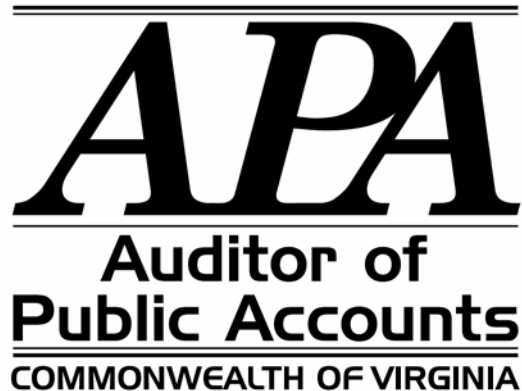


VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2005**



AUDIT SUMMARY

Our audit of the Virginia Commercial Space Flight Authority for the year ended June 30, 2005, found:

- the accompanying financial statements present fairly, in all material respects, the Authority's financial position as of June 30, 2005, and the results of operations and cash flows for the year then ended, in conformity with generally accepted accounting principles;
- no material weaknesses in internal control over financial reporting; and
- no instances of noncompliance with laws and regulations that are required to be reported.

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AUTHORITY OFFICIALS

MANAGEMENT'S DISCUSSION AND ANALYSIS **(unaudited)**

The management of the Virginia Commercial Space Flight Authority (the Authority) offers readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended June 30, 2005. We encourage readers to consider the information presented here in conjunction with the financial statements and accompanying notes.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement 34, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments*, which established new financial reporting requirements. As a related organization of the Commonwealth of Virginia, the Authority implemented these reporting requirements for its fiscal year ended June 30, 2003.

Summary of Organization and Business

The Authority was established by Chapter 758 of the 1995 Acts of Assembly and operates as an independent agency in accordance with the provisions of Chapter 29.1 of Title 9 of the Code of Virginia. The Authority was created to disseminate knowledge pertaining to scientific and technological research and development among public and private entities including, but not limited to, knowledge in the area of commercial space flight, and to promote industrial and economic development. A Board of Directors, composed of 12 members, manages the Authority.

The Authority is considered a related organization of the Commonwealth of Virginia. Organizations for which a primary government is accountable because that government appoints a majority of the Board, but is not financially accountable, are considered related organizations.

OVERVIEW OF ANNUAL FINANCIAL REPORT

The Management's Discussion and Analysis (MD&A) serves as an introduction to the basic financial statements prepared by the Authority. The MD&A represents management's examination and analysis of the financial performance of the Authority. The financial statements of the Authority are presented using the accrual method of accounting.

The financial statements consist of the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Fund Net Assets; and the Statement of Cash Flows. The following analysis discusses elements from these statements, as well as an overview of the Authority's activities.

Statement of Net Assets

The Statement of Net Assets presents the Authority's assets, liabilities, and net assets as of the end of the fiscal year. The purpose of this statement is to present readers a fiscal snapshot at June 30, 2005. From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the Authority's operations. They are also able to determine how much the Authority owes vendors and creditors.

	<u>2005</u>	<u>2004</u>	<u>Change</u>
Assets:			
Current assets	\$ 562,059	\$ 593,077	\$ (31,018)
Capital assets, net of accumulated depreciation	<u>1,603,570</u>	<u>1,720,101</u>	<u>(116,531)</u>
Total assets	<u>2,165,629</u>	<u>2,313,178</u>	<u>(147,549)</u>
Liabilities:			
Total current liabilities	<u>361,130</u>	<u>409,287</u>	<u>(48,157)</u>
Net assets:			
Invested in capital assets	1,603,570	1,720,101	(116,531)
Unrestricted	<u>200,929</u>	<u>183,790</u>	<u>17,139</u>
Total net assets	<u>\$1,804,499</u>	<u>\$1,903,891</u>	<u>\$ (99,392)</u>

The decrease in current assets of \$31,018 is primarily associated with a decrease in accounts receivable of \$57,475 and a corresponding increase in cash balances of \$24,070. The decrease in accounts receivable is primarily related to activity under a contract with the National Aeronautics and Space Administration associated with the development of infrastructure and launch support capabilities as discussed further under Significant Events. The decrease in capital assets of \$116,531 is a result of depreciation expense charged against operations.

