

MANAGEMENT’S DISCUSSION AND ANALYSIS

The State of Florida (the State)’s general purpose external financial statements are presented within the financial section of this Comprehensive Annual Financial Report (CAFR). The components of the general purpose external financial statements include Management’s Discussion and Analysis (MD&A), Basic Financial Statements, and Other Required Supplementary Information (RSI). The MD&A, a component of RSI, introduces the basic financial statements and provides an analytical overview of the State’s financial activities.

Overview of the Financial Statements

The State’s basic financial statements comprise the following elements:

Government-wide Financial Statements

Government-wide financial statements provide both long-term and short-term information about the State's overall financial condition. Changes in the State’s financial position may be measured over time by increases and decreases in the Statement of Net Assets. Information on how the State’s net assets changed during the fiscal year is presented in the Statement of Activities. Financial information for the State’s component units is also presented.

Fund Financial Statements

Fund financial statements focus on individual parts of the State, reporting the State's operations in more detail than the government-wide financial statements. Fund financial statements include the statements for governmental, proprietary, and fiduciary funds.

Notes to the Financial Statements

Notes to the financial statements provide additional information that is essential to the full understanding of the data provided in the government-wide and fund financial statements. Refer to Note 1 to the financial statements for more detailed information on the elements of the financial statements. Table 1 below summarizes the major features of the basic financial statements.

Table 1: Major Features of the Basic Financial Statements

	Government-wide Financial Statements	Fund Financial Statements		
		Governmental Funds	Proprietary Funds	Fiduciary Funds
Scope	Entire State government (except fiduciary funds) and the State’s component units	Activities of the State that are not proprietary or fiduciary	Activities of the State that are operated similar to private businesses	Instances in which the State is the trustee or agent for someone else’s resources
Required financial statements	<ul style="list-style-type: none"> • Statement of net assets • Statement of activities 	<ul style="list-style-type: none"> • Balance sheet • Statement of revenues, expenditures, and changes in fund balances 	<ul style="list-style-type: none"> • Statement of net assets • Statement of revenues, expenses, and changes in net assets • Statement of cash flows 	<ul style="list-style-type: none"> • Statement of fiduciary net assets • Statement of changes in fiduciary net assets
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus	Accrual accounting and economic resources focus
Type of asset/liability information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included	All assets and liabilities, both financial and capital, and short-term and long-term	All assets and liabilities, both short-term and long-term
Type of inflow/outflow information	All revenues and expenses during the year, regardless of when cash is received or paid	<ul style="list-style-type: none"> • Revenues for which cash is received during or soon after the end of the year • Expenditures when goods or services have been received and payment is due during the year or soon thereafter 	All revenues and expenses during the year, regardless of when cash is received or paid	All revenues and expenses during the year, regardless of when cash is received or paid

Condensed Financial Information

Condensed Statement of Net Assets

The largest component (\$43.5 billion) of the State's net assets as of June 30, 2003, reflects its investment in capital assets (e.g. land, infrastructure, buildings, equipment, and others), less any related debt outstanding that was needed to acquire or construct the assets. The State uses these capital assets to provide services to the citizens and businesses in the State; consequently, these net assets are not available for future spending. Restricted net assets are the next largest component, totaling \$14.6 billion as of June 30, 2003. Restricted net assets represent resources that are subject to external restrictions, constitutional provisions, or enabling legislation on how they can be used.

Governmental activities reflect a negative unrestricted net asset balance of \$10.1 billion at June 30, 2003. This deficit is primarily the result of education-related bonds in which the State is responsible for the debt, but the local school districts own the capital assets. Because the State does not own these capital assets, the bonded debt is not netted on the line item "invested in capital assets, net of related debt." Instead, this bonded debt is netted with "unrestricted net assets." Education-related bonds include State Board of Education Capital Outlay Bonds, Public Education Capital Outlay (PECO) Bonds, and Lottery Education Bonds, which have a total ending balance at June 30, 2003, of \$11 billion. The State has an additional \$300 million in bonded debt in which the State does not own the related capital assets, including some Road and Bridge Bonds and Pollution Control Bonds. The resources related to the payment of this debt will be provided from future revenue sources. If these bonds were removed, the adjusted unrestricted net assets for governmental activities would be \$1.2 billion.

