Virginia Military Institute

Financial Statements
For the year ended 30 June 2010
(Audited)

- T A B L E O F C O N T E N T S -

MANAGEMENT’S DISCUSSION AND ANALYSIS

Overview

Virginia Military Institute (VMI) is pleased to present its financial statements for the fiscal year ended 30 June 2010, along with the financial statements of its affiliates as required under Governmental Accounting Standards Board Statement Number 39. This management discussion and analysis (MD&A) is designed to facilitate the reader's understanding of the accompanying financial statements and to provide an objective, easily readable analysis of the Institute's financial activities based on currently known facts, decisions and conditions. This discussion focuses primarily on VMI's fiscal year 2010 and includes highly summarized data that should be read in conjunction with the accompanying financial statements, notes to the financial statements, and other supplementary information.

VMI's financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) standards and include three basic statements: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows. Using criteria provided in GASB Statement 39, *Determining Whether Certain Organizations are Component Units*, the Institute determined that the VMI Alumni Agencies, Inc., and the VMI Research Laboratories, Inc. are both component units of the Institute. The affiliates' financial statements are prepared in accordance with Financial Accounting Standards Board (FASB) standards and include the Statement of Financial Condition and the Statement of Activities. They are presented discretely on a separate page within the Institute's financial statements. The following analysis discusses elements from VMI's statements and provides an overview of the Institute's activities. VMI's affiliated entities are excluded from this MD&A.

Financial Highlights

The overall financial position of the Institute improved slightly in FY 2010 due in large part to an increase in enrollment numbers and a partial recovery of previous year losses on our investments. Net assets (the residual interest in assets after liabilities are deducted) increased by $13.8 million over the previous fiscal year to $227.8 million. The Institute's opening fall enrollment numbers for the Corps has continued to increase from 1,408 cadets for FY 2008 to 1,456 cadets for FY 2009 and to 1,527 cadets for FY 2010.

State appropriations for operations totaled $11.3 million in FY 2010, a decrease of $2.5 million or 17.9% from the previous fiscal year. This is the third straight year State appropriations have decreased.

VMI incurred a net investment gain of $1.6 million for FY 2010 after incurring a net loss of $3.9 million in FY 2009.

VMI made substantial progress on several major capital projects during FY 2010. The renovation of the Maury House ($1.2 million) was completed and the expansion and renovation of the Barracks ($63 million, including $1.9 million of planning) was essentially completed during the 2010 fiscal year. Planning for the renovation of the Science Building ($.8 million) and the VMI Hospital ($.2 million) was completed, but both projects have been placed on hold awaiting funding from the Commonwealth. Construction of the Military and Leadership Field Training Grounds ($17.1 million) is underway and is scheduled for completion April 2011.

Statement of Net Assets

The Statement of Net Assets presents the financial position of the Institute at the end of the fiscal year and includes all assets and liabilities of the Institute. The difference between total assets and total liabilities—net assets—is one indicator of the current financial condition of the Institute, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year. Readers of the Statement of Net Assets should be able to determine the assets available to continue the Institute's operations. They should also be able to determine how much the Institute owes vendors, creditors, and others.

Net Assets are divided into three major categories. The first category, "Invested in capital assets, net of related debt," provides the Institute's equity in property, plant, and equipment. The next category is "Restricted" net assets which comprise two subcategories, expendable and nonexpendable. Expendable restricted resources are available for expenditure by the Institute in accordance with stipulation of donors and/or other entities that have placed time or purpose restrictions on the use of the assets. Nonexpendable restricted resources typically represent the corpus of endowments and are available only for investment purposes. The final category is "Unrestricted" net assets which are available for any lawful purpose of the Institute.

Statement of Net Assets

	30 June 2010	30 June 2009	Variance	
Assets:				
Current assets	$ 21,609,072	$ 19,983,129	$ 1,625,943	8.1%
Capital assets, net	219,172,608	208,305,471	10,867,137	5.2%
Other noncurrent assets	14,877,950	16,637,159	(1,759,209)	-10.6%
Total assets	$ 255,659,630	$ 244,925,759	$ 10,733,871	4.4%
Liabilities:				
Current liabilities	$ 12,331,145	$ 13,560,675	$ (1,229,530)	-9.1%
Noncurrent liabilities	15,568,355	17,410,956	(1,842,601)	-10.6%
Total liabilities	$ 27,899,500	$ 30,971,631	$ (3,072,131)	-9.9%
Net assets:				
Invested in capital assets, net of related debt	$ 205,827,518	$ 194,263,958	$ 11,563,560	6.0%
Restricted - expendable	9,541,747	8,911,373	630,374	7.1%
Restricted - nonexpendable	1,267,021	1,265,690	1,331	0.1%
Unrestricted	11,123,844	9,513,107	1,610,737	16.9%
Total net assets	$ 227,760,130	$ 213,954,128	$ 13,806,002	6.5%

VMI's current assets as of 30 June 2010 increased by $1.6 million, or 8.1% from the 30 June 2009 balance. Auxiliary enterprise cash increased approximately $1.2 million due to enrollment growth of 5% and a cadet auxiliary fee increase of 5.4%. Additionally, auxiliary expenses were less than budgeted due to employee vacancy savings and less spending on Barracks maintenance and cadet uniforms.

Capital assets, net of depreciation, increased by $10.9 million or 5.2% to $219.2 million. This increase can be attributed to the completion of the renovations to the Old and New Barracks and the complete renovation of the Maury House.

Other noncurrent assets decreased by $2 million to $14.9 million. Cash and cash equivalents reflected a deficit balance for our projects funded by VCBA 21st Century bond proceeds. For these projects, we must first incur the expenses and seek reimbursement from the Commonwealth on a monthly basis. As of 30 June, the Institute had $3 million of expenses for which we had not yet been reimbursed.

Current liabilities decreased 9.1% or $1.2 million from the previous year to $12.3 million as a result of fewer vouchers payable to contractors for various capital projects. Noncurrent liabilities decreased by $1.8 million or 10.6% due primarily to the payment of retainage to the contractor of the Barracks Expansion and Renovation project.

As a result of the changes explained above, net assets increased by $13.8 million or 6.5% over the previous fiscal year to $227.8 million.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in the total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of this statement is to present the Institute's operating and nonoperating revenues recognized and expenses paid and any other revenues, expenses, gains, and losses received or incurred by the Institute.

Operating revenues are generally recognized when goods and services are provided to cadets and other constituencies of the Institute. Operating expenses are the cost incurred to acquire or produce the goods and services provided and to carry out the Institute's programs and activities.

Nonoperating revenues generally represent income and support for which goods and services are generally not provided. For example, it includes State appropriations for VMI's Educational and General and Unique Military Activities Programs for which goods and services are not directly provided to the State by VMI.

Statement of Revenues, Expenses, and Changes in Net Assets

	30 June 2010	30 June 2009	Variance	
Operating revenues:				
Tuition and fees	$ 15,251,565	$ 13,743,061	$ 1,508,504	11.0%
Grants and contracts	407,318	491,621	(84,303)	-17.1%
Auxiliary enterprises	13,128,557	12,146,364	982,193	8.1%
Unique military activities	2,058,314	1,794,074	264,240	14.7%
Other sources	1,531,428	1,056,833	474,595	44.9%
Total operating revenues	32,377,182	29,231,953	3,145,229	10.8%
Operating expenses:				
Educational and general	43,541,100	42,878,855	662,245	1.5%
Auxiliary enterprises	18,223,371	16,851,022	1,372,349	8.1%
Unique military activity	6,001,428	5,583,768	417,660	7.5%
Other expense	4,764	-	4,764	100.0%
Total operating expenses	67,770,663	65,313,645	2,457,018	3.8%
Operating loss	(35,393,481)	(36,081,692)	688,211	-1.9%
Nonoperating revenues (expenses):				
State appropriations	11,325,528	13,787,087	(2,461,559)	-17.9%
Gifts, grants and contributions	17,309,785	16,198,887	1,110,898	6.9%
Investments	1,569,522	(3,896,880)	5,466,402	-140.3%
Other	(1,712,558)	(858,746)	(853,812)	99.4%
Net nonoperating revenues	28,492,277	25,230,348	3,261,929	12.9%
Income (loss) before other revenues	(6,901,204)	(10,851,344)	3,950,140	-36.4%
Other revenues/reductions	20,707,206	25,978,061	(5,270,855)	-20.3%
Increase (decrease) in net assets	13,806,002	15,126,717	(1,320,715)	-8.7%
Net assets - beginning of year	213,954,128	198,827,411	15,126,717	7.6%
Net assets - end of year	$227,760,130	$213,954,128	$ 13,806,002	6.5%

Operating revenues increased by 10.8% or $3.1 million to $32.4 million while operating expenses increased by 3.8% or $2.5 million to $67.8 million. The increase to operating revenues can be attributed to tuition and fee increases as well as an increase in enrollment. The opening enrollment increased by 71 cadets to 1,527 over the previous year. The largest portion of the increase in operating expenses was in auxiliary enterprises where depreciation expense increased significantly as a result of bringing the Third Barracks on line and food service costs increased due to an increase in rates paid our food service provider and a greater number of cadets.

Non-operating revenues increased $3.3 million or 12.9% to $28.5 million. Investments realized a gain of $1.6 million during FY 2010 versus a loss of $3.9 million during FY 2009. This overall increase between fiscal years of $5.5 million was partially offset by a $2.5 million decrease in State appropriations.

Other revenues and/or reductions changed by $5.3 million from an increase of $26 million during fiscal year 2009 to an increase of $20.7 million during the 2010 fiscal year. While the Institute received more funding for the Military Leadership and Field Training Grounds project during the 2010 FY, we received no funding for the Center for Leadership and Ethics which was completed during the 2009 FY and less funding for the Barracks Expansion and Renovation project than FY 2009.

Statement of Cash Flows

This statement presents detailed information about the Institute's cash activity during the year. Cash flows from operating activities will always differ from the operating loss on the Statement of Revenues, Expenses and Changes in Net Assets (SRECNA). The SRECNA is prepared on the accrual basis of accounting and includes noncash items such as accounts receivable and accrued liabilities as well as such expenses as depreciation, whereas the Statement of Cash Flows presents cash inflows and outflows without regard to accrual items. The Statement of Cash Flows helps the reader assess the Institute's ability to generate cash flows sufficient to meet its obligations. It is divided into five parts: operating activities, noncapital financing activities, investing activities, capital and related financing activities, and reconciliation of the net cash used, to the operating income or loss reflected on the SRECNA.