The decrease in current liabilities of \$48,157 is primarily associated with a decrease in accounts payable to vendors of \$32,886 and amounts due to the Old Dominion University Research Foundation of \$17,197 associated with funds advanced under grants and contracts on behalf of the Authority. The increase in unrestricted net assets of \$17,139 is a result of the net loss for the fiscal year exclusive of the depreciation charges associated with the capital assets.

For more detailed information see the accompanying Statement of Net Assets.

Statement of Revenues, Expenses, and Changes in Fund Net Assets

The Statement of Revenues, Expenses, and Changes in Fund Net Assets presents a summary of revenue and expense activity, which resulted in the change from beginning to ending net assets. The purpose of this statement is to present the Authority's operating and nonoperating revenues recognized and expenses incurred and any other revenues, expenses, gains, and losses.

Operating expenses generally represent the cost of overall administration of the Authority and depreciation of its capital assets. Nonoperating revenues and expenses generally relate to funds received from federal cooperative agreements associated with the development of space launch capabilities at the Wallops Flight Facility located on the Eastern Shore of Virginia.

The following schedule compares the revenues, expenses, and net assets for the current and previous fiscal year.

	<u>2005</u>	<u>2004</u>	<u>Change</u>
Total operating revenues	\$ -	\$ -	\$ -
Total operating expenses	<u>318,574</u>	<u>385,496</u>	<u>(66,922)</u>
Net operating expense	(318,574)	(385,496)	66,922
Net nonoperating revenue	<u>219,182</u>	<u>163,475</u>	<u>55,707</u>
Net income/(loss)	(99,392)	(222,021)	122,629
Total net assets – Beginning of year	<u>1,903,891</u>	<u>2,125,912</u>	<u>(222,021)</u>
Total net assets – End of year	<u>\$1,804,499</u>	<u>\$1,903,891</u>	<u>\$ (99,392)</u>

Operating expenses decreased as the Authority's activities and administrative personnel efforts increased in the nonoperating functions associated with the development of space launch capabilities and other related activities. For more detailed information see the accompanying Statement of Revenues, Expenses, and Changes in Fund Net Assets.

Statement of Cash Flows

The Statement of Cash Flows provides relevant information that aids in the assessment of the Authority's ability to generate cash to meet present and future obligations and detailed information reflecting the Authority's sources and uses of cash during the fiscal year. Cash flows from operating activities reflect the uses to support the essential mission and administration of the Authority. The primary uses are payments to employees, including salaries, wages, and fringe benefits and payments to suppliers. Cash flows from noncapital financing activities reflect the nonoperating sources and uses of cash. The primary sources are sponsored research of \$895,510 associated with the infrastructure development of the launch pad and launch capability studies and \$100,000 from state appropriations. The primary use is to support the sponsored research tasks and cash requirements of operations.

	<u>2005</u>	<u>2004</u>	<u>Change</u>
Cash flows from operating activities	\$(227,752)	\$(240,108)	\$ 12,356
Cash flows from noncapital financing activities	<u>251,822</u>	<u>291,737</u>	<u>(39,915)</u>
Net change in cash and cash equivalents	<u>\$ 24,070</u>	<u>\$ 51,629</u>	<u>\$(27,559)</u>

Capital Assets and Long-Term Debt

The Authority's capital assets consist primarily of infrastructure development associated with the construction of Launch Pad 0-B at the Wallops Flight Facility on the Eastern Shore of Virginia. In fiscal year 2005, significant modifications were made to Launch Pad 0-B infrastructure to make it ready to support the Air Force *Minotaur* family of launch vehicles. For more detailed information related to capital assets, see the Notes to Financial Statements. The Authority currently has no long-term debt obligations.