Business-type activities reflect a positive unrestricted net asset balance of \$228 million at June 30, 2003.

Table 2 below presents the State's condensed statement of net assets as of June 30, 2003, and 2002, derived from the government-wide Statement of Net Assets.

**Table 2: Condensed Statement of Net Assets
As of June 30
(in millions)**

	Governmental Activities		Business-type Activities		Total Primary Government	
	2003	2002	2003	2002	2003	2002
Current and other assets	\$ 18,711	\$ 17,232	\$ 12,371	\$ 11,393	\$ 31,082	\$ 28,625
Capital assets	44,010	41,834	4,861	4,619	48,871	46,453
Total assets	<u>62,721</u>	<u>59,066</u>	<u>17,232</u>	<u>16,012</u>	<u>79,953</u>	<u>75,078</u>
Other liabilities	6,156	6,745	3,532	2,920	9,688	9,665
Noncurrent liabilities	18,527	17,165	3,530	3,703	22,057	20,868
Total liabilities	<u>24,683</u>	<u>23,910</u>	<u>7,062</u>	<u>6,623</u>	<u>31,745</u>	<u>30,533</u>
Net assets:						
Invested in capital assets, net of related debt	40,382	38,329	3,145	3,061	43,527	41,390
Restricted	7,763	7,117	6,797	6,150	14,560	13,267
Unrestricted	<u>(10,107)</u>	<u>(10,290)</u>	<u>228</u>	<u>178</u>	<u>(9,879)</u>	<u>(10,112)</u>
Total net assets	<u>\$ 38,038</u>	<u>\$ 35,156</u>	<u>\$ 10,170</u>	<u>\$ 9,389</u>	<u>\$ 48,208</u>	<u>\$ 44,545</u>

Condensed Statement of Activities

Table 3 presents the State's condensed statement of activities for the fiscal year ended June 30, 2003, and 2002, as derived from the government-wide Statement of Activities. Over time, increases and decreases in net assets measure whether the State's financial position is improving or deteriorating. During the fiscal year, the net assets (before the effects of prior period adjustments) of the governmental activities increased by \$2.1 billion or 6 percent, and the net assets (before the effects of prior period adjustments) of the business-type activities increased by \$676 million or 7.2 percent.

Table 3: Condensed Statement of Activities
For the Fiscal Year Ended June 30
(in millions)

	Governmental Activities		Business - type Activities		Total Primary Government		Total % Change 2002 to 2003
	2003	2002	2003	2002	2003	2002	
Revenues							
Program revenues							
Charges for services	\$ 4,279	\$ 4,421	\$ 5,481	\$ 4,740	\$ 9,760	\$ 9,161	6.5%
Operating grants & contributions	13,538	12,159	395	184	13,933	12,343	12.9%
Capital grants & contributions	1,699	1,326	1	.....	1,700	1,326	28.2%
Total program revenues	19,516	17,906	5,877	4,924	25,393	22,830	11.2%
General revenues and payments							
Sales and use tax	15,561	15,601	.....	.....	15,561	15,601	-0.3%
Motor fuel tax	2,199	2,101	.....	.....	2,199	2,101	4.7%
Corporate income tax	1,228	1,210	.....	.....	1,228	1,210	1.5%
Documentary stamp tax	2,005	1,591	.....	.....	2,005	1,591	26.0%
Intangible tax	820	738	.....	.....	820	738	11.1%
Communication service tax	1,230	779	.....	.....	1,230	779	57.9%
Estate tax	559	745	.....	.....	559	745	-25.0%
Gross receipts utilities tax	424	527	.....	.....	424	527	-19.5%
Beverage and tobacco taxes	1,002	991	.....	.....	1,002	991	1.1%
Other taxes	1,348	1,156	.....	.....	1,348	1,156	16.6%
Interest	720	419	19	20	739	439	68.3%
Other revenues and payments	.....	114	.....	3	.....	117	-100.0%
Total general revenues and payments	27,096	25,972	19	23	27,115	25,995	4.3%
Total revenues	46,612	43,878	5,896	4,947	52,508	48,825	7.5%
Program expenses							
General government	6,273	6,499	.....	.....	6,273	6,499	-3.5%
Education	15,120	14,488	.....	.....	15,120	14,488	4.4%
Human services	16,639	14,973	.....	.....	16,639	14,973	11.1%
Criminal justice & corrections	3,103	3,066	.....	.....	3,103	3,066	1.2%
Natural resources & environment	1,945	1,738	.....	.....	1,945	1,738	11.9%
Transportation	2,398	2,071	.....	.....	2,398	2,071	15.8%
State courts	279	280	.....	.....	279	280	-0.4%
Turnpike	.....	.....	286	261	286	261	9.6%
Lottery	.....	.....	2,000	1,595	2,000	1,595	25.4%
Unemployment compensation	.....	.....	1,486	1,486	1,486	1,486	0.0%
State Board of Administration	.....	.....	33	41	33	41	-19.5%
Other	2	.....	157	158	159	158	0.6%
Total program expenses	45,759	43,115	3,962	3,541	49,721	46,656	6.6%
Excess (deficiency) before gain (loss) and transfers	853	763	1,934	1,406	2,787	2,169	
Gain (loss) on sale of capital assets	.....	.....	.....	1	.....	1	
Transfers	1,258	1,070	(1,258)	(1,070)	.....	.....
Change in net assets	2,111	1,833	676	337	2,787	2,170	
Beginning net assets	35,156	34,189	9,389	9,101	44,545	43,290	
Prior period adjustments	771	(866)	105	(49)	876	(915)	
Ending net assets	\$ 38,038	\$ 35,156	\$ 10,170	\$ 9,389	\$ 48,208	\$ 44,545	8.2%

