NEW JERSEY

COMPREHENSIVE ANNUAL FINANCIAL REPORT FISCAL YEAR ENDED JUNE 30, 1997

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STATE OF NEW JERSEY
COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR THE FISCAL YEAR ENDING JUNE 30, 1997
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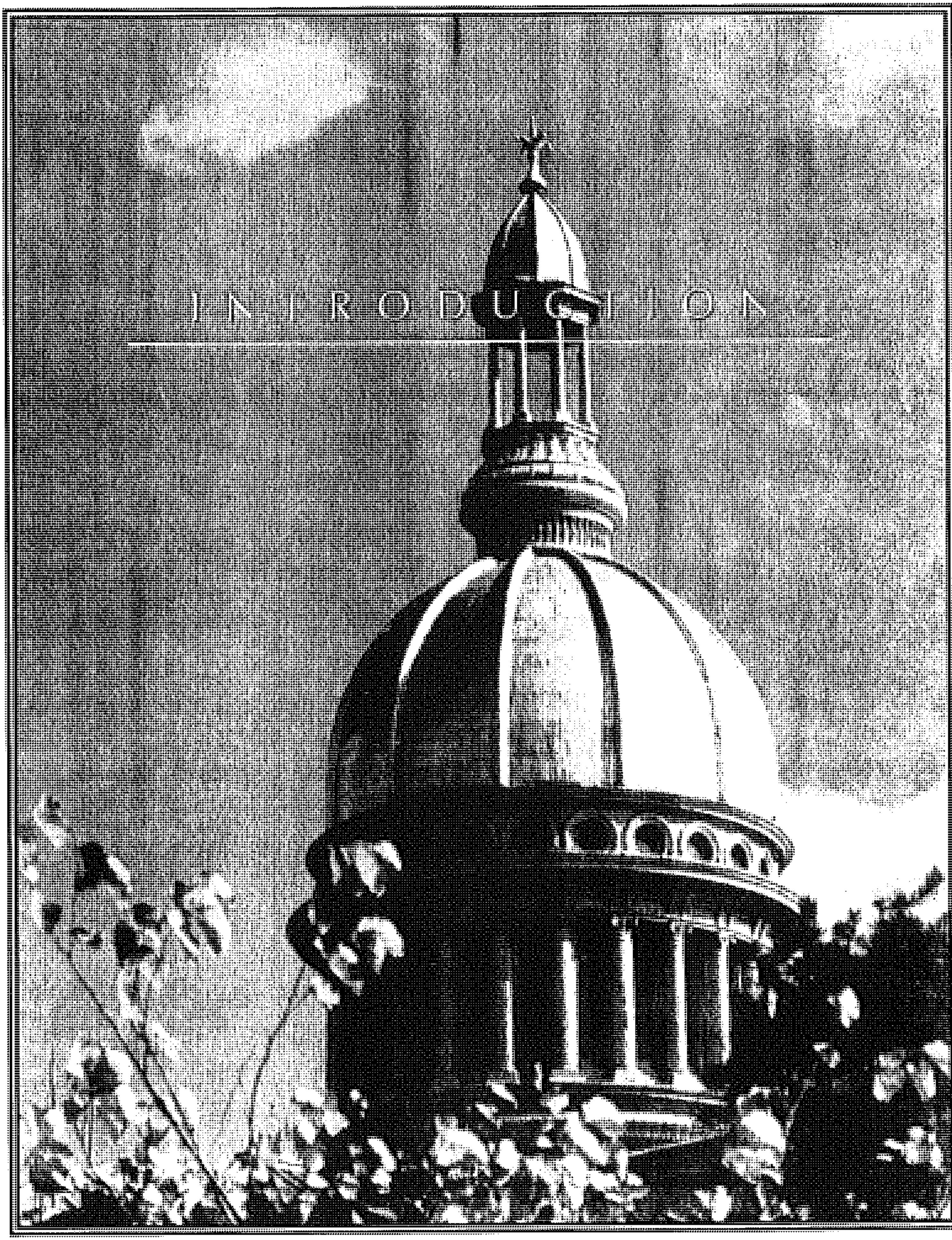
INTRODUCTION