Significant Events

On August 19, 2004, the Authority was awarded a five year task ordering contract by the U.S. Air Force (USAF) with a ceiling value of \$49 million for the support of USAF from facilities owned by the

Authority. This USAF contract will allow the USAF to procure spaceport services and facilities usage for the launch of orbital and sub-orbital launches of small to mid-class payloads from Authority-owned and -leased facilities. As the initial task on the contract, the Authority performed the “Accelerated Launch and Peacekeeper Launch Vehicle Capability Study” in September 2004. Depending on USAF’s need for small satellite launches and the continued availability federal funding, it is expected that this multi-year task ordering contract will provide nonuniform, operating revenues for Authority operations and maintenance.

In early June 2005, a Pathfinder Mission was successfully conducted on Launch Pad 0-B to verify the readiness of the Authority’s facility to support the launch of the USAF NFIRE Mission on a Minotaur II launch vehicle. The USAF NFIRE launch is currently scheduled for September 2006. This launch had previously been scheduled for June 2004, but delays in satellite development by USAF caused delays until the current date. This launch mission is being funded by USAF via the multi-year task ordering contract with the Authority and NASA to provide launch services and facilities for government launches put into place in July 2003.

Maryland and Virginia continue to cooperate in the administration of the Mid-Atlantic Regional Spaceport (MARS) per the Memorandum of Agreement (MOA) between the Governors of Virginia and Maryland signed in July 2003. MARS, the commercial space flight center at Wallops Island, Virginia, is owned by the Authority. Under this agreement, Maryland provided a \$150,000 contribution for fiscal year 2005 for operations of the Authority. In May 2005, Maryland provided an additional \$150,000 contribution for fiscal year 2006 operations. Representatives of Virginia and Maryland are actively engaged in the promotion of MARS and its support to the Authority in carrying out its legislated purposes.

The Authority continues to be a significant participant in the Defense Advanced Research Projects Agency (DARPA) Force Application and Launch from the Continental U.S. (FALCON) Small Launch Vehicle development program. In fiscal year 2005, the Authority provided support to the four DARPA-selected development teams that are under contract to develop a new, low cost, responsive small launch vehicle. The DARPA FALCON program is expected to down select in September 2005 to two contractors to continue development of the FALCON small launch vehicle. The Authority expects to conduct the DARPA FALCON test and demonstration flights from its facilities in fiscal year 2008.

These various sources of funds, the federal contracts, the commercial sub-contracts, the \$100,000 Commonwealth of Virginia appropriation, and the \$150,000 Maryland contribution, along with existing cash assets, are expected to meet the Authority’s fiscal year 2006 operating budget with a small residual being applied to operating reserves at the close of fiscal year 2006. Stabilizing funding from nonoperating sources will continue to be required to provide the operating and maintenance reserves necessary to capture the nonuniform but sizable revenues from the anticipated federal launches over the next several years.

VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY
STATEMENT OF NET ASSETS
As of June 30, 2005

ASSETS	
Current assets:	
Cash	\$ 304,031
Accounts receivable	230,692
Other assets	<u>27,336</u>
Total current assets	<u>562,059</u>
Depreciable capital assets:	
Improvements other than buildings	2,104,849
Land improvements	125,000
Office furniture	15,505
Computer equipment	33,103
Less: Accumulated depreciation	<u>(674,887)</u>
Total depreciable capital assets	<u>1,603,570</u>
Total assets	<u>2,165,629</u>
LIABILITIES	
Current liabilities:	
Accounts payable and accrued expenses	41,335
Deferred revenue	155,768
Due to Old Dominion University Research Foundation	<u>164,027</u>
Total liabilities	<u>361,130</u>
NET ASSETS	
Invested in capital assets	1,603,570
Unrestricted	<u>200,929</u>
Total net assets	<u><u>\$ 1,804,499</u></u>

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

VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
For the Year Ended June 30, 2005