Statement of Cash Flows

	30 June 2010	30 June 2009	Variance	
Net cash used by operating activities	$ (28,444,752)	$ (30,183,588)	$ 1,738,836	-5.8%
Net cash provided by noncapital financing activities	30,413,154	29,261,138	1,152,016	3.9%
Net cash used by capital and related financing activities	(1,629,251)	(4,693,765)	3,064,514	-65.3%
Net cash provided by investing activities	934,848	1,090,641	(155,793)	-14.3%
Net increase (decrease) in cash	1,273,999	(4,525,574)	5,799,573	-128.2%
Cash - beginning of year	8,457,121	12,982,695	(4,525,574)	-34.9%
Cash - end of year	$ 9,731,120	$ 8,457,121	$ 1,273,999	15.1%

Cash provided and/or (used) by operating activities will always result in a net use for the Institute because all State appropriations and private gifts are treated as cash sources for noncapital or capital financing activities rather than sources for operating activities. Tuition and fees ($15.3 million) and auxiliary enterprise revenues ($13.2 million) represent the largest sources of operating cash, while compensation and benefits ($36.6 million) and payments for supplies and services ($23.4 million) are the most significant uses of operating cash. Overall, net cash used for operations decreased slightly for fiscal year 2010 from the previous fiscal year by $1.7 million.

Net cash provided by noncapital financing activities for operations consists largely of State appropriations ($11.3 million) and private fund support ($17.4 million). Overall, cash provided by noncapital financing activities increased $1.2 million during FY 2010 over FY 2009.

Net cash provided by capital and related financing activities consists primarily of gifts and contributions from the VMI Development Board and State VCBA bond funding ($21.4 million). The purchase and construction of capital assets ($22.3 million) and principal and interest paid on capital debt ($5.9 million) account for the largest uses of cash for capital and related financing activities.

Net cash provided by investing activities decreased only slightly by $.2 million from $1.1 million in FY 2009 to $.9 million in FY 2010.

Capital Asset and Debt Administration

FY 2010 was the eighth year of the implementation of VMI's Vision 2039 master plan. Vision 2039 is a leadership plan rather than a construction plan; however, construction of new facilities and the renovations of older buildings on Post are essential components of Vision 2039. During the year, planning and/or renovation and construction continued on a number of academic as well as other mission essential facilities: the Barracks Expansion and Renovation, VMI Museum (Jackson Memorial Hall) casework, the Military and Leadership Field Training Grounds, Maury House, Science Building renovation, and Post Hospital renovation.

The VMI Barracks Expansion and Renovation project has been on-going since the 2005 General Assembly appropriated $1.9 million of State funds to begin planning. The 2006 General Assembly appropriated $46.8 million for construction and the 2007 General Assembly appropriated supplemental funding of $14 million. During FY 2008, the State changed the funding source for this project from general funds to VCBA 21st Century bond proceeds. This project provides much needed repairs and upgrades to this historic facility and allows VMI to grow the Corps to 1,500 cadets. The Barracks expansion was completed in December 2008 and renovation of the Old and New Barracks was completed in July 2010.

The 2008 General Assembly appropriated VCBA bond financing for two new VMI capital projects beginning in FY 2009 consisting of $15.1 million for VMI's Military Leadership and Field Training Grounds (MLFTG) project and $816,000 in detailed planning funds to renovate the Science Building. During June 2010, the Institute appropriated an additional $2 million for the MLFTG project ($1 million from private funds and $1 million from auxiliary funds). Construction of the MLFTG project commenced in September 2009 and is scheduled for completion in April 2011. The Institute has requested through the State's new capital outlay process funds to complete the Science Building Renovation project, but this project has been placed on hold for the time being. Renovations of the Science Building will support changes in VMI's revised Core Curriculum, increases in the size of the Corps of Cadets, and support increases in the number of Science, Technology, Engineering and Math (STEM) graduates and energy conservation and life safety measures.

Authorized by the 2008 General Assembly, in the amount of $400,000 of auxiliary funds and $800,000 of private funds, was the renovation of the Maury House. The historic Maury House was last renovated in 1956 and all building systems were in need of renovation. Significant restoration efforts were expended as the quarters is a contributing historical building to the VMI Historic District (listed as both a National Register property and a National Historic Landmark since 1974). This project was completed in the Spring of 2010. The 2008 General Assembly also appropriated bond financing for two parking projects totaling $4.8 million, South Institute Hill Parking and Lackey Park Parking, which are in the planning stage.

Detailed planning on the Post Hospital was initiated, with authorization granted from the 2009 General Assembly, to utilize $205,000 of non-general funds. This planning was completed and resulted in drawings to the preliminary phase. Improvements to the Post Hospital were recommended in Group 1.B of SCHEV's

2008-2010 Capital Outlay Recommendations for Higher Education. This renovation project has been placed on hold until funding is approved by the State.

The last phase of the Jackson Memorial Hall project was completed during FY 2010. Casework in the VMI Museum to display the Henry Stewart 19th Century Antique Firearms Collection was completed in November 2009.

VMI had three capital projects totaling $79.1 million in progress at the end of FY 2010; however, the Barracks Renovation project ($60.8 million) was completed during July of FY 2011. These projects are all financed with State funds or private funds from VMI's alumni agencies resulting in no debt obligations for VMI. Since VMI began its Vision 2039 capital program, it has incurred debt on only the Jackson Memorial Hall, the Cocke Hall Annex, and the Crozet Hall capital projects. The debt on these projects totaled approximately $14.9 million with annual debt service payments of $1.3 million, most of which is being funded by the VMI Foundation and VMI Development Board. VMI's Board of Visitors adopted debt guidelines in August 2005 to help ensure sound management and control of debt.

Economic Outlook

State appropriations for operations totaled $11.3 million in FY 2010 and $13.8 million in FY 2010 for a decrease of $2.5 million or 17.9%. State appropriations represented 18.1% of VMI's total revenue and support for operations in FY 2010 compared to 24.9% in FY 2009. State appropriations for FY 2010 were reduced approximately $1.1 million by the 2009 General Assembly and $423,000 by the 2010 General Assembly due to continuing shortfalls in State general fund revenues resulting from the nationwide economic recession and sluggish recovery. State appropriations for FY 2010 were also reduced almost another $1.0 million for State changes related primarily to payment of fringe benefits in the 4th quarter of the fiscal year.

State appropriations for FY 2011 are projected to total approximately $12.1 million for an increase of $0.8 million or 6.7% compared to FY 2010. The increase includes the State's share of the cost of a 3% bonus payable to full-time State employees in December 2010. State appropriations for FY 2012 are projected to total $10.3 million for a decrease of $1.8 million or 14.6% and generally reflect continued shortfalls in State revenues. However, State appropriations are being supplemented with approximately $1.9 million in Federal Stabilization Funds (federal "stimulus" funds) for FY 2011 compared to $765,001 in FY 2010.

VMI plans to address the continuing State reductions primarily by supplanting State appropriations with enrollment growth revenue, tuition and fee increases, deferring discretionary expenses, achieving employee vacancy and turnover savings, and using Auxiliary Program fund balances as necessary. The rate of the economic recovery creates significant uncertainty as to the level of State support for the next few years.

Private gifts and contributions in support of operations totaled $15.5 million in FY 2010 and in FY 2009. This support represented 24.8% of VMI's total revenues and support for operations in FY 2010 compared to 28.1% in FY 2009. Gifts and contributions consist primarily of donations and endowment income from VMI's alumni agencies. This support is projected to decrease significantly in FY 2011 and for several years thereafter. This is due to the stock market decline in 2008 and its continued affect on endowment income and donations and to $45 million in debt refinancing in July 2010 by the VMI Foundation and the VMI Development Board (this debt was originally issued in 2004 and 2006 to finance various VMI capital projects). The debt refinancing converted variable rate debt to fixed rates with 10, 20, and 26 year maturities which resulted in an increase in annual debt service costs. Favorable interest rates were obtained due in part to the Moody's Aa2 rating achieved by the VMI Foundation and the VMI Development Board in its first ever bond rating in June 2010. However, the increased debt service costs have reduced the amount of private unrestricted income that can be distributed to VMI annually for support of its programs. VMI is working with the VMI Foundation and the VMI Development Board to establish a funding plan that will minimize reductions in support to VMI in the years ahead. Plans are also being made for a new fund raising campaign during the next several years that is expected to increase donations and endowments in support of new and existing programs.

State funding for capital projects totaled $19.0 million in FY 2010 and $25.6 million in FY 2009 and consists of State bond financing. State funding for FY 2011 is projected to approximate $12.7 million and consists of bond financing for existing on-going capital projects. VMI has submitted requests for State funding for new capital projects totaling about $188 million for FY 2011 and FY 2012; however, State funding for new projects is highly uncertain for the next few years due to the sluggish economic recovery and its impact on the State's funding capacity. The State's Debt Capacity Advisory Committee will be issuing a report before January 2011 that will indicate the State's ability to issue debt for new projects.

Private funding for capital projects totaled $1.7 million in FY 2010 and $3.6 million in FY 2009 and consisted of bond financing and donations. Private funding for FY 2011 is projected to total about $1.0 million from donations for an on-going capital project. Any significant private funding for new capital projects is uncertain for the next several years due to the sluggish economic recovery and to the $45 million debt refinancing. In November 2010, VMI was authorized $2.85 million in bond proceeds through the Virginia College Building Authority for the South Institute Hill Parking project. This additional debt is consistent with VMI's debt policy and will be funded from cadet fees.

VMI increased tuition and fees in FY 2011 by 8.2% for in-state cadets and 5.4% for out-of-state cadets. VMI estimates that increases for FY 2012 will be in the 6% to 7% range since State appropriations continue to decrease in FY 2012, federal "stimulus" funds discontinue, and private income support will decrease.