State of New Jersey
DEPARTMENT OF THE TREASURY
OFFICE OF MANAGEMENT AND BUDGET
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CHRISTINE TODD WHITMAN
Governor

JAMES A. DIELEUTERIO, JR.
State Treasurer

November 7, 1997

Governor Christine Todd Whitman
Members of the State Legislature
Citizens of New Jersey

In accordance with the provisions of N.J.S.A. 52:27B-46, we are pleased to transmit to you the Comprehensive Annual Financial Report of the State of New Jersey for the year ended June 30, 1997. This report is prepared by the Office of Management and Budget, Department of the Treasury, which is responsible for the accuracy of the data and the completeness and fairness of the presentation, including all disclosures.

This Financial Report, which has earned an unqualified audit opinion, presents the financial position and operating results of the State under generally accepted accounting principles as established by the Governmental Accounting Standards Board as well as the traditional budgetary basis presentations. We are confident that the data is accurate in all material respects, that it is presented in a manner designed to set forth fairly the financial position and results of the State's operations as measured by the financial activity of its various funds, and that all disclosures necessary to enable the reader to gain a reasonable understanding of the State's financial affairs have been included.

As reflected in this report, the State ended the year in a sound fiscal position, with an Undesignated Fund Balance (surplus) of $1.1 billion in the major budgeted funds (General Fund, Property Tax Relief Fund, Casino Revenue Fund, and Surplus Revenue Fund).

The Comprehensive Annual Financial Report is presented in three sections: introductory, financial, and statistical. The introductory section includes this transmittal letter with summary financial data and narrative commentary on matters of interest to the reader, the State organization chart, and the 1996 Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting. The financial section includes the general purpose financial statements and footnotes, the combining and individual fund and account group financial statements, and the State Auditor's report on the financial statements. The statistical section includes the budgetary basis schedules, as well as selected financial and demographic information.

This report includes all funds, account groups, and component units of the entity called the State, which provides support for a full range of services including education, health and social services, transportation, law and public safety, justice, recreation, public improvements, and general administrative services. The criteria utilized to determine the entity for the State of New Jersey are those prescribed by the Government Accounting Standards Board (see Note 1 to the Financial Statements).

BUDGETARY CONTROLS, ACCOUNTING SYSTEMS, AND INTERNAL CONTROLS

The State's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) applicable to state governments as prescribed by the Governmental Accounting Standards Board. The governmental funds, expendable trust funds, and agency funds are presented on the modified accrual basis of accounting whereby revenues are recognized when measurable and available, and expenditures are recognized when goods and services are received and the related liabilities are incurred. The proprietary, nonexpendable trust, and pension trust funds are presented on the accrual basis of accounting whereby all revenues and expenses are recognized when the transactions occur, regardless of when the related cash is received or disbursed. The college and university funds are reported in conformance with GAAP as prescribed by the American Institute of Certified Public Accountants (AICPA) audit guide, "Audits of Colleges and Universities."

Encumbrance accounting is employed to ensure that expenditures do not exceed appropriations and allocations. Under encumbrance accounting, purchase orders, contracts, and other commitments involving the expenditure of monies are recorded in estimated amounts in order to reserve a portion of an appropriation until an actual liability is incurred. Total encumbrances and expenditures are monitored so as not to exceed amounts appropriated and/or allocated. Encumbrances outstanding at the end of a fiscal year are reported in the financial statements as reservations of fund balance. Any unencumbered and unexpended non-continuing appropriations lapse at the end of the fiscal year.

