax preference" for purposes of the federal alternative minimum tax imposed on individuals and corporations. Bond Counsel notes, however, that interest on the Series 2006 Bonds held by a corporation (other than an S corporation, regulated investment company, real estate investment trust or real estate mortgage investment conduit) is included in adjusted current earning for purposes of calculating certain taxes including the federal alternative minimum tax imposed on corporations. Corporate purchasers of the Series 2006 Bonds should consult their tax advisors regarding the computation of any alternative minimum tax.

Bond Counsel expresses no opinion regarding other federal income tax consequences caused by the receipt or accrual of interest on the Series 2006 Bonds. The proposed form of the opinion of Bond Counsel is attached to this Official Statement as Appendix H.

The difference, if any, below the initial public offering price to the public (excluding bondhouses, brokers or similar persons acting in the capacity of underwriters or wholesalers) of a maturity of the Series 2006 Bonds at which price a substantial amount of such maturity is sold and the amount payable at maturity constitutes original issue discount, which will be excluded from gross income to the same extent as interest on the Series 2006 Bonds for purposes of federal income taxation. The Code provides that the amount of original issue discount accrues in accordance with a constant interest method based on the compounding of interest, and that an owner's adjusted basis for purposes of determining an owner's gain or loss on disposition of Series 2006 Bonds with original issue discount (the "OID Bonds") will be increased by such amount. A portion of the original issue discount that accrues in each year to an owner which is a corporation of an OID Bond will be included in the calculation of the corporation's federal alternative minimum tax liability. Consequently, corporate owners of any OID Bond should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability although the owner of such OID Bond has not received cash attributable to such original issue discount in such year.

Certain Series 2006 Bonds may initially be offered to the public at prices greater than the amounts payable thereon at maturity (the "Premium Bonds"). As a result of the tax cost reduction requirements of the Code relating to amortization of bond premium, under certain circumstances an initial owner of Premium Bonds may realize a taxable gain upon disposition of such Premium Bonds even though they are sold or redeemed for an amount equal to such owner's original cost of acquiring such Premium Bonds. Owners of Premium Bonds are advised that they should consult with their own tax advisors with respect to the tax consequences of owning such Premium Bonds.

In addition to the matters referred to in the preceding paragraphs, prospective purchasers of the Series 2006 Bonds should be aware that the accrual or receipt of interest on the Series 2006 Bonds may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences may depend upon the recipient's particular tax status or other items of income or deduction. Bond Counsel expresses no opinion regarding any such consequences. Examples of such other federal income tax consequences of acquiring or holding the Series 2006 Bonds include, without limitation, that (i) with respect to certain insurance companies, the Code reduces the deduction for loss reserves by a portion of the sum of certain items, including interest on the Series 2006 Bonds, (ii) interest on the Series 2006 Bonds earned by certain foreign corporations doing business in the United States may be subject to a branch profits tax imposed by the Code, (iii) passive investment income, including interest on the Series 2006 Bonds, may be subject to federal income taxation under the Code for certain S corporations that have certain earnings and profits, (iv) the Code requires recipients of certain Social Security and certain other federal retirement benefits to take into account, in determining gross income, receipts or accruals of interest on the Series 2006 Bonds, and (v) reductions or limitations in the earned income credit to taxpayers who may otherwise be eligible. In addition, the Code denies the interest deduction for indebtedness incurred or continued by a taxpayer, including without limitation, banks, thrift institutions and certain other financial institutions to purchase or carry tax-exempt obligations, such as the Series 2006 Bonds.

Bond Counsel is also of the opinion that interest on the Series 2006 Bonds is exempt under existing statutes from personal income taxes imposed by the United States Virgin Islands, by any state, other territory or possession of the United States or any political subdivision thereof, or by the District of Columbia.

Certain requirements and procedures contained or referred to in the Indenture, the Series 2006 Loan Agreement and the Tax Certificate and other relevant documents may be changed, and certain actions may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of Bond Counsel. Buchanan Ingersoll & Rooney PC expresses no opinion as to any Series 2006 Bond or the interest thereon if any such change occurs or action is taken upon the advice or approval of bond counsel other than themselves.

Bond Counsel has not undertaken to determine in the future (or to inform any person) whether any actions taken (or not taken or events occurring or not occurring) after the date of issuance and delivery of the Series 2006 Bonds may affect the tax status of interest on the Series 2006 Bonds. No assurance can be given that future legislation or amendments to the Code, if enacted into law, will not contain provisions which could directly or indirectly reduce the benefit of the exclusion of the interest on the Series 2006 Bonds from gross income for federal income tax purposes.

All quotations from and summaries and explanation of provisions of law do not purport to be complete and reference is made to such laws for full and complete statements of their provisions.

FINANCIAL STATEMENTS OF THE GOVERNMENT

General

The basic financial statements of the Government for the Fiscal Years ended September 30, 2002, 2003 and 2004 appended hereto as Appendix D as part of this Official Statement, have been audited by KPMG LLP, independent public accountants ("KPMG"), to the extent and for the years indicated in their reports thereon. As presented below, such basic financial statements have been included in reliance upon the reports of KPMG. Such reports refer to reports of other auditors with respect to the financial statements of certain funds and component units that are included in the basic financial statements of the Government but that were not audited by KPMG, contain a disclaimer over the balances and transactions of the enterprise fund caused by certain limitations in their audit scope and contain various qualifications. See Appendix D hereto. Such basic financial statements are included herein for informational purposes only, and the information contained in these basic financial statements should not be read to in any way modify the description of the security for the Series 2006 Bonds contained herein. See "UNITED STATES VIRGIN ISLANDS — Financial Management, Budgeting and Controls — Financial Reporting."

2004 Audit Report

The basic financial statements of the Government of the United States Virgin Islands as of and for the year ended September 30, 2004, were audited by KPMG as stated in their report dated June 7, 2006, accompanying the basic financial statements. KPMG did not audit the financial statements of Virgin Islands Public Finance Authority, West Indian Company, Virgin Island Water and Power Authority, Tobacco Settlement Financing Corporation, Virgin Islands Port Authority, Virgin Islands Housing Authority (VIHA), University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Lottery (VI Lottery), Virgin Islands Economic Development Authority, Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA). These financial statements were audited by other auditors whose reports thereon have been furnished to KPMG, and their opinions, insofar as they relate to the amounts included in the basic financial statements pertaining to such activities, funds, and component units indicated above, are based on the reports of the other auditors. In addition, the scope of KPMG's audit work was not sufficient to enable them to express, and they did not express, an opinion on the business-type activities as of September 30, 2004, and the changes in financial position for the year then ended, because of the matters discussed below:

- The basic financial statements included a receivable for unemployment insurance contributions in the business-type activities of $1.1 million as of September 30, 2004. The basic financial statements of September 30, 2003 did not include a receivable for unemployment insurance contributions in the business-type activities due to inadequate records. The receivable for unemployment insurance contributions at September 30, 2003, enters into the determination of revenue and change in net assets for the year ended September 30, 2004. The Government's records did not permit, nor was it practicable to extend their auditing procedures sufficiently to determine the extent to which the revenue and change in net assets of the business-type activities for the year ended September 30, 2004 may have been affected by this condition.

- The effects of the adjustments as might have been determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether capital assets of $45 thousand, net accounts receivables of $887 thousand, due to the general fund of $4.5 million, and other liabilities of $115 thousand in the financial statements of the VI Lottery were fairly stated.

- The basic financial statements did not include a liability for workers' compensation claims, and the Government's records did not permit, nor was it practical for them to extend their auditing procedures sufficiently to determine the extent by which the business-type activities may have been affected by this condition.

Also, their auditors' report for opinion units other than business-type activities, was qualified for the following:

- The effects of not being able to determine the extent to which the expenses and change in net assets of the governmental activities may have been affected by the exclusion of a liability for landfill closure and post-closure costs in the beginning net assets because no calculation had been made.

- The effects of not being able to determine the extent to which the revenue, change in fund balance/net assets of the general fund (a major fund) and the governmental activities may have been affected by the exclusion of a receivable for corporate income taxes pertaining to tax year 2002 in the beginning net assets due to inadequate records.

- The effects of not being able to determine the extent to which the revenue, change in net assets, and cash flows of the unemployment insurance fund (a major fund) may have been affected by the exclusion of a receivable for unemployment insurance contributions in the beginning net assets due to inadequate records.

- The effects of the adjustments as might have been determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether capital assets and land held for sale, amounting to $67 million and $26 million in the financial statements of VIHA and VIHFA, respectively, were fairly stated.

- The effects on the financial position of the aggregate remaining fund information and the respective changes in financial position of (i) Employee's Retirement System of the Government of the Virgin Islands (GERS) not accruing contributions pursuant to the Early Retirement Act of 1994 and reporting its real estate investment in the GERS complex related to the portion of the St. Thomas building held for lease at fair value, and (ii) the adjustments as might have been determined to be necessary, had KPMG been able to obtain satisfactory evidence with respect to the cash overdraft of GERS with the Department of Finance.

The auditors' report contains an emphasis paragraph for the Government's restatement of beginning net assets and fund balances due to 1) the adoption of Governmental Accounting Standards Board Statement No. 39, *Determining Whether Organizations Are Component Units*, effective October 1, 2003; 2) the reclassification of the PFA capital projects fund as a major fund; and 3) the inclusion of the VI Lottery financial information.

2003 Audit Report

The basic financial statements of the Government as of and for the year ended September 30, 2003, were audited by KPMG as stated in their report dated May 6, 2005, accompanying the basic financial statements. KPMG did not audit the financial statements of Virgin Islands Public Finance Authority, West Indian Company, Virgin Island Water and Power Authority, Tobacco Settlement Financing Corporation, Virgin Islands Port Authority, Virgin Islands Housing Authority (VIHA), University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Economic Development Authority, Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA). These financial statements were audited by other auditors whose reports thereon have been furnished to KPMG, and their opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based on the reports of the other auditors. In addition, the scope of KPMG's audit work was not sufficient to enable them to express, and they did not express, an opinion on the business-type activities as of September 30, 2003, and the changes in financial position for the year then ended, because of the matters discussed below:

- KPMG was unable to determine the extent to which the business-type activities may have been affected by the exclusion of a receivable for unemployment insurance contributions due to inadequate records.

- The basic financial statements did not include the Virgin Islands Lottery, and the amount by which this omission would affect the assets, liabilities, net assets, revenue, and expenses of the business-type activities was not reasonably determinable.

- The basic financial statements did not include a liability for workers' compensation claims, and the Government's records did not permit, nor was it practical for them to extend their auditing procedures sufficiently to determine the extent by which the business-type activities may have been affected by this condition.

Also, their auditors' report, was qualified for the following:

- The effects of not maintaining accounting records for corporate income tax receivables related to tax year 2002 in the general fund and governmental activities and not recording a provision for landfill closure and postclosure costs in governmental activities.

- The effects of not being able to determine the extent to which the unemployment insurance fund (a major fund) may have been affected by the exclusion of a receivable for unemployment insurance contributions due to inadequate records.

- The effects on the financial position of the aggregate discretely presented component units, and the respective changes in financial position of VIHA not reporting an equity interest in a joint venture and the adjustments, if any, as might have been determined to be necessary, had the other auditors been able to (i) satisfy themselves as to the proprietary of the revenue and expenses of the VIHA reported in the statement of activities for the year ended September 30, 2003, and (ii) obtain sufficient audit evidence to determine whether capital assets and land held for sale, amounted to $71 million and $25 million in the financial statements of VIHA and VIHFA, respectively.

- The effects on the financial position of the aggregate remaining fund information and the respective changes in financial position of GERS not accruing contributions pursuant to the Early Retirement Act of 1994 and the adjustments, if any as might have been determined to be necessary, had KPMG been able to (i) obtain satisfactory evidence with respect to the cash overdraft with and amounts due from the Department of Finance and (ii) allocate the appreciation in real estate investments between this and prior years.

2002 Audit Report

The basic financial statements of the Government as of and for the year ended September 30, 2002, were audited by KPMG as stated in their report dated April 23, 2004, accompanying the basic financial statements. KPMG did not audit the financial statements of Virgin Islands Public Finance Authority, West Indian Company, Tobacco Settlement Financing Corporation, Virgin Islands Port Authority, Virgin Islands Housing Authority (VIHA), University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Economic Development Authority, Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA). These financial statements were audited by other auditors whose reports thereon have been furnished to KPMG, and their opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based on the reports of the other auditors.

KPMG auditors' report was qualified for the following:

- the effects of not maintaining accounting records for income tax receivables stated at $87 million nor recording a receivable for gross receipts taxes in the general fund and governmental activities and not recording a provision for landfill closure and postclosure costs in governmental activities, the respective financial position of the governmental activities.

- the effects of the adjustments, if any, as might have been determined to be necessary had the Virgin Islands Lottery (the Lottery) been audited for the business-type activities and had KPMG been able to examine evidence regarding the receivable for unemployment insurance in the business-type activities, and the unemployment insurance fund (a major fund).

- the effects on the financial position of the aggregate discretely presented component units, and the respective changes in financial position of the adjustments, if any, as might have been determined to be necessary, had the other auditors been able to: (i) satisfy themselves as to the propriety of certain transactions of the Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital) recorded in the statement of net assets as of September 30, 2001, (ii) obtain sufficient audit evidence to determine whether capital assets and land held for sale, amounting to $74 million and $25 million in the financial statements of VIHA and VIHFA, respectively.

The auditors' report contains an emphasis paragraph for the Government's adoption of Governmental Accounting Standard Board (GASB) Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* GASB Statement No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities,* GASB No. 37, *Basic Financial Statement—and Management's Discussion and Analysis—for State and Local Governments: Omnibus,* GASB Statement No. 38, *Certain Financial Statement Note Disclosures,* and GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements,* as of October 1, 2001.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

The accuracy of (a) the mathematical computations of the adequacy of the principal of and interest on the Government Obligations to be held in the Escrow Fund to pay the principal or respective redemption prices, as applicable, of the Refunded Bonds and interest thereon when due and (b) the mathematical computations supporting the conclusion that the Series 2006 Bonds are not "arbitrage bonds" under the Code will be verified by Causey Demgen & Moore Inc., independent certified public accountants. Such verification will be based upon certain information supplied to them by the Authority through the Underwriters.

LEGAL OPINIONS

Certain legal matters incident to the issuance of the Series 2006 Bonds are subject to the approving opinion of Buchanan Ingersoll & Rooney PC, New York, New York, Bond Counsel. The approving opinion of Bond Counsel, substantially in the form set forth in Appendix H hereto, is to be furnished upon delivery of the Series 2006 Bonds. Bond Counsel's approving opinion does not express any opinion with respect to information in this Official Statement. Certain legal matters will be passed upon for the Underwriter by its counsel, Duane Morris LLP, New York, New York.

FINANCIAL ADVISOR

The Authority has retained Banc of America Securities LLC of New York, New York, as financial advisor in connection with the issuance of the Series 2006 Bonds. Although Banc of America Securities LLC has assisted in the preparation of this Official Statement, Banc of America Securities LLC is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement.

CONTINUING DISCLOSURE; DISCLOSURE DISSEMINATION

Continuing Disclosure

The Authority and the Government have each covenanted, for the benefit of Bondowners, to provide certain annual and quarterly financial information and operating data relating to the Authority and the Government, respectively (collectively, the "CDA Reports"), and to provide notices of the occurrence of certain enumerated events (the "Notices"). The CDA Reports and Notices will be provided to each nationally recognized municipal securities information repository. The specific nature of the information to be contained in the CDA Reports or the Notices is summarized in Appendices G-1 and G-2, respectively, "— Proposed Form of Continuing Disclosure Agreement." These covenants have been made in order to assist the Underwriter in complying with the Securities and Exchange Commission Rule 15c2-12 (the "Rule").

As of the date hereof, the Government has not provided the required annual financial information on a timely basis under its continuing disclosure certificate for the Series 1999A Bonds and the 2003A Bonds, primarily because the Government audits have not been updated in time. The Government and Authority have provided the required quarterly financial information on a timely basis.

Disclosure Dissemination Agent

In order to provide certain continuing disclosure with respect to the Series 2006 Bonds in accordance with the Rule, the Authority and the Government have each entered into a Disclosure Dissemination Agent Agreement (the "Disclosure Dissemination Agreement") for the benefit of the Bondowners with Digital Assurance Certification, L.L.C. ("DAC"), under which the Authority and the Government have designated DAC as Disclosure Dissemination Agent.

The Disclosure Dissemination Agent has only the duties specifically set forth in the Disclosure Dissemination Agreement. The Disclosure Dissemination Agent's obligation to deliver the information at the times and with the contents described in the Disclosure Dissemination Agreement is limited to the extent the Authority and the Government have provided such information to the Disclosure Dissemination Agent as required by the applicable Disclosure Dissemination Agreement. The Disclosure Dissemination Agent has no duty with respect to the content of any disclosures or notice made pursuant to the terms of the Disclosure Dissemination Agreement. The Disclosure Dissemination Agent has no duty or obligation to review or verify any information in the Annual Reports, Quarterly Reports, audited financial statements, notice of Notice Event or Voluntary Report (in each case as such terms are defined in the Disclosure Dissemination Agreement), or any other information, disclosures or notices provided to it by the Authority or the Government and shall not be deemed to be acting in any fiduciary capacity for the Authority, the Government, the Bondowners or any other party. The Disclosure Dissemination Agent has no responsibility for the Authority's or the Government's failure to report to the Disclosure Dissemination Agent a Notice Event or a duty to determine the materiality thereof. The Disclosure Dissemination Agent shall have no duty to determine or liability for failing to determine whether the Authority or the Government have complied with the Disclosure Dissemination Agreement. The Disclosure Dissemination Agent may conclusively rely upon certifications of the Authority and the Government at all times.

RATINGS

Moody's Investors Service ("Moody's") has assigned the Series 2006 Bonds a rating of "Aaa" and Standard & Poor's Rating Group ("S&P") has assigned the Series 2006 Bonds a rating of "AAA", both such ratings being assigned with the understanding that upon delivery of the Series 2006 Bonds, a municipal bond insurance policy will be delivered by Financial Guaranty Insurance Company, and Moody's and S&P have assigned underlying ratings of "Baa3" and "BBB+", respectively to the 2006 Bonds. Such ratings reflect only the view of Moody's and S&P respectively, and any desired explanation of the significance of any of the above ratings should be obtained from the applicable rating agency. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance that either rating will continue for any given period of time or that either rating will not be revised downward or withdrawn entirely by the rating agency furnishing the same, if in the judgment of such rating agency, circumstances so warrant. Any such downward revision or withdrawal of a rating may have an adverse effect on the market price of the Series 2006 Bonds.

UNDERWRITING

The Series 2006 Bonds are being purchased by UBS Securities LLC (the "Underwriter"). The purchase price payable by the Underwriter for the Series 2006 Bonds is $229,592,316.21. The Underwriter is obligated to purchase all of the Series 2006 Bonds, if any are purchased, the obligation to make such purchase being subject to certain terms and conditions set forth in the Purchase Contract by and between the Authority and the Underwriter, the approval of certain legal matters by counsel and certain other conditions. The Underwriter will receive an underwriting discount of $1,469,835.14 in connection with the underwriting of the Series 2006 Bonds.

The initial public offering price and other terms respecting the offering and sale of the Series 2006 Bonds may be changed from time to time by the Underwriter after the Series 2006 Bonds are released for sale, and the Series 2006 Bonds may be offered and sold at prices other than the initial offering price, including sales to certain dealers (including dealers who may sell the Series 2006 Bonds into investment accounts, some of which may be managed by the Underwriter) and certain dealer banks and banks acting as agents.

An affiliate of the Underwriter will be the 2006 Swap Provider under the 2006 Swap Agreement.

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MISCELLANEOUS

In this Official Statement, any summaries or descriptions of provisions in the Indenture, the Series 2006 Loan Agreement, the Series 2006 Loan Note or the Special Escrow Agreement and all references to other materials not purported to be quoted in full are only brief outlines of certain provisions thereof and do not constitute complete statements of such documents or provisions. Reference is hereby made to the complete documents relating to such matters for further information, copies of which may be obtained from the principal corporate trust office of the Trustee.

Any statement in this Official Statement involving matters of estimates or opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Official Statement is not to be construed as a contract or agreement between the Authority and the owners or holders of, or of interests in, any of the Series 2006 Bonds.

Financial and statistical information has been provided by the Authority and the Government, certain of its agencies and instrumentalities and other sources deemed reliable by the Authority and the Government. The Underwriter is not responsible for any of such information nor has the Underwriter independently verified such information.

This Official Statement is submitted in connection with the sale of the Series 2006 Bonds and may not be reproduced or used, as a whole or in part, for any other purpose. The execution and delivery of this Official Statement has been duly authorized by the Authority.

VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY

By: /s/ Kent E. Bernier, Sr.
Director of Finance and Administration

THE GOVERNMENT OF THE VIRGIN ISLANDS

By: /s/ Bernice A. Turnbull
Commissioner of Finance

Dated: September 19, 2006

APPENDIX A

GLOSSARY OF CERTAIN DEFINED TERMS

Certain terms used in the Original Indenture, the Seventh Supplemental Indenture and the Series 2006 Loan Agreement are defined below unless otherwise defined herein or the context clearly indicates otherwise. When and if such terms are used in this Official Statement they shall have the meanings set forth below. Any capitalized term used in this Official Statement regarding the Indenture and the Series 2006 Loan Agreement and not defined herein shall have the meaning given such term by the Indenture and the Series 2006 Loan Agreement.

Account or **Accounts** means any account or accounts, as the case may be, established pursuant to Section 5.01 of the Indenture.

Accreted Value means with respect to any Bond that is a Capital Appreciation Bond, for each authorized denomination, an amount equal to the principal amount of such Capital Appreciation Bond (determined on the basis of the initial offering price for such denomination at maturity thereof) plus the amount of earnings which would be produced on the investment of such principal amount, assuming compounding (as set forth in the applicable Supplemental Indenture) beginning on the dated date of such Capital Appreciation Bond and ending at the maturity date thereof, at a yield which, if produced until maturity, will produce an amount equal to such denomination at maturity. As of any Valuation Date, the Accreted Value of any Capital Appreciation Bond means the amount set forth for such date in the applicable Supplemental Indenture authorizing such Bond and as of any date other than a Valuation Date, the sum of (i) the Accreted Value on the preceding Valuation Date and (ii) the product of (1) a fraction, the numerator of which is the number of days having elapsed from the preceding Valuation Date and the denominator of which is the number of days from such preceding Valuation Date to the next succeeding Valuation Date, using for such calculation 30 day months and a 360 day year and (2) the difference between the Accreted Values for such Valuation Dates.

Act means, collectively, the Virgin Islands Revised Organic Act of 1954, as amended, 48 U.S.C. Chapter 12, §§1541 through 1645 (West 1987), Title 29 of the Virgin Islands Code, and 1999 V.I. Act 6297 and other applicable law, as the same may be amended from time to time.

Act of Bankruptcy, means (i) the entity under consideration shall have applied for or consented to the appointment of a custodian, receiver, trustee or liquidator of all or substantially all of its assets; (ii) a custodian shall have been appointed with or without consent of such entity; (iii) such entity has made a general assignment for the benefit of creditors, or has filed a voluntary petition in bankruptcy, or a petition or an answer seeking reorganization or an arrangement with creditors or to take advantage of any insolvency law; (iv) such entity has filed an answer admitting the material allegations of a petition in any bankruptcy, reorganization or insolvency proceeding, or taken any action for the purpose of effecting any of the foregoing; (v) a petition in bankruptcy shall have been filed against such entity and shall not have been dismissed for a period of 60 consecutive days; (vi) an order for relief has been entered under the Bankruptcy Code with respect to such entity; (vii) an order, judgment or decree shall have been entered, without the application, approval or consent of such entity by any court of competent jurisdiction approving a petition seeking reorganization of such entity or appointing a receiver, trustee, custodian or liquidator of such entity or substantially all of its assets, and such order, judgment or decree shall have continued unstayed and in effect for any period of 60 consecutive days; or (viii) such entity shall have suspended the transaction of its usual business.

Additional Bonds means Bonds other than the Initial Series of Bonds.

Adjusted Debt Service Requirement means, for any period, as of any date of calculation, the aggregate Debt Service on Outstanding Bonds or on Outstanding Bonds of a particular Series for such period taking into account the following adjustments:

(i) With respect to Bonds that bear interest at a Variable Interest Rate, the aggregate Debt Service thereon is determined as if each such Bond bore interest at the Certified Interest Rate; provided, however, (1) if the Authority (A) enters into a Qualified Swap Agreement with a Swap Provider requiring the Authority to pay a fixed interest rate on a notional amount, and (B) has made a determination that such Qualified Swap Agreement was entered into for the purpose of providing substitute interest payments for a particular maturity of Bonds in a principal amount equal to the notional amount of the Qualified Swap Agreement, then during the term of such Qualified Swap Agreement and so long as the Swap Provider under such Qualified Swap Agreement is not in default under such Qualified Swap Agreement, the interest rate on such Bonds shall be determined as if such Bonds bore interest at the fixed interest rate payable by the Authority under such Qualified Swap Agreement, and (2) if (A) Bonds of a specific maturity within a Series bear interest at a Variable Interest Rate and Bonds which bear a Variable Interest Rate of another Series with the same maturity are issued in an equal principal amount to the first such Series of Bonds of the same maturity and (B) the Variable Interest Rate of the first Series of such Bonds varies inversely to the Variable Interest Rate of the second Series of such Bonds of the same maturity so that the combined interest rate for the aggregate principal amount of such Bonds of the same specific maturity for both such Series is determined by the Authority to result in a combined fixed interest rate, then so long as the same principal amount of each maturity of such Series of Bonds remain Outstanding, the aggregate Debt Service thereon shall be determined as if all such Variable Rate Bonds of such Series and maturity bore interest at the combined fixed interest rate so determined by the Authority with respect to such aggregate principal amount of such Bonds.

(ii) With respect to Fixed Interest Rate Bonds, if the Authority (1) enters into a Qualified Swap Agreement with a Swap Provider requiring the Authority to pay a variable interest rate on a notional amount and (2) has made a determination that such Qualified Swap Agreement was entered into for the purpose of providing substitute interest payments for a particular maturity of Bonds in a principal amount equal to the notional amount of the Qualified Swap Agreement, then during the term of such Qualified Swap Agreement and so long as the Swap Provider under such Qualified Swap Agreement is not in default under such Qualified Swap Agreement the interest rate on such Bonds is determined as if such Bonds bore interest at the Certified Interest Rate on the notional amount of such Bonds.

(iii) Except to the extent described in (iv) below, with respect to Bonds secured by a Credit Facility, the aggregate Debt Service thereon shall be deemed to include any payments required to reimburse the related Credit Provider (including any Debt Service Reserve Account Credit Provider), but shall not include any amounts payable as principal of and interest and premium with respect to any reimbursement obligation to such Credit Provider except and to the extent that such payments on such reimbursement obligation are required to be made to the Credit Provider in excess of any corresponding Debt Service with respect to such Bonds during such period.

(iv) With respect to Optional Tender Bonds, the aggregate Debt Service thereon shall not include any amounts payable to a Credit Provider pursuant to any reimbursement obligation arising as the result of the payment of any purchase price with respect to such Bonds on a Purchase Date except to the extent that, and for any period during which, the Authority is obligated to reimburse the Credit Provider for payments made by such Credit Provider directly or indirectly in satisfaction of any obligation to purchase such Bonds on any Purchase Date following the application of any proceeds of any remarketing of such Bonds.

(v) The aggregate Debt Service for any period on any Bonds shall not include (1) any interest which is payable from Capitalized Interest which is to be transferred to the Debt Service Account for payment of interest on such Bonds or (2) the amount of Debt Service on Bonds to be paid from amounts in a Debt Service Reserve Account at the time of such computation for the period in question, but only if any such amount described in (1) or (2) is available and is to be applied under the applicable Supplemental Indenture to make interest payments on such Bonds when due.

(vi) If the Authority enters into a Qualified Swap Agreement with a Swap Provider requiring the Authority to pay any amount in excess of the amount to be received by the Authority in connection therewith for the period for which any calculation of Adjusted Debt Service Requirement is to be made hereunder, then, to the extent not taken into account in (i) and (ii) above, the net amount of such payments which may be required of the Authority (using the Certified Interest Rate or its equivalent for such purpose if such amount is subject to any variation and excluding any breakage fees or termination payments paid by the Authority) shall be included in Adjusted Debt Service Requirements.

For purposes of this definition of Adjusted Debt Service Requirement, the principal and interest portions of the Accreted Value of Capital Appreciation Bonds and the Appreciated Value of any Deferred Interest Bonds becoming due at maturity or by virtue of Mandatory Sinking Fund Requirements shall be included in the calculation of accrued and unpaid and accruing interest or principal installments on the date on which or for the period during which such amounts become due and payable unless otherwise specified in the Supplemental Indenture authorizing such Capital Appreciation Bonds or Deferred Interest Bonds.

Aggregate Debt Service for any period means, as of any date of calculation, the sum of the amounts of Debt Service for such period with respect to the Bonds.

Annual Administrative Fee means the amount authorized to be transferred annually from the Expense Account to the Authority to pay the Authority's expenses in accordance with the annual budget approved by the Board of the Authority.

Annual Debt Service means, as of any date of calculation with respect to a specified Bond Year, Debt Service plus any premium, if any, payable for the Bonds in the respective Bond Year.

Appreciated Value means with respect to any Bond that is a Deferred Interest Bond until the Interest Commencement Date thereon, for each authorized denomination, an amount equal to the principal amount of such Deferred Interest Bond (determined on the basis of the initial offering price for such denomination at the Interest Commencement Date thereof plus the amount, of earnings which would be produced on the investment of such principal amount, assuming compounding (as set forth in the applicable Supplemental Indenture) beginning on the dated date of such Deferred Interest Bond and ending on the Interest Commencement Date, at a yield which, if produced until the Interest Commencement Date, will produce an amount equal to such denomination at the Interest Commencement Date. As of any Valuation Date, the Appreciated Value of any Bond that is a Deferred Interest Bond means the amount set forth for such date in the Supplemental Indenture authorizing such Deferred Interest Bond and as of any date other than a Valuation Date accruing for that period or due and payable on that date, the sum of (i) the Appreciated Value on the preceding Valuation Date and (ii) the product of (1) a fraction, the numerator of which is the number of days having elapsed from the preceding Valuation Date and the denominator of which is the number of days from such preceding Valuation Date to the next succeeding Valuation Date, using for such calculation 30 day months and a 360 day year, and (2) the difference between the Appreciated Values for such Valuation Dates.

Approved Project means any public improvement or public undertaking authorized by act of the Legislature of the Virgin Islands and by resolution of the Authority to be financed with the proceeds of Authority Bonds.

Authority means the Virgin Islands Public Finance Authority, a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government of the Virgin Islands, or, if said Authority shall be abolished, any authority, board, body or officer succeeding to the principal functions thereof.

Authority Disclosure Dissemination Agreement means the Authority Disclosure Dissemination Agreement by and between the Authority and DAC, dated as of September 1, 2006.

Authorized Officer means the Executive Director or Chairman of the Authority or any other person authorized by the Authority to perform an act or sign a document on behalf of the Authority for purposes of the Indenture or a Supplemental Indenture as set forth in a Supplemental Indenture or a certificate of the Authority which has been delivered to the Trustee.

Available Revenues means the "available amounts" of the Government within the meaning of Treasury Regulations Section 1.148-6(d) (iii) minus (a) an amount equal to 5% of the expenditures paid by the Government from current revenues for the prior fiscal year of the Government and (b) amounts directed to the Series 1999A

Bonds, the Working Capital Series 2003A Bonds or the Working Capital Series 2006 Bonds other than by virtue of mandatory sinking fund redemption or scheduled amortization.

Bankruptcy Code means the United States Bankruptcy Reform Act of 1978, as amended, defined as Title 11 of the United States Code, as amended, or any substitute or replacement legislation.

Board means the Board of Directors of the Authority.

Bond or **Bonds** means any bond or bonds, as the case may be, issued pursuant to the Indenture or any Supplemental Indenture, and may include notes, commercial paper, or other obligations.

Bond Counsel means an attorney or firm of attorneys of nationally recognized expertise in matters relating to the issuance of obligations by states, territories and local governments and political subdivisions and instrumentalities thereof.

Bond Insurance Policy means the municipal bond new issue insurance policy issued by the Bond Insurer that guarantees payment of principal of and interest on the Series 2006 Bonds.

Bond Insurer means Financial Guaranty Insurance Company, a New York Stock insurance company, or any successor thereto.

Bond Register means the register maintained by the Bond Registrar pursuant to Section 3.04 of the Indenture.

Bond Registrar means the Trustee, any successor trustee or bond Registrar appointed as Bond Registrar pursuant to Section 3.04 of the Indenture.

Bond Related Costs means (i) all costs, fees and expenses of the Authority incurred or reasonably related to any Liquidity Facility, Credit Facility, any remarketing or other secondary market transactions and any Qualified Swap Agreement (whether requiring the Authority to pay fixed or variable amounts and excluding breakage fees on or termination payments under such Qualified Swap Agreements) that the Authority has determined was entered into for the purposes of providing substitute interest payments for the maturity of the Bond, (ii) initial and acceptance fees of any Fiduciary together with any fees of Bond Counsel, attorneys, feasibility consultants, engineers, financial advisors, remarketing agents, rebate consultants, accountants and other advisors retained by the Authority in connection with the Bond, and (iii) any other fees, charges and expenses that may be lawfully incurred by the Authority relating to the Bond, including, without limitation, any obligation of the Authority to a Credit Provider for the Bond to repay or reimburse any amounts paid by such Credit Provider due to payment under such Credit Facility and any interest on such repayment obligation.

Bond Service Charges means for any applicable time period or date, principal of and premium, if any, and interest payments due and the fees, expenses and costs of the Trustee, Bond Registrar and Paying Agent, if any, on any of the Bonds accruing for that period or due and payable on that date. In determining Bond Service Charges accruing for any period or due and payable on any date, Mandatory Sinking Fund Requirements accruing for that period or due on that date shall be included together with any amount required to be paid for the replenishment of any Debt Service Reserve Account.

Bond Year means a period of twelve (12) consecutive months beginning on October 2 in any calendar year and ending on October 1 of the succeeding calendar year.

Bondowner, Holder, Owner or **Registered Owner** means the Person in whose name a Series 2006 Bond is registered on the Bond Register.

Business Day means any day that is not a Saturday, Sunday or legal holiday in the United States Virgin Islands or a day on which the Trustee, the Special Escrow Agent or banking institutions organized under the laws of the United States Virgin Islands are legally authorized to close.

Capital Appreciation Bonds means any Bonds as to which interest is payable only at the maturity or prior redemption thereof for the purposes of (i) receiving payment of the Redemption Price, if any, of a Capital Appreciation Bond that is redeemed prior to maturity, and (ii) computing the principal amount of Capital Appreciation Bonds held by the Owner thereof in giving any notice, consent, request, or demand pursuant to the applicable Supplemental Indenture for any purpose whatsoever, the Accreted Value of a Capital Appreciation Bonds as of a specific date shall be deemed to be its principal amount as of such date.

Capitalized Interest means that portion of the proceeds of any Series of Bonds together with any available earnings thereon that are intended to be used to pay interest due or to become due on any Bonds.

Capitalized Interest Subaccount means the subaccount by that name in the Debt Service Account established by the Indenture and the applicable Supplemental Indenture.

Certified Interest Rate means a rate estimated and certified by the financial advisor to the Authority as the rate that would be borne by a Variable Rate Bond if on the date of such certification such Bond was issued as a Bond bearing interest at a fixed rate to its stated maturity.

Code means the Internal Revenue Code of 1986, as amended from time to time. Each reference to a Code section herein shall be deemed to include the Treasury Regulations proposed or in effect thereunder and applicable to the Bonds.

Collecting Agent means the Collecting Agent designated as such under the Collecting Agent Agreement.

Collecting Agent Agreement means the Collecting Agent Agreement, dated as of November 1, 1999, as amended as of February 28, 2003, as further amended as of September 1, 2006, by and among the Government, the Special Escrow Agent and the Collecting Agent, as the same may be supplemented, or amended from time to time.

Corporate Trust Office means the principal corporate trust office of the Trustee in which the corporate trust business of the Trustee shall, at any particular time, be principally administered, which office is, at the date as of which the Indenture is dated, located at except that, with respect to presentation of Bonds for payment or registration of transfer and exchange and the location of the Bond Register, such term means the office or agency of the Bond Registrar in said city at which at any particular time its corporate agency business shall be conducted, which is, at the date as of which the Indenture is dated, is the same address as the corporate trust office as indicated above.

Cost of Issuance means the items of expense payable or reimbursable directly or indirectly by the Authority and related to the authorization, sale and issuance of Bonds which items of expense shall include without limiting the generality of the foregoing: travel expenses; printing costs; costs of reproducing documents; computer fees and expenses; filing and recording fees; initial fees and charges of the Trustee; initial fees and charges of Credit Providers or other parties (including specifically providers of Bond insurance policies and surety policies) pursuant to remarketing, indexing or similar agreements; discounts; legal fees and charges; auditing fees and expense; financial advisor's fees and charges; costs of credit ratings; insurance premiums; fees and charges for execution, transportation and safekeeping of Bonds; and other administrative or other costs of issuing, carrying and repaying such Bonds and investing the proceeds thereof.

Cost of Issuance Account means the account of that name established by the Indenture.

Counsel's Opinion means an opinion signed by an attorney or firm of attorneys of recognized standing in the field of law relating to municipal Bonds (who may be counsel to the Authority) selected by the Authority and reasonably satisfactory to the Trustee.

Credit Agreement means any reimbursement agreement or similar instrument between the Authority (and, if so drafted, the Trustee) and a Credit Provider with respect to a Credit Facility.

Credit Facility means a letter of credit, surety bond, liquidity facility, insurance policy or comparable instrument furnished by a Credit Provider with respect to all or a specific portion of one or more Series of Bonds to satisfy in whole or in part the Authority's obligation to maintain a Debt Service Reserve Requirement with respect thereto or to secure (a) the payment of Debt Service (which may include the premium due on payment of a Bond) or Bonds of a specified Series, or a specific portion thereof, (b) the payment of the purchase price (which may include accrued interest to the date of purchase) of Bonds of a specified Series, or a specific portion thereof, on the applicable purchase dates or tender dates, or (c) both the payment of Debt Service on a specified Series of Bonds, or a specific portion thereof.

Credit Provider means the bank, insurance company, financial institution or other entity providing a Credit Facility or Liquidity Facility pursuant to a Credit Agreement.

Credit Subaccount means a subaccount by that name in the Debt Service Account or Debt Service Reserve Account established by the Indenture.

Cumulative Available Revenues means, as of any October 1, commencing with October 1, 2007, the sum of (i) the Surplus Available Revenues as of such October 1 and (ii) the balance on deposit as of such October 1 in each of the Restricted Moneys Sub-subaccount of the Series 1999A Redemption Subaccount, Series 2003A Redemption Subaccount and the Series 2006 Redemption Subaccount.

Current Interest Bonds mean all Bonds which are not (a) Capital Appreciation Bonds or (b) prior to the Interest Commencement Date, Deferred Interest Bonds.

DAC means Digital Assurance Certification L.L.C., as Disclosure Dissemination Agent under each of the Authority Disclosure Dissemination Agreement and the Government Disclosure Dissemination Agreement.

Debt Service for any period means, as of any date of calculation and with respect to any Series of Bonds then Outstanding, the scheduled principal (including mandatory Sinking Fund Installments) and interest payments required to be made on such Series. For purposes of this definition, unless provided to the contrary in an applicable Supplemental Indenture authorizing the issuance of Capital Appreciation Bonds and Deferred Interest Bonds, the scheduled principal and interest portions of the Accreted Value of Capital Appreciation Bonds and the Appreciated Value of Deferred Interest Bonds becoming due at maturity or by virtue of Mandatory Sinking Fund Installments shall be included in the calculations of accrued and unpaid and accruing interest or principal payments in the year in which such payments are required to be made.

Debt Service Account means the Account by such name established in the Indenture.

Debt Service Reserve Account means the Account by such name established in the Indenture.

Debt Service Reserve Account Credit Facility means a Credit Facility provided to satisfy all or any portion of a Debt Service Reserve Requirement.

Debt Service Reserve Account Credit Provider means the Credit Provider of a Debt Service Reserve Account Credit Facility.

Debt Service Reserve Requirement means, as of any date of calculation, an amount equal to the least of (i) the greatest amount required in the then current or any future Bond Year to pay the sum of the interest on Outstanding Bonds payable during such Bond Year, and the principal (including mandatory Sinking Fund Installments) of Outstanding Bonds payable in such Bond Year, (ii) 125% of the average of the annual amounts required in the then current and all future Bond Years to pay the sum of the interest on the Bonds Outstanding payable during such Bond Years and the principal (including mandatory Sinking Fund Installments) of the Outstanding Bonds payable in such Bond Years, and (iii) 10% of the original aggregate principal amount (net of original issue discount) of the Bonds. The Debt Service Reserve Requirement may be satisfied by cash, Permitted Investments or a Debt Service Reserve Account Credit Facility, or any combination thereof.

Defeasance Securities means

(i) direct and general obligations of, or obligations which as to principal and interest are unconditionally guaranteed as to full and timely payment by, the United States of America, to the payment of which the full faith and credit of the United States of America is irrevocably and unconditionally pledged. The obligations described in this paragraph are hereinafter called *"United States Government Obligations;"* and

(ii) pre-refunded municipal obligations meeting the following conditions:

(1) the municipal obligations (A) are not subject to redemption prior to maturity or (B) the trustee has been given irrevocable instructions concerning their calling and redemption and the issuer of such municipal obligations has covenanted not to redeem such municipal obligations other than as set forth in such instructions;

(2) the municipal obligations are secured by cash or non-callable United States Government Obligations that may be applied only to interest, principal and premium payments of such municipal obligations;

(3) the principal of and interest on such United States Government Obligations (plus any cash in the escrow fund) are sufficient to meet the liabilities of the municipal obligations;

(4) the cash and United States Government Obligations serving as security for the municipal obligations are held by an escrow agent or trustee; and

(5) the United States Government Obligations are not available to satisfy any other claims, including those against the trustee or escrow agent.

Deferred Interest Bonds means any Bonds as to which accruing interest is not paid prior to the Interest Commencement Date specified in the Supplemental Indenture authorizing such Series.

Depository or **DTC** means The Depository Trust Company, New York, New York, and its successors and assigns.

Escrow Agent means The Bank of New York Trust Company, N.A., as escrow agent under the Escrow Trust Agreement.

Escrow Fund means the Escrow Fund established by the Escrow Agreement.

Escrow Trust Agreement means the Escrow Trust Agreement dated as of September 1, 2006 among the Authority, the Escrow Agent and the Government.

Expense Account means the Account by that name established by the Indenture.

Fiduciary or **Fiduciaries** means any bank or other organization acting in a fiduciary capacity with respect to any Bonds whether as Trustee, Paying Agent, Bond Registrar, tender agent, escrow agent or any or all of them, as may be appropriate.

First Supplemental Indenture means the First Supplemental Indenture of Trust, dated as of November 1, 1999, by and between the Authority and the Trustee, authorizing the issuance of and securing the Initial Series of Bonds.

Fiscal Year means the Authority's fiscal year. which is presently October 1 to the following September 30.

Fitch means Fitch ICBA, Inc., or any successor thereof which qualifies as a Rating Agency hereunder,

Fixed Interest Rate Bond means (i) a Bond, the interest rate on which is established (with no right to vary) at the time of calculation at a single numerical rate for the remaining term of such Bond, or (ii) all of those Bonds of a specific maturity described in clause (2)(A) and (B) of paragraph (i) of the definition of Adjusted Debt Service Requirement herein.

Funds means those funds and accounts specified in Section 5.01 of the Indenture.

Government means the Government of the United States Virgin Islands.

Government Disclosure Dissemination Agreement means the Disclosure Dissemination Agreement by and between the Government and DAC, dated as September 1, 2006.

Gross Receipts Taxes means the taxes imposed and the resulting tax revenues collected or/and to be collected by the Government pursuant to the provisions of Title 33, Section 43 of the Virgin Islands Code (together with all fines, interest, penalties and other charges assessed, imposed or otherwise payable in relation to such taxes and revenues) during the period in which the principal amount of the Bonds, together with any interest payable thereon, shall remain due and owing.

Holder shall have the same meaning as the term "Bondowner."

Indenture means the Original Indenture and including the Seventh Supplemental Indenture of Trust, each by and between the Authority and the Trustee and each of which may from time to time be amended or supplemented in accordance with the terms thereof and hereof.

Independent Counsel means an attorney, or firm thereof., admitted to practice law before the highest court of any state in the United States of America, the United States Virgin Islands or the District of Columbia and not an employee on a full-time basis of either the Authority or the Trustee (but who or which may be regularly retained by any one or more of them).

Independent Verification Analyst means a firm retained by the Authority to prepare the certificates required by the Indenture in connection with the issuance of Additional Bonds.

Interest Commencement Date means, with respect to any particular Deferred Interest Bonds, the date specified in the applicable Supplemental Indenture authorizing such Deferred Interest Bonds (which date must be prior to the maturity date for such Deferred Interest Bonds), after which interest accruing on such Deferred Interest Bonds shall be payable with the first such payment date being the applicable Interest Payment Date immediately succeeding such Interest Commencement Date.

Interest Payment Date means each date specified in a Supplemental Indenture as a date for the payment of interest to Owner of the Bond and, with respect to the Series 2006 Bonds, each April 1 and October 1.

Interest Payment Period with respect to any Bond, means, if prior to the first Interest Payment Date, the period from but not including the date specified in each Supplemental Indenture as the date for commencement of accrual of interest for such Bond and alter the first regularly scheduled Interest Payment Date means the period from but not including a regularly scheduled Interest Payment Date, in each case to and including the next regularly scheduled Interest Payment Date, provided that any Supplemental Indenture may adjust this definition with respect to any Bond authorized to be issued thereunder in order to provide for the proper computation of or the timely transfer of amounts payable with respect to interest borne by such Bond on any Interest Payment Date.

Interest Subaccount means the Subaccount by that name in the Debt Service Account established by the Indenture and the applicable Supplemental Indenture.

Issue Date means, for Bonds of a particular Series, the date on which the Bonds of such Series are delivered against payment therefor.

Letter of Representation means the Letter of Representation from the Authority to the Depository in such form as may be acceptable to the Authority and the Depository.

Loan Agreement means a loan agreement by and between the Authority and the Government, entered into in connection with the issuance of one or more Series of Bonds pursuant to a Supplemental Indenture hereto, as the same may from time to time be amended or supplemented in accordance with the terms thereof.

Loan Note or **Loan Notes** means the general obligation note or notes, as the case may be, of the Government, executed and delivered to the Authority pursuant to a Loan Agreement in connection with the issuance by the Authority of one Series or more of Bonds under the Indenture, each such note being in the principal amount equal to the aggregate principal amount of the Series of Bonds to which it relates and being further secured by a pledge by the Government of the Gross Receipts Taxes (other than the Required Annual Moderate Income Housing Fund Deposit) on a parity basis with all other such notes.

Mandatory Sinking Fund Requirements means the principal amount of Term Bonds which are required to be redeemed by mandatory sinking fund redemption, in the principal amounts at the prices and on the dates as set forth in the applicable Supplemental Indenture.

Mandatory Tender Date means a date on which the Bond is required to be purchased by, or on behalf of, the Authority as provided herein or in the Supplemental Indenture authorizing such Bond.

Memorandum of Understanding shall mean that Memorandum of Understanding between the Government and the Department of the Interior, dated October 7, 1999, as amended October 28, 1999, whereby the Government agrees to use its best efforts to undertake certain deficit reduction initiatives.

Monthly Transfer Requirement means the amount sufficient to fund in full all of the amounts specified in Sections 5.04(a)(i) through (vi) of the Indenture which are to be transferred during such calendar month from the Pledged Revenue Account to the various Accounts established under the Indenture.

Moody's means Moody's Investors Service, a corporation organized and existing under the laws of the State of Delaware, its successors and assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, Moody's shall be deemed to refer to any other nationally recognized securities rating agency designated by the Authority, by notice to the Trustee.

Net Payments Reserve Account shall mean the Net Payments Reserve Account established pursuant to Section 505 of the Seventh Supplemental Indenture.

Officer's Certificate means a certificate signed by an Authorized Officer.

Optional Tender Bonds means any Bonds which by their terms may be tendered by and at the option of, or required to be tendered by, the Owner thereof for payment or purchase by the Authority or another party prior to the stated maturity thereof, or the maturities of which may be extended by and at the option of the Owner thereof; provided, however, that a Supplemental Indenture may expressly provide that specific Bonds are not “Optional Tender Bonds” if, in the reasonable judgment of the Authority, the tender requirements of such Bonds are not of the character intended to be included within this definition.

Original Indenture means the Indenture of Trust, dated as of November 1, 1999, between the Authority and the Trustee, as heretofore amended by the First Supplemental Indenture of Trust, dated as of November 1, 1999, by the Second Supplemental Indenture of Trust, dated as of February 28, 2003, by the Third Supplemental Indenture of Trust, dated as of September 4, 2003, between the Authority, by the Fourth Supplemental Indenture of Trust, dated as of December 1, 2003, as amended by the First Amendment to Fourth Supplemental Indenture of Trust, by the Fifth Supplemental Indenture of Trust, dated as of September 7, 2005, and by the Sixth Supplemental Indenture of Trust, dated as of August 31, 2006, each between the Authority and the Trustee .

Outstanding Bonds, **Bonds Outstanding** and **Bonds then Outstanding** means as of the date of determination, all Bonds theretofore issued and delivered under the Indenture as from time to time supplemented except:

(i) Bonds theretofore canceled by the Trustee or Paying Agent or delivered to the Trustee or Paying Agent canceled or for cancellation;

(ii) Bonds for which payment or redemption moneys or securities (as provided in Section 10.01 of the Original Indenture) shall have been theretofore deposited with the Trustee or Paying Agent in trust for the Owners of such Bonds; provided, however, that if such Bonds are to be redeemed, notice of such redemption shall have been duly given pursuant to this Indenture or irrevocable action shall have been taken to call such Bonds for redemption at a stated redemption date;

(iii) Bonds in exchange for or in lieu of which other Bonds shall have been issued and delivered pursuant to the Indenture; and

(iv) Optional Tender Bonds deemed tendered in accordance with the provisions of the Supplemental Indenture authorizing such Bonds on the applicable tender, adjustment or conversion date, if interest thereon shall have been paid through such applicable date and the purchase price thereof shall have been paid or amounts are available for such payments as provided therein (but not if held for reoffering).

In determining requisite percentages of the Owners of aggregate principal amount of Bonds Outstanding for the purposes of direction, consent, approval or waiver under the terms and provision of this Indenture and any Supplemental Indenture: (1) the aggregate "principal amount" of any Bonds that are Capital Appreciation Bonds shall be determined by their Accreted Value as of the date of such determination, and (2) the aggregate "principal amount" of any Bonds that are Deferred Interest Bonds shall be determined by their Appreciated Value as of the date of such determination and provided, however, that in determining whether the Owners of the requisite principal amount of Outstanding Bonds have given any request, demand, authorization, direction, notice, consent or waiver hereunder, Bonds owned by the Authority shall be disregarded and deemed not to be Outstanding Bonds, except that in determining whether the Trustee shall be protected in relying upon any such request, demand, authorization, direction, notice, consent, or waiver, only Bonds which the Trustee knows to be so owned shall be disregarded.

Each Supplemental Indenture may further specify the conditions under which a Credit Provider will be deemed the Owner of Outstanding Bonds for purposes of consents hereto.

Owner or **Bondowner**, or any similar term, means any Person who shall be the registered owner of any Bond.

Parity Indebtedness shall have the meaning set forth in Section 7(c) of the Series 2006 Loan Agreement.

Participants means those broker-dealers, banks and other financial institutions from time to time for which the Depository holds Bonds as securities depository.

Paying Agent means any commercial bank or trust company organized under the laws of the United States Virgin Islands, any state of the United States, or the United States of America, or any national banking association designated as paying agent for the Bond, and its successor or successors hereafter appointed in the manner provided in the Indenture or a Supplemental Indenture.

Payment Default shall mean both a default by the Authority to pay when due the principal of, or interest on, the Series 2006 Bonds and a payment default by the Bond Insurer under the Bond Insurance Policy.

Permitted Investments means any of the following securities, if and to the extent the same are at the time legal for the investment of funds held under the Indenture:

(i) direct obligations of the United States or obligations guaranteed as to principal and interest by the United States;

(ii) general obligations of any state, territory, possession or commonwealth of the United States with a rating at the time of purchase in either of the two highest Rating Categories as designated by any Rating Agency;

(iii) prerefunded obligations of any state, territory, possession or Commonwealth of the United States or political subdivision thereof secured by cash or obligations listed in subsection (i) above, with a rating at the time of purchase in the highest Rating Category as designated by any Rating Agency;

(iv) obligations issued, or the principal of and interest on which are unconditionally guaranteed, by any agency or instrumentality of or a corporation wholly owned by the United States with a rating at the time of purchase in one of the two highest Rating Categories as designated by any Rating Agency;

(v) repurchase agreements with banks, savings and loan associations or trust companies organized under the laws of the United States Virgin Islands, the United States, or any state, territory, possession or commonwealth of the United States, provided, however, that any such bank, savings and loan association or trust company shall have a combined capital and surplus at least equal to $200,000,000 and, further provided that (l) such agreements are fully secured by obligations set forth in (i), (ii), and (iii) above; (2) such collateral is not subject to liens or claims of third parties; (3) such collateral has a market value at least equal to 102% of the amount invested and is held by the Trustee or its agent or, in the case of uncertificated securities, are registered in the name of the Trustee as pledgee; (4) the Trustee has a valid security interest in such collateral and (5) such agreement shall provide that the failure to maintain such collateral at the level required by clause (3) for a period of 10 days will require the Trustee or its agents to liquidate the investments;

(vi) investment agreements, guaranteed investment contracts or similar funding agreements issued by insurance companies or other financial institutions, including without limitation broker/dealers or subsidiaries thereof; provided that (1) such agreements are fully secured by obligations set forth in (i), (ii) and (iii) above; (2) such collateral is not subject to liens or claims of third parties; (3) such collateral has a market value at least equal to 102% of the amount invested and is held by the Trustee or its agent or, in the case of uncertificated securities, are registered in the name of the Trustee as pledgee; (4) the Trustee has a valid security interest in such collateral and (5) such agreement shall provide that the failure to maintain such collateral at the level required by clause (3) for a period of 10 days will require the Trustee or its agents to liquidate the investments;

(vii) U.S. dollar denominated bankers' acceptances with domestic commercial banks which have a rating on their short-term certificates of deposit on the date of purchase in the highest short-term rating category by a national rating agency and maturing no more than 360 days after the date of purchase. (Ratings on holding companies are not considered as the rating of the bank); and

(viii) Certificates of deposit with domestic commercial banks which have a rating on their short-term certificates of deposit on the date of purchase in the highest short-term rating category by a national rating agency and maturing no more than 360 days after the date of purchase. Certificates of deposit will be placed directly with depository institutions and (1) secured by obligations set forth in (i), (ii) and (iii) above; (2) such collateral is not subject to liens of claims of third parties; (3) such collateral has a market value at least equal to 102% of the amount invested and is held by the Trustee or its agent or, in the case of uncertificated securities, are registered in the name of the Trustee as pledgee; (4) the Trustee has a valid security interest in such collateral and (5) such agreement shall provide that the failure to maintain such collateral at the level required by clause (3) for a period of 10 days will require the Trustee or its agents to liquidate the investments; and

(ix) Investments in a money market fund rated in the two highest rating categories including money market funds sponsored by the Authority; and

(x) Commercial Paper issued by U.S. Corporations which is rated at the time of purchase in the highest short-term rating category by a national rating agency and which matures not more than 270 days after the date of purchase.

Any such Permitted Investment may be purchased or sold by, from or through the Authority or the Trustee. The Authority will not direct the Trustee to hold investments described in (vi), (vii) and (ix) unless arrangements satisfactory to the Trustee are in place to verify and monitor compliance with such provisions.

Person means an individual, a corporation, a partnership, an association, a joint stock company, a trust, any unincorporated organization or a government or political subdivision thereof, or any other legal entity or groups of legal entities.

Pledged Revenue Account means the Account by that name established by the Indenture.

Principal Installment means, as of any date of calculation and with respect to the Bond, so long as the Bond thereof is Outstanding, (i) the principal amount of the Bond due on a certain future date, or (ii) the unsatisfied balance of any Sinking Fund Installments due on a certain future date for the Bond.

Principal Payment Date means any date on which a Principal Installment is scheduled to become due on the Bond whether by scheduled maturity or Mandatory Sinking Fund Requirements or otherwise.

Principal Subaccount means the subaccount by that name in the Debt Service Account established by the Indenture and the applicable Supplemental Indenture.

Prior Bonds shall mean the Series 1999A Bonds maturing October 1, 2024 and October 1, 2029.

Project Account means the Account of that name established by the Indenture.

Proportionate Basis means, when used with respect to the redemption of the Bonds of a specific series, that the aggregate principal amount of such Bonds of each maturity of such Series to be redeemed shall be determined as nearly as practicable by multiplying the total amount of funds available for redemption by the ratio which the principal amount Outstanding of such maturity to be redeemed bears to the principal amount of all Bonds of that Series then Outstanding; provided that if the amount available for redemption of Bonds of any maturity is insufficient to redeem a multiple of the minimum authorized denomination of such maturity, such amount shall be applied to the redemption of the highest possible integral multiple of the minimum authorized denomination of such maturity. For purposes of the foregoing, Term Bonds shall be deemed to mature in the years and in the amounts of the Mandatory Sinking Fund Requirements set forth in the applicable Supplemental Indenture. Any Bonds purchased with moneys which would otherwise be applied to redemption on a Proportionate Basis on the next succeeding Payment Date shall be taken into account in determining Proportionate Basis with respect to such redemption. When used with respect to the purchase of Bonds, Proportionate Basis shall have the same meaning as set forth above, substituting "purchase" for "redemption," and "purchased" for "redeemed."

Purchase Date means the date on which any Outstanding Bonds are purchased pursuant to this Indenture or any applicable Supplemental Indenture.

Qualified Swap Agreement means (i) an agreement between the Authority and a Swap Provider under which the Authority agrees to pay the Swap Provider an amount calculated at an agreed-upon rate or index based upon a notional amount and the Swap Provider agrees to pay the Authority for a specific period of time an amount calculated at an agreed-upon rate or index based upon such notional amount, where the Swap Provider, or the Person who guarantees the obligation of the Swap Provider to make its payments to the Authority, has unsecured obligations rated, as of the date the swap agreement is entered into, in one of the three highest applicable Rating Categories by each Rating Agency then rating such Swap Provider or other Person who guarantees such obligation, or shall provide collateral to the Trustee with a market value maintained at levels and upon such conditions as would be acceptable to each such Rating Agency to maintain a rating on such swap agreement in one of the three highest applicable Rating Categories, or (ii) an option with respect to any agreement described in clause (i) above.

Rating Agency or Rating Agencies means one or more of Moody's, S&P or Fitch or any successor or comparable nationally recognized securities rating agency which shall be maintaining a rating on any Series of Bonds.

Rating Category means a generic securities rating category, without regard to any refinement or gradation of such rating category by a numerical modifier or otherwise.

Rebate Account means the Rebate Account established in and maintained pursuant to the Indenture and the applicable Supplemental Indenture.

Rebate Amount Certificate shall have the meaning set forth in Section 703.

Rebate Requirement means the amount required to be paid to the United States Treasury pursuant to Section 148(f) of the Code.

Record Date means with respect to an Interest Payment Date for the Bonds, unless otherwise provided by any Supplemental Indenture, the fifteenth day (or if such day shall not be a Business Day, the preceding Business Day) next preceding such Interest Payment Date.

Redemption Price means with respect to any Bond, the principal amount of such Bond plus the applicable premium, if any, payable upon redemption thereof pursuant to such Bond, this Indenture or the applicable Supplemental Indenture of the Indenture.

Redemption Subaccount means the subaccount by that name in the Debt Service Account established pursuant to the Indenture.

Registered Owner shall have the same meaning as the term "Bondowner."

Related Agreements or **Related Documents** means any Credit Facility, Credit Agreement or Pledge Agreement related to a Series of Bonds or a specific portion thereof, including security agreements or instruments heretofore or hereafter made for the benefit and with the consent of the Trustee or a Credit Provider as creditor to secure payment of any such Series of Bonds or a specific portion thereof, and shall not include documents, agreements or other items entered into only for the purposes of a different Series of Bonds or a specific portion or any amount due to a Credit Provider; but excluding the Indenture and all Supplemental Indentures; provided, that the term "Related Agreements" or "Related Documents," when used in relation to such Series of Bonds or a specific portion thereof, shall include only such Related Agreements or Related Documents as have been entered into for such Series of Bonds or a specific portion thereof.

Required Annual Moderate Income Housing Fund Deposit means the first $250,000 of Gross Receipts Taxes collected during each fiscal year of the Government which are required, pursuant to Title 33, Section 3027(a)(3) of the Virgin Islands Code, to be deposited in the Moderate Income Housing Fund of the Government, which amount shall not be subject to the liens granted by the Special Escrow Agreement and the Loan Agreement in the Gross Receipts Taxes.

Restricted Moneys Sub-subaccount shall mean the Restricted Moneys Sub-subaccount of the Series 2006 Redemption Account established in Section 501 of the Seventh Supplemental Indenture.

Revenues means (i) the Gross Receipts Taxes (other than the Required Annual Moderate Income Housing Fund Deposit), any Substitute Revenues, any other amounts required to be paid by or on behalf of the Government to or for the benefit of the Authority under any Loan Agreement and any other proceeds and collections from any Loan Notes, including investment proceeds, deposited in the Pledged Revenue Account, including any investment earnings earned thereon, and (ii) any proceeds which arise with respect to any disposition of the Trust Estate. Any net payment which the Authority receives with respect to a Qualified Swap Agreement shall be deemed to be "Revenues" and shall be deposited into the Pledged Revenue Account.

S&P means Standard & Poor's Ratings Group, a division of McGraw-Hill, Inc., a corporation organized and existing under the laws of the State of New York, its successors and assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, "S&P" shall be deemed to refer to any other nationally recognized securities rating agency designated by the Authority, by notice to the Trustee.

SLGS means United States Treasury Obligations, State and Local Government Series, as provided for in the United States Treasury Regulations 31 CFR 344.

Securities Depository means, initially, The Depository Trust Company, New York, New York, and its successors and assigns, and any successor Securities Depository appointed pursuant to Section 204.

Series 2006 Bonds shall mean the Authority's $______ Revenue Bonds, (Virgin Islands Gross Receipts Taxes Loan Note), Series 2006 authorized to be issued pursuant to the Seventh Supplemental Indenture.

Series 2006 Bonds Net Payments Sub-subaccount shall mean the Series 2006 Bonds Net Payments Sub-subaccount established in Section 501 of the Seventh Supplemental Indenture.

Series 2006 Capital Project shall mean the capital projects to be financed with the proceeds of the Series 2006 Bonds.

Series 2006 Cost of Issuance Subaccount shall mean the Series 2006 Cost of Issuance Subaccount of the Cost of Issuance Account established in Section 502 of the Seventh Supplemental Indenture.

Series 2006 Expense Subaccount shall mean the Series 2006 Expense Subaccount of the Debt Service Account established pursuant to Section 501 of the Seventh Supplemental Indenture.

Series 2006 Financing Documents means, collectively, the Indenture, the Seventh Supplemental Indenture, the Series 2006 Loan Agreement, the Series 2006 Loan Note, the Escrow Trust Agreement, the Series 2006 Swap Agreement, the Special Escrow Agreement, the Collecting Agent Agreement, Authority Continuing Disclosure Certificate, the Government Continuing Disclosure Certificate, the Authority Disclosure Dissemination Agreement and the Government Disclosure Dissemination Agreement.

Series 2006 Interest Subaccount shall mean the Series 2006 Interest Subaccount of the Debt Service Account established pursuant to Section 501(a) of the Seventh Supplemental Indenture.

Series 2006 Loan Agreement means the Loan Agreement, dated as of September 1, 2006, by and among the Government, the Authority and the Trustee, entered into in connection with the issuance of the Series 2006 Bonds.

Series 2006 Loan Note means the Government's $__________ principal amount 2006 Gross Receipts Taxes Loan Note, executed and delivered to the Authority pursuant to the Series 2006 Loan Agreement.

Series 2006 Principal Subaccount shall mean the Series 2006 Principal Subaccount of the Debt Service Account established pursuant to Section 501(a) of the Seventh Supplemental Indenture.

Series 2006 Project Subaccount shall mean the Series 2006 Project Subaccount established pursuant to Section 701 of the Seventh Supplemental Indenture.

Series 2006 Rebate Subaccount shall mean the Series 2006 Rebate Subaccount established pursuant to Section 701 of the Seventh Supplemental Indenture.

Series 2006 Redemption Subaccount shall mean the Series 2006 Redemption Subaccount of the Debt Service Account established pursuant to Section 501 of the Seventh Supplemental Indenture.

Series 2006 Swap Agreement shall mean that certain ISDA Master Agreement between the Authority and UBS AG dated as of September 19, 2006, together with the Schedule dated as of September 19, 2006, the Confirmation dated September 19, 2006 and the Credit Support Annex relating to the Series 2006 Bonds.

Series 2006 Swap Agreement Net Payments shall mean any and all regularly scheduled payments (net of regularly scheduled payments of the Series 2006 Swap Provider to the Authority) that the Authority is obligated to pay the Series 2006 Swap Provider under the Series 2006 Swap Agreement.

Series 2006 Swap Agreement Termination Payments shall mean all payments that the Authority is obligated to pay the Series 2006 Swap Provider upon the termination of the Series 2006 Swap Agreement.

Series 2006 Swap Provider shall mean UBS AG or any permitted successor or assignee thereto.

Series 1999A Bonds means the Authority's $299,880,000 original principal amount of Revenue Bonds, Series 1999A (Virgin Islands Gross Receipts Taxes Loan Note), issued pursuant to the First Supplemental Indenture.

Seventh Supplemental Indenture shall mean the Seventh Supplemental Indenture of Trust, dated as of September 1, 2006, between the Authority and the Trustee, which supplements and amends the Original Indenture.

Sinking Fund Installment means, with respect to any Series of Bonds, an amount so designated which is established pursuant to the Supplemental Indenture authorizing such Series of Bonds.

Special Escrow Account means the Special Escrow Account established under the Special Escrow Agreement.

Special Escrow Agent means The Bank of New York Trust Company, N.A., the special escrow agent under the Special Escrow Agreement, or any successor thereto.

Special Escrow Agreement means the Special Escrow Agreement dated as of November 1, 1999, as amended as of February 28, 2003, and as further amended as of September 1, 2006, by and among the Authority, the Special Escrow Agent and the Government, as the same may be supplemented or amended from time to time.

Special Record Date means if the Authority shall be in default in payment of principal or interest due, a special Record Date for the payment of such defaulted principal or interest established by notice mailed by the Trustee on behalf of the Authority; notice of such Special Record Date shall be mailed not less than 10 days preceding such Special Record Date, to the owner at the close of business on the fifth Business Day preceding the date of mailing.

Subaccount or **Subaccounts** means any subaccount or subaccounts, as the case may be established in an Account pursuant to the Indenture or in a Supplemental Indenture authorizing a Series of Bonds hereunder.

Substitute Revenues means any taxes or other revenues collected or to be collected by the Government as may hereafter be pledged by the Government pursuant to any Loan Agreement as additional or substitute security for the repayment of any Loan Notes.

Supplemental Indenture means any indenture amending or supplementing the Indenture in accordance with the terms hereof.

Surplus Account means the Surplus Account established in Section 5.01 of the Indenture.

Surplus Available Revenues means as of any October 1, commencing with October 1, 2007, the “available amounts” of the Government within the meaning of Treasury Regulations Section 1.148-6(d)(3)(iii) (including, specifically all amounts available to the Government for expenditure for payment of working capital expenditures, including cash or investments and other amounts held in accounts or otherwise by the Government or any related party as defined in Section 1.150-1 of the Treasury Regulations if those amounts may be used for working capital expenditures without legislative or judicial action and without a legislative, judicial or contractual requirement that those amounts be reimbursed). Surplus Available Revenues shall not include (a) sale proceeds of the Series 2006 Bonds, and (b) an amount equal to 5% of the expenditures paid by the Government from current revenues for the prior fiscal year of the Government.

Swap Provider means the counter party with whom the Authority enters into a Qualified Swap Agreement.

Tax Covenants means the covenants of the Authority expressed in or incorporated by reference in Article VI of the Indenture, or in the corresponding section of a Supplemental Indenture providing for assurance of the preservation of the tax-exempt status of the interest on a Series of Tax-Exempt Bonds.

Tax-Exempt Bonds means Bonds issued pursuant to the Indenture for which the Authority receives, on the date of the closing therefor, an opinion of Bond Counsel to the effect that interest on such Bonds is excludable from the gross income of the owners thereof for federal income lax purposes under section 103 of the Code.

Tax Opinion means, with respect to any action requiring such an opinion hereunder, a Counsel's Opinion to the effect that such action, of itself, will not adversely affect the exclusion of interest on any Series of Tax-Exempt Bonds from gross income for federal income tax purposes.

Tax Regulatory Agreement means the tax certificates and agreements between the Authority and the Government of the Virgin Islands dated as of the date the Bonds are issued, as amended from time to time, relating to the requirements of Sections 148 and 103 of the Code for exemption of interest on the Tax-Exempt Bonds from federal income tax.

Taxable Bonds means any Bonds which are not Tax-Exempt Bonds on the date of original issue thereof.

Term Bonds means Bonds which are designated in a Supplemental Indenture as subject to scheduled Mandatory Sinking Fund Requirements prior to maturity.

Treasury Regulations means all final, temporary or proposed Income Tax Regulations issued or amended with respect to the Code by the Treasury or Internal Revenue Service and applicable to the Bonds. Any reference to a section of the Treasury Regulations shall also refer to any successor provision to such section hereafter promulgated by the Internal Revenue Service pursuant to the Code and applicable to the Bonds.

Trust Estate means the Revenues and the rights to receive the same, the tangible and intangible properties, rights and other assets described in the Granting Clauses of the Indenture as from time to time supplemented, and, with respect to a specific Series of Bonds or specific Bonds within a Series, such funds, rights, properties and assets pledged to secure such Series of Bonds or specific Bonds within a Series pursuant to a Supplemental Indenture.

Trustee means The Bank of New York Trust Company, N.A. (as successor to the Bank of New York), a national association, designated as trustee under the Indenture, and its successor or successors hereafter appointed in the manner provided in the Indenture.

2003 Swap Agreement shall mean the Swap Agreement as defined in the Second Supplemental Indenture.

Valuation Date means with respect to any Bonds that are Capital Appreciation Bonds or Deferred Interest Bonds, the date or dates set forth as such in the Supplemental Indenture authorizing such Bonds on which specific Accreted Values or Appreciated Values, respectively, are assigned to such Bonds.

Variable Interest Rate means a variable interest rate or rates to be borne by the Bond. The method of commuting such variable interest rate shall be specified in the Supplemental Indenture authorizing such Bonds or Related Agreements approved thereby.

Variable Rate Bonds means any Bond that bears interest at a rate which is not established at the time of calculation at a single numerical rate for the remaining term of such Bond.

Working Capital Series 2006 Bonds means the Series 2006 Bonds, the proceeds of which are allocated to the refunding of the Prior Bonds.

Written Order means a written direction of the Authority to the Trustee signed by an Authorized Officer.

APPENDIX B

SUMMARY OF CERTAIN PROVISIONS OF THE ORIGINAL INDENTURE AND THE SEVENTH SUPPLEMENTAL INDENTURE

THE ORIGINAL INDENTURE

The following is a summary of certain provisions of the Original Indenture. Such summary does not purport to be complete or definitive and reference is made to the Indenture for a full and complete statement of the terms and provisions and for the definition of capitalized terms used in this summary and not otherwise defined under APPENDIX A – "Glossary of Certain Defined Terms."

Pledge of Revenues. The Bonds shall be special, limited obligations of the Authority payable as to the principal or Redemption Price, if any, and interest thereon, in accordance with their terms and the terms and provisions of the Indenture solely from Revenues, and secured by a lien on and security interest in the Trust Estate, subject only to the provisions of the Indenture permitting the application thereof for the purposes and on the terms and conditions set forth in the Indenture. The Authority has no taxing power and its debts are not debts of the United States Virgin Islands or any political subdivision of the United States Virgin Islands. No holder of the Bonds shall have the right to compel any exercise of the taxing power of the United States Virgin Islands to pay the principal of or interest on the Bonds.

Authorization of Bonds. The Indenture authorizes Bonds of the Authority to be issued and designated as "Refunding Bonds (Virgin Islands Gross Receipts Taxes Loan Note)" or "Revenue Bonds (Virgin Islands Gross Receipts Taxes Loan Note)" or "Revenue and Refunding Bonds (Virgin Islands Gross Receipts Taxes Loan Note)," as applicable. The aggregate principal amount of the Bonds under the Indenture and Supplemental Indenture is not limited except as provided in the Indenture, the Act, or as may be limited by law.

Sinking Fund Redemption; Purchase. The Bonds of any Series issued pursuant to the Indenture may be subject to optional, mandatory or extraordinary redemption or prepayment on a scheduled or other basis, provided that the Mandatory Sinking Fund Requirements of Bonds or a particular Series and maturity shall be reduced to the extent the Bonds of that Series and maturity have been optionally or mandatorily redeemed prior to or on the date scheduled for payment of the specified principal amount and at the Redemption Prices specified in the applicable Supplemental Indenture.

Additional Bonds; Other Revenue Obligations. All of the Bonds issued under a Supplemental Indenture shall collectively be a charge and lien upon the Trust Estate. Except as permitted by the Indenture, no obligations payable from Revenues or secured by a lien of a superior or equal rank on the Trust Estate (except as to any Credit Facility or Liquidity Facility which secures Bonds or a specific Series of Bonds) shall be issued under the Indenture. If no Event of Default has occurred or will contemporaneously, the Authority may issue Additional Bonds pursuant to a Supplemental Indenture.