Program Expenses and Revenues for Governmental Activities

Table 4 presents the net costs of governmental activities. Overall, program revenues were not sufficient to cover program expenses for governmental activities. The net costs of governmental activities were therefore supported by general revenues, mainly taxes. Program revenues as a percentage of program expenses increased from fiscal year 2001-02 to fiscal year 2002-03 in general government, education, and human services.

**Table 4: Net Costs of Governmental Activities
for the Fiscal Year Ended June 30
(in millions)**

State Programs	Program Expenses 2003	Less Program Revenues 2003	Net Program Costs (a)		Program Revenues as a Percentage of Program Expenses	
			2003	2002	2003	2002
General government	\$ 6,273	\$ 3,322	\$ 2,951	\$ 3,220	53.0%	50.5%
Education	15,120	2,215	12,905	12,615	14.6%	12.9%
Human services	16,639	10,940	5,699	5,332	65.7%	64.4%
Criminal justice & corrections	3,103	300	2,803	2,650	9.7%	13.6%
Natural resources & environment	1,945	743	1,202	960	38.2%	44.8%
Transportation	2,398	1,987	411	167	82.9%	91.9%
State courts	279	9	270	265	3.2%	5.4%
Other	2	.....	2	.....	0.0%	0.0%
Totals	<u>\$ 45,759</u>	<u>\$ 19,516</u>	<u>\$ 26,243</u>	<u>\$ 25,209</u>	<u>42.6%</u>	<u>41.5%</u>

(a) Net program costs are mainly supported by taxes.

Program Expenses and Revenues for Business-type Activities

Table 5 presents the net income and costs of business-type activities. With the exception of unemployment compensation, program revenues generated from business-type activities were more than sufficient to cover program expenses. The net costs of unemployment compensation were supported by fund reserves. With the exception of Lottery, program expenses as a percentage of program revenues decreased for all business-type programs from fiscal year 2001-02 to fiscal year 2002-03.

**Table 5: Net Income (Costs) of Business-type Activities
for the Fiscal Year Ended June 30
(in millions)**

State Programs	Program Revenues 2003	Less Program Expenses 2003	Net Program Income (Costs) (b)		Program Expenses as a Percentage of Program Revenues	
			2003	2002	2003	2002
Turnpike	\$ 541	\$ 286	\$ 255	\$ 217	52.9%	54.6%
Lottery	3,154	2,000	1,154	973	63.4%	62.1%
Unemployment compensation	1,218	1,486	(268)	(562)	122.0%	160.8%
State Board of Administration	633	33	600	592	5.2%	6.5%
Other	331	157	174	163	47.4%	49.2%
Totals	<u>\$ 5,877</u>	<u>\$ 3,962</u>	<u>\$ 1,915</u>	<u>\$ 1,383</u>	<u>67.4%</u>	<u>71.9%</u>

(a) Net program costs are supported by fund reserves.