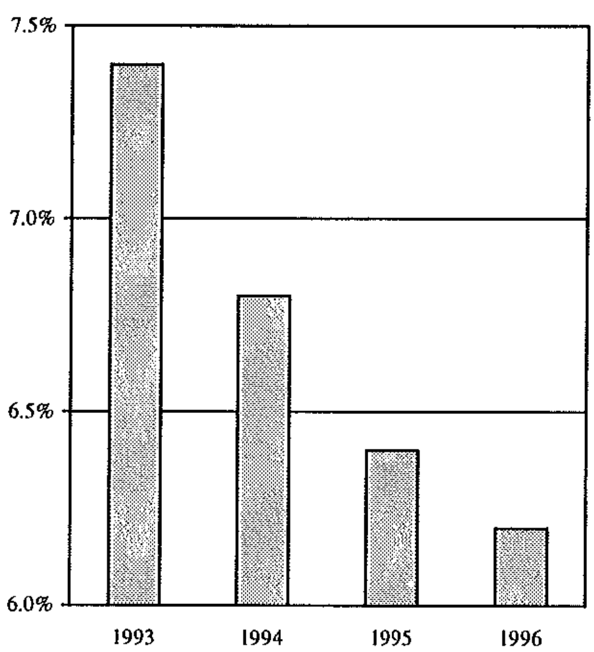
The accounting records of the various State departments are maintained on a central accounting system. The operations of this system are directed and supervised by the Office of Management and Budget. Separate accounting systems are maintained by those component units of government that are included in the State's reporting entity. The State's annual budget is comprised of individual appropriations to departments for specific programs and purposes. Budgetary control is exercised at the department level by individual appropriations and allocations within appropriations to various programs and major objects of expenditure.

In developing and maintaining the State's accounting system, consideration is given to the adequacy of internal controls. Internal accounting controls are designed to provide reasonable assurance regarding the safeguarding of assets against loss from unauthorized use or disposition and that financial records are reliable for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived from its use, and that the evaluation of costs and benefits requires estimates and judgments by management. All internal control evaluations occur within this framework.

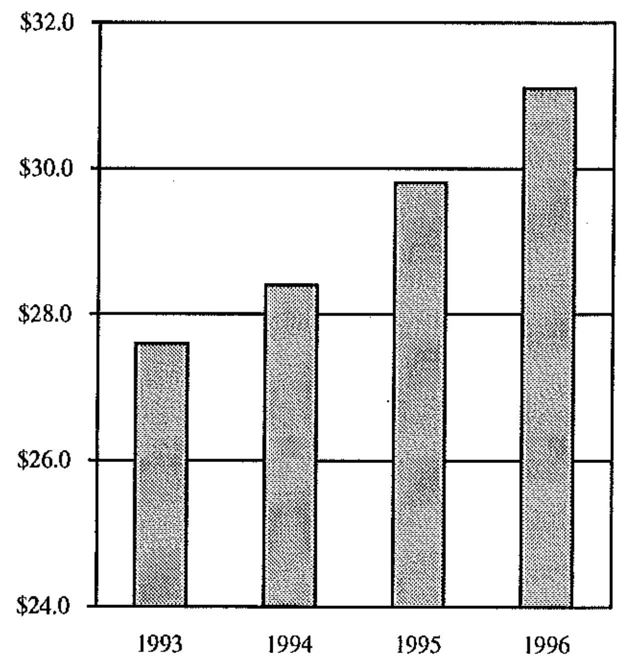
ECONOMIC CONDITION

The New Jersey economy in Calendar Year 1996 continued its positive growth trend. Employment and income growth became stronger as the year progressed. For the year, retail sales grew by 3.9 percent and total employment expanded by 1.7 percent. As demonstrated in the chart below, the State's unemployment rate fell to 6.2 percent, from 6.4 percent for the previous year and total personal income for Calendar Year 1996 grew by 4.7 percent.

New Jersey Unemployment Rate



New Jersey Personal Income (In Thousands)



It is expected that the New Jersey economy in Calendar Years 1997 through 1999 will continue to grow at a moderate pace with little or no inflation. New Jersey's economy, by virtue of its educated, high-technology labor resources, has benefited from newly emerging information-based fields. Meanwhile, corporate restructuring and downsizing in fields such as chemicals, telecommunications, and financial services has abated. Total employment is expected to grow by 1.8 percent for Calendar Year 1997 and continue to grow at an average rate of 0.8 percent through Calendar Year 1999. New Jersey's retail sales are expected to grow at 4.3 percent for Calendar Year 1997, and continue to grow at an average rate of 3.8 percent for Calendar Years 1998 and 1999. New Jersey Gross State Product, the most complete measure of economic activity, is expected to grow by 5.0 percent in Calendar Year 1997 and continue to grow at an average rate of 3.5 percent through 1999.