Conditions to the Issuance of Additional Bonds:

(a) All Bonds shall be payable from Revenues and secured by a lien on the Trust Estate on a parity basis with all Outstanding Bonds and any Additional Bonds that may be issued under the Indenture (except as to any Credit Facility which secures only a specific Series of Bonds or specific Bonds of a Series) if the Trustee shall receive:

(1) a certificate of the Authority that no Event of Default under the Indenture has occurred and shall continue to exist immediately following the date of the Bonds to be issued; and

(2) a certificate of an Independent Verification Analyst stating (i) (A) the actual amount of Gross Receipts Taxes collected by the Government during each of the twenty-four (24) calendar months immediately preceding the calendar month in which such Bonds are issued (the "Test Period"); (B) the actual amount of Gross Receipts Taxes collected by the Government during any twelve (12) consecutive month period

within the Test Period in which collections of Gross Receipts Taxes were the greatest; and (C) the average Gross Receipts Taxes projected to be collected by the Government in the two Fiscal Years succeeding the issuance of such Bonds; (ii) the maximum annual Adjusted Debt Service Requirement in the current or any subsequent Bond Year on Outstanding Bonds after giving effect to the issuance of the proposed Additional Bonds; and (iii) (A) that the Gross Receipts Taxes collected by the Government during the twelve consecutive calendar month period referred to in (i)(B) above equaled or exceeded 150% of the amount of maximum Adjusted Debt Service Requirement on Outstanding Bonds in the current or any subsequent Bond year after giving effect to the issuance of the proposed Additional Bonds in the current or any subsequent Bond Year or (B) the average Gross Receipts Taxes projected to be collected by the Government for the two Fiscal Years succeeding the issuance of the Bonds is projected to equal or exceed 150% of the Adjusted Debt Service Requirement in the current or any subsequent Bond Year on Outstanding Bonds and such Additional Bonds.

(b) For purposes of the certifications described in the Indenture there shall be excluded from the Adjusted Debt Service Requirement any amounts otherwise due or to become due on Outstanding Bonds which are to be refunded and will be no longer Outstanding as a result of the issuance of such Additional Bonds.

(c) Any, Supplemental Indenture that authorizes Bonds under this Section shall state the dollar amount of the Debt Service Reserve Requirement, effective as of the date of issuance of such Additional Bonds, and of the portion thereof, if any, to be funded out of the sale proceeds of such Series of Bonds and/or other moneys to be delivered to the Trustee or on deposit with the Trustee.

(d) If the Bonds are subject to mandatory purchase or are to be purchased upon optional tender by the Owners thereof, any amounts required to be segregated or set aside by the Authority to fulfill its purchase obligation shall be deemed additional Adjusted Debt Service Requirements with respect to the related Series of Bonds in the amounts and at the times such amounts are required to be so set aside.

(e) The conversion of Bonds that are Variable Rate Bonds to Fixed Interest Rate Bonds shall not be treated as the issuance of Additional Bonds subject to the other requirements of this Section unless the interest rate to be borne by such Bonds from and after the date of conversion will exceed the Certified Interest Rate taken into account for the purposes of computing Adjusted Debt Service Requirements under Section 2.05(a) of the Indenture.

(f) Prior to the issuance of any Series of Bonds under the provisions of this Section, and as a condition precedent thereto, the following documents and showings shall be executed and delivered:

(i) a Supplemental Indenture, executed by the Authority and the Trustee, providing for the issuance of such Bonds and the terms and conditions thereof, and

(ii) an Authority certificate setting forth information sufficient to satisfy the Trustee that the requirements of this Section have been fulfilled.

Refunding Bonds. Additional Bonds may be issued pursuant to the Indenture if and to the extent needed to refund Outstanding Bonds, which refunding Additional Bonds may be on a parity with the Bonds that are being refunded and are not required to satisfy the tests of issuance of Additional Bonds set forth in the Indenture, if the aggregate Debt Service on the refunding Additional Bonds is equal to or less than the aggregate Debt Service on the refunded Bonds; and provided further, that the Authority bas made provisions for the repayment of the Bonds to be refunded.

Book-Entry System Only. The ownership of one or more fully registered Bond for each maturity of each Series of Bonds shall be registered in the name of Cede and Company, as nominee for the Depository Trust Company ("DTC"). Payments of interest on, principal of any premium on such Series of Bonds shall be made to the account of the DTC on each payment date at the address indicated for the DTC in the Bond Register by transfer of immediately available funds. DTC maintains a book-entry system for recording ownership interests of its participants (the "Direct Participants"), and the ownership interests of a purchaser of a beneficial interest in the Bonds (a "Beneficial Owner") will be recorded through book entries on the records of the Direct Participants. With respect to Bonds registered in the name of DTC, the Authority, the Trustee and any agent thereof shall have no responsibility or obligation to any Direct Participant or to any Beneficial Owner of such Bonds. DTC may determine to discontinue providing its services with respect to the Bonds of a Series at any time by giving reasonable written notice to the Authority, the Trustee and any tender agent for a Series of Bonds and discharging its responsibilities with respect thereto under applicable law. In addition, the Authority, in its sole discretion and without the consent of any other Person, may terminate, upon provision of notice to the Trustee and any tender agent for a Series of Bonds, the services of the DTC with respect to a Series of Bonds if the Authority determines that the continuation of the system of book entry-only transfers is not in the best interests of the Owners of the Bonds of the Series or is burdensome to the Authority. The Authority may select a new Depository or discontinue the services of a Depository and issue Bond certificates.

General Provisions. The Bonds shall be in minimum denominations of $5,000, or in integral multiples thereof in the form set forth in the exhibit to the appropriate Supplemental Indenture. The Authority shall execute the Bonds by the manual or facsimile signature of the Governor of the Virgin Islands with the seal or facsimile seal of the Authority and attestation by the manual or facsimile signature of the Secretary of the Authority in accordance with the provisions of the Indenture. The Bonds shall be transferable only upon the books of the Authority by the Trustee. In all cases in which the privilege of exchanging Bonds or transferring registered Bonds is exercised, the Authority shall execute and the Trustee shall authenticate and deliver bonds in accordance with, and subject to the restrictions of, the Indenture. Neither the Authority nor the Trustee shall be required (a) to transfer or exchange Bonds for a period beginning on tire Record Date next preceding an interest payment date for the Bonds and ending on such interest payment date, or for a period for fifteen days next preceding the date (as determined by the Trustee) of any selection of Bonds to be redeemed or thereafter until after the mailing of any notice of redemption; or (b) to transfer or exchange any Bonds called or tendered for redemption, in whole or in part.

Exchanges and Transfer of Bonds. The Indenture provides when a Bond is exchanged or transferred, the Authority shall execute and the Trustee shall authenticate and deliver Bonds in accordance with the provisions of the Indenture. Bonds surrendered for exchange or transfer shall be canceled by the Trustee. The Authority may only make a charge sufficient to reimburse itself for any tax or other governmental charge required to be paid with respect to such exchange or transfer. The Indenture provides specific time periods when the Authority and the Trustee cannot be required to transfer or exchange Bonds.

Redemption. Bonds subject to mandatory, optional or extraordinary redemption prior to maturity pursuant to any Supplemental Indenture shall be redeemable, upon notice, at such times, at such Redemption Prices and upon such terms in addition to the terms contained in the Indenture as may be specified in any Supplemental Indenture. At the election or direction of the Authority, the Board shall notify the Trustee of the Authority's decision to redeem and of the particulars of the redemption. If less than all of the Bonds of like maturity of any Series shall be called for prior redemption, the Trustee shall randomly select the particular Bonds or portions of the Bonds to be redeemed.

Notice of Redemption. When the Trustee shall receive notice from the Board, acting on behalf of the Authority, of its election or direction to redeem Bonds pursuant to the Indenture, and when redemption of Bonds is required or authorized pursuant to the Indenture, the Trustee shall give notice, in the name of the Authority, of the redemption of such Bonds, which notice shall specify the Series and maturities of the Bonds to be redeemed, the redemption date and the place or places where amounts due upon such redemption will be payable and, if less than all of the Bonds of any like Series and maturity are to be redeemed, the letters and numbers or other distinguishing marks of such Bonds to be so redeemed, and, in the case of Bonds to be redeemed in part only, such notice shall also specify the respective portions of the principal amount thereof to be redeemed. Such notice shall further state that on such date there shall become due and payable upon each Bond to be redeemed the Redemption Price thereof, or the Redemption Price of the specified portions of the principal thereof in the case of Bonds to be redeemed in part only, together with interest accrued to the redemption date, and that from and after such date interest thereon shall cease to accrue and be payable. Such notice shall be mailed by the Trustee by first class mail, postage prepaid, not more than 60 days nor less than 30 days before the redemption date, to each of the Owners of any Bonds or portions of Bonds which are to be redeemed, at their last addresses, if any, appearing upon the Bond Register, but any defect in, or the failure of any Bondowner to receive, any such notice shall not affect the validity of the proceedings for the redemption of Bonds. Notwithstanding the foregoing, failure to mail any such notice pursuant to the Indenture to any particular Owner of a Bond shall not affect the validity of any proceedings for the redemption of any other Bond.

Payment of Redeemed Bonds. Notice having been given in the manner provided in the Indenture, the Bonds or portions thereof so called for redemption shall become due and payable on the redemption date so designated at the Redemption Price, plus interest accrued and unpaid to the redemption date, and, upon presentation and surrender thereof at the office specified in such notice, such Bonds or portions thereof shall be paid at the Redemption Price, plus interest accrued and unpaid to the redemption date. If there shall be called for redemption less than all of a Bond, without charge to the owner thereof, for the unredeemed balance of the principal amount of the Bond so surrendered, at the option of the Owner thereof, Bonds of like Series and maturity in any of the authorized denominations. If, on the redemption date, moneys for the redemption of all the Bonds or portions thereof of any like Series and maturity to be redeemed, together with interest to the redemption date, shall be held by the Paying Agent so as to be available therefor on said date and if notice of redemption shall have been given as aforesaid, then, from and after the redemption date interest on the Bonds or portions thereof of such Series and maturity so called for redemption shall cease to accrue and become payable. If said moneys shall not be so available on the redemption date, such Bonds or portions thereof shall continue to bear interest until paid at the same rate as they would have borne had they not been called for redemption.

Creation of Accounts, and Subaccounts; Deposit of and Use of Moneys. The proceeds of each Series of Bonds and all Revenues and other sums pledged and assigned by the Indenture to the Trustee for the benefit of Bondowners are to be deposited to the Accounts established by the Indenture and shall not be subject to any lien or attachment by any Creditor of the Authority or any Credit Provider or other person other than the lien of the Indenture. The Accounts and separate Subaccounts within the Accounts created with respect to each series of Bonds under the Indenture shall be held and administered by the Trustee or the Authority in accordance with the terms of the Indenture and may include the following:

(1) The Pledged Revenue Account, to be held by the Trustee;

(2) The Debt Service Account, to be held by the Trustee with such separate Subaccounts as provided in the Indenture or Supplemental Indenture, including any of the following accounts therein:

(A) An Interest Subaccount;

(B) A Principal Subaccount;

(C) A Redemption Subaccount;

(D) A Credit Subaccount with respect to each Credit Facility which is not a Debt Service Reserve Account Credit Facility;

(E) An Expense Subaccount;

(F) A Purchase Subaccount;

(G) A Capitalized Interest Subaccount;

(H) Any other Account or Subaccount established by the applicable Supplemental Indenture;

(3) The Debt Service Reserve Account, to be held by the Trustee, with such separate Credit Subaccounts therein as the Authority shall determine in any Supplemental Indenture;

(4) The Project Account, to be held by the Trustee or the Authority, with such separate Subaccounts therein as the Authority shall determine in any Supplemental Indenture;

(5) The Cost of Issuance Account and such Subaccounts therein as the Authority shall determine in any Supplemental Indenture, to be held by the Trustee;

(6) A Rebate Account, to be held by the Trustee, and such Subaccounts therein as the Authority shall determine in any Supplemental Indenture authorizing a Series of Tax-Exempt Bonds; and

(7) A Surplus Account, to be held by the Authority.

Project Account. There shall be paid into the Project Account the amounts required to be so paid by the provisions of the Indenture and each Supplemental Indenture. There also may be paid into the Project Account, at the option of the Authority, any moneys received by the Authority from any source unless otherwise required to be applied by the Indenture or any Supplemental Indenture. Separate, segregated Subaccounts may be created within the Project Account and held by the Authority, the Trustee, any tender agent, or other entity in the manner provided in any Supplemental Indenture authorizing such Accounts. Money held in such Subaccounts shall be held separately from other moneys in the Project Account and shall be disposed of only in the manner provided in the Supplemental Indentures authorizing such Subaccounts. Such separate, segregated Subaccounts and all funds, investments thereof and investment income earned thereon may be pledged (and a lien and security interest therein may be granted) to secure for any period of time the payment of principal of and/or the purchase price of any or all of any Series of Bonds issued pursuant to such Supplemental Indenture incurred pursuant to such Supplemental Indenture and interest thereon to any date, all as may be more fully provided in such Supplemental Indenture in which case such pledge, lien and security interest will be prior and superior to the lien and pledge on the Project Account granted by the Indenture securing the Bonds generally. Amounts in the Project Account shall be used to pay any or all of the following: (i) the Costs of the Approved Projects and (ii) with respect to special Subaccounts created within the Project Account by a Supplemental Indenture, to pay all amounts authorized by such Supplemental Indenture. Amounts in the Project Account may be transferred to a Debt Service Account and applied to the payment of interest on or principal or Redemption Price of the Bonds when due, to the extent that other funds held for those purposes are insufficient and to the extent that the Authority certifies such amounts are not then obligated to pay costs of an Approved Project.

Pledged Revenue Account. The Trustee shall deposit to the Pledged Revenue Account as received all Revenues received, including but not limited to the Gross Receipts Taxes and any Substitute Revenues pledged under the Loan Agreements, the amounts required by the Indenture, and such other revenues as may be received by the Trustee which are designated for deposit to the Pledged Revenue Account under a Supplemental Indenture. All amounts in the Pledged Revenue Account shall be transferred daily on or before the 5:00 p.m. on each Business Day during each calendar month to Accounts and Subaccounts created under the Indenture, so long as any Bonds remain Outstanding under the Indenture, in the following amounts and in the following order of priority:

(i)(l) to each Interest Subaccount, until the aggregate amount on deposit in all existing Interest Subaccounts is equal to the sum of all Required Interest Subaccount Balances (as hereinafter defined). The Required Interest Subaccount Balance in effect during each calendar month for each Interest Subaccount shall be the greater of (A) the amount determined by multiplying (x) the portion of the Adjusted Debt Service Requirement for the applicable Series of Bonds which constitutes all of the interest accruing or to accrue on such Series of Bonds during the Interest Payment Period ending on the next Interest Payment Date, by (y) a fraction, the numerator of which is equal to one (1) plus the number of whole calendar months that have elapsed since the immediately preceding Interest Payment Date (or, in the case of the period prior to the first Interest Payment Date, one (1) plus the number of whole calendar months that have elapsed since the date interest on such Series of Bonds commenced to accrue) and the denominator of which is the number of whole calendar months in such Interest Payment Period, or (B) the amount specified in the applicable Supplemental Indenture (such transfers to be subject to the credits provided for below in clause (2) of this paragraph (i));

(2) subject in each case to any credit with respect to any amounts on deposit in the Capitalized Interest Subaccount to be used for Capitalized Interest and any earnings thereon to the extent required to be used and available for payment of interest on specific Bonds as contemplated in any applicable Supplemental Indenture and, in connection with clause (1) above, (A) any net payment which the Authority is required to make with respect to any Qualified Swap Agreement shall be treated in the same manner and shall have the same claim upon Revenues as interest on the Series of Bonds to which such Qualified Swap Agreement shall relate and (B) as of each

Interest Payment Date for Bonds which are not Fixed Rate Bonds to the extent that the actual interest payable with respect to such Bonds for any Interest Payment Period is less than the amount deposited into the Interest Subaccount, then the excess amount so deposited shall be applied as a credit to reduce the amount otherwise required to be deposited in the next succeeding month or months pursuant to paragraph (i)(1) hereof; and then

(ii) to each Principal Subaccount, beginning in the first calendar month specified in the applicable Supplemental Indenture (the "Principal Amortization Start Month"), until the aggregate amount on deposit in all existing Principal Subaccounts is equal to the sum of all Required Principal Subaccount Balances (as hereinafter defined). The Required Principal Subaccount Balance in effect during each calendar month for each Principal Subaccount shall be the greater of (A) the amount determined by multiplying (x) the principal (including Sinking Fund Installments) on the applicable Series of Bonds due on the next succeeding Principal Payment Date by (y) a fraction, the numerator of which is equal to one (1) plus the number of whole calendar months that have elapsed since the immediately preceding Principal Payment Date (or, in the case of the period prior to the first Principal Payment Date, one (1) plus the number of whole calendar months that have elapsed since the first day of the Principal Amortization Start Month), and the denominator of which is the number of whole calendar months between the immediately preceding Principal Payment Date (or, in the case of the period prior to the first Principal Payment Date, the first day of the Principal Amortization Start Month), and the next succeeding Principal Payment Date, or (B) the amount specified in the applicable Supplemental Indenture; and then

(iii) to each Credit Subaccount, an amount sufficient to pay any principal or interest then owing to a Credit Provider under the applicable Supplemental Indenture and Credit Agreement by reason of any drawing of amounts under the related Credit Facility for the payment of principal of or interest or premium on any Bonds, <u>provided</u> that the amount transferred pursuant to this Section shall in no event be greater than the sum of (1) amounts received under the related Credit Facility for payment of amounts to or for the benefit of Owners of Bonds secured by such Credit Facility and (2) interest thereon at the rate specified in the Credit Agreement; <u>provided</u>, that the amounts of the transfers described in (i), (ii), (iii) and (iv) shall be reduced to the extent of moneys previously transferred or required to be transferred to said Accounts under other provisions hereof or of a Supplemental Indenture; and then

(iv) to the Debt Service Reserve Account the amount of any transfer required by the provisions of the Indenture described below under the heading "**Debt Service Reserve Account**" to restore any deficiency in the Debt Service Reserve Account (or to pay any amounts then owing to a Credit Provider pursuant to a Credit Agreement relating to a Debt Service Reserve Account Credit Facility); and then

(v) to each Redemption Subaccount, the amount of Revenues required to redeem Bonds subject to redemption pursuant to the related Supplemental Indenture; and then

(vi) to each Expense Subaccount, any amounts then due and owing to the Trustee, any Paying Agent, Remarketing Agent, Bond Registrar, Credit Provider, Special Escrow Agent, Collecting Agent or other Fiduciary which are Bond Services Charges or Bond Related Costs for Bonds relating to the administration (including remarketing) and the Authority's Annual Administrative Fee which otherwise have not been provided for in (i), (ii), (iii) or (iv) above; and then

(vii) to each Subaccount of the Rebate Account, the amount required to comply with the Indenture for Bonds and such amounts shall be applied as provided in the Indenture; and then

(viii) to any Swap Provider for termination payments which the Authority is required to make under any Qualified Swap Agreement, the amounts required to make such payments as set forth in such Qualified Swap Agreement; and then

(ix) except as may be provided in one of more Supplemental Indentures to the contrary, to the Surplus Account for application pursuant to the Indenture.

Solely for the purpose of administering these payments, any interest which is payable on Capital Appreciation Bonds or, prior to the Interest Commencement Date, on Deferred Interest Bonds, shall be deemed to be "due" in the Bond Year in which payment is scheduled to be made thereon and, for such purposes, such amounts shall be deemed to be "principal" under subsection (a)(ii) above rather than "interest" under subsection (a)(i) above.

Debt Service Account and Subaccounts. There shall be deposited into the Debt Service Account all amounts required to be remitted, transferred or otherwise deposited therein as provided in the Indenture together with such additional amounts to be deposited into various specified Subaccounts within the Debt Service Account as described in this Section.

(a) **Interest Subaccount.** There shall be deposited in each Interest Subaccount, upon issuance of each Series of Bonds, the amount of accrued interest received from the sale of such Bonds and there shall be deposited thereafter all other amounts required by the Indenture. If on any Interest Payment Date there are not sufficient amounts on deposit in the Interest Subaccount to pay the total amount of interest coming due on the Bonds on such Interest Payment Date, the Trustee shall transfer to the Interest Subaccount from respectively, the Pledged Revenue Account, the Redemption Account, the Project Account, the Debt Service Reserve Account or the Principal Subaccount, in the order so listed, an amount equal to the deficiency. On each Interest Payment Date the Trustee shall withdraw from the Interest Subaccount an amount sufficient to pay the interest coming due on the Bonds on such Interest Payment Date and shall use such amounts to pay, or make provision with the Paying Agent for the payment of interest on the Bonds on such Interest Payment Date.

(b) **Principal Subaccount.** There shall be transferred to the Principal Subaccount the amounts required to be transferred from the Pledged Revenue Account pursuant to the Indenture. If on any Principal Payment Date there are not sufficient amounts on deposit in the Principal Subaccount to pay the total amount of principal coming due on the Bonds on such Principal Payment Date, the Trustee shall forthwith transfer to the Principal Subaccount from, respectively, the Pledged Revenue Account, the Redemption Account, the Project Account, the Debt Service Reserve Account or the Interest Subaccount, in the order so listed, an amount equal to the deficiency. On or before each Principal Payment Date for Bonds, the Trustee shall withdraw from the Principal Subaccount an amount sufficient to pay the scheduled principal coming due on the Bonds on such Principal Payment Date, and shall use such amounts to pay, or make provision with the Paying Agents for the payment of, principal of the Bonds on such Principal Payment Date, whether by reason of stated maturity or by reason of Mandatory Sinking Account Requirements applicable to any Term Bonds.

(c) **Redemption Subaccount.** Any amounts to be used to prepay Bonds by the Authority shall be deposited in the Redemption Subaccount related to such Series of Bonds to be redeemed and applied as provided by the Supplemental Indenture or, if no provision is made by the applicable Supplemental Indenture such amounts at the direction of the Authority shall be applied to purchase Bonds to be surrendered to the Trustee as a credit against Debt Service Requirements when due or to pay the principal of and premium, if any, of the Bonds then subject to and called for redemption. Any funds transferred to the Redemption Subaccount from a Project Account as excess proceeds shall be applied only to redeem Bonds of the Series from which such Project Account proceeds were derived, if any such Bonds are Outstanding. Other funds transferred to the Redemption Subaccount shall be applied to redeem Bonds then subject to redemption as provided in the applicable Supplemental Indenture or, if the Supplemental Indenture does not specifically so provide, as the Authority shall direct in writing.

(d) **Credit Subaccount.** To the extent so provided in the applicable Supplemental Indenture the Trustee shall create a separate Credit Subaccount within the Debt Service Account for each Series of Bonds (or specific Bonds within a Series) secured by a Credit Facility which is not a Debt Service Reserve Account Credit Facility. In addition, for any Credit Facility which constitutes a bond insurance policy or similar instrument pursuant to which the Credit Provider is entitled to subrogation rights as to amounts paid to Bond Owners secured thereby, the Supplemental Indenture relating thereto may provide for payment directly to such Credit Provider of available amounts in the Principal and Interest Subaccounts by reason of such subrogation rather than establishing a Credit Subaccount and requiring a transfer of such amounts thereto prior to payment of such amounts to such a Credit Provider.

(e) **Expense Subaccount.** The Trustee shall transfer from the Pledged Revenue Account to the respective Expense Subaccounts for each series of Bonds the amounts directed by the Indenture for the payment of amounts due and owing to the Trustee, any Paying Agent, Remarketing Agent, Bond Registrar, Credit Provider, Special Escrow Agent, Collecting Agent or other Fiduciary which are Bond Related Costs or Bond Service Charges.

(f) **Purchase or Repayment of Bonds at Request of Authority, Purchase Subaccount.** Amounts in the respective Purchase Subaccounts, if any shall be used as directed in the applicable Supplemental Indenture to purchase the related Series of Bonds.

(g) **Capitalized Interest Subaccount.** Except as provided in a Supplemental Indenture, to the extent available therein, on each date Revenues are regularly transferred to the Indenture, the Trustee shall transfer from the Capitalized Interest Subaccount to any related Interest Subaccount, the amount of interest required to be transferred under the Indenture.

Debt Service Reserve Account. In connection with the issuance of the Initial Series of Bonds under the Indenture, a deposit to the credit of the Debt Service Reserve Account was made by the Trustee from the proceeds thereof or from such other available moneys in the amount equal to the initial Debt Service Reserve Requirement or, in lieu thereof, the Authority may cause a Debt Service Reserve Account Credit Facility to be delivered to the Trustee for such purpose. Upon delivery of each Series of Additional Bonds under the Indenture, a deposit to the credit of the Debt Service Reserve Account is to be made by the Trustee from the proceeds of such Series of Bonds or such other available moneys as are provided to the Trustee for such purpose, as specified in the applicable Supplemental Indenture, in such amount as will cause the value of the moneys and investments on deposit in the Debt Service Reserve Account to equal the Debt Service Reserve Requirement effective upon the issuance and delivery of such Series of Bonds, or in lieu thereof, the Authority may cause a Debt Service Reserve Account Credit Facility to be delivered to the Trustee for such purpose. Thereafter the Debt Service Reserve Account shall be maintained at the Debt Service Reserve Requirement by transfers to the Debt Service Reserve Account from the Pledged Revenue Account; provided, however, (i) in the event the amount on deposit in the Debt Service Reserve Account is less than the Debt Service Reserve Requirement because of a transfer to the Interest Subaccount or the Principal Subaccount by the Indenture, then the Authority shall be required to restore the deficiency caused thereby (1) to the extent there are any amounts on deposit in the Surplus Account, by the transfer to the Trustee for deposit into the Debt Service Reserve Account of the full amount on deposit in the Surplus Account or such lesser amount as will cure such deficiency in the Debt Service Reserve Account, and (2) to the extent any deficiency remains following application as provided in (i)(1) hereof, by equal monthly transfers of Revenues from the Pledged Revenue Account so as to remedy such deficiency and pay in full all amounts owed under or in connection with a Debt Service Reserve Account Credit Facility, any related Credit Agreement and any Related Agreements over the period of twelve (12) calendar months following the month in which such transfer to the Interest Subaccount or the Principal Subaccount occurs and (ii) in the event the amount on deposit in the Debt Service Reserve Account is less than the Debt Service Reserve Account Requirement because of any valuation of the investment securities as determined pursuant to the Indenture the Authority shall be required to restore the deficiency caused thereby by equal monthly transfers of Revenues from the Pledged Revenue Account over the period of twelve (12) consecutive calendar months following the month in which the determination that such deficiency was made. If on any Interest Payment Date there are not sufficient amounts on deposit in the Interest Subaccount to pay the total amount of interest coming due on any Bonds on such Interest Payment Date or if on any Principal Payment Date there are not sufficient amounts on deposit in the Principal Subaccount to pay the total amount of principal coming due on any Bonds on such Principal Payment Date, and after making the transfers required to be made from other Account as provided in the Indenture and (ii) prior to a transfer from the Debt Service Reserve Account, the Trustee shall transfer sums on deposit in the Debt Service Reserve Account, as provided in the Indenture to the Interest Subaccount or Principal Subaccount, as the case may be, in an amount sufficient to make up any such deficiency.

Cost of Issuance Account. The Trustee may establish within the Cost of Issuance Account a separate, segregated account for the benefit of one or more Series of Bonds as provided in the Supplemental Indenture creating such Series of Bonds. There shall be deposited in the Cost of Issuance Account, from the proceeds of each Series of Bonds, the amount specified pursuant to the Supplemental Indenture creating such account.

Rebate Account. Moneys deposited and held in the Rebate Account shall not be subject to the lien or pledge of the Indenture. If, at the time of any calculation, the amount on deposit in the Rebate Account attributable to a specific Series of Tax-Exempt Bonds exceeds the Rebate Amount for such Series of Tax-Exempt Bonds, the Trustee shall transfer the excess to the Pledged Revenue Account. If the Trustee does not have on deposit in the Rebate Account sufficient amounts to make the payments required by the Indenture, the Trustee shall direct the Authority to remit to the Trustee, in immediately available funds, within five Business Days, the amount of the deficiency Investment earnings on amount held in the Rebate Account shall be credited to the Rebate Account upon receipt.

Surplus Account. Moneys held in the Surplus Account may be used: (a) for transfers to the Debt Service Account and Debt Service Reserve Account to maintain the required balances therein if no other funds are available for such purposes, (b) for transfers to the Project Account or Subaccount thereof to pay costs of an Approved Project, or (c) for any other purpose as directed by the Authority now or hereafter authorized by law.

Investments. If there are Bonds Outstanding and no Event of Default has occurred or is continuing, an authorized Officer may invest moneys on deposit to the credit of the Project Account, Pledged Revenue Account, the Debt Service Account and the Debt Service Reserve Account.

Events of Default. The following constitute "Events of Default" under the Indenture:

(a) payment of interest on any Series of Bonds shall not be made when the same shall become due and payable; or

(b) payment of the principal or Redemption Price of any Series of Bonds or of a Sinking Fund Installment shall not be made when the same shall become due and payable; or

(c) the Authority shall fail to observe or perform in any material way any covenant, condition, agreement or provision contained in any Bonds or in this Indenture or any Supplemental Indenture on the part of the Authority to be performed other than those set forth in (a) and (b) of this Section, and such failure shall continue for thirty (30) days after written notice specifying such failure and requiring the same to be remedied shall have been given to the Authority by the Trustee, which notice may be given by the Trustee in its discretion and shall be given by the Trustee at the written request of the Owners of not less than 25% in principal amount of any Outstanding Bonds; provided, however, that if said default be such that it cannot be corrected within the applicable period, it shall not constitute an Event of Default if corrective action is instituted by the Authority within the applicable period and diligently pursued until the default is corrected and an Authorized Officer of the Authority has delivered to the Trustee a certificate to that effect; or

(d) an "Event of Default" as such term is defined in any Loan Agreement; or

(e) the occurrence of an Act of Bankruptcy by the Authority.

Proceedings by Trustee. Upon the happening and the continuance of any Event of Default the Trustee in its discretion may, and at the written request of the Owners of not less than 25% principal amount of any Series of Bonds Outstanding shall: (i) by mandamus or other suit, action or proceeding at law or in equity, enforce all rights of the Owners and require the Authority to enforce all rights of the Owners of Bonds, and to require the Authority to carry out any other covenant or agreement with Owners of Bonds and to perform its duties under the Indenture, (ii) bring suit upon the Bonds, (iii) by action or suit in equity to require the Authority to account as of they were trustees of an express trust, or to enjoin any acts or things which may be unlawful or in violation of the rights of the Owners, (iv) as a matter of right, have a receiver or receivers appointed for the Trust Estate and of the revenues, issues, earnings, income, products and profits thereof, pending such proceedings, with such powers as the court making such appointment shall confer, (v) by mandamus or other suit, action or proceeding at law or in equity, enforce or require the Authority to enforce, all of the rights of the Authority and the Trustee under and pursuant to the Loan Agreement, the applicable Loan Notes or the Special Escrow Agreement, and to require the Government to carry out any of its other covenants or agreements or perform any of its duties thereunder; and (vi) by mandamus or other suit, action or proceeding at law or in equity, enforce all rights of Owners of Bonds and Swap Providers and require the Authority to enforce all rights of the Owners of Bonds and Swap Providers, and to require the Authority to carry out any other covenant or agreement with Owners of Bonds and Swap Providers and to perform its duties hereunder or under any Qualified Swap Agreements.

Upon the occurrence of an Event of Default under any Related Document, the Trustee may also enforce any and all rights or obligations of the Trustee thereunder.

Rights of Owners. Anything in the Indenture to the contrary notwithstanding, subject to the limitations and restrictions as to the rights of the Owners set forth in the Indenture, upon the happening and continuance of any Event of Default, the Owners of not less than 25% in the principal amount of any Series of Bonds then Outstanding shall have the right upon providing the Trustee security and indemnity reasonably satisfactory to it against the costs, expenses and liabilities to be incurred therein or thereby, by an instrument in writing executed and delivered to the Trustee, to direct the method and place of conducting all remedial proceedings to be taken by the Trustee under the Indenture. The Trustee may refuse to follow any direction that conflicts with law, the Indenture or any Supplemental Indenture or would subject the Trustee to personal liability without adequate indemnification therefor.

Restriction on Action by Owners. No Owner of any of the Bonds shall have any right to institute any suit, action or proceeding in equity or at law for the enforcement of any trust under the Indenture, or any other remedy under the Indenture or on said Bonds, unless such Owner previously shall have given to the Trustee written notice of an Event of Default and unless the Owners of not less than 25% in principal amount of any Series of Bonds then Outstanding shall have made written request of the Trustee to institute any such suit, action, proceeding or other remedy, after the right to exercise such powers or rights of action, as the case may be, shall have accrued, and shall have afforded the Trustee a reasonable opportunity either to proceed to exercise the powers in the Indenture granted, or to institute such action, suit or proceeding in its or their name; nor unless there also shall have been offered to the Trustee security and indemnity reasonably satisfactory to it against the costs, expenses and liabilities to be incurred therein or thereby, and the Trustee shall not have complied with such request within a reasonable time; and such notification, request and offer of indemnity are thereby declared in every such case, at the option of the Trustee, to be conditions precedent to the execution of the trusts of the Indenture or for any other remedy under the Indenture or Supplemental Indenture; it being understood and intended that no one or more Owners of any Series of Bonds secured by the Indenture shall have any right in any manner whatever by his or their action to affect the security of the Indenture, or to enforce any right under the Indenture or under the Bonds and that all proceedings at law or in equity shall be instituted, had and maintained for the equal benefit of all Owners of Outstanding Bonds, subject to the provisions of the Indenture and any Supplemental Indenture.

Waiver of Events of Default; Effect of Waiver. The Trustee may waive any Event of Default under the Indenture and its consequences and shall do so upon the written request of the Owners of at least a majority in principal amount of all Outstanding Bonds, provided, however, that there shall not be waived (i) any Event of Default pertaining to the payment of the principal of any Bond at its maturity date or redemption date prior to maturity, or (ii) any Event of Default pertaining to the payment when due of the interest on any Bond, unless prior to such waiver or rescission, all arrears of principal (due otherwise than by declaration) and interest, with interest (to the extent permitted by law) at the rate per annum borne by the Bonds in respect of which such event of default shall have occurred on overdue installments of interest, and all arrears of payments of principal when due, as the case may be, and all expenses of the Trustee in connection with such event of default, shall have been paid or provided for, and in case of any such waiver or rescission, or in case any proceeding taken by the Trustee on account of any such event of default shall be discontinued or abandoned or determined adversely, then and in every such case the Authority, the Trustee and the Bondowners shall be restored to their former positions and rights under the Indenture.

Priority of Payment. All Bonds issued under and secured by the Indenture shall be equally and ratably secured by and payable from the Debt Service Account without priority of one Bond over any other, except as otherwise expressly provided (i) in the Indenture with respect to Bonds of a specific Series (or specific Bonds within a Series) secured by a Credit Facility, or (ii) in a Supplemental Indenture, or (iii) with respect to moneys or assets whether or not held in the Debt Service Account pledged to secure one or more Series of Bonds (or specific Bonds within a Series) and not other Bonds. Upon the occurrence of an Event of Default, all moneys collected pursuant to action taken pursuant to the Trustees' or Bondowners' remedies under the Indenture after payment of the costs and expenses of the proceedings resulting in the collection of such moneys and of the expenses, liabilities and advances incurred or made by the Trustee and after any other prior application of such moneys has been made as is required by law shall be deposited in such Account or Accounts described in the Indenture as the Trustee deems appropriate;

and all moneys in the Debt Service Account (and at the discretion of the Trustee except when otherwise required), excluding however (1) any moneys held in trust for the payment of any Bonds or interest thereon which have matured or otherwise become payable prior to such Event of Default, (2) any moneys (such as Credit Facility proceeds) pledged exclusively to secure one or more specific Series of Bonds (or specific Bonds within a Series) shall be applied as provided as set forth in the Indenture.

Application of Moneys. Unless the principal of Bonds shall have become due and payable, all such moneys in the respective Accounts and Subaccounts securing such obligations shall be applied consistent with the respective priorities of liens and the respective purposes for such accounts each as follows:

FIRST: To the payment of the persons entitled thereto of all installments of interest then due on the Bonds in the order of the maturity of the installments of such interest and if the amount available shall not be sufficient to pay in full any particular installment then to the payment ratably, according to the amounts due on such installment to the persons entitled thereto without any discrimination or privilege;

SECOND: To the payment of the persons entitled thereto of the unpaid principal of and redemption premium, if any, on any of the Bonds which shall have become due (other than Bonds which have matured or have otherwise become payable prior to such Event of Default and moneys for payment of which are held in trust pursuant to the provisions of the Indenture) in the order of their due dates and if the amount available shall not be sufficient to pay in full the unpaid principal and redemption premium, if any, on Bonds due on any particular due date, then to the payment ratably, according to the amount of principal and premium, if any, due on such date, to the persons entitled thereto, without any discrimination or privilege;

THIRD: To the payment of interest on and the principal of the Bonds as thereafter may from time to time become due, all in accordance with the provisions of the Indenture; and

FOURTH: To reimburse the Trustee for certain costs and expenses described in the Indenture and not reimbursed thereunder.

Whenever moneys are to be applied by the Trustee pursuant to the provisions of this Section, such moneys shall be applied by it at such times and from time to time as the Trustee shall determine having due regard to the source of such moneys, the amount of such moneys available for application and the likelihood of additional moneys becoming available for such application in the future. Whenever the Trustee shall apply such funds, it shall (1) fix the date (which shall be an Interest Payment Date unless it shall deem another date more suitable) upon which such application is to be made and upon such date interest on the amounts of principal to be paid on such dates shall cease to accrue and (2) on or before such date set aside the moneys necessary to effect such application. The Trustee shall give to the Bondowners mailed notice of the deposit with it of any such moneys and of the fixing of any such date. Neither the Trustee nor any Paying Agent shall be required to make payment to the Owner of any Bond until such Bond shall be presented to the Trustee for appropriate endorsement or for cancellation of fully paid.

Whenever all Bonds and interest thereon and all other indebtedness secured by the Indenture have been paid under the provisions of this Section and all expenses and charges of the Trustee have been paid any balance remaining shall be paid to the Authority.

Duties, Immunities and Liabilities of Trustee. The Trustee shall, prior to an Event of Default, and after the curing of all Events of Default which may have occurred, perform such duties and only such duties as are specifically set forth in the Indenture and no implied duties or obligations shall be read into the Indenture against the Trustee. The Trustee shall, during the existence of any Event of Default (which has not been cured) exercise such of the rights and powers vested in it by the Indenture, and use the same degree of care and skill in their exercise as a prudent individual would exercise or use under the circumstances in the conduct of his own affairs.

The Trustee is not required to risk or expend its own funds or otherwise incur any financial liability in the performance of any of its duties if it shall have reasonable grounds for believing that repayment of such funds or adequate indemnity against such risk or liability is not assured to it.

In accepting the trust created by the Indenture, the Trustee acts solely as Trustee for the Owners and not in its individual capacity.

The Trustee makes no representation or warranty, express or implied, as to the compliance with legal requirements of the use contemplated by the Authority of the funds under the Indenture or any Supplemental Indenture. In no event shall the Trustee be liable for incidental, indirect, special or consequential damages in connection with or arising from the Indenture or Supplemental Indenture.

The Trustee shall not be responsible for the sufficiency, timeliness or enforceability of the remedies. The Trustee shall have no responsibility in respect of the validity or sufficiency of the Indenture or any Supplemental Indenture or the security provided hereunder or the due execution of the Indenture by the Authority, or the due execution of any other document by any party (other than the Trustee) thereto, or in respect of the validity of any Bonds authenticated and delivered by the Trustee in accordance with the Indenture or to see to the recording or filing (but not refiling) of the Indenture, any Supplemental Indenture or any financing statement or any other document or instrument whatsoever.

The Trustee shall not be deemed to have knowledge of any Event of Default under the Indenture unless and until an officer of its corporate trust department shall have actual knowledge thereof.

The Trustee shall not be liable or responsible because of the failure of the Authority to perform any act required of it by the Indenture or any Supplemental Indenture or because of the loss of any moneys arising through the insolvency or the act or default or omission of any depository other than itself in which such moneys shall have been deposited under the Indenture or any Supplemental Indenture. The Trustee shall not be responsible for the application of any of the proceeds of the Bonds or any other moneys deposited with it and paid out, invested, withdrawn or transferred in accordance with the Indenture or for any loss resulting from any such investment. The Trustee shall not be liable in connection with the performance of its duties under the Indenture except for its own misconduct, negligence or bad faith.

The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Holders of a majority in principal amount of the Outstanding Bonds relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee or any trust or power conferred upon the Trustee under the Indenture or any Supplemental Indenture.

Removal, Resignation of Trustee, Successor Trustee. The Authority in its sole discretion may remove the Trustee without cause at any time if no Event of Default has occurred and is continuing and shall remove the Trustee if at any time requested to do so by an instrument or concurrent instruments in writing signed by the Owners of not less than a majority in aggregate principal amount of the Bonds then Outstanding (or their attorneys duly authorized in writing) or if at any time the Trustee shall cease to be eligible or shall become incapable of acting, or shall commence a case under any bankruptcy, insolvency or similar law, or a receiver of the Trustee or of its property shall be appointed, or any public officer shall take control or charge of the Trustee or its property or affairs for the purpose of rehabilitation, conservation or liquidation, in each case by giving written notice of such removal to the Trustee, and thereupon shall appoint a successor Trustee by an instrument in writing.

The Trustee may resign by giving written notice of such resignation to the Authority and by giving notice of such resignation by mail, first class postage prepaid, to the Owners at the addresses listed in the Bond Register. Upon receiving such notice of resignation, the Authority shall promptly appoint a successor Trustee by an instrument in writing.

Any removal or resignation of the Trustee and appointment of a successor Trustee shall become effective upon acceptance of appointment by the successor Trustee. If no successor Trustee shall have been appointed and shall have accepted appointment within 45 days of giving notice of removal or notice of resignation as aforesaid, the resigning Trustee, or any Owner (on behalf of himself and all other Owners) may petition any court of competent jurisdiction for the appointment of a successor Trustee, and such court may thereupon, after such notice (if any) as it may deem proper, appoint such successor Trustee. Any successor Trustee appointed under the Indenture shall signify its acceptance of such appointment by executing and delivering to the Authority and to its predecessor Trustee a written acceptance of such appointment by executing and delivering to the Authority and to its predecessor

Trustee a written acceptance thereof, and thereupon such successor Trustee, without any further act, deed or conveyance, shall become vested with all the moneys, estates, properties, rights, powers, trusts, duties and obligations of such predecessor Trustee, with like effect as if originally named Trustee in the Indenture; but, nevertheless, at the written request of the Authority or of the successor Trustee, such predecessor Trustee shall execute and deliver any and all instruments of conveyance or further assurance and do such other things as may reasonably be required for more fully and certainly vesting and confirming to such successor Trustee all the right, title and interest of such predecessor Trustee in and to any property held by it under the Indenture and shall pay over, transfer, assign and deliver to the successor Trustee any money or other property subject to the trusts and conditions set forth in the Indenture. Upon acceptance of appointment by a successor Trustee as provided in this subsection, such successor Trustee provide notice of the succession of such Trustee to the trusts hereunder by first class mail, postage prepaid, to each Paying Agent and to the Owners at their addresses listed in the Bond Register.

Any Trustee appointed shall be a trust company or bank having the powers of a trust company, having a corporate trust office in the United States, having a combined capital and surplus of at least one hundred million dollars ($100,000,000), and subject to supervision or examination by federal or state authority.

Merger or Consolidation of Trustee. Any company into which the Trustee or any Paying Agent may be merged or converted or with which it may be consolidated or any company resulting from any merger, conversion or consolidation to which it shall be a party or any company to which the Trustee or any Paying Agent may sell or transfer all or substantially all of its corporate trust business provided such company shall be eligible under the Indenture, may succeed to the rights and obligations of such Trustee or Paying Agent, as the case may be, without the execution or filing of any paper or any further act, anything in the Indenture to the contrary notwithstanding; provided that upon the sale or transfer of corporate trust business as a result of such merger or consolidation, so long as no Event of Default has occurred and is continuing, the Authority may by an instrument in writing appoint a successor Trustee or Paying Agent other than the company resulting from such merger, conversion or consolidation by the Trustee or the Paying Agent.

Liability of Fiduciaries. Facts in the Indenture, in any Supplemental Indenture and in the Bonds shall be taken as statements of the Authority, and neither the Trustee nor any Paying Agent assumes any responsibility for the correctness or makes any representations as to the validity or sufficiency of the Indenture, any Supplemental Indenture or of the Bonds other than in connection with the duties or obligations therein or in the Bonds assigned to or imposed upon it. The Trustee shall, however, be responsible for its representations contained in its certificate of authentication on the Bonds. Neither the Trustee nor any Paying Agent shall be liable in connection with the performance of its duties under the Indenture, except for its own negligence or default. The Trustee or any Paying Agent may become the Owner of Bonds with the same rights they would have if they were not Trustee or Paying Agent, respectively, and, to the extent permitted by law, may act as depository for and permit any of their officers or directors to act as a member of, or in any other capacity with respect to, any committee formed to protect the rights of Owners, whether or not such committee shall represent the Owners of a majority in principal amount of the Bonds then Outstanding.

No Recourse on the Bonds. No recourse shall be had for the payment of the principal of or interest on the Bonds or for any claim based thereon or on the Indenture against any member or officer of the Authority or any person executing the Bonds and no such member, officer or person shall be liable personally on the Bonds.

Right to Indemnification. The Trustee shall be under no obligation to institute any suit, or to take any remedial proceeding under the Indenture, or to enter any appearance in or in any way defend in any suit in which it may be made defendant, or to take any steps in the execution of the trusts created by the indenture or in the enforcement of any rights and powers under the Indenture, until it shall be indemnified to its satisfaction against any and all reasonable costs and expenses, outlays, and counsel fees and other disbursements, and against all liability not due to its willful misconduct, negligence or bad faith.

Supplemental Indenture Without Consent of Bondowners. For any one or more of the following purposes and at any time or from time to time, a Supplemental Indenture of the Authority may be entered into, which, without the requirement of consent of Bondowners, shall be fully effective in accordance with its terms:

(a) To provide for the issuance of a Series of Bonds and to prescribe the terms and conditions pursuant to which the same may be issued, paid or redeemed; provided, however, that such Supplemental Indenture shall not conflict with the Indenture as theretofore in effect;

(b) To add to the covenants and agreements of the Authority in the Indenture, other covenants and agreements to be observed by the Authority which are not contrary to or inconsistent with the Indenture as theretofore in effect;

(c) To add to the limitations and restrictions in the Indenture, other limitations and restrictions to be observed by the Authority which are not contrary to or inconsistent with the Indenture as theretofore in effect;

(d) To confirm, as further assurances, any pledge under, and the subjection to any lien or pledge created or to be created by, the Indenture, of any moneys, securities or fund, or to establish any additional funds or accounts to be held under the Indenture;

(e) To cure any ambiguity, supply any omission, or cure or correct any defect or inconsistent provision in the Indenture;

(f) To insert such provisions clarifying matters or questions arising under the Indenture as are necessary or desirable and are not contrary to or inconsistent with the Indenture as theretofore in effect;

(g) To modify the Indenture or the Bonds to permit qualification under the Trust Indenture Act of 1939 or any similar federal statute at the time in effect, or to permit the qualification of the Bonds for sale under the securities laws of any state of the United States;

(h) To make such changes as may be necessary to obtain an investment grade rating or to maintain or upgrade any rating for all or any Series of Bonds by a Rating Agency;

(i) To grant to or confer upon the Trustee for the benefit of the Owners any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the Owners or the Trustee;

(j) To subject to the lien and pledge of the Indenture additional revenue, properties or collateral;

(k) To evidence the appointment of a separate trustee or a co-trustee or the successor of a Trustee and/or Paying Agent under the Indenture;

(l) To modify, eliminate and/or add to the provisions of the Indenture to such extent as shall be necessary to prevent any interest on Tax-Exempt Bonds from becoming taxable under the Code; or

(m) To make any other change which in the judgment of Authority and Trustee is necessary or desirable and will not materially prejudice any non-consenting owner of a Bond.

Supplemental Indenture With Consent of Bondowners. Any modification or amendment of the Indenture and of the rights and obligations of the Authority and of the Owners of the Bonds thereunder, in any particular, may be made by a Supplemental Indenture, with the written consent (a) of the Owners of at least 51% in principal amount of the Bonds Outstanding at the time such consent is given, and (b) in the case less than all of the several Series of Bonds then Outstanding are affected by the modification or amendment, of the Owners of at least 51% in principal amount of the Bonds of each Series so affected and Outstanding at the time such consent is given; provided, however, that if such modification or amendment will, by its terms, not take effect so long as any Bonds of any specified like Series and maturity remain Outstanding, the consent of the Owners of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of any calculation of Outstanding Bonds under this Section. No such modification or amendment shall permit a change in the terms of redemption or maturity of the principal of any Outstanding Bond or of any installment of interest thereon or a reduction in the principal amount or the Redemption Price, if any, thereof, or in the rate of interest thereon without the consent of the Owners of such Bond, or shall reduce the percentages or otherwise affect the classes of Bonds the consent of the

Owners of which is required to effect any such modification or amendment, or shall change or modify any of the rights or obligations of any Fiduciary without the filing with the Trustee of the written assent thereto of such Fiduciary in addition to the consent of the Bondowners. For the purposes of this Section, a Series shall be deemed to be affected by a modification or amendment of the Indenture if the same adversely affects or diminishes the rights of the Owners of Bonds of such Series.

Defeasance. The pledge and other moneys and securities pledged under the Indenture and any Supplemental Indenture and all covenants, agreements and other obligations of the Authority to the Bondowners shall cease and be satisfied if the Authority shall pay or cause to be paid, or there shall otherwise be paid: (i) to the Owners of all Bonds the principal or Redemption Price, if applicable, and interest due or to become due thereon, at the times and in the manner stipulated in the Bonds and in the Indenture and any Supplemental Indenture and (ii) to the Trustee all amounts due and owing the Trustee. Subject to the Indenture provisions, any Outstanding Bonds shall, prior to the maturity or redemption date thereof be deemed to have been paid if (i) in case any of said Bonds are to be redeemed on any date prior to their maturity, the Authority shall have given to the Trustee irrevocable instructions and notice of redemption, (ii) there shall have been set aside irrevocably in trust, in compliance with the Act, an amount which shall be sufficient to generate the principal of and the interest on which when due to provide moneys which, together with the moneys, if any, set aside in trust, in compliance with the Act, at the same time, shall be sufficient, to pay when due the principal or Redemption Price, if applicable, and interest due and to become due on said Bonds on or prior to the redemption date or maturity date thereof, as the ease may be, and (iii) in the event said Bonds are not by their terms subject to redemption within the next succeeding 60 days, the Authority shall have given the Trustee in form satisfactory to it instructions to mail a notice to the Owners of such Bonds that the deposit required by (ii) above has been made with the Trustee and a verification report from an independent certified public accountant confirming the sufficiency of the Defeasance Securities received by the Trustee and that said Bonds are deemed to have been paid and stating such maturity or redemption date upon which moneys are expected to be available for the payment of the principal or Redemption Price, if applicable, on said Bonds.

Notice. Any Notice, demand, direction, request or other instrument authorized or required by the Indenture to be given to or filed with the Authority or the Trustee shall be deemed to have been sufficiently given or filed for all purposes of the Indenture if and when sent by registered mail, return receipt requested.

THE SEVENTH SUPPLEMENTAL INDENTURE

The following is a summary of certain provisions of the Seventh Supplemental Indenture. Such summary does not purport to be complete or definitive and reference is made to the Seventh Supplemental Indenture for a full and complete statement of the terms and provisions and for the definition of capitalized terms used in this summary and not otherwise defined under APPENDIX A - “Glossary of Certain Defined Terms.”

Authorization and Details of Series 2006 Bonds. The Seventh Supplemental Indenture authorizes the issuance of the Series 2006 Bonds, the proceeds of which shall be used to (i) advance refund the Prior Bonds, (ii) fund certain capital projects identified on Exhibit C hereto, (iii) pay the costs associated with terminating the 2003 Swap Agreement, (iv) fund the Debt Service Reserve Account, (v) fund the Net Payments Reserve Account, and (vi) pay certain costs incidental to the issuance of the Series 2006 Bonds.

Bonds Equally and Ratably Secured. Except as provided in the Seventh Supplemental Indenture, the Series 2006 Bonds shall in all respects be equally and ratably secured.

Details of the Series 2006 Bonds. The Series 2006 Bonds shall be dated the date of delivery, shall be issuable as fully registered bonds in the denomination of $5,000, or any multiple thereof., and shall bear interest paid semiannually on each April 1 and October 1 in the years and amounts specified in the Seventh Supplemental Indenture.

Securities Depository Provisions. Initially, one certificate for each maturity of each Series of Series 2006 Bonds will be issued and registered to the Securities Depository, or its nominee, in a book-entry system.

Optional Redemption. As directed by the Authorized Representative of the Authority, the Series 2006 Bonds are subject to redemption upon payment of the Redemption Prices specified in the Seventh Supplemental Indenture. If less than all of the Series 2006 Bonds of any Series are called for redemption, they shall be called in such order of maturity as the Authority may determine. The portion of any Bond to be redeemed shall be in the principal amount of $5,000 or some multiple thereof, owner upon the surrender thereof. Notice of redemption shall be given in the manner set forth in Indenture.

Funds and Accounts. There shall be established within the Debt Service Account the Series 2006 Interest Subaccount and the Series 2006 Principal Subaccount. Moneys in such subaccounts shall be used in accordance with the Indenture. There shall be established within the Debt Service Account the Series 2006 Interest Subaccount, the Series 2006 Principal Subaccount, the Series 2006 Redemption Subaccount, the Restricted Moneys Sub-Subaccount within the Series 2006 Redemption Subaccount and the Series 2006 Expense Subaccount. Moneys in such subaccounts shall be used in accordance with Sections 5.05(b), (c), (d) and (f), respectively, of the Original Indenture. Pursuant to Section 5.01(b)(ii)(2)(H) and in accordance with Section 5.01(e) of the Original Indenture, there shall be established within the Series 2006 Bond Interest Subaccount of the Debt Service Account the Series 2006 Bonds Net Payments Sub-subaccount. Moneys in such subaccount shall be used, at the direction of the Authority, to make Series 2006 Swap Agreement Net Payments.

There shall be established within the Project Account the Series 2006 Project Subaccount. The portion of the proceeds of the Series 2006 Bonds specified in the Seventh Supplemental Indenture shall be deposited in the Series 2006 Project Subaccount and used to pay costs associated with the Series 2006 Capital Project. Moneys in the Series 2006 Project Subaccount shall be disbursed upon the written order of an authorized officer of the Authority .

Any net payment which the Authority receives with respect to any Qualified Swap Agreement shall be deemed to be “Revenues” and shall be deposited in the Pledged Revenue Account.

There shall be established with the Trustee the Net Payments Reserve Account. The portion of the proceeds of the Series 2006 Bonds specified in the Seventh Supplemental Indenture shall be deposited in the Net Payments Reserve Account. The Trustee shall notify the Authority of any required Series 2006 Swap Agreement Net Payments. Moneys in the Net Payments Reserve Account shall be used by the Trustee at the direction of the

Authority to make any required deposits to the Series 2006 Bonds Net Payments Sub-subaccount. If the Series 2006 Swap Agreement is terminated, remaining moneys on deposit in the Net Payments Reserve Account, at the direction of the Authority, shall be either (i) used to pay any termination fee, (ii) transferred to the Series 2006 Project Account to be used for the Series 2006 Capital Project or (iii) used to redeem Series 2006 Bonds. Moneys deposited and held in the Net Payments Reserve Account shall *not* be subject to the lien or pledge of the Indenture.

There shall be established within the Cost of Issuance Account the Series 2006 Cost of Issuance Subaccount. Moneys in the Series 2006 Cost of Issuance Subaccount shall be used in accordance with the provisions of the Indenture.

Security for Series 2006 Bonds. The Series 2006 Bonds shall be equally and ratably secured under the Indenture with any other Bonds issued pursuant to the Indenture, without preference, priority or distinction of any Bonds over any other Bonds, as provided in the Indenture.

Rebate Account. There shall be established within the Rebate Account.. the Series 2006 Rebate Subaccount to be held by the Trustee. Moneys deposited in the Series 2006 Rebate Subaccount shall be applied in accordance with the Indenture.

Additional Provisions Relating to Bond Insurer and Bond Insurance Policy. The Seventh Supplemental Indenture provides certain rights to the Bond Insurer. The Bond Insurer is deemed to be the sole holder of the Series 2006 Bonds with respect to all provisions governing events of default and remedies (except the giving of notice of default to Bondholders). Any waiver of an Event of Default by the Trustee is subject to the prior written consent of the Bond Insurer. Certain amendments or supplements to the Original Indenture or Seventh Supplemental Indenture are subject to the prior written consent of the Bond Insurer.

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APPENDIX C

SUMMARY OF CERTAIN PROVISIONS OF THE SERIES 2006 LOAN AGREEMENT

The following is a summary of certain provisions of the Series 2006 Loan Agreement. Such summary does not purport to be complete or definitive, and reference is made to the Loan Agreement for a full and complete statement of its terms and provisions and for the definition of capitalized terms used in this summary and not otherwise defined under APPENDIX A - "Glossary of Certain Defined Terms."

The Loan. The Authority, on the terms and conditions set forth in the Series 2006 Loan Agreement, shall issue, sell, and deliver the Series 2006 Bonds to the Underwriter and make a Loan of the proceeds of the Series 2006 Bonds to the Government.

Repayment of the Loan. The Government promises to repay the Loan and observe the terms and provisions of the Series 2006 Loan Agreement. The Loan shall be evidenced by the Government's 2006 Gross Receipts Taxes Loan Note in the principal amount of $219,490,000. The Government shall repay the Series 2006 Loan Note in installments of principal not later than the second Business Day preceding October 1 in each year in amounts equal to the amounts due for principal or Redemption Price of, and interest on, the Series 2006 Bonds. The Series 2006 Loan Note will accrue interest at rates equal to the rates of interest accruing on the Bonds, payable semiannually not later than the second Business Day preceding each April 1 and October 1, commencing April 1, 2007 and ending on the second Business Day preceding the final maturity thereof. Interest on the Series 2006 Loan Note shall be computed on the basis of a 360 day year composed of twelve (12) thirty (30) day months.

Redemption of the Series 2006 Loan Note. The Series 2006 Loan Note may, at the option of the Government, be redeemed, in whole or in part, prior to its maturity at the times, in the manner of and on the same maturities as an optional redemption of the Authority's respective Series 2006 Bonds and at a Redemption Price equal to the principal amount of, plus accrued interest thereon to the date of redemption and any premium required to provide for the payment of the optional redemption of the Authority's respective Series 2006 Bonds. In addition, in the event the Series 2006 Bonds are subject to mandatory redemption in whole or in part or in the event the Series 2006 Bonds are tendered by the holders thereof for purchase and are purchased by the Authority for retirement and cancellation then, upon payment of the Redemption Price or purchase price of such Bonds, the Government shall be deemed to have made a prepayment on the Series 2006 Loan Note, in accordance with the terms of the Series 2006 Loan Agreement, in a principal amount equal to the aggregate principal amount of the Series 2006 Bonds so redeemed or purchased.

Monthly Funding of Series 2006 Loan Note Payments. In order to provide for the timely payment of the principal of, the purchase price of, Redemption Price, if any, of and interest on the Series 2006 Loan Note on the dates specified in the Series 2006 Loan Agreement and all other amounts due thereunder, the Special Escrow Agent will make, or cause the Collecting Agent to make on its behalf, transfers to the Trustee for deposit into the Pledged Revenue Account at the times and in the amounts specified in the Special Escrow Agreement. To the extent such amounts so transferred by or on behalf of the Special Escrow Agent to the Trustee are not sufficient to fund in flail any installment of principal, interest or other amount payable on the Series 2006 Loan Note by the date which is thirty (30) days prior to the due date thereof in the amounts set forth therein and in the Series 2006 Loan Agreement, the Trustee shall promptly provide written notification to the Government and the Authority of such deficiency and the Government shall on or before the date which is fifteen (15) days prior to such due date, remit or cause to be remitted to the Trustee for deposit in the Pledged Revenue Account immediately available funds out of any other monies of the Government legally available therefore an amount equal to such deficiency.

Application of Proceeds. The Authority shall deposit all funds received from the proceeds of the Series 2006 Bonds into the respective Accounts and Subaccounts in accordance with the Series 2006 Loan Agreement.

Security. The Series 2006 Loan Note is a general obligation of the Government and is secured by its full faith and credit and taxing power. As further security for the payment of the Series 2006 Loan Note, the Government grants and pledges to the Trustee a lien and security interest in the Gross Receipts Taxes (with the exception of the Required Annual Moderate Income Housing Fund Deposit), on a parity with the outstanding Bonds, the regularly scheduled net payments under the Series 2006 Swap Agreement and any other additional parity indebtedness and to the extent provided in the Series 2006 Loan Agreement, and the Government consents to the deposit of the Gross Receipts Taxes into the Special Escrow Account, as provided for in the Special Escrow Agreement and the Collecting Agent Agreement.

Representations and Warranties of the Government. The Government makes the following representations and warranties to the Authority:

(a) As of the date of the execution and delivery of the Loan Agreement, the amount of Gross Receipts Taxes anticipated to be collected by the Government is a sum which, during the period the Series 2006 Loan Note is outstanding, is reasonably expected to be in excess of the amount necessary to pay the principal of, interest on and all other amounts payable under the Series 2006 Loan Note and parity obligations as the same becomes due.

(b) The Government is duly authorized and has full power and authority to execute, deliver and perform its obligations under the Series 2006 Loan Agreement, the Special Escrow Agreement, the Series 2006 Loan Note and the Collecting Agent Agreement.

(c) The aggregate principal amount of outstanding public indebtedness of the Government is and, as of the date of issuance and delivery of the Series 2006 Bonds, will be, in compliance with the limitation on such public indebtedness contained in Section 8(b) of the Revised Organic Act (48 USC § 1574(b)(ii)(A)).

(d) The execution, delivery and performance by the Government of the Series 2006 Loan Agreement, the Special Escrow Agreement, the Series 2006 Loan Note and the Collecting Agent Agreement (i) have been duly authorized by all necessary action on the part of the Government; (ii) do not conflict with, or result in a violation of, any provision of law or any order, writ, rule or regulation of any court or governmental agency or instrumentality binding upon or applicable to the Government; (iii) do not and will not conflict with, result in a violation of, or constitute a default under, any agreement, resolution, mortgage, indenture or instrument to which the Government is a party or by which the Government or any of its property is bound; and (iv) do not and will not result in, or require, the creation or imposition of any mortgage, deed of trust, pledge, lien, security interest or other charge or encumbrance of any nature (other than as permitted or arising under this Agreement) upon or with respect to any property of the Government.

(e) No authorization, consent, approval, permit, license, exemption of or filing or registration with, any court or governmental department, commission, board, bureau, agency or instrumentality is or will be necessary for the valid execution, delivery or performance by, or enforcement against or by, the Government of the Series 2006 Loan Agreement, the Special Escrow Agreement, the Series 2006 Loan Note or the Collecting Agent Agreement.

The Series 2006 Loan Agreement, the Special Escrow Agreement, the Series 2006 Loan Note and the Collecting Agent Agreement when executed and delivered by the other parties thereto, constitute, the legal, valid and binding obligations of the Government enforceable against the Government in accordance with their terms, except as such enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws hereinafter enacted or principles of equity affecting the enforcement of creditors' rights generally as such laws may be applied in the event of insolvency, reorganization or other similar proceeding of, or moratorium applicable to, the Government.

(g) The Government is duly authorized under all applicable laws to issue the Series 2006 Loan Note as a general obligation indebtedness of the Government, secured by its full faith and credit and taxing power and to further secure the Series 2006 Loan Note by pledging and assigning the Gross Receipts Taxes (other than the Required Annual Moderate Income Housing Fund Deposit) for the payment of principal and interest on the Series 2006 Loan Note and all amounts payable hereunder and thereunder. The Gross Receipts Taxes pledged and assigned by the Series 2006 Loan Agreement to the payment of principal and interest on the Series 2006 Loan Note, subject to the provisions of Section 7(c) of the Series 2006 Loan Agreement regarding the issuance of parity indebtedness and the Outstanding Bonds, will be free and clear of any pledge, lien, charge or encumbrance thereon or with respect thereto prior to or of equal rank with, the pledge created by the Series 2006 Loan Agreement, and all action on the part of the Government to that end has been and will be duly and validly taken. Upon deposit of the Gross Receipts Taxes (other than the Required Annual Moderate Income Housing Fund Deposit into the Special

Escrow Account pursuant to the Special Escrow Agreement, such amounts so deposited shall not be subject to any prior lien or attachment by any creditor of the Government or any other person other than the lien created by the Series 2006 Loan Agreement, the Special Escrow Agreement or the Indenture.

(h) There are no suits, actions, proceedings or investigations pending or, to the best knowledge of the Government, threatened against or affecting the Government or any of its properties, before or by any court or governmental department, commission, board, bureau, agency or instrumentality, which involve or would materially adversely affect any of the transactions contemplated by the Series 2006 Loan Agreement or by the Series 2006 Loan Note, the Special Escrow Agreement or the Collecting Agent Agreement, or which, if determined adversely. could have a material adverse effect on the financial condition, properties or operations of the Government, or adversely affect the authority of the Government to perform its obligations hereunder or under the Series 2006 Loan Note, the Special Escrow Agreement or the Collecting Agent Agreement.

(i) The Government is not, in any material respect, in breach of or in default under any applicable law or administrative regulation of the United States Virgin Islands or of the United States, relating, in each case, to the Issuance of debt securities by the Government, or any applicable judgment, decree or loan agreement, note, resolution, ordinance, agreement or other instrument to which the Government is a party or is otherwise subject, the consequence of which or the correction of which would materially and adversely affect the financial condition or operations of the Government as a whole.

(j) At the time of issuance of the Series 2006 Loan Note, there are no other bonds, notes or other evidences of indebtedness of the Government outstanding that are secured by the Gross Receipts Taxes (other than the Series 1999A Bonds, the Series 2003 Bonds, and the Subordinate Lien Revenue Notes.

Affirmative Covenants of the Government. The Government covenants and agrees that so long as the Series 2006 Loan Note shall remain outstanding and the principal thereof, interest thereon, and all other amounts payable thereunder shall be unpaid or unprovided for, the Government shall, unless the Authority and the Trustee shall otherwise consent in writing:

(a) Observe and comply with the terms and conditions of and perform all of its obligations under the Series 2006 Loan Agreement, under the Series 2006 Loan Note, the Special Escrow Agreement and the Collecting Agent Agreement, and pay all amounts payable by it under the Series 2006 Loan Agreement and the Series 2006 Loan Note according to the terms of the Loan Agreement and the Series 2006 Loan Note.

(b) Promptly notify the Authority and the Trustee in writing of the occurrence of (i) any Event of Default under the Series 2006 Loan Agreement and (ii) any default under documents governing any debt of the Government.

(c) In furtherance of the pledge of Gross Receipts Taxes set forth in the Series 2006 Loan Agreement, to ensure (1) the receipt of and the maximization of Gross Receipts Taxes and, if applicable, the Substitute Revenues, and (2) the deposit of all Gross Receipts Taxes, and, if applicable, the Substitute Revenues, in the Special Escrow Account of the Government maintained by the Collecting Agent, as agent for the Special Escrow Agent, pursuant to the Special Escrow Agreement and the Collecting Agent Agreement, or such other place as the Government, with the consent of the Authority and the Trustee, may designate in writing.

(d) Observe and comply with the terms and conditions of and perform all of its obligations under the Special Escrow Agreement and the Collecting Agent Agreement.

(e) At all times while the Series 2006 Loan Note is outstanding, to the extent permitted by law, defend, preserve and protect the pledge of the Gross Receipts Taxes and, if applicable, the Substitute Revenues, under the Series 2006 Loan Agreement and the security interest under the Special Escrow Agreement in all amounts on deposit or required to be deposited in the Special Escrow Account and all rights of the holder of the Series 2006 Loan Note against all claims and demands of all third parties.

(f) Consent to the assignment, pursuant to the Indenture, of all right, title and interest of the Authority herein, and all amendments, modifications and renewals thereof, to the Trustee, reserving to the Authority, however, the rights providing that notices and other communications be given to the Authority.

(g) Provide to the Authority and the Trustee within 180 calendar days of the end of each Fiscal Year a financial report summarizing annual receipts of Gross Receipts Taxes and, if applicable the Substitute Revenues.

(h) In the event the Gross Receipts Taxes collected by the Government during any period of twelve (12) consecutive calendar months are less than 150% of maximum annual Adjusted Debt Service Requirement on all Outstanding Bonds and any outstanding Parity Indebtedness permitted by the Series 2006 Loan Agreement during the current or any Subsequent Bond Year, the Government will use its best efforts to identify an additional stream of revenues (the "Substitute Revenues") and to pledge such Substitute Revenues to repayment of the Series 2006 Loan Note. Any such pledge of Substitute Revenues shall remain in effect until such time as the Gross Receipts Taxes collected by the Government during any period of twelve (12) consecutive calendar months occurring thereafter equal or exceed 150% of the maximum Adjusted Debt Service Requirement on Outstanding Bonds and any outstanding Parity Indebtedness permitted by the Series 2006 Loan Agreement, for the current and any Subsequent Bond Year.

(i) The Government has covenanted to require the independent certified public accounting firm that bas contracted with the Government to perform its annual audit (the "Auditor") to perform on a quarterly basis certain agreed-upon procedures on Gross Receipts Tax deposits made to the Collecting Agent. As part of its contract, the Auditor will be required to deliver an agreed-upon procedures report (the "Report") comparing the Gross Receipts Tax payments documented in the Government's financial management system with the total revenues deposited with the Collecting Agent and the deposit receipts remitted by the Collecting Agent to the Revenue Audit section of the Department of Finance, the Authority and the Trustee. The Report will be delivered within 45 days of the end of each fiscal quarter (of the Bond Year) beginning with the quarter ending September 30, 2006.

(j) Provide to the Authority and the Trustee the financial statements, reports and notifications required by the Indenture at the times set forth therein.

Negative Covenants of the Government. The Government covenants and agrees that so long as the Series 2006 Loan Note shall remain outstanding and the principal thereof or interest thereon shall be unpaid or unprovided for, the Government shall not unless the Authority and the Trustee otherwise consent in writing:

(a) Revoke or amend in any way the Special Escrow Agreement or the Collecting Agent Agreement or terminate the Special Escrow Agreement or Collecting Agent Agreement.

(b) Cause or permit the Authority to issue any Additional Bonds under the Indenture other than in conformance with the terms thereof.

(c) Issue any bonds, notes or other obligations or incur any liability for funded indebtedness secured by a pledge, lien, charge or encumbrance of the Gross Receipts Taxes and, if applicable, the Substitute Revenues, which is of a rank superior to or, subject to the immediately following sentence, equal to, the pledge created by the Series 2006 Loan Agreement. Notwithstanding the immediately preceding sentence, the Government may issue its bonds, notes or other obligations for funded indebtedness on a rank equal to the pledge created by the Series 2006 Loan Agreement (hereinafter referred to as "Parity Indebtedness"), provided it bas delivered or caused to be delivered to the Authority and the Trustee a Certificate of an Independent Verification Analyst (as defined in the Indenture) satisfying the requirements of the Indenture.

(d) Take any action, or fail to take any action, if any such action or failure to take action would adversely affect the exclusion from gross income of the interest represented by the Series 2006 Bonds, under Section 103 of the Code. The Government will not directly or indirectly use or permit the use of any proceeds of the Series 2006 Bonds or take or omit to take any action that would cause the Series 2006 Bonds to be "arbitrage bonds" within the meaning of Section 148 of the Code or private activity bonds with the meaning of Section 141 of the

Code. To that end, the Government will comply with all requirements of Section 148 of the Code and Section 141 of the Code to the extent applicable to the Series 2006 Bonds.

(e) Take any actions that would, directly or indirectly result in (1) the repeal, rescission or other termination of the effectiveness of Title 33, Section 43 of the Virgin Islands Code (the “Gross Receipts Taxes Act”), (2) a reduction in the rate or rotes at which the Gross Receipts Taxes are imposed or levied, or (3) a restriction or reduction in the application of the Gross Receipts Taxes; provided, however, that the covenants contained in this subsection (e) shall not restrict the Government's right to provide exemptions to any eligible businesses which apply for new or renewal benefits pursuant to Title 29, Chapters 12 and 13 of the Virgin Islands Code, pertaining to the industrial development program or any similar incentive program determined by the Government to be in the best economic interest of the Government, so long as the grant of any such exemptions do not cause the aggregate Gross Receipts Taxes estimated to be collected thereafter in any fiscal year of the Government to be less than 150% of the maximum Adjusted Debt Service Requirement on Outstanding Bonds and all outstanding Parity Indebtedness permitted by the Series 2006 Loan Agreement, for the current and any subsequent Bond Year, such determination to be made only as of the date of the grant of any such exemptions.

(f) Take any actions or fail to take any actions which will limit, restrict, or in any way impair the collection, transfer, deposit, or disbursement of the Gross Receipts Taxes in accordance with the terms of the Series 2006 Loan Agreement, the Special Escrow Agreement and the Collecting Agent Agreement.

Affirmative Covenants of the Authority. If the Authority shall pay or cause to be paid, or there shall otherwise be deemed to be paid to the Owners of all the Authority's Bonds the principal, Redemption Price, if applicable, or purchase price of, and interest due or to become due thereon and such other amounts as are set forth therein, at the times and in the manner stipulated in the Bonds and in the Indenture, and the Trustee and Paying Agent shall pay over or deliver to the Authority all moneys or securities held by them upon defeasance pursuant to the Indenture, then the Authority shall credit ratably (or otherwise as directed in writing by the Government) against amounts due under the Series 2006 Loan Note any moneys and securities thereupon remaining and held under the Indenture, including amounts, if any, on deposit in the Debt Service Reserve Account created under the Indenture, and transfer such remaining money and securities to, at the direction of, or on behalf of the Government.

The Authority shall use its best efforts to cause the Government to comply with the covenants set forth in the Series 2006 Loan Agreement.

Event of Default. The occurrence of any of the following events shall be an “Event of Default” under the Series 2006 Loan Agreement:

(a) The Government shall fail to pay when due any amount payable on the Series 2006 Loan Note; or

(b) The Government shall fail to deposit or cause to be deposited into the Special Escrow Account, within one Business Day after the date required under the Special Escrow Agreement, any Gross Receipts Taxes collected by the Government or, in the event such failure is caused by reason of *“force majeure”* (as defined in the Series 2006 Loan Agreement), on the first Business Day on which, in the reasonable judgment of the Government, the condition which gave rise to such force majeure no longer prevents the Government from making such deposit. The determination of whether a failure to make a deposit of Gross Receipts Taxes as required by the Special Escrow Agreement is due to *force majeure* shall be made in the reasonable judgment of the Government, upon telephonic written notice to the Trustee, if possible; or

(c) The Government shall fail to perform or observe any term, covenant or agreement contained in the Series 2006 Loan Agreement, the Special Escrow Agreement or the Collecting Agent Agreement (other than the covenant referred to in paragraph (b) above) on its part to be performed or observed and any such failure shall remain unremedied for thirty (30) days after written notice thereof shall have been given to the Government by the Authority or the Trustee, provided, however, that if said default be such that it cannot be corrected within the applicable period, it shall not constitute an Event of Default if corrective action is instituted by the Government within the applicable period and diligently pursued until the default is corrected; or

(d) An "Event of Default" under the Indenture; or

(e) Failure by the Authority to pay when due any Series 2006 Swap Agreement Net Payment or Series 2006 Swap Agreement Termination Payment.