Operating expenses:	
Administration	\$ 173,762
Depreciation	116,531
Other	<u>28,281</u>
Total operating expenses	<u>318,574</u>
Operating loss	<u>(318,574)</u>
Nonoperating revenues/(expenses):	
State appropriation	100,000
Federal grants	387,492
State grants	137,690
Private grants	99,961
Pass-through grant	220,530
Expenses related to grants	<u>(726,491)</u>
Total nonoperating revenues	<u>219,182</u>
Net loss	(99,392)
Net assets - July 1, 2004	<u>1,903,891</u>
Net assets - June 30, 2005	<u><u>\$ 1,804,499</u></u>

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

VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2005

Cash flows from operating activities:	
Cash paid to employees	\$ (93,824)
Cash paid to suppliers	<u>(133,928)</u>
Net cash provided by/(used in) operating activities	<u>(227,752)</u>
Cash flows from noncapital financing activities:	
Cash received from state appropriation	100,000
Cash received for sponsored research	895,510
Cash payments for sponsored research	<u>(743,688)</u>
Net cash provided by/(used in) noncapital financing activities	<u>251,822</u>
Net increase in cash and cash equivalents	24,070
Cash and cash equivalents - July 1, 2004	<u>279,961</u>
Cash and cash equivalents - June 30, 2005	<u><u>\$ 304,031</u></u>

RECONCILIATION OF NET INCOME TO NET CASH
PROVIDED BY OPERATING ACTIVITIES:

Net operating loss	\$ (318,574)
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	116,531
Changes in assets and liabilities:	
Increase in other assets	(2,387)
Increase in accounts payable	<u>(23,322)</u>
Net cash provided by/(used in) operating activities	<u><u>\$ (227,752)</u></u>

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

VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Virginia Commercial Space Flight Authority was established by Chapter 758 of the 1995 Acts of Assembly and operates as an independent agency in accordance with the provisions of Chapter 29.1 of Title 9 of the Code of Virginia. The Authority was created to disseminate knowledge pertaining to scientific and technological research and development among public and private entities including, but not limited to, knowledge in the area of commercial space flight, and to promote industrial and economic development. A Board of Directors, composed of 12 members, manages the Authority.

The Authority is considered a related organization of the Commonwealth of Virginia. Organizations for which a primary government is accountable because that government appoints a majority of the Board, but is not financially accountable, are considered related organizations.

B. Fund Accounting

The activities of the Authority are accounted for in an enterprise fund. The enterprise fund is used to account for governmental operations that are financed and operated in a manner similar to private business enterprises. Enterprise fund accounting is used where the intent of the governing body is that the costs of providing goods and services to the general public on a continuing basis, including depreciation, be financed or recovered primarily through user charges. All fund accounts of the Authority are presented in total on the financial statements.

The Authority's accounting policies conform with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), including all applicable 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 Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The Authority has the option to apply FASB pronouncement issued after November 30, 1989, unless FASB conflicts with GASB. The Authority has elected not to apply FASB pronouncements issued after the applicable date.

C. Basis of Accounting

The Authority's records are maintained on the accrual basis whereby revenues are recognized when earned and expenses are recognized when the liability is incurred.

D. Classification of Revenues and Expenses

The Authority presents its revenues and expenses as operating or non-operating based on the following criteria: Operating expenses generally represent the cost of the overall administration of the Authority and the depreciation of its capital assets. Nonoperating revenues and expenses generally relate to funds received from federal cooperative agreements associated with the development of space launch capabilities.

2. CASH

As of June 30, 2005, cash balances of \$304,031 were held by the Old Dominion University Research Foundation. The Foundation maintains its cash balances in depository accounts at financial institutions with deposits insured by FDIC.

3. CAPITAL ASSETS

The schedule below shows the breakdown of capital assets by category at June 30, 2005.