FISCAL YEAR 1997 REVENUE SUMMARY

The following revenue discussion encompasses the activity of the State's General Fund and four Special Revenue Funds--the Property Tax Relief Fund, the Casino Revenue Fund, the Casino Control Fund, and the Gubernatorial Elections Fund. The amounts included in this section are the actual anticipated revenues realized in support of the annual appropriations and do not include federal grants.

Fiscal Year 1997 revenue collections totaled $16.2 billion, $513.4 million above Fiscal Year 1996 revenue which included $359.2 million in one-time tax amnesty collections. Revenue growth in the State's three major taxes over Fiscal Year 1996 levels were as follows: the Sales Tax increased by $97.1 million or 2.2 percent, the Gross Income Tax increased by $91.6 million or 1.9 percent, and the Corporation Business Tax increased by $114.9 million or 9.8 percent. Overall, Fiscal Year 1997 revenue growth for the State's three major taxes totaled $303.6 million. Increased revenue over Fiscal Year 1996 levels reflect enhanced collection efforts implemented by the New Jersey Division of Taxation during its tax amnesty program which enabled the State to continue to collect from delinquent taxpayers without having a State revenue decline in its base in future fiscal years.

Collections for the State's three major taxes, as a percentage of Fiscal Year 1997 total receipts, were as follows: the Gross Income Tax represented 29.9 percent; the Sales Tax equaled 27.3 percent; and the Corporation Business Tax represented 8.0 percent. The State's three major taxes represented 65.2 percent of Fiscal Year 1997 total receipts, as compared to 65.4 percent for Fiscal Year 1996.

Even with major reductions in tax rates, the total revenues have grown over the past four years by $1.6 billion.

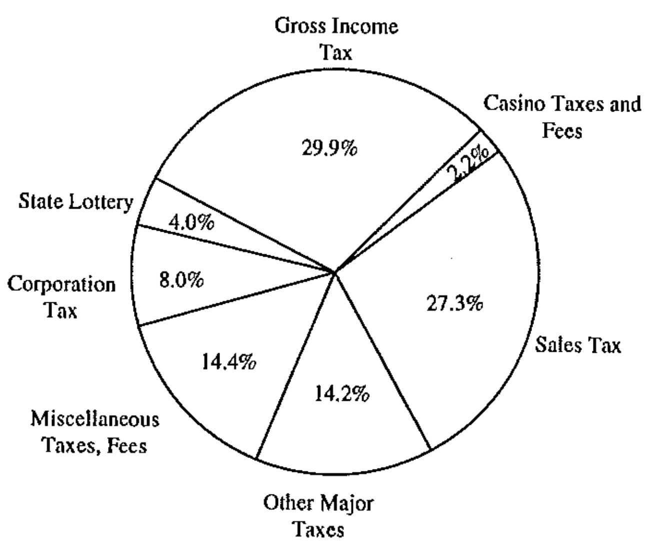
REVENUE SUMMARY BY MAJOR TAX
1993-1997 (Expressed in Millions)

	1997	1996	1995	1994	1993
Gross Income Tax	$ 4,825.4	$ 4,733.8	$ 4,540.0	$ 4,493.6	$ 4,350.5
Sales Tax	4,415.4	4,318.3	4,133.3	3,778.5	3,651.1
Other Major Taxes	2,297.2	2,276.1	2,215.4	2,263.8	2,161.4
Miscellaneous Taxes, Fees	2,320.9	2,121.1	2,016.8	2,446.2	2,543.2
Corporation Tax	1,286.4	1,171.5	1,085.5	1,063.1	960.7
State Lottery	650.0	662.1	647.8	602.8	581.7
Casino Taxes and Fees	359.6	358.6	355.4	319.8	315.4
Total	$ 16,154.9	$ 15,641.5	$ 14,994.2	$ 14,967.8	$ 14,564.0