Rights on Default. If an Event of Default shall happen and shall not have been remedied, then, and in every such case, the holder of the Series 2006 Loan Note may (i) sue to collect sums due under such Series 2006 Loan Note, (ii) compel to the extent permitted by law, by mandamus or otherwise, the performance by the Government of any covenant made in the Series 2006 Loan Agreement or the Series 2006 Loan Note, and (iii) examine the books and records of the Government to account for all moneys and securities constituting the Gross Receipts Taxes and all other revenues of the Government.

Continuing Obligation. Until the date on which all amounts due and owing to the Authority from the Government pursuant to the Series 2006 Loan Note shall have been paid in full or otherwise provided for, the Series 2006 Loan Agreement is a continuing obligation of the Government and shall (i) be binding upon the Government, its successors and assigns and (ii) inure to the benefit of and be enforceable by the Authority and the Trustee and their respective successors, transferees and assigns.

Amendments, Changes and Modifications. The Government and the Authority, with the consent of the Trustee, may cause to be executed an amendment or supplement to the Series 2006 Loan Agreement curing any ambiguity or curing, correcting or supplementing any defect or inconsistent provision contained in the Series 2006 Loan Agreement or making such provisions in regard to matters or questions arising in the Series 2006 Loan Agreement as may be necessary or desirable and as shall not materially adversely affect the interests of the holder of the Series 2006 Loan Note. Such amendment or supplement shall become effective upon the filing with the Government an instrument of the Trustee approving such supplement. In addition, the Government and the Authority may cause to be executed an amendment or supplement to the Series 2006 Loan Agreement at any time and from time to time modifying any provision of the Series 2006 Loan Agreement with the consent of the Trustee, except as provided in the Indenture.

APPENDIX D

AUDITED FINANCIAL STATEMENTS OF THE GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS FOR FISCAL YEARS 2004, 2003 AND 2002

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Basic Financial Statements

September 30, 2004

(With Independent Auditors' Report Thereon)

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KPMG LLP
American International Plaza
Suite 1100
250 Muñoz Rivera Avenue
San Juan, PR 00918-1819

Independent Auditors' Report

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

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government) as of and for the year ended September 30, 2004, which collectively comprise the Government's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Government's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following component units:

- The Virgin Islands Public Finance Authority (PFA), a blended component unit, which represents 100% of the assets, fund balance, and revenue of the PFA Debt Service Fund (a major fund); 100% of the assets, net assets, and revenue of the PFA Capital Projects Fund (a major fund); 100% of the assets, net assets, and revenue of the West Indian Company (a major fund); 1.17%, 1.29%, and 1.96% of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information; 25.2%, 87.6%, and 17.6% of the assets, net assets, and revenue of the governmental activities; and 59.65%, 49.56%, and 35.34% of the assets, net assets, and revenue of the business-type activities, respectively.
- Virgin Islands Lottery (VI Lottery), a nonmajor enterprise fund, which represents 0.06%, 0.48%, and 2.06%, respectively, of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information, and 1.14%, 11.26%, and 21.21%, respectively, of the assets, net assets, and revenue of the business-type activities.
- The Tobacco Settlement Financing Corporation, a blended component unit, which represents 0.73%, 1.09%, and 0.28%, respectively, of the assets, fund balance, and revenue of the aggregate remaining fund information, and 0.91%, 4.10%, and 0.14%, respectively, of the assets, net assets, and revenue of the governmental activities.
- The Virgin Islands Port Authority, Virgin Islands Water and Power Authority, Virgin Islands Housing Authority (VIHA), University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Economic Development Authority (VIEDA), Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA), discretely presented component units, which collectively represent 100% of the assets, net assets, and revenue of the aggregate discretely presented component units.

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

Except as discussed in the following eight paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Government's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

The basic financial statements include a receivable for corporate income taxes in the general fund (a major fund) and the governmental activities of $8.7 million as of September 30, 2004. The basic financial statements of September 30, 2003 did not include a receivable for corporate income taxes pertaining to tax year 2002 in the general fund (a major fund) and the governmental activities due to inadequate records. The receivable for corporate income taxes at September 30, 2003, enters into the determination of revenue and change in fund balance/net assets for the year ended September 30, 2004. The Government's records do not permit, nor is it practicable to extend our auditing procedures sufficiently to determine the extent to which the revenue and change in fund balance/net assets of the general fund (a major fund) and the governmental activities for the year ended September 30, 2004 may have been affected by this condition.

The report of the other auditors on the financial statements of VIHA, a discretely presented component unit, as of and for the year ended December 31, 2003, was qualified because they were unable to obtain sufficient audit evidence to determine whether capital assets amounting to $67 million were fairly stated.

The report of the other auditors on the 2004 financial statements of VIHFA, a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether land held for sale amounting to approximately $25.7 million was fairly stated.

The basic financial statements include a receivable for unemployment insurance contributions in the unemployment insurance fund (a major fund) and the business-type activities of $1.1 million as of September 30, 2004. The basic financial statements of September 30, 2003 did not include a receivable for unemployment insurance contributions in the unemployment insurance fund (a major fund) and the business-type activities due to inadequate records. The receivable for unemployment insurance contributions at September 30, 2003, enters into the determination of revenue, change in net assets, and, where applicable, cash flows for the year ended September 30, 2004. The Government's records do not permit, nor is it practicable to extend our auditing procedures sufficiently to determine the extent to which the revenue, change in net assets, and, where applicable, cash flows of the unemployment insurance fund (a major fund) and the business-type activities for the year ended September 30, 2004 may have been affected by this condition.

The report of the other auditors on the 2004 financial statements of the VI Lottery, a nonmajor enterprise fund, was qualified because they were unable to obtain sufficient audit evidence to determine whether capital assets of $45 thousand, net accounts receivables of $887 thousand, due to the general fund of $4.5 million, and other liabilities of $115 thousand were fairly stated.

The basic financial statements do not include a liability for workers' compensation claims. The Government's records do not permit, nor is it practical to extend our auditing procedures sufficiently to determine the extent by which the business-type activities as of and for the year ended September 30, 2004 may have been affected by this condition.

The Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), is recording contributions pursuant to the Early Retirement Act of 1994 as the cash is received which, in our opinion, should be accrued in order to conform with U.S. generally accepted accounting principles. If these contributions were accrued, contributions receivable and net assets held in trust for employees' pension benefits would be increased by $7.2 million and the change in net assets would be increased by $1.1 million. In addition, GERS maintains its real estate investment in the GERS complex related to the portion of the St. Thomas building held for lease based on historical cost. As of September 30, 2004, this real estate investment amounted to approximately $8.6 million. Such investment should be presented at fair value in accordance with U.S. generally accepted accounting principles. GERS has not performed a recent valuation of this real estate investment. Finally, we were unable to obtain sufficient audit evidence about the cash overdraft balance reported by GERS with the Department of Finance of approximately $10.5 million in specially designated pooled accounts.

The basic financial statements include a provision for landfill closure and postclosure costs as required by U.S. generally accepted accounting principles in the governmental activities of $28.8 million as of September 30, 2004. The basic financial statements of September 30, 2003 did not include a provision for landfill closure and postclosure costs in the governmental activities because no calculation had been made. The provision for landfill closure and postclosure costs at September 30, 2003, enters into the determination of expenses and change in net assets for the year ended September 30, 2004. The Government's records do not permit, nor is it practicable to extend our auditing procedures sufficiently to determine the extent to which the expenses and change in net assets of the governmental activities for the year ended September 30, 2004 may have been affected by this condition.

Because of the matters discussed in the sixth, seventh, and eighth paragraphs of this report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the business-type activities as of September 30, 2004 and the changes in financial position for the year then ended.

In our opinion, based on our audit and the report of other auditors, except for:

- the effects of not being able to determine the extent to which the expenses and change in net assets of the governmental activities may have been affected by the exclusion of a provision for landfill closure and postclosure costs in the beginning net assets, as described in paragraph ten above, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities of the Government as of September 30, 2004 and the changes in financial position thereof for the year then ended in conformity with U.S. generally accepted accounting principles;

- the effects of not being able to determine the extent to which the revenue and change in fund balance/net assets of the general fund (a major fund) and the governmental activities may have been affected by the exclusion of a receivable for corporate income taxes pertaining to tax year 2002 in the beginning fund balance/net assets due to inadequate records, as described in paragraph three above, the financial statements referred to above present fairly, in all material respects, the financial position of the general fund and the governmental activities of the Government as of September 30, 2004 and the changes in financial position thereof for the year then ended in conformity with U.S. generally accepted accounting principles;

- the effects of not being able to determine the extent to which the revenue, change in net assets, and cash flows of the unemployment insurance fund (a major fund) may have been affected by the exclusion of a receivable for unemployment insurance contributions in the beginning net assets due to inadequate records, as described in paragraph six above, the financial statements referred to above present fairly, in all material respects, the financial position of the unemployment insurance fund of the Government as of September 30, 2004, and the changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with U.S. generally accepted accounting principles;
- the effects of the adjustments as might have been determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether capital assets and land held for sale amounting to $67 million and $26 million in the financial statements of VIHA and VIHFA, respectively, were fairly stated, as described in paragraphs four and five above, the financial statements referred to above present fairly, in all material respects, the financial position of the discretely presented component units of the Government of the United States Virgin Islands as of September 30, 2004, and the respective changes in financial position thereof for the year then ended in conformity with U.S. generally accepted accounting principles; and
- the effects of (i) GERS not accruing contributions pursuant to the Early Retirement Act of 1994 and not recording its real estate investment in the GERS complex related to the portion of the St. Thomas building held for lease at fair value, and (ii) the adjustments as might have been determined to be necessary, had we been able to obtain satisfactory evidence with respect to the cash overdraft of GERS with the Department of Finance, as described in paragraph nine above, the financial statements referred to above present fairly, in all material respects, the financial position of the aggregate remaining fund information of the Government of the United States Virgin Islands, as of September 30, 2004, and the respective changes in financial position thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

Finally, in our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the PFA Debt Service Fund, PFA Capital Projects Fund, and the West Indian Company of the Government of the United States Virgin Islands as of September 30, 2004, and the respective changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for the general fund for the year then ended in conformity with U.S. generally accepted accounting principles.

As discussed in note 14 to the basic financial statements, the Government has restated beginning net assets and fund balances.

(Continued)

The management's discussion and analysis on pages 6 through 15 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

June 7, 2006

Stamp No. 2102947 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

Introduction

The following discussion and analysis presents an overview of the financial position and activities of the Government of the United States Virgin Islands (the Government) as of and for the fiscal years ended September 30, 2004 and 2003.

Government-wide Financial Statements

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

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

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

Governmental Activities – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with the primary government (PG) fall into this category, including general government, public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.

Business-Type Activities – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Government include the operations of the (i) unemployment insurance program and (ii) the West Indian Company (WICO). Both of these programs operate with minimal assistance from the governmental activities of the Government.

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

Fund Financial Statements

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

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

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

Governmental Funds

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

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

The PFA Debt Service accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by the Virgin Islands Public Finance Authority (PFA) on behalf of the Government.

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

Proprietary Funds

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

The unemployment insurance fund and the West Indian Company (WICO) fund are major proprietary funds.

The unemployment insurance fund is a federally mandated program to manage unemployment insurance.

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

Fiduciary Funds

The Government is the trustee, or fiduciary, for several agency funds.

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

Financial Analysis of the Government as a Whole

The primary government (PG) and its component units experienced an economic downturn following the slowdown of the U.S. economy in fiscal year 2002 and the events of September 11, 2001. As explained in note 13 to the basic financial statements, the Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, the development of a series of detailed revenue enhancement and expenditure reduction initiatives, and the enactment of certain laws directed toward improving the Government's financial situation.

In fiscal year 2004, the Government issued the 2003A Series Revenue Bonds amounting to S268 million to repay the bond anticipation note and to fund necessary capital projects of the PG.

Financial Analysis of the Primary Government

Total assets of the government as of September 30, 2004 and 2003 were $1.564 billion and $1.337 billion, respectively, an increase of approximately $227 million. Total liabilities as of September 30, 2004 and 2003 were $1.836 billion and $1.637 billion, respectively, an increase of approximately $199 million.

For the year ended September 30, 2004, the PG net deficit of $272 million consisted of $239 million invested in capital assets, net of related debt; $173 million restricted by statute or other legal requirements that were not available to finance day to day operations of the government; and an unrestricted net deficit of $684 million. For the year ended September 30, 2003, the PG net asset deficit of $300 million consisted of $245 million invested in capital assets, net of related debt; $148 million restricted by statute or other legal requirements and were not available to finance day to day operations of the government; and an unrestricted net deficit of $693 million.

For the fiscal year ended September 30, 2004, the PG earned program and general revenue amounting to $977 million, and reported expenses of $946 million, resulting in a decrease in the net deficit, before transfers, of $31 million. For the fiscal year ended September 30, 2003, the PG earned program and general revenue amounting to $854 million, and reported expenses of $888 million, resulting in an increase in the net deficit, before a special item and transfers, of $34 million. During fiscal year 2003, the Government reported a special item of $159 million resulting from the forgiveness of the 1996 Community Disaster Loan (CDL) resulting in an overall reduction in the net deficit of $125 million.

In overall, revenue demonstrated an increase of approximately $123 million in fiscal year 2004, when compared to fiscal year 2003. Expenses increased in fiscal year 2004 when compared to fiscal year 2003 by $58 million, including $29 million in landfill closure and postclosure care cost recognized in fiscal year 2004. A summary of net assets (deficit) and changes in net assets (deficit) for the primary government follows:

Net Assets (Deficit) – Primary Government

September 30, 2004 and 2003

(In thousands)

	Governmental activities		Business-type activities		Total	
	2004	2003	2004	2003 (a)	2004	2003 (a)
Assets						
Current assets	$ 836,161	626,829	43,833	54,979	879,994	681,808
Capital assets	625,530	608,158	42,693	43,008	668,223	651,166
Other assets	15,421	3,211	437	553	15,858	3,764
Total assets	1,477,112	1,238,198	86,963	98,540	1,564,075	1,336,738
Liabilities						
Long-term debt outstanding	1,061,655	913,925	21,376	22,015	1,083,031	935,940
Other liabilities	743,737	693,964	9,610	6,917	753,347	700,881
Total liabilities	1,805,392	1,607,889	30,986	28,932	1,836,378	1,636,821
Net Assets						
Invested in capital assets, net of related debt	217,677	224,189	21,318	20,993	238,995	245,182
Restricted	131,496	105,633	41,375	42,464	172,871	148,097
Unrestricted (deficit)	(677,453)	(699,513)	(6,716)	6,151	(684,169)	(693,362)
Total net assets (deficit)	S (328,280)	(369,691)	55,977	69,608	(272,303)	(300,083)

(a) The 2003 balances were not restated to reflect the restatements that were made to the beginning net asset balances because the 2003 information is not readily available.

Changes in Net Assets (Deficit) – Primary Government

September 30, 2004 and 2003

(In thousands)

	Governmental activities		Business-type activities		Total	
	2004	2003	2004	2003 (a)	2004	2003 (a)
Revenue:						
Program revenue:						
Charges for services	$ 28,932	26,988	41,294	29,590	70,226	56,578
Operating grants and contributions	151,118	143,295	—	—	151,118	143,295
Capital grants and contributions	9,553	20,564	—	—	9,553	20,564
General revenue:						
Taxes	664,510	594,616	—	—	664,510	594,616
Interest and other	77,848	33,991	2,749	3,785	80,597	37,776
Other general revenue	1,102	1,577	—	—	1,102	1,577
Total revenue	933,063	821,031	44,043	33,375	977,106	854,406
Expenses:						
General government	381,282	350,600	—	—	381,282	350,600
Public safety	55,677	49,394	—	—	55,677	49,394
Health	92,694	97,243	—	—	92,694	97,243
Public housing and welfare	62,712	63,874	—	—	62,712	63,874
Education	186,122	186,293	—	—	186,122	186,293
Transportation and communication	45,987	29,240	—	—	45,987	29,240
Culture and recreation	7,549	14,365	—	—	7,549	14,365
Interest on long-term debt	60,024	49,633	—	—	60,024	49,633
Unemployment insurance	—	—	7,117	19,664	7,117	19,664
West Indian Company	—	—	9,926	8,432	9,926	8,432
Workmen's Compensation	—	—	8,431	8,922	8,431	8,922
VI Lottery	—	—	11,663	—	11,663	—
Other business-type activities	—	—	17,004	10,521	17,004	10,521
Total expenses	892,047	840,642	54,141	47,539	946,188	888,181
Increase (decrease) in net assets before special item and transfers	41,016	(19,611)	(10,098)	(14,164)	30,918	(33,775)
Special item	—	159,271	—	—	—	159,271
Transfers	395	(1,379)	(395)	1,379	—	—
	395	157,892	(395)	1,379	—	159,271
Change in net assets	41,411	138,281	(10,493)	(12,785)	30,918	125,496
Net assets (deficit), beginning of year, as previously reported	(369,691)	(508,798)	69,608	77,212	(300,083)	(431,586)
Restatements to beginning net assets	—	826	(3,138)	5,181	(3,138)	6,007
Net assets (deficit), end of year, as restated	$ (328,280)	(369,691)	55,977	69,608	(272,303)	(300,083)

(a) The 2003 balances were not restated to reflect the restatements that were made to the beginning net asset balances because the 2003 information is not readily available.

The Virgin Islands Office of Management and Budget of the PG prepares an annual executive budget subject to approval by the Governor and the Legislature of the Virgin Islands. The executive budget is prepared on a budgetary basis similar to the cash basis of accounting. The executive budget includes only those funds that are subject to appropriation by law. More information regarding budgetary procedures is provided in note 3 of the basic financial statements. A summary of the budgetary report for the General Fund of the PG, included on page 23 of the financial statements, follows:

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

Year ended September 30, 2004

(In thousands)

	Original budget	Amended budget	Actual	Variance
Total revenue	$ 526,849	526,849	478,387	(48,462)
Total expenditures	566,282	596,545	531,007	65,538
Excess of expenditures over revenue	(39,433)	(69,696)	(52,620)	17,076
Other financing sources (uses)	70,968	70,968	81,709	10,741
Excess of revenue and other financing sources (uses) over expenditures	$ 31,535	1,272	29,089	27,817

For fiscal year 2004, the PG realized a revenue variance $(48) million due to a slower-than-expected recovery following the 2002 recession. The PG realized a $66 million variance in expenditures due to control spending imposed by revenue shortfalls. The PG realized a $11 million variance in other financing sources due to the fact that transfers to the General Fund were higher than budgetary estimates.

Capital Assets

Capital assets additions during fiscal years 2004 and 2003 amounted to $36 million and $34 million, respectively, for governmental activities and $1.6 million and $7.5 million, respectively, for business-type activities.

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

Capital Assets – Primary Government

(In thousands)

	Governmental activities		Business-type activities		Total	
	2004	2003	2004	2003 (a)	2004	2003 (a)
Land and improvements	$ 188,523	188,109	5,357	5,358	193,880	193,467
Building and improvements	402,450	400,309	47,575	46,490	450,025	446,799
Machinery and equipment	78,159	69,788	3,791	2,585	81,950	72,373
Infrastructure	126,249	121,413	—	—	126,249	121,413
Construction in progress	24,578	4,046	809	722	25,387	4,768
Total assets	819,959	783,665	57,532	55,155	877,491	838,820
Less accumulated depreciation	(194,429)	(175,507)	(14,839)	(12,147)	(209,268)	(187,654)
Total capital assets	$ 625,530	608,158	42,693	43,008	668,223	651,166

(a) The 2003 balances were not adjusted to reflect the restatements that were made to the beginning net asset balances because the 2003 information is not readily available.

Debt Administration

The Government issues both general obligation bonds and revenue bonds. The Revised Organic Act [48 U.S.C. Section 1574 (b)(ii)] restricts the principal amount of general obligation debt that the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the U.S. Virgin Islands. Following is a summary of bonds outstanding as of September 30, 2004:

Primary Government – Bonds Payable

(In thousands)

Bonds payable	Final maturity	Interest rates (%)	Balance
1998 Series A, C, D, and E Revenue and Refunding Bonds	2023	5.50 to 7.11	$ 473,745
1999 Project Revenue Bonds	2005	6.25	1,550
1999 Series A General Obligation Bonds	2010	6.50	5,650
1999 Series A Revenue Bonds	2033	4.20 to 6.40	283,335
2001 Series A Tobacco Bonds	2031	5.00	22,310
2002 Series Garvee Bonds	2009	2.50 to 5.00	15,840
2003 Series A Revenue Bonds	2033	4.00 to 5.25	268,020
Subtotal			1,070,450
Deferred amount on refundings			(2,464)
Bond premium			3,819
Bond discount			(9,052)
Bond accretion			(1,098)
Total			$ 1,061,655

Note 9 provides detailed information regarding all bonds of the U.S. Virgin Islands.

During fiscal year 2004, the 2003 Series A revenue bonds amounting to $268 million were issued.

The PG made bond principal payments on all outstanding general and special revenue bonds amounting to $25 million during fiscal year 2004, and $24 million during fiscal year 2003.

The Government's bonds carry insured ratings of "AAA" and "Aaa" from Fitch Ratings and Moody's Investors Services, respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained from the respective rating agency.

Other liabilities of the PG include:

Primary Government – Other Liabilities
September 30, 2004 and 2003
(In millions)

		2004	2003
Accrued compensated absences	$	60	52
Retroactive union arbitration liability		384	375
Accrued litigation		15	13
Landfill closure and post closure costs		29	—
Accrued federal cost disallowances		6	13
Total other liabilities	$	494	453

Economic Condition and Outlook

The PG ended fiscal year 2004 with a deficit amounting to $272 million, of which $684 million relates to an unrestricted deficit. The PG is working towards a recovery from the recession of 2002 through a combination of revenue initiatives and budgetary restraint on expenditures.

Revenue Initiatives

The PG collects income tax revenue under the "mirror" income tax system. The Government's tax laws mirror the U.S. Internal Revenue Service (IRS) Code, Rules, and Regulations. The 2003 and 2004 Tax Acts passed by U.S. Congress may have a negative impact on revenue due to changes in sourcing of revenue rules as defined for the U.S. Virgin Islands, restrictions on residency rules, a decrease in tax rates, expanded tax credits, and expanded tax deductions. In April 2005, the U.S. Treasury issued draft tax regulations for the territories and possessions defining residency and source of income. The Government has proactively responded to these changes through meetings with the U.S. Treasury. The regulations have not been issued and the Government's response is under review by the U.S. Treasury.

In connection with a real property tax case instituted against the PG in the U.S. District Court of the Virgin Islands, the Government was enjoined for a four-month period in fiscal year 2003 from appraising and assessing any real property taxes until it modified its system of appraisal to comply with certain court mandates. As a result, effective August 2003, it has been using the 1998 assessment value to issue tax bills and collect taxes, and expects to continue to do so until a new appraisal system is implemented, which is intended to satisfy the court's decision, or the decision is reversed on appeal. In fiscal year 2004, the Government retained a consultant to modify its system of appraisal and to comply with the court mandates.

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

(Continued)

Budgetary Control of Expenditures

The PG faces the challenge of carryforward expenditures from prior fiscal years and increasing expenditures in the current fiscal year. Carryforward expenditures consist mainly of retroactive salary increases, which accumulated following Hurricanes Hugo, Marilyn, and Bertha in the years of 1990 through 1998.

Current increasing governmental expenditures include increased health insurance premiums, pharmaceutical premiums, and salary expense. Expenditures are closely monitored and controlled through the budgetary process.

Deficit Reduction Measures

The PG has implemented a number of deficit reducing measures including: (i) increasing of local taxes including the highway users tax and stamp tax; (ii) implementation of new local taxes including an excise tax on importation of personal goods and a petroleum tax; and (iii) exerting greater control of expenditures through the budgetary process, and (iv) implementation of tax amnesties for property and gross receipts taxes.

Contacting the Government's Financial Management

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

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit)

September 30, 2004

(In thousands)

		Primary Government			
		Governmental activities	Business-type activities	Total	Component units
Assets:					
Cash and cash equivalents	$	247,100	8,004	255,104	58,153
Investments		349,120	—	349,120	29,388
Receivables, net		179,632	3,352	182,984	54,210
Internal balances		6,999	(6,999)	—	—
Loans and advances		—	—	—	1,622
Due from component units		29,382	—	29,382	—
Note receivable		—	—	—	7,486
Due from primary government		—	—	—	3,531
Due from federal government		22,963	—	22,963	4,204
Inventories		—	435	435	20,866
Other assets		965	843	1,808	18,856
Restricted:					
Cash and cash equivalents		—	38,198	38,198	34,544
Investments		—	—	—	91,794
Other		—	—	—	1,188
Capital assets		625,530	42,693	668,223	764,325
Deferred expenses		15,421	437	15,858	21,167
Total assets		1,477,112	86,963	1,564,075	1,111,334
Liabilities:					
Current liabilities:					
Accounts payable and accrued liabilities		52,003	5,637	57,640	73,605
Tax refunds payable		75,352	—	75,352	—
Unemployment insurance benefits		—	1,744	1,744	—
Customer deposits		—	—	—	16,710
Due to primary government		—	—	—	29,382
Due to component units		3,531	—	3,531	—
Due to federal government		—	—	—	5,690
Interest payable		29,133	—	29,133	5,281
Unearned revenue		87,250	—	87,250	4,545
Other current liabilities		1,990	2,229	4,219	6,619
Due within one year:					
Loans payable		—	813	813	8,298
Bonds payable		22,467	—	22,467	8,476
Other liabilities		39,663	—	39,663	—
Noncurrent liabilities:					
Due in more than one year:					
Loans payable		—	20,563	20,563	2,583
Bonds payable		1,039,188	—	1,039,188	277,923
Other liabilities		454,815	—	454,815	28,708
Total liabilities	$	1,805,392	30,986	1,836,378	467,820

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit), continued

September 30, 2004

(In thousands)

		Primary Government			
		Governmental activities	Business-type activities	Total	Component units
Net assets:					
Invested in capital assets, net of related debt	$	217,677	21,318	238,995	538,835
Restricted for:					
Unemployment insurance		—	33,840	33,840	—
Debt service		131,496	—	131,496	—
Other purposes		—	7,535	7,535	71,790
Unrestricted (deficit)		(677,453)	(6,716)	(684,169)	32,889
Total net assets (deficit)	$	(328,280)	55,977	(272,303)	643,514

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities

Year ended September 30, 2004

(In thousands)

	Expenses	Program revenue: Charges for services	Program revenue: Operating grants and contributions	Program revenue: Capital grants and contributions	Net revenue (expense) and changes in net assets – Primary government: Governmental activities	Net revenue (expense) and changes in net assets – Primary government: Business-type activities	Net revenue (expense) and changes in net assets – Primary government: Total	Component units
Functions:								
Primary government:								
Governmental activities:								
General government	$ 381,282	24,853	36,729	4,982	(314,718)	—	(314,718)	—
Public safety	55,677	1,296	16,833	—	(37,548)	—	(37,548)	—
Health	92,694	416	29,065	—	(63,213)	—	(63,213)	—
Public housing and welfare	62,712	409	36,510	—	(25,793)	—	(25,793)	—
Education	186,122	—	31,481	—	(154,641)	—	(154,641)	—
Transportation and communication	45,987	1,947	350	4,571	(39,119)	—	(39,119)	—
Culture and recreation	7,549	11	150	—	(7,388)	—	(7,388)	—
Interest on long-term debt	60,024	—	—	—	(60,024)	—	(60,024)	—
Total governmental activities	892,047	28,932	151,118	9,553	(702,444)	—	(702,444)	—
Business-type activities:								
Unemployment insurance	7,117	3,771	—	—	—	(3,346)	(3,346)	—
West Indian Company	9,926	12,381	—	—	—	2,455	2,455	—
Workmen's compensation	8,431	7,169	—	—	—	(1,262)	(1,262)	—
VI Lottery	11,663	9,390				(2,273)	(2,273)	
Other	17,004	8,583	—	—	—	(8,421)	(8,421)	—
Total business-type activities	54,141	41,294	—	—	—	(12,847)	(12,847)	—
Total primary government	$ 946,188	70,226	151,118	9,553	(702,444)	(12,847)	(715,291)	—
Component units:								
Virgin Islands Housing Authority	$ 44,206	5,121	30,766	5,437	—	—	—	(2,882)
Virgin Islands Port Authority	41,910	36,651	—	10,037	—	—	—	4,778
Virgin Islands Water and Power Authority:								
Electric system	146,378	144,745	—	820	—	—	—	(813)
Water system	21,637	25,406	—	1,088	—	—	—	4,857
Virgin Islands Government Hospital and Health Facilities Corporation:								
Roy L. Schneider Hospital	66,171	40,235	21,778	4,541	—	—	—	383
Juan F. Luis Hospital	50,843	24,867	18,249	1,631	—	—	—	(6,096)
University of the Virgin Islands	59,484	13,607	45,476	3,192	—	—	—	2,791
Other component units	12,028	2,695	6,370	1,711	—	—	—	(1,252)
Total component units	$ 442,657	293,327	122,639	28,457	—	—	—	1,766

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities, continued

Year ended September 30, 2004

(In thousands)

	Net revenue (expense) and changes in net assets – Primary government: Governmental activities	Net revenue (expense) and changes in net assets – Primary government: Business-type activities	Net revenue (expense) and changes in net assets – Primary government: Total	Component units
Total primary government and component units	$ (702,444)	(12,847)	(715,291)	1,766
General revenue:				
Taxes	664,510	—	664,510	—
Interest and other	77,848	2,749	80,597	9,425
Tobacco settlement rights	1,102	—	1,102	—
Transfers – internal activities of primary government	395	(395)	—	—
Total general revenue and transfers	743,855	2,354	746,209	9,425
Changes in net assets (deficit)	41,411	(10,493)	30,918	11,191
Net assets (deficit), beginning of year (as restated)	(369,691)	66,470	(303,221)	632,323
Net assets (deficit), end of year	$ (328,280)	55,977	(272,303)	643,514

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Balance Sheet – Governmental Funds

September 30, 2004

(In thousands)

Assets		General	PFA debt service	PFA capital projects	Other governmental	Total governmental
Cash and cash equivalents	$	136,279	—	46,135	64,686	247,100
Investments		72,888	150,285	112,729	13,218	349,120
Receivables:						
Taxes		140,553	38,253	—	—	178,806
Accrued interest and other		390		—	541	931
Due from:						
Other funds		8,846	—	313	10,794	19,953
Component units		29,382	—	—	—	29,382
Federal government		—	—	—	22,963	22,963
Other assets		—	—	—	34	34
Total assets	$	388,338	188,538	159,177	112,236	848,289
Liabilities and Fund Balances						
Accounts payable and accrued liabilities	$	33,893	—	346	17,764	52,003
Tax refunds payable		75,352	—	—	—	75,352
Due to:						
Other funds		7,654	2,000	158	3,178	12,990
Component units		3,531	—	—	—	3,531
Deferred revenue		140,193	72,939	6,639	18,976	238,747
Other current liabilities		—	—	—	1,954	1,954
Total liabilities		260,623	74,939	7,143	41,872	384,577
Fund balances reserved for:						
Encumbrances		48,340	—	—	—	48,340
Debt service		—	113,599	—	17,898	131,497
Unreserved fund balance, reported in:						
General fund		79,375	—	—	—	79,375
Special revenue funds		—	—	—	55,925	55,925
Capital projects funds		—	—	152,034	(3,459)	148,575
Total fund balances		127,715	113,599	152,034	70,364	463,712
Total liabilities and fund balances	$	388,338	188,538	159,177	112,236	

Amounts reported for governmental activities in the statement of net assets (deficit) are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.		625,530
Bond issue costs are not financial resources and, therefore, are not reported in the funds.		15,421
Because the focus of governmental funds is on short-term financing, some assets, primarily taxes receivable, will not be available to pay for current period expenditures. Those assets are offset by deferred revenue in the funds.		152,323
Interest on long-term debt is not accrued in the funds, but rather is recognized as an expenditure when due.		(29,133)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.		(1,556,133)
Deficit of governmental activities	$	(328,280)

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenditures, and Changes in Fund Balances
Governmental Funds

Year ended September 30, 2004

(In thousands)

		General	PFA debt service	PFA capital projects	Other governmental	Total governmental
Revenue:						
Taxes	$	459,809	152,449	—	18,248	630,506
Federal grants and contributions		—	3,651	—	157,020	160,671
Charges for services		21,424	—	—	7,508	28,932
Tobacco settlement rights		—	—	—	1,102	1,102
Interest and other		42,514	5,143	2,608	27,583	77,848
Total revenue		523,747	161,243	2,608	211,461	899,059
Expenditures:						
Current:						
General government		246,658	—	2,702	87,717	337,077
Public safety		40,954	—	—	13,152	54,106
Health		70,808	—	—	18,514	89,322
Public housing and welfare		31,231	—	426	31,055	62,712
Education		149,077	—	—	31,300	180,377
Transportation and communication		29,950	—	6,562	4,939	41,451
Culture and recreation		6,203	—	—	1,076	7,279
Capital outlays		—	—	22,461	14,089	36,550
Debt service:						
Principal		—	120,570	—	4,125	124,695
Interest		—	50,155	—	1,365	51,520
Bond issuance costs		—	13,033	—	—	13,033
Total expenditures		574,881	183,758	32,151	207,332	998,122
Excess (deficiency) of revenue over (under) expenditures		(51,134)	(22,515)	(29,543)	4,129	(99,063)
Other financing sources (uses):						
Bonds issued		—	126,520	141,500	—	268,020
Transfers from other funds		87,302	—	1,015	15,314	103,631
Transfers to other funds		(5,593)	(85,562)	(4,000)	(8,081)	(103,236)
Premium on bonds issued		—	2,830		—	2,830
Total other financing sources (uses), net		81,709	43,788	138,515	7,233	271,245
Net change in fund balances		30,575	21,273	108,972	11,362	172,182
Fund balance, beginning of year (as restated)		97,140	92,326	43,062	59,002	291,530
Fund balance, end of year	$	127,715	113,599	152,034	70,364	463,712

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2004

(In thousands)

Net change in fund balances – total governmental funds	$	172,182
Government funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		17,372
Tax revenue in the statement of activities, which do not provide current financial resources, are not reported as revenue in the funds.		34,004
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of the governmental funds. These transactions have no effect on net assets. This is the amount by which bond and loan proceeds of $268,020 exceeded principal retirement of $124,695 in the current period.		(143,325)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. This is the amount by which the increase in certain liabilities reported in the statement of net assets of the previous year increased expenses reported in the statement of activities that do not require the use of current financial resources.		(40,521)
Bond issue costs are expended in the governmental funds when paid, and are capitalized and amortized in the statement of activities. This is the amount by which current year bond issue costs exceeded amortization expense in the current period.		12,210
Bond premiums and discounts are reported as other financing sources and uses in the governmental funds when the bonds are issued, and are capitalized and amortized in the government-wide financial statements. This amount represents the capitalization of premiums on bonds issued during the current year of $2,830 and the additional net interest expense of $1,575 reported in the statement of activities related to the amortization of premiums, discounts deferred refunding loss, and accreted interest on capital appreciation bonds during the current year.		(4,405)
Certain interest reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This amount represents the increase in interest payable reported in the statement of net assets less the portion of accrued interest.		(6,106)
Change in net assets of governmental activities	$	41,411

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2004

(In thousands)

		Original budget	Amended budget	Actual	Variance
Revenue:					
Taxes	$	493,048	493,048	436,422	(56,626)
Charges for services		10,259	10,259	15,055	4,796
Interest and other		23,542	23,542	26,910	3,368
Total revenue		526,849	526,849	478,387	(48,462)
Expenditures:					
Current:					
General government		123,578	136,318	211,439	(75,121)
Public safety		62,242	64,895	40,446	24,449
Health		84,539	87,812	65,030	22,782
Public housing and welfare		43,046	41,771	31,846	9,925
Education		190,192	197,675	145,723	51,952
Transportation and communication		43,924	48,928	27,402	21,526
Culture and recreation		18,761	19,146	9,121	10,025
Total expenditures		566,282	596,545	531,007	65,538
Excess of expenditures over revenue		(39,433)	(69,696)	(52,620)	17,076
Other financing sources (uses):					
Transfers from other funds		78,043	78,043	87,302	9,259
Transfer to other funds		(7,075)	(7,075)	(5,593)	1,482
Total other financing sources (uses), net		70,968	70,968	81,709	10,741
Excess of revenue and other financing sources over expenditures	$	31,535	1,272	29,089	27,817

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets – Proprietary Funds

September 30, 2004

(In thousands)

		Business-type activities – Enterprise funds			
		Unemployment insurance	West Indian Company	Other	Totals
Assets:					
Current assets:					
Cash and cash equivalents	$	244	5,450	2,310	8,004
Receivables, net:					
Premiums receivable		1,136	—	—	1,136
Accrued interest and other			1,091	60	1,151
Other receivables		—	—	1,065	1,065
Due from other funds		—	—	300	300
Inventories and other current assets		—	—	435	435
Other assets		—	783	60	843
Total current assets		1,380	7,324	4,230	12,934
Noncurrent assets:					
Restricted cash and cash equivalents		36,433	1,765	—	38,198
Capital assets		—	35,621	7,072	42,693
Deferred expenses		—	437	—	437
Total noncurrent assets		36,433	37,823	7,072	81,328
Total assets		37,813	45,147	11,302	94,262
Liabilities:					
Current liabilities:					
Accounts payable and accrued liabilities		—	990	4,647	5,637
Due to other funds		—	1,000	6,299	7,299
Unemployment insurance benefits		1,744	—	—	1,744
Unearned revenue		2,229	—	—	2,229
Loans payable related to capital assets		—	813	—	813
Total current liabilities		3,973	2,803	10,946	17,722
Noncurrent liabilities:					
Loans payable related to capital assets		—	20,563	—	20,563
Total liabilities		3,973	23,366	10,946	38,285
Net assets:					
Invested in capital assets, net of related debt		—	14,246	7,072	21,318
Restricted		33,840	7,535	—	41,375
Unrestricted (deficit)		—	—	(6,716)	(6,716)
Total net assets	$	33,840	21,781	356	55,977

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenses, and Changes in Fund Net Assets
Proprietary Funds

Year ended September 30, 2004

(In thousands)

		Business-type activities – Enterprise funds			
		Unemployment insurance	West Indian Company	Other	Total
Operating revenue:					
Charges for services	$	3,771	12,381	25,143	41,295
Total operating revenue		3,771	12,381	25,143	41,295
Operating expenses:					
Cost of services		7,117	7,511	36,528	51,156
Depreciation and amortization		—	1,435	569	2,004
Total operating expenses		7,117	8,946	37,097	53,160
Operating income (loss)		(3,346)	3,435	(11,954)	(11,865)
Nonoperating revenue (expenses):					
Interest income		2,118	95	535	2,748
Interest expense		—	(981)	—	(981)
Total nonoperating revenue (expenses), net		2,118	(886)	535	1,767
Income (loss) before operating transfers		(1,228)	2,549	(11,419)	(10,098)
Transfers from other funds		—	—	2,500	2,500
Transfers to other funds		—	(2,000)	(895)	(2,895)
Change in net assets		(1,228)	549	(9,814)	(10,493)
Net assets, beginning of year (as restated)		35,068	21,232	10,170	66,470
Net assets, end of year	$	33,840	21,781	356	55,977

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Cash Flows
Proprietary Funds

Year ended September 30, 2004

(In thousands)

	Business-type activities – Enterprise funds			
	Unemployment insurance	West Indian Company	Other	Total
Cash flows from operating activities:				
Receipts from customers and users	$ 2,635	13,173	31,167	46,975
Payments to beneficiaries	(9,036)	—	(6,748)	(15,784)
Payments to suppliers and employees	—	(8,065)	(27,122)	(35,187)
Net cash provided by (used in) operating activities	(6,401)	5,108	(2,703)	(3,996)
Cash flows from noncapital financing activities:				
Contribution from U.S. Government	2,229	—	—	2,229
Transfer from other funds	—	—	2,500	2,500
Transfers to other funds	—	(2,000)	—	(2,000)
Net cash provided by (used in) noncapital financing activities	2,229	(2,000)	2,500	2,729
Cash flows from capital and related financing activities:				
Acquisition and construction of capital assets	—	(1,205)	(353)	(1,558)
Principal paid on long-term debt	—	(639)	—	(639)
Proceeds from sale of asset	—	2	—	2
Interest paid on long-term debt	—	(981)	—	(981)
Net cash used in capital and related financing activities	—	(2,823)	(353)	(3,176)
Cash flows from investing activities:				
Interest and dividends on investments	2,118	95	535	2,748
Net cash provided by investing activities	2,118	95	535	2,748
Net increase (decrease) in cash and cash equivalents	(2,054)	380	(21)	(1,695)
Cash and cash equivalents – beginning of year (as restated)	38,731	6,835	2,331	47,897
Cash and cash equivalents – end of year	$ 36,677	7,215	2,310	46,202
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:				
Operating income (loss)	$ (3,346)	3,435	(11,954)	(11,865)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:				
Depreciation expense	—	1,435	569	2,004
Change in assets and liabilities:				
Receivables, net	(1,136)	575	6,024	5,463
Deferred charges	—	114	—	114
Other assets	—	103	(60)	43
Accounts payable and accrued expenses	(1,919)	(554)	2,718	245
Net cash provided by (used in) operating activities	$ (6,401)	5,108	(2,703)	(3,996)
Reconciliation of cash and cash equivalents to the statement of net assets:				
Cash and cash equivalents – current	$ 244	5,450	2,310	8,004
Cash and cash equivalents – restricted	36,433	1,765	—	38,198
Cash and cash equivalents at end of year on statement of cash flows	$ 36,677	7,215	2,310	46,202

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Fiduciary Net Assets – Fiduciary Funds

September 30, 2004

(In thousands)

	Pension trust funds	Agency funds
Assets:		
Cash and cash equivalents:		
Unrestricted	$ 139,443	6,898
Restricted	72	—
Investments	1,453,090	4,048
Receivables, net:		
Loans and advances	108,135	—
Accrued interest	4,553	—
Other	48,299	—
Due from other funds	36	—
Other assets	10,966	—
Total assets	1,764,594	10,946
Liabilities:		
Accounts payable and accrued liabilities	—	10,946
Cash overdraft with the Department of Finance	10,454	—
Cash overdraft with bank	1,598	—
Unsettled securities purchased	110,876	—
Securities lending collateral	275,453	—
Notes payable	6,781	—
Other liabilities	9,126	—
Total liabilities	414,288	10,946
Net assets held in trust for employees' pension benefits	$ 1,350,306	—

See accompanying notes to basic financial statements.

Statement of Changes in Fiduciary Net Assets

Year ended September 30, 2004

(In thousands)

		Pension trust funds
Additions:		
Contributions:		
Employer	$	54,085
Plan members		30,801
Total contributions		84,886
Investment income:		
Net appreciation of fair value of investments		95,818
Interest, dividends, and other, net		40,202
Real estate – rental income		3,392
		139,412
Less investment expense		7,443
Net investment income		131,969
Other income		300
Total additions		217,155
Deductions:		
Benefits paid		131,691
Refunds of contributions		2,838
Administrative and operational expenses		8,096
Total deductions		142,625
Change in net assets		74,530
Net assets, beginning of year		1,275,776
Net assets, end of year	$	1,350,306

See accompanying notes to basic financial statements.

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Notes to Basic Financial Statements

September 30, 2004

(1) Summary of Significant Accounting Policies

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

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

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

(a) *Financial Reporting Entity*

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

(i) Blended Component Units

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

Virgin Islands Public Finance Authority

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

PFA has a component unit, the West Indian Company (WICO), which is presented as an enterprise fund in the Government's basic financial statements as further described in note 1(d).

Tobacco Settlement Financing Corporation

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

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

Administrative Offices of Blended Component Units

Virgin Islands Public Finance Authority
2400 Honduras, 2nd Floor
St. Thomas, VI 00802

Tobacco Settlement Financing Corporation
2400 Honduras, 2nd Floor
St. Thomas, VI 00802

(ii) Discretely Presented Component Units

The following component units, consistent with GASB Statements No. 14 and 39, are discretely presented in the basic financial statements because of the nature of the services they provide and the Government's ability to impose its will. The component units are reported in a separate column to emphasize that they are legally separate from the PG and governed by separate boards.

(iii) Major Component Units

Virgin Islands Housing Authority

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

Given the nature of VIHA's operations and the significance of its relationship with the Government, management believes that its exclusion from the financial reporting entity would cause the Government's basic financial statements to be incomplete and misleading. Accordingly, VIHA continues to be reported as a major component unit of the Government even though the Government no longer appoints its commissioners.

Virgin Islands Port Authority

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

Virgin Islands Water and Power Authority

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

Virgin Islands Government Hospital and Health Facilities Corporation

The Virgin Islands Government Hospital and Health Facilities Corporation (VIGHHFC) was created by Act No. 6012 on August 23, 1994 and became active on May 1, 1999. Its purpose is to provide healthcare services and hospital facilities to the people of the U. S. Virgin Islands. The powers of VIGHHFC are exercised by a board of directors consisting of 15 members as follows: the Director of the Office of Management and Budget, the Commissioner of Finance, and 13 other members appointed by the Governor with the advice and consent of the Legislature. The VIGHHFC is composed of the Roy L. Schneider Hospital located in St. Thomas and the Juan F. Luis Hospital and Medical Center located in St. Croix. Both entities issue separate audited financial statements.

University of the Virgin Islands

The University of the Virgin Islands (the University) was organized as an instrumentality of the Government under Act No. 852 of March 16, 1962, in accordance with Section 6(a) of the Revised Organic Act of 1954, as amended. The purpose of the University is the stimulation and utilization of the intellectual resources of the people of the U.S. Virgin Islands and the development of a center of higher education. The powers of the University are exercised by a board of trustees consisting of 17 members as follows: Chairman of the Board of Education, Commissioner of Education, and the President of the University, all serving as members ex-officio, 9 other members appointed by the Governor with the advice and consent of the Legislature, two other members elected by the board of trustees, one representative of the student body, one alumnus of the University, and another of the teaching faculty. The University was not organized as a self-sustaining entity and therefore receives substantial financial and other support from the Government.

The University's financial statements include its component units: The Foundation for the University of the Virgin Islands, The Reichhold Foundation, and the University of the Virgin Islands Research and Technology Park. The Foundation for the University of the Virgin Islands is a not-for-profit corporation whose purpose is to assist and support the University in accomplishing its charitable and educational mission. The Reichhold Foundation is a not-for-profit corporation that supports the arts and provides financial assistance in operating the Reichhold Center for the Arts on St. Thomas. The University of the Virgin Islands Research and Technology Park is a nontaxable public corporation developed to promote economic growth, development, and diversification in the Virgin Islands.

(iv) Nonmajor Component Units

Virgin Islands Economic Development Authority

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

Magens' Bay Authority

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

Virgin Islands Housing Finance Authority

The Virgin Islands Housing Finance Authority (VIHFA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government by Act No. 4636 of October 20, 1981, with the purpose of stimulating low- and moderate-income housing construction and home ownership through the issuance of revenue bonds to obtain funds to be used for low-interest mortgage loans to qualified purchasers of low- and moderate-income housing. The powers of VIHFA are exercised by a board of directors consisting of the Commissioner of the Department of Housing, Parks, and Recreation (the Chairman), the Director of the Office of Management and Budget, and three persons not employed by the Government appointed by the Governor with advice and consent of the Legislature.

Virgin Islands Public Television System

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

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

Administrative Offices

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

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

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

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

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

Virgin Islands Economic Development Authority
1050 Norre Gade #5
St. Thomas, VI 00802

Magens' Bay Authority
PO Box 10583
St. Thomas, VI 00802

Virgin Islands Housing Finance Authority
210-3A Altona
Frostco Center Building, Suite 101
St. Thomas, VI 00802

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

All financial statements of the discretely presented component units have a fiscal year-end of September 30, 2004, except for WAPA and VIHA that have a year-end of June 30, 2004 and December 31, 2003, respectively.

(v) Fiduciary Component Units

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

Employees' Retirement System of the Government of the Virgin Islands

The Employees' Retirement System of the Government of the Virgin Islands (known as GERS) was created as an independent and separate agency of the Government with the

purpose of administering the Government employees' defined-benefit pension plan established as of October 1, 1959. The responsibility for the proper operation of GERS is vested in a board of trustees composed of seven members appointed by the Governor with the advice and consent of the Legislature.

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

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

Employees' Retirement System of the Government of the Virgin Islands
GERS Building, 3rd Floor
St. Thomas, VI 00802

(b) Government-wide and Fund Financial Statements

The government-wide financial statements (that is, the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the PG and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the PG is reported separately from certain legally separate component units for which the PG is financially accountable. The statement of net assets presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes (i) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (ii) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenue are reported instead as general revenue.

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

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

Government-wide Financial Statements

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

Governmental Fund Financial Statements

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

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

Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements – The financial statements of the proprietary funds, fiduciary funds, and discretely presented component units are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

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

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

(d) ***Fund Accounting***

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

Governmental Funds

The Government reports the following major governmental funds:

- ***General Fund*** – The General Fund is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- ***PFA Debt Service*** – The PFA Debt Service accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by PFA on behalf of the Government.
- ***PFA Capital Projects Fund*** – The PFA Capital Projects Fund accounts for bond proceeds of debt issued by the PFA on behalf of the Government. The bond proceeds have been designated for certain necessary public safety and capital development projects which are accounted for in this fund.

Proprietary Funds

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

- ***Unemployment Insurance Fund*** – The unemployment insurance fund accounts for the collection of unemployment premiums from employers in the U.S. Virgin Islands, and the payment of unemployment benefits to eligible unemployed recipients.
- ***West Indian Company*** – WICO, a component unit of PFA, accounts for the activities of a cruise ship pier and shopping mall complex on the island of St. Thomas.

Fiduciary Funds

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

- ***Pension Trust Fund*** – The pension trust fund accounts for the activities of the Employees' Retirement System of the Government of the Virgin Islands, which accumulates resources for pension benefit payments to qualified employees.

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

(e) ***Cash and Cash Equivalents***

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

Cash equivalents of the proprietary funds and discretely presented component units consist of demand accounts, money market accounts, certificates of deposit with maturities of not more than 90 days from the date of acquisition, short-term U.S. government and its agencies' obligations and repurchase agreements with a U.S. commercial bank maturing within three months and collateralized by U.S. government obligations. Cash and cash equivalents of the discretely presented component units are maintained in separate bank accounts, from those of the PG, in their own names.

(f) ***Investments***

Title 33, Chapter 117 of the Virgin Islands Code (V.I. Code) authorizes the Government to invest in U.S. Government and agencies' obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. Investments are reported at fair value.

Investments in equity securities in the pension trust fund are carried at quoted market values. Realized gains and losses on securities are determined by the average cost method. Investments in real estate are carried at appraised value to the extent available. Investments without appraisals are carried at cost.

(g) ***Receivables***

Taxes receivable represent amounts owed by taxpayers for individual and corporate income taxes, gross receipts taxes and real property taxes. Tax revenue is recognized in the governmental fund financial statements when they become both measurable and available based on actual collections during the months subsequent to September 30.

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

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

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

Members who have contributed to the Pension Trust Fund for at least five years can borrow up to $18,000 for the purchase of an automobile. The loans bear interest at 11% with a maximum term of four years. A member may also borrow up to 75% of their contributions to the Pension Trust Fund to a maximum borrowing of $20,000 as a personal loan. The interest rate offered on personal loans was 9% throughout the year.

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

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

(h) ***Inventories***

In governmental fund types, the costs of inventories are recorded as expenditures when purchased. The proprietary fund types and component units recognize an asset when the inventory is purchased and an expense when it is consumed. Inventories in proprietary fund types are primarily valued at the lower of cost or market using the first-in, first-out method.

(i) ***Restricted Assets***

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

(j) ***Capital Assets***

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

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

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

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the PG are depreciated on the straight-line method over the assets' estimated useful lives. There is no depreciation recorded for land and construction in progress.

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

The Government chose the option available under GASB No. 34 to defer the recording of wastewater treatment facilities as information for this network of infrastructure assets was not available. These assets were deemed to be nonmajor relative to total infrastructure assets and are not reported.

(k) Tax Refunds Payable

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

(l) Deferred and Unearned Revenue

Deferred revenue at the governmental fund level arises when potential revenue neither meets measurable nor available criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Government has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Government has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized.

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Unearned revenue at the government-wide and proprietary fund levels arises only when the Government receives resources before it has a legal claim to them.

(m) Long-term Debt

The liabilities reported in the government-wide financial statements include the Government's bonds, long-term notes, and other long-term liabilities including vacation, retroactive union arbitration salaries, legal claims, and noncurrent federal fund cost disallowances related to expenditures of federal grants. Bond premiums and discounts, losses incurred on bond refundings, and debt issuance costs are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premiums or discounts and deferred refunding losses. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, government fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Losses incurred on bond refundings are not recognized in the fund financial statements as the corresponding liability for the bonds is only recorded in the government-wide financial statements. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

(n) Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

(o) Net Assets

Net assets are reported in three categories:

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

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

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

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

(p) ***Postemployment Benefits***

In addition to the pension benefits described in note 12, the Government provides postretirement healthcare benefits, in accordance with the V.I. Code to all employees who retire from the Government on or after attaining age 55 with at least 30 years of service; except for policemen and firemen who can retire with at least 20 years of service. Currently, 4,048 retirees meet those eligibility requirements. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree and the Government. The Government contributes three-fourths of the healthcare benefits' premiums. The Government does not accrue a liability for postemployment benefit costs, which are recognized on a pay-as-you-go basis. During the year ended September 30, 2004, the cost of providing healthcare benefits amounted to approximately $19.5 million.

(q) ***Compensated Absences***

The vacation policy of the Government provides for the accumulation of four, six, or eight hours for each full biweekly pay period depending on the time of entry into government service. At the beginning of each calendar year, vacation leave is limited to 480 hours (60 days). However, the excess of 480 hours is considered by GERS for service credit towards the employees' retirement. This vacation policy does not apply to professional educational personnel of the Virgin Islands Department of Education, who receive compensation during the school breaks. Upon retirement, an employee receives compensation for unused vacation leave at the employee's base rate pay. As of September 30, 2004, the Government had accrued compensated absences amounting to $60.2 million, including related benefits, of which $39.2 million was included in current liabilities in the government-wide financial statements.

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

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

(r) ***Interfund and Intra-entity Transactions***

The Government has the following types of transactions among funds:

- ***Interfund Transfers*** – Legally required transfers are reported as interfund transfers in (out) when incurred.
- ***Intra-entity Transactions*** – These are transactions between the PG and its component units, and among the component units. Transfers between the PG and its blended component units are reported as interfund transfers, except for transfers within the same fund type. Similarly, receivables and payables between the PG and its blended component units are reported as amounts due to, and due from other funds. Transfers between the PG and discretely presented component units (and among those component units) are reported separately as revenue and expenses or expenditures. Amounts owed to and from discretely presented component units by the PG are reported separately from interfund payables and receivables.

(s) ***Risk Management***

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

The Government does not maintain accounting records in support of individual claim liabilities or for claims incurred but not reported (IBNR). Accordingly, workers' compensation claims are accounted for on a cash basis. As such, the basic financial statements do not include a liability for workers' compensation claims outstanding, including related IBNR, as of September 30, 2004.

Certain component units are exposed to various risks of loss related to their specialized operations, which are mitigated by purchasing commercial insurance.

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(t) Future Adoption of Accounting Requirements

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

GASB Statement number		Adoption required in fiscal year
40	Deposit and Investment Risk Disclosures – An Amendment of GASB Statement No. 3	2005
42	Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries	2006
43	Financial Reporting for Postemployment Benefit Plans Other than Pension Plans	2007
44	Economic Condition Reporting: The Statistical Section – An amendment of NCGA Statement 1	2006
45	Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions	2008
46	Net Assets Restricted by Enabling Legislation – An amendment of GASB Statement No. 34	2006
47	Accounting for Termination Benefits	2006

The impact of these statements has not yet been determined.

(u) Use of Estimates

Management of the Government has made a number of estimates and assumptions relating to the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

(2) Component Units

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

- Virgin Islands Housing Authority
- Virgin Islands Port Authority
- Virgin Islands Water and Power Authority
- Virgin Islands Government Hospital and Health Facilities Corporation

- University of the Virgin Islands
- Economic Development Authority
- Magens' Bay Authority
- Virgin Islands Housing Finance Authority
- Virgin Islands Public Television System

Condensed financial information of all discretely presented component units follows (expressed in thousands):

Information on net assets		Virgin Islands Housing Authority	Virgin Islands Port Authority	Virgin Islands Water and Power Authority: Electric System	Virgin Islands Water and Power Authority: Water System	Virgin Islands Government Hospital and Health Facilities Corporation: Roy L. Schneider Hospital	Virgin Islands Government Hospital and Health Facilities Corporation: Juan F. Luis Hospital	University of the Virgin Islands	Other entities	Total component units
Assets:										
Current assets	$	7,067	19,974	50,071	18,407	17,370	11,737	50,774	15,181	190,581
Due from primary government		—	674	—	—	—	—	2,737	120	3,531
Due from federal government		2,515	235	—	—	200	—	1,254	—	4,204
Restricted assets		300	15,002	52,853	8,388	2,655	—	37,325	11,003	127,526
Capital assets, net		67,038	267,263	201,770	48,992	64,862	26,140	41,514	46,746	764,325
Deferred expenses		—	1,950	17,526	1,691	—	—	—	—	21,167
Total assets		76,920	305,098	322,220	77,478	85,087	37,877	133,604	73,050	1,111,334
Liabilities:										
Current liabilities		6,634	8,737	51,359	3,674	12,085	11,909	9,452	2,910	106,760
Due to primary government		—	—	—	—	7,609	17,530	—	4,243	29,382
Due to federal government		—	—	5,300	—	—	390	—	—	5,690
Bonds payable		—	37,221	163,845	34,909	—	—	44,059	6,365	286,399
Loans payable		—	890	5,600	—	—	—	3,490	901	10,881
Other noncurrent liabilities		6,484	—	—	—	558	299	132	21,235	28,708
Total liabilities		13,118	46,848	226,104	38,583	20,252	30,128	57,133	35,654	467,820
Net assets:										
Invested in capital assets – net of related debt		67,038	237,596	70,117	14,942	63,882	25,579	22,623	37,058	538,835
Restricted		—	7,149	17,486	7,674	—	—	37,003	2,478	71,790
Unrestricted (deficit)		(3,236)	13,505	8,513	16,279	953	(17,830)	16,845	(2,140)	32,889
Total net assets	$	63,802	258,250	96,116	38,895	64,835	7,749	76,471	37,396	643,514

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Information on statements of activities	Expenses	Program revenue: Charges for services	Program revenue: Operating grants and contributions	Program revenue: Capital grants and contributions	Total component units
Virgin Islands Housing Authority	$ 44,206	5,121	30,766	5,437	(2,882)
Virgin Islands Port Authority	41,910	36,651	—	10,037	4,778
Virgin Islands Water and Power Authority:					
Electric System	146,378	144,745	—	820	(813)
Water System	21,637	25,406	—	1,088	4,857
Virgin Islands Government Hospital and Health Facilities Corporation:					
Roy L. Schneider Hospital	66,171	40,235	21,778	4,541	383
Juan F. Luis Hospital	50,843	24,867	18,249	1,631	(6,096)
University of the Virgin Islands	59,484	13,607	45,476	3,192	2,791
Other component units	12,028	2,695	6,370	1,711	(1,252)
Total activities	$ 442,657	293,327	122,639	28,457	1,766
General revenue:					
Interest and other					9,425
Changes in net assets					11,191
Net assets, beginning of year (as restated)					632,323
Net assets, end of year					$ 643,514

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(3) Stewardship, Compliance, and Accountability

(a) *Budgetary Process and Control*

The V.I. Code requires the Governor to submit an annual balanced executive budget to be adopted by the Legislature for the ensuing fiscal year. The Governor is required by law to submit to the Legislature the annual executive budget no later than May 30. The annual executive budget is prepared essentially on a GAAP basis, except for encumbrances, which are reported as expenditures for budget reporting purposes, by the Virgin Islands Office of Management and Budget (OMB) working in conjunction with other Government offices and agencies. If the annual executive budget has not been approved before the commencement of any fiscal year, then the appropriations for the preceding fiscal year, insofar as they may be applicable, are automatically deemed reappropriated item by item. The annual executive budget, which includes those funds of the Government subject to appropriation pursuant to law, is composed of all proposed expenditures and estimated revenue for the Government. The Legislature enacts the annual executive budget through passage of lump-sum appropriations for each department. The Legislature may add, change, or delete any items in the annual executive budget proposed by the Governor. Upon passage by the Legislature, the annual executive budget is submitted to the Governor, who may veto the budget partially or in its entirety and return it to the Legislature with his objections. A veto by the Governor can be overridden only by a two-third majority of all members of the Legislature. The Legislature is obligated by law to pass a final annual executive budget no later than September 30, the last day of the fiscal year. Supplemental budgetary appropriations' bills that are signed into law may be created during the year

without the identification of a specific revenue source to finance them. In August 1999, the Legislature enacted the Financial Accountability Act (Act No. 6289). The purpose of the Financial Accountability Act is to require by law that the budget of the Government be balanced each year, and the appropriations in each fiscal year not exceed a verifiable revenue source.

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

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

(b) *Budget/GAAP Reconciliation*

The following schedule presents comparisons of the General Fund legally adopted budget with actual data on a budgetary basis. Because accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of timing and entity difference in the excess of revenue and other financing sources over expenditures and other financing uses for the year ended September 30, 2004 is presented below (expressed in thousands):

Excess of revenue and other financing sources (uses) over expenditures – budget basis	$ 29,089
Timing difference – change in encumbrances	(3,494)
Entity difference – excess of revenue and other financing sources over expenditures and other financing uses – activities with budgets not legally adopted	4,980
Excess of revenue and other financing sources over expenditures – GAAP basis	$ 30,575

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

(4) Cash and Investments

By law, banks or trust companies designated as depository of public funds of the Government and its various agencies, authorities, and instrumentalities are to maintain corporate surety bond or pledge collateral satisfactory to the Commissioner of Finance to secure all governmental funds deposited.

At September 30, 2004, the PG and the discretely presented component units carrying amounts of cash and cash equivalents were covered by federal deposit insurance, corporate surety bonds, or by collateral held by the Government.

Legally authorized investments vary by fund, but generally include obligations of the United States or its States, Commonwealth of Puerto Rico, the Government of the U.S. Virgin Islands, or of any agency thereof, common and preferred stocks of any U.S. corporation, common and preferred stocks of any foreign corporation listed in any internationally recognized security exchange, certain bonds or other indebtedness issued by foreign governments or foreign corporations, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Specific bond indentures also provide investment requirements.

For the fiscal year ended September 30, 2004, the PG, discretely presented component units and fiduciary funds have classified their investments into three risk categories. Category 1 includes investments that were insured or registered or for which the securities were held by a government entity, or its agent, in the entity's name and investments for which the entity has safekeeping responsibilities but no equity or ownership interest or control. Category 2 includes uninsured and unregistered investments for which the securities were held by the counterparty's trust department or agent in a government entity's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in a government entity's name. The investments of the PG and the discretely presented component units by custodial credit risk categories at September 30, 2004 were as follows (expressed in thousands):

Primary Government – Investments

	Category			Reported
	1	2	3	amount
Commercial paper	$ 93,572	—	—	93,572
Certificates of deposit	41,072	—	—	41,072
Federal Home Loan Bank	4,024	—	—	4,024
	$ 138,668	—	—	138,668
Investments not categorized:				
Mutual funds				210,452
Total investments				$ 349,120

Discretely Presented Component Units – Investments

	Category			Reported
	1	2	3	amount
U.S. government and agency securities	$ 60,038	—	—	60,038
Common stocks	1,785	—	—	1,785
Corporate bonds	5,005	—	—	5,005
Certificates of deposit	113	—	2,857	2,970
Money market funds	145	—	—	145
Investment contracts	306	—	—	306
Mortgage-backed securities		4,851	—	4,851
Other investments	—	2,353	—	2,353
	$ 67,392	7,204	2,857	77,453
Investments not subject to classification:				
Mutual funds				43,729
Total investments				$ 121,182

The investment balance consists of the following:

Unrestricted	$ 29,388
Restricted	91,794
Total investments	$ 121,182

Fiduciary Funds – Investments

	Category 1	Category 2	Category 3	Reported amount
U.S. government and agency securities	$ 7,098	—	—	7,098
Corporate obligations	28,836	—	—	28,836
Foreign bonds	88,646	—	—	88,646
Common stocks – U.S.	573,248	—	—	573,248
Certificates of deposit	4,048	—	—	4,048
Common stocks – foreign	84,967	—	—	84,967
Mortgage- and asset-backed securities	50,103	—	—	50,103
	$ 836,946	—	—	836,946
Investments not categorized:				
Mutual funds				4,625
Investments held by broker – dealers under security loans:				
U.S. government and agency securities				126,804
Corporate obligations				3,286
Common stocks – U.S.				41,425
Common stocks – foreign				30,420
Mortgage- and asset-backed securities				67,216
Securities lending short-term collateral investment pool				275,453
Real estate				70,963
Total investments				$ 1,457,138

The investment balance consists of the following:

Pension trust funds	$ 1,453,090
Agency funds	4,048
Total investments	$ 1,457,138

The pension trust fund's investments in marketable securities are administered by several professional investment managers and are held in trust by a commercial bank in the name of GERS. The investments in marketable securities generated interest and dividend income of $25 million, which is reported in interest, dividends, and other, net in the accompanying statement of change in the fiduciary net assets. During the year ended September 30, 2004, GERS' investments (including gains and losses on investments bought and sold, as well as held during the year) (depreciated) appreciated in value as follows (expressed in thousands):

U.S. government and government-guaranteed obligations	$ (366)
Corporate bonds – U.S.	(1,585)
Corporate bonds – foreign	3,233
Common stocks – U.S.	79,378
Common stocks – foreign	11,322
Collaterized debt obligations	3,235
Mutual funds	601
Net appreciation of fair value of investments	$ 95,818

The Government's statutes permit GERS to participate in securities lending transactions, and GERS has, via a securities lending authorization agreement (the Agreement), authorized State Street Bank and Trust Company (the Custodian) to lend its securities to broker-dealers and banks pursuant to a form of loan agreement. Lent securities are collateralized with cash, securities issued or guaranteed by the U.S. government, or irrevocable bank letters of credit. GERS does not have the ability to pledge or sell collateral securities delivered absent a borrower default. No restrictions were imposed during 2004 as to the amount of loans the Custodian can make on behalf of the GERS. Under the terms of the Agreement the Custodian must indemnify the Government for losses attributable to violations by the Custodian under the "standard of care" clause described in the Agreement. There were neither such violations during the fiscal year 2004 nor losses resulting from the default of the borrowers or the Custodian.

Loans are generally terminable on demand. The collateral received shall, in the case of loaned securities denominated in U.S. dollars or whose primary trading market is located in the U.S. or sovereign debt issued by foreign governments, have a market value of 102% of the market value of the security for domestic borrowers and 105% for foreign borrowers at the inception of the securities lending transaction. Such collateral should be kept at a minimum of 100% of the market value of the security for all borrowers throughout the outstanding period of the transaction. At September 30, 2004, approximately $273.1 million of U.S. government and agency securities, fixed income, and equity corporate securities were on loan. The cash collateral received with a corresponding liability of an equal amount, is recorded in the statement of fiduciary net assets. The cash collateral received on each loan was invested, together with the cash collateral of other lenders, in a collective investment pool. As of September 30, 2004, such investment pool had a weighted average maturity of 40 days and an average expected maturity of 410 days. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral.

(5) Receivables

Receivables at September 30, 2004 consist of the following (expressed in thousands):

		General fund	PFA debt service fund	Total
Income taxes	$	113,528	—	113,528
Real property taxes		27,025	—	27,025
Gross receipts taxes		—	38,253	38,253
Tax receivables	$	140,553	38,253	178,806
Other long-term receivables – tobacco settlement rights				826
Total receivables reported in the statement of net assets				$ 179,632

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

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

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

Property taxes are levied each calendar year on all taxable real property located in the U.S. Virgin Islands. The revenue is recognized in the General Fund and in the fiscal period for which the property tax was levied, provided the tax is collected within 60 days subsequent to fiscal year-end, unless the facts justify a period greater than 60 days.

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

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

For businesses with gross receipts of $120,000 per annum or less, gross receipts taxes are levied on an annual basis, based on 4% of gross receipts in excess of $5,000. Businesses with annual gross receipts greater than $120,000 and up to $150,000 are levied on a monthly basis, based on 4% of gross receipts in excess of $5,000 per month. Businesses with annual gross receipts of more than $150,000, lose the $5,000 monthly exemption and are levied on a monthly basis of 4% of gross receipts. The gross receipts tax is due within 30 calendar days following the last day of the calendar month collected.

Component unit receivables at September 30, 2004, consist of the following (expressed in thousands):

Utility service charges	$	26,816
Port fees		3,862
Students		2,231
Patients		17,796
Other		3,505
Total	$	54,210

Loans and advances receivable at September 30, 2004, consist of the following (expressed in thousands):

		Fiduciary funds pension trust	Component units
Mortgage loans	$	21,455	—
Personal loans		88,786	—
Other loans and advances		894	1,672
Subtotal		111,135	1,672
Less allowance for uncollectible accounts		(3,000)	(50)
Loans and advances, net	$	108,135	1,622

(6) Interfund Transactions

(a) Interfund Transfers

Interfund transfers constitute the transfer of resources from the fund that receives the resources to the fund that utilizes them. The most significant transfers to the General Fund from other governmental funds include a $79.2 million transfer from the PFA Debt Service representing tax revenue in excess of bond service requirements, and a $7.1 million transfer from the nonmajor governmental funds primarily representing $2.3 million of property tax revenue in excess of debt service requirements and $4.8 million of transfers from the special revenue fund. Transfers to nonmajor governmental funds consisted of $4 million from the General Fund to the Emergency Molasses Fund. Transfers from the PFA Debt Service to the nonmajor governmental funds amounting to approximately $6.3

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million represents revenue in excess of bond service requirements that were transferred to PFA operating fund (nonmajor governmental fund).

Interfund transfers for the year ended September 30, 2004 consisted of the following (expressed in thousands):

Transfer to		General fund	PFA debt service fund	PFA capital projects fund	Nonmajor governmental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Total
General fund	$	--	79,196	—	7,106	1,000	—	87,302
PFA capital projects fund		—	40	—	975	—	—	1,015
Nonmajor governmental funds		5,593	6,326	1,500	—	1,000	895	15,314
Nonmajor enterprise funds		—	—	2,500	—	—	—	2,500
Total	$	5,593	85,562	4,000	8,081	2,000	895	106,131
Transfer from								
General fund	$	—	—	—	5,593	.	—	5,593
PFA debt service fund		79,196	—	40	6,326	—	—	85,562
PFA capital projects fund		—	—	—	1,500	—	2,500	4,000
Nonmajor governmental funds		7,106	—	975	—	—	—	8,081
Major enterprise fund – WICO		1,000	—	—	1,000	—	—	2,000
Nonmajor enterprise funds		—	—	—	895	—	—	895
Total	$	87,302	—	1,015	15,314	—	2,500	106,131

(b) Due From/To Other Funds

The following table summarizes interfund receivables and payables at September 30, 2004 (expressed in thousands):

Due to		General fund	PFA debt service fund	PFA capital projects fund	Nonmajor governmental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Pension trust fund	Total
General fund	$	—	—	—	3,178	1,000	4,668	—	8,846
PFA capital projects fund		—	—	—	—	—	313		313
Nonmajor governmental funds		7,318	2,000	158	.		1,318	—	10,794
Total governmental funds		7,318	2,000	158	3,178	1,000	6,299	—	19,953
Propriety fund – nonmajor Enterprise fund		300	—	—	—	—	—	—	300
Fiduciary funds – pension Trust fund		36	—	—	—	—	—	—	36
Total	$	7,654	2,000	158	3,178	1,000	6,299	.	20,289
Due from									
General fund	$	.	.	.	7,318	—	300	36	7,654
PFA debt service fund		.			2,000	—	—	—	2,000
PFA capital projects fund		—	—	—	158	—	—	—	158
Nonmajor governmental funds		3,178	—	—	—	—	—	—	3,178
Total governmental funds		3,178	—	—	9,476	—	300	36	12,990
Enterprise fund – West Indian Company		1,000	—	—	—	—	—	—	1,000
Nonmajor enterprise funds		4,668	—	313	1,318	—	—	—	6,299
Total propriety funds		5,668	—	313	1,318	—	—	—	7,299
Total	$	8,846	—	313	10,794	.	300	36	20,289

The due from/to other funds include $3.5 million due from the General Fund to the Emergency Molasses Fund (nonmajor governmental fund) from unpaid appropriations. Other balances composing the due from/to other funds include $2.7 million from the bond proceeds fund (nonmajor governmental fund) to the General Fund and $2.0 million from the PFA Debt Service to PFA operating fund (nonmajor governmental fund). The due to the General Fund from the nonmajor enterprise fund amounting to $4,668 is mainly composed of the amount owed by the Virgin Islands Lottery to the General Fund amounting to $4,468, consisting primarily of 8% of the total lottery revenue that is required to be transferred to the General Fund.