	<u>Balance at July 1, 2004</u>	<u>Acquired/ Increased</u>	<u>Deleted/ (Decreased)</u>	<u>Balance at June 30, 2005</u>
Improvements other than buildings	\$2,104,849	\$ -	\$ -	\$2,104,849
Land improvements	125,000	-	-	125,000
Office equipment	15,505	-	-	15,505
Computer equipment	<u>33,103</u>	<u>-</u>	<u>-</u>	<u>33,103</u>
Total at historical cost	<u>2,278,457</u>	<u>-</u>	<u>-</u>	<u>2,278,457</u>
Less accumulated depreciation:				
Improvements other than buildings	473,591	105,242	-	578,833
Land improvements	43,744	8,334	-	52,078
Office equipment	15,307	196	-	15,503
Computer equipment	<u>25,714</u>	<u>2,759</u>	<u>-</u>	<u>28,473</u>
Total accumulated depreciation	<u>558,356</u>	<u>116,531</u>	<u>-</u>	<u>674,887</u>
Capital assets, net	<u>\$1,720,101</u>	<u>\$(116,531)</u>	<u>\$ -</u>	<u>\$1,603,570</u>

Capital assets are generally defined by the Authority as assets with an initial cost of \$2,000 or more and an estimated useful life in excess of one year. Property, plant, and equipment of the Authority are stated at cost and at the time of acquisition are set up in a comprehensive fixed asset system. Depreciation of the cost of property, plant, and equipment is provided on a straight line basis over their estimated useful lives as follows:

Office equipment	7 years
Computer equipment	5 years
Land improvements	15 years
Improvements other than buildings	20 years

4. DUE TO OLD DOMINION UNIVERSITY RESEARCH FOUNDATION

The Old Dominion University Research Foundation has advanced funds out of its reserves to finance various sponsored research programs for the Authority. The Authority will refund these advances as funds are received from grantors.

5. RELATED PARTY

The Authority has entered into a limited liability corporation agreement with DynSpace, LLC. This agreement will create a joint venture called Flight Center One. The finalization of the agreement is incumbent on execution of a facilities lease, which will be executed when commercial business opportunities warrant the need for the facility.

6. RETIREMENT AND PENSION SYSTEMS

Certain employees of the Authority participate in a defined benefit pension plan administered by the Virginia Retirement System (VRS) through Old Dominion University. The VRS also administers life insurance and health-related plans for retired employees. Information relating to these plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report (CAFR). Other regular full-time employees receive fixed contributions of 11 percent, which can be invested through an Old Dominion University Research Foundation-sponsored 403(b) Tax Sheltered Annuity Plan or received as taxable income. The Commonwealth, not the Authority, has overall responsibility for contributions to these plans.

7. VIRGINIA LOCAL GOVERNMENT RISK MANAGEMENT PLAN

The Authority is exposed to various risks of loss related to torts; theft, damage, or destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The employees, directors, and agents of the Authority were insured for these risks under a self-insured liability plan, VaRISK 2, administered by the Commonwealth of Virginia's Department of Treasury, Division of Risk Management, with liability limits of \$1 million for each occurrence.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

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

November 4, 2005

The Honorable Mark R. Warner
Governor of Virginia

The Honorable Lacey E. Putney
Chairman, Joint Legislative Audit
and Review Commission

Board of Directors
Virginia Commercial Space Flight Authority

We have audited the accounts and records of the **Virginia Commercial Space Flight Authority** for the year ended June 30, 2005, and submit herewith our complete reports on financial statements and on compliance and internal control over financial reporting.

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of the Authority as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2005, and the changes in its net assets and its cash flows 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 1 through 4 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.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

Internal Control over Financial Reporting

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

Compliance and Other Matters

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

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

EXIT CONFERENCE

We discussed this report with management at an exit conference held on November 23, 2005.

AUDITOR OF PUBLIC ACCOUNTS

SW/kva

VIRGINIA COMMERCIAL SPACE FLIGHT AUTHORITY

BOARD MEMBERS

Michael Schewel
Chairman

Frederick B. Cooke, Jr.
Vice-Chairman

Mark E. Bitterman
Vincent C. Boles
Brian Darmody
Eugene Huang
Peter Jobse

Robert H. Meurer
Frank V. Moore
Roseann Runte
Thomas J. Savage, Jr.
Elmer Travis

Billie M. Reed
Executive Director

Linda E. Gentry
Treasurer