VMI enrolled a record 1,603 cadets in fall 2010 (FY 2011) which compares to 1,527 cadets in fall 2009 (FY 2010) for an increase of 76 cadets or 5.0%. The enrollment consisted of 59.6% in-state cadets in fall 2010 compared to 58.6% in fall 2009. VMI is planning for approximately 1,590 cadets in fall 2011 consisting of 59.5% in-state cadets. VMI's Six-Year Institutional Plan projects fall enrollment to be maintained at approximately 1,600 to 1,625 cadets with the proportion of in-state cadets at about 60%.

VMI's executive management believes that the Institute is well positioned to continue to provide excellent programs and services to its cadets as it maintains a clear educational focus and a well-established niche in the higher education marketplace. VMI continues to enjoy favorable student demand and a national reputation especially for its engineering programs. VMI received 1,791 applications for its new cadet class this fall for an increase of almost 4% over last year. A total of 983 or 55% of the applicants were offered admissions and a total of 501 students or 51% enrolled in August 2010.

Reductions in State support and in private support for the next few years will affect operations and programs for the near term; however, VMI plans to keep its tuition and fees competitive and continue to offer attractive financial assistance packages that will help to sustain enrollment and the quality of its programs and services. Although the number of cadets who receive Reserve Officers Training Corps (ROTC) scholarships has declined this year, the number continues to be about 25% of the Corps (approximately 60% of VMI's graduates in May 2011 are expected to receive a commission in the armed services). A Corps size of at least 1500 cadets on average for the year with about 40% out-of-state cadets will mitigate some of the impact of reduced State and private funding. VMI will also continue to improve the efficiency and the effectiveness of all its operations and programs through regular assessments in accordance with its internal initiatives, the mandates of its accrediting body, and the State's Agency Risk Management and Internal Control Systems policies.

The Governor's Commission on Higher Education Reform, Innovation, and Investment is expected to issue its recommendations in November 2010 to improve higher education. Some of the major topics include: affordability; increasing the number of graduates; attracting more students to science, technology, engineering and math; developing a sustainable higher education funding model; developing innovative ways to deliver quality instruction; and cost containment. These recommendations may result in legislation and policies that will help to bolster State funding for institutions overall and especially to those who make progress in specific areas.

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FINANCIAL STATEMENTS

VIRGINIA MILITARY INSTITUTE
Statement of Net Assets
As of 30 June 2010

ASSETS	
Current assets	
Cash and cash equivalents (Note 2)	$ 12,160,165
Cash equivalent held by Treasurer of Virginia (Note 2)	1,868,622
Collateral held for securities lending (Note 2)	1,007,110
Accounts receivable, *Net of allowance for doubtful accounts of $49,655* (Note 3)	860,922
Due from the Commonwealth	160,544
Prepaid expenditures	853,757
Inventory (Note 4)	4,597,054
Loans receivable	100,898
Total current assets	21,609,072
Noncurrent assets	
Cash and cash equivalents (Note 2)	(2,429,045)
Investments held with trustees (Note 2)	11,655,203
Appropriations available\Due from Commonwealth	4,043,387
Accounts receivable (Note 3)	338,554
Loans receivable, *Net of allowance for doubtful accounts of $27,888*	1,269,851
Nondepreciable capital assets (Note 5)	10,558,223
Depreciable capital assets, *Net of accumulated depreciation* (Note 5)	208,614,385
Total noncurrent assets	234,050,558
Total assets	255,659,630
LIABILITIES	
Current liabilities	
Accounts payable and accrued expenses (Note 6)	6,298,808
Unearned revenue	1,480,348
Obligations under securities lending	2,875,732
Deposits held for others	21,487
Long-term liabilities-current portion: (Note 7)	
Compensated absences	992,808
Bonds payable (Note 8)	440,000
Notes payable (Note 8)	200,000
Capital lease payable (Note 8)	7,073
Installment purchase obligations (Note 8)	14,889
Total current liabilities	12,331,145
Noncurrent liabilities	
Accrued liabilities (Note 6)	909,394
Federal loan program contributions refundable	1,320,049
Retainage payable (Note 10)	305,007
Long-term liabilities-noncurrent portion: (Note 7)	
Compensated absences	350,778
Bonds payable (Note 8)	9,339,037
Notes payable (Note 8)	3,340,541
Capital lease payable (Note 8)	616
Installment purchase obligations (Note 8)	2,933
Total noncurrent liabilities	15,568,355
Total liabilities	27,899,500
NET ASSETS	
Invested in capital assets, net of related debt	205,827,518
Restricted-nonexpendable	
Endowment	1,267,021
Restricted-expendable	
Scholarships and other	1,263,475
Loan funds	537,634
Quasi-endowment-restricted	7,740,638
Unrestricted	11,123,844
Total net assets	227,760,130
Total liabilities and net assets	$ 255,659,630

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

COMBINED STATEMENT OF FINANCIAL POSITION
Component Units of Virginia Military Institute
As of 30 June 2010

ASSETS	
Current assets:	
Cash and cash equivalents	$ 10,093,999
Contributions receivable (Note 18)	6,459,408
Accounts receivable	147,806
Other	279,821
Total current assets	16,981,034
Noncurrent assets:	
Contributions Receivable (Note 18)	7,573,287
Investments held by trustees (Note 18)	249,352,856
Investments, other (Note 18)	14,306,247
Investment securities	104,194
Cash surrender of life insurance	5,007,649
Property and equipment, net of accumulated depreciation	314,968
Total noncurrent assets	276,659,201
Total assets	293,640,235
LIABILITIES	
Current liabilities:	
Accounts payable and accrued expenses	805,335
Unearned revenue	8,304
Long-term liabilities-current portion:	
Trust and annuity obligations	716,396
Total current liabilities	1,530,035
Noncurrent liabilities:	
Other liabilities	240,896
Long-term liabilities-noncurrent portion:	
Bonds payable (Note 18)	47,372,462
Trust and annuity obligations	3,818,420
Total noncurrent liabilities	51,431,778
Total liabilities	52,961,813
NET ASSETS	
Unrestricted	45,312,739
Temporarily restricted	92,491,141
Permanently restricted	102,874,542
Total net assets	240,678,422
Total liabilities and net assets	$ 293,640,235

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

VIRGINIA MILITARY INSTITUTE
Statement of Revenues, Expenses, and Changes in Net Assets
For the Year Ended 30 June 2010

Operating revenues:	
Tuition and fees, *Net of scholarships allowances of $4,843,167*	$ 15,251,565
Federal grants and contracts	398,318
State and private grants and contracts	9,000
Sales and services of educational departments	605,833
Auxiliary enterprise, *Net of scholarship allowances of $4,058,386*	13,128,557
Unique military activities, *Net of scholarships allowances of $704,094*	2,058,314
Other sources:	
Museum programs	478,207
Rents and commissions	259,767
Miscellaneous	187,621
Total operating revenues	32,377,182
Operating expenses:	
Educational and general	
Instruction	18,142,297
Research	304,011
Public service	1,248,969
Academic support	6,340,536
Student services	3,555,590
Institutional support	4,995,369
Operation and maintenance of physical plant	8,265,578
Scholarships and related expense	688,750
Auxiliary enterprises	18,223,371
Unique military activities	6,001,428
Loan cancellations and write-offs bad debt expense	4,764
Total operating expenses (Note 11)	67,770,663
Net operating income (loss)	(35,393,481)
Nonoperating revenues/(expenses):	
State appropriations (Note 12)	11,325,528
Gifts and contributions	15,529,830
Federal student financial aid (Pell)	1,014,954
Federal stabilization funds (ARRA)	765,001
Investment income (loss)	1,569,522
Interest on capital asset - related debt	(478,187)
Loss on disposal of plant assets	(1,234,371)
Net nonoperating revenues/(expenses)	28,492,277
Income (loss) before other revenues	(6,901,204)
Other revenues:	
Grants and contributions-capital	20,707,194
Investment income-capital	12
Total other revenues	20,707,206
Increase/(Decrease) in net assets	13,806,002
Net assets beginning of the year	213,954,128
Net assets end of year	$ 227,760,130

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

COMBINED STATEMENT OF ACTIVITIES
Component Units of Virginia Military Institute
For the Year Ended 30 June 2010

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES				
Amounts raised on behalf of VMI	$ 7,336,447	$ 5,461,294	$ 3,253,828	$ 16,051,569
Grants, contributions and contracts	861,170	102,826	-	963,996
Event sponsorships, registrations and fees	3,555	-	-	3,555
Investment income	2,902,076	1,548	-	2,903,624
Actuarial gain/(loss) on trust and annuity obligations	(208,565)	(274,409)	(89,674)	(572,648)
Unrealized loss on swap contract	-	(406,858)	-	(406,858)
Administrative fees	40,000	-	-	40,000
Other income	32,911	-	-	32,911
Net assets released from restrictions and reclassifications	7,176,086	(7,176,086)	-	-
Total revenues	18,143,680	(2,291,685)	3,164,154	19,016,149
EXPENSES				
Amounts remitted directly to or on behalf of VMI:				
Unrestricted	8,871,618	-	-	8,871,618
Designated	9,297,841	-	-	9,297,841
Cost of operations	5,860,355	-	-	5,860,355
Conference, research and education	647,531	-	-	647,531
Total expenses	24,677,345	-	-	24,677,345
Change in net assets before net realized and unrealized gains on investments	(6,533,665)	(2,291,685)	3,164,154	(5,661,196)
Net realized and unrealized gains on investments	10,910,575	18,960,833	-	29,871,408
Change in net assets	4,376,910	16,669,148	3,164,154	24,210,212
NET ASSETS				
Beginning	40,935,829	75,821,993	99,710,388	216,468,210
Ending	$ 45,312,739	$ 92,491,141	$ 102,874,542	$ 240,678,422