(7) Restricted Assets

(a) Primary Government

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

Restricted Assets – Proprietary Funds and Business-type Activities

Unemployment insurance funds	$	36,433
WICO debt service funds		1,765
Total restricted assets of proprietary funds and business-type activities	$	38,198

(b) Component Units

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

Restricted Assets – Component Units

Debt service and sinking fund requirements	$	18,281
Construction funds		1,647
Endowment funds		10,601
HUD project funds		300
Revolving loan funds		3,244
Other		471
Total cash and cash equivalents		34,544
Investments:		
Debt service and sinking fund requirements		25,400
Construction funds		25,442
Endowment funds		26,723
Renewal and replacement funds		7,025
Revolving loan funds		7,204
Total investments		91,794
Other:		
Accrued interest receivable		1,188
Total restricted assets of component units	$	127,526

(8) Capital Assets

(a) Primary Government

The capital assets activity for the governmental activities for the year ended September 30, 2004, is summarized as follows (expressed in thousands):

		Beginning balance	Additions	Reductions	Ending balance
Capital assets, not being depreciated					
Land	$	184,525	414	—	184,939
Construction in progress		4,046	24,450	3,918	24,578
Total capital assets, not depreciated		188,571	24,864	3,918	209,517
Capital assets, being depreciated:					
Land improvements		3,584	—	—	3,584
Infrastructure		121,413	4,836	—	126,249
Buildings and improvements		400,309	2,141	—	402,450
Machinery and equipment		69,788	8,627	256	78,159
Total capital assets, being depreciated		595,094	15,604	256	610,442
Less accumulated depreciation for:					
Land improvements		1,494	165	—	1,659
Infrastructure		13,458	4,119	—	17,577
Buildings and improvements		121,140	7,903	—	129,043
Machinery and equipment		39,415	6,991	256	46,150
Total accumulated depreciation		175,507	19,178	256	194,429
Total capital assets, being depreciated, net		419,587	(3,574)	—	416,013
Governmental activities capital assets, net	$	608,158	21,290	3,918	625,530

Capital assets activity for the business-type activities for the year ended as of September 30, 2004, is summarized as follows (expressed in thousands):

	Beginning balance (as adjusted)	Additions	Reductions	Ending balance
Capital assets, not being depreciated				
Land and land improvements	$ 5,357	—	—	5,357
Construction in progress	722	87	—	809
Total capital assets, not depreciated	6,079	87	—	6,166
Capital assets, being depreciated:				
Buildings and improvements	46,490	1,088	3	47,575
Machinery and equipment	3,478	383	70	3,791
Total capital assets, being depreciated	49,968	1,471	73	51,366
Less accumulated depreciation for:				
Buildings and improvements	11,215	1,813	—	13,028
Machinery and equipment	1,690	191	70	1,811
Total accumulated depreciation	12,905	2,004	70	14,839
Total capital assets, being depreciated, net	37,063	(533)	3	36,527
Business-type activities capital assets, net	$ 43,142	(446)	3	42,693

Depreciation and amortization expense was charged to functions/programs of the PG for the year ended September 30, 2004 as follows (expressed in thousands):

Governmental activities:	
General government	$ 3,953
Public safety	1,571
Health	3,373
Education	5,744
Transportation and communication	4,537
Total depreciation expense – governmental activities	$ 19,178
Business-type activities:	
WICO (major enterprise fund) – depreciation and amortization	$ 1,435
Nonmajor enterprise fund – depreciation	569
Total depreciation and amortization – business-type activities	$ 2,004

The capital assets activity for the discretely presented component units for the year ended September 30, 2004 is summarized as follows (expressed in thousands):

	Beginning balance	Additions	Reductions	Ending balance
Capital assets, not being depreciated:				
Land	$ 93,789	1,906	—	95,695
Construction in progress	52,114	78,207	56,848	73,473
Total capital assets, not depreciated	145,903	80,113	56,848	169,168
Capital assets being depreciated:				
Buildings and improvements	1,122,835	54,286	539	1,176,582
Airport and marine terminal facilities	96,914	5,751	—	102,665
Personal property and equipment	90,303	8,511	4,394	94,420
Total capital assets being depreciated	1,310,052	68,548	4,933	1,373,667
Less accumulated depreciation:				
Buildings and improvements	(617,030)	37,974	7	(654,997)
Airport and marine terminal facilities	(60,807)	4,420	—	(65,227)
Personal property and equipment	(56,022)	6,621	4,357	(58,286)
Total accumulated depreciation	(733,859)	49,015	4,364	(778,510)
Total capital assets being depreciated, net	576,193	19,533	569	595,157
Component unit capital assets, net	$ 722,096	99,646	57,417	764,325

Depreciation expense charged to each component unit for the year ended September 30, 2004 was as follows (expressed in thousands):

Virgin Islands Housing Authority	$	9,375
Virgin Islands Port Authority		13,802
Virgin Islands Water and Power Authority:		
Electric system		10,323
Water system		5,407
Virgin Islands Government Hospital and Health Facilities Corporation:		
Roy L. Schneider Hospital		3,947
Juan F. Luis Hospital		2,723
University of the Virgin Islands		2,930
Other component units		508
Total depreciation – component units	$	49,015

(9) Long-Term Liabilities

Long-term liabilities activities for the year ended September 30, 2004 were as follows (expressed in thousands):

		Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year	Amounts due thereafter
Governmental activities:							
Bonds payable:							
1998 Series Revenue and Refunding Bonds	$	486,970	—	(13,225)	473,745	13,955	459,790
1999 Project Revenue Bonds		4,510	—	(2,960)	1,550	1,550	—
1999 General Obligation Bonds, Series A		6,480	—	(830)	5,650	885	4,765
1999 Series A Revenue Bonds		287,875	—	(4,540)	283,335	4,765	278,570
2001 Series A Tobacco Bonds		22,645	—	(335)	22,310	—	22,310
2002 Series Garvee Bonds		18,645	—	(2,805)	15,840	2,900	12,940
2003 Series A Revenue Bonds		—	268,020	—	268,020	—	268,020
Subtotal bonds payable		827,125	268,020	(24,695)	1,070,450	24,055	1,046,395
Less:							
Deferred amount on refundings		(3,080)	—	616	(2,464)	(616)	(1,848)
Bonds premium		1,299	2,830	(310)	3,819	311	3,508
Bonds discount		(10,001)	—	949	(9,052)	(948)	(8,104)
Bonds accretion		(1,418)	—	320	(1,098)	(335)	(763)
Total bonds payable, net		813,925	270,850	(23,120)	1,061,655	22,467	1,039,188
Loans payable:							
Bond anticipation note		100,000	—	(100,000)	—	—	—
Total loans payable		100,000	—	(100,000)	—	—	—
Other liabilities:							
Accrued compensated absences		52,358	7,852	—	60,210	39,213	20,997
Retroactive union arbitration		375,252	9,006	—	384,258	—	384,258
Litigation		13,235	2,478	(538)	15,175	450	14,725
Landfill closure and postclosure costs		—	28,821	—	28,821	—	28,821
Accrued disallowed costs		13,112	—	(7,098)	6,014	—	6,014
Total other liabilities		453,957	48,157	(7,636)	494,478	39,663	454,815
Total governmental activities	$	1,367,882	319,007	(130,756)	1,556,133	62,130	1,494,003
Business-type activities:							
Notes payable:							
WICO	$	22,015	—	(639)	21,376	813	20,563
Fiduciary activities:							
Note payable							
Pension trust fund	$	10,000	—	(3,219)	6,781	6,781	—

Accrued compensated absences, retroactive union arbitration liabilities, accrued litigation, and the landfill closure and post-closure costs are generally expected to be liquidated with resources derived from the General Fund. Accrued disallowed costs are generally expected to be liquidated with resources derived from the General Fund.

(a) ***Debt Margin***

Pursuant to 48 U.S.C. Section 1574(b)(i) of the Revised Organic Act, the Government may issue revenue bonds for public improvements or undertakings authorized by an act of the Legislature, without limitation as to principal amount. Such revenue bonds are payable solely from the revenue directly derived from and attributable to such public improvements or undertakings. Pursuant to 48 U.S.C. Section 1574(b)(ii), the Government is authorized to issue general obligation bonds for any public purpose provided that no such indebtedness is in excess of 10% of the aggregate assessed valuation of the taxable real property in the U.S. Virgin Islands. In addition, pursuant to 48 U.S.C. Section 1574(a) (Public Law 94-932), the U.S. Virgin Islands is authorized to cause to be issued bonds or other obligations in anticipation of the matching funds to be received from the federal government pursuant to 26 U.S.C. Section 7652(b)(3). There is no legal limit on the value of bonds that the Government may issue pursuant to 48 U.S.C. Section 1574(a). The Legislature of the U.S. Virgin Islands must authorize all bond issuances. PFA is authorized to issue bonds for the purpose of financing any project or for the purpose authorized by the Legislature. Given that PFA's powers to issue bonds are derived from 48 U.S.C. Section 1574(b), the bonds issued by PFA are subject to the limitations of said 48 U.S.C. Section 1574(b). On August 23, 1999, the Legislature amended the V.I. Code to add a Mandatory Balanced Budget Provision. Such provisions, specifically Title 2 of the V.I. Code Section 256, provide that the amount of debt of the Government existing on October 1, 2000 shall be the debt limit of the Government, exclusive of bond principal and interest that may become due. The debt limit specified under Title 2 of the V.I. Code Section 256 does not include bonds authorized by law for which a specific source of revenue is identified and committed to retiring those bonds. As used in Title 2 of the V.I. Code Section 256, the term "debt" means the total accumulated unpaid obligations that are due and payable, including unpaid income tax refunds, amounts owed to vendors, and current year unpaid debt service obligations, if any. As used in the statute, the term "debt" does not include that portion of principal or interest on bonds that is not yet due and payable.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS
Notes to Basic Financial Statements
September 30, 2004

(b) ***Bonds Payable***

Bonds payable outstanding at September 30, 2004 are comprised of the following (expressed in thousands):

Primary Government – Bonds Payable

Bonds payable	Final maturity	Interest rates (%)	Balance
1998 Series A, C, D, and E Revenue and Refunding Bonds	2023	5.50 – 7.11	$ 473,745
1999 Project Revenue Bonds	2005	6.25	1,550
1999 Series A General Obligation Bonds	2010	6.50	5,650
1999 Series A Revenue Bonds	2033	4.20 – 6.50	283,335
2001 Series A Tobacco Bonds	2031	5.00	22,310
2002 Series Garvee Bonds	2009	2.50 – 5.00	15,840
2003 Series A Revenue Bonds	2033	4.00 – 5.25	268,020
Subtotal			1,070,450
Less:			
Deferred amount on refundings			(2,464)
Bonds premium			3,819
Bonds discount			(9,052)
Bonds accretion			(1,098)
Total			$ 1,061,655

On May 1, 1998, PFA issued the revenue and refunding bonds series 1998 A, B, C, D, and E amounting to $541.8 million, secured by general obligation notes issued by the Government. These bonds were issued for the purpose of, among other things, advance refunding of previously issued bonds in order to obtain lower interest rates.

The proceeds of the 1998 Series A and B Bonds were placed in an irrevocable trust account to provide for all future debt service payments on the Highway Revenue Bonds Series 1989, Series 1991, Series 1992, Series 1993, and Series 1994 Bonds. At September 30, 2004, $194.6 million of the above-mentioned defeased bonds were outstanding.

The proceeds of the Series 1992 Revenue Bonds were placed in an irrevocable trust to provide for all future debt service payments on the Series 1989 Revenue Bonds. At September 30, 2004, $165.9 million of defeased bonds were outstanding. All assets held by irrevocable trusts for refunding of prior outstanding debt and the corresponding liabilities are not included in the Government's basic financial statements.

The 1998 Series C Bonds and the 1998 Series D Bonds were issued to pay, on behalf of the Government, the full principal balance and interest due and payable on the Revenue Anticipation Note, issued in February 1998. The remaining balance of the 1998 Series D Bonds amounting to approximately $11.6 million was primarily provided to the Government for additional working capital. The net proceeds of the 1998 Series E Bonds amounting to $104 million were primarily designated to fund the construction of certain capital projects amounting to $94 million. The remaining $10 million was deposited in a debt service reserve account.

The U.S. Department of the Treasury makes certain transfers to the Government of substantially all excise taxes imposed and collected under the Internal Revenue laws of the United States in any fiscal year on certain products produced in the U.S. Virgin Islands (primarily rum) and exported to the United States from the Virgin Islands. The amount required to be remitted to the Government by the U.S. Department of the Treasury is an amount no greater than the total amount of local revenue (primarily taxes) collected by the Government in each fiscal year. As a result, the term "matching fund revenue" is used to denote these payments. The Government has pledged the matching fund revenue, as described above, to the timely payment of principal and interest on the 1998 Series A, B, C, D, and E Bonds. Thus, amounts to be received by the Government from federal excise taxes, mostly in rum, are deposited directly in a trust account until the 1998 Bonds are paid in accordance with the Indenture of Trust.

Estimated prepayments of matching fund revenue are made to the Government prior to the beginning of each fiscal year, subject to adjustment for the amount of local revenue actually collected by the U.S. Department of the Treasury during such year. Prepayments of matching fund revenue are recorded as deferred revenue in the accompanying statement of net assets and the balance sheet of the governmental funds and reversed against revenue in the following year. The adjustments for actual collections made to the estimated prepayments are recorded in the year determined.

In November 1999, the U.S. Congress approved an increase in the rate of federal excise taxes on rum transferred to the Government from $10.50 to $13.25 per proof gallon. The increase was retroactive to July 1999 and effective through December 31, 2003. In October 2004, Congress extended the $13.25 per proof gallon rate to December 31, 2005.

Interest on the Revenue and Refunding Bonds Series 1998 A, B, C, D, and E and 1999 Bonds are payable semiannually on April 1 and October 1, and principal is payable annually on October 1. The Government is responsible for all principal and interest payments on the 1998 Series bonds. The principal due on October 1 and interest payments due on October 1 and April 1, are funded by the matching fund revenue and deposited into the debt service reserve accounts.

On April 13, 1999, a loan agreement was made between and among the Government, the PFA, International Business Machine Corporation (IBM), Banco Popular de Puerto Rico, and U.S. Trust Company of New York (Y2K Loan). The purpose of this loan was to finance certain costs of compliance by the Government with Year 2000 computer system issues. The loan was evidenced by the Government's issuance of General Obligation Bonds Series 1999 A amounting to $18 million. Principal and interest are payable semiannually on January 1 and July 1. On July 9, 2001, the Government paid the outstanding IBM portion of the bonds amounting to $7.4 million.

The Bonds are secured by the full faith and credit and taxing power of the Government, including a pledge on annual real property tax revenue from its taxation of the Hovensa Oil Refinery (the Refinery), which revenue is deposited in the Hovensa Property Tax Fund, and a contingent pledge of all franchise taxes on foreign sales corporations collected by the Government

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(Franchise Tax Revenue). Pursuant to the Hovensa Oil Contract, the Refinery agreed to pay $14 million annually of real property taxes on the Refinery properties. Foreign sales corporations qualified to do business in the Virgin Islands must pay a franchise tax of $1.50 for each thousand dollars of capital stock issued (Franchise Tax).

On April 13, 1999, PFA also issued Project Revenue Bonds (the 1999 Project Revenue Bonds), amounting to $13.5 million on behalf of the Government, to finance a portion of the Government's Year 2000 (Y2K) compliance efforts, including the costs related to transportation, installation, and related hardware, software, consulting services, and related expenses. The 1999 Project Revenue Bonds are secured by lease payments made by the Government to PFA pursuant to a municipal lease purchase agreement, dated April 13, 1999. Such lease payments shall be funded by appropriation from the real property taxes deposited in the Hovensa Property Tax Fund and all franchise taxes on a subordinated basis and subject to any superior rights of the Series 1999 A General Obligation Bonds. The 1999 Project Revenue Bonds mature on January 1, 2005 with interest payable semiannually on January 1 and July 1.

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

The Government pledged gross receipts taxes for the timely payment of the principal and interest on the 1999 Series A Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. Gross receipts revenue amounted to $112.4 million for the year ended September 30, 2004.

On November 20, 2001, TSFC issued Tobacco Settlement Asset-Backed Bonds amounting to $23.6 million of the aggregate principal. The proceeds were used for the purpose of (i) purchasing all rights, title, and interest in certain litigation awards under the master settlement agreement (MSA) entered into by participating cigarette manufacturers, (ii) issuance of Tobacco Settlement Asset-Backed Bonds to pay the purchase price for the rights, and (iii) to provide funds for hospital and healthcare projects in the U.S. Virgin Islands.

Interest on the 2001 bonds is payable semiannually on each May and November 15, beginning with May 2002 for the term bonds amounting to $15.5 million and convertible capital appreciation bonds amounting to $8.2 million, with a nominal value of $6.2 million.

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

Bonds payable at September 30, 2004, amounted to $22.3 million with accumulated accretion of $1.1 million. Under early redemption provisions, any MSA payments exceeding annual debt service requirements of the 2001 Series A Tobacco Bonds must be applied to early redemption of principal. MSA payments and interest earnings on the trust funds during the year ended September 30, 2004, resulted in early redemption of $335 thousand during fiscal year 2004.

On October 1, 2002, PFA issued the Series 2002 Revenue Bonds (Garvee Bonds), the proceeds of which amounted to $20.8 million. The Garvee Bonds are special, limited obligations, secured solely by the pledge and assignment of the Government's security interest in Federal Highway Reimbursement Revenues. The bonds were issued to (i) fund construction costs related to renovation and construction of two sea docks, (ii) fund the Debt Service Reserve Accounts, and (iii) pay certain costs of issuing the bonds. The Series 2002 Bonds are not subject to redemption prior to maturity.

Interest and principal on the Series 2002 Revenue Bonds are payable semiannually on March 1 and September 1. As of September 30, 2004, the outstanding 2002 Revenue Bonds amounted to $15.8 million.

On February 28, 2003, PFA entered into a swaption contract that provided PFA with an up-front payment of $8.3 million. PFA has outstanding $243,985,000 Series of 1999A Bonds with maturities from 2011 to 2029. The 1999A Bonds are callable by PFA on October 1, 2010 at 101%. Having been advised by its underwriters and financial advisor that there were no net present value savings available to it by issuing conventional advance refunding bonds, PFA sold a LIBOR-based swaption to Lehman Brothers Special Financing, Inc. on the 2024 and 2029 maturities, totaling $162,870,000. Lehman purchased the swaption for $8.3 million and it is exercisable on July 1, 2010 only. The objective of PFA was to monetize the economics of the Series of 1999A Bonds call option and lock in the favorable interest rates prevailing on February 28, 2003 without currently issuing refunding bonds. The swaption was the most efficient mechanism available to PFA to effect savings from the Series 1999A Bonds at that time. As a synthetic refunding of its 1999 Series A Bonds, this payment represents the risk-adjusted, present-value savings of the refunding as of October 1, 2010, without issuing refunding funds at February 2003. The swaption gave the counterparty the option to make PFA enter into a pay-fixed, receive-variable interest rate swap. If the option is exercised, PFA would then expect to issue variable-rate refunding bonds.

The $8.3 million payment was based on a notional amount of $174.9 million. The counterparty has the option to exercise the agreement on October 1, 2010—PFA's 1999 bonds' first call date. If the swap is exercised, it will also commence October 1, 2010. The fixed swap rate (5.2%) was set at a rate that, when added to an assumption for remarketing and liquidity costs, will approximate the coupons of the refunded bonds. The swap's variable payment would be 64% of the London Interbank Offered Rate (LIBOR).

The up-front payment of $8.3 million was received by PFA on behalf of the PG. The Government has deferred the recognition of revenue from the $8.3 million received in advance, and is amortizing it into income through October 1, 2010, which is the exercise date of the swaption. The up-front payment was restricted to capital expenditures. In 2004, PFA authorized the use of $2 million of the up-front payment for a Micro Loan Financing Program, which is managed by the Economic Development Authority. As of September 30, 2004, the PFA had expended $104 thousand on capital projects and $78 thousand on micro-loans.

As of September 30, 2004, the swap had a negative fair value of approximately $21.8 million in favor of the counterparty estimated using the zero-coupon method. This method calculated the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipated future spot interest rates. These payments were then discounted

using the spot rates implied by the current yield curve for the hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

If the option is exercised and refunding bonds are not issued, the 1999 bonds would not be refunded and PFA would make net swap payments as required by the terms of the contract – that is, making a fixed payment to the counterparty for the term of the swap at 5.27% and receiving a variable payment of 64% of LIBOR. If the option is exercised and the variable rate bonds issued, the actual savings ultimately recognized by the transaction will be affected by the relationship between the interest rate terms of the to-be issued variable-rate bonds versus the variable payment on the swap (64 % of LIBOR). If the option is not exercised, PFA is not obligated to repay the up-front payment.

On December 17, 2003, PFA issued the Series 2003A Revenue Bonds, the proceeds of which amounted to approximately $268 million. The bonds were issued to: (i) repay the Government outstanding Revenue Bond Anticipation Notes, Series 2003, (ii) fund certain necessary public safety and other public sector capital development projects, (iii) fund debt service accounts for the bond issuance, and (iv) to pay certain costs of issuing the bonds.

The Government has pledged gross receipts taxes for the timely payment of the principal and interest on the Series 2003A Revenue Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1, beginning October 1, 2005. The Series 2003A Revenue Bonds are not subject to optional redemption prior to October 1, 2014.

Debt service requirements at September 30, 2004 were as follows (expressed in thousands):

Governmental Activities – Bonds

	Revenue Bonds Series 1998 A Principal	Revenue Bonds Series 1998 A Interest	Revenue Bonds Series 1998 C Principal	Revenue Bonds Series 1998 C Interest	Revenue Bonds Series 1998 D Principal	Revenue Bonds Series 1998 D Interest	Revenue Bonds Series 1998 E Principal	Revenue Bonds Series 1998 E Interest	Revenue Bonds Series 1998 Total Principal	Revenue Bonds Series 1998 Total Interest
Year:										
2005 $	—	15,821	9,990	2,801	3,965	1,220	—	6,261	13,955	26,103
2006	—	15,821	10,555	2,236	4,210	974	—	6,261	14,765	25,292
2007	—	15,821	11,150	1,640	4,470	714	—	6,261	15,620	24,436
2008	—	15,821	11,780	1,009	4,750	437	—	6,261	16,530	23,528
2009	—	15,821	12,455	343	4,915	147	—	6,261	17,370	22,572
2010 – 2014	73,175	69,891	—	—	—	—	30,095	27,178	103,270	97,069
2015 – 2019	96,095	50,199	—	—	—	—	39,665	17,098	135,760	67,297
2020 – 2024	81,700	26,444	—	—	—	—	36,670	4,366	118,370	30,810
2025 – 2029	38,105	3,215	—	—	—	—	—	—	38,105	3,215
Total $	289,075	228,854	55,930	8,029	22,310	3,492	106,430	79,947	473,745	320,322

	General Obligation Bonds Series 1999 A Principal	General Obligation Bonds Series 1999 A Interest	Project Revenue Bonds Series 1999 Principal	Project Revenue Bonds Series 1999 Interest	Revenue Bonds Series 1999 A Principal	Revenue Bonds Series 1999 A Interest	Tobacco Bonds Series A 2001 Principal	Tobacco Bonds Series A 2001 Interest	Garvee Bonds Series 2002 Principal	Garvee Bonds Series 2002 Interest
Year:										
2005 $	885	353	1,550	48	4,765	17,470	—	705	2,900	748
2006	945	295	—	—	5,005	17,210	—	705	3,000	646
2007	1,005	232	—	—	5,285	16,921	—	705	3,155	497
2008	1,075	166	—	—	5,585	16,615	910	705	3,310	339
2009	1,140	95	—	—	5,900	16,292	1,030	705	3,475	173
2010 – 2014	600	19	—	—	35,020	75,693	6,270	3,525	—	—
2015 – 2019	—	—	—	—	47,510	62,751	—	3,525	—	—
2020 – 2024	—	—	—	—	64,815	44,865	6,055	2,465	—	
2025 – 2029	—	—	—	—	88,385	20,664	—	2,011	—	—
2030 – 2034	—	—	—	—	21,065	645	8,045	603	—	—
Total $	5,650	1,160	1,550	48	283,335	289,126	22,310	15,654	15,840	2,403

	Revenue Bonds Series 2003 A Principal	Revenue Bonds Series 2003 A Interest	Total governmental activities Principal	Total governmental activities Interest
Year:				
2005 $	—	13,301	24,055	58,728
2006	2,875	13,244	26,590	57,392
2007	2,990	13,126	28,055	55,917
2008	3,110	13,004	30,520	54,357
2009	3,230	12,877	32,145	52,714
2010 – 2014	18,315	62,130	163,475	238,436
2015 – 2019	23,335	56,937	206,605	190,510
2020 – 2024	30,115	49,995	219,355	128,135
2025 – 2029	38,520	41,386	165,010	67,276
2030 – 2034	145,530	21,133	174,640	22,381
$	268,020	297,133	1,070,450	925,846

(c) *Conduit Debt*

In February 2004, the PFA issued private activity bonds amounting to $50.6 million to finance costs of construction of a coker plant for a refinery on the island of St. Croix. The bonds are limited obligations of PFA and will be payable solely from and secured by a pledge and assignment of the amounts payable under the loan agreement between PFA and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the

repayment of the bonds. The bonds are not reported as liabilities in the Government's basic financial statements.

(d) *Notes Payable*

On September 4, 2003, the PG issued $100 million Bond Anticipation Notes (BANs) in anticipation of the issuance of the 2003 Series A Revenue Bonds. Interest accrued quarterly at a rate of 3.25%. The proceeds of the BANs were used for the purpose of (i) funding vendor payments and tax refunds, (ii) funding capitalized interest, and (iii) paying the cost of issuance of the BANs. On December 17, 2003, the 2003 Series A Series Bonds were issued, and the BANs were repaid.

On November 20, 2002, WICO consolidated and refinanced the 1993 and 2000 loans, and obtained an additional $2 million in financing for infrastructure improvements. The consolidated loan amounts to $22.5 million, to be repaid in 239 monthly installments of $142 thousand, and a final payment of outstanding principal balance plus any unpaid interest accrued to the date of the final payment. The consolidated loan has a fixed interest rate of 4.5% for the first four years of the loan. After the first four years, WICO will have the option to adjust the interest rate to one of the following: (i) prime rate plus 75 basis points, (ii) one-year LIBOR rate plus 200 basis points, or (iii) three-year treasury note rate plus 125 basis points. The revenue of WICO and lease agreements are pledged for the payment of principal and interest on the loan. WICO paid approximately $981 thousand in interest expense during fiscal year 2004.

Debt service requirements for the WICO loan at September 30, 2004 were as follows (expressed in thousands):

Year:		
2005	$	768
2006		804
2007		840
2008		879
2009		920
2010 – 2014		5,271
2015 – 2019		6,598
2020 – 2023		5,296
Total	$	21,376

(e) *Fiduciary Funds – Notes Payable*

On December 30, 2002, the pension trust fund entered into a line-of-credit agreement with a bank to provide working capital. The pension trust fund obtained a line-of-credit of $10 million, which accrues interest at a fixed interest rate of 4.8% calculated on a 360-day basis and is due and payable quarterly in arrears commencing on the first day of the fourth calendar month following the closing of the loan. The terms of the line-of-credit require the pension trust fund to repay the line-of-credit in a period of 30 consecutive days during each 12-month period. The bank retains a certificate of deposit in the amount of $10 million as security on the note payable. As of September 30, 2004, the outstanding balance on the line-of-credit agreement was $6.8 million.

(f) Component Units – Bonds Payable

Bonds payable of discretely presented component units are those liabilities that are paid out of resources pledged by such entities. These revenue bonds do not constitute a liability or debt of the PG. Bonds payable outstanding at September 30, 2004 are as follows (expressed in thousands):

Bonds payable	Final maturity	Interest rates (%)		Balance
University of the Virgin Islands:				
General obligation bonds of 2004	2035	2.02 – 5.38	$	21,150
General obligation bonds of 1999	2029	6.50 – 7.75		23,500
Virgin Islands Water and Power Authority (Electric System)				
Revenue bonds of 2003	2023	4.00 – 5.00		69,960
Revenue bonds of 1998	2022	4.25 – 5.30		92,350
Virgin Islands Water and Power Authority (Water System)				
Revenue bonds of 1999	2017	4.90 – 5.50		37,450
Virgin Islands Port Authority				
Revenue bonds of 2003	2023	3.73 – 5.43		33,440
Revenue bonds of 1998	2005	3.45 – 4.50		496
Revenue draw down bonds of 2003	2023	4.40		2,972
Virgin Islands Housing Finance Authority:				
Revenue bonds of 1995	2025	5.50 – 6.50		3,715
Revenue bonds of 1998	2028	4.10 – 5.25		2,650
Subtotal				287,683
Plus unamortized premium				5,648
Less unamortized discount				(876)
Less deferred amount on debt refunding and reacquisition costs				(6,056)
Bonds payable, net				286,399
Less amount due within one year				(8,476)
Bonds payable, due in more than one year			$	277,923

Following is a schedule of changes in long-term debt for discretely presented component units for fiscal year 2004 (expressed in thousands):

		Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year	Amounts due thereafter
Bonds payable:							
University of the Virgin Islands	$	23,533	21,150	(624)	44,059	290	43,769
Virgin Islands Water and Power Authority:							
Electric System		167,673	—	(3,828)	163,845	4,355	159,490
Water System		36,415	—	(1,506)	34,909	1,900	33,009
Virgin Islands Port Authority		35,738	3,038	(1,555)	37,221	1,806	35,415
Virgin Islands Housing Finance Authority		6,485	—	(120)	6,365	125	6,240
Total bonds payable, net		269,844	24,188	(7,633)	286,399	8,476	277,923
Loans payable:							
Virgin Islands Economic Development Authority		947	—	(46)	901	55	846
Virgin Islands Water and Power Authority:							
Electric System		—	5,600	—	5,600	5,600	—
Virgin Islands Port Authority		913	1,200	(1,223)	890	890	—
University of the Virgin Islands		3,540	—	(50)	3,490	1,753	1,737
Total loans payable		5,400	6,800	(1,319)	10,881	8,298	2,583
Other long-term liabilities:							
University of the Virgin Islands		132	—	—	132	—	132
Virgin Islands Housing Authority		5,538	946	—	6,484	—	6,484
Virgin Islands Economic Development Authority		8,106	407	—	8,513	—	8,513
Juan F. Luis Hospital		561	—	(263)	298	—	298
Roy L. Schneider Hospital		474	508	(424)	558	—	558
Virgin Islands Housing Finance Authority		12,433	290	—	12,723	—	12,723
Total other long-term liabilities	$	27,244	2,151	(687)	28,708	—	28,708

On December 1, 1999, the University issued the 1999 Series A Bonds. The University issued these bonds to finance a portion of the construction, furnishing, and equipping of various facilities of the University, to refund the 1994 Series A bonds issued by the University, to fund a debt service reserve fund for the 1999 Series A Bonds, and to pay certain costs issued under and secured by an indenture of trust dated. The 1999 Series A Bonds maturing on or after December 1, 2010 are subject to redemption prior to maturity at the option of the University, as a whole or in part of any date, on and after December 1, 2009, at redemption prices ranging between 100% and 102% of their principal amount plus accrued interest to the date fixed for redemption. At September 30, 2004, $14.1 million of the 1994 Series A Bonds are considered defeased and outstanding.

In fiscal year 2004, the University of the Virgin Islands General Obligation Improvement Bonds, 2004 Series A (the 2004 Series A Bonds) were issued in the amount of $21.2 million under and secured by the Indenture of Trust dated as of December 1, 1999 and a First Supplemental Indenture of Trust dated as of June 1, 2004, between the University and the trustees. These Bonds will be used to finance the costs of construction, furnishings, and equipping of various facilities of the University, to fund the debt service reserve fund and to pay the cost of issuance.

In June 2003, the Virgin Islands Water and Power Authority (Electric System) issued the Electric System Revenue Bonds, Series 2003, amounting to $69.9 million. The proceeds from the bonds were used to finance capital improvements, repay $18 million of then outstanding lines-of-credit, cover underwriters' costs, and establish a debt service fund.

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

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

The Bond Resolution contains certain restrictions and commitments, including the Electric System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net electric revenue, as defined, that will be at least 125% of aggregate annual principal and interest. The Electric System's net electric revenue for the fiscal year ended June 30, 2004 was 199% of the aggregate debt service as defined in the Bond Resolution.

The Series 2003 Bonds maturing on or after July 1, 2013 are subject to redemption prior to their stated maturity date, at the option of the Electric System, on or after July 1, 2013, as a whole or in part at any time, at a redemption price equal to the principal amount thereof plus accrued interest thereon to the date fixed for redemption.

The 1998 Series Electric System Revenue and Refunding Bonds are subject to redemption on or after July 1, 2008, as a whole or in part at any time, at a redemption price of 101% in 2008, 100.5% in 2009, and 100% thereafter. The Electric System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the Electric System was damaged, destroyed, taken, or condemned, or (ii) any for-profit nongovernmental investor shall acquire an ownership interest in some or all of the assets of the Electric System.

In December 1998, the Virgin Islands Water and Power Authority (Water System) issued the 1998 Water System Revenue and Refunding Bonds amounting to $44.1 million. The proceeds from the bonds were used to repay the 1990 Series A Water System Revenue Bonds at a redemption price of 100% and to refund the 1992 Series B Water System Revenue Bonds, repay outstanding lines of credit balances, pay underwriters' costs, provide funding for a Renewal and Replacement Reserve Fund, and to purchase obligations of the United States Government, which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining principal amount of the 1992 Series B Bonds. At June 30, 2004, $37.4 million of the original principal amount of the defeased 1992 Series B Bonds remained outstanding.

Payment of principal and interest of the 1998 Series Bonds is secured by an irrevocable lien on the Water System's net revenues (exclusive of any funds that may be established pursuant to the Bond

Resolution for certain other specified purposes) and funds established under the Bond Resolution, including investment securities. To provide additional security, the Water System has conveyed to the bond trustee, a subordinate lien and security interest in the Water System's General Fund. The Water System is also required to make deposits in a debt service reserve fund in accordance with the Bond Resolution.

The Bond Resolution contains certain restrictions and commitments, including the Water System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net water revenue, as defined, that will be at least 125% of aggregate annual principal and interest payments. The Water System's net water revenue for the fiscal year ended June 30, 2004 was 135% of the aggregate debt service.

The 1998 Series Bonds maturing on or after July 1, 2010 are subject to redemption prior to their stated maturity date, at the option of the Water System, as a whole or in part at any time, at a redemption price of 101% during July 1, 2009 through June 30, 2010 and 100% thereafter. The Water System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the water system shall be damaged, destroyed, taken, or condemned or (ii) any for-profit non-governmental investor shall acquire an ownership interest in some or all assets of the Water System.

In October 1998, the VIPA issued the 1998 Rohlsen Terminal Airport Revenue Bonds Series A, with a principal amount of $3.1 million. The bonds were issued for the advance refunding of previously issued bonds. The Rohlsen Terminal Bonds constitute special obligations payable solely from, and secured by a pledge of, net revenue of VIPA derived from the Rohlsen Terminal. In addition, net marine revenue is pledged for payment of the Rohlsen Terminal Bonds if revenue from the Rohlsen Terminal is not enough to meet the debt service requirements.

On January 16, 2003 VIPA issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable) with principal amounts of approximately $18.4 million and $17.4 million, respectively. VIPA is using the proceeds of the bonds to finance the dredging, rehabilitation, and construction of berthing piers for cruise and seagoing vessels on the island of St. Thomas and the construction of mixed used commercial facilities.

On October 20, 2003, the VIPA issued the Marine Revenue Bonds Series 2003C (non-AMT), in the amount of $3 million with an authorized principal amount not to exceed approximately $10.8 million. VIPA is using the proceeds of the bonds to finance the completion of several projects of rehabilitation and construction of berthing piers for cruise and seagoing vessels on the island of St. Thomas.

The revenue of the Airport System is not available for the payment of principal or interest on the Rohlsen Terminal Bonds; likewise, the revenue of the Marine Division and the Rohlsen Terminal are not available to pay Airport system obligations except for any surplus or marine revenue, which is available as designated by VIPA. Neither the credit of the Government nor any of its subdivisions or independent corporations is pledged or available for the payment of the principal or interest of the Bonds.

The bonds' indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance, and other costs as specified in the corresponding bond indentures.

Management of VIPA believes that VIPA has established the aforementioned required accounts and has complied with the contribution requirements with respect to the bonds. In addition, it is VIPA's management's opinion that VIPA has complied with limitations and restrictions imposed by the bonds' indentures.

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

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

Fixed maturities required to pay principal and interest on discretely presented component units' bonds payable with fixed maturities at September 30, 2004 are as follows (expressed in thousands):

	Principal	Interest	Total
Year:			
2005	$ 8,476	14,896	23,372
2006	8,850	14,815	23,665
2007	11,010	14,314	25,324
2008	11,555	13,782	25,337
2009	12,130	13,215	25,345
2010 – 2014	64,457	52,150	116,607
2015 – 2019	66,075	36,970	103,045
2020 – 2024	54,875	23,088	77,963
2025 – 2029	33,900	8,111	42,011
2030 – 2034	16,355	2,701	19,056
Total	287,683	$ 194,042	481,725
Plus unamortized premium	5,648		
Less unamortized discount	(876)		
Less deferred amount on debt refunding and reacquisition costs	(6,056)		
Bonds payable, net	$ 286,399		

(10) General Tax Revenue

For the year ended September 30, 2004, general tax revenue of the PG consisted of the following (expressed in thousands):

	General fund	PFA debt service fund	Other governmental funds	Total
Income taxes	$ 313,735	—	—	313,735
Real property taxes	48,007	—	16,000	64,007
Gross receipts taxes	—	112,387	250	112,637
Other taxes	98,067	40,062	1,998	140,127
Tax revenue	$ 459,809	152,449	18,248	630,506
Tax revenue not recognized on the modified accrual basis				34,004
Total tax revenue – government-wide				$ 664,510

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(11) Commitments and Contingencies

(a) *Primary Government*

The current labor relations environment of the Government is defined by 13 distinct labor organizations subject to approximately 26 collective bargaining agreements. Fourteen bargaining units are without collective bargaining agreements. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and nonprofessional workers in different departments throughout the Government, represented by different unions. Of the approximately 9,566 government workers, including employees of the executive branch of the Government, approximately 7,143 belong to unions. The present collective bargaining statute requires binding arbitration for certain classified employees in the event of an impasse during salary negotiations between the Government and any union. Under this process, each side chooses an arbitrator and a third impartial arbitrator is selected by the chosen arbitrators. The arbitration panel investigates and reviews the issues in dispute and renders a final and binding decision. For other classified employees, the Government must decide to go to impasse or to enjoin any strike. The Government has contractual liabilities for retroactive union arbitration salary increases aggregating $384 million accruing from fiscal years 1993 through 2004. Pursuant to Title 24 of the V.I. Code Section 374(h), no such contractual amount is due until appropriation of funds is made by the Legislature. Upon action of the Legislature, the General Fund will have the responsibility to satisfy the obligations arising from the retroactive wages. Until such time, the liability is recorded as a long-term debt in the governmental activities column in the government-wide financial statements. Retroactive union negotiated salaries account increased by $9 million from fiscal year 2003 to fiscal year 2004.

The Government receives financial assistance from the federal government in the form of loans, grants, and entitlements. Loans received are described in note 9(c). Monetary and nonmonetary federal financial assistance amounted to approximately $137.4 million and $19.8 million, respectively, for the year ended September 30, 2004.

Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially, all grants are subject to audit under OMB Circular A-133. Disallowances as a result of these audits may become liabilities of the Government. At September 30, 2004, based on an evaluation of pending disallowances, the Government has recorded approximately $6 million as other long-term liabilities in the governmental activities column of the government-wide financial statements.

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

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

condition for the Government to designate a third-party fiduciary to administer U.S. Department of Education grants. The terms and conditions of the original compliance agreement have been extended until the Government is in full compliance with the agreement.

The Government is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Title 33, Section 3411(c) of the V.I. Code, no judgment shall be awarded against the Government in excess of $25,000 for tort claims filed under Government statutes. In cases involving several survivors, each award must be construed separately for purposes of applying the limitation upon recovery imposed by the Tort Claims Act. Under Title 27, Section 166(e) of the V.I. Code, the Government's waiver of immunity is expanded to $250,000 for medical malpractice actions, including actions for wrongful death based on malpractice. Under certain circumstances, as provided in Title 33, Section 3414 of the V.I. Code, the Government may assume the payment of a judgment entered against an officer or employee acted reasonably and within the scope of his employment. The Government may pay up to a maximum amount of $100,000 of the settlement. With respect to pending and threatened litigation, the Government has accrued a provision for legal claims and judgments of approximately $15.2 million for awarded and anticipated unfavorable judgments as of September 30, 2004. Management believes that the ultimate liability in excess of amounts provided would not be significant.

Changes in the reported estimated litigation payable since September 30, 2002, resulted from the following activity (expressed in thousands):

		Beginning fiscal year liability	Current year claims and changes in estimates	Claim payments	Ending fiscal year liability
2002 – 2003	$	4,171	9,504	(440)	13,235
2003 – 2004	$	13,235	2,478	(538)	15,175

The breakdown of the estimated litigation payable at September 30, 2004 is as follows (expressed in thousands):

Governmental activities		
Current portion of estimated litigation payable	$	450
Long-term portion of estimated litigation payable		14,725
	$	15,175

As of September 2002, the Government was a defendant in a lawsuit regarding the assessment of property taxes. Under the lawsuit, taxpayers asserted that properties should be assessed at actual value in accordance with the Organic Act of 1933. The U.S. District Court agreed with the plaintiffs and, in May 2003, imposed an injunction on the collection of real property taxes for years subsequent to 1998. The Government complied with the Court order to develop a plan to implement the new valuation method, and the injunction was lifted in August 2003. Assessments will continue at the 1998 level until the new assessment method is in place.

State and federal laws and regulations require the Government to place a final cover on its landfill sites when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and post-closure care costs will be paid only near or after the date that the landfill stops accepting waste, the Government reports a portion of these closure and post-closure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The $28.8 million reported as landfill closure and post-closure care liability at September 30, 2004, represents the cumulative amount reported to date based on the use of the estimated capacity of each landfill. The Government will recognize the remaining estimated cost of closure and post-closure care of $9.6 million as the remaining estimated capacities are filled. These amounts are based on what it would cost to perform all closure and post-closure care in 2004.

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

Landfill	Estimated used capacity	Estimated closure date
Bovoni	57.41%	2020
Angilla	82.86	2009
Susannaberg	100	1993

Actual cost may be higher due to inflation, changes in technology, or changes in regulations. The Government is required by state and federal laws and regulations to make annual contributions to a trust to finance closure and post-closure care. The Government will begin to make annual contributions to a trust in 2006 to finance closure and post-closure costs. The Government expects that future inflation costs will be paid from interest earnings on these annual contributions. However, if interest earnings are inadequate or additional post-closure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), these costs may need to be covered by charges to future landfill users.

Since 1985, the Government has been subject to a consent decree issued by the Virgin Islands District Court, governing the operation of its wastewater treatment plants. The consent decree was amended in 1996 and further modified with the 2002 Stipulation to the Amended Consent Decree (the Stipulation) to establish deadlines for the construction of new secondary treatment facilities, including the replacement of the existing St. Croix and Airport Lagoon (Charlotte Amalie) wastewater treatment plants. The Stipulation requires that the new St. Croix wastewater treatment plants be completed by the end of 2005 and the new Charlotte Amalie wastewater treatment plants be completed by the end of 2006. The cost of both facilities is estimated at approximately $50 million. The Stipulation also establishes certain interim deadlines and performance standards that must be met by the Government pending completion of the new facilities. In addition, the Stipulation establishes specified penalties for violation of any of the deadlines or performance standards set forth therein. As of the date of the basic financial statements, the Government is current on all of its

outstanding obligations pursuant to the Stipulation. In January 2004, the Government's Legislature authorized the creation of the Virgin Islands Waste Management Authority (WMA) for the purpose of meeting environmental requirements of waste treatment in the U.S. Virgin Islands. On December 2004, the PFA issued revenue bonds amounting to $94 million for the purpose of constructing and rehabilitating wastewater treatment plants noted above. The bond proceeds will be administered by WMA.

On August 21, 2002, the Government and the United States Environmental Protection Agency (EPA) entered into a memorandum of understanding documenting the EPA's agreement to support the renewal of the Territorial Pollutant Discharge Elimination System permit for its St. Croix distillery operations provided that the Government make certain funding available to (i) conduct treatability studies regarding the Virgin Islands Rum Industries, Ltd. effluent and the means to mitigate its potential environmental effects in the vicinity of the discharge, (ii) identify practicable, available, reliable, and cost-effective potential mitigation measures, and (iii) implement (or assist in the implementation of) such mitigation measures in the event such measures are determined by the V.I. Department of Planning and Natural Resources after consultation with EPA to be necessary and appropriate. Pursuant to the memorandum of understanding, the Government's obligation to fund such activities is limited to $6 million in the aggregate, commencing on October 13, 2003. In June 2004, the Government entered into a three years contract with a locally licensed environmental consulting firm to facilitate the Government's commitments with the memorandum of understanding with the EPA.

As of September 2004, the Government was a defendant in a lawsuit regarding the assessment of franchise taxes. Under the lawsuit, taxpayers asserted that franchise taxes should be assessed in accordance with Title 13 Virgin Islands Code Section 531(a). The plaintiff taxpayers interpret the definition of "capital stocks used in conducting business in the Virgin Islands" in the V.I. Code as tax collected only on the par value of the stock, while the Government's position is that the amount allocated should be over the par value and additional paid-in capital upon a subsequent reorganization. The Government also imposed a six-year statute of limitations on tax refund claims against the Government. Management believes that the ultimate liability of this case would not have a material adverse impact on the Government's overall financial position as reported in the government-wide financial statements.

(b) Discretely Presented Component Units

In September 1989, WAPA electric facilities were damaged by Hurricane Hugo. WAPA reconstructed the facilities with proceeds from insurance and FEMA. Subsequent to the receipt of funds, FEMA deobligated approximately $7.9 million in questioned costs. Approximately $2.6 million of these questioned costs related to an oil spill that was subsequently settled with FEMA. During 1998, WAPA submitted a second appeal for $4.4 million of the remaining questioned costs, and agreed to refund approximately $900 thousand. During 1999, FEMA denied the second appeal and formally closed the disaster claim. WAPA has recorded a liability for $5.3 million related to the questioned costs. FEMA has not made a formal request for repayment of the funds.

In September 1995, WAPA electric facilities were again damaged by a hurricane—Hurricane Marilyn. WAPA again reconstructed its facilities with proceeds from insurance and FEMA. In

March 1999, FEMA denied WAPA's claim for $8.9 million in remaining expenditures related to the reconstruction. WAPA reduced its claim to $5.7 million and is negotiating with FEMA regarding these remaining reimbursements. WAPA has not recorded any amounts related to this recovery pending final resolution.

In September 2004, WAPA electric facilities sustained damages amounting to $1.3 million due to Tropical Storm Jeanne. WAPA is pursuing recovery of these costs from FEMA.

WAPA estimates that capital expenditures in connection with continuing capital improvements will be approximately $37.6 million for the Electric System and $8.2 million for the Water System during the year ended June 30, 2005.

In August 2003, VIHA was declared to be in substantial default of its annual contributions contract with the U.S. Department of Housing and Urban Development. Due to the severity of the compliance violations, VIHA was placed in receivership. As of September 30, 2004, VIHA remained in receivership.

In July 2004, VIHA executed a memorandum of understanding with WAPA for the repayment of $4.16 million in overdue utility accounts. The terms of the memorandum call for monthly payments of $175 thousand with the remainder to be paid by December 2005.

In 2002, the Federal Aviation Administration (FAA) conducted an on-site wildlife evaluation of the St. Croix landfill, which is located next to the St. Croix airport. The FAA determined that the landfill posed an environmental and navigational threat to the airport due to flocks of birds that reside in the landfill area. The FAA may require VIPA to repay $9.3 million in federal grants and has refused further discretionary grants for the airport until VIPA shows progress toward closing the landfill. VIPA has negotiated a remediation plan with FAA to close the landfill within the next four years, to purchase parcels of land adjacent to the airport, and to provide maintenance to the surrounding area.

In connection with the purchase of lands adjacent to the airport, VIPA was awarded federal financial assistance in 2002 amounting to $8 million under a real property acquisition and relocation Program. VIPA is in noncompliance with certain federal requirements of the assistance program. Noncompliance with requirements of federal financial assistance programs may result in a refund of the funds granted. VIPA management believes that noncompliance instances should not materially affect VIPA's financial position.

In 2004, VIGHHFC entered into two agreements for the purchase of equipment. VIGHHFC paid 10% down on the equipment, with a balance due of $3.6 million for equipment purchased for the St. Thomas hospital and $2.5 million for equipment purchased for the St. Croix hospital.

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

(12) Retirement Systems

(a) Plan Description

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

The monthly annuity benefit payment is determined by applying a stipulated benefit ratio to the member's average compensation. Average compensation is determined by averaging the three highest years of salary the member earned within the last 10 years of service. The maximum annual salary that can be used in this computation is $65,000. The annuity payment to retirees 60 years or older increases by 1.5% of the original amount on July 1 of each year after the first year of payments.

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

(b) Funding Policy

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

The contributions required to fund GERS on an actuarial reserve basis are calculated periodically by the GERS actuarial consultant. The actuarial valuation as of September 30, 2001 indicates that the current combined statutory employer and employee contribution rates are not sufficient to meet the cost of GERS on an actuarial basis.

The Government's required contribution for the year ended September 30, 2004 was 14.5% of the member's annual salary. Since April 1, 1991, required member contributions are 8% of annual salary for regular employees, 9% for senators, and 10% for Act 5226 eligible employees. Through September 30, 2000, member contributions were refundable without interest upon withdrawal from employment before retirement. Subsequent to September 30, 2000, legislation was passed that provided for 4% annual interest on refunded contributions. The Government's contractually required contributions, actual contributions made, and percentage contributed to the plan for the years ended September 30, 2004, 2003, and 2002, are as follows (expressed in thousands):

	Contractually required contributions	Contributions made	Percentage contributed
2002	$ 50,595	50,595	100%
2003	51,588	51,588	100
2004	54,085	54,085	100

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

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

For employees electing to retire under Section 8(b) of the Act, the Government contributes to GERS a sum equal to the additional contribution the employer and employee would have made had the employee received a salary 4% higher during the three years used to compute the employee's average compensation figure plus a sum of $5,000. Based on this calculation, the amount was $24.8 million as of September 30, 2004. As of September 30, 2004, GERS has received $17.6 million of such amount.

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

The University has two retirement plans in which all eligible employees are required to participate. The Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) is a defined-contribution pension plan covering participating, full-time faculty members and other exempt employees, under which the contributions, including employees' contributions, are used to purchase annuities. There are no unfunded past service costs, and vested benefits are equal to the annuities purchased under TIAA-CREF. As of September 30, 2004, 213 faculty members and other employees were TIAA-CREF participants. The number of active participants from the University

participating in GERS as of September 30, 2004 was 269. Total contributions made by the University to TIAA-CREF and GERS participant accounts amounted to $1.7 million and $1.1 million, respectively.

(13) Liquidity

At September 30, 2004, the Government had a net deficit in the governmental activities amounting to $328.2 million, mostly attributable to approximately $268 million in long-term debt that was issued to provide resources for working capital and other noncapital related purposes. The Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, engaging a consulting firm to assist it in its efforts to develop a series of detailed revenue enhancement and expenditure reduction initiatives and the enactment of certain laws directed toward improving the Government's financial situation. In October 1999, the Government and the U.S. Department of Interior (DOI) entered into a memorandum of understanding (the MOU) whereby the Government agreed to use its best efforts to undertake certain deficit reduction initiatives. As a condition to certain new and additional federal financial and technical assistance included in or being proposed by federal appropriations or other legislation, certain financial performance and accountability standards were agreed upon by the Government, which the DOI believes are necessary for the Government to achieve long-term economic recovery. Pursuant to the MOU, the release of such new and additional federal funds to the Government is subject to compliance with such performance and verifiable objectives agreed upon in such agreement. The accountability and financial performance standards agreed upon in the MOU include: (i) preparation of five-year financial recovery plan to be provided to DOI within 90 days of the date of the MOU; (ii) a fiscal year 2000 budget mandating substantial reductions in departmental budgets and overall General Fund fiscal year 2000 expenditures not to exceed $432.1 million; (iii) absent extraordinary circumstances to maintain balanced budgets after fiscal year 2003 with any generated surpluses applied to the reduction of the accumulated deficit and unfunded obligations; (iv) annual preparation of financial reports; and (v) efforts to reduce the outstanding debt of the Government. On October 29, 1999, the DOI and the Government entered into an amendment of the MOU, which amended the Government's requirement to seek change in the Virgin Islands public labor relations law to comply with federal labor law. Pursuant to such amendment, the Government, in collaboration with union representatives, is encouraged to pursue reform initiatives through collective bargaining to bring fiscal solvency to the Government. In addition to the financial performance standards set forth in the MOU, the MOU further provides for the DOI and the Government to enter into a program of preservation and enhancement of the natural, cultural, and historic resources of the U.S. Virgin Islands to stimulate local economic growth through sustainable tourism. The Government is discussing with DOI certain events of noncompliance, remedial actions necessary to comply with the provisions of the MOU, and its effect on the Government's financial condition and results of operations.

In April 2000, the Economic Recovery Task Force submitted the five-year operating and strategic financial plan to the Governor for action. The plan provides over 200 recommendations that propose to reduce and eventually eliminate the structural budget deficit by restructuring and reforming Government operations and forging a partnership with the private sector intended to result in sustained growth.

In January 2003, the U.S. Department of Interior issued an audit report concluding that all criteria of the (the proposed MOU) were partially or substantially achieved except: (i) implementation of collective bargaining reforms to assist the fiscal solvency of the Government and (ii) completion of comprehensive annual reports within 120 days of year-end and single audits within nine months of year-end. As part of the MOU, the Government has committed to maintaining balanced budgets after the fiscal year ended September 30, 2003, with any surpluses applied to liquidating outstanding debt. The U.S. Department of Interior acknowledged that it had not achieved its objective of providing funding for the V.I. Conservation Fund and committed to providing funds for capital improvements, technical assistance, and other assistance once the Government has achieved substantial compliance.

The DOI and the Government are currently negotiating a proposed memorandum of understanding (the proposed MOU) regarding the fiscal and economic recovery of the Government to supersede the existing MOU. The proposed MOU is expected to provide standards of financial performance and accountability to guide the Government in developing and implementing its fiscal and economic recovery program and in achieving a balanced budget. The proposed MOU is expected to set forth the goals and commitments of the DOI with respect to additional federal financial and technical assistance that may be required to achieve the fiscal and economic objectives under the proposed MOU.

(14) Restatements of Net Assets and Fund Balances

(a) Adoption of New Accounting Standard

Effective October 1, 2003, the PG and its component units adopted the provisions of GASB Statement No. 39, *Determining Whether Organizations Are Component Units*. In adopting this statement, UVI included the Reichhold Foundation for the Arts and the Virgin Islands Research and Technology Park into its audited financial statements. The beginning net assets of UVI increased by $3.2 million due to the inclusion of these entities. Beginning net assets of the component units have been restated as follows (expressed in thousands):

Beginning net assets, as previously reported	$	629,102
Restatement – UVI		3,221
Beginning net assets as restated	$	632,323

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(b) Reclassification of the PFA Capital Projects Fund as a Major Fund

The following table illustrates the change to fund balances at the beginning of the year, as previously reported, in the statement of revenue, expenditures, and changes in fund balances – governmental funds. The change is due to the reclassification of the PFA capital projects fund as a major fund. Previously, the PFA capital projects fund was reported in other governmental funds as a nonmajor governmental fund.

		Other governmental funds	PFA capital projects fund
Beginning fund balance, as previously reported	$	102,064	—
PFA capital projects fund		(43,062)	43,062
Beginning fund balance, as restated	$	59,002	43,062

(c) Inclusion of VI Lottery Financial Information

The following table summarizes the change in net assets at the beginning of the year in the statement of activities and statement of revenue, expenses, and changes in fund net assets – proprietary funds from the amounts previously reported. The change resulted from the inclusion of the VI Lottery (nonmajor enterprise fund) financial information as of and for the fiscal year ended September 30, 2004. Previously, this financial information had not been included because it was not available. The beginning net assets of the business type-activities and the other enterprise funds have been restated as follows (expressed in thousands):

		Business-type activities	Other enterprise funds
Beginning net assets, as previously reported	$	69,608	13,308
Inclusion of VI Lottery financial information		(3,138)	(3,138)
Beginning net assets, as restated	$	66,470	10,170

(15) Subsequent Events

(a) Primary Government

In October 2004, the excise tax on rum of 13.5 cents per gallon, which was scheduled to expire on December 31, 2003, was extended to December 31, 2005.

In October 2004, the President of the United States signed the American Jobs Creation Act, which changes the residency requirements and source of income requirements for U.S. territories and possessions, including the U.S. Virgin Islands. The PG retained an independent consultant to evaluate the effect of this legislation on the territorial economy and tax structure. The independent consultant's report was issued in February 2005 and concludes that the American Jobs Creation Act is detrimental to the economy of the U.S. Virgin Islands. In April 2005, the U.S. Department of the Treasury issued draft regulations for residency and source of income requirements for U.S. territories and possessions. In July 2005, the U.S. Department of the Treasury accepted testimony regarding the draft regulations. The PG provided testimony regarding the effect of the proposed regulations on the economy of the U.S. Virgin Islands.

In December 2004, the PFA issued the Series 2004A Internal Revenue Matching Fund Bonds in the amount of $94 million. The proceeds of the bonds will be used to finance the construction of two wastewater treatment plants to be built on the islands of St. Thomas and St. Croix, the rehabilitation of other wastewater facilities, and provide start-up capital for the newly created Virgin Islands' WMA. The Government has pledged rum excise tax matching funds for the repayment of the bonds.

In July 2005, the PFA issued $7.5 million in revenue notes to finance the acquisition of a fleet of police vehicles for the PG and to pay the costs of issuance of the notes.

In September 2005, the U.S. Department of Education extended indefinitely the three-year compliance agreement entered into with the PG in 2002 to address problems in administering federal education grants; and imposed the requirement that the PG designate a third-party fiduciary to administer U.S. Department of Education grants.

(b) Component Units

In March 2005, UVI's board of trustees approved a resolution authorizing the issuance of a one-time payout of 100% of merit earned for fiscal years 2001 – 2004 and the balance of the merit accumulation through fiscal year 2000. The payout amount of $2.7 million was disbursed in April 2005.

As authorized with the passage of Act No. 6638 by the Government's Legislature in January of 2004, WMA was created in June 2005 as a separate and independent corporation of the Government for the purpose of meeting environmental requirements of waste treatment in the U.S. Virgin Islands. The responsibility for the operations of WMA is vested in a board of seven directors composed of three Government officials including the Commissioner of the Department of Public Works, and four private citizens appointed by the Governor. The activities of WMA are limited to activities conducted on behalf of the Government. In December 2004, PFA issued revenue bonds amounting to $94 million for the purpose of constructing and rehabilitating wastewater treatment plants, as authorized by Act No. 6663. The bond proceeds will be administered by WMA.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Basic Financial Statements

September 30, 2003

(With Independent Auditors' Report Thereon)

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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KPMG LLP
American International Plaza
Suite 1100
250 Muñoz Rivera Avenue
San Juan, PR 00918-1819

Independent Auditors' Report

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

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government) as of and for the year ended September 30, 2003, which collectively comprise the Government's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Government's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following component units:

- The Virgin Islands Public Finance Authority (PFA), a blended component unit, which represents 100% of the assets, fund balance, and revenue of the PFA Debt Service Fund (a major fund); 100% of the assets, net assets, and revenue of the West Indian Company (a major fund); 3.73%, 4.36%, and 0.24% of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information; 18.8%, 43.4%, and 15.3% of the assets, net assets, and revenue of the governmental activities; and 51.1%, 35.9%, and 31.6% of the assets, net assets, and revenue of the business-type activities, respectively.
- The Tobacco Settlement Financing Corporation, a blended component unit, which represents 0.99%, 1.22%, and 0.09%, respectively, of the assets, fund balance, and revenue of the aggregate remaining fund information, and 1.4%, 4.6%, and 0.22% of the assets, net assets, and revenue of the governmental activities.
- The Virgin Islands Port Authority, Virgin Islands Water and Power Authority, Virgin Islands Housing Authority (VIHA), University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Economic Development Authority, Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority (VIHFA), discretely presented component units, which collectively represent 100% of the assets, net assets, and revenue of the aggregate discretely presented component units.

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

Except as discussed in the following seven paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

The Government did not maintain accounting records for corporate income tax receivables related to tax year 2002. Corporate income tax receivables amounting to $44.6 million in the general fund and governmental activities as of September 30, 2003, excludes receivables pertaining to tax year 2002. It was impracticable to extend our procedures sufficiently to determine the extent to which the general fund and the governmental activities as of and for the year ended September 30, 2003 may have been affected by these conditions.

The report of the other auditors on the 2002 financial statements of VIHA, a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence as to the proprietary of the revenue and expenses reported by VIHA, or to determine whether capital assets amounting to $71 million were fairly stated. In addition, the report was also qualified because VIHA did not report an equity interest in a joint venture because it had not been able to determine its carrying value. Total revenue and expenses reported for the year ended December 31, 2002 amounted to $55.5 million and $59.6 million, respectively.

The report of the other auditors on the 2003 financial statements of the VIHFA, a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether land held for sale amounting to approximately $25 million was fairly stated.

The basic financial statements do not include a receivable for unemployment insurance contributions in the unemployment insurance fund (a major fund) and the business-type activities as of September 30, 2003 due to inadequate records. The Government's records do not permit, nor is it practicable to extend our auditing procedures sufficiently to determine the extent to which the unemployment insurance fund (a major fund) and business-type activities as of and for the year ended September 30, 2003 may have been affected by this condition.

The Government has not included the Virgin Islands Lottery Fund (the Lottery) in the basic financial statements. Accounting principles generally accepted in the United States of America require the Lottery to be presented as a nonmajor enterprise fund and financial information about the Lottery to be part of the business-type activities, thus increasing the assets, liabilities, revenue, expenses, and changes in net assets of the aggregate remaining fund information and business-type activities. The amount by which this omission would affect the assets, liabilities, net assets, revenue, and expenses of the business-type activities is not reasonably determinable.

The basic financial statements do not include a liability for workers' compensation claims. The Government's records do not permit, nor is it practical to extend our auditing procedures sufficiently to determine the extent by which the business-type activities as of and for the year ended September 30, 2003 may have been affected by this condition.

The Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), is not recording contributions pursuant to the Early Retirement Act of

The Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), is not recording contributions pursuant to the Early Retirement Act of 1994. If these contributions were accrued, contributions receivable and plan net assets would be increased by $9.8 million. Additionally, plan net assets would be increased by $1.4 million. During fiscal year 2003, GERS reappraised its real estate investments resulting in appreciation in value of approximately $25.4 million. We were not able to determine the portion of such appreciation that pertains to prior years. Finally, we were unable to obtain sufficient audit evidence through independent confirmation or other alternative procedures about (i) the bank overdraft balance reported by GERS with the Department of Finance of approximately $10.5 million in specially designated pooled accounts, and (ii) the reasonableness of amounts reported by GERS as due from the Department of Finance amounting to $523,000.

The basic financial statements do not include a provision for landfill closure and postclosure costs as required by accounting principles generally accepted in the United States of America. The effects of this departure from accounting principles generally accepted in the United States of America on the governmental activities have not been determined.

Because of the matters discussed in the sixth, seventh, and eighth paragraphs of this report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the business-type activities as of September 30, 2003, and the changes in financial position for the year then ended.

In our opinion, based on our audit and the report of other auditors, except for:

- the effects of not maintaining accounting records for corporate income tax receivables related to tax year 2002 in the general fund and governmental activities and not recording a provision for landfill closure and postclosure costs in governmental activities, as described in paragraphs three and ten above, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of the Government as of September 30, 2003, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America;

- the effects of not being able to determine the extent to which the unemployment insurance fund (a major fund) may have been affected by the exclusion of a receivable for unemployment insurance contributions due to inadequate records, as described in paragraph six above, the financial statements referred to above present fairly, in all material respects, the respective financial position of the unemployment insurance fund (a major fund) of the Government as of September 30, 2003, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America;

- the effects of VIHA not reporting an equity interest in a joint venture and the adjustments, if any, as might have been determined to be necessary, had the other auditors been able to (i) satisfy themselves as to the proprietary of the revenue and expenses of VIHA reported in the statement of activities for the year ended September 30, 2003, and (ii) obtain sufficient audit evidence to determine whether capital assets and land held for sale amounting to $71 million and $25 million in the financial statements of VIHA and VIHFA, respectively, were fairly stated, as described in paragraphs four and five above, the financial statements referred to above present fairly, in all material respects, the financial position of the discretely presented component units of the Government of the United States Virgin Islands as of September 30, 2003, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America; and

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- the effects of GERS not accruing contributions pursuant to the Early Retirement Act of 1994 as described in paragraph nine above and the adjustments, if any, as might have been determined to be necessary, had we been able to (i) obtain satisfactory evidence with respect to the cash overdraft with and amounts due from the Department of Finance, and (ii) allocate the appreciation in real estate investments between this and prior years, the financial statements referred to above present fairly, in all material respects, the financial position of the aggregate remaining fund information of the Government of the United States Virgin Islands, as of September 30, 2003, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Finally, in our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the PFA Debt Service Fund and the West Indian Company of the Government of the United States Virgin Islands as of September 30, 2003, and the respective changes in financial position and cash flows, where applicable, thereof, and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 5 through 14 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

May 6, 2005

Stamp No. 2056644 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

Introduction

The following discussion and analysis presents an overview of the financial position and activities of the Government of the United States Virgin Islands (the Government) as of and for the fiscal years ended September 30, 2003 and 2002.

Government-wide Financial Statements

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

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

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

Governmental Activities – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with the primary government (PG) fall into this category, including general government, public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.

Business-Type Activities – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Government include the operations of the unemployment insurance program and (ii) the West Indian Company (WICO). Both of these programs operate with minimal assistance from the governmental activities of the Government.

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

Fund Financial Statements

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

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

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

Governmental Funds

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

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

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The PFA Debt Service Fund accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by the Virgin Islands Public Finance Authority (PFA) on behalf of the Government.

Proprietary Funds

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

The unemployment insurance fund and the West Indian Company (WICO) fund are major proprietary funds.

The unemployment insurance fund is a federally mandated program to manage unemployment insurance.

The WICO fund accounts for the activities of WICO, that owns a port facility including a cruise ship pier, and manages a shopping mall and a rental complex.

Fiduciary Funds

The Government is the trustee, or fiduciary, for several agency funds.

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

Financial Analysis of the Government as a Whole

The primary government (PG) and its component units experienced an economic downturn following the slowdown of the U.S. economy in fiscal year 2002, and the events of September 11, 2001. As explained in note 13 to the basic financial statements, the Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, the development of a series of detailed revenue enhancement and expenditure reduction initiatives, and the enactment of certain laws directed toward improving the Government's financial situation. In fiscal year 2003, the PG reported the Community Disaster Loan (CDL) forgiveness of $127.2 million of principal and $32.1 million of interest. Prior to September 30, 2003, the Government had met all the federal requirements for Administrative Loan Cancellation of the 1996 CDL related to Hurricane Marilyn and had petitioned the Federal Emergency Management Agency (FEMA) for forgiveness of the principal and related accrued interest. The PG was advised on October 25, 2004 that FEMA had granted full forgiveness of the 1996 CDL.

Financial Analysis of the Primary Government

Total assets of the government as of September 30, 2003 and 2002 were $1.337 billion and $1.248 billion, respectively, an increase of approximately $89 million. Total liabilities as of September 30, 2003 and 2002 were $1.637 billion and $1.680 billion, respectively, a decrease of approximately $43 million.

For the year ended September 30, 2003, the PG net deficit of $300 million consisted of $245 million invested in capital assets, net of related debt; $148 million restricted by statute or other legal requirements and were not available to finance day to day operations of the government; and an unrestricted net deficit as of $693 million. For the year ended September 30, 2002, the PG net asset deficit of $432 million consisted of $201 million invested in capital assets, net of related debt; $225 million restricted by statute or other legal requirements and were not available to finance day to day operations of the government; and an unrestricted net deficit of $857 million. The reduction in the PG net deficit was primarily caused by the CDL loan forgiveness.

For the fiscal year ended September 30, 2003, the PG earned program and general revenue amounting to $854 million, and reported expenses of $888 million, resulting in an increase in the net deficit, before the special item and transfers, of $34 million. During the fiscal year ended September 30, 2003, the Government reported a special item of $159.3 million resulting from the forgiveness of the 1996 CDL resulting in an overall reduction in the net deficit of $125 million. For the fiscal year ended September 30, 2002, the PG earned program and general revenue amounting to $854 million, and reported expenses of $891 million, resulting in an increase in the net asset deficit of $37 million. In overall, revenue and expenses remained fairly stable in fiscal year 2003 when compared to fiscal year 2002. The change in net assets was primarily caused by the CDL loan forgiveness in fiscal year 2003. A summary of net assets (deficit) and changes in net assets (deficit) for the primary government follows:

Net Assets (Deficit) – Primary Government

September 30, 2003 and 2002

(In thousands)

	Governmental activities		Business-type activities		Total	
	2003	2002	2003	2002	2003	2002
Assets						
Current assets	$ 626,829	542,653	54,979	72,856	681,808	615,509
Capital assets	608,158	592,969	43,008	37,279	651,166	630,248
Other assets	3,211	1,975	553	497	3,764	2,472
Total assets	1,238,198	1,137,597	98,540	110,632	1,336,738	1,248,229
Liabilities						
Current liabilities	393,313	260,259	7,652	13,096	400,965	273,355
Other liabilities	1,214,576	1,386,136	21,280	20,324	1,235,856	1,406,460
Total liabilities	1,607,889	1,646,395	28,932	33,420	1,636,821	1,679,815
Net Assets						
Invested in capital assets, net of related debt	224,189	183,746	20,993	16,955	245,182	200,701
Restricted	105,633	166,257	42,464	58,786	148,097	225,043
Unrestricted (deficit)	(699,513)	(858,801)	6,151	1,471	(693,362)	(857,330)
Total net assets (deficit)	$ (369,691)	(508,798)	69,608	77,212	(300,083)	(431,586)

(Continued)

Changes in Net Assets (Deficit) – Primary Government

September 30, 2003 and 2002

(In thousands)

	Governmental activities		Business-type activities		Total	
	2003	2002	2003	2002	2003	2002
Revenue:						
Program revenue:						
Charges for services	$ 26,988	11,469	29,590	45,690	56,578	57,159
Operating grants and contributions	143,295	132,686		—	143,295	132,686
Capital grants and contributions	20,564	18,636		—	20,564	18,636
General revenue:						
Taxes	594,616	599,315		—	594,616	599,315
Interest and other	33,991	40,349	3,785	4,715	37,776	45,064
Other general revenue	1,577	1,263		—	1,577	1,263
Total revenue	821,031	803,718	33,375	50,405	854,406	854,123
Expenses:						
General government	350,600	335,084	—	—	350,600	335,084
Public safety	49,394	45,230		—	49,394	45,230
Health	97,243	96,473	—	—	97,243	96,473
Public housing and welfare	63,874	62,440	—	—	63,874	62,440
Education	186,293	168,809		—	186,293	168,809
Transportaion and communication	29,240	38,534	—	—	29,240	38,534
Culture and recreation	14,365	9,410	—	—	14,365	9,410
Interest on long-term debt	49,633	71,190	—	—	49,633	71,190
Unemployment insurance		—	19,664	22,276	19,664	22,276
West Indian Company	—	—	8,432	8,671	8,432	8,671
Lottery	—	—	—	14,054	—	14,054
Workmen's Compensation	—		8,922	7,426	8,922	7,426
Other business-type activities	—	—	10,521	11,676	10,521	11,676
Total expenses	840,642	827,170	47,539	64,103	888,181	891,273
Decrease in net assets before special item and transfers	(19,611)	(23,452)	(14,164)	(13,698)	(33,775)	(37,150)
Special item	159,271	—	—	—	159,271	—
Transfers	(1,379)	(1,294)	1,379	1,294	—	—
	157,892	(1,294)	1,379	1,294	159,271	—
Change in net assets	138,281	(24,746)	(12,785)	(12,404)	125,496	(37,150)
Net assets (deficit), beginning of year, as previously reported	(508,798)	(484,052)	77,212	89,616	(431,586)	(394,436)
Adjustments to beginning net assets	826	—	5,181	—	6,007	—
Net assets (deficit), end of year, as adjusted	$ (369,691)	(508,798)	69,608	77,212	(300,083)	(431,586)

(Continued)

The Virgin Islands Office of Management and Budget of the PG prepares an annual executive budget subject to approval by the Governor and the Legislature of the Virgin Islands. The executive budget is prepared on a budgetary basis similar to the cash basis of accounting. The executive budget includes only those funds that are subject to appropriation by law. More information regarding budgetary procedures is provided in note 3 of the basic financial statements. A summary of the budgetary report for the general fund of the PG, included on page 22 of the financial statements, follows:

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

Year ended September 30, 2003
(In thousands)

		Original budget	Amended budget	Actual	Variance
Total revenue	$	489,673	489,673	464,232	(25,441)
Total expenditures		581,367	630,022	564,050	65,972
Excess of expenditures over revenue		(91,694)	(140,349)	(99,818)	40,531
Other financing sources (uses)		99,925	199,925	174,803	(25,122)
Excess of revenue and other financing sources (uses) over expenditures	$	8,231	59,576	74,985	15,409

For fiscal year 2003, the PG realized a revenue variance ($25.4) million due to declining revenue following the 2002 recession. The PG realized a $66 million variance in expenditures due to control spending imposed by revenue shortfalls. The PG realized a $74.9 million variance in other financing sources due to the proceeds from long-term debt issuance of $100 million and transfers to other funds of ($25.1) million.

Capital Assets

Capital assets additions during fiscal years 2003 and 2002 amounted to $34 million and $38.7 million, respectively, for governmental activities and $7.5 million and $4.5 million, respectively, for business-type activities.

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

Capital Assets – Primary Government
(In thousands)

		Governmental activities		Business-type activities		Total	
		2003	2002	2003	2002	2003	2002
Land and improvements	$	188,109	187,187	5,358	5,375	193,467	192,562
Building and improvements		400,309	390,630	46,490	38,859	446,799	429,489
Machinery and equipment		69,788	63,438	2,585	3,310	72,373	66,748
Infrastructure		121,413	103,170	-	—	121,413	103,170
Construction in progress		4,046	5,544	722	1,119	4,768	6,663
Total assets		783,665	749,969	55,155	48,663	838,820	798,632
Less accumulated depreciation		(175,507)	(157,000)	(12,147)	(11,384)	(187,654)	(168,384)
Total capital assets	$	608,158	592,969	43,008	37,279	651,166	630,248

Debt Administration

The Government issues both general obligation bonds and revenue bonds. The Revised Organic Act [48 U.S.C. Section 1574 (b)(ii)] restricts the principal amount of general obligation debt which the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the U.S. Virgin Islands. Following is a summary of bonds outstanding as of September 30, 2003:

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Primary Government – Bonds Payable

(In thousands)

Bonds payable	Final maturity	Interest rates	Balance
1998 Series A, B, C, D, and E revenue and refunding bonds	2023	5.50% to 7.11%	$ 486,970
1999 Project revenue bonds	2005	6.25%	4,510
1999 Series A general obligation bonds	2010	6.50%	6,480
1999 Series A revenue bonds	2033	4.20% to 6.40%	287,875
2001 Series A tobacco bonds	2031	5%	22,645
2002 Series revenue bonds	2009	2.50% to 5.00%	18,645
Subtotal			827,125
Deferred amount on refundings			(3,080)
Bond premium			1,299
Bond discount			(10,001)
Bond accretion			(1,418)
Total			$ 813,925

Note 9 provides detailed information regarding all bonds of the territory.