Overall Analysis

Financial highlights for the State as a whole during the fiscal year ended June 30, 2003, include the following:

- The assets of the State exceeded its liabilities (net assets) at the close of the fiscal year by \$38 billion for governmental activities and by \$10.2 billion for business-type activities.
- The State's total net assets (before effects of prior period adjustments) increased during the year by \$2.7 billion. Net assets of governmental activities increased by \$2.1 billion, while net assets of business-type activities increased by \$676 million.

Fund Analysis

Funds that experienced significant changes during the fiscal year ended June 30, 2003, are as follows:

Governmental Funds

As of the close of the fiscal year, the State's governmental funds reported a combined ending fund balance of \$12.6 billion, with \$4.7 billion reported as unreserved fund balance and the remaining amount of \$7.9 billion reserved for specific purposes. See Note 1 to the financial statements for an explanation of the different types of reserve categories.

Public Education

Fund balance at June 30, 2003, totaled \$1.3 billion, which includes an increase of \$364 million before the effects of a prior period adjustment in the amount of \$669 million. The change in fund balance is primarily the result of a change in the method for reporting the remaining balances of capital outlay projects. The remaining balances are reported as fund balance reserved for fixed capital outlay items. The balances were previously reported as expenditures and liabilities (Refer to Note 13 to the financial statements).

Tax Collection and Administration

Fund balance at June 30, 2003, totaled \$348 million, an increase of \$77 million. The increase relates to an increase in documentary stamp tax collections due to low interest rates encouraging financing activities.

Employment Services

Fund balance at June 30, 2003, totaled \$292 million, an increase of \$74 million. The increase relates to an increased premium base for workers' compensation and special disability assessments.

Proprietary Funds

The State's proprietary funds reported net assets of \$10.4 billion, including \$10.2 billion for enterprise funds and \$239 million for internal service funds.

Lottery

Net assets at June 30, 2003, totaled \$353 million, an increase of \$118 million during the fiscal year. The increase primarily relates to an increase in the market value of restricted investments held to pay prize winners and investments purchased with cash collateral from security lending activities.

Unemployment Compensation

Net assets at June 30, 2003, totaled \$1.4 billion, which includes a decrease of \$274 million before the effects of a prior period adjustment in the amount of \$100 million. The \$274 million decrease primarily relates to payments associated with unemployment compensation claims exceeding program revenues by approximately \$268 million in 2003. Additionally, the ending net asset balance includes a prior period adjustment to report \$100 million for previously unreported receivables (Refer to Note 13 to the financial statements).

Budget Variances in the General Fund

As a result of changes during the fiscal year in the State's projected revenues, various appropriation revisions were made to the original budget. Refer to the budgetary comparison schedule for the General Fund in the Other RSI section of the CAFR for additional detail on budget variances.

Capital Asset and Long-term Debt Activity**Capital Asset Activity**

At June 30, 2003, the State reported \$44 billion in capital assets for governmental activities and \$4.9 billion in capital assets for business-type activities. Refer to Note 5 to the financial statements for additional information on capital assets and Note 7 to the financial statements for additional information on construction commitments.

Long-term Debt Activity

Section 11 of Article VII of the State Constitution authorizes the State to issue general obligation bonds and revenues bonds to finance or refinance the cost of state fixed capital outlay projects authorized by law. General obligation bonds are secured by the full faith and credit of the State and payable from the proceeds of various taxes. Revenue bonds are payable from funds that receive legally restricted revenues. The Division of Bond Finance of the State Board of Administration has the responsibility to issue all state bonds. During the past year, the State continued to maintain a high bond rating from Moody's Investors Services (Aa2), Standard and Poor's Corporation (AA+), and Fitch, Inc. (AA) on all State general obligation bonds.