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

VIRGINIA MILITARY INSTITUTE

Statement of Cash Flows
For the Year Ended 30 June 2010

Cash provided/(used) by operating activities:	
Tuition and fees	$ 15,346,689
Federal grants and contracts	398,318
State and private grants and contracts	9,000
Sales and services-educational and general	599,477
Auxiliary charges	13,170,779
Unique military activity charges	2,058,767
Other operating receipts	666,693
Payments to employees for salaries and benefits	(36,577,224)
Payments for supplies and services	(23,365,874)
Payments for scholarships and fellowships	(618,507)
Loan funds issued to students	(302,104)
Collections of loans from students	169,234
Net cash provided/(used) by operating activities	(28,444,752)
Cash provided/(used) by noncapital financing activities:	
State appropriations	11,325,528
Nonoperating grants and contracts	1,779,955
Gifts and contributions for other than capital purposes	17,403,143
Federal Direct Lending Program-receipts	4,895,218
Federal Direct Lending Program-disbursements	(4,895,218)
Agency receipts	5,112,514
Agency disbursements	(5,207,986)
Net cash provided/(used) by noncapital financing activities	30,413,154
Cash provided/(used) by capital and related financing activities:	
Capital appropriations	379,963
Capital gifts and contributions	21,439,488
Proceeds from sale of capital assets	12,810
Purchase and construction of capital assets	(22,280,808)
Proceeds from capital debt	4,736,032
Principal paid on capital debt, leases and installments	(5,365,846)
Interest paid on capital debt, leases and installments	(550,902)
Investment income-capital	12
Net cash provided/(used) by capital and relating financing activities	(1,629,251)
Cash provided/(used) by investing activities:	
Interest on investments	107,202
Investment/Endowment income	180,894
Sale of investments	669,252
Purchase of investments	(22,500)
Net cash provided/(used) by investing activities	934,848
Net increase/(decrease) in cash	1,273,999
Cash-beginning of year	8,457,121
Cash-end of year	$ 9,731,120

VIRGINIA MILITARY INSTITUTE
Statement of Cash Flows
For the Year Ended 30 June 2010

Reconciliation of net operating expenses to net cash used by operating activities:

Operating loss	$	(35,393,481)
Adjustments to reconcile net operating expenses to cash used by operating activities:		
Depreciation expense		6,954,540
Changes in assets and liabilities:		
Accounts receivable		(332,906)
Inventories		(327,582)
Prepaid expenditures		10,593
Due from Commonwealth		74,298
Loans receivable		(140,375)
Accounts payable and accrued liabilities		468,373
Unearned revenue		216,550
Compensated absences		12,970
Federal loan program contributions refundable		12,268
Net cash used in operating activities	$	(28,444,752)

Noncash investing, noncapital financing, and capital related financing transactions:

Change in fair value of investments recognized as a component of investment income	$	643,977
Capital assets acquired through in-kind donations as a component of capital gifts and contributions income		492,929
	$	1,136,906

Reconciliation of cash and cash equivalents to the Statement of Net Assets:

Cash and cash equivalents classified as current assets		12,160,165
Cash and cash equivalents classified as noncurrent assets		(2,429,045)
	$	9,731,120

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

- NOTES TO FINANCIAL STATEMENTS -

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Virginia Military Institute (VMI) have been prepared in accordance with generally accepted accounting principles for colleges and universities. The significant accounting policies followed by the Institute are as follows:

A. Reporting Entity

The Virginia Military Institute believes that the measure of a college lies in the quality and performance of its graduates and their contributions to society. Therefore, it is the mission of the Virginia Military Institute to produce educated, honorable men and women prepared for the varied work of civil life, imbued with love of learning, confident in the functions and attitudes of leadership, possessing a high sense of public service, advocates of the American Democracy and free enterprise system, and ready as citizen-soldiers to defend their country in time of national peril.

To accomplish this result, Virginia Military Institute shall provide to qualified young men and women undergraduate education of highest quality – embracing engineering, science, and the arts – conducted in, and facilitated by, the unique VMI system of military discipline.

Virginia Military Institute is part of the Commonwealth of Virginia's statewide system of public higher education. The Board of Visitors, appointed by the Governor, is responsible for overseeing the Institute's governance. A separate report is prepared for the Commonwealth of Virginia which includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. The Institute is a component unit of the Commonwealth of Virginia and is included in the general purpose financial statements of the Commonwealth.

The Governmental Accounting Standards Board (GASB) Statement 39, *Determining Whether Certain Organizations Are Component Units,* became effective for the fiscal year ended 30 June 2004. GASB Statement 39 provides guidance to determine whether certain organizations for which the Institute is not financially accountable should be reported as component units. Generally, it requires reporting as a component unit, an organization that raises and holds economic resources for the direct benefit of the Institute.

The VMI Alumni Agencies is a legally separate, tax-exempt entity whose purpose is to organize the alumni of the Institute and to aid in the promotion of its welfare and the successful prosecution of its educational purposes. It accomplishes this through fund-raising to supplement the support VMI receives from the Commonwealth of Virginia and the tuition and fees charged to cadets. Because the VMI Alumni Agencies' resources are held almost entirely for the benefit of the Institute and these resources are considered significant to the Institute, we have determined that the Alumni Agencies should be included as a component unit.

The VMI Research Laboratories (VMIRL) is a legally separate, tax-exempt entity whose purpose is to administer contract and grant research at the Institute. Because of the VMIRL's close relationship to the Institute, we believe in our professional judgment, it should be included as a component unit in our financial statements. Both the VMI Alumni Agencies and the VMIRL have been discretely presented in these statements.

Because the VMI Alumni Agencies and the VMIRL report under a different reporting model, the Financial Accounting Standards Board (FASB) standards, the VMI Board of Visitors and the administration of the Institute believe the Institute's financial statements should be presented on a page separate from the Institute's component units as allowed by GASB Statement 39. Separate financial statements for the VMI Alumni Agencies may be obtained by writing the Chief Financial Officer, VMI Foundation, Inc., P.O. Box 932, Lexington, Virginia 24450. Separate financial statements for the VMI Research Laboratories, Inc., may be obtained by writing the Treasurer, VMI Research Laboratories, Inc., Virginia Military Institute, Lexington, Virginia 24450.

B. Financial Statement Presentation

The Institute's accounting policies conform with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) pronouncements as well as applicable Financial Accounting Standards Board (FASB) statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before 30 November 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The financial statements have been prepared in accordance with GASB Statement 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities.*

The VMI Alumni Agencies and the VMI Research Laboratories, Inc. are private, nonprofit organizations that report under FASB standards including FASB Statement 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the VMI Alumni Agencies' or the VMI Research Laboratories' financial information in the Institute's financial report for these differences.

C. Basis of Accounting

For financial statement purposes, the Institute is considered a special-purpose government engaged only in business-type activities. Accordingly, the Institute's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-agency transactions have been eliminated.

D. Cash, Cash Equivalents and Investments

In accordance with GASB Statement 9, *Definition of Cash and Cash Equivalents*, cash represents cash with the Treasurer, cash on hand, and cash deposits including certificate of deposits, and temporary investments with original maturities of three months or less.

In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools,* purchased investments, interest-bearing temporary investments classified with cash, and investments received as gifts are recorded at fair value. All investment income, including changes in the fair value of investments (unrealized gains and losses), is reported as nonoperating revenue in the Statement of Revenues, Expenses, and Changes in Net Assets.

E. Capital Assets

Capital assets include land, buildings and other improvements, library materials, equipment, infrastructure assets such as sidewalks, steam tunnels, and electrical and computer network cabling systems, and intangible assets. The Institute capitalizes construction costs that have a value or cost in excess of $100,000 at the date of acquisition. Renovations in excess of $100,000 are capitalized if they significantly extend the useful life of the existing asset. Expenses for major capital assets and improvements are capitalized (construction in progress) as projects are constructed. Routine repairs and maintenance are charged to operating expense in the year the expense is incurred. Interest expense relating to construction is capitalized net of interest income earned on resources set aside for this purpose. The costs of normal maintenance and repairs that do not add to an asset's value or materially extend its useful life are not capitalized.

The Institute capitalizes moveable equipment at a value or initial cost of $5,000 or more and an estimated useful life in excess of two years. Buildings and equipment are stated at appraised value or actual cost where determinable. Land is stated at cost. Library materials are valued using published average prices for library acquisitions. Intangible assets are capitalized with an acquisition cost of $100,000 and a useful life of one or more years.

Depreciation is computed using the straight-line method over the estimated useful life of the asset. Average useful lives by asset categories are listed below:

Buildings	50 years
Other improvements	10-30 years
Equipment	5-25 years
Library materials	10 years
Intangible assets	5 years to indefinite

The Institute does not capitalize works of art, historical treasures and similar assets. Such items are held for public exhibition, education or research in the furtherance of public service rather than financial gain. Institute collections may be sold but the proceeds must be used for the acquisition of similar type Institute collections. Exceptions to this requirement must be pre-approved by the Deputy Superintendent for Finance, Administration and Support.

F. Inventories

Inventory cost values for the museum, post hospital and physical plant are determined by using the weighted average method. The military store inventory is valued at cost using the first-in first-out method.

G. Unearned Revenue

Unearned revenue represents revenues collected but not earned as of 30 June 2010. This is primarily composed of revenue for student tuition and fees received in advance of the next semester or term.

H. Interest Capitalization

Interest expense incurred during the construction of capital assets is capitalized, if material, net of interest income earned on resources set aside for this purpose. The Institute incurred interest expense totaling $478,187 for the fiscal year ended 30 June 2010, of which none was capitalized as construction period interest.

I. Accrued Compensated Absences

Nonfaculty salaried employee's attendance and leave regulations make provisions for the granting of a specified number of days of leave with pay each year. Instructional personnel do not earn leave. The amount of leave earned but not taken as of 30 June 2010 is recorded as a liability on the Statement of Net Assets. The liability reflects all earned vacation, compensatory and overtime leave not taken as well as the amount payable under the Commonwealth of Virginia's sick leave payout policy upon termination which is the lesser of 25% of sick leave not taken or $5,000 per employee with five or more years of service. Also included is an estimation of sick leave for those employees who, while not currently vested, will probably attain the 5 years of service required to vest. The last element reflected in the liability is Social Security and Medicaid taxes to be paid by the Institute on all accrued compensated absences.

J. Federal Financial Assistance Programs

The Institute participates in federally funded Pell Grants, Supplemental Educational Opportunity Grants, Federal Work-Study and Perkins Loans programs. Federal programs are audited in accordance with the Single Audit Act Amendments of 1996, the Office of Management and Budget Revised Circular A-133, *Audit of States, Local Governments and Non-Profit Organizations,* and the Compliance Supplement.

K. Net Assets

The Institute's net assets are classified as follows:

Invested in capital assets, net of related debt: This represents the Institute's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted net assets – nonexpendable: Nonexpendable restricted net assets consist of endowment funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.