During fiscal year 2003, the 2002 Series revenue bonds amounting to $21 million were issued. During fiscal year 2002, the Tobacco Settlement Financing Corporation, a blended component unit, issued the 2001 Series A, Term, and Serial Bonds amounting to $24 million.

The PG made bond principal payments on all outstanding general and special revenue bonds amounting to $24 million during fiscal year 2003, and $19 million during fiscal year 2002.

The Government's bonds carry insured ratings of "BBB" and "Aaa" from Standard and Poor's and Moody's Investors Services, respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained from the respective rating agency.

At September 30, 2003, the PG issued a bond anticipation note in the amount of $100 million in anticipation of the issuance of the 2003 Series A Bonds, which were issued in December 2003.

At September 30, 2002, the PG had an outstanding Community Disaster Loan amounting to $127.2 million and accrued interest of $32.1 million. The PG received notification of full forgiveness of the loan principal and interest on October 25, 2004, and reported the forgiveness in the fiscal year ended September 30, 2003 because all requirements for Administrative Loan Cancellation had been met as of September 30, 2003.

Other liabilities of the PG include:

Primary Government – Other Liabilities

September 30, 2003 and 2003

(In millions)

		2003	2002
Accrued compensated absences	$	52	54
Retroactive union arbitration liability		375	368
Accrued litigation		13	4
Accrued federal cost disallowances		13	19
Total other liabilities	$	453	445

Economic Condition and Outlook

The PG ended fiscal year 2003 with a deficit amounting to $300 million, of which $693 million relates to an unrestricted deficit. The PG is experiencing the combined challenge of revenue decreases and expenditure increases.

Revenue Decreases

The PG collects income tax revenue under the "mirror" income tax system. The Government's tax laws "mirror" the U.S. Internal Revenue Service (IRS) Code, Rules and Regulations.

New Tax Acts passed by U.S. Congress in fiscal year 2003 and 2002 had a negative impact on revenue due to changes in sourcing of revenue rules as defined for the US Virgin Islands, restrictions on residency rules, decreases in tax rates, expanded tax credits, and expanded tax deductions.

In connection with a real property tax case instituted against the PG in the U.S. District Court of the Virgin Islands, the Government was enjoined for a four-month period in fiscal year 2003 from appraising and assessing any real property taxes until it modified its system of appraisal to comply with certain court mandates. As a result, effective August 2003, it has been using the 1998 assessment value to issue tax bills and collect taxes, and expects to continue to do so until a new appraisal system is implemented which is intended to satisfy the court's decision, or the decision is reversed on appeal.

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

Congress passed legislation in October 2004, which changes the source of income requirements and residency requirements for tax reporting purposes in United States territories. The PG is assessing the effect of this legislation on the US Virgin Islands economy.

Expenditure Increases

The PG faces the challenge of carryforward expenditures from prior fiscal years and increasing expenditures in the current fiscal year. Carryforward expenditures consist mainly of retroactive salary increases, which accumulated following Hurricanes Hugo, Marilyn, and Bertha in the years of 1990 through 1998.

Current increasing governmental expenditures include: increased health insurance premiums, pharmaceutical premiums, unemployment insurance benefits, and salary expense.

In addition, the Government is still experiencing the impact of the general economic decline in the United States and the impact of the terrorist attacks on September 11, 2001.

Deficit Reduction Measures

The PG has implemented a number of deficit reducing measures including: (i) increasing of local taxes including the highway users tax and stamp tax; (ii) implementation of new local taxes including an excise tax on importation of personal goods and a petroleum tax; and (iii) exerting greater control of expenditures through the budgetary process.

Contacting the Government's Financial Management

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

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit)

September 30, 2003

(In thousands)

	Primary Government			
	Governmental activities	Business–type activities	Total	Component units
Assets:				
Cash and cash equivalents	$ 109,327	5,954	115,281	46,247
Investments	298,634	—	298,634	26,530
Receivables, net	169,216	3,522	172,738	51,549
Internal balances	1,606	(1,606)	—	—
Loans and advances	—	5,417	5,417	2,475
Due from component units	22,797	—	22,797	—
Note receivable	—	—	—	7,387
Due from primary government	—	—	—	5,231
Due from federal government	22,703	—	22,703	7,164
Inventories		435	435	20,933
Other assets	2,546	886	3,432	21,927
Restricted:				
Cash and cash equivalents	—	40,371	40,371	24,966
Investments	—	—	—	116,432
Other	—	—	—	119
Capital assets	608,158	43,008	651,166	722,096
Deferred expenses	3,211	553	3,764	12,535
Total assets	1,238,198	98,540	1,336,738	1,065,591
Liabilities:				
Current liabilities:				
Accounts payable and accrued liabilities	52,098	3,254	55,352	73,495
Tax refunds payable	75,761	—	75,761	—
Unemployment insurance benefits	—	3,663	3,663	—
Customer deposits	—	—	—	16,912
Due to primary government	—	—	—	22,797
Due to component units	5,231	—	5,231	—
Due to federal government	—	—	—	5,300
Interest payable	23,027	—	23,027	3,798
Deferred revenue	81,987		81,987	6,502
Other current liabilities	1,903	—	1,903	5,197
Due within one year:				
Loans payable	100,000	735	100,735	1,016
Bonds payable	22,694	—	22,694	7,994
Other liabilities	30,612	—	30,612	—
Noncurrent liabilities:				
Due in more than one year:				
Loans payable	—	21,280	21,280	4,384
Bonds payable	791,231		791,231	261,850
Other liabilities	423,345	—	423,345	27,244
Total liabilities	$ 1,607,889	28,932	1,636,821	436,489

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit), continued

September 30, 2003

(In thousands)

	Primary Government			
	Governmental activities	Business-type activities	Total	Component units
Net assets:				
Invested in capital assets, net of related debt	$ 224,189	20,993	245,182	534,190
Restricted for:				
Unemployment insurance	—	35,068	35,068	—
Debt service	102,782	—	102,782	—
Capital projects	2,851	—	2,851	—
Other purposes	—	7,396	7,396	66,038
Unrestricted (deficit)	(699,513)	6,151	(693,362)	28,874
Total net assets (deficit)	$ (369,691)	69,608	(300,083)	629,102

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities

Year ended September 30, 2003

(In thousands)

		Program revenue			Net (expense) revenue and changes in net assets			
					Primary government			
	Expenses	Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total	Component units
Functions:								
Primary government:								
Governmental activities:								
General government	$ 350,600	15,062	21,663	8,605	(305,270)	—	(305,270)	—
Public safety	49,394	869	10,865	—	(37,660)	—	(37,660)	—
Health	97,243	1,508	30,046	—	(65,689)	—	(65,689)	—
Public housing and welfare	63,874	2,132	42,787	—	(18,955)	—	(18,955)	—
Education	186,293	871	33,521	—	(151,901)	—	(151,901)	—
Transportation and communication	29,240	6,531	4,094	11,959	(6,656)	—	(6,656)	—
Culture and recreation	14,365	15	319	—	(14,031)	—	(14,031)	—
Interest on long-term debt	49,633	—	—	—	(49,633)	—	(49,633)	—
Total governmental activities	840,642	26,988	143,295	20,564	(649,795)	—	(649,795)	—
Business-type activities:								
Unemployment insurance	19,664	2,223	—	—	—	(17,441)	(17,441)	—
West Indian Company	8,432	9,950	—	—	—	1,518	1,518	—
Workmen's compensation	8,922	7,275	—	—	—	(1,647)	(1,647)	—
Other	10,521	10,142	—	—	—	(379)	(379)	—
Total business-type activities	47,539	29,590	—	—	—	(17,949)	(17,949)	—
Total primary government	888,181	56,578	143,295	20,564	(649,795)	(17,949)	(667,744)	—
Component units:								
Virgin Islands Housing Authority	59,607	3,258	46,395	5,885	—	—	—	(4,069)
Virgin Islands Port Authority	43,660	35,565	15,163	—	—	—	—	7,068
Virgin Islands Water and Power Authority:								
Electric system	129,994	134,459	—	349	—	—	—	4,814
Water system	30,505	26,395	—	485	—	—	—	(3,625)
University of the Virgin Islands	56,672	10,753	40,099	3,074	—	—	—	(2,746)
Other component units	118,999	56,359	47,271	7,816	—	—	—	(7,553)
Total component units	$ 439,437	266,789	148,928	17,609	—	—	—	(6,111)

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities, continued

Year ended September 30, 2003

(In thousands)

	Net (expense) revenue and changes in net assets			
	Primary government			
	Governmental activities	Business-type activities	Total	Component units
Total primary government and component units	$ (649,795)	(17,949)	(667,744)	(6,111)
General revenue:				
Taxes	594,616	—	594,616	—
Interest and other	33,991	3,785	37,776	10,299
Tobacco Settlement Rights	1,577	—	1,577	—
Special item – loan forgiveness	159,271	—	159,271	—
Transfers – internal activities of primary government	(1,379)	1,379	—	—
Total general revenue, special item, and transfers	788,076	5,164	793,240	10,299
Changes in net assets (deficit)	138,281	(12,785)	125,496	4,188
Net assets (deficit), beginning of year (as adjusted)	(507,972)	82,393	(425,579)	624,914
Net assets (deficit), end of year	$ (369,691)	69,608	(300,083)	629,102

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Balance Sheet – Governmental Funds

September 30, 2003

(In thousands)

Assets		General	PFA Debt Service	Other governmental funds	Total governmental funds
Cash and cash equivalents	$	72,647	—	36,680	109,327
Investments		102,201	128,571	67,862	298,634
Receivables (net of allowance for uncollectible):					
Taxes		150,976	11,969	—	162,945
Accrued interest and other		4,930		515	5,445
Due from:					
Other funds		4,378	—	11,842	16,220
Component units		22,797	—	—	22,797
Federal government		—	—	22,703	22,703
Other assets		—	—	2,546	2,546
Total assets	$	357,929	140,540	142,148	640,617
Liabilities and Fund Balances					
Accounts payable and accrued liabilities	$	38,512	—	13,586	52,098
Tax refund payable		75,761	—	—	75,761
Due to:					
Other funds		9,959	2,000	3,178	15,137
Component units		5,231	—	—	5,231
Deferred revenue		131,326	46,214	21,940	199,480
Other current liabilities		—	—	1,380	1,380
Total liabilities		260,789	48,214	40,084	349,087
Fund balances reserved for:					
Encumbrances		44,839	—	—	44,839
Debt service		—	92,326	10,456	102,782
Unreserved fund balance, reported in:					
General fund		52,301	—	-	52,301
Special revenue funds		—	—	47,586	47,586
Capital projects funds		—	—	44,022	44,022
Total fund balances		97,140	92,326	102,064	291,530
Total liabilities and fund balances	$	357,929	140,540	142,148	

Amounts reported for governmental activities in the statement of net assets (deficit) are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.		608,158
Bond issue costs are not financial resources and, therefore, are not reported in the funds.		3,211
Because the focus of governmental funds is on short-term financing, some assets, primarily tax receivables, will not be available to pay for current period expenditures. Those assets are offset by deferred revenue in the funds.		118,319
Interest on long-term debt is not accrued in the funds, but rather is recognized as an expenditure when due.		(23,027)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.		(1,367,882)
Deficit of governmental activities	$	(369,691)

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenditures, and Changes in Fund Balances
Governmental Funds

Year ended September 30, 2003

(In thousands)

		General	PFA Debt Service	Other governmental funds	Total governmental funds
Revenue:					
Taxes	$	421,371	141,442	28,204	591,017
Federal grants and contributions		—	2,921	160,938	163,859
Charges for services		19,907	—	7,081	26,988
Tobacco settlement rights		—		1,577	1,577
Interest and other		25,599	4,683	3,709	33,991
Total revenue		466,877	149,046	201,509	817,432
Expenditures:					
Current:					
General government		254,110	—	83,666	337,776
Public safety		42,291	—	5,742	48,033
Health		70,106	—	26,013	96,119
Public housing and welfare		31,935	—	31,939	63,874
Education		149,538	—	29,544	179,082
Transportation and communication		23,193	—	6,230	29,423
Culture and recreation		5,554	—	3,745	9,299
Capital outlays		—	—	34,022	34,022
Debt service:					
Principal		—	19,030	4,605	23,635
Interest		—	46,286	1,633	47,919
Bond issuance costs			1,625	—	1,625
Total expenditures		576,727	66,941	227,139	870,807
Excess (deficiency) of revenue over (under) expenditures		(109,850)	82,105	(25,630)	(53,375)
Other financing sources (uses):					
Bond anticipation note issued		100,000	—	—	100,000
Bonds issued		—	2,345	18,500	20,845
Transfers from other funds		96,251	5,299	18,148	119,698
Transfers to other funds		(18,148)	(80,501)	(22,428)	(121,077)
Premium on bonds issued		—	1,516	—	1,516
Total other financing sources (uses), net		178,103	(71,341)	14,220	120,982
Net change in fund balances		68,253	10,764	(11,410)	67,607
Fund balance, beginning of year		28,887	81,562	113,474	223,923
Fund balance, end of year	$	97,140	92,326	102,064	291,530

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2003

(In thousands)

Net change in fund balances – total governmental funds	$	67,607
Government funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		15,189
Tax revenue in the statement of activities that do not provide current financial resources are not reported as revenue in the funds.		3,599
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of the governmental funds. These transactions have no effect on net assets. This is the amount by which bond and loan proceeds of $120,845 exceeded principal retirement of $23,635 in the current period.		(97,210)
Forgiveness of FEMA loan that did not provide current financial resources to the governmental funds and, as such, is not reported as revenue in the funds.		159,271
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. This is the amount by which the increase in certain liabilities reported in the statement of net assets of the previous year exceeded expenses reported in the statement of activities that do not require the use of current financial resources.		(8,570)
Bond issue costs are expended in the governmental funds when paid, and are capitalized and amortized in the statement of activities. This is the amount by which current year bond issue costs exceeded amortization expense in the current period.		1,237
Bond premiums and discounts are reported as other financing sources and uses in the governmental funds when the bonds are issued, and are capitalized and amortized in the government-wide financial statements. This amount represents the capitalization of premiums on bonds issued during the current year of $1,516 and the additional net interest expense of $1,653 reported in the statement of activities related to the amortization of premiums and discounts during the current year.		(3,169)
Certain interest reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This amount represents the decrease in interest payable reported in the statement of net assets less the portion of accrued interest forgiven by FEMA and included with the loan forgiveness amount above.		327
Change in net assets of governmental activities	$	138,281

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2003

(In thousands)

		Original budget	Amended budget	Actual	Variance
Revenue:					
Taxes	$	458,207	458,207	421,371	(36,836)
Charges for services		9,796	9,796	19,907	10,111
Interest and other		21,670	21,670	22,954	1,284
Total revenue		489,673	489,673	464,232	(25,441)
Expenditures:					
Current:					
General government		134,903	150,862	243,984	(93,122)
Public safety		55,548	56,148	41,779	14,369
Health		91,787	98,787	69,692	29,095
Public housing and welfare		42,224	44,324	31,935	12,389
Education		183,006	183,006	148,436	34,570
Transportation and communication		56,286	78,902	22,040	56,862
Culture and recreation		17,613	17,993	6,184	11,809
Total expenditures		581,367	630,022	564,050	65,972
Excess of expenditures over revenue		(91,694)	(140,349)	(99,818)	40,531
Other financing sources (uses):					
Bond anticipation note issued		—	100,000	100,000	—
Transfers from other fund		105,500	105,500	92,951	(12,549)
Transfer to other fund		(5,575)	(5,575)	(18,148)	(12,573)
Total other financing sources (uses)		99,925	199,925	174,803	(25,122)
Excess of revenue and other financing sources (uses) over expenditures	$	8,231	59,576	74,985	15,409

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets – Proprietary Funds

September 30, 2003

(In thousands)

		Business-type activities – enterprise funds			
		Unemployment insurance	West Indian Company	Other funds	Totals
Assets:					
Current assets:					
Cash and cash equivalents	$	98	5,097	759	5,954
Receivables, net:					
Loans and advances		—	—	5,417	5,417
Accrued interest and other		—	1,666	1,856	3,522
Due from other funds		—	—	300	300
Inventories and other current assets		—	886	435	1,321
Total current assets		98	7,649	8,767	16,514
Noncurrent assets:					
Restricted cash and cash equivalents		38,633	1,738	—	40,371
Capital assets		—	35,851	7,157	43,008
Deferred expenses		—	553	—	553
Total noncurrent assets		38,633	38,142	7,157	83,932
Total assets		38,731	45,791	15,924	100,446
Liabilities:					
Current liabilities:					
Accounts payable and accrued liabilities		—	1,544	1,710	3,254
Due to other funds		—	1,000	906	1,906
Unemployment insurance benefits		3,663	—	—	3,663
Loans payable related to capital assets		—	735	—	735
Total current liabilities		3,663	3,279	2,616	9,558
Noncurrent liabilities:					
Loans payable related to capital assets		—	21,280	—	21,280
Total liabilities		3,663	24,559	2,616	30,838
Net assets:					
Invested in capital assets, net of related debt		—	13,836	7,157	20,993
Restricted		35,068	7,396	—	42,464
Unrestricted		—	—	6,151	6,151
Total net assets	$	35,068	21,232	13,308	69,608

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenses, and Changes in Fund Net Assets
Proprietary Funds

Year ended September 30, 2003

(In thousands)

		Business-type activities – enterprise funds			
		Unemployment insurance	West Indian Company	Other funds	Total
Operating revenue:					
Charges for services	$	2,223	9,950	17,417	29,590
Total operating revenue		2,223	9,950	17,417	29,590
Operating expenses:					
Cost of services		19,664	6,166	19,008	44,838
Depreciation and amortization		—	1,227	435	1,662
Total operating expenses		19,664	7,393	19,443	46,500
Operating (loss) income		(17,441)	2,557	(2,026)	(16,910)
Nonoperating revenue (expenses):					
Gain on sale of assets		—	218	—	218
Interest income		2,933	158	476	3,567
Interest expense		—	(1,039)	—	(1,039)
Total nonoperating revenue (expenses), net		2,933	(663)	476	2,746
(Loss) income before operating transfers		(14,508)	1,894	(1,550)	(14,164)
Transfers from other funds		—	—	2,379	2,379
Transfers to other funds			(1,000)	—	(1,000)
Change in net assets		(14,508)	894	829	(12,785)
Net assets, beginning of year (as adjusted)		49,576	20,338	12,479	82,393
Net assets, end of year	$	35,068	21,232	13,308	69,608

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Cash Flows – Proprietary Funds

Year ended September 30, 2003

(In thousands)

	Business-type activities – enterprise funds			
	Unemployment insurance	West Indian Company	Other funds	Total
Cash flows from operating activities:				
Receipts from customers and users	$ —	9,950	17,462	27,412
Receipts from employers	2,223	--	...	2,223
Payments to beneficiaries	(24,611)	—	—	(24,611)
Payments to suppliers and employees	—	(5,866)	(18,088)	(23,954)
Net cash (used in) provided by operating activities	(22,388)	4,084	(626)	(18,930)
Cash flows from noncapital financing activities:				
Transfers (to) from other funds	—	(500)	2,672	2,172
Net cash (used in) provided by noncapital financing activities	—	(500)	2,672	2,172
Cash flows from capital and related financing activities:				
Acquisition and construction of capital assets	—	(6,021)	(1,860)	(7,881)
Principal paid on long-term debt	—	(20,809)	—	(20,809)
Proceeds from issuance of long-term debt	—	22,500	—	22,500
Proceeds from sale of assets	—	614	—	614
Interest paid on long-term debt	—	(1,039)	—	(1,039)
Net cash used in capital and related financing activities	—	(4,755)	(1,860)	(6,615)
Cash flows from investing activities:				
Interest and dividends on investments	2,933	97	476	3,506
Net cash provided by investing activities	2,933	97	476	3,506
Net decrease (increase) in cash and cash equivalents	(19,455)	(1,074)	662	(19,867)
Cash and cash equivalents, beginning of year (as adjusted)	58,186	7,909	97	66,192
Cash and cash equivalents, end of year	$ 38,731	6,835	759	46,325
Reconciliation of operating income (loss) to net cash (used in) provided by operating activities:				
Operating (loss) income	$ (17,441)	2,557	(2,026)	(16,910)
Adjustments to reconcile operating income (loss) to net cash (used in) provided by operating activities:				
Depreciation and amortization	—	1,227	435	1,662
Change in assets and liabilities:				
Receivables, net	—	—	47	47
Deferred charges		71	—	71
Accounts payable and accrued expenses	—	229	918	1,147
Other liabilities	(4,947)	—	—	(4,947)
Net cash (used in) provided by operating activities	$ (22,388)	4,084	(626)	(18,930)
Reconciliation of cash and cash equivalents to the statement of net assets:				
Cash and cash equivalents	$ 98	5,097	759	5,954
Restricted cash and cash equivalents	38,633	1,738	—	40,371
Cash and cash equivalents at end of year on statement of cash flows	$ 38,731	6,835	759	46,325

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Fiduciary Net Assets – Fiduciary Funds

September 30, 2003

(In thousands)

	Pension trust funds	Agency funds
Assets:		
Cash and cash equivalents:		
Unrestricted	$ 138,175	—
Restricted	110	—
Investments	1,274,662	2,925
Receivables, net:		
Loans and advances	105,500	—
Accrued interest	3,967	—
Other	34,993	—
Due from other funds	523	—
Other assets	12,912	—
Total assets	1,570,842	2,925
Liabilities:		
Accounts payable and accrued liabilities	—	2,925
Cash overdraft with the Department of Finance	10,454	—
Cash overdraft with bank	5,593	—
Unsettled securities purchased	91,827	
Securities lending collateral	169,682	—
Line of credit	10,000	—
Other liabilities	7,510	—
Total liabilities	295,066	2,925
Net assets held in trust for employees' pension benefits	$ 1,275,776	—

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Changes in Fiduciary Net Assets

Year ended September 30, 2003

(In thousands)

		Pension trust funds
Additions:		
Contributions:		
Employer	$	51,588
Plan members		30,509
Total contributions		82,097
Investment income:		
Net appreciation of fair value of investments		131,112
Appreciation in Havensight Mall		25,398
Interest, dividends, and other, net		37,460
Real estate – rental income (net of related expenses)		3,096
		197,066
Less investment expense		5,000
Net investment income		192,066
Other income		2,598
Total additions		276,761
Deductions:		
Benefits paid		126,797
Refunds of contributions		2,894
Administrative and operational expenses		8,268
Total deductions		137,959
Change in net assets		138,802
Net assets, beginning of year		1,136,974
Net assets, end of year	$	1,275,776

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Notes to Basic Financial Statements

September 30, 2003

(1) Summary of Significant Accounting Policies

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

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

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

(a) *Financial Reporting Entity*

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

1. Blended Component Units

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

Virgin Islands Public Finance Authority

The Virgin Islands Public Finance Authority (PFA) was created as a public corporation and autonomous governmental instrumentality by Act No. 5365, the Government Capital Improvement Act of 1988, with the purpose of aiding the Government in the performance of its fiscal duties and in effectively carrying out its governmental responsibility of raising capital for essential public projects. Under the enabling legislation, PFA has the power, among other

(Continued)

matters, to borrow money and issue bonds and to lend the proceeds of its bonds to the Government or any governmental instrumentality. The powers of PFA are exercised by a board of directors consisting of the Governor (Chairperson), the Commissioner of Finance, the Director of the Office of Management and Budget, and two representatives of the private sector appointed by the Governor with the advice and consent of the Legislature. PFA activities are blended within the PG because it is so intertwined with the Government that, in substance, they are the same.

PFA has a component unit, the West Indian Company (WICO) which is presented as an enterprise fund in the Government's basic financial statements as further described in note (1)(d).

Tobacco Settlement Financing Corporation

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

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

Administrative Offices of Blended Component Units

Virgin Islands Public Finance Authority
2400 Honduras, 2nd Floor
St. Thomas, V.I. 00802

Tobacco Settlement Financing Corporation
2400 Honduras, 2nd Floor
St. Thomas, V.I. 00802

(2) Discretely Presented Component Units

The following component units, consistent with GASB No. 14, are discretely presented in the basic financial statements because of the nature of the services they provide and the Government's ability to impose its will. The component units are reported in a separate column to emphasize that they are legally separate from the PG and governed by separate boards.

Major Component Units

Virgin Islands Housing Authority

The Virgin Islands Housing Authority (VIHA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act

No. 903 on June 18, 1962 with the purpose of providing housing for low-income families. Up until August 2003, the powers of VIHA were exercised by a board of commissioners consisting of seven members as follows: the Commissioner of Housing and Community Renewal and six other members appointed by the Governor.

In August 2003, the U.S. Department of Housing and Urban Development (HUD) determined that because of the severity of compliance violations, VIHA was declared to be in substantial default of its annual contributions contract (ACC) dated July 12, 1996 with HUD. The VIHA was placed in receivership and HUD assumed possession of all assets, projects, and programs.

Given the nature of VIHA's operations and the significance of its relationship with the Government, management believes that its exclusion from the financial reporting entity would cause the Government's basic financial statements to be incomplete and misleading. Accordingly, VIHA continues to be reported as a major component unit of the Government even though the Government no longer appoints its commissioners.

University of the Virgin Islands

The University of the Virgin Islands (the University) was organized as an instrumentality of the Government under Act No. 852 of March 16, 1962, in accordance with Section 6(a) of the Revised Organic Act of 1954, as amended. The purpose of the University is the stimulation and utilization of the intellectual resources of the people of the U.S. Virgin Islands and the development of a center of higher education. The powers of the University are exercised by a board of trustees consisting of 17 members as follows: Chairman of the Board of Education, Commissioner of Education, and the President of the University, all serving as members ex officio, 10 other members appointed by the Governor with the advice and consent of the Legislature, two other members elected by the board of trustees, one representative of the student body, and another of the teaching faculty. The University was not organized as a self-sustaining entity and therefore, receives substantial financial and other support from the Government.

Virgin Islands Port Authority

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

Virgin Islands Water and Power Authority

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

Nonmajor Component Units

Virgin Islands Economic Development Authority

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

Magens' Bay Authority

Magens' Bay Authority (MBA) was created as a corporate instrumentality by Act No. 2085 on December 20, 1967, with the purpose of acquiring, improving, and operating parks and beaches. The powers of MBA are exercised by a board of directors consisting of the Governor and six members appointed by the board of directors.

Virgin Islands Government Hospital and Health Facilities Corporation

The Virgin Islands Government Hospital and Health Facilities Corporation (VIGHHFC) was created by Act No. 6012 on August 23, 1994 and became active on May 1, 1999. Its purpose is to provide healthcare services and hospital facilities to the people of the U. S. Virgin Islands. The powers of VIGHHFC are exercised by a board of directors consisting of 15 members as follows: the Director of the Office of Management and Budget, the Commissioner of Finance, and 13 other members appointed by the Governor with the advice and consent of the Legislature. The VIGHHFC is composed of the Roy L. Schneider Hospital located in St. Thomas and the Juan F. Luis Hospital and Medical Center located in St. Croix. Both entities issue separate audited financial statements.

Virgin Islands Housing Finance Authority

The Virgin Islands Housing Finance Authority (VIHFA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government by Act No. 4636 of October 20, 1981, with the purpose of stimulating low- and moderate-income housing construction and home ownership through the issuance of revenue bonds to obtain funds to be used for low-interest mortgage loans to qualified purchasers of

low- and moderate-income housing. The powers of VIHFA are exercised by a board of directors consisting of the Commissioner of the Department of Housing, Parks, and Recreation (the Chairman), the Director of the Office of Management and Budget, and three persons not employed by the Government appointed by the Governor with advice and consent of the Legislature.

Virgin Islands Public Television System

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

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

Administrative Offices

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

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

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

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

Virgin Islands Economic Development Authority
1050 Norre Gade #5
St. Thomas, V.I. 00802

Magens' Bay Authority
PO Box 10583
St. Thomas, V.I. 00802

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

Virgin Islands Housing Authority
42 Annas Retreat
St. Thomas, V.I. 00802

Virgin Islands Housing Finance Authority
210-3A Altona
Frostco Center Building
St. Thomas, V.I. 00802

All financial statements of the discretely presented component units have a fiscal year-end of September 30, 2003, except for WAPA and VIHA that have a year-end of June 30, 2003 and December 31, 2002, respectively.

(3) Fiduciary Component Units

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

Employees' Retirement System of the Government of the Virgin Islands

The Employees' Retirement System of the Government of the Virgin Islands (known as GERS) was created as an independent and separate agency of the Government with the purpose of administering the Government employees' defined benefit pension plan established as of October 1, 1959. The responsibility for the proper operation of GERS is vested in a board of trustees composed of seven members appointed by the Governor with the advice and consent of the Legislature.

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

Employees' Retirement System of the Government of the Virgin Islands
GERS Building, 3rd Floor
St. Thomas, V.I. 00802

(b) Government-wide and Fund Financial Statements

The government-wide financial statements (that is, the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the PG and its component units. For the most part, the effect of interfund activity has been removed from these statements.

Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the PG is reported separately from certain legally separate component units for which the PG is financially accountable. The statement of net assets presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes (i) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (ii) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenue are reported instead as general revenue.

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

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

Government-wide Financial Statements

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

Governmental Fund Financial Statements

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

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

Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements – The financial statements of the proprietary funds, fiduciary funds, and discretely presented component units are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

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

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

(d) Fund Accounting

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

Governmental Funds

The Government reports the following major governmental funds:

- ***General Fund*** The general fund is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- ***PFA Debt Service Fund*** – The PFA Debt Service Fund accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by PFA on behalf of the Government.

Proprietary Funds

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

- ***Unemployment Insurance Fund*** – The unemployment insurance fund accounts for the collection of unemployment assessments from employers in the U.S. Virgin Islands, and the payment of unemployment benefits to eligible unemployed recipients.
- ***West Indian Company*** – WICO, a component unit of PFA, accounts for the activities of a cruise ship pier and shopping mall complex on the island of St. Thomas.

Fiduciary Funds

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

- ***Pension Trust Fund Accounts*** – The pension trust fund accounts for the activities of the Employees' Retirement System of the Government of the Virgin Islands, which accumulates resources for pension benefit payments to qualified employees.
- ***Agency Fund*** – The agency fund is custodial in nature (assets equal liabilities) and does not involve measurement of the results of operations.

(e) Cash and Cash Equivalents

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

Cash equivalents of the discretely presented component units consist of demand accounts, money market accounts, certificates of deposit with maturities of not more than 90 days from the date of acquisition, short-term U.S. government and its agencies' obligations and repurchase agreements with a U.S. commercial bank maturing within three months and collateralized by U.S. government obligations. Cash and cash equivalents of the discretely presented component units are maintained in separate bank accounts, from those of the PG, in their own names.

(f) Investments

Title 33, Chapter 117 of the Virgin Islands Code (V.I. Code) authorizes the Government to invest in U.S. Government and agencies' obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. Investments are reported at fair value.

Investments in marketable equity securities in the pension trust fund are carried at quoted market values. Realized gains and losses on securities are determined by the average cost method. Investments in real estate are carried at appraised value to the extent available. Investments without appraisals are carried at cost.

(g) ***Receivables***

Tax receivables represent amounts owed by taxpayers for individual and corporate income taxes, gross receipts taxes and real property taxes. Tax revenue is recognized in the governmental fund financial statements when they become both measurable and available based on actual collections during the months subsequent to September 30.

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

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

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

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

(h) ***Inventories***

In governmental fund types, the costs of inventories are recorded as expenditures when purchased. The proprietary fund types and component units recognize an asset when the inventory is purchased and an expense when it is consumed. Inventories in proprietary fund types are primarily valued at the lower of cost or market using the first-in, first-out method.

(i) ***Restricted Assets***

Restricted assets in the PG and discretely presented component units are set aside primarily for the payment of bonds, notes, construction funds, and other specific purposes (see note 7).

(j) ***Capital Assets***

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

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

Capital assets purchased or acquired are carried at historical cost or normal cost. The normal costing method to estimate cost based on replacement cost indexed by a reciprocal factor of the price

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increase from the appraisal date to the actual or estimated acquisition date was used to estimate the historical cost of certain land, buildings, and building improvements because invoices and similar documentation was no longer available in certain instances. Donated capital assets are recorded at fair value at the time of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest costs are capitalized during the construction period only for business-type activities and various component units. The costs of routine maintenance and repairs that do not add value to the assets or materially extend asset lives are not capitalized.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the PG are depreciated on the straight-line method over the assets estimated useful lives. There is no depreciation recorded for land and construction in progress.

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

The Government chose the option available under GASB No. 34 to defer the recording of wastewater treatment facilities as information for this network of infrastructure assets was not available. These assets were deemed to be nonmajor relative to total infrastructure assets and are not reported.

(k) ***Tax Refunds Payable***

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

(l) ***Deferred Revenue***

Deferred revenue at the governmental fund level arises when potential revenue does not meet both the "measurable" and "available" criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Government has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Government has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized. Deferred revenue at the government-wide and proprietary fund levels arises only when the Government receives resources before it has a legal claim to them.

(m) Long-Term Debt

The liabilities reported in the government-wide financial statements include the Government's bonds, long-term notes, and other long-term liabilities including vacation, retroactive union arbitration salaries, legal claims, and noncurrent federal fund cost disallowances related to expenditures of federal grants. Bond premiums and discounts, losses incurred on bond refundings, and debt issuance costs are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premiums or discounts and deferred refunding losses. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, government fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Losses incurred on bond refundings are not recognized in the fund financial statements as the corresponding liability for the bonds is only recorded in the government-wide financial statements. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

(n) Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

(o) Net Assets

Net assets are reported in three categories:

- ***Invested in Capital Assets, Net of Related Debt*** – These consists of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets. Debt pertaining to significant unspent debt proceeds is not included in the calculation of invested in capital assets, net of related debt. The unspent portion of the debt is presented, net of the related debt, as restricted net assets for capital projects.
- ***Restricted Net Assets*** – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- ***Unrestricted Net Assets*** – These consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

(p) Postemployment Benefits

In addition to the pension benefits in note 12, the Government provides postretirement healthcare benefits, in accordance with the V.I. Code to all employees who retire from the Government on or after attaining age 55 with at least 30 years of service; except for policemen and firemen who can retire with at least 20 years of service. Currently, 5,042 retirees meet those eligibility requirements. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree and the Government. The Government contributes three-fourths of the healthcare benefits' premiums. During the year ended September 30, 2003, the cost of providing healthcare benefits amounted to approximately $18.9 million.

(q) Compensated Absences

The vacation policy of the Government provides for the accumulation of four, six, or eight hours for each full biweekly pay period depending on the time of entry into government service. At the beginning of each calendar year, vacation leave is limited to 480 hours (60 days). However, the excess of 480 hours is considered by GERS for service credit towards the employees' retirement. This vacation policy does not apply to professional educational personnel of the Virgin Islands Department of Education, who receive compensation during the school breaks. Upon retirement, an employee receives compensation for unused vacation leave at the employee's base rate pay. As of September 30, 2003, the Government had accrued compensated absences amounting to $52.4 million, including related benefits, of which $30.6 million was included in current liabilities in the government-wide financial statements.

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

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

(r) Interfund and Intra-entity Transactions

The Government has the following types of transactions among funds:

- ***Interfund Transfers*** – Legally required transfers that are reported when incurred as "operating transfers from" by the recipient fund, and as "operating transfers to" by the disbursing fund.
- ***Intra-entity Transactions*** – These are transactions between the PG and its component units, and among the component units. Transfers between the PG and its blended component units are reported as interfund transfers, except for transfers within the same fund type. Similarly, receivables and payables between the PG and its blended component units are reported as amounts due to, and due from other funds. Balances and transfers between the PG and

discretely presented component units (and among those component units) are reported separately.

(s) ***Risk Management***

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

The Government does not maintain accounting records in support of individual claim liabilities or for claims incurred but not reported (IBNR). Accordingly, workers' compensation claims are accounted for on a cash basis. As such, the basic financial statements do not include a liability for workers' compensation claims outstanding, including related IBNR, as of September 30, 2003.

Certain component units are exposed to various risks of loss related to their specialized operations, which are mitigated by purchasing commercial insurance.

(t) ***Future Adoption of Accounting Requirements***

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

Statement number		Adoption required in fiscal year
39	Determining Whether Certain Organizations Are Component Units – An Amendment of GASB Statement No. 14	2004
40	Deposit and Investment Risk Disclosures – An Amendment of GASB Statement No. 3	2005
42	Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries	2006
43	Financial Reporting for Postemployment Benefit Plans Other than Pension Plans	2007
45	Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions	2008
46	Net Assets Restricted by Enabling Legislation-an amendment of GASB Statement No. 34	2006

The impact of these statements has not yet been determined.

(u) ***Reclassifications***

The presentation of the separately issued financial statements of certain component units have been reclassified to conform to the account classifications used by the Government in the 2003 basic financial statements.

(v) ***Use of Estimates***

Management of the Government has made a number of estimates and assumptions relating to the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

(2) Component Units

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

- University of the Virgin Islands
- Virgin Islands Port Authority

- Virgin Islands Water and Power Authority
- Economic Development Authority
- Virgin Islands Public Television System
- Magens' Bay Authority
- Virgin Islands Government Hospital and Health Facilities Corporation
- Virgin Islands Housing Authority
- Virgin Islands Housing Finance Authority

Condensed financial information of all discretely presented component units follows (expressed in thousands):

Information on net assets		Virgin Islands Housing Authority	Virgin Islands Port Authority	Virgin Islands Water and Power Authority: Electric System	Virgin Islands Water and Power Authority: Water System	University of the Virgin Islands	Other entities	Total component units
Assets:								
Current assets	$	5,980	15,988	53,057	17,871	41,854	42,298	177,048
Due from primary government		—	746	—	—	4,338	147	5,231
Due from federal government		4,000	788	—	—	2,176	200	7,164
Restricted assets		278	29,668	80,143	8,586	10,942	11,900	141,517
Capital assets, net		71,021	251,033	170,193	50,132	42,596	137,121	722,096
Deferred expenses		—	1,858	9,752	925	—	—	12,535
Total assets		81,279	300,081	313,145	77,514	101,906	191,666	1,065,591
Liabilities and net assets:								
Current liabilities		9,133	10,806	44,208	7,277	10,174	24,306	105,904
Due to primary government		—	—	—	—	—	22,797	22,797
Due to federal government		—	—	5,300	—	.	—	5,300
Bonds payable		—	35,738	167,673	36,415	23,533	6,485	269,844
Loans payable			913	—	—	3,540	947	5,400
Other noncurrent liabilities		5,538	—	—	—	132	21,571	27,244
Total liabilities		14,671	47,457	217,181	43,692	37,379	76,109	436,489
Net assets:								
Invested in capital assets – net of related debt		71,021	235,320	64,371	14,642	22,986	125,850	534,190
Restricted		—	2,758	20,455	7,581	30,526	4,718	66,038
Unrestricted (deficit)		(4,413)	14,546	11,138	11,599	11,015	(15,011)	28,874
Total net assets	$	66,608	252,624	95,964	33,822	64,527	115,557	629,102

Information on statements of activities		Expenses	Program revenue: Charges for services	Program revenue: Operating grants and contributions	Program revenue: Capital grants and contributions		Total component units
Virgin Islands Housing Authority	$	59,607	3,258	46,395	5,885		(4,069)
Virgin Islands Port Authority		43,660	35,565	15,163			7,068
Virgin Islands Water and Power Authority:							
Electric system		129,994	134,459	—	349		4,814
Water system		30,505	26,395	—	485		(3,625)
University of the Virgin Islands		56,672	10,753	40,099	3,074		(2,746)
Other entities		118,999	56,359	47,271	7,816		(7,553)
Total activities	$	439,437	266,789	148,928	17,609		(6,111)
General revenue:							
Interest and other							10,299
Changes in net assets							4,188
Net assets, beginning of year							624,914
Net assets, end of year						$	629,102

(3) Stewardship, Compliance, and Accountability

(a) Budgetary Process and Control

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

Act No. 6587, approved on July 24, 2003, authorized the issuance of debt to finance vendor payments and tax refunds in an amount up to $100 million. On September 4, 2003, the PG issued $100 million in Bond Anticipation Notes to finance its working capital needs as provided in Act No. 6587 (see note 9).

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

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

(b) Budget/GAAP Reconciliation

The following schedule presents comparisons of the general fund legally adopted budget with actual data on a budgetary basis. Because accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of timing and entity difference in the deficiency of revenue and other financing sources over expenditures and other financing uses for the year ended September 30, 2003 is presented below (expressed in thousands):

Excess of revenue and other financing sources (uses) over expenditures – budget basis	$	74,985
Timing difference – change in encumbrances		(10,080)
Entity difference – deficiency of revenue and other financing sources over expenditures and other financing uses – activities with budgets not legally adopted		3,348
Excess of revenue and other financing sources (uses) over expenditures – GAAP basis	$	68,253

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

(c) Deficit Fund Equity

As of September 30, 2003, fund deficits exceeding 10% of the total assets were reported in the following funds (expressed in thousands):

Nonmajor governmental fund:		
Paternity and child support	$	11,649
Nonmajor proprietary fund:		
Reciprocal insurance fund	$	9,673

(4) Cash and Investments

By law, banks or trust companies designated as depository of public funds of the Government and its various agencies, authorities, and instrumentalities are to maintain corporate surety bond or pledge collateral satisfactory to the Commissioner of Finance to secure all governmental funds deposited.

At September 30, 2003, the PG and the discretely presented component units carrying amounts of cash and cash equivalents were covered by federal deposit insurance, corporate surety bonds, or by collateral held by the Government.

Legally authorized investments vary by fund, but generally include obligations of the United States or its States, Commonwealth of Puerto Rico, the Government of the U.S. Virgin Islands, or of any agency thereof, common and preferred stocks of any U.S. corporation, common and preferred stocks of any foreign corporation listed in any internationally recognized security exchange, certain bonds or other indebtedness issued by foreign governments or foreign corporations, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Specific bond indentures also provide investment requirements.

For the fiscal year ended September 30, 2003, the PG, discretely presented component units and fiduciary funds and has classified their investments into three risk categories. Category 1 includes investments that were insured or registered or for which the securities were held by a government entity, or its agent, in the entity's name and investments for which the entity has safekeeping responsibilities but no equity or ownership interest or control. Category 2 includes uninsured and unregistered investments for which the securities were held by the counterparty's trust department or agent in a government entity's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in a government entity's name. The investments of the PG and the discretely presented component units by custodial credit risk categories at September 30, 2003, were as follows (expressed in thousands):

Primary Government – Investments

	Category 1	Category 2	Category 3	Reported amount
Commercial paper	$ 107,752	—	—	107,752
Certificates of deposit	41,949	—	—	41,949
Federal Home Loan Bank	1,782	—	—	1,782
	$ 151,483	—	—	151,483
Investments not categorized:				
Mutual funds				147,151
Total investments				$ 298,634

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Discretely Presented Component Units – Investments

	Category 1	Category 2	Category 3	Reported amount
U.S. government and agency securities	$ 104,396	—	—	104,396
Common stocks	1,433	—	—	1,433
Corporate bonds	3,829	—	—	3,829
Certificates of deposit	1,237	—	3,141	4,378
Money market funds	138	—	—	138
Investment contracts	306	—	—	306
Mortgage-backed securities	—	5,496	—	5,496
Other investments	—	1,610	—	1,610
	$ 111,339	7,106	3,141	121,586
Investments not subject to classification:				
Mutual funds				21,376
Total investments				$ 142,962

The investment balance consists of the following:

Unrestricted	$ 26,530
Restricted	116,432
Total investments	$ 142,962

Fiduciary Funds – Investments

		Category		Reported
	1	2	3	amount
U.S. government and agency securities	$ 66,787	—	—	66,787
Corporate obligations	61,132	—	—	61,132
Foreign bonds	81,953	—	—	81,953
Certificates of deposit	2,925	—	—	2,925
Common stocks – U.S.	578,223	—	—	578,223
Common stocks – foreign	98,930	—	—	98,930
Collateralized debt obligations	142,535	—	—	142,535
	$ 1,032,485	—	—	1,032,485
Investments not categorized:				
Investments held by broker – dealers under security loans:				
U.S. government and agency securities				120,945
Common stocks – U.S.				30,730
Common stocks – foreign				18,008
Mutual funds				4,361
Real estate				71,058
Total investments				$ 1,277,587

The investment balance consists of the following:

Pension Trust funds	$ 1,274,662
Agency funds	2,925
Total investments	$ 1,277,587

The pension trust fund's investments in marketable securities are administered by several professional investment managers and are held in trust by a commercial bank in the name of GERS. The investments in marketable securities generated interest and dividend income of $26.4 million, which is reported in interest, dividends, and other, net in the accompanying statement of change in the fiduciary net assets. During the year ended September 30, 2003, GERS' investments (including gains and losses on investments bought and sold, as well as held during the year) (depreciated) appreciated in value as follows (expressed in thousands):

U.S. government and government-guaranteed obligations	$ (3,374)
Corporate bonds – U.S.	2,920
Corporate bonds – foreign	14,795
Common stocks – U.S.	94,797
Common stocks – foreign	17,654
Collaterized debt obligations	2,493
Mutual funds	1,827
Net appreciation of fair value of investments	$ 131,112

The Government's statutes permit GERS to participate in securities lending transactions, and GERS has, via a Securities Lending Authorization Agreement (the Agreement), authorized State Street Bank and Trust Company (the Custodian) to lend its securities to broker-dealers and banks pursuant to a form of loan agreement. Lent securities are collateralized with cash, securities issued or guaranteed by the U.S. government, or irrevocable bank letters of credit. The Government does not have the ability to pledge or sell collateral securities delivered absent a borrower default. No restrictions were imposed during 2003 as to the amount of loans the Custodian can make on behalf of the Government, and the Custodian indemnified the Government for losses attributable to violations by the Custodian of the "Standard of Care" clause described in the Agreement. There were no such violations during the fiscal year 2003. In addition, there were no losses during the fiscal year resulting from the default of the borrowers or the Custodian.

Loans are generally terminable on demand. The system may be exposed to off-balance sheet risk in the event a borrower is unable to meet its contractual obligation. The Custodian must receive collateral at a minimum of 102% of the market value of the security for domestic borrowers and 105% for foreign borrowers at the inception of the securities lending transaction. Such collateral should be kept at a minimum of 100% of the market value of the security for all borrowers throughout the outstanding period of the transaction. At September 30, 2003, approximately $165.7 million of U.S. government and agency securities, fixed income, and equity corporate securities were on loan. The cash collateral received with a corresponding liability of an equal amount, is recorded in the statement of fiduciary net assets. The cash collateral received on each loan was invested, together with the cash collateral of other lenders, in a collective investment pool. As of September 30, 2003, such investment pool had an average duration of 68 days and an average weighted maturity of 482 days. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral.

(5) Receivables

Receivables at September 30, 2003 consist of the following (expressed in thousands):

		General fund	PFA debt service fund	Other governmental funds	Total
Income taxes	$	102,058	—	—	102,058
Real property taxes		48,918	—	—	48,918
Gross receipts taxes		—	11,969	—	11,969
Tax receivables	$	150,976	11,969	—	162,945
Accrued interest and other current receivables	$	4,930	—	515	5,445
Other long-term receivables — tobacco taxes					826
Total receivables — government-wide					$ 169,216

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

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

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

Property taxes are levied each calendar year on all taxable real property located in the U.S. Virgin Islands. The revenue is recognized in the general fund and in the fiscal period for which the property tax was levied, provided the tax is collected within 60 days subsequent to fiscal year-end, unless the facts justify a period greater than 60 days.

The Office of the Tax Assessor is responsible for the assessment of all taxable real property. Noncommercial real property subject to taxation is reassessed once every five years and commercial real property subject to taxation is reassessed biannually. The Tax Assessor prepares an annual assessment roll

and schedule of collections for each parcel of real property that is used by the Department of Finance, as the basis for issuing tax bills to all taxpayers in the U.S. Virgin Islands.

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

For fiscal year 2003, property tax assessments were not issued until August 20, 2003, were due on or before October 31, 2003, and penalties were assessed if not paid by November 30, 2003. The delay in assessment was due to a District Court injunction imposed in connection with a property tax lawsuit. Assessments for 2003 were made at the 1998 level to comply with a District Court order.

For businesses with gross receipts of $120,000 per annum or less, gross receipts taxes are levied on an annual basis, based on 4% of gross receipts in excess of $5,000. Businesses with annual gross receipts greater than $120,000 and up to $150,000 are levied on a monthly basis, based on 4% of gross receipts in excess of $5,000 per month. Businesses with annual gross receipts of more than $150,000 lose the $5,000 monthly exemption and are levied on a monthly basis of 4% of gross receipts. The gross receipts tax is due within 30 calendar days following the last day of the calendar month collected.

Component unit receivables at September 30, 2003, consist of the following (expressed in thousands):

Utility receivable	$	28,541
Port fees		2,634
Students		2,960
Patients		17,022
Other		392
Total	$	51,549

Loans and advances receivable at September 30, 2003, consist of the following (expressed in thousands):

		Primary government business-type activities	Fiduciary funds pension trust	Component units
Mortgage loans	$	9,625	24,250	—
Personal loans		—	83,040	—
Other loans and advances		963	1,210	2,475
Subtotal		10,588	108,500	2,475
Less allowance for uncollectible accounts		(5,171)	(3,000)	—
Loans and advances, net	$	5,417	105,500	2,475

(6) Interfund Transactions

(a) Operating Transfers

Operating transfers constitute the transfer of resources from the fund that receives the resources to the fund that utilizes them. The most significant transfers to the general fund from other governmental funds include a $80.5 million transfer from the debt service fund representing tax revenue in excess of bond service requirements and a $14.8 million transfer from the nonmajor governmental funds primarily representing $12.0 million of property tax revenue in excess of debt service requirements and $2.0 million of transfers from the land bank fund, and $1 million from WICO related to payment in lieu of tax. Transfers to nonmajor governmental funds consisted of $11 million from the general fund to the VI Wastewater Fund to be used for the construction of a water treatment plant and $3.5 million to the Emergency Molasses Fund to be used for molasses subsidies provided to local rum producers.

Interfund transfers for the year ended September 30, 2003 consisted of the following (expressed in thousands):

Transfer to		General fund	PFA Debt Service fund	Nonmajor governmental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Total
General fund	$	—	80,501	14,750	1,000	—	96,251
PFA Debt Service fund		—	—	5,299	—	—	5,299
Nonmajor governmental		18,148	—	—	—		18,148
Nonmajor enterprise		—	—	2,379	—	—	2,379
Total	$	18,148	80,501	22,428	1,000	—	122,077
Transfer from							
General fund	$	—	—	18,148	—	—	18,148
PFA Debt Service fund		80,501	—	—	—	—	80,501
Nonmajor governmental		14,750	5,299	—	—	2,379	22,428
Enterprise fund – West Indian Company		1,000	—	—	—	—	1,000
Total	$	96,251	5,299	18,148		2,379	122,077

(b) Due From/To Other Funds

The following table summarizes interfund receivables and payables at September 30, 2003 (expressed in thousands):

Due to		General fund	PFA Debt Service fund	Nonmajor govern-mental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Pension trust fund
General fund	$	—	—	3,178	1,000	200	—
Nonmajor governmental		9,136	2,000	-	—	706	—
Total governmental funds		9,136	2,000	3,178	1,000	906	—
Proprietary fund – nonmajor enterprise		300		—	—	—	—
Fiduciary funds – pension trust fund		523	—	—	—		—
Total	$	9,959	2,000	3,178	1,000	906	
Due from							
General fund	$	—	—	9,136	—	300	523
PFA Debt Service fund		—	—	2,000	—	—	—
Nonmajor governmental		3,178	—	—	—	—	—
Total governmental funds		3,178	—	11,136	—	300	523
Enterprise fund – West Indian Company		1,000	—	—		—	—
Nonmajor enterprise		200		706	—	—	—
Total proprietary funds		1,200	—	706	—	—	—
Total	$	4,378	—	11,842	—	300	523

The due from/to other funds include $4.9 million due from the general fund to the Emergency Molasses Fund (nonmajor governmental fund) from unpaid appropriations. Other balances composing the due from/to other funds include $2.7 million from the Bond Proceeds Fund (nonmajor governmental fund) to the general fund, $1 million from WICO (nonmajor enterprise fund) to the general fund and $2 million from the PFA Debt Service Fund to PFA Operating Fund (nonmajor governmental fund).

The due to PG balance reported by the discretely presented component units is composed of $18.6 million due from VIGHHFC and $4.2 million due from VIHFA, both discretely presented component units. These receivables exist because a portion of payroll expenditures that the Government processes are ultimately the responsibility of these component units. The due from PG reported by the discretely presented component units is mainly composed of $4.3 million and $746 thousand due to the University and VIPA, respectively.

(7) Restricted Assets

(a) Primary Government

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

Restricted Assets – Proprietary Funds and Business-type Activities

Unemployment insurance funds	$	38,633
WICO debt service funds		1,738
Total restricted assets of proprietary funds and business-type activities	$	40,371

(b) Component Units

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

Restricted Assets – Component Units

Debt service and sinking fund requirements	$	14,935
Construction funds		84
Endowment funds		4,958
HUD project funds		278
Revolving loan funds		4,560
Other		151
Total cash and cash equivalents		24,966
Investments:		
Debt service and sinking fund requirements		42,694
Construction funds		54,765
Endowment funds		5,984
Renewal and replacement funds		5,883
Revolving loan funds		7,106
Total investments		116,432
Other:		
Accrued interest receivable		119
Total restricted assets of component units	$	141,517

(8) Capital Assets

(a) *Primary Government*

The capital assets activity for the governmental-type activities funds for the year ended September 30, 2003, is summarized as follows (expressed in thousands):

	Beginning balance	Additions	Reductions	Ending balance
Capital assets, not being depreciated:				
Land	$ 183,630	895	—	184,525
Construction in progress	5,544	408	1,906	4,046
Total capital assets, not depreciated	189,174	1,303	1,906	188,571
Capital assets, being depreciated:				
Land improvements	3,557	27	—	3,584
Infrastructure	103,170	18,243	—	121,413
Buildings and improvements	390,630	9,679	—	400,309
Machinery and equipment	63,438	6,676	326	69,788
Total capital assets, being depreciated	560,795	34,625	326	595,094
Less accumulated depreciation for:				
Land improvements	1,307	187	—	1,494
Infrastructure	8,990	4,468	—	13,458
Buildings and improvements	114,487	6,653	—	121,140
Machinery and equipment	32,216	7,420	221	39,415
Total accumulated depreciation	157,000	18,728	221	175,507
Total capital assets, being depreciated, net	403,795	15,897	105	419,587
Governmental-type activities capital assets, net	$ 592,969	17,200	2,011	608,158

Capital assets activity for the business-type activities for the year ended as of September 30, 2003, is summarized as follows (expressed in thousands):

	Beginning balance (as adjusted)	Additions	Reductions	Ending balance
Capital assets, not being depreciated:				
Land and land improvements	$ 5,375	—	17	5,358
Construction in progress	1,119	—	397	722
Total capital assets, not depreciated	6,494	—	414	6,080
Capital assets, being depreciated:				
Buildings and improvements	38,859	7,631	—	46,490
Machinery and equipment	2,451	249	115	2,585
Total capital assets, being depreciated	41,310	7,880	115	49,075
Less accumulated depreciation for:				
Buildings and improvements	7,430	1,104	—	8,534
Machinery and equipment	3,189	558	134	3,613
Total accumulated depreciation	10,619	1,662	134	12,147
Total capital assets, being depreciated, net	30,691	6,218	(19)	36,928
Business-type activities capital assets, net	$ 37,185	6,218	395	43,008

Depreciation and amortization expense was charged to functions/programs of the PG for the year ended September 30, 2003, as follows (expressed in thousands):

Governmental activities:		
General government	$	4,255
Public safety		1,361
Health		1,124
Education		7,211
Transportation and communication		4,777
Total depreciation expense governmental activities	$	18,728
Business-type activities:		
WICO (major enterprise fund) – depreciation and amortization	$	1,227
Nonmajor enterprise funds – depreciation		435
Total depreciation and amortization- business-type activities	$	1,662

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The capital assets activity for the discretely presented component units for the year ended September 30, 2003, is summarized as follows (expressed in thousands):

		Beginning balance	Additions	Reductions	Ending balance
Capital assets, not being depreciated:					
Land	$	77,677	16,112	—	93,789
Construction in progress		32,735	45,550	26,171	52,114
Total capital assets, not depreciated		110,412	61,662	26,171	145,903
Capital assets being depreciated:					
Buildings and improvements		1,109,609	27,293	14,067	1,122,835
Airport and marine terminal facilities		84,487	12,427	—	96,914
Personal property and equipment		85,145	6,015	857	90,303
Total capital assets being depreciated		1,279,241	45,735	14,924	1,310,052
Less accumulated depreciation:					
Buildings and improvements		(579,795)	39,642	2,407	(617,030)
Airport and marine terminal facilities		(57,195)	3,612	—	(60,807)
Personal property and equipment		(48,283)	8,496	757	(56,022)
Total accumulated depreciation		(685,273)	51,750	3,164	(733,859)
Total capital assets being depreciated, net		593,968	(6,015)	11,760	576,193
Component unit capital assets, net	$	704,380	55,647	37,931	722,096

Depreciation expense charged to each component unit for the year ended September 30, 2003 was as follows (expressed in thousands):

Virgin Islands Housing Authority	$	9,365
Virgin Islands Port Authority		12,947
Virgin Islands Water and Power Authority:		
Electric system		13,644
Water system		2,566
University of the Virgin Islands		3,707
Other component units		9,521
Total depreciation – component units	$	51,750

(9) Long-Term Liabilities

Long-term liabilities activities for the year ended September 30, 2003, were as follows (expressed in thousands):

	Beginning balance	Additions	Reductions	Debt forgiveness	Ending balance	Amounts due within one year	Amounts due thereafter
Governmental activities:							
Bonds payable:							
1998 Series Revenue and Refunding Bonds	$ 499,495	—	(12,525)	—	486,970	13,225	473,745
1999 Project Revenue Bonds	7,295	—	(2,785)	—	4,510	2,960	1,550
1999 General Obligation Bonds, Series A	7,260	—	(780)	·	6,480	830	5,650
1999 Series A Revenue Bonds	292,180	—	(4,305)	—	287,875	4,540	283,335
2001 Series A, Tobacco Bonds	23,685	·	(1,040)	—	22,645	—	22,645
2002 Series Garvee Bonds	—	20,845	(2,200)	·	18,645	2,805	15,840
Subtotal bonds payable	829,915	20,845	(23,635)		827,125	24,360	802,765
Less:							
Deferral on refundings	(3,696)	—	616	—	(3,080)	(616)	(2,464)
Bonds premium	—	1,516	(217)	—	1,299	217	1,082
Bonds discount	(10,949)	--	948	—	(10,001)	(948)	(9,053)
Bonds accretion	(1,723)	—	305	—	(1,418)	(319)	(1,099)
Total bonds payable, net	813,547	22,361	(21,983)	-	813,925	22,694	791,231
Loans payable:							
Bond Anticipation Note	-	100,000	—	—	100,000	100,000	—
Marilyn CDL	127,200	—		(127,200)	—	—	—
Total loans payable	127,200	100,000	—	(127,200)	100,000	100,000	—
Other liabilities:							
Accrued compensated absences	54,002	5,424	(7,068)	—	52,358	30,561	21,797
Retroactive union arbitration	368,512	6,740	—	—	375,252	—	375,252
Litigation	4,171	9,064	—	—	13,235	51	13,184
Accrued disallowed costs	18,704	—	(5,592)	—	13,112	-	13,112
Total other liabilities	445,389	21,228	(12,660)	—	453,957	30,612	423,345
Total governmental activities	$ 1,386,136	143,589	(34,643)	(127,200)	1,367,882	153,306	1,214,576
Business-type activities:							
Notes payable:							
WICO	$ 20,324	22,500	(20,809)	—	22,015	735	21,280
Fiduciary activities:							
Line of credit							
GERS Pension Trust	$ —	10,000	—	—	10,000	10,000	—

Accrued compensated absences, retroactive union arbitration liabilities, and litigation reserves are generally expected to be liquidated with resources derived from the general fund. Accrued disallowed costs are generally expected to be liquidated with resources derived from either the general fund or the grant funds.

(a) Debt Margin

Pursuant to 48 U.S.C. Section 1574(b)(i) of the Revised Organic Act, the Government may issue revenue bonds for public improvements or undertakings authorized by an act of the Legislature, without limitation as to principal amount. Such revenue bonds are payable solely from the revenue directly derived from and attributable to such public improvements or undertakings. Pursuant to 48 U.S.C. Section 1574(b)(ii), the Government is authorized to issue general obligation bonds for any public purpose provided that no such indebtedness is in excess of 10% of the aggregate assessed valuation of the taxable real property in the U.S. Virgin Islands. In addition, pursuant to 48 U.S.C. Section 1574a (Public Law 94-932), the U.S. Virgin Islands is authorized to cause to be issued bonds or other obligations in anticipation of the matching funds to be received from the federal government pursuant to 26 U.S.C. Section 7652(b)(3). There is no legal limit on the value of bonds that the Government may issue pursuant to 48 U.S.C. Section 1574a. The Legislature of the U.S. Virgin Islands must authorize all bond issuances. PFA is authorized to issue bonds for the purpose of financing any project or for the purpose authorized by the Legislature. Given that PFA's powers to issue bonds are derived from 48 U.S.C. Section 1574(b), the bonds issued by PFA are subject to the limitations of said 48 U.S.C. Section 1574(b). On August 23, 1999, the Legislature amended the V.I. Code to add a Mandatory Balanced Budget Provision. Such provisions, specifically Title 2 of the V.I. Code Section 256, provide that the amount of debt of the Government existing on October 1, 2000 shall be the debt limit of the Government, exclusive of bond principal and interest that may become due. The debt limit specified under Title 2 of the V.I. Code Section 256 does not include bonds authorized by law for which a specific source of revenue is identified and committed to retiring those bonds. As used in Title 2 of the V.I. Code Section 256, the term "debt" means the total accumulated unpaid obligations that are due and payable, including unpaid income tax refunds, amounts owed to vendors, and current year unpaid debt service obligations, if any. As used in the statute, the term "debt" does not include that portion of principal or interest on bonds that is not yet due and payable.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS
Notes to Basic Financial Statements
September 30, 2003

(b) Bonds Payable

Bonds payable outstanding at September 30, 2003, are comprised of the following (expressed in thousands):

Primary Government – Bonds Payable

Bonds payable	Final maturity	Interest rates	Balance
1998 Series A, B, C, D, and E revenue and refunding bonds	2023	5.50% to 7.11%	$ 486,970
1999 Project revenue bonds	2005	6.25%	4,510
1999 Series A general obligation bonds	2010	6.50%	6,480
1999 Series A revenue bonds	2033	4.20% to 6.40%	287,875
2001 Series A tobacco bonds	2031	5%	22,645
2002 Series revenue bonds	2009	2.50% to 5.00%	18,645
Subtotal			827,125
Less:			
Deferred amount on refundings			(3,080)
Bonds premium			1,299
Bonds discount			(10,001)
Bonds accretion			(1,418)
Total			$ 813,925

On May 1, 1998, PFA issued the revenue and refunding bonds series 1998 A, B, C, D, and E amounting to $541.8 million, secured by general obligation notes issued by the Government. These bonds were issued for the purpose of, among other things, advance refunding of previously issued bonds in order to obtain lower interest rates. The economic gain obtained by this advance refunding is the difference between the present value of old debt service requirements and the new debt service. This refunding resulted in a debt service saving of approximately $40 million and an economic gain of approximately $19 million.

The proceeds of the 1998 Series A and B Bonds were placed in an irrevocable trust account to provide for all future debt service payments on the Highway Revenue Bonds Series 1989, Series 1991, Series 1992, Series 1993, and Series 1994 Bonds. At September 30, 2003, $205.6 million of the above-mentioned defeased bonds were outstanding.

The proceeds of the Series 1992 Revenue Bonds were placed in an irrevocable trust to provide for all future debt service payments on the Series 1989 Revenue Bonds. At September 30, 2003, $171.6 million of defeased bonds were outstanding. All assets held by irrevocable trusts for refunding of prior outstanding debt and the corresponding liabilities are not included in the Government's basic financial statements.

The 1998 Series C Bonds and the 1998 Series D Bonds were issued to pay, on behalf of the Government, the full principal balance and interest due and payable on the Revenue Anticipation Note, issued in February 1998. The remaining balance of the 1998 Series D Bonds amounting to approximately $11.6 million was primarily provided to the Government for additional working capital. The net proceeds of the 1998 Series E Bonds amounting to $104 million were primarily designated to fund the construction of certain capital projects amounting to $94 million. The remaining $10 million was deposited in a debt service reserve account.

The U.S. Department of the Treasury makes certain transfers to the Government of substantially all excise taxes imposed and collected under the Internal Revenue laws of the United States in any fiscal year on certain products produced in the U.S. Virgin Islands (primarily rum) and exported to the United States from the Virgin Islands. The amount required to be remitted to the Government by the U.S. Department of the Treasury is an amount no greater than the total amount of local revenue (primarily taxes) collected by the Government in each fiscal year. As a result, the term "matching fund revenue" is used to denote these payments. The Government has pledged the matching fund revenue, as described above, to the timely payment of principal and interest on the 1998 Series A, B, C, D, and E Bonds. Thus, amounts to be received by the Government from federal excise taxes, mostly in rum, are deposited directly in a trust account until the 1998 Bonds are paid in accordance with the Indenture of Trust.

Estimated prepayments of matching fund revenue are made to the Government prior to the beginning of each fiscal year, subject to adjustment for the amount of local revenue actually collected by the U.S. Department of the Treasury during such year. Prepayments of matching fund revenue are recorded as deferred revenue in the accompanying statement of net assets and the balance sheet of the governmental funds and reversed against revenue in the following year. The adjustments for actual collections made to the estimated prepayments are recorded in the year determined.

In November 1999, the U.S. Congress approved an increase in the rate of federal excise taxes on rum transferred to the Government from $10.50 to $13.25 per proof gallon. The increase was retroactive to July 1999 and effective through December 31, 2003. In October 2004, Congress extended the $13.25 per proof gallon rate to December 31, 2005.

Interest on the revenue and refunding bonds series 1998 A, B, C, D, and E and 1999 bonds are payable semiannually on April 1 and October 1, and principal is payable annually on October 1. The Government is responsible for all principal and interest payments on the 1998 Series bonds. The principal due on October 1 and interest payments due on October 1 and April 1, are funded by the matching fund revenue and deposited into the debt service reserve accounts.

On April 13, 1999, a loan agreement was made between and among the Government, the PFA, International Business Machine Corporation (IBM), Banco Popular de Puerto Rico, and U.S. Trust Company of New York (Y2K Loan). The purpose of this loan was to finance certain costs of compliance by the Government with Year 2000 computer system issues. The loan was evidenced by the Government's issuance of General Obligation Bonds Series 1999 A amounting to $18 million. Principal and interest are payable semiannually on January 1 and July 1. On July 9, 2001, the Government paid the outstanding IBM portion of the bonds amounting to $7.4 million.

The Bonds are secured by the full faith and credit and taxing power of the Government, including a pledge on annual real property tax revenue from its taxation of the Hovensa Oil Refinery (the Refinery), which revenue is deposited in the Hovensa Property Tax Fund, and a contingent pledge of all franchise taxes on foreign sales corporations collected by the Government

(Franchise Tax Revenue). Pursuant to the Hovensa Oil Contract, the Refinery agreed to pay $14 million annually of real property taxes on the Refinery properties. Foreign sales corporations qualified to do business in the Virgin Islands must pay a franchise tax of $1.50 for each thousand dollars of capital stock issued (Franchise Tax).

On April 13, 1999, PFA also issued Project Revenue Bonds (the 1999 Project Revenue Bonds), amounting to $13.5 million on behalf of the Government, to finance a portion of the Government's Year 2000 (Y2K) compliance efforts, including the costs related to transportation, installation, and related hardware, software, consulting services, and related expenses. The 1999 Project Revenue Bonds are secured by lease payments made by the Government to PFA pursuant to a municipal lease purchase agreement, dated April 13, 1999. Such lease payments shall be funded by appropriation from the real property taxes deposited in the Hovensa Property Tax Fund and all franchise taxes on a subordinated basis and subject to any superior rights of the Series 1999 A General Obligation Bonds. The 1999 Project Revenue Bonds mature on January 1, 2005 with interest payable semiannually on January 1 and July 1.

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

The Government pledged gross receipts taxes for the timely payment of the principal and interest on the 1999 Series A Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. Gross receipts revenue amounted to $107.8 million for the year ended September 30, 2003.

On November 20, 2001, TSFC issued Tobacco Settlement Asset-Backed Bonds amounting to $21.7 million of the aggregate principal. The proceeds were used for the purpose of (i) purchasing all rights, title, and interest in certain litigation awards under the Master Settlement Agreement (MSA) entered into by participating cigarette manufacturers, (ii) issuance of Tobacco Settlement Asset-Backed Bonds to pay the purchase price for the rights, and (iii) to provide funds for hospital and healthcare projects in the U.S. Virgin Islands.

Interest on the 2001 bonds is payable semiannually on each May and November 15, beginning with May 2002 for the term bonds amounting to $15.5 million and convertible capital appreciation bonds amounting to $8.2 million, with a nominal value of $6.2 million.

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

Bonds payable at September 30, 2003, amounted to $23 million with accumulated accretion of $1.4 million. Under early redemption provisions, any MSA payments exceeding annual debt service requirements of the 2001 Series A Tobacco Bonds must be applied to early redemption of principal. MSA payments and interest earnings on the trust funds during the year ended September 30, 2003, resulted in early redemption of $1.04 million during fiscal year 2003.

On October 1, 2002, PFA issued the Series 2002 Revenue Bonds (Garvee Bonds), the proceeds of which amounted to $20.8 million. The Garvee Bonds are special, limited obligations, secured solely by the pledge and assignment of the Government's security interest in Federal Highway Reimbursement Revenues. The bonds were issued to (i) fund construction costs related to renovation and construction of two sea docks, (ii) fund the Debt Service Reserve Accounts, and (iii) pay certain costs of issuing the bonds. The Series 2002 Bonds are not subject to redemption prior to maturity.

Interest and principal on the Series 2002 Revenue Bonds are payable semiannually on March 1 and September 1. As of September 30, 2003, the outstanding 2002 Revenue Bonds amounted to $18.6 million.

On February 28, 2003, PFA entered into a swaption contract that provided PFA with an up-front payment of $8.3 million. PFA has outstanding $243,985,000 Series of 1999A Bonds with maturities from 2011 to 2029. The 1999A Bonds are callable by PFA on October 1, 2010 at 101%. Having been advised by its underwriters and financial advisor that there were no net present value savings available to it by issuing conventional advance refunding bonds, PFA sold a LIBOR-based swaption to Lehman Brothers Special Financing, Inc. on the 2024 and 2029 maturities, totaling $162,870,000. Lehman purchased the swaption for $8.3 million and it is exercisable on July 1, 2010 only. The objective of PFA was to monetize the economics of the Series of 1999A Bonds call option and lock in the favorable interest rates prevailing on February 28, 2003 without currently issuing refunding bonds. The swaption was the most efficient mechanism available to PFA to effect savings from the Series 1999A Bonds at that time. As a synthetic refunding of its 1999 Series A Bonds, this payment represents the risk-adjusted, present-value savings of the refunding as of October 1, 2010, without issuing refunding funds at February 2003. The swaption gave the counterparty the option to make PFA enter into a pay-fixed, receive-variable interest rate swap. If the option is exercised, PFA would then expect to issue variable-rate refunding bonds.

The up-front payment of $8.3 million was received by PFA on behalf of the primary Government. The Government has deferred the recognition of revenue from the $8.3 million received in advance, and is amortizing it into income using the straight-line method which approximates the effective-interest method through October 1, 2010 which is the exercise date of the swaption. The proceeds received in advance is restricted for capital projects. As of September 30, 2003, PFA had expended $1.4 million of the up-front payment.

The $8.3 million payment was based on a notional amount of $174.9 million. The counterparty has the option to exercise the agreement on October 1, 2010 –PFA's 1999 bonds' first call date. If the swap is exercised, it will also commence October 1, 2010. The fixed swap rate (5.27%) was set at a rate that, when added to an assumption for remarketing and liquidity costs, will approximate the coupons of the "refunded" bonds. The swap's variable payment would be 64% of the LIBOR.

As of September 30, 2003, the swap had a negative fair value of approximately $18,960,000 in favor of the counterparty estimated using the zero-coupon method. This method calculated the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipated future spot interest rates. These payments were then discounted using the spot rates implied by the current yield curve for the hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

If the option is exercised and refunding bonds are not issued, the 1999 bonds would not be refunded and PFA would make net swap payments as required by the terms of the contract – that is, making a fixed payment to the counterparty for the term of the swap at 5.27% and receiving a variable payment of 64% of LIBOR. If the option is exercised and the variable rate bonds issued, the actual savings ultimately recognized by the transaction will be affected by the relationship between the interest rate terms of the to-be issued variable-rate bonds versus the variable payment on the swap (64% of LIBOR). If the option is not exercised, PFA is not obligated to repay the up-front payment.