The *State of Florida 2003 Debt Affordability Report*, prepared by the Division of Bond Finance, showed an increase in the State's benchmark debt ratio of debt service to revenue for net tax-supported debt from 5.82% for the fiscal year ended June 30, 2002, to 6.12% for the fiscal year ended June 30, 2003. The increase is due to additional debt issuance for capital outlay projects related to educational facilities, environmental purposes, and transportation. To obtain a copy of this report, contact the Division of Bond Finance, 1801 Hermitage Blvd., Suite 200, Tallahassee, Florida 32308, (850) 488-4782.

Refer to Notes 8, 9, and 10 to the financial statements and the Statistical and Economic Data section of the CAFR for additional information on the State's long-term debt and other liabilities.

Infrastructure

The State has elected to use the modified approach to account for its bridges and roadways included on the State Highway System. Under this approach, the Florida Department of Transportation (FDOT) has made the commitment to preserve and maintain these assets at levels established by the FDOT and approved by the Florida Legislature. No depreciation expense is reported for such assets, nor are amounts capitalized in connection with improvements that lengthen the lives of such assets, unless the improvements also increase their service potential. The FDOT maintains an inventory of these assets and performs periodic condition assessments to establish that the predetermined condition level is being maintained.

The condition assessments performed during fiscal year 2002-03 show that the condition of the roadway and bridges included on the State Highway System are being maintained at or near FDOT standards. These condition assessments were also consistent with condition assessments conducted during the last two years. In addition, the FDOT makes annual estimates of the amounts that must be expended to preserve and maintain the roadway and bridges included on the State Highway System at the predetermined condition levels. There were no significant differences from the estimated annual amount to preserve and maintain these assets compared with the actual amounts spent during the current period.

For further information on the FDOT's established condition standards, recent condition assessments, or other information on infrastructure reported on the modified approach, refer to the Other RSI section of this report.

Economic Conditions and Outlook

Florida's economy grew in fiscal year 2002-03 but at a slower rate than might be expected in an economic recovery. Even so, compared to the rest of the nation, Florida performed relatively better. While the U.S. experienced a decline in non-farm employment in fiscal year 2002-03, Florida posted positive growth, had a lower unemployment rate, and stronger income growth rate. This performance could be attributed to favorable natural, economic, and tax environments, and a growing population that fuels increased demand for goods and services.

A major element of Florida's economy is the construction sector. Because of low interest rates, housing starts spiked in fiscal year 2002-03. The strong performance of the housing market is expected to peak in fiscal year 2003-04. Total construction employment, which added 6,800 jobs in fiscal year 2002-03, is anticipated to create 13,400 more jobs in fiscal year 2003-04. Total residential construction expenditures increased 18.6 percent in fiscal year 2002-03 and are projected to rise 8.9 percent in fiscal year 2003-04. These represent a major stimulus to the economy as well as an increase to state revenue.

Florida has remained top ranked in the nation in total job growth and has the fastest job growth rate among the ten most populous states. Florida's non-farm employment growth grew 1.1 percent in fiscal year 2002-03, adding 81,600 jobs, led by gains in the construction, financial, government and services industries. Eighty four percent of the job increase in fiscal year 2002-03 was from services. With the strengthening economy, non-farm employment is anticipated to add 113,000 jobs in fiscal year 2003-04, pushing wages and salaries to rise 5.3 percent. The unemployment rate is anticipated to slightly decline from 5.36 percent in fiscal year 2002-03 to 5.20 percent in fiscal year 2003-04.

Population has been a major source of increased economic activity in Florida, growing by 381,000 in fiscal year 2002-03. An estimated 369,000 will be added to the state's population in fiscal year 2003-04. Over the next ten years, population growth is estimated to reach 3.3 million. Population growth has been a major driver of Florida's sustained expansion as the demand for housing, durable and non-durable goods and other services continues to increase. The projected growth in population will continue to fuel the state's economic expansion.

Florida's economy has again shown its strength and resilience. While most states have been experiencing major economic problems because of the sluggish U.S. and world economy, Florida's economy has steadily been moving up as evidenced by the strength in its labor market. Although the long-term growth is projected to be slower than previously anticipated, Florida's economic fundamentals remain strong. Such strength should provide impetus for the State's economy to achieve a more sustained growth.

Contact the State's Financial Management

Questions about this report or requests for additional financial information may be addressed to:

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