Restricted net assets – expendable: Restricted expendable net assets include resources in which the Institute is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets: Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the Institute, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for students, faculty and staff. Also included in unrestricted net assets are funds that have been set aside by the Board of Visitors as quasi-endowments. These funds are treated the same as true endowment funds; however, unlike true endowments they may be expended.

The Institute has no policy regarding flow assumption to determine which assets (restricted or unrestricted) are being used when both restricted and unrestricted assets are available for the same purpose. Our practice is to allow Department Heads to make this determination and they typically spend unrestricted assets prior to spending restricted resources.

L. Classification of Revenues

The Institute has classified its revenues as either operating or nonoperating revenues according to the following criteria:

Operating revenues: Operating revenues include activities that have the characteristics of exchange transactions, such as (1) student tuition and fees, net of scholarship discounts and allowances, (2) sales and services of auxiliary enterprises, net of scholarship discounts and allowances, (3) most federal, state and local grants and contracts, and (4) interest on student loans.

Nonoperating revenues: Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB 9 *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting,* GASB 33 *Accounting and Financial Reporting for Nonexchange Transactions,* and GASB 34, such as state appropriations and investment income.

Scholarship Discounts and Allowances: Student tuition and fee revenues are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the Institute, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in the Institute's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees, the Institute has recorded a scholarship discount and allowance.

NOTE 2: CASH AND CASH EQUIVALENTS AND INVESTMENTS

The following information is provided with respect to the Institute's cash, cash equivalents, and investments as of 30 June 2010. The following risk disclosures are required by GASB Statement 40, *Deposit and Investment Risk Disclosures*.

Custodial credit risk (Category 3 deposits and investments) – The custodial risk for deposits is the risk that, in the event of a failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in possession of an outside party. The Institute had no category 3 deposits or investments for fiscal year 2010.

Credit risk – The risk that an issuer or other counterparty to an investment will not fulfill its obligations. GASB Statement 40 requires the disclosure of the credit quality ratings of all investments subject to credit risk.

Concentration of credit risk – The risk of loss attributed to the magnitude of a government's investment in a single issuer is referred to as a credit risk. GASB Statement Number 40 requires disclosure of any issuer with more than five percent of total investments.

Interest rate risk - This is the risk that interest rate changes will adversely affect the fair value of an investment. GASB Statement 40 requires disclosure of maturities for any investments subject to interest rate risk. The Institute does not have an interest rate risk policy.

Foreign currency risk – This risk refers to the possibility that changes in exchange rates will adversely affect the fair value of an investment or a deposit.

The Institute's credit risk, concentration of credit risk, interest rate risk, and foreign currency risk are described in the Investments note below.

Cash and Cash Equivalents

Pursuant to Section 2.2-1800, et seq., Code of Virginia, all state funds of VMI are maintained by the Treasurer of Virginia, who is responsible for the collection, disbursement, custody, and investment of state funds. Cash deposits held by VMI are maintained in accounts that are collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400, et seq., Code of Virginia.

Cash and cash equivalents consist of the following balances as of 30 June 2010:

	Current	Noncurrent	Total
Cash with Treasurer of Virginia	$ 10,021,016	$ (2,782,540)	$ 7,238,476
SunTrust NOW checking	2,101,029	353,495	2,454,524
Securities under securities lending	1,868,622	-	1,868,622
Petty cash	10,120	-	10,120
Wachovia Bank time deposit	28,000	-	28,000
Total cash and cash equivalents	$ 14,028,787	$ (2,429,045)	$ 11,599,742

As of 30 June 2010, the Institute had approximately $2.8 million of expenses in Virginia College Building Authority (VCBA) 21st Century bond funded capital projects for which it had not yet been reimbursed, resulting in a cash deficit in noncurrent funds. For these projects, the Institute must first incur the expenses and seek reimbursement from the Commonwealth on a monthly basis. An equal amount is reflected as a receivable, due from the Commonwealth, and is included in the line Appropriations available/due from the Commonwealth, within the noncurrent assets portion of the Statement of Net Assets.

Investments

Investments include endowment and similar funds pooled and invested with VMI affiliates and retirement fund investments for selected employees. It also includes VMI's allocated share of securities held for security lending transactions conducted by the Commonwealth. Investments consist of the following balances as of 30 June 2010:

	Current	Noncurrent	Total
Investments with the Treasurer of Virginia:			
Securities under securities lending	$ 1,007,110	$ -	$ 1,007,110
Investments with trustees:			
Investments pooled with VMI affiliates	-	10,745,810	10,745,810
Mutual fund investments (retirement accounts)	-	909,393	909,393
Total with trustees	-	11,655,203	11,655,203
Total investments	$ 1,007,110	$ 11,655,203	$ 12,662,313

VMI's endowment, loan and similar funds are pooled for investment purposes with the endowment funds of its affiliate, the VMI Alumni Agencies (the VMI Foundation, Inc., the VMI Development Board, Inc., and the VMI Keydet Club) and the George C. Marshall Foundation. VMI owns units in the pooled fund (the "Fund") that operates similar to a mutual fund. VMI Investment Holdings, LLC (LLC) manages and operates the unitized investment pool with BNY Mellon serving as custodian. The VMI Foundation, Inc. is the sole member of the LLC and acts as an intermediary between the LLC and VMI and the other agencies. Deposits to and withdrawals from the pool by VMI and the other agencies are made through the LLC. A separate board of directors manages the LLC. The board has approved an investment policy that outlines the standards and disciplines adopted, and the investment objectives, principles, and guidelines for managing the Fund. Authorized investments are set forth in the Uniform Prudent Management of Institutional Funds Act, Section 55-268 et seq. of the Code of Virginia and may include any real or personal property, whether or not it produces a current return, including mortgages, stocks and bonds, debentures, and other securities of profit or nonprofit corporations, shares in or obligations of associations, partnerships, or individuals, and obligations of any government or subdivision.

The market value of the Fund as of 30 June 2010 was $266.1 million, of which, VMI owned $10.7 million or 4.0 percent of the Fund assets. The Fund annually approves an asset allocation which includes how assets are invested in major categories of investments. The Fund held $48.7 million in debt securities with an average maturity of 7.6 years. The average quality rating was AA (Moody's). The Fund held $71.1 million in US equity investments. The Fund held $38.0 million in developed markets international funds with equities denominated primarily in the Euro, the Pound, and the Yen, and $13.9 million in emerging markets international funds with equities denominated in a variety of currencies. The Fund held $72.3 million in absolute return fund investments which may also hold fixed income and equity securities. The remaining investments are held in other diversifying investments. The custodians for the Fund are independently audited annually.

Securities Lending Transactions

Collateral held for securities lending and the securities lending transactions reported on the financial statements represent the Institute's allocated share of securities received for securities lending transactions held in the General Account of the Commonwealth. Information related to the credit risk of these investments and securities lending transactions held in the General Account is available on a statewide level in the Commonwealth of Virginia's *Comprehensive Annual Financial Report.* The Commonwealth's policy is to record unrealized gains and losses in the General Fund in the Commonwealth's basic financial statements. When gains or losses are realized, the actual gains and losses are recorded by the affected agencies.

Funds Held In Trust By Others

Assets of funds held by trustees for the benefit of the Institute are not reflected in the accompanying Statement of Net Assets. The Institute has irrevocable rights to all or a portion of the income of these funds. However, assets of the funds are not under the management discretion of the Institute according to the trust agreements. Income from funds held by trustees for the benefit of the Institute totaled $59,997 for fiscal year 2010 and is included in the endowment income.

NOTE 3: ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following at 30 June 2010:

Current:		
Student tuition and fees	$	483,056
Other educational and general		31,545
Auxiliary enterprises		75,133
Unique military activity		3,403
Private gifts		260,553
Other		29,672
Retirement of indebtedness		27,215
	$	910,577
Less: Allowance for doubtful accounts		(49,655)
Total current accounts receivable, net	$	860,922
Noncurrent:		
Other operating		338,554
Total noncurrent accounts receivable	$	338,554
Total accounts receivable, net	$	1,199,476

NOTE 4: INVENTORIES

Inventories consisted of the following at 30 June 2010:

Physical Plant	$	377,592
Military Store		4,058,238
Museums		139,104
VMI Hospital		22,120
Total	$	4,597,054

NOTE 5: CAPITAL ASSETS

A summary of changes in the various capital asset categories is presented as follows:

	Beginning Balance 1 July 2009	Additions	Reductions	Ending Balance 30 June 2010
Nondepreciable capital assets:				
Land	$ 2,523,476	$ 485,500	$ -	$ 3,008,976
Construction in progress	14,013,393	2,210,146	(8,674,292)	7,549,247
Total nondepreciable capital assets	16,536,869	2,695,646	(8,674,292)	10,558,223
Depreciable capital assets:				
Buildings	232,664,584	24,022,793	(2,228,600)	254,458,777
Improvements other than buildings	13,933,684	-	(668,234)	13,265,450
Equipment	13,471,536	761,663	(366,449)	13,866,750
Library books	10,890,992	263,049	(80,161)	11,073,880
Total depreciable capital assets	270,960,796	25,047,505	(3,343,444)	292,664,857
Less accumulated depreciation for:				
Buildings	57,909,101	4,802,319	(1,098,795)	61,612,625
Improvements other than buildings	3,101,684	614,180	(599,277)	3,116,587
Equipment	8,763,347	1,281,690	(318,030)	9,727,007
Library books	9,418,063	256,351	(80,161)	9,594,253
Total accumulated depreciation	79,192,195	6,954,540	(2,096,263)	84,050,472
Depreciable capital assets, net	191,768,601	18,092,965	(1,247,181)	208,614,385
Total capital assets, net	$ 208,305,470	$ 20,788,611	$ (9,921,473)	$ 219,172,608

NOTE 6: ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consisted of the following at 30 June 2010:

Current liabilities:	
Employee salaries, wages and benefits payable	$ 3,616,505
Vendors and supplies accounts payable	2,565,095
Accrued interest payable	87,208
Other accrued liabilities	30,000
Total current-accounts payable and accrued expenses	$ 6,298,808
Noncurrent liabilities:	
Retirement annuities	$ 909,394
Total noncurrent-accrued liabilities	$ 909,394