Debt service requirements at September 30, 2003, were as follows (expressed in thousands):

	Governmental Activities -- Bonds										
		Revenue Bonds Series 1998 A		Revenue Bonds Series 1998 C		Revenue Bonds Series 1998 D		Revenue Bonds Series 1998 E		Revenue Bonds Series 1998 Total	
		Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Year:											
2004	$	—	15,821	9,480	3,313	3,745	1,442	—	4,441	13,225	25,017
2005		—	15,821	9,990	2,801	3,965	1,220	—	6,261	13,955	26,103
2006		—	15,821	10,555	2,236	4,210	974	—	6,261	14,765	25,292
2007		—	15,821	11,150	1,640	4,470	714	—	6,261	15,620	24,436
2008		—	15,821	11,780	1,009	4,750	437	—	6,261	16,530	23,528
2009-2013		56,930	73,343	12,455	343	4,915	147	30,095	28,715	104,395	102,548
2014-2018		51,545	54,260	—	—	—	—	76,335	19,362	127,880	73,622
2019-2023		142,495	32,610	—		—	—	—	6,581	142,495	39,191
2024-2028		38,105	5,359	—	—	—	—		245	38,105	5,604
2029-2033		—	—		—	—	—	—	—	—	
Total	$	289,075	244,677	65,410	11,342	26,055	4,934	106,430	84,388	486,970	345,341

		General Obligation Bonds Series 1999 A		Project Revenue Bonds Series 1999		Revenue Bonds Series A 1999		Tobacco Bonds Series A 2001		Garvee Bonds Series 2002	
		Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Year:											
2004	$	830	408	2,960	236	4,540	17,703	—	715	2,805	890
2005		885	353	1,550	48	4,765	17,470		705	2,900	792
2006		945	295		—	5,005	17,210	—	705	3,000	647
2007		1,005	232	—	—	5,285	16,921	—	705	3,155	857
2008		1,075	166	—		5,585	16,615	910	705	3,310	339
2009-2013		1,740	114	—	—	33,055	77,745	5,895	3,525	3,475	178
2014-2018		—	—	—	—	44,665	65,689	1,405	3,525	—	—
2019-2023		—	—	—	—	60,885	48,929	6,390	2,806	—	—
2024-2028		—	—	—	—	83,175	26,004	—	2,011	—	—
2029-2033		—	—	—	—	40,915	2,543	8,045	1,056	—	—
Total	$	6,480	1,568	4,510	284	287,875	306,829	22,645	16,458	18,645	3,703

		Total governmental activities	
		Principal	Interest
Year:			
2004	$	24,360	44,969
2005		24,055	45,471
2006		23,715	44,149
2007		25,065	43,151
2008		27,410	41,353
2009-2013		148,560	184,110
2014-2018		173,950	142,836
2019-2023		209,770	90,926
2024-2028		121,280	33,619
2029-2033		48,960	3,599
	$	827,125	674,183

(c) Notes Payable

The Government and FEMA entered into a Community Disaster Loan Agreement (CDL) on June 14, 1996. The purpose of the 1996 CDL was to enable the Government to continue to provide vital municipal services such as public health and safety, police and fire protection, and the operation of public schools, among other things, after the Government had suffered a substantial loss of tax and other revenue as a result of Hurricane Marilyn, which occurred in 1995. The loan proceeds were not intended to provide funds to finance capital projects nor the repair or restoration of public property damaged by Hurricane Marilyn. The CDL, by its terms, was secured by a pledge of the full faith, credit, and taxing power of the Government.

Pursuant to 44 Code of Federal Regulations (CFR) Section 206.366, Subpart K, the Government submitted an Application for Administrative Loan Cancellation in connection with the Hurricane Marilyn 1067-60 CDL in June 2001. By this application, the Government requested cancellation of $127.2 million in principal drawdowns and the corresponding accumulated interest to date.

In October 2004, FEMA notified the Government the results of its review of the Application for Administrative Loan Cancellation in connection with Hurricane Marilyn. As a result of such review, FEMA concluded that all principal and associated interest was eligible for cancellation.

The 1996 CDL accrued interest at the annual rate of 6.35%.

Given that the requirements for Administrative Loan Cancellation were effectively met prior to September 30, 2003 and notification of FEMA's decision was received prior to the release of the basic financial statements, the Government reported the forgiveness of the 1996 CDL in the amount of $127.2 million and related accrued interest of $32.1 million as a special item in the statement of activities for the year ended September 30, 2003.

On September 4, 2003, the PG issued $100 million Bond Anticipation Notes (BANs) in anticipation of the issuance of the 2003 Series A Bonds. Interest accrued quarterly at a rate of 3.25%. The proceeds of the BANs were used for the purpose of (i) funding vendor payments and tax refunds, (ii) funding capitalized interest, and (iii) paying the cost of issuance of the BANs. On December 17, 2003, the 2003 Series A Bonds were issued, and the BANs were repaid.

On November 20, 2002, WICO consolidated and refinanced the 1993 and 2000 loans, and obtained an additional $2 million in financing for infrastructure improvements. The consolidated loan amounts to $22.5 million, to be repaid in 239 monthly installments of $142 thousand, and a final payment of outstanding principal balance plus any unpaid interest accrued to the date of the final payment. The consolidated loan has a fixed interest rate of 4.5% for the first four years of the loan. After the first four years, WICO will have the option to adjust the interest rate to one of the following: (i) prime rate plus 75 basis points, (ii) one-year LIBOR rate plus 200 basis points, or (iii) three-year treasury note rate plus 125 basis points. The revenue of WICO and lease agreements are pledged for the payment of principal and interest on the loan. WICO paid approximately $1 million in interest expense during fiscal year 2003.

Debt service requirements for the WICO loan at September 30, 2003 were as follows (expressed in thousands):

Year:		
2004	$	735
2005		768
2006		804
2007		840
2008		879
Thereafter		17,989
Total	$	22,015

(d) ***Fiduciary Funds – Line of Credit***

On December 30, 2002, the GERS entered into a loan agreement with a bank to provide working capital. GERS obtained a line of credit of $10 million which accrues interest at a fixed interest rate of 4.8% calculated on a 360-day basis and is due and payable quarterly in arrears commencing on the first day of the fourth calendar month following the closing of the loan. The terms of the line of credit require GERS to repay the line of credit in a period of 30 consecutive days during each 12-month period. The bank retains a certificate of deposit in the amount of $10 million as security on the loan. As of September 30, 2003, the outstanding balance on the line of credit was $10 million.

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(e) ***Component Units – Bonds Payable***

Bonds payable of discretely presented component units are those liabilities that are paid out of resources pledged by such entities. These revenue bonds do not constitute a liability or debt of the PG. Bonds payable outstanding at September 30, 2003, are as follows (expressed in thousands):

Bonds payable	Final maturity	Interest rates		Balance
University of the Virgin Islands:				
General obligation bonds of 1999	2029	6.50% to 7.75%	$	23,740
Various building bonds	2004	3.00% to 7.50%		224
Virgin Islands Water and Power Authority (Electric System)				
Revenue bonds of 2003	2023	4.00% to 5.00%		69,960
Revenue bonds of 1999	2022	4.25% to 5.30%		96,490
Virgin Islands Water and Power Authority (Water System)				
Revenue bonds of 1999	2017	4.90% to 5.50%		39,260
Virgin Islands Port Authority				
Revenue bonds of 2003	2023	3.73% to 5.43%		34,520
Revenue bonds of 1998	2005	3.45% to 4.50%		971
Virgin Islands Housing Finance Authority:				
Revenue bonds of 1995	2027	5.50% to 6.50%		3,785
Revenue bonds of 1998	2028	4.10% to 5.25%		2,700
Subtotal				271,650
Plus unamortized premium				5,812
Less unamortized discount				(738)
Less deferred amount on debt refunding and reacquisition costs				(6,880)
Bonds payable, net				269,844
Less amount due within one year				(7,994)
Bonds payable, due in more than one year			$	261,850

Following is a schedule of changes in long-term debt for discretely presented component units for fiscal year 2003 (expressed in thousands):

	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year	Amounts due thereafter
Bonds payable:						
University of the Virgin Islands	$ 24,701	—	(1,168)	23,533	369	23,164
Virgin Islands Water and Power Authority:						
Electric System	96,108	74,996	(3,431)	167,673	4,140	163,533
Water System	37,836	—	(1,421)	36,415	1,810	34,605
Virgin Islands Port Authority	10,163	35,815	(10,240)	35,738	1,555	34,183
Virgin Islands Housing Finance Authority	7,115	—	(630)	6,485	120	6,365
Total bonds payable, net	175,923	110,811	(16,890)	269,844	7,994	261,850
Loans payable:						
Roy L. Schneider Hospital	82	—	(82)	—	—	—
Virgin Islands Economic Development Authority	342	671	(66)	947	53	894
Virgin Islands Port Authority		2,000	(1,087)	913	913	—
University of the Virgin Islands	3,585	—	(45)	3,540	50	3,490
Total loans payable	4,009	2,671	(1,280)	5,400	1,016	4,384
Other long-term liabilities:						
University of the Virgin Islands	132	—	—	132	—	132
Virgin Islands Housing Authority	6,781	—	(1,243)	5,538	—	5,538
Virgin Islands Economic Development Authority	8,380	—	(274)	8,106	—	8,106
Juan Luis Hospital	812	—	(251)	561	—	561
Roy L. Schneider Hospital	407	67	—	474	—	474
Virgin Islands Industrial Development Park	42	—	(42)	—	—	—
Virgin Islands Housing Finance Authority	8,856	3,850	(273)	12,433	—	12,433
Total other long-term liabilities	$ 25,410	3,917	(2,083)	27,244	—	27,244

The University issued general obligation bonds in 1994 for the financing or refinancing of the construction of the St. Croix and St. Thomas residence halls and ancillary facilities. These bonds have sinking fund requirements whereby principal payments and interest are being deposited quarterly into a debt service account held by the trustee. These bonds are general obligations of the University and are collateralized by gross revenue, excluding the required appropriations for debt service made by the Government.

On December 29, 1994, the University issued additional general obligation bonds totaling $5 million to be used for the refinancing of certain equipment. These bonds also require the University to establish a debt service reserve fund, which is to be maintained at a sum equal to 5% of the bond proceeds. These bonds are secured by the refinanced equipment and are being paid in semiannual installments of approximately $413,000, including interest.

During fiscal year 2000, the University issued the 1999 Series A Bonds. The University issued these bonds to finance a portion of the construction, furnishing, and equipping of various facilities of the University, to refund the $14.1 million outstanding principal amount of general obligation bonds 1994 Series A issued by the University, to fund a debt service reserve fund for the 1999 Series A

Bonds, and to pay certain costs issued under and secured by an indenture of trust dated as of December 1, 1999, between the University and the trustee. The 1999 Series A Bonds maturing on or after December 1, 2010, are subject to redemption prior to maturity at the option of the University, as a whole or in part of any date, on and after December 1, 2009, at the redemption prices ranging between 100% and 102% of their principal amount plus accrued interest to the date fixed for redemption. At September 30, 2003, $14.1 million of 1994 Bonds are considered defeased and outstanding.

The various building bonds payable of the University as of September 30, 2003, are collateralized by mortgages on its property, by a pledge of the gross revenue derived from the operation of certain student and faculty housing and service facilities, a lien and pledge of funds available to the University for general operation purposes as required under the bond indenture agreements, and by annual grant payments that the U.S. government has agreed to fund as a debt subsidy. The bonds are subject to redemption at predetermined amounts, which may include penalties, as provided in the indentures' agreements. These indentures require the University to meet certain funding requirements for repair and replacement reserves, and bond sinking funds.

The bonds payable of the Virgin Islands Water and Power Authority (Electric System) consist of Electric System Revenue and Refunding Bonds. In June 2003, the Authority issued $75 million in Electric System Revenue Bonds, Series 2003. The proceeds from the bonds were used to finance capital improvements, repay the $18 million outstanding lines of credit, underwriters' costs, and establish a debt service fund.

In June 1998, the Electric System issued Revenue and Refunding Bonds of $110.9 million. The proceeds from the bonds, and approximately $14 million in funds from the existing debt service and debt service funds, were used to repay the lines of credit of the Electric System in the amount of $18 million, to provide for approximately $30 million in funds for the construction of certain capital projects, and to pay underwriters discount and issuance costs of approximately $1.7 million. The remaining proceeds were used to purchase direct obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining $69 million principal amount of the 1991 Series A Electric System Revenue Bonds.

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

The Bond Resolution contains certain restrictions and commitments, including the Electric System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net electric revenue, as defined, that will be at least 125% of aggregate annual principal and interest. The Electric System's net electric revenue for the fiscal year ended June 30, 2003, was 199% of the aggregate debt service.

The Series 2003 Bonds maturing on or after July 1, 2013, shall be subject to redemption prior to their stated maturity date, at the option of the Authority, on or after July 1, 2013, as a whole or in part at any time, at a redemption price equal to the principal amount thereof plus accrued interest thereon to the date fixed for redemption.

The 1998 Series Electric System Revenue and Refunding Bonds are subject to redemption on or after July 1, 2008, as a whole or in part at any time, at a redemption price of 101% in 2008, 100.5% in 2009 and 100% thereafter. The Electric System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the Electric System was damaged, destroyed, taken, or condemned, or (ii) any for-profit, nongovernmental investor shall acquire an ownership interest in some or all of the assets of the Authority.

The bonds payable of the Virgin Islands Water and Power Authority (Water System) consist of Water System Revenue and Refunding Bonds amounting to $42.6 million, issued in December 1998. The proceeds from the bonds and approximately $750,000 in funds from the existing debt service reserve fund were used to repay the lines of credit balances of the Water System in the amount of $2 million; to pay underwriters' discount and issuance costs of approximately $865,000; and to provide for $750,000 in funding for a renewal and replacement reserve fund. The remaining proceeds were used to refund the 1990 Series A Bonds at a redemption price of 100% of the principal amount and to purchase obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining $17 million principal amount of the 1992 Series B Bonds.

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

The Bond Resolution contains certain restrictions and commitments, including the Water System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net water revenue, as defined, that will be at least 125% of aggregate annual principal and interest payments. The Water System's net water revenue for the year ended June 30, 2003 was 141% of the aggregate debt service.

The 1998 Series Bonds maturing on or after July 1, 2010, are subject to redemption prior to their stated maturity date, at the option of the Water System, as a whole or in part at any time, at a redemption price of 101% during July 1, 2009 through June 30, 2010 and 100%, thereafter.

In October 1998, the VIPA issued the 1998 Airport Revenue Bonds Refunding Series A, the 1998 Rohlsen Terminal Airport Revenue Bonds Series A, and the 1998 Marine Revenue Bonds Refunding Series A with principal amounts of $19.3 million, $3.1 million, and $2.7 million, respectively. The bonds were issued for the advance refunding of previously issued bonds. The refunding resulted in a debt service savings of approximately $3.2 million and an economic gain of $2.4 million.

The Airport Revenue Bonds constitute special obligations payable solely from, and secured by a pledge of, net revenue of VIPA derived from its Airport System which consists of the airside and landside operations at the Cyril E. King Airport in St. Thomas and airside operations at the Henry E. Rohlsen Airport in St. Croix. The Rohlsen Terminal Bonds constitute special obligations payable solely from, and secured by a pledge of, net revenue of VIPA derived from the Rohlsen Terminal. In

addition, net marine revenue is pledged for payment of the Rohlsen Terminal Bonds if revenue from the Rohlsen Terminal is not enough to meet the debt service requirements. The Marine Revenue Bonds are secured solely by the net available revenue of VIPA's Marine Division.

On January 16, 2003 VIPA issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable) with principal amounts of approximately $18.4 million and $17.4 million, respectively. VIPA plans to use the bond proceeds to finance the dredging, rehabilitation, and construction of berthing piers for cruise and seagoing vessels on the island of St. Thomas and the construction of mixed used commercial facilities.

The Airport Revenue Bonds, the Marine Revenue Bonds, and the Rohlsen Terminal Bonds do not constitute general obligations of VIPA, the Aviation Statute or Marine Division, the Government, or the United States. The revenues of the Airport System are not available for the payment of principal or interest on the Marine Revenue Bonds or Rohlsen Terminal Bonds; likewise, the revenue of the Marine Division and the Rohlsen Terminal is not available to pay the principal and interest of the Airport Revenue Bonds except for any surplus of marine revenue which is available for any lawful purpose designated by VIPA. Neither the credit of the U.S. Virgin Islands nor that of its political subdivisions is pledged or available for the payment of principal or interest on the bonds. VIPA has no taxing power.

The bonds' indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance, and other costs as specified in the corresponding bond indentures. Management of VIPA believes that VIPA has established the aforementioned required accounts and has complied with the contribution requirements with respect to the bonds. In addition, it is VIPA's management's opinion that VIPA has complied with limitations and restrictions imposed by the bonds' indentures.

The bonds' indentures also specify certain debt service coverage requirements determined from net available revenue of VIPA's Airport System, the Rohlsen Terminal, and the Marine Division. The provisions of each of the bonds' indentures require that rates and fees charged for the use of each facility should be sufficient to generate enough revenue to pay all operation and maintenance expenses, exclusive of depreciation and certain noncash charges, of the respective facilities, plus: (i) at least 125% of the principal and interest and redemption account sinking fund deposit requirement of each of the bonds becoming due during such year; (ii) the amount of the debt service reserve fund deposit requirement for such period; (iii) the deposit required to the Renewal and Replacement Fund; and (iv) the amount of the Capital Improvements Appropriations for such period.

The VIHFA issued the 1995 A and 1998 A Revenue Bonds for the purpose of building single-family housing. As of September 30, 2003, the 1995 A Revenue Bond Series amount was $3.8 million and the 1998 A Revenue Bond Series amount was $2.7 million.

The VIHFA has agreed in the indenture agreements for the bonds to deposit with the trustee the full amount of the bond proceeds. The funds will be used to purchase Government National Mortgage Association (GNMA) certificates acquired by the bond servicer. The servicer is obligated to pay the principal and interest due on the GNMA certificates to the trustee in an amount equal to the scheduled principal and interest payments of the underlying mortgages. All mortgage loans issued by the Authority must be originated by the participants and secured by a first priority mortgage lien on the applicable single-family residences.

Fixed maturities required to pay principal and interest on discretely presented component units' bonds payable with fixed maturities at September 30, 2003, are as follows (expressed in thousands):

		Principal		Interest	Total
Year:					
2004	$	7,994		10,574	18,568
2005		8,381		13,596	21,977
2006		8,285		13,045	21,330
2007		10,420		12,636	23,056
2008		10,940		12,119	23,059
2009-2013		63,710		49,022	112,732
2014-2018		65,580		34,409	99,989
2019-2023		57,150		20,184	77,334
2024-2028		35,560		6,540	42,100
2029		3,630		230	3,860
Total		271,650	$	172,355	444,005
Plus unamortized premium		5,812			
Less unamortized discount		(738)			
Less deferred amount on debt refunding and reacquisition costs		(6,880)			
Bonds payable, net	$	269,844			

(10) General Tax Revenue

For the year ended September 30, 2003, general tax revenue of the PG consisted of the following (expressed in thousands):

		General fund	PFA Debt Service fund	Other governmental funds		Total
Income taxes	$	270,554	—	—		270,554
Real property taxes		40,184	—	15,500		55,684
Gross receipts taxes		—	101,387	250		101,637
Other taxes		110,633	40,055	12,454		163,142
Tax receivables	$	421,371	141,442	28,204		591,017
Tax revenue not recognized on the modified accrual basis						3,599
Total tax revenue – government-wide					$	594,616

(11) Commitments and Contingencies

(a) Primary Government

The current labor relations environment of the Government is defined by 13 distinct labor organizations subject to approximately 25 collective bargaining agreements, 5 bargaining units are without collective bargaining agreements. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and nonprofessional workers in different departments throughout the Government represented by different unions. Of the approximately 9,871 government workers, including employees of the executive branch of the Government, approximately 6,943 belong to unions. The present collective bargaining statute requires binding arbitration for certain classified employees in the event of an impasse during salary negotiations between the Government and any union. Under this process, each side chooses an arbitrator and a third impartial arbitrator is selected by the chosen arbitrators. The arbitration panel investigates and reviews the issues in dispute and renders a final and binding decision. For other classified employees, the Government must decide to go to impasse or to enjoin any strike. The Government has contractual liabilities for retroactive union arbitration salary increases aggregating $375 million accruing from fiscal years 1993 through 2003. Pursuant to Title 24 of the V.I. Code Section 374(h), no such contract is binding until appropriation of funds is made by the Legislature. Upon action of the Legislature, the general fund will have the responsibility to satisfy the obligations arising from the retroactive wages. Until such time, the liability is recorded as a long-term debt in the governmental activities column in the government-wide financial statements. Retroactive union arbitration salaries account increased by $6.7 million from fiscal year 2002 to fiscal year 2003.

The Government receives financial assistance from the federal government in the form of loans, grants, and entitlements. Loans received are described in note 9(c). Noncash federal financial assistance programs received by the Government during fiscal year ended September 30, 2003, amounted to approximately $19 million.

Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially, all grants are subject to audit under OMB Circular A-133. Disallowances as a result of these audits may become liabilities of the Government. At September 30, 2003, based on an evaluation of pending disallowances, the Government has recorded approximately $13.1 million as other long-term liabilities in the governmental activities column of the government-wide financial statements.

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

On September 23, 2002, the Government entered into a three-year compliance agreement with the U.S. Department of Education requiring that the Government develop integrated and systemic solutions to problems in managing its federally funded education programs. The compliance agreement focuses on the areas of program design and evaluation, financial management, human capital, and property management and procurement. In the event of noncompliance, the U.S. Department of Education may impose additional conditions or enforcement actions against the Government as authorized by the compliance agreement or by law.

The Government is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Title 33, Section 3411(c) of the V.I. Code, no judgment shall be awarded against the Government in excess of $25,000 for tort claims filed under Government statutes. In cases involving several survivors, each award must be construed separately for purposes of applying the limitation upon recovery imposed by the Tort Claims Act. Under Title 27, Section 166(c) of the V.I. Code, the Government's waiver of immunity is expanded to $250,000 for medical malpractice actions, including actions for wrongful death based on malpractice. Under certain circumstances, as provided in Title 33, Section 3414 of the V.I. Code, the Government may assume the payment of a judgment entered against an officer or employee acted reasonably and within the scope of his employment. The Government may pay up to a maximum amount of $100,000 of the settlement. With respect to pending and threatened litigation, the Government has accrued a provision for legal claims and judgments of approximately $13.2 million for awarded and anticipated unfavorable judgments as of September 30, 2003. Management believes that the ultimate liability in excess of amounts provided would not be significant.

As of September 2002, the Government was a defendant in a lawsuit regarding the assessment of property taxes. Under the lawsuit, taxpayers asserted that properties should be assessed at actual value in accordance with the Organic Act of 1933. The U.S. District Court agreed with the plaintiffs and, in May 2003, imposed an injunction on the collection of real property taxes for years subsequent to 1998. The Government complied with the Court order to develop a plan to implement the new valuation method, and the injunction was lifted in August 2003. Assessments will continue at the 1998 level until the new assessment method is in place, which is scheduled for fiscal year 2005.

State and federal laws and regulations require the Government to place a final cover on the Government landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site until compliance is achieved. In accordance with GASB Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Cost* (GASB

No. 18), the Government should perform a study of the activities that need to be implemented at the Government landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. In addition, GASB No. 18 requires that estimated landfill closure and postclosure care costs be accrued as a liability in the basic financial statements. The Government has not conducted the study needed to comply with the requirements of GASB No. 18; therefore, no liability has been accrued as of September 30, 2003.

Since 1985, the Government has been subject to a consent decree issued by the Virgin Islands District Court, governing the operation of its wastewater treatment plants. The consent decree was amended in 1996 and further modified in 2002 (the "2002 Stipulation to the Amended Consent Decree") to establish deadlines for the construction of new secondary treatment facilities, including the replacement of the existing St. Croix and Airport Lagoon (Charlotte Amalie) wastewater treatment plants. The 2002 Stipulation to the Amended Consent Decree requires that the new St. Croix wastewater treatment plants be completed by the end of 2005 and the new Charlotte Amalie wastewater treatment plants be completed by the end of 2006. The cost of both facilities is estimated at approximately $50 million. The 2002 Stipulation to the Amended Consent Decree also establishes certain interim deadlines and performance standards that must be met by the Government pending completion of the new facilities. In addition, the 2002 Stipulation to the Amended Consent Decree establishes stipulated penalties for violation of any of the deadlines or performance standards set forth in the 2002 Stipulation to the Amended Consent Decree. As of the date of the basic financial statements, the Government is current on all of its outstanding obligations pursuant to the 2002 Stipulation to the Amended Consent Decree. In January 2004, the Government created the Waste Management Authority, a nonprofit, public corporation for the purpose of meeting environmental requirements of waste treatment in the Territory. In December 2004, the PFA issued revenue bonds amounting to $94 million for the purpose of constructing and rehabilitating wastewater treatment plants noted above. The bond proceeds will be administered by the Waste Management Authority.

On August 21, 2002, the Government and the United States Environmental Protection Agency (EPA) entered into a Memorandum of Understanding documenting the EPA's agreement to support the renewal of the Territorial Pollutant Discharge Elimination System permit for its St. Croix distillery operations provided that the Government make certain funding available to (i) conduct treatability studies regarding the Virgin Islands Rum Industries, Ltd. effluent and the means to mitigate its potential environmental effects in the vicinity of the discharge, (ii) identify practicable, available, reliable, and cost-effective potential mitigation measures, and (iii) implement (or assist in the implementation of) such mitigation measures in the event such measures are determined by the V.I. Department of Planning and Natural Resources after consultation with EPA to be necessary and appropriate. Pursuant to the Memorandum of Understanding, the Government's obligation to fund such activities is limited to $6,000,000 per year, commencing on October 13, 2003.

As of September 2003, the Government was a defendant in a lawsuit regarding the assessment of franchise taxes. Under the lawsuit, taxpayers asserted that franchise taxes should be assessed in accordance with Title 13 Virgin Islands Code Section 531(a). The plaintiff taxpayers interpret the definition of "capital stocks used in conducting business in the Virgin Islands" in the V.I. Code as tax collected only on the par value of the stock, while the Government's position is that the amount allocated should be over the par value and additional paid-in capital upon a subsequent reorganization. The Government also imposes a six-year statute of limitations of six years on tax refund claims against the Government. Management believes that the ultimate liability of this case would not have a material impact on the Government's overall financial position as reported in the government-wide financial statements.

(b) Discretely Presented Component Units

WAPA estimates that capital expenditures in connection with continuing capital improvements will be approximately $58.7 million for the Electric System and $16.6 million for the Water System during the year ended June 30, 2004. WAPA is presently a defendant or codefendant in various lawsuits; however, any adverse outcome involving a material claim is expected to be substantially covered by the insurance. WAPA facilities were damaged by Hurricane Hugo in September 1989. WAPA reconstructed its system with proceeds from insurance and FEMA. On March 23, 1998, FEMA issued an audit report concluding that WAPA should refund approximately $7.9 million aggregated questioned costs. Approximately $2.6 million of these questioned costs are related to an oil spill that was subsequently settled with FEMA. During 1998, WAPA submitted a second appeal for $4.4 million of the remaining questioned costs and agreed to refund approximately $900,000 of questioned costs to FEMA. During 1999, FEMA denied WAPA's second appeal and formally closed the Hurricane Hugo disaster. At June 30, 2003, WAPA has recorded a liability of $5.3 million for amounts owed to FEMA for overpayments related to these questioned costs. FEMA has not made a formal request for repayment of these funds.

In September 1995, WAPA's facilities suffered extensive damage from Hurricane Marilyn. During 1996, WAPA reconstructed its system with proceeds from insurance and FEMA. In March 1999, FEMA denied WAPA's claim for $8.9 million of remaining expenditures related to the reconstruction. WAPA has subsequently reduced its claim to $5.7 million and is currently negotiating with FEMA regarding reimbursement of these remaining expenditures. Although management of WAPA believes the ultimate resolution of this matter will result in WAPA receiving additional reimbursement for prior expenditures, WAPA has not recorded any amounts to reflect these potential recoveries in the accompanying financial statements.

In connection with federal grant programs, VIPA is obligated to administer and spend the grant money in accordance with regulatory restrictions, and is subject to audit by the grantor agencies. In cases of noncompliance, the agencies involved may require VIPA to refund programs' moneys. During the normal course of business, VIPA is a defendant in various lawsuits. In the opinion of management and legal counsel, the outcome of these cases and resulting liability, if any, is either adequately covered by insurance or should not materially affect VIPA's financial position.

The Federal Aviation Administration (FAA) has conducted an on-site wildlife evaluation of the landfill, airport, and surrounding area of the Anguilla Landfill at St. Croix. The landfill, which is adjacent to St. Croix airport (Henry E. Rohlsen), caused environmental and navigational problems to the airport. The landfill attracts flocks of birds and there have been plane crashes elsewhere when birds have flown into jet engines. The FAA is threatening to force VIPA to repay $9.3 million in grants and to refuse further grants for the airport unless VIPA and the Government show rapid progress toward closing the landfill.

(12) Retirement Systems

(a) Plan Description

GERS is the administrator of a cost-sharing multiple-employer defined benefit pension plan established as of October 1, 1959 by the Government to provide retirement, death, and disability benefits to its employees. The following description of the plan is provided for general information purposes only. Refer to the actual text of the retirement law in the V.I. Code, Title 3, Chapter 27 for more complete information. Regular employees are eligible for a full-service retirement annuity when they have completed 30 years of credited service or have attained the age of 60 with at least 10 years of credited service. Members who are considered "Safety Employees," as defined in the V.I. Code, are eligible for full retirement benefits when they have earned at least 20 years of government service or have reached the age of 55 with at least 10 years of credited service. Regular employees who have attained the age of 50 with at least 10 years of credited service can elect to retire early with a reduced benefit. Senators and members of the Legislature may receive a retirement annuity when they have attained the age of 50 and completed six years of credited service or earned at least six years of credited service as a member of the Legislature. GERS is a blended component unit included in the financial reporting entity and is presented as a pension trust fund of the PG. GERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Employees' Retirement System of the Government of the Virgin Islands, GERS Complex, Veterans Drive, St. Thomas, V.I. 00802.

(b) Funding Policy

The Government's required contribution for the year ended September 30, 2003 was 14.5% of the member's annual salary. Since April 1, 1991, required member contributions are 8% of annual salary for regular employees, 9% for senators, and 10% for Act 5226 eligible employees. Through September 30, 2000, member contributions were refundable without interest upon withdrawal from employment before retirement. Subsequent to September 30, 2000, legislation was passed that provided for 4% annual interest on refunded contributions. The Government's annual required contributions, actual contributions made, and percentage contributed to the plan for the years ended September 30, 2003, 2002, and 2001, are as follows (expressed in thousands):

	Annual required contributions	Contributions made	Percentage contributed
2001	$ 64,179	43,387	67.60%
2002	95,186	50,595	53.15%
2003	117,125	51,588	44.05%

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

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

For employees electing to retire under Section 8(b) of the Act, the Government contributes to GERS a sum equal to the additional contribution the employer and employee would have made had the employee received a salary 4% higher during the three years used to compute the employee's "average compensation" figure plus a sum of $5,000. Based on the calculation, this amount was $17.8 million as of September 30, 2003. As of September 30, 2003, GERS has received $7.9 million of such amount.

The actuaries of GERS have determined that the specific funding provided under the Early Retirement Act of 1994 is inadequate to cover the costs of the program. GERS is seeking to recover any unfunded costs of the program under a newly enacted provision of the retirement law, which provides that the employer will compensate GERS for the costs of any special early retirement program.

The University has two retirement plans in which all eligible employees are required to participate. The Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) is a defined contribution pension plan covering participating, full-time faculty members and other exempt employees, under which the contributions, including employees' contributions, are used to purchase annuities. There are no unfunded past service costs, and vested benefits are equal to the annuities purchased under TIAA-CREF. As of September 30, 2003, 232 faculty members and other employees were TIAA-CREF participants. The number of active participants from the University participating in GERS as of September 30, 2003 was 275. Total contributions made by the University to TIAA-CREF participant accounts amounted to $1.7 million.

(13) Liquidity

At September 30, 2003, the Government had an unrestricted deficit in the governmental activities amounting to $700 million mostly attributed approximately $500 million in long-term debt that was issued to provide resources for working capital and other noncapital related purposes. The Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, engaging a consulting firm to assist it in its efforts to develop a series of detailed revenue enhancement and expenditure reduction initiatives and the enactment of certain laws directed toward improving the Government's financial situation. In October 1999, the Government and the U.S. Department of Interior (DOI) entered into a Memorandum of Understanding (the MOU) whereby the Government agreed to use its best efforts to undertake certain deficit reduction initiatives. As a condition to certain new and additional federal financial and technical assistance included in or being proposed by federal appropriations or other legislation, certain financial performance and accountability standards were agreed upon by the Government, which the DOI believes are necessary for the Government to achieve long-term economic recovery. Pursuant to the MOU, the release of such new and additional federal funds to the Government is subject to compliance with such performance and verifiable objectives agreed upon in such

agreement. The accountability and financial performance standards agreed upon in the MOU include: (i) preparation of five-year financial recovery plan to be provided to DOI within 90 days of the date of the MOU; (ii) a fiscal year 2000 budget mandating substantial reductions in departmental budgets and overall general fund fiscal year 2000 expenditures not to exceed $432.1 million; (iii) absent extraordinary circumstances, to maintain balanced budgets after fiscal year 2003 with any generated surpluses applied to the reduction of the accumulated deficit and unfunded obligations; (iv) annual preparation of financial reports; and (v) efforts to reduce the outstanding debt of the Government. On October 29, 1999, the DOI and the Government entered into an amendment of the MOU, which amended the Government's requirement to seek change in the Virgin Islands public labor relations law to comply with federal labor law. Pursuant to such amendment, the Government, in collaboration with union representatives, is encouraged to pursue reform initiatives through collective bargaining to bring fiscal solvency to the Government. In addition to the financial performance standards set forth in the MOU, the MOU further provides for the DOI and the Government to enter into a program of preservation and enhancement of the natural, cultural, and historic resources of the U.S. Virgin Islands to stimulate local economic growth through sustainable tourism. The Government is discussing with DOI certain events of noncompliance, remedial actions necessary to comply with the provisions of the MOU, and its effect on the Government's financial condition and results of operations.

In April 2000, the Economic Recovery Task Force submitted the five-year operating and strategic financial plan to the Governor for action. The plan provides over 200 recommendations that propose to reduce and eventually eliminate the structural budget deficit by restructuring and reforming Government operations and forging a partnership with the private sector intended to result in sustained growth.

In January 2003, the U.S. Department of Interior issued an Audit Report concluding that all criteria of the MOU were partially or substantially achieved except: (i) implementation of collective bargaining reforms to assist the fiscal solvency of the Government and (ii) completion of comprehensive annual reports within 120 days of year-end and single audits within nine months of year-end. As part of the MOU, the Government has committed to maintaining balanced budgets after the fiscal year ended September 30, 2003, with any surpluses applied to liquidating outstanding debt. The U.S. Department of Interior acknowledged that it had not achieved its objective of providing funding for the V.I. Conservation Fund and committed to providing funds for capital improvements, technical assistance, and other assistance once the Government has achieved substantial compliance.

The DOI and the Government are currently negotiating a proposed Memorandum of Understanding (MOU) regarding the fiscal and economic recovery of the Government to supersede the existing MOU. The proposed MOU is expected to provide standards of financial performance and accountability to guide the Government in developing and implementing its fiscal and economic recovery program and in achieving a balanced budget. The proposed MOU is expected to set forth the goals and commitments of the DOI with respect to additional federal financial and technical assistance that may be required to achieve the fiscal and economic objectives under the proposed MOU.

(14) Restatements and Other Changes to Net Assets

(a) Restatement

The following table illustrates the change to net assets at the beginning of the year as previously reported in the governmental activities' statement of net assets. The change is due to the early adoption of GASB Technical Bulletin 2004-1, *Tobacco Settlement Reporting and Financial Reporting Entity Issues,* by the TSFC in which they accrued an estimate of the fiscal year 2003 tobacco settlement revenues as of September 30, 2003, based on the payments received subsequent to September 30, 2003. The beginning net assets of the governmental activities have been restated as follows (expressed in thousands):

Beginning net assets, as previously reported	$	(508,798)
Restatement		
Tobacco Settlement Financing Corporation		826
Beginning net assets as restated	$	(507,972)

(b) ***Other Changes to Beginning Net Assets***

The following table summarizes the change in net assets at the beginning of the year in the statement of net assets and statement of net assets—proprietary funds as previously reported in the statement of net assets. The change resulted from the exclusion of the VI Lottery (nonmajor enterprise fund) financial statements as of and for the fiscal year ended September 30, 2003 due to their unavailability. The beginning net assets of the business-type activities and the other enterprise funds have been adjusted as follows (expressed in thousands):

		Business-type activities	Enterprise funds Other funds
Beginning net assets, as previously reported	$	77,212	7,298
Exclusion of VI Lottery financial statements		5,181	5,181
Beginning net assets, as adjusted	$	82,393	12,479

(15) Subsequent Events

(a) ***Primary Government***

In December 2003, the PFA issued $257.9 million in Series 2003 A Revenue Bonds. The proceeds of the bonds will be used to: (i) repay the Revenue Bond Anticipation Note, Series 2003 of $100 million mentioned above, (ii) fund certain necessary public safety and other public sector capital development projects, (iii) fund the Debt Service Reserve Account, and (iv) pay the costs of issuing the Series 2003A Bonds. The bonds are supported by pledged gross receipts taxes.

In February 2004, the PFA issued private activity bonds amounting to $50.6 million to finance costs of construction of a coker plant for a refinery on the island of St. Croix. The refinery is responsible for all debt service payments of the private activity bonds.

In October 2004, the excise tax on rum of 13.5 cents per gallon, which was scheduled to expire on December 31, 2003, was extended to December 31, 2005.

(Continued)

In October 2004, FEMA notified the PG that it had received full forgiveness of the Hurricane Marilyn Community Disaster Loan of $127.2 million and accrued interest of $32.1 million. Under FEMA guidelines, the loan became a capital grant at the date in which the requirements for Administrative Loan Cancellation were met and notification of forgiveness was received from FEMA. The loan forgiveness is recognized as a special item in the statement of activities for the fiscal year ended September 30, 2003.

In October 2004, the President signed the American Jobs Creation Act which changes the residency requirements and source of income requirements for U.S. territories and possessions, including the U.S. Virgin Islands. The Government has retained an independent consultant to evaluate the effect of this legislation on the Territorial economy and tax structure.

In December 2004, the PFA issued the Series 2004A Internal Revenue Matching Fund bonds in the amount of $94 million. The proceeds of the bonds will be used to finance the construction of two wastewater treatment plants to be built on the islands of St. Thomas and St. Croix, the rehabilitation of other wastewater facilities, and provide start-up capital for the newly created Virgin Islands' Waste Management Authority. The Government has pledged rum excise tax matching funds for the repayment of the bonds.

(b) ***Component Units***

In October 2003, VIPA issued the Series 2003C Marine Revenue Bonds amounting to $10.8 million. Bond proceeds will be used to finance the rehabilitation and construction of berthing piers on the island of St. Thomas.

In January 2004, the Virgin Islands' Waste Management Authority was created by Act No. 6638 as a nonprofit, public body corporate and politic of the Government with the purpose of providing environmentally sound management for the collection and disposal of solid waste, including operation and closure of landfills, and wastewater collection, transport, treatment, and disposal in the Territory. A board of directors consisting of seven members will be appointed by the Governor.

On July 2004, the University of Virgin Islands issued $21.1 million in Series 2004A General Obligation Improvement Bonds. The proceeds of the bonds will be used to (i) finance a portion of the costs of the construction, furnishing and equipment of the 2004 project, (ii) fund the Debt Service Reserve Requirement, and (iii) pay certain cost of issuance of the 2004 Series A Bonds.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Basic Financial Statements

September 30, 2002

(With Independent Auditors' Report Thereon)

Table of Contents

KPMG

KPMG LLP
American International Plaza
Suite 1100
250 Muñoz Rivera Avenue
San Juan, PR 00918-1819

Independent Auditors' Report

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

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government) as of and for the year ended September 30, 2002, which collectively comprise the Government's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Government's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following component units:

- The Virgin Islands Public Finance Authority (PFA), a blended component unit, which represents 100% of the assets, fund balance, and revenue of the PFA Debt Service Fund (a major fund); 100% of assets, net assets, and revenue of the West Indian Company (a major fund); 3.07%, 2.86%, and 8.56% of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information; 14.84%, 23.10%, and 18.20% of the assets, net assets, and revenue of the governmental activities; and 41%, 29%, and 28% of the assets, net assets, and revenue of the business-type activities.
- The Tobacco Settlement Financing Corporation, a blended component unit, which represents 1.12%, 0.22%, and 0.75%, respectively, of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information, and 1.63%, 0.56%, and 0.18% of the assets, net assets, and revenue of the governmental activities.
- The Virgin Islands Port Authority, Virgin Islands Housing Authority, University of the Virgin Islands, Virgin Islands Public Television System, Virgin Islands Economic Development Authority, Magens' Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), and the Virgin Islands Housing Finance Authority, discretely presented component units, which collectively represent 66%, 80%, and 67%, respectively, of the assets, net assets, and revenue of the aggregate discretely presented component units.

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

Except as discussed in the following six paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

The Government did not maintain accounting records for income tax receivables stated at $87 million in the general fund and governmental activities as of September 30, 2002. It was impracticable to extend our procedures sufficiently to determine the extent to which the general fund and the governmental activities as of and for the year ended September 30, 2002 may have been affected by these conditions.

The financial statements of the Virgin Islands Lottery (the Lottery) have not been audited, and we were not engaged to audit the Lottery's financial statements as part of our audit of the Government's basic financial statements. The Lottery's financial activities are recorded in the Government's basic financial statements as a nonmajor enterprise fund and represent 0.10%, 0.41%, and 6.81%, respectively, of the assets, net assets, and revenue of the aggregate remaining fund information, and 2%, 7%, and 28% of the assets, net assets, and revenue of the business-type activities.

We were unable to obtain sufficient competent evidential matter supporting the Government's receivable for unemployment insurance contributions in the Unemployment Insurance Fund (a major fund) and the business-type activities as of September 30, 2002 due to inadequate records. The Government's records do not permit, nor is it practicable to extend our auditing procedures sufficiently to determine the extent to which the Unemployment Insurance Fund (a major fund) and business-type activities as of and for the year ended September 30, 2002 may have been affected by these conditions.

The report of the other auditors on the 2002 financial statements of the Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital), a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence as to the propriety of transactions recorded in the statement of net assets as of September 30, 2001. Total assets and net assets as of September 30, 2001 amounted to $78 million and $68 million, respectively. Such amounts may affect the determination of results of operations for the year ended September 30, 2002.

The report of the other auditors on the 2001 financial statements of the Virgin Islands Housing Authority (VIHA), a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether capital assets amounting to $74 million were fairly stated.

The report of the other auditors on the 2002 financial statements of the Virgin Islands Housing Finance Authority (VIHFA), a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether land held for sale amounting to approximately $25 million was fairly stated.

The Government did not record a receivable for gross receipts taxes. Accounting principles generally accepted in the United States of America require the Government to record a receivable for taxes levied on gross receipts in periods prior to September 30, 2002 estimated to be collectible. The amount by which this departure would affect the assets, net assets, and revenue of the general fund and governmental activities is not reasonably determinable.

The basic financial statements do not include a provision for landfill closure and postclosure costs in long-term liabilities as required by accounting principles generally accepted in the United States of America. The effects of this departure from accounting principles generally accepted in the United States of America on the governmental activities have not been determined.

In our opinion, based on our audit and the reports of the other auditors, except for:

- the effects of not maintaining accounting records for income tax receivables stated at $87 million nor recording a receivable for gross receipts taxes in the general fund and governmental activities and not recording a provision for landfill closure and postclosure costs in governmental activities, as described in paragraphs three, nine, and ten above, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of the Government as of September 30, 2002, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America;
- the effects of the adjustments, if any, as might have been determined to be necessary had the Lottery been audited for the business-type activities and had we been able to examine evidence regarding the receivable for unemployment insurance in the business-type activities and the Unemployment Insurance Fund (a major fund), as described in paragraphs four and five above, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the Unemployment Insurance Fund (a major fund) of the Government as of September 30, 2002, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America; and
- the effects of the adjustments, if any, as might have been determined to be necessary, had the other auditors been able to: (i) satisfy themselves as to the propriety of certain transactions of the Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital) recorded in the statement of net assets as of September 30, 2001, (ii) obtain sufficient audit evidence to determine whether capital assets and land held for sale amounting to $74 million and $25 million in the financial statements of VIHA and VIHFA, respectively, were fairly stated, as described in paragraphs six, seven, and eight above, the financial statements referred to above present fairly, in all material respects, the financial position of the aggregate discretely presented component units of the Government of the United States Virgin Islands, as of September 30, 2002, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Finally, in our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the PFA Debt Service Fund, the West Indian Company, and the aggregate remaining fund information of the Government of the United States Virgin Islands as of September 30, 2002, and the respective changes in financial position and cash flows, where applicable, thereof, and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in notes 1 and 15, the Government has implemented a new financial reporting model, as required by GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* GASB Statement No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities,* GASB No. 37, *Basic Financial Statement—and Management's Discussion and Analysis—for State and Local Governments: Omnibus,* GASB Statement No. 38, *Certain Financial Statement Note Disclosures,* and GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements,* as of October 1, 2001.

The management's discussion and analysis on pages 5 through 14 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

April 23, 2004

Stamp No. 1987942 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

Introduction

The following discussion and analysis presents an overview of the financial position and activities of the Government of the United States Virgin Islands (the Government) as of and for the fiscal year ended September 30, 2002. Since this is the first year that the Government is required to present this format, only one year of financial data is presented. In future years, a comparative analysis will be presented.

Changes in Financial Reporting

The Government's financial reporting for this fiscal year uses a substantially revised format as compared to previous years. The new reporting focus is on the Government as a whole, and on the major individual funds of the Government. This is due to the implementation of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements—and Management Discussion and Analysis—for State and Local Governments*, and GASB Statement No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*, as amended for GASB Statement No. 37, *Basic Financial Statements—and Management's Discussion and Analysis for State and Local Governments: Omnibus*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.*

The basic financial statements include government-wide financial statements, fund financial statements, and notes that provide more detailed information to supplement the basic financial statements.

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Government-wide Financial Statements

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

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

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

Governmental Activities – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with the primary government (PG) fall into this category, including general government, public safety, health, public housing and welfare, education, transportation and communication and culture and recreation.

Business-Type Activities – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Government include the operations of the following major funds: (i) the unemployment insurance fund and (ii) the West Indian Company (WICO). Both of these programs operate with minimal assistance from the governmental activities of the Government.

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

Fund Financial Statements

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

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

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

Governmental Funds

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

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

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

Proprietary Funds

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

The unemployment insurance fund and the WICO fund are major proprietary funds.

The unemployment insurance fund is a federally mandated program to manage unemployment insurance.

The WICO fund accounts for the activities of WICO, that owns a port facility including a cruise ship pier, and manages a shopping mall and rental complex.

Fiduciary Funds

The Government is the trustee, or fiduciary, for several agency funds.

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

Financial Analysis of the Government As a Whole

Since comparable numbers are not available for prior years, the analysis of the Government's overall financial position under the accrual basis of accounting, will be limited to an analysis of the current year. A comparative analysis will be provided in fiscal year 2003.

Financial Analysis of the Primary Government (PG)

The total deficit of the PG amounted to $431 million as of September 30, 2002. It represents the net effect of $201 million invested in capital assets, net of related debt; $225 million restricted by statute or other legal requirements, not available to finance day to day operations of the government; and $857 million representing an unrestricted deficit of the PG. For the fiscal year ended September 30, 2002, the PG earned program and general revenue amounting to $854 million, and reported expenses of $891 million, resulting in a change in the deficit of $37 million. As explained in note 14 to the basic financial statements, the Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, the development of a series of detailed revenue enhancement and expenditure reduction initiatives and the enactment of certain laws directed toward improving the Government's financial situation.

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

Summary Schedule of Net Assets (Deficit) – Primary Government
September 30, 2002

(In thousands)

	Governmental activities	Business-type activities	Total
Assets:			
Current assets	$ 542,653	72,856	615,509
Capital assets	592,969	37,279	630,248
Other assets	1,975	497	2,472
Total assets	1,137,597	110,632	1,248,229
Liabilities:			
Current liabilities	260,259	13,096	273,355
Noncurrent liabilities	1,386,136	20,324	1,406,460
Total liabilities	1,646,395	33,420	1,679,815
Net assets:			
Invested in capital assets, net of related debt	183,746	16,955	200,701
Restricted	166,257	58,786	225,043
Unrestricted (deficit)	(858,801)	1,471	(857,330)
Total net assets (deficit)	$ (508,798)	77,212	(431,586)

Summary Schedule of Changes in Net Assets (Deficit) – Primary Government
Year ended September 30, 2002

(In thousands)

	Governmental activities	Business-type activities	Total
Revenue:			
Program revenue:			
Charges for services	$ 11,469	45,690	57,159
Operating grants and contributions	132,686	—	132,686
Capital grants and contributions	18,636	—	18,636
General revenue:			
Taxes	599,315	—	599,315
Transfers	(1,294)	1,294	—
Other general revenue	41,612	4,715	46,327
Total revenue	802,424	51,699	854,123
Expenses:			
General government	335,084	—	335,084
Public safety	45,230	—	45,230
Health	96,473	—	96,473
Public housing and welfare	62,440	—	62,440
Education	168,809	—	168,809
Transportation and communication	38,534	—	38,534
Culture and recreation	9,410	—	9,410
Interest on long-term debt	71,190	—	71,190
Unemployment insurance	—	22,276	22,276
West Indian Company	—	8,671	8,671
Lottery	—	14,054	14,054
Workmen's compensation	—	7,426	7,426
Other business-type activities	—	11,676	11,676
Total expenses	827,170	64,103	891,273
Change in net assets (deficit)	(24,746)	(12,404)	(37,150)
Net assets (deficit), beginning of year	(484,052)	89,616	(394,436)
Net assets (deficit), end of year	$ (508,798)	77,212	(431,586)

Budgetary Highlights

The Office of Management and Budget of the PG prepares an annual executive budget subject to approval by the Governor and the Legislature of the Virgin Islands. The executive budget is prepared on a budgetary basis similar to the cash basis of accounting. The executive budget includes only those funds that are subject to appropriation by law. More information regarding budgetary procedures is provided in note 3 of the financial statements.

A summary of the budgetary report for the general fund of the PG, included on page 22 of the financial statements, follows:

Summary Statement of Revenue and Expenditures – Budget and Actual –
Budgetary Basis – General Fund
Year ended September 30, 2002

(In thousands)

	Original budget	Amended budget	Actual	Variance
Total revenue	$ 477,026	477,026	416,970	(60,056)
Total expenditures	601,021	604,061	548,425	55,636
Excess of expenditures over revenue	(123,995)	(127,035)	(131,455)	(4,420)
Other financing sources (uses)	81,245	81,245	87,666	6,421
Excess of expenditures and other uses over revenue and other sources	$ (42,750)	(45,790)	(43,789)	2,001

The PG realized a revenue variance of ($60 million) due to declining tax revenue. The PG realized a $55.6 million variance in expenditures, due to controlled spending imposed by revenue shortfalls.

For more information regarding the financial condition of the PG, see the Economic Condition and Outlook section of this report.

Capital Assets

During fiscal year 2002, the PG contracted with an independent national appraisal firm to develop a schedule of capital assets. The PG also developed standard capitalization thresholds and major classes of assets for all government entities.

Capital asset additions during the fiscal year amounted to $38.7 million for governmental activities and $4.5 million for business-type activities.

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

Capital Assets – Primary Government

(In thousands)

	Governmental activities	Business-type activities	Total
Land and improvements	$ 187,187	5,375	192,562
Buildings and improvements	390,630	38,859	429,489
Machinery and equipment	63,438	3,310	66,748
Infrastructure	103,170	—	103,170
Construction in progress	5,544	1,119	6,663
	749,969	48,663	798,632
Less accumulated depreciation	(157,000)	(11,384)	(168,384)
Total capital assets	$ 592,969	37,279	630,248

Debt Administration

The Government issues both general obligation bonds and revenue bonds. The Revised Organic Act (48 U.S.C. Section 1574 (b)(ii) restricts the principal amount of general obligation debt which the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the U.S. Virgin Islands. Following is a summary of bonds outstanding as of September 30, 2002:

Primary Government – Bonds Payable

(In thousands)

Bonds payable	Final maturity	Interest rates	Balance
1998 Series A, B, C, D, and E revenue and refunding bonds	2022	5.50% to 7.11%	$ 499,495
1999 Project revenue bonds	2005	6.25%	7,295
1999 Series A general obligation bonds	2010	6.50%	7,260
1999 Series A revenue bonds	2029	4.2% to 6.40%	292,180
2001 Series A tobacco bonds	2031	5%	23,685
Subtotal			829,915
Less:			
Deferred amount on refundings			(3,696)
Bonds discount			(10,949)
Bonds accretion			(1,723)
Total			$ 813,547

The 1998 Bonds are nonrecourse bonds secured by rum excise taxes remitted by the U.S. Treasury. The 1999 Series A Revenue Bonds are secured by the pledge of gross receipts, and along with the 1999 Series A General Obligation and Project Revenue Bonds are general obligations of the PG. Note 9 provides detailed information regarding all bonds of the territory.

During fiscal year 2002, the Tobacco Settlement Financing Corporation, a blended component unit, issued the 2001 Series A, Term and Serial Bonds amounting to $23.7 million.

The PG made bond principal payments on all outstanding general and special revenue bonds amounting to $19.3 million during fiscal year 2002.

Standard & Poor's and Moody's have given the Government's bonds ratings of "BBB" and "AAA", respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained only from the respective rating agency.

At September 30, 2002, the PG had an outstanding Community Disaster Loan amounting to $127.2 million and had accrued interest of $32 million related to this loan.

The PG also had an unrecorded actuarial valuation of unfunded pension plan liability estimated at $815.9 million at September 30, 2002.

Other liabilities of the PG include:

Primary Government -- Other Liabilities

(In millions)

Accrued compensated absences	$	54
Retroactive union arbitration liability		368
Accrued litigation		4
Accrued disallowed costs		19
Total other liabilities	$	445

Economic Condition and Outlook

The PG ended fiscal year 2002 with a deficit amounting to $431 million, of which $857 million relates to an unrestricted deficit. The PG is experiencing the combined challenge of revenue decreases and expenditure increases.

Revenue Decreases

The PG collects income tax revenue under the "mirror" income tax system. The Government's tax laws "mirror" the U.S. Internal Revenue Service (IRS) Code, Rules and Regulations.

New Tax Acts passed by U.S. Congress in fiscal year 2003 will have a negative impact on revenue due to decreases in tax rates, expanded tax credits, and expanded tax deductions.

In connection with a real property tax case instituted against the PG in the U.S. District Court of the Virgin Islands, the Government was enjoined for a four-month period in fiscal year 2003 from appraising and assessing any real property taxes until it modified its system of appraisal to comply with certain court mandates. As a result, effective August 2003, it has been using the 1998 assessment value to issue tax bills and collect taxes, and expects to continue to do so until a new appraisal system is implemented which is intended to satisfy the court's decision, or the decision is reversed on appeal. The PG is assessing the effect of this order on fiscal year 2003 revenue.

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

Expenditure Increases

The PG faces the challenge of carryforward expenditures from prior fiscal years and increasing expenditures in the current fiscal year. Carryforward expenditures consist mainly of retroactive salary increases, which accumulated following Hurricanes Hugo, Marilyn, and Bertha in the years of 1990 through 1998.

Current increasing governmental expenditures include: increased health insurance premiums, pharmaceutical premiums, unemployment insurance benefits, and salary expense.

In addition, the Government is still experiencing the impact of the general economic decline in the United States and the impact of the terrorist attacks on September 11, 2001.

Deficit Reduction Measures

The PG is implementing a number of deficit reducing measures including: (i) increase of local taxes including the highway users tax and stamp tax; (ii) implementation of new local taxes including an excise tax on importation of personal goods and a petroleum tax; and (iii) exerting greater control of expenditures through the budgetary process.

Contacting the Government's Financial Management

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

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit)

September 30, 2002

(In thousands)

		Primary Government			
		Governmental activities	Business-type activities	Total	Component units
Assets:					
Cash and cash equivalents	$	96,869	7,133	104,002	62,615
Investments		227,693	—	227,693	24,442
Receivables, net		133,959	4,126	138,085	45,684
Internal balances		5,282	(5,282)	—	—
Loans and advances		—	5,417	5,417	2,369
Due from component units		15,365	—	15,365	—
Note receivable		—	—	—	15,689
Due from primary government		—	—	—	4,382
Due from federal government		24,929	—	24,929	5,673
Inventories		—	435	435	18,501
Food stamp coupons		4,740	—	4,740	—
Other assets		1,121	1,012	2,133	9,911
Restricted:					
Cash and cash equivalents		32,695	60,015	92,710	29,767
Investments		—	—	—	49,301
Other		—	—	—	195
Capital assets		592,969	37,279	630,248	704,380
Deferred expenses		1,975	497	2,472	3,344
Total assets		1,137,597	110,632	1,248,229	976,253
Liabilities:					
Current liabilities:					
Accounts payable and accrued liabilities		55,722	4,486	60,208	69,695
Tax refund payable		53,134	—	53,134	—
Unemployment insurance benefits		—	8,610	8,610	—
Customer deposits		—	—	—	16,282
Due to primary government		—	—	—	15,365
Due to component units		4,382	—	4,382	—
Due to federal government		—	—	—	5,300
Lines of credit		—	—	—	20,000
Interest payable		55,425	—	55,425	3,803
Deferred revenue		89,703	—	89,703	3,546
Other current liabilities		1,893	—	1,893	12,006
Due within one year:					
Loans payable		—	1,030	1,030	152
Bonds payable		18,580	—	18,580	10,270
Other liabilities		29,325	—	29,325	56
Noncurrent liabilities:					
Due in more than one year:					
Loans payable		127,200	19,294	146,494	3,857
Bonds payable		794,967	—	794,967	165,653
Other liabilities		416,064	—	416,064	25,354
Total liabilities	$	1,646,395	33,420	1,679,815	351,339

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets (Deficit), continued

September 30, 2002

(In thousands)

		Primary Government			
		Governmental activities	Business-type activities	Total	Component units
Net assets:					
Invested in capital assets, net of related debt	$	183,746	16,955	200,701	523,889
Restricted for:					
Unemployment insurance		—	49,576	49,576	—
Debt service		132,637	—	132,637	—
Capital projects		33,620	—	33,620	—
Other purposes		—	9,210	9,210	53,320
Unrestricted (deficit)		(858,801)	1,471	(857,330)	47,705
Total net assets (deficit)	$	(508,798)	77,212	(431,586)	624,914

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities

Year ended September 30, 2002

(In thousands)

		Program revenue			Net (expense) revenue and changes in net assets			
					Primary government			
	Expenses	Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total	Component units
Functions:								
Primary government:								
Governmental activities:								
General government	$ 335,084	2,488	22,249	11,575	(298,772)	—	(298,772)	
Public safety	45,230	2,375	14,916	—	(27,939)	—	(27,939)	—
Health	96,473	1,816	26,105	—	(68,552)	—	(68,552)	
Public housing and welfare	62,440	1,114	45,037	—	(16,289)	—	(16,289)	—
Education	168,809	1,553	22,431	—	(144,825)	—	(144,825)	—
Transportation and communication	38,534	1,827	1,266	7,061	(28,380)	—	(28,380)	—
Culture and recreation	9,410	296	682	—	(8,432)	—	(8,432)	—
Interest on long-term debt	71,190	—	—	—	(71,190)	—	(71,190)	—
Total governmental activities	827,170	11,469	132,686	18,636	(664,379)	—	(664,379)	—
Business-type activities:								
Unemployment insurance	22,276	6,152	—	—	—	(16,124)	(16,124)	—
West Indian Company	8,671	9,995	—	—	—	1,324	1,324	—
Lottery	14,054	14,061	—	—	—	7	7	—
Workmen's compensation	7,426	7,652	—	—	—	226	226	—
Other	11,676	7,830	—	—	—	(3,846)	(3,846)	—
Total business-type activities	64,103	45,690		—	—	(18,413)	(18,413)	—
Total primary government	891,273	57,159	132,686	18,636	(664,379)	(18,413)	(682,792)	—
Component units:								
Virgin Islands Housing Authority	64,604	5,717	31,826	13,963	—	—	—	(13,098)
Virgin Islands Port Authority	47,232	33,951	19,844	—	—	—	—	6,563
Virgin Islands Water and Power Authority:								
Electric System	111,260	111,496	1,993	—	—	—	—	2,229
Water System	24,817	25,832	1,605	—	—	—	—	2,620
University of the Virgin Islands	57,852	10,402	39,696	4,758	—	—		(2,996)
Other component units	139,903	67,111	49,313	5,476	—	—	—	(18,003)
Total component units	$ 445,668	254,509	144,277	24,197	—	—		(22,685)

(Continued)

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Activities, continued

Year ended September 30, 2002

(In thousands)

		Program revenue			Net (expense) revenue and changes in net assets			
					Primary government			
	Expenses	Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total	Component units
Total primary government and component units					(664,379)	(18,413)	(682,792)	(22,685)
General revenue:								
Taxes					$ 599,315	—	599,315	—
Transfers					(1,294)	1,294	—	
Interest and other					40,349	4,715	45,064	3,801
Tobacco Settlement Rights					1,263	—	1,263	—
Other general revenue					—	—	—	5,482
Total general revenue and transfers					639,633	6,009	645,642	9,283
Changes in net assets (deficit)					(24,746)	(12,404)	(37,150)	(13,402)
Net assets (deficit), beginning of year, as restated					(484,052)	89,616	(394,436)	638,316
Net assets (deficit), end of year					$ (508,798)	77,212	(431,586)	624,914

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Balance Sheet – Governmental Funds

September 30, 2002

(In thousands)

Assets		General	PFA Debt Service	Other governmental funds	Total governmental funds
Cash and cash equivalents	$	56,619	-	40,250	96,869
Investments		73,376	121,611	32,706	227,693
Receivables (net of allowance for uncollectible):					
Taxes		127,471	—	5,013	132,484
Federal government		—	—	24,929	24,929
Accrued interest and other		741	--	637	1,378
Due from:					
Other funds		8,346	—	9,861	18,207
Component units		15,365	—	—	15,365
Food stamp coupons		—	—	4,740	4,740
Restricted cash		—	—	32,695	32,695
Other assets		—	—	1,121	1,121
Total assets	$	281,918	121,611	151,952	555,481
Liabilities and Fund Balances					
Accounts payable and accrued liabilities	$	38,321	—	17,401	55,722
Tax refund payable		53,134	—	—	53,134
Due to:					
Other funds		10,173	—	3,178	13,351
Component units		4,382	-	—	4,382
Deferred revenue		147,021	40,049	16,529	203,599
Other current liabilities		—	—	1,370	1,370
Total liabilities		253,031	40,049	38,478	331,558
Fund balances reserved for:					
Encumbrances		53,419	—	—	53,419
Debt service		—	81,562	15,926	97,488
Unreserved fund balance (deficit), reported in:					
General fund		(24,532)	—	—	(24,532)
Special revenue funds		—	—	58,568	58,568
Capital projects funds		—	—	38,980	38,980
Total fund balance		28,887	81,562	113,474	223,923
Total liabilities and fund balances	$	281,918	121,611	151,952	

Amounts reported for governmental activities in the statement of net assets (deficit) are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	$	592,969
Debt issued by the Government has associated costs that are paid from current available resources in the funds. However, these costs are deferred on the statement of net assets.		1,975
Deferred revenue in governmental funds are recognized as revenue in governmental activities.		113,896
Other long-term liabilities not available to pay for current-period expenditures and therefore, not reported in the funds		(55,425)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.		(1,386,136)
Deficit of governmental activities	$	(508,798)

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenditures, and Changes in Fund Balances
Governmental Funds

Year ended September 30, 2002

(In thousands)

		General	PFA Debt Service	Other governmental funds	Total governmental funds
Revenue:					
Taxes	$	387,893	137,076	30,485	555,454
Federal grants and contributions		—	—	151,322	151,322
Charges for services		4,923	—	6,546	11,469
Tobacco Settlement Rights			—	1,263	1,263
Interest and other		24,865	4,258	11,226	40,349
Total revenue		417,681	141,334	200,842	759,857
Expenditures:					
Current:					
General government		266,409	—	73,255	339,664
Public safety		37,718	—	6,180	43,898
Health		67,150	—	28,470	95,620
Public housing and welfare		30,178	—	31,948	62,126
Education		136,784	—	26,374	163,158
Transportation and communication		37,090	—	1,218	38,308
Culture and recreation		6,759	—	2,365	9,124
Capital outlays		—	—	38,710	38,710
Debt service:					
Principal		—	15,935	7,827	23,762
Interest		—	46,369	1,683	48,052
Bond issuance costs		--	—	3,311	3,311
Total expenditures		582,088	62,304	221,341	865,733
Excess (deficiency) of revenue over (under) expenditures		(164,407)	79,030	(20,499)	(105,876)
Other financing sources (uses):					
Bonds issued		—	--	23,685	23,685
Transfers from other funds		99,326	—	21,287	120,613
Transfers to other funds		(10,360)	(83,339)	(28,208)	(121,907)
Discount on bonds issued		—	—	(124)	(124)
Total other financing sources (uses), net		88,966	(83,339)	16,640	22,267
Deficiency of revenue and other financing sources under expenditures and other financing uses		(75,441)	(4,309)	(3,859)	(83,609)
Fund balance, beginning of year (as restated)		104,328	85,871	117,333	307,532
Fund balance, end of year	$	28,887	81,562	113,474	223,923

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2002

(In thousands)

Net change in fund balances – total governmental funds	$	(83,609)
Government funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays ($38,710) exceeded depreciation ($14,669) in the current period.		24,041
Revenue in the statement of activities that do not provide current financial resources are not reported as revenue in the funds.		43,860
Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets. This is the amount by which proceeds ($23,762) exceeded repayments ($23,685).		77
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.		10,588
Debt issuance costs, bond accretion, and bond discount are expenditures to governmental funds, but are deferred in the statements of net assets. This is the amount of debt issue costs, bond accretion, and bond discount for the year.		3,435
Certain interest and other costs reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount equivalent to the increase in interest payable, combined with the amortization of debt issue costs, bond discount, and the net accretion of debt issue discount.		(23,138)
Changes in net assets (deficit) of governmental activities	$	(24,746)

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

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

Year ended September 30, 2002

(In thousands)

		Original budget	Amended budget	Actual	Variance
Revenue:					
Taxes	$	452,714	452,714	387,893	(64,821)
Charges for services		7,100	7,100	4,239	(2,861)
Interest and other		17,212	17,212	24,838	7,626
Total revenue		477,026	477,026	416,970	(60,056)
Expenditures:					
Current:					
General government		162,728	162,728	243,237	(80,509)
Public safety		56,497	59,537	37,404	22,133
Health		96,493	96,493	68,168	28,325
Public housing and welfare		41,017	41,017	28,999	12,018
Education		183,578	183,578	136,058	47,520
Transportation and communication		44,376	44,376	28,905	15,471
Culture and recreation		16,332	16,332	5,654	10,678
Total expenditures		601,021	604,061	548,425	55,636
Excess of expenditures over revenue		(123,995)	(127,035)	(131,455)	(4,420)
Other financing sources (uses):					
Transfers from other fund		97,010	97,010	98,026	1,016
Transfer to other fund		(15,765)	(15,765)	(10,360)	5,405
Total other financing sources (uses)		81,245	81,245	87,666	6,421
Excess of expenditures and other uses over revenue and other sources	$	(42,750)	(45,790)	(43,789)	2,001

See accompanying notes to basic financial statements.

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GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Net Assets – Proprietary Funds

September 30, 2002

(In thousands)

	Business-type activities – enterprise funds			
	Unemployment insurance	West Indian Company	Other funds	Totals
Assets:				
Current assets:				
Cash and cash equivalents	$ 353	5,728	1,051	7,132
Receivables, net				
Loans and advances	—	—	5,417	5,417
Accrued interest and other	—	1,606	2,521	4,127
Due from other funds	—	—	300	300
Inventories and other current assets	-	1,013	434	1,447
Total current assets	353	8,347	9,723	18,423
Noncurrent assets:				
Restricted cash and cash equivalents	57,833	2,181	—	60,014
Capital assets	—	31,452	5,827	37,279
Deferred expenses	—	497	—	497
Total noncurrent assets	57,833	34,130	5,827	97,790
Total assets	58,186	42,477	15,550	116,213
Liabilities:				
Current liabilities:				
Accounts payable and accrued liabilities	—	1,315	3,170	4,485
Due to other funds	—	500	5,082	5,582
Unemployment insurance benefits	8,610	—	—	8,610
Loans payable related to capital assets	—	1,030	—	1,030
Total current liabilities	8,610	2,845	8,252	19,707
Noncurrent liabilities:				
Loans payable related to capital assets	—	19,294	—	19,294
Total liabilities	8,610	22,139	8,252	39,001
Net assets:				
Invested in capital assets, net of related debt	—	11,128	5,827	16,955
Restricted	49,576	9,210	—	58,786
Unrestricted	-	—	1,471	1,471
Total net assets	$ 49,576	20,338	7,298	77,212

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Revenue, Expenses, and Changes in Net Assets
Proprietary Funds

Year ended September 30, 2002

(In thousands)

	Business-type activities – enterprise funds			
	Unemployment insurance	West Indian Company	Other funds	Total
Operating revenue:				
Charges for services	$ 6,152	9,995	29,543	45,690
Total operating revenue	6,152	9,995	29,543	45,690
Operating expenses:				
Cost of services	22,276	6,157	32,722	61,155
Depreciation and amortization	—	1,227	434	1,661
Total operating expenses	22,276	7,384	33,156	62,816
Operating (loss) income	(16,124)	2,611	(3,613)	(17,126)
Nonoperating revenue (expenses):				
Interest income	3,974	220	521	4,715
Interest expense	—	(1,287)	—	(1,287)
Total nonoperating revenue (expenses), net	3,974	(1,067)	521	3,428
(Loss) income before operating transfers	(12,150)	1,544	(3,092)	(13,698)
Transfers from other funds	—	—	2,594	2,594
Transfers to other funds	—	(1,300)	—	(1,300)
Change in net assets	(12,150)	244	(498)	(12,404)
Net assets, beginning of year (as restated)	61,726	20,094	7,796	89,616
Net assets, end of year	$ 49,576	20,338	7,298	77,212

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Cash Flows – Proprietary Funds

Year ended September 30, 2002

(In thousands)

	Business-type activities – enterprise funds			
	Unemployment insurance	West Indian Company	Other funds	Total
Cash flows from operating activities:				
Receipts from customers and users	$ 6,152	10,051	29,442	45,645
Payments to beneficiaries	(16,561)	—	—	(16,561)
Payments to suppliers and employees	—	(6,248)	(38,329)	(44,577)
Net cash (used in) provided by operating activities	(10,409)	3,803	(8,887)	(15,493)
Cash flows from noncapital financing activities:				
Transfers (to) from other funds		(1,300)	2,594	1,294
Net cash (used in) provided by noncapital financing activities	—	(1,300)	2,594	1,294
Cash flows from capital and related financing activities:				
Acquisition and construction of capital assets	—	(1,578)	—	(1,578)
Principal paid on long-term debt	—	(957)	—	(957)
Interest paid on long-term debt	—	(1,287)	—	(1,287)
Net cash used in capital and related financing activities	—	(3,822)	—	(3,822)
Cash flows from investing activities:				
Interest and dividends on investments	3,974	220	361	4,555
Net cash provided by investing activities	3,974	220	361	4,555
Net decrease in cash and cash equivalents	(6,435)	(1,099)	(5,932)	(13,466)
Cash and cash equivalents, beginning of year (as restated)	64,621	9,008	6,983	80,612
Cash and cash equivalents, end of year	$ 58,186	7,909	1,051	67,146
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:				
Operating (loss) income	$ (16,124)	2,611	(3,613)	(17,126)
Adjustments to reconcile operating income (loss) to net cash (used in) provided by operating activities:				
Depreciation and amortization	—	1,227	434	1,661
Change in assets and liabilities:				
Receivables, net	—	37	(5,551)	(5,514)
Other assets	—	(220)	(72)	(292)
Accounts payable and accrued expenses	—	148	(106)	42
Due to other funds	—	—	21	21
Other liabilities	5,715	—	—	5,715
Net cash (used in) provided by operating activities	$ (10,409)	3,803	(8,887)	(15,493)

See accompanying notes to basic financial statements.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Statement of Fiduciary Net Assets – Fiduciary Funds

September 30, 2002

(In thousands)

	Pension trust funds	Agency funds
Assets:		
Cash and cash equivalents:		
Unrestricted	$ 132,814	15,875
Restricted	126	—
Investments	1,194,001	11,979
Receivables, net:		
Loans and advances	94,480	—
Accrued interest	6,676	—
Other	12,445	—
Due from other funds	523	—
Capital assets, net	12,154	—
Other assets	16,281	—
Total assets	1,469,500	27,854
Liabilities:		
Accounts payable and accrued liabilities	101,580	27,593
Securities lending collateral	225,396	—
Due to other funds	—	97
Other liabilities	5,550	164
Total liabilities	$ 332,526	27,854
Net assets:		
Held in trust for employees' pension benefits	1,136,974	
Total net assets	$ 1,136,974	

See accompanying notes to basic financial statements.

Statement of Changes in Fiduciary Net Assets

Year ended September 30, 2002

(In thousands)

		Pension trust funds
Additions:		
Contributions:		
Employer	$	50,595
Plan members		29,510
Total contributions		80,105
Investment income:		
Net depreciation of fair value of investments		(72,038)
Interest and dividends		47,296
Real estate – rental income (net of related expenses)		4,370
		(20,372)
Less investment expense		4,231
Net investment loss		(24,603)
Other income		264
Total additions		55,766
Deductions:		
Benefits paid		123,025
Refunds of contributions		3,199
Administrative and operational expenses		6,751
Total deductions		132,975
Change in net assets		(77,209)
Net assets, beginning of year		1,214,183
Net assets, end of year	$	1,136,974

See accompanying notes to basic financial statements.

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Notes to Basic Financial Statements

September 30, 2002

(1) Summary of Significant Accounting Policies

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

The accompanying basic financial statements of the Government have been prepared in conformity with accounting principles generally accepted (GAAP) in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments* (GASB No. 34). This statement establishes new financial reporting requirements for state and local governments. The Government adopted the provisions of GASB No. 34 as well as other statements referred to below as of October 1, 2001 (see note 15). They require new information and restructure much of the information that governments have presented in the past. Comparability with reports issued in prior years is affected. With the implementation of GASB No. 34, the Government has prepared required supplementary information titled Management's Discussion and Analysis, which precedes the basic financial statements.