REVENUE COMPARISONS

Source of Revenue ($000)	Fiscal Year 1997	Fiscal Year 1996	Increase/Decrease Amount	Increase/Decrease Percent
Gross Income Tax	$ 4,825,411	$ 4,733,786	$ 91,625	1.9
Sales Tax	4,415,428	4,318,373	97,055	2.2
Other Major Taxes	2,297,155	2,276,112	21,043	0.9
Miscellaneous Taxes, Fees	2,320,852	2,121,052	199,800	9.4
Corporation Tax	1,286,447	1,171,509	114,938	9.8
State Lottery	650,025	662,120	(12,095)	(1.8)
Casino Taxes and Fees	359,561	358,634	927	0.3
	$ 16,154,879	$ 15,641,586	$ 513,293	3.3

FISCAL YEAR 1997
MAJOR REVENUE CATEGORY COLLECTIONS
AS A PERCENT OF TOTAL REVENUE COLLECTIONS



FISCAL YEAR 1997 REVENUE SUMMARY:
PERCENT DISTRIBUTION OF REVENUE COLLECTIONS

Gross Income Tax	29.9%
Sales Tax	27.3
Other Major Taxes	14.2
Miscellaneous Taxes, Fees	14.4
Corporation Tax	8.0
State Lottery	4.0
Casino Taxes and Fees	2.2
Total	100.0%

FISCAL YEAR 1997 EXPENDITURE SUMMARY

Expenditure Category Descriptions

The following discussion of expenditures encompasses the activity of the State's General Fund and four Special Revenue Funds--the Property Tax Relief Fund, the Casino Revenue Fund, the Casino Control Fund, and the Gubernatorial Elections Fund. The amounts listed in this section are on a budgetary basis and do not include federal grants.

State expenditures fall into five major categories. They are State Aid, Direct State Services, Grants-in-Aid, Debt Service, and Capital Construction. Each expenditure category is described below.

State Aid represents funds that are distributed to municipalities, counties, and school districts. Most of the Gross Income Tax revenue is apportioned to State Aid, as is certain other revenue that is collected in the State's General Fund. By far the largest portion of expenditures in this category is for elementary and secondary school aid. This category also provides funding for the various public assistance programs and county psychiatric hospitals, as well as municipal property tax relief programs.

Direct State Services represent those functions operated directly by State government. Funding is largely for the salary and benefits of State employees, as well as faculty and staff at the State colleges and universities. Direct State Services support the operation of the State's departments, the Executive Office, several commissions, the State Legislature, and the Judiciary. Direct State Services partially support the operation of the colleges and universities. Public services offered by State government, such as motor vehicle inspections, testing laboratories, social services, legal services, State Police services, and the operation of prisons, psychiatric hospitals, and developmental disability centers are included in this grouping as well.

Grants-in-Aid represent programs and services provided to the public on behalf of the State by a third party provider. Grants-in-Aid payments are made to individuals and public or private agencies for benefits to which a recipient is entitled by law, or for the provision of services on behalf of the State. These payments include the Homestead Rebate program and the Medicaid program, which reimburses hospitals, nursing homes, and physicians for services rendered to the State's needy population. Community programs for the developmentally disabled, pharmaceutical assistance to the aged and disabled, Lifeline utility credits to senior citizens, financial aid grants to college students, and bus and railroad subsidies to New Jersey Transit are programs which also are included under the Grants-in-Aid umbrella.

Debt Service represents payments of interest and principal on capital projects funded through the sale of State General Obligation Bonds. Projects that have been funded through State General Obligation Bonds include prisons, bridges, roads, human services facilities, and various environmental protection projects.

Capital Construction represents pay-as you-go allocations for various construction projects. Included in this expenditure category is the appropriation to the Transportation Trust Fund Authority.

EXPENDITURE COMPARISONS

Expenditure Category ($000)	Fiscal Year 1997	Fiscal Year 1996	Increase/Decrease Amount
State Aid	$ 6,336,564	$ 6,336,997	$ (433)
Direct State Services	5,125,821	5,403,975	(278,154)
Grants-in-Aid	4,053,380	3,792,895	260,485
Debt Service	446,901	453,352	(6,451)
Capital Construction	373,318	275,477	97,841
	$ 16,335,984	$ 16,262,696	$ 73,288

Fiscal Year 1997 Expenditures

Fiscal Year 1997 expenditures of $16.3 billion are $73.3 million more than the expenditures of the prior fiscal year.