NOTE 7: LONG-TERM LIABILITIES SUMMARY

The Institute's long-term liabilities primarily consist of long-term debt (further described in Note 8) and accrued compensated absences. A summary of changes in long-term liabilities for the year ending 30 June 2010 is presented as follows:

	Beginning Balance 1 July 2009	Additions	Reductions	Ending Balance 30 June 2010	Current Portion 30 June 2010
Long-term debt:					
Bonds payable	$ 10,237,193	$ 779,417	$ (1,237,573)	$ 9,779,037	$ 440,000
Notes payable	3,740,320	-	(199,779)	3,540,541	200,000
Capital leases	14,204	-	(6,515)	7,689	7,073
Installment purchases	49,796	-	(31,974)	17,822	14,889
Total long-term debt	$ 14,041,513	$ 779,417	$ (1,475,841)	$ 13,345,089	$ 661,962
Accrued compensated absences	1,330,617	1,081,597	(1,068,628)	1,343,586	992,808
Total long-term liabilities	$ 15,372,130	$ 1,861,014	$ (2,544,469)	$ 14,688,675	$ 1,654,770

NOTE 8: LONG-TERM INDEBTEDNESS DETAIL

Bonds payable:

In August 2004, pursuant to Section 9(c) of Article X of the Constitution of Virginia, $11,240,000 of revenue bonds, Series 2004A, were issued by the Department of Treasury for the Commonwealth of Virginia, on behalf of the Institute for renovation and expansion of Crozet Hall, the Institute dining facility, and parking. The bonds bear interest at an average coupon rate of 4.8% and are payable over 20 years through June 2025. Net proceeds after the cost of issuance total $11,889,591 and included a premium realized on the sale. The revenue bonds are secured by the net revenues of the facility which is comprised primarily of cadet fees.

Bonds Payable:	Interest Rates (%)	Maturity	Balance 30 June 2010
Crozet Hall:			
Series 2004A, issued $11,240,000 - partial refunding *	3.75 - 5.00	2025	$ 5,062,357
Series 2009D, issued $4,241,860 - refunding Series 2004A *	2.50 - 5.00	2022	4,716,680
			$ 9,779,037

* See Note 9 Long-Term Debt Defeasance

Notes payable:

Notes payable are debt obligations between the Virginia College Building Authority (VCBA) and the Institute. The VCBA issues bonds through the Pooled Bond Program and uses the proceeds to purchase debt obligations (notes) of the Institute. The JM Hall Renovation note is secured by funds paid by the VMI Foundation, Inc. on a year-to-year basis as a gift to the Institute. Should the gift be discontinued, repayment will be made from the general revenues of the Institute. The Cocke Hall Annex note will be paid from auxiliary reserve funds which consist predominantly of cadet fees.

Notes Payable:	**Interest Rates (%)**	**Maturity**	**Balance 30 June 2010**
Cocke Hall Annex:			
Series 2002A, issued $2,025,000 - partial refunding *	4.00 - 5.25	2022	$ 875,255
Series 2007B, issued $735,000 - refunding Series 2002A *	4.00 - 4.50	2020	769,643
Jackson Memorial Hall Renovation:			
Series 2002A, issued $2,335,000 - partial refunding *	4.00 - 5.25	2022	1,005,607
Series 2007B, issued $850,000 - refunding Series 2002A *	4.00 - 4.50	2020	890,036
			$ 3,540,541

* See Note 9 Long-Term Debt Defeasance

Maturities on notes and bonds payable for years succeeding 30 June 2010 are as follows:

Year	**Bonds Payable**	**Notes Payable**	**Total**
2011	$ 440,000	$ 200,000	$ 640,000
2012	455,000	210,000	665,000
2013	475,000	220,000	695,000
2014	500,000	230,000	730,000
2015	525,000	240,000	765,000
2016-2020	2,796,860	1,360,000	4,156,860
2021-2025	3,885,000	985,000	4,870,000
Unamortized premium	965,480	101,984	1,067,464
Deferral on debt defeasance	(263,303)	(6,443)	(269,746)
Total future principal requirements	$ 9,779,037	$ 3,540,541	$ 13,319,578

A summary of future interest commitments for fiscal years subsequent to 30 June 2010 is presented as follows:

Year	Bonds Payable	Notes Payable	Total
2011	$ 437,199	$ 157,275	$ 594,474
2012	420,699	147,125	567,824
2013	397,949	136,475	534,424
2014	374,199	125,050	499,249
2015	349,199	114,275	463,474
2016-2020	1,375,373	450,100	1,825,473
2021-2025	556,659	35,437	592,096
Total future interest requirements	$ 3,911,277	$ 1,165,737	$ 5,077,014

Installment Purchase Obligations

The Institute has future obligations under installment purchase agreements. The book value of the assets capitalized under these installment purchase agreements is $176,468 with no interest. A summary of future obligations under these agreements as of 30 June 2010 follows:

Year Ending 30 June	Principal
2011	$ 14,889
2012	2,200
2013	733
Total	$ 17,822

Capital Leases Payable

VMI is the lessee of equipment under capital leases expiring in 2012. The assets acquired under capital leases are recorded as property, plant, and equipment at the lower of the net present value of the minimum lease payments during the lease term or the fair market value of the asset.

For all capital leases, the minimum lease payments together with the present value of the net minimum lease payments as of 30 June 2010 are as follows:

Year Ending 30 June	Capital Leases
2011	$ 9,925
2012	827
Total minimum lease payments	10,752
Less: Executory costs	(2,688)
Less: Interest	(375)
Present value of net minimum lease payments	$ 7,689

Equipment Trust Fund

The Equipment Trust Fund (ETF) program was established to provide state-supported institutions of higher education bond proceeds for financing the acquisition and replacement of instructional and research equipment. The Virginia College Building Authority (VCBA) manages the program. The VCBA issues bonds and uses the proceeds to reimburse the Institute and other institutions of higher education for equipment purchased. For fiscal years prior to 1999, the VCBA purchased the equipment and leased it to the Institute. For fiscal years 1999 and following, financing agreements for ETF were changed so that the Institute now owns the equipment from the date of purchase.

The Statement of Net Assets line-Current assets “Due from the Commonwealth of Virginia” includes $37,066 representing equipment purchased by the Institute that was not reimbursed by the VCBA as of 30 June 2010.

Operating Leases

VMI is committed under various operating leases for equipment. Operating leases do not give rise to property rights or lease obligations, and therefore the results of the lease agreements are not reflected in the Institute’s Statement of Net Assets. In general, the leases are for a three year term and the Institute has renewal options. In most cases, the Institute expects these leases will be replaced by similar leases in the normal course of business. Rental expense was approximately $82,800 for the year ended 30 June 2010. Rental expense commitments for subsequent fiscal years are as follows:

Year Ending 30 June	Amount
2011	$ 82,923
2012	57,546
2013	20,382
Total	$ 160,851

Capital Improvement Commitments

As of 30 June 2010, the Institute had outstanding construction contract commitments of $8,273,457. This amount represents the value of obligations remaining on capital improvement project contracts. These obligations are for future efforts and as such have not been accrued as expenses or liabilities on the Institute’s financial statements.

NOTE 9: LONG-TERM DEBT DEFEASANCE

Current Year:
On 21 October 2009, the Virginia Department of Treasury Board, on behalf of the Institute, issued $5,012,603 of Section 9(c) general obligation bonds to advance-refund $4,727,357 of section 9(c) debt in fiscal year 2010. The advance refunding reduced the aggregate debt service by $430,969, representing a net present-value savings of $379,637

Previous Years:
In previous fiscal years, in accordance with GASB Statement 7, *Advance Refundings Resulting in the Defeasance of Debt,* the Institute has excluded from its financial statements the assets in escrow and the Section 9(d) notes payable that were defeased in-substance. For the year ended 30 June 2010, notes payable considered defeased in previous years totaled $1,585,000.

NOTE 10: RETAINAGE PAYABLE

At 30 June 2010, $305,007 was held by the Institute as retainage on various contracts for work, which had been performed. The retainage will be remitted to the various contractors upon satisfactory completion of the projects.

NOTE 11: EXPENSES BY NATURAL CLASSIFICATIONS

The Institute's operating expenses by natural classification were as follows for the year ended 30 June 2010:

Program	Personal Services	Supplies	Contractual Services	Equipment	Utilities	Student Aid	Other Operating Expenses	Depreciation Expense	TOTAL
Instruction	$ 15,014,100	$ 159,257	$ 354,833	$ 357,397	$ -	$ -	$ 82,964	$ 2,173,746	$ 18,142,297
Research	141,534	16,584	49,365	6,163	-	-	52,838	37,527	$ 304,011
Public service	574,902	140,967	235,440	3,679	-	-	3,927	290,054	$ 1,248,969
Academic support	3,917,491	141,544	1,215,840	158,117	-	-	91,128	816,416	$ 6,340,536
Student services	2,431,082	70,752	743,082	22,710	-	-	73,307	214,657	$ 3,555,590
Institutional support	3,586,933	119,452	833,862	21,489	4,210	-	304,522	124,901	$ 4,995,369
Operation & maintenance of plant	2,969,797	1,084,147	1,438,395	929,835	876,603	-	402,735	564,066	$ 8,265,578
Student aid	13,612	2,057	93,265	6,914	-	572,902	-	-	$ 688,750
Auxiliary enterprises	4,420,710	462,579	6,877,297	388,485	190,196	37,298	3,464,593	2,382,213	$ 18,223,371
Unique military activities	3,717,020	1,372,958	184,719	46,440		8,307	321,024	350,960	$ 6,001,428
Loan administration expense	-	-	-	-	-	-	4,764	-	$ 4,764
Total operating expenditures	$ 36,787,181	$ 3,570,297	$ 12,026,098	$ 1,941,229	$ 1,071,009	$ 618,507	$ 4,801,802	$ 6,954,540	$ 67,770,663

NOTE 12: STATE APPROPRIATIONS

Virginia Military Institute receives state appropriations from the General Fund of the Commonwealth of Virginia. The Appropriation Act specifies that such unexpended appropriations shall revert, as specifically provided by the General Assembly, at the end of the biennium. For years ending at the middle of the biennium, unexpended appropriations that have not been approved for reappropriation in the next year by the Governor become part of the General Fund of the Commonwealth and are, therefore, no longer available to VMI for disbursement. Fiscal year 2010 ends the biennium.