As previously mentioned, other GASB Statements and Interpretations were required to be implemented in conjunction with GASB No. 34. Therefore, the Government has implemented the following GASB Statements in the current fiscal year: GASB Statement No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities* (GASB No. 35), GASB Statement No. 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus* (GASB No. 37), GASB Statement No. 38, *Certain Financial Statement Note Disclosures* (GASB No. 38), and Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

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

(a) Financial Reporting Entity

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

(1) Blended Component Units

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

Virgin Islands Public Finance Authority

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

Tobacco Settlement Financing Corporation

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

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

Administrative Offices of Blended Component Units

Virgin Islands Public Finance Authority
2400 Honduras, 2nd Floor
St. Thomas, V.I. 00802

Tobacco Settlement Financing Corporation
2400 Honduras, 2nd Floor
St. Thomas, V.I. 00802

(2) Discretely Presented Component Units

The following component units, consistent with GASB No. 14, are discretely presented in the basic financial statements because of the nature of the services they provide and the Government's ability to impose its will. The component units are reported in a separate column to emphasize that they are legally separate from the PG and governed by separate boards.

Major Component Units

University of the Virgin Islands

The University of the Virgin Islands (the University) was organized as an instrumentality of the Government under Act No. 852 of March 16, 1962, in accordance with Section 6(a) of the Revised Organic Act of 1954, as amended. The purpose of the University is the stimulation and utilization of the intellectual resources of the people of the U.S. Virgin Islands and the development of a center of higher education. The powers of the University are exercised by a board of trustees consisting of 17 members as follows: Chairman of the Board of Education, Commissioner of Education, and the President of the University, all serving as members ex officio, 10 other members appointed by the Governor with the advice and consent of the Legislature, two other members elected by the board of trustees, one representative of the student body, and another of the teaching faculty. The University was not organized as a self-sustaining entity and therefore, receives substantial financial and other support from the Government.

Virgin Islands Port Authority

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

Virgin Islands Water and Power Authority

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

Nonmajor Component Units

Economic Development Authority

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

Virgin Islands Public Television System

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

Magens' Bay Authority

MBA was created as a corporate instrumentality by Act No. 2085 on December 20, 1967, with the purpose of acquiring, improving, and operating parks and beaches. The powers of MBA are exercised by a board of directors consisting of the Governor and six members appointed by the board of directors.

Virgin Islands Government Hospital and Health Facilities Corporation

The Virgin Islands Government Hospital and Health Facilities Corporation (VIGHHFC) was created by Act No. 6012 on August 23, 1994 and became active on May 1, 1999. Its purpose is to provide healthcare services and hospital facilities to the people of the U. S. Virgin Islands. The powers of VIGHHFC are exercised by a board of directors consisting of 15 members as follows: the Director of the Office of Management and Budget, the Commissioner of Finance, and 13 other members appointed by the Governor with the advice and consent of the Legislature. The VIGHHFC is composed of the Roy L. Schneider Hospital located in

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS
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St. Thomas and the Juan F. Luis Hospital and Medical Center located in St. Croix. Both entities issue separate audited financial statements.

Virgin Islands Housing Authority

The Virgin Islands Housing Authority (VIHA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act No. 903 on June 18, 1962 with the purpose of providing housing for low-income families. The powers of VIHA are exercised by a board of commissioners consisting of seven members as follows: the Commissioner of Housing and Community Renewal and six other members appointed by the Governor.

Virgin Islands Housing Finance Authority

The Virgin Islands Housing Finance Authority (VIHFA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government by the Act No. 4636 of October 20, 1981, with the purpose of stimulating low- and moderate-income housing construction and home ownership through the issuance of revenue bonds to obtain funds to be used for low-interest mortgage loans to qualified purchasers of low- and moderate-income housing. The powers of VIHFA are exercised by a board of directors consisting of the Commissioner of the Department of Housing, Parks, and Recreation (the Chairman), the Director of the Office of Management and Budget, and three persons not employed by the Government appointed by the Governor with advice and consent of the Legislature.

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

Administrative Offices

University of the Virgin Islands
2 John Brewer's Bay
St. Thomas, V.I. 00802
Virgin Islands Port Authority
PO Box 301707
St. Thomas, V.I. 00803

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

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

Economic Development Authority
1050 Norre Gade #5
St. Thomas, V.I. 00802

Magens' Bay Authority
PO Box 10583
St. Thomas, V.I. 00802

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

Virgin Islands Housing Authority
42 Annas Retreat
St. Thomas, V.I. 00802

Virgin Islands Housing Finance Authority
210-3A Altona
Frostco Center Building
St. Thomas, V.I. 00802

All financial statements of the discretely presented component units have a fiscal year-end of September 30, 2002, except for WAPA and VIHA that have a year-end of June 30, 2002 and December 31, 2001, respectively.

(3) Fiduciary Component Units

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

Employees' Retirement System of the Government of the Virgin Islands

The Employees' Retirement System of the Government of the Virgin Islands (known as GERS) was created as an independent and separate agency of the Government with the purpose of administering the Government employees' defined-benefit pension plan established as of October 1, 1959. The responsibility for the proper operation of GERS is vested in a board of trustees composed of seven members appointed by the Governor with the advice and consent of the Legislature.

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

Employees' Retirement System of the Government of the Virgin Islands
GERS Building, 3rd Floor
St. Thomas, V.I. 00802

(b) Government-wide and Fund Financial Statements

The government-wide financial statements (that is, the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the PG and its component units.

For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the PG is reported separately from certain legally separate component units for which the PG is financially accountable. The statement of net assets presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes (i) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (ii) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenue are reported instead as general revenue.

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

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

Government-wide Financial Statements

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

Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Government considers most revenue to be available if collected within 90 days of the end of the current fiscal year-end. Grant revenue is considered to be available if collected within the 12 months after the end of the current fiscal year-end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, are recorded only when payment is due.

Income taxes, gross receipts, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the Government.

Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements – The financial statements of the proprietary funds, fiduciary funds, and discretely presented component units are reported using the economic measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

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

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

(d) ***Fund Accounting***

The Government reports its financial position and results of operations in funds, which are considered separate accounting entities and discrete presentations of those component units, which are not required to be blended. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions. The new model as defined in GASB No. 34 establishes criteria (percentage of the assets, liabilities, revenue, or expenditures/expenses of either fund category or the governmental and enterprise funds combined) for the determination of major funds. The nonmajor funds are combined in a single column in the fund financial statements. The Government reports the following major funds:

Governmental Funds

The Government reports the following major governmental funds:

- ***General Fund*** – The general fund is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- ***PFA Debt Service Fund*** – The PFA Debt Service Fund accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by PFA on behalf of the Government.

Proprietary Funds

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

- ***Unemployment Insurance Fund*** – The unemployment insurance fund accounts for the collection of unemployment assessments from employers in the U.S. Virgin Islands, and the payment of unemployment benefits to eligible unemployed recipients.
- ***West Indian Company*** – The West Indian Company (WICO) accounts for the activities of a cruise ship pier and shopping mall complex on the island of St. Thomas.

Fiduciary Funds

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

- ***Pension Trust Fund Accounts*** – The pension trust fund accounts for the activities of the Employees' Retirement System of the Government of the Virgin Islands, which accumulates resources for pension benefit payments to qualified employees.
- ***Agency Fund*** – The agency fund is custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

(e) ***Cash and Cash Equivalents***

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

Cash equivalents of the discretely presented component units consist of demand accounts, money market accounts, certificates of deposit with maturities of not more than 90 days from the date of acquisition, short-term U.S. government and its agencies obligations and repurchase agreements with a U.S. commercial bank maturing within three months and collateralized by U.S. government obligations. Cash and cash equivalents of the discretely presented component units are maintained in separate bank accounts, from those of the PG, in their own names.

(f) ***Investments***

Title 33, Chapter 117 of the Virgin Islands Code (V.I. Code) authorizes the Government to invest in U.S. Government and agencies' obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. Investments are reported at fair value.

Investments in marketable equity securities in the pension trust fund are carried at quoted market values. Realized gains and losses on securities are determined by the average cost method. Investment in real estate is carried at fair value. Management has determined the fair value based upon an appraisal and a capitalization of net rental income. Member loans are valued at the outstanding loan principal balance less an allowance for estimated loan losses. Management believes that, based upon interest rate and risk factors, this valuation approximates fair value.

(g) ***Receivables***

Tax receivables represent amounts owed by taxpayers for individual and corporate income taxes, gross receipts taxes and real property taxes. Tax revenue is recognized in the governmental fund financial statements when they become both measurable and available based on actual collections during the months subsequent to September 30.

Individual and corporate income tax receivables are comprised of actual collections during the next 90 days following the fiscal year-end related to tax returns due before year-end. Gross receipts tax receivables are comprised of actual collections during the month after year-end. Real property tax receivables are comprised of actual collections during the next 60 days after year-end.

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

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

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

(h) ***Inventories***

In governmental fund types, the costs of inventories are recorded as expenditures when purchased. The proprietary fund types and component units recognize an asset when the inventory is purchased and an expense when it is consumed. Inventories in proprietary fund types are primarily valued at the lower of cost or market using the first-in, first-out method.

(i) ***Restricted Assets***

Restricted assets in the PG and discretely presented component units are set aside primarily for the payment of bonds, notes, construction funds and other specific purposes (see note 7).

(j) ***Capital Assets***

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

The PG defines capital assets as assets which have an initial, individual cost of and a useful life of: (i) $5,000 for personal property with a useful life of five years; (ii) $50,000 for buildings and building improvements with an estimated useful life of 40 and 20 years, respectively; (iii) $100,000

for land improvements; and (iv) $200,000 for infrastructure with an estimated useful life of 30 years. The value of land is capitalized.

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

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the PG are depreciated on the straight-line method over the assets estimated useful lives. There is no depreciation recorded for land and construction in progress.

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

The Government chose the option available under GASB 34 of not recording wastewater treatment facilities as information for this network of infrastructure asset was not available. These assets were deemed to be nonmajor relative to total infrastructure assets and are not reported.

(k) ***Tax Refunds Payable***

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

(l) ***Deferred Revenue***

Deferred revenue at the governmental fund level arises when potential revenue does not meet both the "measurable" and "available" criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Government has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Government has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized. Deferred revenue at the government-wide and proprietary fund levels arises only when the Government receives resources before it has a legal claim to them. Also included in deferred revenue at all levels are the undistributed food stamp coupons.

(m) Long-Term Debt

The liabilities reported in the government-wide financial statements include the Government's bonds, long-term notes, and other long-term liabilities including vacation, retroactive union arbitration salaries, legal claims, and noncurrent federal fund cost disallowances related to expenditures of federal grants. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, government fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

(n) Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

(o) Net Assets

Net assets are reported in three categories:

- ***Invested in Capital Assets, Net of Related Debt*** – These consists of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets. Significant unspent related debt proceeds are not included in the calculation of invested in capital assets, net of related debt. The unspent portion of the debt is presented as restricted net assets for capital projects.
- ***Restricted Net Assets*** – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- ***Unrestricted Net Assets*** – These consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

(p) Postemployment Benefits

In addition to the pension benefits in note 12, the Government provides postretirement healthcare benefits, in accordance with the V.I. Code to all employees who retire from the Government on or after attaining age 55 with at least 30 years of service; except for policemen and firemen who can retire with at least 15 years of service. Currently 5,343 retirees meet those eligibility requirements. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree and the Government. The Government contributes two-thirds of the of the healthcare benefits premiums. During the year ended September 30, 2002, the cost of providing healthcare benefits amounted to approximately $11.4 million.

(q) Compensated Absences

The vacation policy of the Government provides for the accumulation of four, six, or eight hours for each full biweekly pay period depending on the time of entry into government service. At the beginning of each calendar year, vacation leave is limited to 480 hours (60 days). However, the excess of 480 hours is considered by GERS for service credit towards the employees' retirement. This vacation policy does not apply to professional educational personnel of the Virgin Islands Department of Education, who are entitled to pay for school vacations. Upon retirement, an employee receives compensation for unpaid vacation leave at the employee's base rate pay. As of September 30, 2002, the Government had accrued compensated absences amounting to $52 million, including related benefits, of which $28.4 million was included in noncurrent liabilities in the government-wide financial statements.

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

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

(r) Interfund and Intra-Entity Transactions

The Government has the following types of transactions among funds:

- ***Interfund Transfers*** – Legally required transfers that are reported when incurred as "operating transfers from" by the recipient fund, and as "operating transfers to" by the disbursing fund.
- ***Intra-Entity Transactions*** – These are transactions between the PG and its component units, and among the component units. Transfers between the PG and its blended component units are reported as interfund transfers, except for transfers within the same fund type. Similarly, receivables and payables between the PG and its blended component units are reported as

amounts due to, and due from other funds. Balances and transfers between the PG and discretely presented component units (and among those component units) are reported separately.

(s) ***Lottery Revenue and Prizes***

The revenue, expenses, and prizes awarded by the Virgin Islands Lottery (the Lottery) are reported within the enterprise funds and are recognized as drawings are held. Moneys collected prior to September 30 for tickets related to drawings to be conducted subsequent to September 30 are reported as deferred revenue. Unpaid prizes awarded as of September 30 are reported as a fund liability.

(t) ***Risk Management***

With some exceptions, the Government does not carry general casualty or liability insurance coverage on its properties or the acts of its employees, relying instead on self-insurance and/or statutory liability limitations. However, as a result of an agreement with the Federal Emergency Management Agency (FEMA), with respect to properties and structures damaged by Hurricane Hugo and repaired with federal disaster assistance funds, the Government has obtained insurance for certain hospitals, schools, and other insurable public buildings that were repaired with such federal assistance. The Government purchases commercial insurance covering physical losses or damages against its property. The limit of liability for all risks excluding earthquake and flood is $10 million for each and every occurrence except for windstorm losses which has a $5 million limit. For physical losses arising from earthquake or flood, the insurance policy shall pay the difference between $5 million and $25 million for each and every occurrence. If the annual aggregate amount of the losses arising from such types of peril exceeds $40 million, the insurance covers an additional annual aggregate of $10 million for earthquake and $5 million for flood. For workmen's compensation, the Government has an enterprise fund that provides workmen's compensation to both public and private employees.

Certain component units are exposed to various risks of loss related to their specialized operations, which are mitigated by purchasing commercial insurance.

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(u) ***Future Adoption of Accounting Requirements***

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

Statement number		Adoption required in fiscal year
39	Determining Whether Certain Organizations Are Component Units – An Amendment of GASB Statement No. 14	2004
40	Deposit and Investment Risk Disclosures – An Amendment of GASB Statement No. 3	2005
41	Budgetary Comparison Schedules – Perspective Differences – an amendment of GASB Statement No. 34	2003
42	Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries	2006
43	Financial Reporting for Postemployment Benefit Plans Other than Pension Plans	2006

The impact of these statements has not yet been determined.

(v) ***Reclassifications***

The presentation of the separately issued financial statements of certain component units have been reclassified to conform to the account classifications used by the Government in the 2002 basic financial statements.

(w) ***Use of Estimates***

Management of the Government has made a number of estimates and assumptions relating to the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

(2) Component Units

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

- University of the Virgin Islands
- Virgin Islands Port Authority
- Virgin Islands Water and Power Authority
- Economic Development Authority

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- Virgin Islands Public Television System
- Magens' Bay Authority
- Virgin Islands Government Hospital and Health Facilities Corporation
- Virgin Islands Housing Authority
- Virgin Islands Housing Finance Authority

Condensed financial information of all discretely presented component units follows (expressed in thousands):

Information on net assets	Virgin Islands Housing Authority	Virgin Islands Port Authority	Virgin Islands Water and Power Authority: Electric System	Virgin Islands Water and Power Authority: Water System	University of the Virgin Islands	Other entities	Total component units
Assets:							
Current assets	$ 7,926	20,747	49,047	25,766	40,229	35,496	179,211
Due from primary government	—	695	—	—	3,568	119	4,382
Due from federal government	—	362	—	—	3,469	1,842	5,673
Restricted assets	4,527	11,852	26,918	8,558	12,382	15,026	79,263
Capital assets, net	74,169	231,753	170,378	51,425	42,161	134,494	704,380
Other noncurrent assets	—	150	2,203	991	—	—	3,344
Total assets	86,622	265,559	248,546	86,740	101,809	186,977	976,253
Liabilities and net assets:							
Current liabilities	9,690	12,095	56,693	11,810	10,712	24,332	125,332
Due to primary government	—	—	—	—	—	15,365	15,365
Due to federal government	—	—	5,300	—	—	—	5,300
Bonds payable	—	10,163	96,107	37,837	24,701	7,115	175,923
Notes payable	—	—	—	—	3,585	424	4,009
Other noncurrent liabilities	6,781	—	—	—	132	18,497	25,410
Total liabilities	16,471	22,258	158,100	49,647	39,130	65,733	351,339
Net assets:							
Invested in capital assets – net of related debt	74,169	221,590	65,275	12,580	24,995	125,280	523,889
Restricted	—	3,894	13,978	7,510	27,790	148	53,320
Unrestricted (deficit)	(4,018)	17,817	11,193	17,003	9,894	(4,184)	47,705
Total net assets	$ 70,151	243,301	90,446	37,093	62,679	121,244	624,914

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

Notes to Basic Financial Statements

September 30, 2002

Information on statements of activities	Expenses	Program revenue: Charges for services	Program revenue: Operating grants and contributions	Program revenue: Capital grants and contributions	Total component units
Virgin Islands Housing Authority	$ 64,604	5,717	31,826	13,963	(13,098)
Virgin Islands Port Authority	47,232	33,951	19,844	—	6,563
Virgin Islands Water and Power Authority:					
Electric system	111,260	111,496	1,993	—	2,229
Water system	24,817	25,832	1,605	—	2,620
University of the Virgin Islands	57,852	10,402	39,696	4,758	(2,996)
Other entities	139,903	67,111	49,313	5,476	(18,003)
Total activities	$ 445,668	254,509	144,277	24,197	(22,685)
General revenue:					
Interest and other					3,801
Other general revenue					5,482
Total general revenue					9,283
Change in net assets					(13,402)
Net assets, beginning of year					638,316
Net assets, end of year					$ 624,914

(3) Stewardship, Compliance, and Accountability

(a) Budgetary Process and Control

The V.I. Code requires the Governor to submit an annual balanced executive budget to be adopted by the Legislature for the ensuing fiscal year. The Governor is required by law to submit to the Legislature the annual executive budget no later than May 30. The annual executive budget is prepared essentially on a cash basis by the Virgin Islands Office of Management and Budget (OMB) working in conjunction with other Government offices and agencies. If the annual executive budget has not been approved before the commencement of any fiscal year, then the appropriations for the preceding fiscal year, insofar as they may be applicable, are automatically deemed reappropriated item by item. The annual executive budget, which includes those funds of the Government subject to appropriation pursuant to law, is composed of all proposed expenditures and estimated revenue for the Government. The Legislature enacts the annual executive budget through passage of lump-sum appropriations for each department. The Legislature may add, change, or delete any items in the annual executive budget proposed by the Governor. Upon passage by the Legislature, the annual executive budget is submitted to the Governor, who may veto the budget partially or in its entirety and return it to the Legislature with his objections. A gubernatorial veto can be overridden only by a two-third majority of all members of the Legislature. The Legislature is obligated by law to pass a final annual executive budget no later than September 30, the last day of the fiscal year. Supplemental budgetary appropriations' bills that are signed into law, may be created during the year without the identification of a specific revenue source to finance them. In August 1999, the Legislature enacted the Financial Accountability Act (Act No. 6289). The purpose of the Financial Accountability Act is to require by law, that the budget of the Government be balanced each year, and the appropriations in each fiscal year not exceed a verifiable revenue received.

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

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

(b) Budget/GAAP Reconciliation

The following schedule presents comparisons of the general fund legally adopted budget with actual data on a budgetary basis. Because accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of timing and entity difference in the deficiency of revenue and other financing sources over expenditures and other financing uses for the year ended September 30, 2002, is presented below (expressed in thousands):

Excess of expenditures and other uses over revenue and other financing sources – non-GAAP budgetary basis	$	(43,789)
Timing difference – change in encumbrances		(7,985)
Entity difference – deficiency of revenue and other financing sources over expenditures and other financing uses – activities with budgets not legally adopted		(23,667)
Excess of expenditures and other financing uses over revenue and other financing sources – GAAP basis	$	(75,441)

Controls over spending in special revenue funds not subject to appropriation are maintained at the Department of Finance by use of budgets and available resources (revenue). The Government makes appropriations to authorize expenditures for various capital projects. Budgets for capital projects normally remain available until completion of the project unless modified or rescinded.

(4) Cash and Investments

By law, banks or trust companies designated as depository of public funds of the Government and its various agencies, authorities and instrumentalities, are to maintain corporate surety bond or pledge collateral satisfactory to the Commissioner of Finance to secure all governmental funds deposited.

At September 30, 2002, the PG and the discretely presented component units carrying amounts of cash and cash equivalents were covered by federal deposit insurance, corporate surety bonds, or by collateral held by the Government.

Legally authorized investments vary by fund, but generally include obligations of the United States or its States, Commonwealth of Puerto Rico, the Government of the U.S. Virgin Islands, or of any agency thereof, common and preferred stocks of any U.S. corporation, common and preferred stocks of any foreign corporation listed in any internationally recognized security exchange, certain bonds or other indebtedness issued by foreign governments or foreign corporations, certificates of deposit, collateralized repurchase agreements and certain corporate bonds. Specific bond indentures also provide investment requirements.

For the fiscal year ended September 30, 2002, the PG, discretely presented component units and fiduciary funds has classified their investments into three risk categories. Category 1 includes investments that were insured or registered or for which the securities were held by a government entity, or its agent, in the entity's name and investments for which the entity has safekeeping responsibilities but no equity or ownership interest or control. Category 2 includes uninsured and unregistered investments for which the securities were held by the counterparty's trust department or agent in a government entity's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in a government entity's name. The investments of the PG, discretely presented component units by custodial credit risk categories at September 30, 2002, were as follows (expressed in thousands):

Primary Government – Investments

	Category 1	Category 2	Category 3	Reported amount
Commercial paper	$ 99,997	—	—	99,997
Certificates of deposit	61,996	—	—	61,996
Federal Home Loan Bank	1,782	—	—	1,782
	$ 163,775	—	—	163,775
Investments not categorized:				
Pooled investments				63,918
Total investments				$ 227,693

Discretely Presented Component Units – Investments

	Category 1	Category 2	Category 3	Reported amount
U.S. government and agency securities	$ 19,068	—	—	19,068
Common stocks	896	—	—	896
Corporate bonds	3,401	—	—	3,401
Certificates of deposit	4,314	—	—	4,314
Money market funds	1,471	—	—	1,471
Investment contracts	2,234	—	—	2,234
Mortgage-backed securities	—	6,608	—	6,608
Other investments	—	1,083	—	1,083
	$ 31,384	7,691	—	39,075
Investments not subject to classification:				
Mutual funds				22,479
Other				12,189
Total investments				$ 73,743

The investment balance consists of the following:

Unrestricted	$ 24,442
Restricted	49,301
Total investments	$ 73,743

Fiduciary Funds – Investments

	Category 1	Category 2	Category 3	Reported amount
U.S. government and agency securities	$ 182,160	—	—	182,160
Corporate obligations	97,015	—	—	97,015
Foreign bonds	88,503	—	—	88,503
Common stocks – U.S.	368,392	—	—	368,392
Common stocks – foreign	38,731	—	—	38,731
Collateralized debt obligations	145,907	—	—	145,907
	$ 920,708	—	—	920,708
Investments not categorized:				
Investments held by broker – dealers under security loans:				
U.S. government and agency securities				180,354
Common stocks –				39,723
U.S. Common stocks – foreign				5,320
Mutual funds				14,896
Pooled investments				11,979
Real estate				33,000
Total investments				$ 1,205,980

The pension trust fund's investments in marketable securities are administered by several professional investment managers and are held in trust by a commercial bank in the name of GERS. The investments in marketable securities generated interest and dividend income of $36.4 million. During the year ended September 30, 2002, GERS' investments (including gains and losses on investments bought and sold, as well as held during the year) (depreciated) appreciated in value as follows (expressed in thousands):

U.S. government and government-guaranteed obligations	$ 2,316
Corporate bonds – U.S.	2,469
Corporate bonds – foreign	10,644
Common stocks – U.S.	(83,977)
Common stocks – foreign	(9,823)
Collaterized debt obligations	10,150
Mutual funds	(3,817)
Net depreciation of fair value of investments	$ (72,038)

GERS participates in securities lending program administered by State Street Bank & Trust (the Custodian). Loans are generally terminable on demand. The system may be exposed to off-balance sheet risk in the event a borrower is unable to meet its contractual obligation. The Custodian must receive collateral at a minimum of 102% of the market value of the security for domestic borrowers, and 105% for foreign borrowers. The securities are marked-to-market, and settlements are made with the borrowers on a daily basis by the Custodian. At September 30, 2002, approximately $225.4 million of securities were on loan.

(5) Receivables

Taxes receivable at September 30, 2002 consist of the following (expressed in thousands):

Income	$	94,444
Real property		33,027
Gross receipts		5,013
	$	132,484

The Naval Appropriations Act, 1922, and Section 28(a) of the Revised Organic Act created a separate tax structure for the U.S. Virgin Islands that mirrors the Internal Revenue Code of 1986, as amended. Income taxes are due from every corporation, partnership, individual, association, estate, or trust that meets the filing requirements of the U.S. Internal Revenue Code. A U.S. taxpayer who is a permanent resident of the U.S. Virgin Islands satisfies his Virgin Islands income tax obligations by filing his return with and paying income taxes to the Government. Virgin Islands residents are taxed by the Virgin Islands on their world-wide income. A nonresident of the U.S. Virgin Islands pays income taxes on his U.S. Virgin Islands source income to the Government. The revenue is recognized in the general fund in the fiscal period for which the income tax return was filed. The revenue from income tax withholding and estimated payments are recognized in the general fund as collected, net of estimated tax refunds.

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

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

Property taxes are levied each calendar year on all taxable real property located in the U.S. Virgin Islands. The revenue is recognized in the general fund and in the fiscal period for which the property tax was levied, provided the tax is collected within 60 days subsequent to fiscal year-end, unless the facts justify a period greater than 60 days.

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

Property taxes are to be levied by May 15 of each year in the name of the record owner on January 15 of the same year. The taxes are due on September 30 and become delinquent if not paid by October 30. The taxes assessed become an enforceable first lien against the real property as of the levy date.

For businesses with gross receipts of less than $150,000 per annum, gross receipts taxes are levied on a monthly basis, based on a 4% of gross receipts in excess of $5,000. Businesses with annual gross receipts of more than $150,000, lose the $5,000 monthly exemption. The gross receipts tax is due within 30 calendar days following the last day of the calendar month collected.

Receivables in the government-wide financial statements also include accrued interest and other amounting to $1,378,000 and $97,000 of amounts due from the agency fund to the governmental activities.

Loans and advances receivable at September 30, 2002, consist of the following (expressed in thousands):

		Primary government	Fiduciary funds	Component units
Mortgage loans	$	9,625	26,373	—
Personal loans		—	69,872	—
Other loans and advances		963	1,235	2,369
Subtotal		10,588	97,480	2,369
Less allowance for uncollectible accounts		(5,171)	(3,000)	—
Loans and advances, net	$	5,417	94,480	2,369

(6) Interfund Transactions

(a) *Operating Transfers*

Operating transfers constitute the transfer of resources from the fund that receives the resources to the fund that utilizes them. The most significant transfers to the general fund from other governmental funds include a $73.2 million transfer from the debt service fund representing tax revenue in excess of bonds debt service requirements and a $25.6 million transfer from the nonmajor governmental funds, $5.6 million from the PFA Blended Capital Projects Fund for reimbursement of capital outlays made by the general fund and $20 million from the Government's debt service fund representing tax revenue in excess of bonds debt service requirements. Transfers to nonmajor governmental funds consisted primarily of $10.1 million transferred from the debt service fund and $10.3 million from the general fund. Other significant transfers include a transfer of $2.6 million from PFA Blended Capital Projects Fund to the King's Alley Management Fund (a nonmajor enterprise fund).

Interfund transfers for the year ended September 30, 2002 consisted of the following (expressed in thousands):

Transfer to		General fund	PFA Debt Service Fund	Nonmajor governmental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Total
General fund	$	—	73,212	25,614	500	—	99,326
Nonmajor governmental		10,360	10,127	—	800	—	21,287
Nonmajor enterprise		—	-	2,594	—	—	2,594
Total	$	10,360	83,339	28,208	1,300	—	123,207
Transfer from							
General fund	$	—	—	10,360	—	—	10,360
Debt service fund		73,212	—	10,127	—	—	83,339
Nonmajor governmental		25,614	—	—	—	2,594	28,208
Enterprise fund – West Indian Company		500	—	800	—	—	1,300
Total	$	99,326	—	21,287	—	2,594	123,207

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(b) Due From/To Other Funds

The following table summarizes interfund receivables and payables at September 30, 2002 (expressed in thousands):

Due to		General fund	Nonmajor govern-mental funds	Enterprise fund – West Indian Company	Nonmajor enterprise funds	Pension trust fund	Agency fund	Discretely presented component units	Total
General fund	$		3,178	500	4,668	—	—	15,365	23,711
Nonmajor governmental		9,350	—	—	414	—	97	—	9,861
Total govern-mental funds	$	9,350	3,178	500	5,082	.	97	15,365	33,572
Proprietary fund nonmajor enterprise	$	300	—	—	—	—	—	—	300
Fiduciary funds – pension trust fund	$	523	-	—	—	—	—	—	523
Discretely presented component units	$	4,382	—	—	—	—	—	—	4,382
Due from									
General fund		—	9,350	—	300	523	—	4,382	14,555
Nonmajor governmental		3,178	—	—	—	—	—	—	3,178
Total govern-mental funds	$	3,178	9,350	—	300	523	—	4,382	17,733
Enterprise fund West Indian Company		500	—	—	—	.	—	—	500
Nonmajor enterprise		4,668	414	—	—	—	—	—	5,082
Total proprietary funds	$	5,168	414	—	—	—	—	—	5,582
Fiduciary funds – agency fund	$	—	97	—	—	—	—	—	97
Discretely presented component units	$	15,365	—	...	—	—	—	—	15,365

The due from/to other funds include $4.9 million due from the general fund to the Emergency Molasses Fund (nonmajor governmental fund) from unpaid appropriations. Other balances composing the due from/to other funds, include $2.7 million from the Bond Proceeds Fund (nonmajor governmental fund) to the general fund and $500,000, from WICO (nonmajor enterprise fund) to the general fund. In addition, $4.4 million from the Lottery, (nonmajor enterprise fund) to the general fund consisting primarily of 8% of the total Lottery revenue that is required to be transferred to the general fund.

The due to PG balance is composed of $10.8 million due from VIGHIIFC, a discretely presented component unit. This liability exists because a portion of payroll expenditures that the Government processes are ultimately the responsibility of the Medical Center. The due from PG is mainly composed of $3.5 million and $695,000 due to the University and VIPA, respectively.

(7) Restricted Assets

(a) Primary Government

Restricted assets of the PG include cash and cash equivalents for debt service and sinking fund requirements.

(b) Component Units

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

Restricted Assets – Component Units

Debt service and sinking fund requirements	$	14,174
Construction funds		4,604
Renewal and replacement funds		834
Endowment funds		3,830
HUD project funds		4,527
Revolving loan fund		1,798
Total cash and cash equivalents		29,767
Investments:		
Debt service and sinking fund requirements		16,950
Construction funds		14,494
Renewal and replacement funds		3,481
Endowment funds		8,552
Other		5,824
Total investments		49,301
Other:		
Accrued interest receivable		195
Total restricted assets of component units	$	79,263

(8) Capital Assets

(a) Primary Government

The capital assets activity for the governmental-type activities funds for the year ended September 30, 2002 is summarized as follows (expressed in thousands):

	Beginning balance (as restated)	Additions	Reductions	Ending balance
Capital assets, not being depreciated:				
Land	$ 172,907	10,723	—	183,630
Construction in progress	11,311	8,158	13,925	5,544
Total capital assets, not depreciated	184,218	18,881	13,925	189,174
Capital assets, being depreciated:				
Land improvements	3,557	—	—	3,557
Infrastructure	84,818	18,352	—	103,170
Buildings and improvements	390,099	531	—	390,630
Machinery and equipment	48,566	14,872	—	63,438
Total capital assets, being depreciated	527,040	33,755	—	560,795
Less accumulated depreciation for:				
Land improvements	1,158	149	—	1,307
Infrastructure	5,821	3,169	—	8,990
Buildings and improvements	108,708	5,779	—	114,487
Machinery and equipment	26,644	5,572	—	32,216
Total accumulated depreciation	142,331	14,669	—	157,000
Total capital assets, being depreciated, net	384,709	19,086	—	403,795
Governmental-type activities capital assets, net	$ 568,927	37,967	13,925	592,969

Capital assets activity for the enterprise funds for the year ended as of September 30, 2002, is summarized as follows (expressed in thousands):

		Beginning balance (as restated)	Additions	Reductions	Ending balance
Capital assets, not being depreciated:					
Land and land improvements	$	5,375	—	—	5,375
Construction in progress		526	593	—	1,119
Total capital assets, not depreciated		5,901	593	—	6,494
Capital assets, being depreciated:					
Buildings and improvements		35,491	3,368	—	38,859
Machinery and equipment		2,842	535	67	3,310
Total capital assets, being depreciated		38,333	3,903	67	42,169
Less accumulated depreciation		9,820	1,631	67	11,384
Total capital assets, being depreciated, net		28,513	2,272	—	30,785
Business-type activities capital assets, net	$	34,414	2,865	—	37,279

Depreciation expense was charged to functions/programs of the PG for the year ended September 30, 2002 was as follows (expressed in thousands):

Governmental activities:		
General government	$	6,008
Public safety		1,332
Health		853
Public housing and welfare		314
Education		5,651
Transportation and communication		511
Total depreciation expense – governmental activities	$	14,669
Business-type activities:		
WICO		1,197
Lottery		67
Other		367
Total depreciation business-type activities	$	1,631

The capital assets activity for the fiduciary funds for the year ended September 30, 2002, is summarized as follows (expressed in thousands):

		Beginning balance (as restated)	Additions	Reductions	Ending balance
Capital assets, not being depreciated:					
Land	$	2,245	—	—	2,245
Total capital assets, not depreciated		2,245	—	—	2,245
Capital assets being depreciated:					
Buildings and improvements		10,947	—	—	10,947
Total capital assets being depreciated		10,947	—	—	10,947
Less accumulated depreciation		943	95	—	1,038
Total capital assets being depreciated, net		10,004	(95)	—	9,909
Capital assets, net	$	12,249	(95)	—	12,154

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(b) *Component Units*

Capital asset activity for the discretely presented component units for the year ended September 30, 2002 is summarized as follows (expressed in thousands):

	Beginning balance (as restated)	Additions	Reductions	Ending balance
Land	$ 74,607	3,248	178	77,677
Buildings and improvements	1,046,692	159,861	96,944	1,109,609
Infrastructure – airport and marine terminal facilities	70,452	14,035	—	84,487
Personal property and equipment	75,596	11,203	1,654	85,145
Construction in progress	64,111	43,979	75,355	32,735
Capital assets	1,331,458	232,326	174,131	1,389,653
Less accumulated depreciation	630,235	59,215	4,177	685,273
Capital assets, net	$ 701,223	173,111	169,954	704,380

(9) Long-Term Liabilities

Long-term liabilities activities for the year ended September 30, 2002, were as follows (expressed in thousands):

	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year	Amounts due thereafter
Governmental activities:						
Bonds payable:						
1998 Series revenue and refunding bonds	$ 511,340	—	(11,845)	499,495	12,525	486,970
1999 Project revenue bonds	9,915	—	(2,620)	7,295	2,785	4,510
1999 general obligation bonds, Series A	7,990	—	(730)	7,260	780	6,480
1999 Series A revenue bonds	296,270	—	(4,090)	292,180	4,305	287,875
2001 Series A, tobacco bonds	—	23,685	—	23,685	—	23,685
Subtotal bonds payable	825,515	23,685	(19,285)	829,915	20,395	809,520
Less:						
Deferred amount on refundings	(4,312)	—	616	(3,696)	(616)	(3,080)
Bonds discount	(11,772)	(124)	947	(10,949)	(947)	(10,002)
Bonds accretion	—	(1,975)	252	(1,723)	(252)	(1,471)
Total bonds payable	809,431	21,586	(17,470)	813,547	18,580	794,967
Loans payable:						
FEMA State Share	4,477	—	(4,477)	—	—	—
Marilyn CDL	127,200	—	—	127,200	—	127,200
Total loans payable	131,677	—	(4,477)	127,200	—	127,200
Other liabilities:						
Accrued compensated absences	49,559	4,443	—	54,002	28,402	25,600
Retroactive union arbitration	368,512	—	—	368,512	—	368,512
Litigation	11,045	2,217	(9,091)	4,171	923	3,248
Accrued disallowed costs	26,289	—	(7,585)	18,704	—	18,704
Total other liabilities	455,405	6,660	(16,676)	445,389	29,325	416,064
Total governmental activities	$ 1,396,513	28,246	(38,623)	1,386,136	47,905	1,338,231
Business-type activities:						
Notes payable:						
WICO (see note 13d)	$ 21,281	—	(957)	20,324	1,030	19,294
Total notes payable	21,281	—	(957)	20,324	1,030	19,294
Total business-type activities	$ 21,281	—	(957)	20,324	1,030	19,294

(a) Debt Margin

Pursuant to 48 U.S.C. Section 1574(b)(i) of the Revised Organic Act, the Government may issue revenue bonds for public improvements or undertakings authorized by an act of the Legislature, without limitation as to principal amount. Such revenue bonds are payable solely from the revenue directly derived from and attributable to such public improvements or undertakings. Pursuant to 48 U.S.C. Section 1574(b)(ii), the Government is authorized to issue general obligation bonds for any public purpose provided that no such indebtedness is in excess of 10% of the aggregate assessed valuation of the taxable real property in the U.S. Virgin Islands. In addition, pursuant to 48 U.S.C. Section 1574a (Public Law 94-932), the U.S. Virgin Islands is authorized to cause to be issued bonds or other obligations in anticipation of the matching funds to be received from the federal government pursuant to 26 U.S.C. Section 7652(b)(3). There is no legal limit on the value of bonds that the Government may issue pursuant to 48 U.S.C. Section 1574a. The Legislature of the U.S. Virgin Islands must authorize all bond issuances. PFA is authorized to issue bonds for the purpose of financing any project or for the purpose authorized by the Legislature. Given that PFA's powers to issue bonds are derived from 48 U.S.C. Section 1574(b), the bonds issued by PFA are subject to the limitations of said 48 U.S.C. Section 1574(b). On August 23, 1999, the Legislature amended the V.I. Code to add a Mandatory Balanced Budget Provision. Such provisions, specifically Title 2 of the V.I. Code Section 256, provide that the amount of debt of the Government existing on October 1, 2000 shall be the debt limit of the Government, exclusive of bond principal and interest that may become due. The debt limit specified under Title 2 of the V.I. Code Section 256 does not include bonds authorized by law for which a specific source of revenue is identified and committed to retiring those bonds. As used in Title 2 of the V.I. Code Section 256, the term "debt" means the total accumulated unpaid obligations that are due and payable, including unpaid income tax refunds, amounts owed to vendors, and current year unpaid debt service obligations, if any. As used in the statute, the term "debt" does not include that portion of principal or interest on bonds that is not yet due and payable.

(b) Bonds Payable

Bonds payable outstanding at September 30, 2002 are comprised of the following (expressed in thousands):

Primary Government – Bonds Payable

Bonds payable	Final maturity	Interest rates	Balance
1998 Series A, B, C, D, and E revenue and refunding bonds	2023	5.50% to 7.11%	$ 499,495
1999 Project revenue bonds	2005	6.25%	7,295
1999 Series A general obligation bonds	2010	6.50%	7,260
1999 Series A revenue bonds	2029	4.2% to 6.40%	292,180
2001 Series A tobacco bonds	2031	5%	23,685
Subtotal			829,915
Less:			
Deferred amount on refundings			(3,696)
Bonds discount			(10,949)
Bonds accretion			(1,723)
Total			$ 813,547

On May 1, 1998, PFA issued the revenue and refunding bonds series 1998 A, B, C, D, and E amounting to $541.8 million, secured by general obligation notes issued by the Government. These bonds were issued for the purpose of, among other things, advance refunding of previously issued bonds in order to obtain lower interest rates. The economic gain obtained by this advance refunding is the difference between the present value of old debt service requirements and the new debt service. This refunding resulted in a debt service saving of approximately $40 million and an economic gain of approximately $19 million.

The proceeds of the 1998 Series A and B Bonds were placed in an irrevocable trust account to provide for all future debt service payments on the Highway Revenue Bonds Series 1989, Series 1991, Series 1992, Series 1993, and Series 1994 Bonds. At September 30, 2002, $220.7 million of the above-mentioned defeased bonds were outstanding.

The proceeds of the Series 1992 Revenue Bonds were placed in an irrevocable trust to provide for all future debt service payments on the Series 1989 Revenue Bonds. At September 30, 2002, $176.9 million of defeased bonds were outstanding. All assets held by irrevocable trusts for refunding of prior outstanding debt and the corresponding liabilities are not included in the Government's basic financial statements.

The 1998 Series C Bonds and the 1998 Series D Bonds were issued to pay, on behalf of the Government, the full principal balance and interest due and payable on the Revenue Anticipation

Note, issued in February 1998. The remaining balance of the 1998 Series D Bonds amounting to approximately $11.6 million was primarily provided to the Government for additional working capital. The net proceeds of the 1998 Series E Bonds amounting to $104 million were primarily designated to fund the construction of certain capital projects amounting to $94 million. The remaining $10 million was deposited in a debt service reserve account.

The U.S. Department of the Treasury makes certain transfers to the Government of substantially all excise taxes imposed and collected under the Internal Revenue laws of the United States in any fiscal year on certain products produced in the U.S. Virgin Islands (primarily rum), and exported to the United States from the Virgin Islands. The amount required to be remitted to the Government by the U.S. Department of the Treasury is an amount no greater than the total amount of local revenue (primarily taxes) collected by the Government in each fiscal year. As a result, the term "matching fund revenue" is used to denote these payments. The Government has pledged the matching fund revenue, as described above, to the timely payment of principal and interest on the 1998 Series A, B, C, D, and E Bonds. Thus, amounts to be received by the Government from federal excise tax, mostly in rum, are deposited directly in a trust account until the 1998 Bonds are paid in accordance with the Indenture of Trust.

Estimated prepayments of matching fund revenue are made to the Government prior to the beginning of each fiscal year, subject to adjustment for the amount of local revenue actually collected by the U.S. Department of the Treasury during such year. Prepayments of matching fund revenue are recorded as deferred revenue in the accompanying statement of net assets and the balance sheet of the governmental funds and reversed against revenue in the following year. The adjustments for actual collections made to the estimated prepayments are recorded in the year determined.

In November 1999, the U.S. Congress approved an increase in the rate of federal excise taxes on rum transferred to the Government from $10.50 to $13.25 per proof gallon. The increase was retroactive to July 1999 and will be effective through December 31, 2003.

Interest on the revenue and refunding bonds series 1998 A, B, C, D, and E and 1999 bonds are payable semiannually on April 1 and October 1, and principal is payable annually on October 1. The Government is responsible for all principal and interest payments on the 1998 Series bonds. The principal due on October 1, and interest payments due on October 1 and April 1 are funded by the matching fund revenue and deposited into the debt service reserve accounts.

On April 13, 1999, a loan agreement was made between and among the Government, the PFA, International Business Machine Corporation (IBM), Banco Popular de Puerto Rico, and U.S. Trust Company of New York (Y2K Loan). The purpose of this loan was to finance certain costs of compliance by the Government with Year 2000 computer systems issues. The loan was evidenced by the Government's issuance of General Obligation Bonds Series 1999 A amounting to $18 million. Principal and interest is payable semiannually on January 1 and July 1. On July 9, 2001, the Government paid the outstanding IBM portion of the bonds amounting to $7.4 million.

The Bonds are secured by the full faith and credit and taxing power of the Government, including a pledge on annual real property tax revenue from its taxation of the Hovensa Oil Refinery (the Refinery) which revenue is deposited in the Hovensa Property Tax Fund and a contingent pledge of all franchise taxes on Foreign Sales Corporations collected by the Government (Franchise Tax

Revenue). Pursuant to the Hovensa Oil Contract, the Refinery agreed to pay $12 million annually of real property taxes on the refinery properties. Foreign sales corporations qualified to do business in the Virgin Islands must pay a franchise tax of $1.50 for each thousand dollars of capital stock issued (Franchise Tax).

On April 13, 1999, PFA also issued Project Revenue Bonds (the 1999 Project Revenue Bonds), amounting to $13.5 million on behalf of the Government, to finance a portion of the Government's Year 2000 (Y2K) compliance efforts, including the costs related to transportation, installation, and related hardware, software, and consulting services and related expenses. The 1999 Project Revenue Bonds are secured by lease payments made by the Government to PFA pursuant to a municipal lease purchase agreement, dated April 13, 1999. Such lease payments shall be funded by appropriation from the real property taxes deposited in the Hovensa Property Tax Fund and all franchise taxes on a subordinated basis and subject to any superior rights of the Series 1999 A General Obligation Bonds. The 1999 Project Revenue Bonds mature on January 1, 2005 with interest payable semiannually on January 1 and July 1.

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

The Government pledged gross receipts taxes for the timely payment of the principal and interest on the 1999 Series A Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. Gross receipts revenue amounted to $97.2 million for the year ended September 30, 2002.

On November 20, 2001, TSFC issued Tobacco Settlement Asset-Backed Bonds amounting to $21.7 million aggregate principal. The proceeds were used for the purpose of (i) purchasing all rights, title, and interest in certain litigation awards under the Master Settlement Agreement (MSA) entered into by participating cigarette manufacturers, (ii) issuance of Tobacco Settlement Asset-Backed Bonds to pay the purchase price for the rights, and (iii) to provide funds for hospital and healthcare projects in the U.S. Virgin Islands. As of September 30, 2002, the outstanding debt amounted $23.7 million.

Interest on the 2001 bonds is payable semiannually on each May and November 15, beginning with May 2002 for the term bonds amounting to $15.5 million and convertible capital appreciation bonds amounting to $8.2 million, with a nominal value of $6.2 million.

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

Bonds payable at September 30, 2002, amounted to $22 million with accumulated accretion of $1.7 million. Under early redemption provisions any MSA payments exceeding annual debt service requirements of the 2001 Series A Tobacco Bonds must be applied to early redemption of principal. MSA payments and interest earnings on the trust funds during the year ended September 30, 2002, resulted in redemption of $520,000 on November 15, 2002.

Debt service requirements at September 30, 2002 were as follows (expressed in thousands):

		Governmental Activities – Bonds									
		Revenue Bonds Series 1998 A		Revenue Bonds Series 1998 B		Revenue Bonds Series 1998 C		Revenue Bonds Series 1998 D		Revenue Bonds Series 1998 E	
		Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Year:											
2003	$	—	15,821	2,410	86	6,575	3,714	3,540	1,642	—	6,261
2004			15,821	—	—	9,480	3,313	3,745	1,441	—	6,261
2005		—	15,821	—	—	9,990	2,801	3,965	1,220	—	6,261
2006		—	15,821	—	—	10,555	2,236	4,210	974	—	6,261
2007		-	15,821	—	—	11,150	1,640	4,470	714	—	6,261
2008-2012		56,930	89,164	—	—	24,235	1,351	9,665	585	23,365	34,976
2013-2017		90,950	52,122	—	—	—	—	—	-	37,530	19,362
2018-2022		103,090	23,783	—	—	—		—	—	45,535	6,827
2023-2027		38,105	3,636		—	—	—	—	—	.	—
2028-2032		—	-	—	—	—	—	—	—	—	—
Total	$	289,075	247,810	2,410	86	71,985	15,055	29,595	6,576	106,430	92,470

		General Obligation Bonds Series 1999 A		Project Revenue Bonds Series 1999		Revenue Bonds Series A 1999		Tobacco Bonds Series A 2001		Total governmental activities	
		Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Year:											
2003	$	780	459	2,785	413	4,305	17,935	-	870	20,395	47,201
2004		830	408	2,960	236	4,540	17,703	—	774	21,555	45,957
2005		885	353	1,550	48	4,765	17,470	—	774	21,155	44,748
2006		945	295	—	—	—	17,351	—	774	15,710	43,712
2007		1,005	232	—	—		17,351	—	774	16,625	42,793
2008-2012		2,815	280	—	—	34,585	99,243	5,470	3,869	157,065	229,468
2013-2017		—	—	—	—	—	77,028	7,700	3,869	136,180	152,381
2018-2022		—	—	..	—	81,115	58,930	3,130	3,312	232,870	92,852
2023-2027		—	—	—	—	69,015	35,472	3,755	2,011	110,875	41,119
2028-2032		—	—	—	—	93,855	8,623	3,630	1,408	97,485	10,031
Total	$	7,260	2,027	7,295	697	292,180	367,106	23,685	18,435	829,915	750,262

(c) *Notes Payable*

The Government and FEMA entered into a Community Disaster Loan Agreement (CDL) on June 14, 1996. The purpose of the 1996 CDL was to enable the Government to continue to provide vital municipal services such as public health and safety, police and fire protection and the operation of public schools, among other things, after the Government had suffered a substantial loss of tax and other revenue as a result of Hurricane Marilyn which occurred in 1995. The loan proceeds were not intended to provide funds to finance capital projects, nor the repair or restoration of public property damaged by Hurricane Marilyn. The CDL, by its terms, is secured by a pledge of the full faith, credit and taxing power of the Government.

Pursuant to 44 Code of Federal Regulations (CFR), Section 206.366, Subpart K, the Government submitted an Application for Administrative Loan Cancellation in Connection with Hurricane Marilyn 1067-60 CDL in June 2001. By this application the Government requested cancellation of \$127.2 million in principal drawdowns and the attendant accumulated interest to date.

In November 2003, FEMA notified the Government the results of its review of the Application for Administrative Loan Cancellation in connection with Hurricane Marilyn. As a result of such review, FEMA concluded that only \$19.7 million of principal and associated interest was eligible for cancellation. The Government continues to pursue its request for cancellation.

The 1996 CDL accrues interest at the annual rate of 6.35% and was scheduled to be paid in 40 quarterly payments starting on June 26, 2001. The Government plans to pursue its rights under FEMA rules and regulations for administrative cancellation of all or part of the Hurricane Marilyn CDL. The Government also intends to pursue relief through federal legislation, if necessary, following administrative proceedings before FEMA. The 1996 CDL loan outstanding principal balance as of September 30, 2002 amounted to \$127 million.

In addition to the 1996 CDL, FEMA provided the Government a state share loan on May 3, 1996. The loan provides the Government with funds to be used for the matching portion of FEMA programs. The loan accrues interest at an annual rate of 6.35% with final maturity in August 2002. As of September 30, 2002, the outstanding principal balance of this loan had been paid.

In the event of a default by the Government, FEMA is entitled to recover the delinquent outstanding principal, plus any accrued and unpaid interest, under federal debt collection procedures, including administrative offset against other federal funds due to the Government, which may include matching fund revenue.

Debt service requirements for notes payable outstanding at September 30, 2002 were as follows (expressed in thousands):

		Principal	Interest	Total
Year:				
2003	$	—	42,365	42,365
2004		14,047	7,730	21,777
2005		14,540	6,841	21,381
2006		15,485	5,895	21,380
2007		16,492	4,889	21,381
2008-2012		66,636	8,197	74,833
Total	$	127,200	75,917	203,117

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(d) *Component Units – Bonds Payable*

Bonds payable of discretely presented component units are those liabilities that are paid out of resources pledged by such entities. These revenue bonds do not constitute a liability or debt of the PG. Bonds payable outstanding at September 30, 2002 are as follows (expressed in thousands):

Bonds payable	Final maturity	Interest rates		Balance
University of the Virgin Islands:				
General obligation bonds of 1995	2003	6.12% to 7.82%	$	399
General obligation bonds of 1999	2029	6.50% to 7.75%		24,390
Various building bonds	2004	3.00% to 7.50%		359
Virgin Islands Water and Power Authority (Electric System)				
Revenue bonds of 1999	2022	4.25% to 5.30%		100,435
Virgin Islands Water and Power Authority (Water System)				
Revenue bonds of 1999	2018	4.90% to 5.50%		40,985
Virgin Islands Port Authority				
Revenue bonds of 1998	2005	3.45% to 4.50%		10,301
Virgin Islands Housing Finance Authority:				
Revenue bonds of 1995	2027	5.50% to 6.50%		4,365
Revenue bonds of 1998	2028	4.10% to 5.25%		2,750
Subtotal				183,984
Plus unamortized premium				558
Less unamortized discount				(776)
Less deferred amount on debt refunding and reacquisition costs				(7,843)
Bonds payable, net			$	175,923

Following is a schedule of changes in long-term debt for discretely presented component units for fiscal year 2002 (expressed in thousands):

	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year	Amounts due thereafter
Bonds payable:						
University of the Virgin Islands	$ 26,188	—	(1,487)	24,701	1,185	23,516
Virgin Islands Water and Power Authority:						
Electric System	99,349		(3,241)	96,108	3,945	92,163
Water System	39,172		(1,336)	37,836	1,725	36,111
Virgin Islands Port Authority	13,486	—	(3,323)	10,163	3,285	6,878
Virgin Islands Housing Finance Authority	7,910	—	(795)	7,115	130	6,985
Total bonds payable, net	186,105	—	(10,182)	175,923	10,270	165,653
Notes payable:						
Roy L. Schneider Hospital	269	—	(187)	82	82	—
Economic Development Authority	365	—	(23)	342	24	318
University of the Virgin Islands	3,633	—	(48)	3,585	46	3,539
Total notes payable	4,267		(258)	4,009	152	3,857
Other long-term liabilities:						
University of the Virgin Islands	132	—	-	132	—	132
Virgin Islands Housing Authority	13,899	—	(7,118)	6,781	—	6,781
Economic Development Authority	585	8,579	—	8,380	56	8,324
Juan Luis Hospital	—	812	—	812	—	812
Roy L. Schneider Hospital	—	407	—	407	.	407
Virgin Islands Industrial Development Park	40	2	—	42	—	42
Virgin Islands Housing Finance Authority	6,765	2,091	—	8,856		8,856
Total other long-term liabilities	$ 21,421	11,891	(7,118)	25,410	56	25,354

The University issued general obligation bonds in 1994 for the financing or refinancing of the construction of the St. Croix and St. Thomas residence halls and ancillary facilities. These bonds have sinking fund requirements whereby principal payments and interest is being deposited quarterly into a debt service account held by the trustee. These bonds are general obligations of the University and are collateralized by gross revenue, excluding the required appropriations for debt service made by the Government.

On December 29, 1994, the University issued additional general obligation bonds totaling $5 million to be used for the refinancing of certain equipment. These bonds also require the University to establish a debt service reserve fund, which is to be maintained at a sum equal to 5% of the bond proceeds. These bonds are secured by the refinanced equipment and are being paid in semiannual installments of approximately $413,000, including interest.

During fiscal year 2000, the University issued the 1999 Series A Bonds. The University issued these bonds to finance a portion of the construction, furnishing, and equipping of various facilities of the University, to refund $14.1 million outstanding principal amount of general obligation bonds 1994 Series A issued by the University, to fund a debt service reserve fund for the 1999 Series A Bonds, and to pay certain cost issued under and secured by an indenture of trust dated as of December 1, 1999 between the University and the trustee. The 1999 Series A Bonds maturing on or after December 1, 2010 are subject to redemption prior to maturity at the option of the University, as a whole or in part of any date, on and after December 1, 2009 at the redemption prices ranging between 100% and 102% of their principal amount, plus accrued interest to the date fixed for redemption. At September 30, 2002, $14.1 million of 1994 Bonds are considered defeased and outstanding.

The various building bonds payable of the University as of September 30, 2002, are collateralized by mortgages on its property, by a pledge of the gross revenue derived from the operation of certain student and faculty housing and service facilities, a lien and pledge of funds available to the University for general operation purposes as required under the bond indenture agreements, and by annual grant payments that the U.S. government has agreed to fund as a debt subsidy. The bonds are subject to redemption at predetermined amounts, which may include penalties, as provided in the indentures agreements. These indentures require the University to meet certain funding requirements for repair and replacement reserves, and bond sinking funds.

The bonds payable of the Virgin Islands Water and Power Authority (Electric System) consist of Electric System Revenue and Refunding Bonds. The Electric System Revenue and Refunding Bonds of $110.9 million were issued in June 1998. The proceeds from the bonds, and approximately $14 million in funds from the existing debt service and debt service funds, were used to repay the lines of credit of the Electric System in the amount of $18 million, to provide for approximately $30 million in funds for the construction of certain capital projects, and to pay underwriters discount and issuance costs of approximately $1.7 million. The remaining proceeds were used to purchase direct obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining $69 million principal amount of the 1991 Series A Electric System Revenue Bonds. At June 30, 2002, $55.9 million of the original principal amount of the defeased 1991 bonds remained outstanding.

The advance refunding of the 1991 Series A Electric System Revenue Bonds resulted in a difference between the reacquisition price and the net carrying amount of the bonds of $7.1 million. This amount is recorded as a reduction of the new bonds and is being amortized as a component of interest expense through 2011. The Electric System completed the refunding to reduce the interest rate component of its bonds, to pay down its outstanding variable rate lines of credit, and to provide for additional funds to finance certain capital projects. The transaction decreased debt service payments related to the refunded debt by $5.2 million over the life of the new bonds and resulted in an economic gain of $3.1 million.

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

The Bond Resolution contains certain restrictions and commitments, including the Electric System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net electric revenue, as defined, that will be at least 125% of aggregate annual principal and interest. The

Electric System's net electric revenue for the fiscal year ended June 30, 2002, was 183% of aggregate debt service.

The 1998 Series Electric System Revenue and Refunding Bonds are subject to redemption on or after July 1, 2008, as a whole or in part at any time at a redemption price of 101% in 2008, 100.5% in 2009 and 100% thereafter. The Electric System Revenue Bonds are subject to mandatory redemption if any significant part of the Electric System was damaged, destroyed, taken, or condemned, or any for-profit, nongovernmental investor shall acquire an ownership interest in some or all of the assets of the authority.

The bonds payable of the Virgin Islands Water and Power Authority (Water System) consist of Water System Revenue and Refunding Bonds. The Water System Revenue and Refunding Bonds amounting to $42.6 million were issued in December 1998. The proceeds from the bonds and approximately $750,000 in funds from the existing debt service reserve fund were used to repay the lines of credit balances of the Water System in the amount of $2 million; to pay underwriters discount and issuance costs of approximately $865,000; and to provide for $750,000 in funding for a renewal and replacement reserve fund. The remaining proceeds were used to refund the 1990 Series A Bonds at a redemption price of 100% of the principal amount outstanding of $20.4 million, and to purchase obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining $17 million principal amount of the 1992 Series B Bonds. At June 30, 2002, $15.2 million of the original principal amount of the defeased 1992 bonds remained outstanding.

The refunding of the 1990 Series A and 1992 Series B Bonds resulted in a difference between the reacquisition price and the net carrying amount of the bonds of $3.8 million. The transaction increased debt service related to the refunded debt by $9.8 million over the life of the new bonds as a result of extending the maturity date, and resulted in an economic gain of $2.4 million.

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

The Bond Resolution contains certain restrictions and commitments, including the Water System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net water revenue, as defined, that will be at least 125% of aggregate annual principal and interest payments. The Water System's net water revenue for the year ended June 30, 2002 was 164% of aggregate debt service.

The 1998 Series Bonds maturing on or after July 1, 2010, are subject to redemption prior to their stated maturity date, at the option of the Water System, as a whole or in part at any time at a redemption price of 101% during July 1, 2009 through June 30, 2010 and 100%, thereafter.

In October 1998, the VIPA issued the 1998 Airport Revenue Bonds Refunding Series A, the 1998 Rohlsen Terminal Airport Revenue Bonds Series A, and the 1998 Marine Revenue Bonds Refunding Series A, with principal amounts of $19.3 million, $3.1 million, and $2.7 million, respectively. The bonds were issued for the advance refunding of previously issued bonds. The refunding resulted in a debt service savings of approximately $3.2 million and an economic gain of $2.4 million.

The Airport Revenue Bonds constitute special obligations payable solely from, and secured by a pledge of, net revenue of VIPA derived from its Airport System which consists of the airside and landside operations at the Cyril E. King Airport in St. Thomas and airside operations at the Henry E. Rohlsen Airport in St. Croix. The Rohlsen Terminal Bonds constitute special obligations payable solely from, and secured by a pledge of, net revenue of VIPA derived from the Rohlsen Terminal. In addition, net marine revenue are pledged for payment of the Rohlsen Terminal Bonds if revenue from the Rohlsen Terminal are not enough to meet the debt service requirements. The Marine Revenue Bonds are secured solely by the net available revenue of VIPA's Marine Division.

The Airport Revenue Bonds, the Marine Revenue Bonds, and the Rohlsen Terminal Bonds, do not constitute general obligations of VIPA, the Aviation or Marine Division, the Government, or the United States. The revenue of the Airport System is not available for the payment of principal or interest on the Marine Revenue Bonds or Rohlsen Terminal Bonds; likewise, the revenue of the Marine Division and the Rohlsen Terminal is not available to pay the principal and interest of the Airport Revenue Bonds except for any surplus of marine revenue which is available for any lawful purpose designated by VIPA. Neither the credit of the U.S. Virgin Islands nor that of its political subdivisions is pledged or available for the payment of principal or interest on the bonds. VIPA has no taxing power.

The bonds' indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance, and other costs as specified in the corresponding bond indentures. Management of VIPA believes that VIPA has established the aforementioned required accounts and has complied with the contribution requirements with respect to the bonds. In addition, it is VIPA's management's opinion that VIPA has complied with limitations and restrictions imposed by the bonds indentures.

The bonds' indentures also specify certain debt service coverage requirements determined from net available revenue of VIPA's Airport System, the Rohlsen Terminal, and from the Marine Division. The provisions of each of the bonds' indentures require that rates and fees charged for the use of each facility should be sufficient to generate enough revenue to pay all operation and maintenance expenses, exclusive of depreciation and certain noncash charges, of the respective facilities, plus: (i) at least 125% of the principal and interest and redemption account sinking fund deposit requirement of each of the bonds becoming due during such year; (ii) the amount of the debt service reserve fund deposit requirement for such period; (iii) the deposit required to the Renewal and Replacement Fund; and (iv) the amount of the Capital Improvements Appropriations for such period.

In fiscal year 2002, VIPA did not meet the debt service coverage requirement of the Airport Revenue Bonds. As required by the bond indenture, effective February 1, 2003, VIPA increased the landing and passenger fees of the Airport System by approximately 25%. Management believes that the revenue resulting from the increase in rates will not be sufficient to comply with the debt service

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coverage requirement of the Airport System in fiscal year 2003 and that VIPA will have to use certain funds deposited in the sinking funds to meet the requirement.

VIPA entered into use agreements with certain airlines servicing the Airport System which provided the basis for determining landing fee rates and other charges to those airlines for the use of the Airport System facilities for as long as any of the Airport Revenue Bonds outstanding.

The proceeds of the 1998 Airport Revenue Bonds and the 1998 Marine Revenue Bonds were used, together with certain other funds of VIPA, to: (i) advance refund the outstanding aggregate principal amount of the 1989 Bonds and Marine notes, respectively; (ii) fund a required deposit to the debt service reserve fund; and (iii) pay certain costs of issuance of the respective bonds.

The Rohlsen Terminal Bonds were used to: (i) pay, in part, the cost of construction of certain improvements, extensions, betterments, and additions to the HERA airport in St. Croix; (ii) fund a required deposit to the Debt Service Reserve Fund; and (iii) pay certain cost of issuance of the Rohlsen Terminal Bonds.

The VIHGA issued the 1995 A and 1998 A Revenue Bonds for the purpose of building single-family housing. As of September 30, 2002, the 1995 A Revenue Bond Series amount was $4.4 million and the 1998 A Revenue Bond Series amount was $2.7 million.

The Authority has agreed in the indenture agreements for the bonds to deposit with the trustee the full amount of the bond proceeds. The funds will be used to purchase Government National Mortgage Association (GNMA) certificates acquired by the bond servicer. The servicer is obligated to pay the principal and interest due on the GNMA certificates to the trustee in an amount equal to the scheduled principal and interest payments of the underlying mortgages. All mortgage loans issued by the Authority must be originated by the participants and secured by a first priority mortgage lien on the applicable single family residences.

The bonds payable of the VIHA consist of several bonds issued in prior years for construction of the Low Rent Housing Program. The outstanding balance of the bonds at December 31, 2001 was $18.3 million. Under the provisions of the contract, HUD serviced all guaranteed debt for the Authority during the year. HUD has affirmed that the guaranteed debt is no longer the liability of the Authority. The bonds payable of the VIHA are not included in the schedule below.

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Fixed maturities required to pay principal and interest on discretely presented component units' bonds payable with fixed maturities at September 30, 2002, are as follows (expressed in thousands):

		Principal	Interest	Total
Year:				
2003	$	10,270	9,288	19,558
2004		9,975	8,839	18,814
2005		10,262	8,371	18,633
2006		7,125	7,877	15,002
2007		7,485	7,519	15,004
2008-2012		42,990	31,471	74,461
2013-2017		43,840	19,928	63,768
2018-2022		35,725	9,060	44,785
2023-2027		9,425	2,761	12,186
2028-2029		6,887	507	7,394
Total	$	183,984	105,621	289,605
Plus unamortized premium		558		
Less unamortized discount		(776)		
Less deferred amount on debt refunding and reacquisition costs		(7,843)		
Bonds payable, net	$	175,923		

(10) General Tax Revenue

For the year ended September 30, 2002, general tax revenue of the PG consisted of the following (expressed in thousands):

Income taxes	$	304,748
Gross receipts taxes		97,273
Property taxes		69,341
Other taxes		127,953
	$	599,315

(11) Commitments and Contingencies

(a) Primary Government

The current labor relations environment of the Government is defined by 13 distinct labor organizations subject to approximately 30 collective bargaining agreements. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and nonprofessional workers,

in different departments throughout the Government represented by different unions. Of the approximately 9,534 government workers, including employees of the executive branch of the Government, approximately 6,620 belong to unions. The present collective bargaining statute requires binding arbitration for certain classified employees in the event of an impasse during salary negotiations between the Government and any union. Under this process, each side chooses an arbitrator and a third impartial arbitrator is selected by the chosen arbitrators. The arbitration panel investigates and reviews the issues in dispute and renders a final and binding decision. For other classified employees, the Government must decide to go to impasse or to enjoin any strike. The Government has contractual liabilities for retroactive union arbitration salary increases aggregating $369 million accruing from fiscal years 1993 through 2001. Pursuant to Title 24 of the V.I. Code Section 374(h), no such contract is binding until appropriation of funds is made by the Legislature. Upon action of the Legislature, retroactive wages become a current liability of the Government payable from the general fund. Until such time, the liability is recorded as a long-term debt in the governmental activities column, in the government-wide financial statements. Retroactive union arbitration salaries account has not changed from fiscal year 2001. This is due to the fact that there was no retroactive salary increase in fiscal year 2002 because all unionized employees were brought to step according to their last negotiated wage agreement that went into effect September 1, 2001 for the fiscal year ending September 30, 2002.

The Government receives financial assistance from the federal government in the form of loans, grants and entitlements. Loans received are described in note 9(c). Noncash federal financial assistance programs received by the Government during fiscal year ended September 30, 2002, amounted to approximately $17.9 million.

Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially, all grants are subject to audit under OMB Circular A-133. Disallowances as a result of these audits may become liabilities of the Government. At September 30, 2002, based on an evaluation of pending disallowances, the Government has recorded approximately $18.7 million as other long-term liabilities in the governmental activities column of the government-wide financial statements.

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

On September 23, 2002, the Government entered into a three-year compliance agreement with the U.S. Department of Education requiring that the Government develop integrated and systemic solutions to problems in managing its federally funded education programs. The compliance agreement focuses on the areas of program design and evaluation, financial management, human capital, and property management and procurement. In the event of noncompliance, the U.S. Department of Education may impose additional conditions or enforcement actions against the Government as authorized by the compliance agreement or by law.

The Government is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under the Title 33, Section 3411(c) of the V.I. Code, no judgment shall be awarded against the Government in excess of $25,000 for tort claims filed under Government statutes. In cases involving several survivors, each award must be construed separately for purposes of applying the limitation upon recovery imposed by the Tort Claims Act. Under the Title 27, Section 166(e) of the V.I. Code, the Government's waiver of immunity is expanded to $100,000 for medical malpractice actions, including actions for wrongful death based on malpractice. Under certain circumstances, as provided in Title 33, Section 3414 of the V.I. Code, the Government may assume the payment of a judgment entered against an officer or employee acted reasonably and within the scope of his employment. The Government may pay up to a maximum amount of $100,000 of the settlement. With respect to pending and threatened litigation, the Government has accrued a provision for legal claims and judgments of approximately $4.2 million for awarded and anticipated unfavorable judgments as of September 30, 2002. Management believes that the ultimate liability in excess of amounts provided would not be significant.

As of September 2002, the Government was a defendant in a lawsuit regarding the assessment of property taxes. Under the lawsuit, taxpayers asserted that properties should be assessed at actual value in accordance with the Organic Act of 1933. The U.S. District Court agreed with the plaintiffs and in May 2003, imposed an injunction on the collection of real property taxes for years subsequent to 1998. The Government complied with the Court order to develop a plan to implement the new valuation method, and the injunction was lifted in August 2003. Assessments will continue at the 1998 level until the new assessment method is in place, scheduled for fiscal year 2005.

State and federal laws and regulations require the Government to place a final cover on the Government landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site until compliance is achieved. In accordance with GASB Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Cost* (GASB No. 18), the Government should perform a study of the activities that need to be implemented at the Government landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. In addition, GASB No. 18 requires that estimated landfill closure and postclosure care costs be accrued as a liability in the basic financial statements. The Government has not conducted the study needed to comply with the requirements of GASB No. 18; therefore, no liability has been accrued as of September 30, 2002.

Approximately $94 million of the proceeds of the Series 1998 E Bonds, together with certain federal funds amounting to approximately $61 million and other funding sources of approximately $15 million are intended, to finance certain capital projects with estimated total costs of approximately $170 million. The nature of the capital projects include the construction and improvements to wastewater treatment facilities, pursuant to a Consent Decree entered by the Government and the U.S. Environmental Protection Agency (EPA) in September 1995, with an estimated cost of approximately $41 million.

Under the Consent Decree with EPA, the Government has committed to: (i) construct two regional wastewater treatment facilities in St. Thomas and St. John; (ii) construct an outfall extension for the wastewater treatment plant in St. Croix; (iii) replace the Anguilla Force Main in St. Croix; and (iv) implement plant-by-plant operational improvements and pump station rehabilitation throughout the Territory, including the replacement of equipment, repairs, and maintenance at 37 wastewater

facilities. These projects are currently funded by EPA and the bond proceeds (see note 9). As of September 30, 2002, $7.7 million of the proceeds of the Series 1998 E Bonds remained unexpended.

In fiscal year 2002, the EPA levied a fine of $25 million against the Government for failure to comply with mandates pertaining to the management of solid waste disposal. In October 2002, the Government negotiated with EPA to pay $1.6 million of this fine and in December 2002 appropriated $8.4 million for the start-up costs associated with the Wastewater Treatment Facility on the island of St. Croix.

GERS filed a lawsuit in District Court, in April 2001, to recover approximately $42.6 million in administrative payments, as well as $23 million for breach of contract, from the general fund of the Government. No liability has been accrued as of September 30, 2002.

(b) Discretely Presented Component Units

WAPA estimates that capital expenditures in connection with continuing capital improvements will be approximately $40 million for the Electric System and $12.5 million for the Water System during the year ended June 30, 2002. WAPA is presently a defendant or codefendant in various lawsuits; however, any adverse outcome involving a material claim is expected to be substantially covered by the insurance. WAPA facilities were damaged by Hurricane Hugo in September 1989. WAPA reconstructed its system with proceeds from insurance and FEMA. On March 23, 1998, FEMA issued an audit report concluding that WAPA should refund approximately $7.9 million aggregated questioned costs. Approximately $2.6 million of these questioned costs are related to an oil spill that was subsequently settled with FEMA. During 1998, WAPA submitted a second appeal for $4.4 million of the remaining questioned costs and agreed to refund approximately $900,000 of questioned costs to FEMA. During 1999, FEMA denied WAPA's second appeal and formally closed the Hurricane Hugo disaster. At June 30, 2002, WAPA has recorded a liability of $5.3 million for amounts owed to FEMA for overpayments related to these questioned costs. FEMA has not made a formal request for repayment of these funds.

In September 1995, WAPA's facilities suffered extensive damage from Hurricane Marilyn. During 1996, WAPA reconstructed its system with proceeds from insurance and FEMA. In March 1999, FEMA denied WAPA's claim for $8.9 million of remaining expenditures related to the reconstruction. WAPA has subsequently reduced its claim to $5.7 million and is currently negotiating with FEMA regarding reimbursement of these remaining expenditures. Although management of WAPA believes the ultimate resolution of this matter will result in WAPA receiving additional reimbursement for prior expenditures, WAPA has not recorded any amounts to reflect these potential recoveries in the accompanying financial statements.

At June 30, 2002, there was $20 million outstanding under the lines of credit for the Electric and Water Systems, respectively, and no funds were available for borrowing under these lines. The lines of credit expire in April 2003, subject to annual renewal.

In connection with federal grants programs, VIPA is obligated to administer and spend the grant money in accordance with regulatory restrictions, and is subject to audit by the grantor agencies. In cases of noncompliance, the agencies involved may require VIPA to refund programs' moneys. During the normal course of business, VIPA is a defendant in various lawsuits. In the opinion of management and legal counsel, the outcome of these cases and resulting liability, if any, is either adequately covered by insurance or should not materially affect VIPA's financial position.

(12) Retirement Systems

(a) Plan Description

GERS is the administrator of a cost-sharing multiple-employer defined-benefit pension plan established as of October 1, 1959 by the Government to provide retirement, death, and disability benefits to its employees. The following description of the plan is provided for general information purposes only. Refer to the actual text of the retirement law in the V.I. Code, Title 3, Chapter 27 for more complete information. Regular employees are eligible for a full service retirement annuity when they have completed 30 years of credited service or have attained the age of 60 with at least 10 years of credited service. Members who are considered "Safety Employees," as defined in the V.I. Code, are eligible for full retirement benefits when they have earned at least 20 years of government service or have reached the age of 55 with at least 10 years of credited service. Regular employees who have attained the age of 50 with at least 10 years of credited service can elect to retire early with a reduced benefit. Senators and members of the Legislature may receive a retirement annuity when they have attained the age of 50 and completed six years of credited service or earned at least six years of credited service as a member of the Legislature. GERS is a blended component unit included in the financial reporting entity and is presented as a pension trust fund of the PG. GERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Employees' Retirement System of the Government of the Virgin Islands, GERS Complex, Veterans Drive, St. Thomas, V.I. 00802.