During the fiscal year ended 30 June 2010, the Institute received the following supplemental appropriations and reversions in accordance with the Appropriation Act:

Originial legislative appropriation:	
Educational and general programs	$ 8,899,125
Unique military activity	3,139,904
Student financial assistance	750,632
Adjustments:	
Compensation adjustments	(783,751)
ETF lease payment - NGF portion	(88,844)
Student financial assistance	6,075
Debt service fee - Non-Virginia cadets	(191,055)
Appropriations transfers:	
VMI budget reduction	(422,553)
SCHEV programs	15,995
Adjusted appropriations	$ 11,325,528

NOTE 13: RETIREMENT AND PENSION SYSTEMS

Employees of the Institute are employees of the Commonwealth of Virginia. Most full-time classified salaried employees of the Institute participate in the defined benefit retirement plan administered by the Virginia Retirement System (VRS). The Institute Post Police officers participate in the Virginia Law Officers Retirement System, (VaLORS), instead of VRS. Both VRS and VaLORS are agent multiple-employer public employee retirement systems (PERS) that act as a common investment and administrative agency for the Commonwealth of Virginia and its political subdivisions.

The Institute's payroll costs for employees covered by VRS totaled $14,340,000 for the year ended 30 June 2010. The Institute's total payroll costs were $29,354,790 for the year ended 30 June 2010.

Information regarding types of employees covered, benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions as well as employer and employee obligations to contribute are established, can be found in the Commonwealth's Comprehensive Annual Financial Report (CAFR).

The Institute's total VRS contribution was $1,538,723 for the year ended 30 June 2010, which included the 5% employee contribution assumed by the employer. These contributions represent 12.26% of covered payrolls for 2010.

The Institute's payroll cost for employees covered by VaLORS was $311,848 for the year ended 30 June 2010. The Institute's total VaLORS contribution was $52,895 for the year ended 30 June 2010, which represents 20.23% of the covered payroll for the 2010 fiscal year.

The VRS does not measure assets and pension benefit obligations separately for individual state institutions. The CAFR provides disclosure of the Commonwealth's unfunded pension benefit obligation at 30 June 2010. The same report contains historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

TIAA/CREF Insurance Company Optional Retirement Plan

Some full-time faculty and contracted administrative staff participate in a retirement annuity program through TIAA/CREF Insurance Companies rather than the VRS. This is a fixed-contribution program where the retirement benefits received are based entirely upon the employer's (10.4%) contributions, plus interest and dividends, with the employer assuming the employee's contribution share.

Individual contracts issued under the plan provide for full and immediate vesting of both the Institute's and the employees' contributions. Total pension costs under this plan were approximately $914,883 year ended 30 June 2010. Contributions to the TIAA/CREF Insurance Companies were calculated using the base salary amount of approximately $8,796,962 for fiscal year 2010.

Fidelity Investments

The Institute also contributed to one other defined contribution pension plan, which is insignificant in relation to VRS and TIAA/CREF. Full-time faculty, certain administrative staff that hold academic rank, and athletic coaches are eligible to participate in this program (ORP) other than VRS and TIAA/CREF. Retirement benefits received are based entirely upon the employer's (10.4%) contributions, plus interest and dividends, with the employer assuming the employee's contribution share.

Amounts contributed to Fidelity Investments were calculated using the base salary amount of approximately $1,440,232 for fiscal year ended 30 June 2010. Total pension costs under this plan were approximately $149,784 for fiscal year 2010.

Deferred Compensation Plan

Employees of the Commonwealth may participate in the Commonwealth's Deferred Compensation Plan. Participating employees can contribute to the plan each pay period with the

Commonwealth matching up to $20 per pay period. The dollar amount match can change depending on the funding available in the Commonwealth's budget. The Deferred Compensation Plan is a qualified defined contribution plan under Section 401(a) of the Internal Revenue Code. Employer contributions under the Deferred Compensation Plan were approximately $124,170 for the fiscal year 2010.

NOTE 14: POST-EMPLOYMENT BENEFITS

The Commonwealth participates in the VRS administered statewide group life insurance program which provides postemployment life insurance benefits to eligible retired and terminated employees. The Commonwealth also provides health care credits against the monthly health insurance premiums of its retirees who have at least 15 years of service and participate in the State's health plan. Information related to these plans is available at the statewide level in the Commonwealth's *Comprehensive Annual Financial Report*.

NOTE 15: RISK MANAGEMENT

The Institute is exposed to various risks of loss related to torts; theft or, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The Institute participates in insurance plans maintained by the Commonwealth of Virginia. The state employee health care and worker's compensation plans are administered by the Department of Human Resource Management and the risk management insurance plans are administered by the Department of Treasury, Division of Risk Management. Risk management insurance includes property, general liability, medical malpractice, faithful performance of duty bond, automobile, and air and watercraft plans. The Institute pays premiums to each of these Departments for its insurance coverage. Information relating to the Commonwealth's insurance plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report.

NOTE 16: CONTINGENCIES

The Institute has received federal grants for specific purposes that are subject to review and audit by the grantor agencies. Claims against these resources are generally conditional upon compliance with the terms and conditions of grant agreements and applicable federal regulations, including the expenditure of resources for allowable purposes. Any disallowance resulting from a federal audit may become a liability of the Institute.

In addition, the Institute is required to comply with various federal regulations issued by the Office of Management and Budget. Failure to comply with certain systems requirements of these regulations may result in questions concerning the allowability of related direct and indirect charges pursuant to such agreements. As of 30 June 2010 the Institute estimates that no material liabilities will result from such audits or questions.

In October 2003, VMI entered into a contract modification with ARAMARK Educational Services, VMI's contracted dining services vendor. Under this agreement, ARAMARK provided $1,200,000 to VMI to support the expansion and renovation of the Crozet Hall dining facility. The agreement requires ARAMARK to amortize this cost on a straight-line basis over a ten-year period. In the event that VMI or ARAMARK terminates the contract, VMI must re-pay any unamortized balance to ARAMARK within 90 days of termination.

In August 2007, the Institute entered into a five year contract (with the option of one additional renewal term of five years) with ARAMARK to provide dining services to cadets. Under this agreement, ARAMARK agreed to provide a $750,000 financial commitment for food service facility renovations and for the purchase and installation of food service equipment, area treatment, signage and marketing materials and other costs associated with the Campus Food Service Program on our premises. During the first year of this contract (2008 fiscal year), the Institute received $500,000 of this commitment with the remaining balance ($250,000) to be paid during the fourth year (2011 fiscal year). In accordance with the agreement, ARAMARK agrees to amortize this commitment on a straight-line basis over a ten year period through 2017. Upon expiration or termination of this agreement by either party prior to 2017, VMI agrees to pay ARAMARK the unamortized balance plus all accrued but unbilled interest (prime rate plus two percentage points per annum, compounded monthly) within 30 days.

NOTE 17: LITIGATION

The renovation of Crozet Hall project was substantially completed on 27 July 2006, 270 days after the original contracted completion date. On 23 May 2007, the contractor filed a claim in Rockbridge County Court, suing the Institute for damages in the amount of $430,242 as a result of these delays. On 26 July 2007, the Institute paid the contractor $99,646, the amount to which the Institute believed the contractor was entitled, leaving an outstanding claim against the Institute of $330,596. On 1 May 2008, the trial court granted final judgment in favor of VMI. The contractor filed a Petition for Appeal in the Supreme Court of Virginia. The Supreme Court found in favor of the contractor and on 1 July 2009 the Supreme Court denied the Virginia Office of the Attorney General petition for reconsideration. VMI, with the assistance of the Virginia Office of Attorney General, settled the claim with the contractor for an additional $190,000 avoiding further litigation.

Separately, VMI notified the designer of a potential claim for errors and omissions. There have been multiple meetings, offers, and counter offers with the designer. On 9 February 2011 a tentative agreement was reached for $390,000. The Office of the Attorney General (OAG) has reviewed the tentative agreement and is staffing documentation to the Governor recommending approval.

NOTE 18: VMI ALUMNI AGENCIES

The VMI Alumni Agencies (the "Agencies") are comprised of four organizations that share the common purpose of raising funds, investing funds, and performing other activities on behalf of VMI alumni and other donors in support of Virginia Military Institute ("VMI"). Significant sources of revenue consist of contributions and investment return. Due to their shared purpose, the Agencies have elected to present their financial statements on a combined basis. All significant interagency accounts and transactions have been eliminated in combination. The individual organizations comprising the Agencies and their purposes are as follows:

The VMI Alumni Association
The purpose of The VMI Alumni Association is to organize the alumni of VMI into one general body.

VMI Foundation, Incorporated
The purposes of the VMI Foundation, Incorporated are to solicit and to accept various funds and to disburse such funds, or income earned from those funds, for the advancement of VMI and the Alumni Association.

VMI Development Board, Incorporated
The purposes of the VMI Development Board, Incorporated are to support VMI by coordinating development and fundraising efforts conducted on behalf of VMI Alumni and other donors.

VMI Keydet Club, Incorporated
The purposes of the VMI Keydet Club, Incorporated are to support, strengthen, and develop the intercollegiate athletic program at VMI.

Contributions receivable

Contributions receivable consist of the following:

	2010
Unconditional promises to give	$ 13,867,196
Charitable trust held by others	165,499
Total contributions receivable	14,032,695
Less: current portion	(6,459,408)
Noncurrent contributions receivable	$ 7,573,287
Gross amounts expected to be collected in:	
Less than one year	$ 7,391,311
One to five years	7,918,110
More than five years	2,124,392
	17,433,813
Less:	
Discount net present value at 3% - 6%	(1,674,286)
Allowance for uncollectible contributions	(1,726,832)
	$ 14,032,695

The distribution of contributions receivable for each class of net assets as of 30 June is as follows:

Temporarily restricted	$ 10,539,038
Permanently restricted	3,493,657
	$ 14,032,695

At 30 June 2010, the Agencies had also received bequest and other intentions of approximately $97.0 million. These intentions to give are not recognized as assets and, if they are received, they will generally be restricted for specific purposes stipulated by the donors.

For the year ended 30 June 2010 approximately 40% of the contributions receivable balance was from four donors.

Investments held by trustees

The Agencies participate in a combined investment fund (the "Fund") controlled by the VMI Investment Committee, a committee comprised of representatives from each agency. BNY Mellon, N.A. serves as custodian for the Fund's assets. The Fund's investments consist of the following:

	2010	
Equities	$ 127,686,965	50.8%
Hedge funds	67,793,187	27.0%
Fixed income	38,078,226	15.2%
Commodities	6,885,891	2.8%
Cash and cash equivalents	5,343,886	2.1%
Private bonds	4,092,738	1.6%
Private equities	1,338,133	0.5%
	251,219,026	100.0%
Less: amount payable for securities purchased and unrealized depreciation on short sales, net	(1,866,170)	
	$ 249,352,856	

These investments, which comprise the majority of the Agencies' assets, are subject to market risk. However, the Agencies' investment funds are managed by a number of investment managers, which limits the amount of risk in any one fund. The Agencies' Investment Committee establishes investment guidelines and performance standards which further reduce its exposure to market risk.

Investments held by trustees activity is reflected in the table below:

Investments held by trustees	2010
Investments, beginning	$ 219,033,145
Investments returns:	
Dividends and interest	4,128,481
Net realized and unrealized gains (losses)	28,346,914
Less: investment fees	(1,875,684)
	30,599,711
Net receipts (disbursements) from Mellon account used to fund operations	(280,000)
Investment, ending	$ 249,352,856

Endowment Funds

The Agencies employ a total return spending policy that establishes the amount of investment return that is available to support current needs and restricted purposes. This policy is designed to insulate program spending from capital market fluctuations and increase the amount of return that is reinvested in the corpus of the fund in order to enhance its long-term value. For the year ended 30 June 2010, the Board-approved spending formula for the endowment provided for an annual spending rate of 4.8% of the average of the prior twelve quarters' December 31 market values adjusting these market values upward to reflect subsequent receipt of gifts, or downward to reflect extraordinary withdrawals. If cash yield (interest and dividends) is less than the spending rate, realized gains can be used to make up the deficiency. Any income in excess of the spending rate is to be reinvested in the endowment. The primary investment objective is long-term capital appreciation and total return. The Agencies utilize diversified investment classes that provide the opportunity to achieve the return objective without exposing the funds to unnecessary risk.

VMI Investment Holdings, LLC

On 29 April 2008, VMI Investment Holdings, LLC (LLC) was formed to manage the investments held by trustees. On 1 June 2009, all investments held by trustees and for which BNY Mellon, N.A. serves as custodian were transferred to the LLC. The Foundation is the sole member of the LLC, and acts as an intermediary between the LLC and the other agencies. As stated in the Deposit and Management Agreement, the LLC will operate the unitized investment pool and issue a number of units in the pool to each depositor based on the amount of its deposit divided by the then unit value. Each depositor is entitled to its pro rata share of the value, taking into account aggregate investment returns. Deposits to and withdrawals from the pool by the other agencies will be made through the Foundation. A separate board of directors was established to manage the LLC.

Investments, Other

Investments, other, consist of the following:

	2010			
	Held by Agent	Held by Foundation	Held in Irrevocable Trusts*	Total at Fair Value**
Equities	$ 1,341,904	$ 9	$ 5,298,495	$ 6,640,408
Fixed income	19,570	5,891	5,453,439	5,478,900
Real estate	-	1,907,770	-	1,907,770
Cash and cash equivalents	29,112	783	227,392	257,287
Limited partnerships	4,754	17,128	-	21,882
	$ 1,395,340	$ 1,931,581	$ 10,979,326	$ 14,306,247

*Investments held in irrevocable trusts are not available for use until the occurrence of a future event as noted in the applicable trust agreements.

**For certain components of these investments, primarily real estate, limited partnerships, and common stocks of closely held companies, where fair values were not readily determinable, cost was used.

Bonds Payable

Bonds payable consists of the following:

	2010
Variable Rate Educational Facilities Revenue Bonds, Series 2006, payable in varying installments from $1,080,000 to $2,770,000, commencing 2012 through 2036. Interest payments commenced August 2006, rate is variable and averaged .2% during the year ended June 30, 2010. Interest is subject to an interest rate swap agreement which requires a fixed rate payment by the Agencies of 3.42% on $30,000,000 of the debt. Collateralized by a $45.4 million letter of credit.	$ 45,000,000
Mark-to-market estimate of bank swap transaction related to Industrial Development Authority Bonds	2,372,462
	$ 47,372,462

Debt matures as follows for future years ending 30 June:

Year ending 30 June:	
2011	$ -
2012	1,080,000
2013	1,125,000
2014	1,170,000
2015	1,215,000
Thereafter	40,410,000
Mark-to-market on interest rate swap	2,372,462
	$ 47,372,462

The Agencies entered into an interest rate swap agreement in May 2006. The swap agreement has a notational amount of $30,000,000 that effectively converts the variable rate based payments on $30,000,000 of bond debt to a fixed rate interest payment at 3.92780%. This swap was effective beginning 1 August 2006 and expires 1 August 2013. Terms of the swap were revised effective 1 April 2008 including a change in the fixed rate payment to 3.42%.

Subsequent Events

Effective 15 July 2010, the Industrial Development Authority of the City of Lexington, Virginia approved a request by the Agencies to remarket Variable Rate Educational Facilities Revenue Bonds, Series 2006. This remarketing superseded the original issuance, dated 13 July 2006. The bonds were initially issued in a single series bearing interest at a variable rate. The bonds were remarketed at a premium of $2,525,000, net of expenses. The bonds were remarketed in three series, Series 2006A-1 ($5,000,000) and 2006A-2 ($5,000,000), 2006B ($10,000,000), and 2006C ($22,475,000), and interest was converted to a fixed rate on each series. Series 2006A-1 bears interest of 4.25%, the remainder each bear interest at 5.00%. Interest will accrue at these rates and will be payable commencing on 1 December 2010, and each June 1 and December 1 thereafter. The first principal payment, of $10,000,000, is due in 2021. Upon this conversion, the bonds are no longer collateralized by any credit or liquidity facility, nor are the bonds collateralized by any of the Agencies' assets.

On 13 August 2010, the Agencies entered into a promissory note in the amount of $2,500,000. The proceeds of the note will be used to terminate the interest swap agreement in place at 30 June 2010. Interest on the note accrues at the 1-month London Interbank Offered Rate (LIBOR) plus .85%. Monthly payments commence 30 September 2010, all principal and accrued interest is payable on 13 August 2013. As of the date of these financial statements, the interest rate swap agreement has not yet been terminated.

NOTE 19: COMPONENT UNITS

Condensed financial statements for the component units of the Institute are as follows:

CONDENSED STATEMENTS OF NET ASSETS As of 30 June 2010	VMI Research Laboratories Inc.	VMI Alumni Agencies	TOTAL
Assets:			
Current assets	$ 555,036	$ 16,425,998	$ 16,981,034
Noncurrent assets	402,128	276,257,073	276,659,201
Total assets	957,164	292,683,071	293,640,235
Liabilities:			
Current liabilities	97,614	1,432,421	1,530,035
Noncurrent liabilities	88,555	51,343,223	51,431,778
Total liabilities	186,169	52,775,644	52,961,813
Net Assets:			
Unrestricted	713,408	44,599,331	45,312,739
Temporarily restricted	47,587	92,443,554	92,491,141
Permanently restricted	10,000	102,864,542	102,874,542
Total net assets	770,995	239,907,427	240,678,422
Total net assets and liabilities	$ 957,164	$ 292,683,071	$ 293,640,235

CONDENSED STATEMENTS OF REVENUES EXPENSES AND CHANGES IN NET ASSETS As of 30 June 2010	VMI Research Laboratories Inc.	VMI Alumni Agencies	TOTAL
Total revenues	$ 1,014,091	$ 18,002,058	$ 19,016,149
Total expenses	(700,598)	(23,976,747)	(24,677,345)
Total net realized and unrealized gains on investments	-	29,871,408	29,871,408
Total change in net assets	313,493	23,896,719	24,210,212
Total beginning net assets	457,502	216,010,708	216,468,210
Total ending net assets	$ 770,995	$ 239,907,427	$ 240,678,422

NOTE 20: SUBSEQUENT EVENTS

In November 2010, the Institute signed a promissory note with the Virginia College Building Authority (VCBA) in order to participate in the Educational Facilities Revenue and Refunding Bonds, Series 2010A-1, Series 2010A-2, and Series 2010B under the Public Higher Education Financing Program. The Institute will receive $825,000 of the tax exempt Series 2010A-1 proceeds and $2,025,000 of the Build America Bonds Series 2010A-2 proceeds to construct the South Institute Hill Parking area. Payments on this portion of the note will be made semi-annually, with interest rates ranging from 3.75 to 5.50%. Thirty five percent (35%) of the interest to be paid on the Build America Bonds proceeds is to be paid by the Federal government. The Institute will also receive $1,205,000 of the Series 2010B proceeds to refund a portion of the 9(d) Series 2002A and 2007B debt for Cocke Hall and JM Hall. Payments on this portion of the note will be made semi-annually with a 5.00% interest rate. The note will be paid from auxiliary reserve funds which consist predominantly of cadet fees. The final payment will be due in 2030.

Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

April 25, 2011

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable Charles J. Colgan
Chairman, Joint Legislative Audit
and Review Commission

Board of Visitors
Virginia Military Institute

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the business-type activities and aggregate discretely presented component units of the **Virginia Military Institute**, a component unit of the Commonwealth of Virginia, as of and for the year ended June 30, 2010, which collectively comprise the Virginia Military Institute's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Virginia Military Institute'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 component units of the Virginia Military Institute, which are discussed in Note 1. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the component units of the Virginia Military Institute is based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the component units of the Virginia Military Institute that were audited by other auditors upon whose reports we are relying were audited in accordance with auditing standards generally accepted in the United States of America, but not in accordance with Government Auditing Standards. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

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 financial position of the business-type activities and aggregate discretely presented component units of the Virginia Military Institute as of June 30, 2010, 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 Management's Discussion and Analysis on pages one through eight is not a required part of the basic financial statements, but is supplementary information required by the 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.

In accordance with Government Auditing Standards, we have also issued our report dated April 25, 2011 on our consideration of the Virginia Military Institute's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Walter J. Kucharski

AUDITOR OF PUBLIC ACCOUNTS

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