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(b) Funding Policy

The Government's required contribution for the year ended September 30, 2002 was 14.5% of the member's annual salary. Since April 1, 1991, required member contributions are 8% of annual salary for regular employees, 9% for senators, and 10% for Act 5226 eligible employees. Through September 30, 2000, member contributions were refundable without interest upon withdrawal from employment before retirement. Subsequent to September 30, 2000, legislation was passed that provided for 4% annual interest on refunded contributions. The Government's contributions to the plan for the years ended September 30, 2002 amounted to $50.5 million that represented 53.15%, of the annual required contributions. In August 1994, legislation providing an early retirement incentive was passed. The legislation was subsequently amended on October 13, 1994, December 30, 1994, and December 5, 1995. Among other matters, the legislation allows a member of GERS who has a combined aggregate number of years of credited service plus number of years of age, equal to at least 75 years as of the date of the legislation to retire without reduction of annuity. Members, who have attained the age of 50 with at least 10 but less than 30 years of credited service, may add an additional three years to their age for this computation. Members with 30 years of service or who can retire without penalty under the V.I. Code shall have their average compensation increased by four percentage points.

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

For employees electing to retire under Section 8(b) of the Act, the Government contributes to GERS a sum equal to the additional contribution the employer and employee would have made had the employee received a salary 4% higher during the three years used to compute the employee's "average compensation" figure, plus a sum of $5,000. Based on the calculation, this amount was $16.1 million as of September 30, 2002. As of September 30, 2002, GERS has received $6.9 million of such amount.

The actuaries of GERS have determined that the specific funding provided under the Early Retirement Act of 1994 is inadequate to cover the costs of the program. GERS is seeking to recover any unfunded costs of the program under a newly enacted provision of the retirement law, which provides that the employer will compensate GERS for the costs of any special early retirement program.

The University has two retirement plans in which all eligible employees are required to participate. The Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) is a defined contribution pension plan covering participating, full-time faculty members and other exempt employees, under which the contributions, including employees' contributions, are used to purchase annuities. There are no unfunded past service costs, and vested benefits are equal to the annuities purchased under TIAA-CREF. As of September 30, 2002, 232 faculty members and other employees were TIAA-CREF participants. The number of active participants from the University participating in GERS as of September 30, 2002 was 280. Total contributions made by the University to TIAA-CREF participant accounts amounted to $738,822.

(13) Additional Information – Enterprise Funds

The enterprise funds are composed of approximately 47 funds and two entities that provide a variety of services to commercial and government entities as well as individuals. It includes the operation of health facilities, dock facilities, a shopping mall, lottery services, loan programs, insurance, housing facilities, commercial services, and others.

The significant funds and entities are as follows:

(a) Virgin Islands Lottery

The Lottery was created as an instrumentality of the Government by Act No. 3055 of May 28, 1971. The revenue is generated from the sale of tickets to pay administrative expenses and prizes and increase general fund revenue. The Lottery is required to transfer to the general fund not less than 8% of total revenue and the surplus, if any, from its operation in accordance with Title 32 of the V.I. Code. The prize money of a drawing for which the winning ticket is not sold, is carried over and added to the prize money of the next drawing. Any unclaimed prizes, after six months of being awarded, are retained by the Lottery for the payment of future prizes.

(b) Government Insurance Fund

The Government Insurance Fund accounts for the operating results of the administration of the Workmen Compensation Law. The law was created on July 1, 1941, to insure workers in the event of work-related accidents. Revenue consists of premiums collected from all employers in the Virgin Islands. Expenses are mainly administrative and benefits provided to covered employees. Temporary benefits provided include medical rehabilitation, restoration of a portion of lost wages and vocational rehabilitation, when necessary continuous income benefits are paid for permanent total disability, lapsing upon death of the recipient.

(c) Unemployment Insurance Fund

The Unemployment Insurance Fund is a federally mandated program to assess employers for unemployment insurance. The assessments are remitted to the U.S. Treasury and drawdowns are made to pay eligible unemployed recipients. During the fiscal year ended September 30, 2002, the Territory collected $4 million in insurance assessments and paid $16.8 million in benefits. Of the amount paid in benefits, $1.8 million was funded through the Temporary Extended Unemployment Benefits (TEUCA) of the Federal Reed Act Distribution of March 13, 2002. The Virgin Islands share of the Reed Act Distribution was $1.95 million. As of September 30, 2002, the Government had a restricted balance of $57.8 million with the U.S. Treasury to fund unemployment insurance claims.

(d) The West Indian Company

WICO is engaged in the operation of a dock facility and shopping mall in St. Thomas. The Government acquired all of the outstanding stock of WICO, on July 1, 1993, for a purchase price of $54 million. In connection with the purchase, the Government obtained a short-term note payable amounting to $18 million. On December 21, 1993, the note payable was refinanced with a long-term loan amounting to $18.2 million with interest rate of 5.75% payable in monthly installments of $127,000, including interest and a final payment comprised of the principal sum outstanding and all accrued unpaid interest to the date of the final payment.

In 2000, WICO obtained an additional long-term loan in the amount of $8 million, bearing interest at 7.48%. Effective October 1, 2001, the loan is payable in 239 monthly installments of $64,000, and a final payment of principal and interest outstanding. The revenue of WICO is pledged for the payment of principal and interest on the loans.

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS
Notes to Basic Financial Statements
September 30, 2002

Debt service requirements for loans payable outstanding at September 30, 2002 were as follows (expressed in thousands):

		Principal	Interest	Total
Year:				
2003	$	1,030	1,272	2,302
2004		1,093	1,209	2,302
2005		1,161	1,140	2,301
2006		1,234	1,067	2,301
2007		1,312	990	2,302
2008-2012		7,804	3,706	11,510
2013-2017		4,073	1,703	5,776
2018-2022		2,617	669	3,286
Total	$	20,324	11,756	32,080

(e) Condensed Financial Information of Significant Enterprise Funds

Condensed financial information of significant enterprise funds as of September 30, 2002 and for the year then ended is presented below (expressed in thousands):

Schedule of Net Assets

September 30, 2002

	Unemployment insurance	West Indian Company	Lottery	Government insurance fund	Other enterprise funds	Total enterprise funds
Current assets	$ 353	8,347	1,573	6,839	1,011	18,123
Due from other funds	—	—	—	—	300	300
Other assets	57,833	2,678	—	—	—	60,511
Capital assets	—	31,452	94	—	5,733	37,279
Total assets	58,186	42,477	1,667	6,839	7,044	116,213
Current liabilities	8,610	2,345	2,380	367	423	14,125
Due to other funds	—	500	4,468	—	614	5,582
Other liabilities	—	19,294		—	—	19,294
Total liabilities	8,610	22,139	6,848	367	1,037	39,001
Net assets:						
Invested in capital assets, net of related debt	—	11,128	94	—	5,733	16,955
Restricted	49,576	9,210	—	—	—	58,786
Unrestricted	—	—	(5,275)	6,472	274	1,471
Net assets (deficit)	$ 49,576	20,338	(5,181)	6,472	6,007	77,212

Schedule of Changes in Net Assets

Year ended September 30, 2002

	Unemployment insurance	West Indian Company	Lottery	Government insurance fund	Other enterprise funds	Total enterprise funds
Operating revenue:						
Total operating revenue	$ 6,152	9,995	14,061	7,652	7,830	45,690
Operating expenses:						
Operating expenses	22,276	6,157	13,910	7,426	11,386	61,155
Depreciation and amortization	—	1,227	67	—	367	1,661
Total operating expenses	22,276	7,384	13,977	7,426	11,753	62,816
Operating income (loss)	(16,124)	2,611	84	226	(3,923)	(17,126)
Nonoperating revenue (expenses):						
Total nonoperating revenue (expenses)	3,974	(1,067)	—	—	521	3,428
Income (loss) before transfers	(12,150)	1,544	84	226	(3,402)	(13,698)
Transfers from other funds	—	—	—	—	2,594	2,594
Transfers to other funds	—	(1,300)	—	—	—	(1,300)
Change in net assets	(12,150)	244	84	226	(808)	(12,404)
Net assets, beginning of year (as restated)	61,726	20,094	(5,265)	6,246	6,815	89,616
Net assets, end of year	$ 49,576	20,338	(5,181)	6,472	6,007	77,212

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Schedule of Cash Flows

Year ended September 30, 2002

	Unemployment insurance	West Indian Company	Lottery	Government insurance	Other funds	Total enterprise funds
Net cash provided by (used in) operating activities	$ (10,409)	3,803	(115)	(31)	(8,741)	(15,493)
Net cash provided by (used in) noncapital financing activities	—	(1,300)	—	—	2,594	1,294
Net cash used in capital and related financing activities	—	(3,822)	—	—	—	(3,822)
Net cash provided by investing activities	3,974	220		—	361	4,555
Net decrease in cash and cash equivalents	(6,435)	(1,099)	(115)	(31)	(5,786)	(13,466)
Cash and cash equivalents, beginning of year (as restated)	64,621	9,008	1,070	5,205	708	80,612
Cash and cash equivalents, end of year	$ 58,186	7,909	955	5,174	(5,078)	67,146

(14) Liquidity

At September 30, 2002, the Government had an unrestricted deficit in the governmental activities amounting to $859 million mostly attributed to long-term debt amounting to approximately $1.39 billion, which was required to be recognized in the statement of net assets pursuant to the adoption of GASB No. 34. The Government has initiated specific actions to improve its future cash flows through the issuance of long-term debt, engaging a consulting firm to assist them in their efforts to develop a series of detailed revenue enhancement and expenditure reduction initiatives and the enactment of certain laws directed toward improving the Government's financial situation. In October 1999, the Government and the U.S. Department of Interior (DOI) entered into a Memorandum of Understanding (the MOU) whereby the Government agreed to use its best efforts to undertake certain deficit reduction initiatives. As a condition to certain new and additional federal financial and technical assistance included in or being proposed by federal appropriations or other legislation, certain financial performance and accountability standards were agreed upon by the Government, which the DOI believes are necessary for the Government to achieve long-term economic recovery. Pursuant to the MOU, the release of such new and additional federal funds to the Government is subject to compliance with such performance and verifiable objectives agreed upon in such agreement. The accountability and financial performance standards agreed upon in the MOU include: (i) preparation of five-year financial recovery plan to be provided to DOI within 90 days of the date of the MOU; (ii) a fiscal year 2000 budget mandating substantial reductions in departmental budgets and overall general fund fiscal year 2000 expenditures not to exceed $432.1 million; (iii) absent extraordinary circumstances to maintain balanced budgets after fiscal year 2003 with any generated

surpluses applied to the reduction of the accumulated deficit and unfunded obligations; (iv) annual preparation of financial reports; and (v) efforts to reduce the outstanding debt of the Government. On October 29, 1999, the DOI and the Government entered into an amendment of the MOU, which amended the Government's requirement to seek change in the Virgin Islands public labor relations law to comply with federal labor law. Pursuant to such amendment, the Government, in collaboration with union representatives, is encouraged to pursue reform initiative through collective bargaining to bring fiscal solvency to the Government. In addition to the financial performance standards set forth in the MOU, the MOU further provides for the DOI and the Government to enter into a program of preservation and enhancement of the natural, cultural, and historic resources of the U.S. Virgin Islands to stimulate local economic growth through sustainable tourism. The Government is discussing with DOI certain events of noncompliance, remedial action necessary to comply with the provisions of the MOU and its effect on the Government's financial condition and results of operations.

In April 2000, the Economic Recovery Task Force submitted the five-year operating and strategic financial plan to the Governor for action. The plan provides over 200 recommendations that propose to reduce and eventually eliminate the structural budget deficit by restructuring and reforming Government operations and forging a partnership with the private sector intended to result in sustained growth.

In January 2003, the U.S. Department of Interior issued an Audit Report concluding that all criteria of the MOU were partially or substantially achieved except: (i) implementation of collective bargaining reforms to assist the fiscal solvency of the Government, and (ii) completion of comprehensive annual reports within 120 days of year-end and single audits within nine months of year-end. As part of the MOU, the Government has committed to maintaining balanced budgets after the fiscal year ended September 30, 2003, with any surpluses applied to liquidating outstanding debt. The U.S. Department of Interior acknowledged that it had not achieved its objective of providing funding for the V.I. Conservation Fund, and committed to providing funds for capital improvements, technical assistance, and other assistance once the Government has achieved substantial compliance.

As mentioned in note 16, in September 2003, the Government received a $100 million Revenue Bond Anticipation Note for the payment of income tax refunds and operating expenses.

(15) Restatements

During the year ended September 30, 2002, the Government implemented several new accounting standards and an interpretation issued by GASB, as previously stated in note 1.

GASB No. 34, as amended by GASB No. 37, establishes new financial reporting standards for state and local governments. This statement's requirements represent a significant change in the financial reporting model used by state and local governments, including statement formats and changes in fund types and elimination of account groups. In addition to fund financial statements, governments are required to report government-wide financial statements, prepared using the accrual basis of accounting and the economic resources measurement focus. As a result, fund reclassifications and adjustments to the fund equities reported in the prior financial statement balances were required.

GASB No. 35 establishes accounting and financial reporting standards for public colleges and universities within the financial reporting guidelines of GASB No. 34. The University reported as a discretely presented component unit adopted the requirements of GASB No. 35.

GASB No. 38 requires certain note disclosures when GASB No. 34 is implemented. The provisions of these new standards have been incorporated into the basic financial statements and notes.

GASB Interpretation No. 6 clarifies the application of existing standards for distinguishing the respective portions of certain types of liabilities that should be reported as (i) governmental fund liabilities and (ii) general long-term liabilities of the Government. The provisions of this interpretation have been incorporated into the basic financial statements and notes.

These new accounting standards caused most of the accounting changes, changes in reporting entity, and restatements described in the ensuing discussions below. Changes and restatements for reasons other than the adoption of the above pronouncements are also explained below.

The following schedule reconciles the September 30, 2001 fund balance/net assets as previously reported by the primary government to beginning fund balance/net assets, as restated (expressed in thousands).

	September 30, 2001 fund balance/net assets, as previously reported	Fund reclassifications	Change in basis of accounting	September 30, 2001 fund balance/net assets, as restated
General	$ 71,652	(24,835)	57,511	104,328
Debt service	$ 110,262	(24,391)	—	85,871
Nonmajor governmental funds:				
Special revenue	$ 13,837	49,001	(3,605)	59,233
Capital projects	57,566	7,744	(7,210)	58,100
Total	$ 71,403	56,745	(10,815)	117,333
Enterprise funds:				
Unemployment insurance	$ —	64,621	(2,895)	61,726
West Indian Company	20,094	—	—	20,094
Nonmajor enterprise funds	(2,026)	8,900	922	7,796
Total	$ 18,068	73,521	(1,973)	89,616
Trust and agency funds:				
Pension trust	$ 1,214,183	—	—	1,214,183
Unemployment insurance	64,621	(64,621)	—	—
Other expendable trust	16,419	(16,419)	—	—
Total	$ 1,295,223	(81,040)	—	1,214,183

The most significant changes in fund structure occurring between fiscal year 2001 and 2002 include the following:

- Major funds were identified and separately reported based on criteria specified in GASB No. 34 and other qualitative factors. In prior years, all funds were reported by fund type, as defined by accounting principles generally accepted in the United States of America, without respect to whether the fund type was significant.
- A number of funds reported in agency funds were reclassified to the general fund.
- The expendable trust funds were eliminated and reclassified to the special revenue, enterprise, general, capital projects.

The following table summarizes changes to fund equities as previously reported in the balance sheet by certain discretely presented component units. The changes resulted primarily from implementation of these GASB statements and reclassifications in the manner of presentation of certain component units (expressed in thousands):

Beginning net assets, as previously reported	$	715,436
Restatements:		
Virgin Islands Housing Authority		(29,792)
Roy L. Schneider Hospital		2,215
Magens' Bay Authority		24
Economic Development Authority		(868)
University of the Virgin Islands		(48,699)
Beginning net assets, as restated	$	638,316

The beginning net assets' restatement noted in the VIHA was attributed to a change in 2000 depreciation expense and an overstatement of debt amortization fund in 2000. Beginning of year net assets were reduced by $12 million for prior years depreciation and by $17 million for debt amortization fund.

The beginning net assets' restatement noted in the Roy L. Schneider Hospital, the Economic Development Authority, and MBA was attributed to prior period adjustments.

The University was reported in previous years as a public university fund. With the implementation of GASB No. 34 and No. 35, the University is now reported within the same column as all other discretely presented component units. Changes in the beginning net assets of the University relates to the adoption of GASB No. 35, attributed to the depreciation of capital assets, reporting tuition and fee revenue net of certain scholarship allowances and reporting revenue from auxiliary enterprises net of cost of goods sold and scholarships and allowances. Beginning of year net assets was reduced by $27 million for prior years infrastructure depreciation and by $21 million for property, plant, and equipment adjustments.

(16) Subsequent Events

(a) Primary Government

In November 2002, the Refinery entered into a resolution with the PG allowing the issuance of $25.7 million private activity bonds to repay costs incurred in the construction of a coker plant completed in June 2002. All debt service amounts related to the bonds are paid by the Refinery.

In November 2002, the PG issued GARVEE bonds amounting to $18.5 million under an agreement with the U.S. Federal Highway Administration. The bond proceeds are to be used for commercial port facilities. Federal highway funds are utilized for debt servicing requirements.

In September 2003, the PG received a $100 million Revenue Bond Anticipation Note, Series 2003 from a local bank for the payment of income tax refunds and operating expenses of the Government. Interest on the loan is 3.25% for the first six months outstanding, and 3.5% thereafter.

In November 2003, the excise tax on rum of 13.5 cents per gallon was extended to December 2004. The amount had been set to expire on December 31, 2003.

In December 2003, the PFA issued $257.9 million in Series 2003 A Revenue Bonds. The proceeds of the bonds will be used to: (i) repay the Revenue Bond Anticipation Note, Series 2003 of $100 million mentioned above, (ii) fund certain necessary public safety and other public sector capital development projects, (iii) fund the Debt Service Reserve Account, and (iv) pay the costs of issuing the Series 2003A Bonds. The bonds are supported by pledged gross receipts taxes.

(b) Component Units

In June 2003, WAPA issued $70 million in electric revenue bonds. The bonds will be used to pay off an existing line of credit and to fund capital projects.

In August 2003, the VIHA went into federal receivership due to default of the agreement that allows it to receive federal funding.

On January 16, 2003, the VIPA issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable), with principal amounts of $18,005,000 and $17,425,000, respectively. VIPA plans to use the proceeds of the bonds to finance the dredging, rehabilitation, and construction of berthing piers for cruise and seagoing vessels at Crown Bay in St. Thomas, and the construction of certain buildings to be used for commercial, retail, and cultural purposes at the dock facilities.

In August 2003, the U.S. Department of Housing and Urban Development (HUD) declared VIHA to be in substantial default of its annual contributions contract with HUD and placed VIHA in receivership. HUD assumed possession of all assets, projects, and programs.

On January 23, 2004, the Waste Management Authority was created by Act No. 6638 as a nonprofit, public body corporate and politic of the Government with the purpose of providing environmentally sound management for the collection and disposal of solid waste, including operation and closure of landfills, and wastewater collection, transport, treatment and disposal in the Territory. A board of directors consisting of seven member who will be appointed by the Governor will govern the authority.

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APPENDIX E

UNITED STATES VIRGIN ISLANDS
ECONOMIC AND DEMOGRAPHIC INFORMATION

Economic and Demographic Information

Geography, Landscape and Climate

The United States Virgin Islands — also known as the U.S. Virgin Islands or more commonly the Virgin Islands — is located some 1,600 miles southeast of New York City, about 1,075 miles from Miami, and 60 miles east of Puerto Rico. Approximately 70 small islands, islets and cays make up the Virgin Islands.

The principal islands are St. Croix, St. Thomas, St. John and Water Island. St. Croix, the largest of the four islands, has an area of 84 square miles and lies entirely in the Caribbean Sea. It is marked by undulating hills that rise gently to the north and lagoons that lie on the south coast. It has two main urban centers — Christiansted to the north and Frederiksted to the west — which both lie on a broad central plain. St. Thomas, which lies approximately 35 miles north of St. Croix, is 32 square miles in area. It is distinguished by a ridge of east-west hills that rise abruptly from the sea. It is marked by numerous sandy beaches along the shoreline, including Magens Bay. The main urban center, Charlotte Amalie, which also is the capital of the Virgin Islands, is surrounded by a protected deep water harbor. St. John is a 20-mile square area located approximately three miles east of St. Thomas. Its topography is similar to St. Thomas with steep, rugged hills and white-sandy beaches. About two-thirds of the island is preserved as the Virgin Islands National Park. Water Island is located approximately one-half mile from the harbor in Charlotte Amalie. Water Island was transferred to the Virgin Islands in December 1996 from the exclusive jurisdiction of the Department of Interior.

The Virgin Islands has temperatures ranging between 70°F and 90°F with an average of 78°F. Humidity is low and annual rainfall averages 40 inches. However, three hurricanes since 1989 – Hugo, Marilyn and Bertha – did cause considerable damage.

Population

In 2005, the population of the Virgin Islands was estimated at 112,128. St. Thomas has a population of 52,838. There are 54,957 people on St. Croix and 4,333 people in St. John. In 2005, the population of the Virgin Islands increased by 0.6% from 2004.

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Table 1
Comparative United States Virgin Islands and United States Population Growth 1950-2005

Year	United States Virgin Islands Population	Annual Percentage Increase (Decrease)	United States Population	Annual Percentage Increase (Decrease)
1950	26,665	–	152,271,417	–
1960	32,099	2.0%	180,671,158	1.9%
1970	62,468	9.5	205,052,174	1.3
1980	96,569	5.5	227,224,681	1.0
1990	101,809	0.5	249,464,396	1.0
1999	116,770	1.0	279,040,168	1.2
2000	108,612	(7.0)	282,177,754	1.1
2001	109,344	0.7	285,093,813	1.0
2002	110,026	0.6	287,973,924	1.0
2003	110,740	0.6	290,809,777	1.0
2004	111,459	0.6	293,655,404	0.9
2005	112,128	0.6	297,821,175	1.4

Sources: U.S. Census Bureau and United States Virgin Islands Bureau of Economic Research.

Per Capita Income

In 2005, per capita income of the Virgin Islands was $18,652, an increase of approximately 3.0% from 2004. In comparison, the per capita income in the United States was $34,586, an increase of approximately 4.6% for the same period.

Table 2
Comparative Per Capita Income United States Virgin Islands and United States 1980-2005 (current dollars)

Year	United States Virgin Islands	Annual Percentage Increase (Decrease)	United States	Annual Percent Increase (Decrease)
1980	6,230	–	10,183	–
1990	12,799	10.5%	19,572	9.2%
1999	16,242	2.8	27,843	3.5
2000	16,567	2.0	29,469	5.8
2001	16,898	2.0	30,271	2.7
2002	17,236	2.0	31,039	2.5
2003	17,581	2.0	31,632	2.4
2004	18,108	3.0	33,050	4.5
2005	18,652	3.0	34,586	4.6

Sources: U.S. Bureau of Economic Analysis and United States Virgin Islands Bureau of Economic Research.

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Employment

Civilian employment grew during 2003, 2004 and 2005. Modest growth in employment is expected due to tourism-related development activity, and construction through Government capital improvement programs is anticipated to continue through 2006. The improvement in the job market was largely a result of an increase in private sector jobs, particularly in construction and financial services.

The Virgin Islands' unemployment rate decreased to 7.1% in 2005 from 7.8% in 2004. The unemployment rate rose to 9.4% in 2003, primarily as a result of the completion of construction of the coker plant by Hovensa, which left approximately 2,000 construction workers unemployed.

Table 3
United States Virgin Islands Labor Force,
Employment and Unemployment Rates and
United States Unemployment Rates
2001-2005

Year	Labor Force	Employment	Unemployment Rate United States Virgin Islands	Unemployment Rate United States
2001	49,900	46,370	7.1%	4.7%
2002	49,457	44,975	8.7	5.8
2003	48,170	43,640	9.4	6.0
2004	50,066	46,295	7.8	5.5
2005	50,906	47,301	7.1	5.1

Sources: United States Virgin Islands Department of Labor, Bureau of Labor Studies Reports, and the U.S. Department of Labor, Bureau of Labor Statistics.

About 71% of the Virgin Islands' jobs are provided by the private sector. Private sector employment growth is fueled by tourism and related services. The services sector experienced positive growth during 2005, and currently accounts for 25% of private employment. Wholesale and retail trade accounted for 23%, while construction, mining and manufacturing accounted for 13%.

Total public sector employment, which accounts for approximately 29% of jobs in the Virgin Islands, remained virtually at the same level for 2004 and 2005. In 2005, there were 12,318 public sector jobs compared to 12,368 in 2004. Federal and local government are the largest employers in the public sector, with local government as the source of over 90% of all public sector jobs. The number of local government jobs was 11,445 in 2005 compared to 11,796 local government jobs in 2002. This trend of decreases in local government employment is due to certain of the Government's cost-cutting measures. The decline is likely to continue at a decreasing rate and then flatten. The number of United States federal government jobs was 873 in 2005, up slightly from 860 in 2004.

Table 4
Annual Wage and Salary Employment
United States Virgin Islands
2001-2005

	2001	2002	2003	2004	2005
Private sector:					
Construction & mining	3,697	3,017	1,666	1,709	1,901
Manufacturing	2,191	2,148	2,019	2,084	2,208
Transportation, communication & public utilities	2,507	2,446	1,429	1,518	1,549
Wholesale & retail trade	9,602	9,787	6,845	6,886	6,938
Finance, insurance & real estate	1,931	1,918	2,370	2,517	2,536
Leisure and Hospitality	-	-	6,836	7,131	7,023
Information	-	-	873	893	890
Services (professional, business, education, health)	12,113	11,195	10,733	7,446	7,732
Total Private Sector	**32,041**	**30,511**	**29,095**	**30,184**	**30,777**
U.S. federal government	905	905	905	860	873
Territorial government	11,438	11,796	11,657	11,508	11,445
Total Government	**12,343**	**12,701**	**12,562**	**12,368**	**12,318**
Total	**44,384**	**43,212**	**41,657**	**42,552**	**43,095**

Source: United States Virgin Islands Department of Labor, Bureau of Labor Statistics. Some figures may not add due to rounding. Nonagricultural wage and salary employment 2003 series have been converted from the 1987 Standard Classification (SIC) system to the North American Industry Classification System (NAICS).

In 2002, hotels and other lodging places accounted for 44.1% of the total tourism-related employment, eating and drinking places accounted for 25.8%, gift shops and other retail stores accounted for 23.9% and transportation accounted for 6.2%.

Table 5
Selected Tourism-Related Employment
United States Virgin Islands
2001-2005

	2001	2002	2003	2004	2005
Hotels & Other Lodging Places	4,060	3,930	4,020	4,260	4,054
Gifts Shops & Other Retail Stores*	2,110	2,130			
Eating & Drinking Places	2,290	2,300	2,230	2,360	2,476
Transportation*	560	550			
Total	**9,020**	**8,910**	**6,250**	**6,620**	**6,530**

Source: United States Virgin Islands Department of Labor, Bureau of Labor Statistics. Some figures may not add due to rounding.
*Nonagricultural wage and salary employment 2003 series have been converted from the 1987 Standard Classification (SIC) system to the North American Industry Classification System (NAICS), and thus are no longer reported.

Presented below are the ten largest private sector employers in the Virgin Islands as of July 2006.

Table 6
United States Virgin Islands
Ten Largest Employers
Private Sector
(July 2006)

	Name of Employer	Principal Business
1.	Hovensa L.L.C	Oil Refining
2.	Turner St. Croix Maintenance......	Maintenance
3.	Ritz-Carlton Hotel VI Inc.	Resort Hotel
4.	Triangle Construction and Maintenance Corp.	Construction
5.	Innovative Telephone Corporation	Utility
6.	CBI Acquisition, LLC.................	Resort Hotel
7.	Westin St. John Hotel, Inc.	Resort Hotel
8.	Plaza Extra Supermarket, St. Croix	Grocery Store
9.	K-Mart Corporation	Department Store
10.	Frenchman's Reef Beach Resort	Resort Hotel

Source: United States Virgin Islands Department of Labor, Bureau of Labor Statistics.

Hovensa L.L.C. ("Hovensa"), a limited liability joint venture between Amerada Hess and Petróleos de Venezuela, is the largest manufacturer in the Virgin Islands and the industry's strongest performer. The company owns and operates one of the largest crude oil refineries in the world located in St. Croix. In July 2002, the company completed the construction of a new 58,000 barrels per day delayed coking unit at the refinery. This coker unit began commercial operations in August 2002, and integration and performance testing was completed in September 2003. The Authority and the Government have issued bonds to provide reimbursement to Hovensa for certain costs of the construction of the new coking unit. See "UNITED STATES VIRGIN ISLANDS – Outstanding Indebtedness of the Government."

Tax Incentives Programs

Economic Development Commission

The Government offers various tax incentives that promote industrial and economic development in the Virgin Islands. The most notable incentive program was created by the Legislature in October 1975. The Government of the Virgin Islands Industrial Development Commission, subsequently renamed as the Economic Development Commission (the "Commission" or the "EDC"), was created to promote the growth, development and diversification of the economy of the Virgin Islands. Qualifying businesses—corporations, partnerships or sole proprietorships—receive various benefits if they meet certain criteria set forth in the legislation. Gross Receipts Taxes are eligible for abatement by the Commission that could result in a reduction of Gross Receipts Taxes payable to the Government.

To qualify for tax incentives, investors must invest at least $100,000, exclusive of inventory, in an eligible business and employ at least ten Virgin Islands residents full-time. Small, locally-owned manufacturers of import substitutes or tourist souvenirs may receive EDC benefits for up to five years if they invest at least $20,000 and have two employees. A beneficiary receives a substantial reduction in, or an exemption from, all taxes imposed on businesses, including the Gross Receipts Taxes. Most importantly, the industrial development legislation permits a 90% income tax reduction, resulting in a maximum tax rate of less than 4% on income for approved operations. Tax benefits also extend to passive income from certain qualifying investments, such as the Virgin Islands government obligations. The 90% reduction extends to dividends received by a beneficiary's Virgin Islands resident shareholders. Currently, 112 enterprises are operating with incentive benefits granted pursuant to the EDC Program, 80 enterprises have been approved for benefits but have not elected to commence receipt of benefits and an additional 29 enterprises are awaiting final certification to the Commission. Investors receiving tax benefits under this program include hotels and other tourism-related businesses, goods-producing enterprises, and businesses serving customers outside the Territory. See "GROSS RECEIPTS TAXES."

The American Jobs Creation Act of 2004 ("Jobs Act") made significant changes to the federal tax rules affecting the EDC benefits. Specifically, the Jobs Act created a strict 183 day residency requirement instead of the previous facts and circumstances test for Virgin Islands residency and changed the rules regarding Virgin Islands' sourced income. As a result of the changes brought about by the Jobs Act, the EDC has seen a reduction in the number of applications submitted for EDC benefits from a high of 78 in fiscal year 2003 to 27 applications submitted in fiscal year 2005. There has been a reduction in the number of applicants seeking benefits as Designated Services Companies, which are mainly financial services and consulting companies and which are required to have clients or customers outside of the Virgin Islands. The EDC has not seen a material decline in the number of non-Designated Service Company applicants. As a result of the changes caused by the Jobs Act the EDC has implemented a mitigation program to assist EDC beneficiaries who can document economic harm or loss. To date 23 EDC beneficiaries have filed formal requests pursuant to the mitigation program. Six (6) EDC beneficiaries have requested waivers of the employment and charitable giving requirements for the benefits; ten (10) beneficiaries have sought six (6) month suspension of their certificate of benefits, and; seven (7) beneficiaries have sought termination of their benefits and discontinued operations in the Virgin Islands.

While in the past the Commission had certain compliance monitoring requirements, it lacked adequate personnel to fully enforce compliance with the Commission program requirements. The Commission now has six (6) compliance officers which it feels is adequate to monitor the current 112 EDC beneficiaries. The Commission developed more effective compliance monitoring mechanisms, including revocation and suspensions hearings which allow the Commission to collect retroactive taxes owed by beneficiaries who have failed to comply with Commission conditions. Such revocation and suspensions hearings typically occur three times in each Fiscal Year.

The following is a table setting forth the Commission's historical applicant information:

Table 7
Economic Development Commission
Historical Applicant Information
2001-2005

	2001	2002	2003	2004	2005
Number of Applications Received	24	48	78	40	19
Number of Applications Approved	19	45	53	9	12
Number of Applications Denied	2	0	3	0	0
Applications Pending	3	3	6	7	5
New Job Opportunities	619	1,202	1,097	1,498	605
Approximate Wages by New Applicants	$18,321,940	$36,955,860	$43,285,393	$40,684,988	$25,806,713
Minimum Potential Investment of New Applicants	$199,676,900	$162,022,016	$25,617,699	$59,380,321	$79,827,000

Source: Government of the Virgin Islands Economic Development Commission.

The EDC Program allows some qualifying investors to receive limited extensions or renewals of tax benefits, provided such investors fulfill certain criteria, including the ability to continue to promote economic development in the Virgin Islands. The Commission is currently trying to limit the numbers of extensions or renewals of benefits in favor of granting benefits to new businesses in growing industries such as financial services industries, tourism, marine and medical technology-based enterprises, which will further stimulate the economy of the Virgin Islands by providing positions for skilled labor and college educated personnel. The decrease in the minimum potential investment of new applicants since 2002 to 2003 was due to the absence of a major hotel operator application in 2003.

Section 934 Tax Incentives

Pursuant to 26 U.S.C. § 934 ("Section 934 Tax Incentives"), the Government, through the EDC, may provide certain tax reductions in income tax liability incurred to the Virgin Islands. See "Economic Development Commission." Such income tax reductions are permitted for (i) income derived from sources within the Virgin Islands or income effectively connected with the conduct of a trade or business within the Virgin Islands, (ii) income tax liability paid by citizens or residents of the United States, and (iii) income derived by qualified foreign corporations from sources outside the United States and which is not effectively connected with the conduct of a trade or business within the United States.

Section 934 Tax Incentives may have the effect of reducing the amount of income tax paid to the Government. However, such tax incentives may increase the conduct of business in the Virgin Islands.

Transportation

The Virgin Islands are accessible by air from around the world. The Cyril E. King Airport Terminal on St. Thomas was completed and opened in October 1990. The expansion of the runway to 7,000 feet was completed and opened in December 1992.

The Henry E. Rohlsen Airport Terminal on St. Croix has undergone major renovation and expansion. The terminal's square footage has doubled its previous size to 181,000 square feet. The runway has been further expanded to 10,000 feet.

Approximately 80 flights per week during the off-tourist season and 90 flights per week during the peak tourist season travel between the Virgin Islands and the United States mainland on six major airlines.

Over a dozen flights per day travel between St. Thomas and St. Croix, taking approximately 30 minutes, as well as regular ferry service. The island of St. John can be reached by seaplane and private ferry boat. Inter-island ferry service provides, several times daily, passenger service between St. Thomas and the nearby British Virgin Islands.

The Virgin Islands' internal transportation needs are served by a large number of taxis, taxivans, open-air buses, the public transit system (VITRAN) and rental cars.

Utilities and Energy Use

The Virgin Islands Water and Power Authority, an instrumentality of the Government ("WAPA"), owns and operates electric power generation and distribution facilities on St. Thomas and St. Croix and currently is the sole provider of electricity in the Virgin Islands with the exception of a limited number of commercial entities that produce electricity for their own use. WAPA provides electricity to approximately 50,000 customers. WAPA also operates a water production and distribution system and provides water service to approximately 10,000 customers. Gas is available from various companies throughout the Virgin Islands.

Electricity sales in 2005 increased by 3.5% from 2004 electricity sales, with sales to industrial users representing 47% of such sales, sales to residential users representing 36% of such sales and the remaining sales being to commercial users. Fuel consumption in 2005 decreased by 5.5% from 2004.

Tourism

Tourism is the Virgin Islands' largest industry and represents the largest segment in the private sector.

Visitor Arrivals

In 2005, the Virgin Islands recorded 2.605 million visitor arrivals. A slight decrease from the record 2.619 million visitor arrivals recorded in 2004. Visitor arrivals increased in each of 2003 and 2004.

After a decrease in tourism during 2001 and 2002, the performance in the tourism sector during 2003, 2004 and 2005 indicates that the sector is recovering. Total visitors in 2005 increased by 10% from 2002. Cruise passenger arrivals in St. John increased by 8% as compared to 2002. The number of cruise ship arrivals on St. Croix increased from 11 in 2004 to 48 in 2005 which helped account for a 118% increase in the number of cruise passengers arriving on St. Croix between those two years. In 2005, air visitors to St. Thomas and St. John increased by 9% as compared to 2002.

Table 8
United States Virgin Islands
Visitor Arrivals
2001-2005
(000's)

	2001	2002	2003	2004	2005
St. Thomas/St. John:					
Air Visitors	469.6	471.2	505.9	524.2	543.0
Cruise Passengers	1,790.5	1,671.3	1,751.9	1,960.9	1,910.2
Total Visitors	2,259.9	2,145.8	2,256.5	2,485.1	2,453.2
Number of Cruise Ship Visits*	909	812	878	922	814
St. Croix:					
Air Visitors	136.4	126.8	114.9	130.8	149.6
Cruise Passengers	237.4	120.5	23.0	25.0	54.5
Total Visitors	377.6	243.8	137.1	155.8	204.1
Number of Cruise Ship Visits*	138	71	25	11	48
Total U.S. Virgin Islands:					
Air Visitors	606.0	598.0	620.8	655.0	692.6
Cruise Passengers	1,891.4	1,738.7	1,773.9	1,964.7	1,912.5
Total Visitors	2,500.8	2,336.5	2,392.6	2,619.7	2,605.1
Number of Cruise Ship Visits*	976	845	888	924	818

*Actual, not thousands. Totals by island include first and second port of entry arrivals. Total arrivals for the U.S.V.I. include first territorial port of entry only; passengers visiting more than one U.S. Virgin Island during the same cruise are only counted once in the U.S.V.I. total. Consequently, the U.S.V.I. total will always be less than or equal to the sum of the two island totals as indicated.

Source: United States Virgin Islands Bureau of Economic Research.

Hotel Occupancy

Hotel occupancy increased slightly in 2005 to 63.8%, from 61.3% in 2004 although the number of hotel and condominium rooms decreased to 4,761 in 2005, down slightly from 4,959 in 2004. The decrease in rooms was a result of the closure of the Renaissance Hotel.

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Table 9
United States Virgin Islands
Hotel and Other Tourist Accommodations
2001-2005

	2001	2002	2003	2004	2005
St. Thomas/St. John:					
Total rooms/units	3,840	3,940	3,864	3,787	3,612
Number of hotels	30	30	29	31	30
Hotel rooms	3,099	3,168	3,119	3,034	2,830
Condominium/other units	741	773	745	753	782
Occupancy rate (percent)	59.3	61.0	62.3	65.2	66.1
St. Croix:					
Total rooms/units	1,213	1,197	1,180	1,172	1,149
Number of hotels	18	17	17	17	17
Hotel rooms	888	868	866	872	856
Condominium/other units	325	329	314	299	293
Occupancy rate (percent)	46.0	42.8	40.5	49.2	56.7
Total U.S. Virgin Islands:					
Total rooms/units	5,053	5,138	5,044	4,959	4,761
Number of hotels	48	47	46	48	47
Hotel rooms	3,987	4,036	3,985	3,906	3,686
Condominium/other units	1,066	1,102	1,059	1,052	1,075
Occupancy rate (percent)	56.6	57.0	57.2	61.3	63.8

Source: United States Virgin Islands Bureau of Economic Research.

Visitor Expenditures

Total expenditures by all visitors (tourists, cruise passengers and other excursionists) to the Virgin Islands totaled $1.493 billion in 2005, an annual increase of 10.1% from 2004.

Table 10
United States Virgin Islands
Visitor Expenditures
2001-2005
(in millions)

	2001	2002	2003	2004	2005
Tourists	$722.1	$723.5	$765.4	$789.8	$863.8
Excursionists:					
Day-trip by air	18.6	18.5	20.3	27.6	30.0
Cruise passengers	493.4	453.4	470.8	538.6	599.2
Total	512.0	471.9	491.1	566.2	629.2
Total Expenditures	**$1,234.1**	**$1,195.4**	**$1,256.5**	**$1,356.0**	**$1,493.0**

Source: United States Virgin Islands Bureau of Economic Research.

The Virgin Islands benefits from a $1,600 duty-free exemption for articles purchased in the Virgin Islands and either mailed or brought back to the United States mainland from the Virgin Islands once each 30 days without regard to the length of stay abroad while other countries in the Caribbean basin only have a $600 duty-free exemption (a two-to-one advantage). In addition, each adult is permitted to return with up to one gallon of duty-free liquor as compared to one quart from other areas. In response to falling U.S. tariff rates and increased competition from Caribbean neighbors, local customs duties and excise taxes were removed from selected tourist-oriented merchandise in 1982. As a result, prices of various luxury items, such as jewelry, china, cameras, leather goods, perfumes, watches and clocks, can be significantly below average United States mainland prices.

Construction and Real Estate

The construction sector averaged 1,834 in 2005 or 8.2% growth over 2004. First quarter fiscal year 2006 showed a 15.8 percent job growth over the same period in fiscal year 2005. Construction is expected to be strong during 2006, supported by major hotel construction, the upgrade and expansion of roads, housing and seaports and the development of commercial and residential properties. The construction of Hovensa's desulphurization unit, which began in September 2005, is expected to create 400 construction jobs. Additionally, the Yacht Haven Hotel and Marina is expected to add another 120 jobs.

The total value of approved building construction permits for all of the Virgin Islands, an indicator of current and future industry activity, rose 15.0% due to increases in private residential and non-residential construction from 2004 to 2005, particularly hotel and time share related construction on St. Thomas. Private residential construction increased by 22% on St. Thomas and St. John between 2004 and 2005 but was down by 23% on St. Croix during the same period. Private non-residential construction increased by 24% on St. Thomas and St. John from 2004 to 2005 but only increased by 7% on St. Croix.

Table 11
United States Virgin Islands
Value of Construction Permits
2001-2005

Year	Total USVI (millions)	Percent Increase (Decrease)	St. Thomas/ St. John (millions)	Percent Increase (Decrease)	St. Croix (millions)	Percent Increase (Decrease)
2001	164.3	(18.7)	106.6	(26.0)	39.9	(31.2)
2002	258.6	57.5	189.9	78.1	68.8	72.5
2003	255.6	1.2	174.7	(8.0)	80.9	17.6
2004	339.4	32.8	210.2	20.3	129.2	59.7
2005	390.2	15.0	274.3	30.4	115.9	(10.2)

Source: United States Virgin Islands Bureau of Economic Research.

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Table 12
United States Virgin Islands
Residential Real Estate Market Sales Analysis
2001-2005

	2001	2002	2003	2004	2005
St. Thomas/ St. John:					
Number of Homes Sold	218	224	249	304	244
Average Home Sales Price ($)........	365,879	408,219	546,488	509,879	649,655
No. of Condominium Sales.............	168	218	295	318	277
Average Condominium					
Sales Price ($)............................	117,210	133,435	144,333	184,498	234,233
St. Croix:					
Number of Homes Sold	180	197	256	283	267
Average. Home Sales Price ($).......	181,335	230,244	330,557	302,278	302,874
No. of Condominium Sales.............	125	151	188	233	261
Average Condominium Sales Price ($)............................	126,155	116,186	132,633	120,440	151,361
Total U.S. Virgin Islands:					
Number of Homes Sold	398	421	505	587	511
Average Home Sales ($).................	282,417	324,939	437,026	409,792	468,460
No. of Condominium Sales.............	293	369	485	551	538
Average Condominium Sales Price ($)............................	121,026	126,376	139,203	157,410	194,029

Source: United States Virgin Islands Bureau of Economic Research.

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The table below presents the largest real property taxpayers in the United States Virgin Islands in 2004.

Table 13
Largest Real Property Taxpayers of the
United States Virgin Islands
2004

Name	Assessment	Taxes
Hovensa	$1,880,452,628.66	$14,068,288.79
Lockhart Family (St. Thomas/St. Croix)	84,543,702.00	516,588.72
Topa Equities (St. Thomas/St. Croix)	57,470,604.00	437,529.55
Innovative Telephone (St. Thomas/St. Croix)	37,706,989.00	280,781.61
Palace Resorts	32,523,301.00	243,924.82
Hartman (Family)	40,924,979.00	220,701.75
Sunny Isles Shopping Center (De Chabert Family)	21,144,125.00	156,832.40
Ginn-LA Fund IV Magohany, LLC (Ginn-LA USVI Golf, LLP) (Ginn-LA Fund Sanctuary, LLC)	22,306,324.00	142,593.55
Cabrita Grand Estates, LLC	16,895,890.00	129,703.85
Banco Popular De Puerto Rico	16,083,370.00	120,625.28
Boschulte Family	16,270,908.00	94,785.44
St. Thomas Liquor Co.	12,303,597.00	94,327.00
B & W Realty Investment, Ltd	11,655,551.00	93,066.64
Davis Bay (Carambola)	11,099,013.00	83,242.60
Isidore Paiewonsky	8,927,526.00	67,512.05
V.I. Inns, Ltd/Circa 1675, LLP	6,496,789.00	51,375.88
K.R. Development (Joe Hodge/Bellevista)	5,269,922.00	22,353.17
Buccaneer & Armstrong Group	12,638,523.00	2,696.26

*Assessments are at 100%.

Source: United States Virgin Islands Office of the Tax Assessor.

Capital Program

Since 1998, the significant capital projects funded by the Government are summarized below:

Project	Funded Amount ($ millions)	Source of Funding
Hazard Mitigation	$42.0	Bond proceeds and Federal funds
Wastewater Treatment Facilities	40.8	Bond proceeds, Federal funds, General Fund and other funding
School Construction	40.2	Bond proceeds
Crown Bay Cruise Ship Terminal	35.0	Bond proceeds
Road and Other Repairs	33.3	Federal funds
Correctional Facilities	24.4	Bond proceeds
Enighed Pond Port	16.0	Bond proceeds
Government House Renovation	12.0	Bond proceeds and other funding
WAPA Infrastructure Project St. Croix	10.7	Bond proceeds
Flood Control	10.3	Bond proceeds, Federal funds and other funding
Frederiksted Waterfront Development	6.0	Bond proceeds
Red Hook Ferry Terminal Improvement	6.0	Bond proceeds
Henry E. Rohlsen FAA Tower	4.5	Federal funds
Charles Harwood Phase I	4.0	Bond proceeds
Cruz Bay Parking Facility	2.1	Other funding
Sugar Estate Head Star	2.1	Federal funds

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Appendix F

DTC BOOK-ENTRY-ONLY SYSTEM

The Depository Trust Company ("DTC"), New York, New York will act as securities depository for the Series 2006 Bonds. The Series 2006 Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Series 2006 Bond certificate will be issued for each series and maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provision of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfer and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities, clearing Corporation, MBS Clearing Corporation and Emerging Markets Clearing Corporation, also subsidiaries of DTCC, as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). The DTC Rules applicable to Participants are on file with the Securities and Exchange Commission.

Purchases of Series 2006 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for such Series 2006 Bonds on DTC's records. The ownership interest of each actual purchaser of each Series 2006 Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers or ownership interests in the Series 2006 Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Series 2006 Bonds, except in the event that use of the book-entry system for the Series 2006 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2006 Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Series 2006 Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series 2006 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series 2006 Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participant to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Series 2006 Bonds may wish to take certain steps to augment to transmission to them to notices of significant events with respect to the Series 2006 Bonds, such as redemptions, tenders, defaults and proposed amendments to the Series 2006 bond documents. For example, Beneficial Owners of Series 2006 Bonds may wish to ascertain that the nominee holding the Series 2006 bonds for their benefits has agreed to obtain and transmit notices to Beneficial Owners.

Redemption notices shall be sent to DTC. If less than all the Series 2006 Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the series 2006 Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participant to whose accounts the Series 2006 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, redemption premium, if any, and interest payments on the Series 2006 Bonds will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts, upon DTC's receipt of funds and corresponding detailed information from the Authority or the Trustee, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, redemption premium, if any, and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Series 2006 Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, such Series 2006 Bond certificates will be printed and delivered. The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series 2006 Bond certificates will be printed and delivered.

The above information concerning DTC and DTC's book-entry system has been obtained from sources that the Authority and Underwriter believe to be reliable, but none of the Authority or the Underwriter take responsibility for the accuracy thereof. The Beneficial Owners should confirm the foregoing information with DTC, the Direct Participants or the Indirect Participants.

So long as Cede & Co. is the registered owner of the Series 2006 Bonds of a series, as nominee for DTC, references herein to Bondholders or registered owners of the Series 2006 Bonds of such series (bother than under the caption "TAX MATTERS") shall mean Cede & Co., as aforesaid, and shall not mean the Beneficial Owners of such Series 2006 Bonds.

When reference is made to any action which is required or permitted to be taken by the Beneficial Owners, such reference shall only relate to those permitted to act (by statute, regulation or otherwise) on behalf o such Beneficial Owners for such purposes. When notices are given, they shall be sent by the Trustee to DTC only.

NONE OF THE AUTHORITY, THE UNDERWRITER NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATION TO DIRECT PARTICIPANTS, TO INDIRECT PARTICIPANTS, OR TO ANY BENEFICIAL OWNER WITH RESPECT TO (1) THE ACCURACY OF ANY RECORDS MAINTAINED BY DTC, ANY DIRECT PARTICIPANT, OR ANY INDIRECT PARTICIPANT; (II) ANY NOTICE THAT IS PERMITTED OR REQUIRED TO BE GIVEN TO THE OWNERS OF THE SERIES 2006 BONDS UNDER THE RESOLUTIONS; (III) THE SELECTION BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY PERSON TO RECEIVE PAYMENT IN THE EVENT OF A PARTIAL REDEMPTION OF THE SERIES 2006 BONDS; (IV) THE PAYMENT BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY AMOUNT WITH RESPECT TO THE PRINCIPAL OR REDEMPTION PREMIUM, IF ANY, OR INTEREST DUE WITH RESPECT TO THE SERIES 2006 BONDS; (V) ANY CONSENT GIVEN OR OTHER ACTION TAKEN BY DTC AS THE OWNER OF THE SERIES 2006 BONDS; OR (VI) ANY OTHER MATTER.

APPENDIX G-l

FORM OF AUTHORITY CONTINUING DISCLOSURE AGREEMENT

This Continuing Disclosure Agreement (the "Disclosure Agreement"), dated September __, 2006, is executed and delivered by and between the Virgin Islands Public Finance Authority (the "Authority") and The Bank of New York Trust Company, N.A., a national banking association (the "Trustee"), in connection with the issuance by the Authority of its $219,490,000 original principal amount of Virgin Islands Public Finance Authority Revenue Bonds (Virgin Islands Gross Receipts Taxes Loan Notes) Series 2006 (the "Series 2006 Bonds"). Capitalized terms used in this Disclosure Agreement which are not defined herein shall have the respective meanings specified in the Indenture of Trust, dated as of November 1, 1999, between the Authority and the Trustee and, as to each Series of Bonds, the Supplemental Indenture pertaining thereto, as the Indenture or any Supplemental Indenture may from time to time be amended or supplemented in accordance with the terms thereof.

The Undertaking

1. Purpose of this Disclosure Agreement. This Disclosure Agreement is being executed and delivered for the benefit of the holders of the Series 2006 Bonds and delivered in order to assist the underwriter of the Series 2006 Bonds (the "Underwriter") in complying with the provisions of Section (b)(5)(i) of Rule 15c2-12 (the "Rule") promulgated by the Securities and Exchange Commission (the "SEC") under the Securities Exchange Act of 1934, as the same may be amended from time to time.

2. Disclosure. (a) The Authority shall provide certain financial and operating information in accordance with the provisions of Section (b)(5)(i) of the Rule as follows:

(i) Annual Financial Information with respect to each Fiscal Year of the Authority. "Annual Financial Information" means, collectively: (A) financial statements for the Authority prepared in accordance with government accounting standards and audited by an independent firm of certified public accountants in accordance with auditing standards generally accepted in the United States; (B) an update of the tabular information presented in the Official Statement dated September 19, 2006 with respect to the Series 2006 Bonds under the headings "GROSS RECEIPTS TAXES," "UNITED STATES VIRGIN ISLANDS" and APPENDIX E - "United States Virgin Islands Economic and Demographic Information"; (C) updated information with respect to the percentage of Gross Receipts Tax collections from the top 5 and the top 10 taxpayers; (D) the information regarding amendments to this Disclosure Agreement required pursuant to this Disclosure Agreement; together with (E) such narrative explanation as may be necessary to avoid misunderstanding and to assist the reader in understanding the presentation of financial and operating data concerning the Gross Receipts Taxes, the Authority and the United States Virgin Islands; and

(ii) the Authority shall provide summaries of the information provided by the Virgin Islands Bureau of Internal Revenue on Gross Receipts Taxes collected as reported by the Bureau of Internal Revenue and the quarterly review of Gross Receipts Taxes transferred to the Collecting Agent for deposit into the Special Escrow Account by the certified public accounting firm in accordance with the terms of the Loan Agreement, dated as of September 1, 2006, among the Government, the Trustee and the Authority.

The descriptions contained in clause 2(a)(i)(B) above constituting Annual Financial Information are of general categories of financial information and operating data. When such descriptions include information that no longer can be generated because the operations to which it related have been materially changed or discontinued, a statement to that effect shall be provided in lieu of such information.

The financial information described in clause 2(a)(i) and 2(a)(ii) above are hereinafter referred to collectively as the "Continuing Disclosure."

(b) The Authority will provide annually the financial information described in clause (2) above as follows: (i) with respect to the Annual Financial Information described in clause 2(a)(i)(A) above, within 180 days after the end of the Authority's Fiscal Year, (ii) with respect to the Annual Financial Information described in clause

2(a)(i)(B), (C) and (D) above, within 180 days after the end of the Authority's Fiscal Year, commencing not later than March 31, 2008 for the Authority's Fiscal Year ending September 30, 2007, and (iii) with respect to the information described in clause 2(a)(ii) above, within sixty (60) days after the end of each fiscal quarter during the Authority's Fiscal Year, commencing not later than November 30, 2006 for the fiscal quarter ending September 30, 2006. The Continuing Disclosure will be provided to each nationally recognized municipal securities information repository ("NRMSIR") and to the appropriate state information depository ("SID"), if any is hereafter created.

(c) Any of the Continuing Disclosure may be included by specific reference to other documents previously provided to each NRMSIR and to the appropriate SID, if any is hereafter created, or filed with the SEC; provided, however, that any final official statement incorporated by reference must be available from the Municipal Securities Rulemaking Board (the "MSRB").

(d) The Authority will provide in a timely manner to each NRMSIR or the MSRB and with the appropriate SID, if any is hereafter created, notice of the occurrence of any of the following events with respect to the Series 2006 Bonds, if material:

(1) principal and interest payment delinquencies;
(2) non-payment related defaults;
(3) unscheduled draws on debt service reserves reflecting financial difficulties;
(4) unscheduled draws on any credit enhancement reflecting financial difficulties;
(5) substitution of credit or liquidity providers, or their failure to perform;
(6) adverse tax opinions or events affecting the tax-exempt status of the Series 2006 Bonds;
(7) modifications to the rights of Series 2006 Bondowners;
(8) Series 2006 Bond calls, other than mandatory sinking fund redemptions;
(9) defeasance of all or any portion of the Series 2006 Bonds;
(l0) release, substitution or sale of property securing repayment of the Series 2006 Bonds; and
(11) rating changes.

(e) The Authority will provide in a timely manner to each NRMSIR or the MSRB and to the appropriate SID, if any is hereafter created, notice specifying any failure of the Authority to provide the Continuing Disclosure by the date specified.

3. Remedies. The sole and exclusive remedy for breach or default under this Disclosure Agreement to provide the Continuing Disclosure is an action to compel specific performance of the undertakings contained herein, and no person or entity may recover monetary damages hereunder under any circumstances; provided, however, that the Trustee shall not be required to take any enforcement action except at the written direction of the holders of not less than 51% in aggregate principal amount of Series 2006 Bonds then outstanding. Failure by any party to perform its obligations hereunder shall not constitute an Event of Default under the Indenture or any other agreement executed and delivered in connection with the issuance of the Series 2006 Bonds.

4. Amendments. (a) Without the consent of any of the holders of the Series 2006 Bonds, the Authority, the Government and the Trustee at any time and from time to time may enter into amendments or changes to this Disclosure Agreement for any purposes if:

(i) (A) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, a change in law, or a change in the identity, nature or status of the Authority, the Government or the Trustee or any type of business or affairs conducted by either of the Authority, the Government or the Trustee; (B) the undertakings set forth herein, as amended, would have complied with the requirements of the Rule on the date hereof, after taking into account any amendments to, or former authoritative interpretation by the staff of the SEC of, the Rule; (C) the amendment adds to the covenants of the Authority for the benefit, of the holders of the Series 2006 Bonds, or surrenders any right or power herein conferred upon the Authority; and (D) the amendment does not materially impair the interests of the holders of the Series 2006 Bonds, as determined by the Trustee or by nationally recognized bond counsel.

(In determining whether or not the interest of the holders of the Series 2006 Bonds are materially impaired, the Trustee may rely upon an opinion of nationally recognized bond counsel); or

(ii) the amendment adds or changes a dissemination agent for the information required to be provided hereby and to make any necessary or desirable provisions with respect thereto.

(b) Annual Financial Information of the Authority for any fiscal year containing any amended operating data or financial information for such fiscal year shall explain, in narrative form, the reasons for such amendment and the impact of the change on the type of operating data or financial information in the Annual Financial Information being provided for such fiscal year. If a change in accounting standards is included in any such amendment, such Annual Financial Information shall present a comparison between the financial statements or information prepared on the basis of the amended accounting standards and those prepared on the basis of the former accounting standards for the fiscal year in which such change is made. Such comparison shall include a qualitative discussion of the differences in the accounting standards and the impact of the change in the accounting standards on the presentation of the financial information. To the extent reasonably feasible, the comparison also should be quantitative. A notice of the change in accounting standards shall be sent by the Authority to each NRMSIR or the MSRB, and to the appropriate SID, if any is hereafter created.

IN WITNESS WHEREOF, the undersigned have duly executed and delivered this Disclosure Agreement on September __, 2006.

VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY

By:________________________
Authorized Officer

THE BANK OF NEW YORK TRUST COMPANY, N.A.

By:________________________
Authorized Officer

Acknowledged and Accepted:

GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS

By:________________________

Dated: September __, 2006

APPENDIX G-2

FORM OF GOVERNMENT CONTINUING DISCLOSURE AGREEMENT

This Continuing Disclosure Agreement (the "Disclosure Agreement"), dated September __, 2006, is executed and delivered by the Government of the United States Virgin Islands (the "Government") and The Bank of New York Trust Company, N.A., a national banking association (the "Trustee"), in connection with the issuance by the Virgin Islands Public Finance Authority (the "Authority") of its $219,490,000 original principal amount of Virgin Islands Public Finance Authority Revenue Bonds (Virgin Islands Gross Receipts Taxes Loan Notes) Series 2006 (the "Series 2006 Bonds"). Capitalized terms used in this Disclosure Agreement which are not defined herein shall have the respective meanings specified in the Indenture of Trust, dated as of November 1, 1999, between the Authority and the Trustee and, as to each Series of Bonds, the Supplemental Indenture pertaining thereto, as the Indenture or any Supplemental Indenture may from time to time be amended or supplemented in accordance with the terms thereof.

The Undertaking

1. Purpose of this Disclosure Agreement. This Disclosure Agreement is being executed and delivered for the benefit of the holders of the Series 2006 Bonds and delivered in order to assist the underwriter of the Series 2006 Bonds (the "Underwriter") in complying with the provisions of Section (b)(5)(i) of Rule 15c2-12 (the "Rule") promulgated by the Securities and Exchange Commission (the "SEC") under the Securities Exchange Act of 1934, as the same may be amended from time to time.

2. Disclosure. (a) The Government shall provide certain financial and operating information in accordance with the provisions of Section (b)(5)(i) of the Rule as follows:

(i) Annual Financial Information with respect to each Fiscal Year of the Government. "Annual Financial Information" means, collectively: (A) financial statements for the Government prepared in accordance with accounting principles generally accepted in the United States and audited by an independent firm of certified public accountants in accordance with auditing standards generally accepted in the United States when available and, until such time, statements of revenues and expenditures prepared by the Commissioner of Finance; (B) an update of the tabular information presented in the Official Statement dated September 19, 2006 with respect to the Series 2006 Bonds under the headings "GROSS RECEIPTS TAXES," "UNITED STATES VIRGIN ISLANDS" and APPENDIX E - "United States Virgin Islands Economic and Demographic Information;" (C) updated information with respect to the percentage of Gross Receipts Tax collections from the top 5 and the top 10 taxpayers; and (D) the information regarding amendments to this Disclosure Agreement required pursuant to this Disclosure Agreement; together with (E) such narrative explanation as may be necessary to avoid misunderstanding and to assist the reader in understanding the presentation of financial and operating data concerning the Gross Receipts Taxes and the United States Virgin Islands; and

(ii) the Government shall provide quarterly summaries of the information provided by the Virgin Islands Bureau of Internal Revenue on Gross Receipts Taxes collected as reported by the Bureau of Internal Revenue.

The descriptions contained in clause 2(a)(i)(B) above constituting Annual Financial Information are of general categories of financial information and operating data. When such descriptions include information that no longer can be generated because the operations to which it related have been materially changed or discontinued, a statement to that effect shall be provided in lieu of such information.

The financial information described in clause 2(a)(i) and 2(a)(ii) above are hereinafter referred to collectively as the "Continuing Disclosure."

(b) The Government will provide annually the financial information described in clause (2) above as follows: (i) with respect to the Annual Financial Information described in clause 2(a)(i)(A) above, within 365 days after the end of the Government's Fiscal Year, commencing with the Government's Fiscal Year ending September 30, 2007, (ii) with respect to the Annual Financial Information described in clause 2(a)(i)(B), (C) and (D) above, within 180 days after the end of the Government's Fiscal Year, commencing not later than March 31, 2008 for the Government's Fiscal Year ended September 30, 2007, and (iii) with respect to the information described in clause 2(a)(ii) above, within sixty (60) days after the end of each fiscal quarter during the Government's Fiscal Year, commencing not later than February 28, 2007 for the fiscal quarter ending December 31, 2006. The Continuing Disclosure will be provided to each nationally recognized municipal securities information repository ("NRMSIR") and to the appropriate state information depository ("SID"), if any is hereafter created.

(c) Any of the Continuing Disclosure may be included by specific reference to other documents previously provided to each NRMSIR and to the appropriate SID, if any is hereafter created, or filed with the SEC; provided, however, that any final official statement incorporated by reference must be available from the Municipal Securities Rulemaking Board (the "MSRB").

(d) The Government will provide in a timely manner to each NRMSIR or the MSRB and to the appropriate SID, if any is hereafter created, notice specifying any failure of the Government to provide the Continuing Disclosure by the date specified.

3. Remedies. The sole and exclusive remedy for breach or default under this Disclosure Agreement to provide the Continuing Disclosure is an action to compel specific performance of the undertakings contained herein, and no person or entity may recover monetary damages hereunder under any circumstances; provided, however, that the Trustee shall not be required to take any enforcement action except at the written direction of the holders of not less than 51 % in aggregate principal amount of Series 2006 Bonds then outstanding. Failure by any party to perform its obligations hereunder shall not constitute an Event of Default under the Indenture or any other agreement executed and delivered in connection with the issuance of the Series 2006 Bonds.

4. Amendments. (a) Without the consent of any of the holders of the Series 2006 Bonds, the Government and the Trustee at any time and from time to time may enter into amendments or changes to this Disclosure Agreement for any purposes if:

(i) (A) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, a change in law, or a change in the identity, nature or status of the Government or the Trustee or any type of business or affairs conducted by either of the Government or the Trustee; (B) the undertakings set forth herein, as amended, would have complied with the requirements of the Rule on the date hereof, after taking into account any amendments to, or former authoritative interpretation by the staff of the SEC of, the Rule; (C) the amendment adds to the covenants of the Government for the benefit of the holders of the Series 2006 Bonds, or surrenders any right or power herein confirmed upon the Government; and (D) the amendment does not materially impair the interests of the holders of the Series 2006 Bonds, as determined by the Trustee or by nationally recognized bond counsel. (In determining whether or not the interest of the holders of the Series 2006 Bonds are materially impaired, the Trustee may rely upon an opinion of nationally recognized bond counsel); or

(ii) the amendment adds or changes a dissemination agent for the information required to be provided hereby and to make any necessary or desirable provisions with respect thereto.

(b) Annual Financial Information of the Government for any fiscal year containing any amended operating data or financial information for such fiscal year shall explain, in narrative form, the reasons for such amendment and the impact of the change on the type of operating data or financial information in the Annual Financial Information being provided for such fiscal year. If a change in accounting standards is included in any such amendment, such Annual Financial Information shall present a comparison between the financial statements or information prepared on the basis of the amended accounting standards and those prepared on the basis of the former accounting standards for the fiscal year in which such change is made. Such comparison shall include a qualitative discussion of the differences in the accounting standards and the impact of the change in the accounting standards on the presentation of the financial information. To the extent reasonably feasible, the comparison also should be quantitative. A notice of the change in accounting standards shall be sent by the Government to each NRMSIR or the MSRB, and to the appropriate SID, if any is hereafter created.

IN WITNESS WHEREOF, the undersigned have duly executed and delivered this Disclosure Agreement on September __, 2006.

GOVERNMENT OF THE UNITED STATES
VIRGIN ISLANDS

By:________________________________
Authorized Officer

THE BANK OF NEW YORK TRUST COMPANY, N.A.

By:________________________________
Authorized Officer

APPENDIX H

PROPOSED FORM OF BOND COUNSEL OPINION

$219,490,000
Virgin Islands Public Finance Authority
Revenue Bonds, Series 2006
(Virgin Islands Gross Receipts Taxes Loan Note)

September __, 2006

Virgin Islands Public Finance Authority
Director of Finance and Administration
P.O. Box 430
St. Thomas, U.S. Virgin Islands 00802

Ladies and Gentleman:

We have served as bond counsel to the Virgin Islands Public Finance Authority (the "Authority") in connection with the issuance by the Authority of its Revenue Bonds, Series 2006 (Virgin Islands Gross Receipts Taxes Loan Note) in the aggregate principal amount of $219,490,000 (the "Series 2006 Bonds"). The Series 2006 Bonds are issued under and pursuant to (i) United States Virgin Islands Revised Organic Act of 1954, as amended (48 U.S.C.A. § 1574(b)(ii)(A) (the "Revised Organic Act"), (ii) the laws of the Virgin Islands including Title 29 of the Virgin Islands Code 2002 V.I. Act No. 6514, as amended by Act. No. 6533 (collectively with the Revised Organic Act, the "Act"), (iii) Resolution No. 06-006, dated June 7, 2006 (the "Bonds Resolution"), and (iv) an Indenture of Trust, as supplemented by the First Supplemental Indenture of Trust, each dated as of November 1, 1999, as further amended and supplemented by the Second Supplemental Indenture of Trust, dated as of February 28, 2003, the Third Supplemental Indenture of Trust, dated as of September 4, 2003, the Fourth Supplemental Indenture of Trust, dated as of December 1, 2003, the Fifth Supplemental Indenture of Trust, dated as of September 7, 2005, the Sixth Supplemental Indenture of Trust, dated as of August 31, 2006, and the Seventh Supplemental Indenture of Trust, dated as of September 1, 2006 (collectively, the "Indenture"), each by and between the Authority and The Bank of New York Trust Company, N.A., Jacksonville, Florida, successor to United States Trust Company of New York, as trustee (the "Trustee"). All terms not otherwise defined herein shall have the meanings set forth in the Indenture.

Under the Act, the Series 2006 Bonds are being issued for the purpose of providing funds to (i) refund a portion of the Authority's Revenue Bonds, Series 1999A (Virgin Islands Gross Receipts Taxes Loan Note) (the "Series 1999A Bonds"), (ii) pay the cost of a termination fee in connection with an outstanding swap option agreement, (iii) fund certain necessary public sector capital development projects of the Government of the United States Virgin Islands (the "Government"), (iv) fund the Debt Service Reserve Account in an amount necessary to meet the Debt Service Reserve Requirement, (v) pay the premium in connection with the Series 2006 Bond Insurance Policy, (vi) fund a reserve for interest rate swap payments and (vii) pay the costs of issuing the Series 2006 Bonds.

The proceeds of the Series 2006 Bonds are being loaned by the Authority to the Government pursuant to a Loan Agreement, dated as of September 1, 2006, by and among the Authority, the Government and the Trustee, against delivery by the Government of its $219,490,000 principal amount 2006 Gross Receipts Taxes Loan Note (the "Loan Note").

The Series 2006 Bonds are dated the date of their issuance, bear interest from that date on the unpaid principal amount thereof, at the rates set forth therein and in the Indenture, and mature on the dates set forth therein and in the Indenture. The Series 2006 Bonds are subject to redemption prior to maturity, in the manner and upon the terms and conditions set forth in the Indenture and the Series 2006 Bonds. The Series 2006 Bonds are equally and ratably secured by the Indenture, which pledges and assigns to the Trustee the Trust Estate (as defined in the Indenture).

The Internal Revenue Code of 1986, as amended, and the regulations and rulings of the United States Treasury Department thereunder (collectively, the "Code") establish certain requirements which must be met at and subsequent to the date of issuance and delivery of the Series 2006 Bonds in order that interest on the Series 2006 Bonds will be and remain excludable from gross income for federal income tax purposes. Included among these continuing requirements are certain restrictions and prohibitions on the use of bond proceeds, restrictions on the investment of bond proceeds and other moneys or properties and the rebate to the United States of certain earnings in respect of investments. Failure to comply with the continuing requirements may cause the interest on the Series 2006 Bonds to be includable in gross income for federal income tax purposes retroactive to the date of their issuance irrespective of the date on which such noncompliance occurs. The Authority and the Government have covenanted in the Indenture and the Loan Agreement, respectively, and in documents relating to federal tax matters delivered at the time of delivery of the Series 2006 Bonds (collectively, the "Tax Certificates") to comply with certain procedures, and have made certain representations and certifications, designed to assure satisfaction of the requirements of the Code.

We have examined and relied on the record of proceedings of the Authority and the Government in connection with the authorization and issuance of the Series 2006 Bonds and have made such investigation of law and such further review, inquiry or examination as we deemed necessary or desirable in rendering the opinions set forth herein. Further, we have examined originals or copies, certified or otherwise identified to our satisfaction, of such instruments, certificates and documents as we have deemed necessary or appropriate for the purposes of the opinions rendered below. In such examination, we have assumed the genuineness of all signatures, the authenticity and due execution of all documents submitted to us as originals and the conformity to the original documents of all documents submitted to us as copies. As to any facts material to our opinion, we have relied upon, and assumed the accuracy and truthfulness of, the aforesaid instruments, certificates and documents, without having conducted any independent investigation.

We have not undertaken to verify the factual accuracy of any matter set forth in the official statement or other disclosure material delivered in connection with the issuance of the Series 2006 Bonds and we express no opinion herein with respect thereto.

Based upon and subject to the foregoing, we are of the opinion that:

1. The Authority is duly created and validly existing under provisions of the Act.

2. The Series 2006 Bonds have been duly authorized and issued in accordance with the Act, and constitute valid and binding special limited obligations of the Authority payable solely from the Trust Estate.

3. The Indenture has been duly authorized, executed and delivered by the Authority and, assuming the due authorization, execution and delivery thereof by the Trustee, constitutes a legally binding agreement of the Authority and is enforceable against the Authority in accordance with its terms.

4. Under existing statutes, regulations, administrative interpretations and court decisions as of the date hereof, interest on the Series 2006 Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of computing the federal alternative minimum tax imposed on individuals and corporations. However, interest on the Series 2006 Bonds held by a corporate taxpayer is included in the adjusted current earnings for purposes of calculating certain taxes including the federal alternative minimum tax imposed on corporations.

5. Under existing statues, interest on the Series 2006 Bonds is exempt from personal income taxes imposed by the United States Virgin Islands, any state, other territory or possession on the United States or any political subdivision thereof, or by the District of Columbia.

In rendering the opinion set forth in paragraph 4 above, we have assumed the accuracy of certain factual certifications made by the Authority and by the Government in the Tax Certificates and the continuing compliance by the Authority and the Government with the covenants, provisions and procedures set forth in the Indenture, the Loan Agreement and the Tax Certificates. In the event of the inaccuracy or incompleteness of any of the certifications made by the Authority or the Government, or of the failure by the Authority or the Government to comply with certain covenants, provisions and procedures set forth in the Indenture, the Loan Agreement or the Tax Certificates, the interest on the Series 2006 Bonds could become includable in gross income for federal income tax purposes retroactive to the date of the original execution and delivery of the Series 2006 Bonds, regardless of the date on which the event causing such inclusion occurs. We render no opinion as to the exclusion from gross income of interest on the Series 2006 Bonds for federal, territorial, state or local income tax purposes on or after the date on which any change occurs in or action is taken or omitted under the Indenture, the Loan Agreement or the Tax Certificates by the Authority or the Government, or under any other relevant documents without the advice or approval of, or upon the advice or approval of any bond counsel other than, Buchanan Ingersoll & Rooney PC. We have not undertaken to determine in the future (or to inform any person) whether any actions taken or not taken or events occurring or not occurring after the date of issuance and delivery of the Series 2006 Bonds may affect the tax status of interest on the Series 2006 Bonds. No assurance can be given that future legislation or amendments to the Code, if enacted into law, will not contain provisions which could directly or indirectly reduce the benefit of the exclusion of the interest on the Series 2006 Bonds from gross income for federal income tax purposes.

The opinions contained in paragraphs 2 and 3 above are qualified to the extent that the enforceability of the Indenture and the Series 2006 Bonds may be limited by applicable bankruptcy, insolvency, moratorium, reorganization or other laws affecting creditors' rights generally or as to the availability of any particular remedy. Except as stated in paragraphs 4 and 5 above, we express no opinion as to the federal, territorial, state or local tax consequences caused by the receipt or accrual of interest on the Series 2006 Bonds and holders of the Series 2006 Bonds should consult their tax advisors with respect thereto. We undertake no obligation to update this opinion.

Truly yours,

BUCHANAN INGERSOLL & ROONEY PC

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VIRGIN ISLANDS PUBLIC FINANCE AUTHORITY • REVENUE BONDS (VIRGIN ISLANDS GROSS RECEIPTS TAXES LOAN NOTE), SERIES 2006

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