State Aid represented 38.8 percent of total Fiscal Year 1997 expenditures. State Aid includes aid to public schools, teachers' pensions and social security costs, municipal aid for over 14 different programs, reimbursement to counties for welfare programs, and other miscellaneous programs.

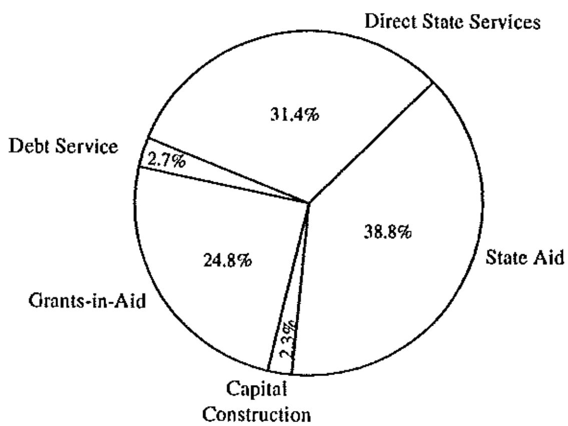
Direct State Services accounted for 31.4 percent of total Fiscal Year 1997 expenditures. Direct State Services expenditures decreased between Fiscal Year 1997 and Fiscal Year 1996 by $278.2 million. This amount includes a $138.3 million decrease in expenditures for employee benefits.

Grants-in-Aid accounted for 24.8 percent of total Fiscal Year 1997 expenditures. This is a $260.5 million increase from the prior fiscal year. The largest increase in Grants-in-Aid expenditures was for the Department of Health and Senior Services which includes medical services provided under the Medicaid program, pharmaceutical assistance to the aged and disabled, and the Lifeline Program for senior citizens previously administered by the Department of Human Services.

Debt Service represented 2.7 percent of total Fiscal Year 1997 expenditures. Debt Service expenditures decreased by $6.5 million.

Capital Construction represented 2.3 percent of total Fiscal Year 1997 expenditures. Construction for capital projects grew by $97.8 million as compared to the prior fiscal year. The primary areas of focus for these increases centered on transportation and environmental projects.

PERCENTAGE OF FISCAL YEAR 1997 EXPENDITURES BY MAJOR EXPENDITURE CATEGORY



EXPENDITURE DOLLAR
Fiscal Year 1997

State Aid	38.8%
Direct State Services	31.4
Grants-in-Aid	24.8
Debt Service	2.7
Capital Construction	2.3
Total	100.0%

The following table details expenditures by department for Fiscal Year 1997:

EXPENDITURES BY DEPARTMENT
STATE FUNDS
(Thousands of Dollars)

Department	State Aid	Direct State Services	Grants In-Aid	Debt Service	Capital Construction	Total
Legislative	$ --	$ 55,839	$ --	$ --	$ 1,150	$ 56,989
Executive	--	5,103	--	--	--	5,103
Judicial	--	357,265	--	--	--	357,265
Agriculture	--	9,064	4,162	--	--	13,226
Banking & Insurance	--	37,638	--	--	--	37,638
Commerce & Economic Dev.	5,507	24,790	16,282	5,796	--	52,375
Community Affairs	841,857	27,196	40,855	--	--	909,908
Corrections	--	627,301	127,903	--	14,672	769,876
Education	4,813,311	32,857	9,696	--	1,489	4,857,353
Environmental Protection	7,794	188,277	624	100,480	19,616	316,791
Health	20,566	48,451	989,322	--	318	1,058,657
Human Services	417,362	585,172	2,047,650	--	4,424	3,054,608
Labor	--	68,636	19,101	--	--	87,737
Law & Public Safety	3,075	399,714	7,182	--	7,333	417,304
Military & Veterans' Affairs	--	54,951	978	--	1,256	57,185
Personnel	--	27,127	--	--	--	27,127
State & Public Defender	13,984	776,525	47,641	--	4,851	843,001
Transportation	21,107	180,967	219,918	--	304,649	726,641
Treasury	192,001	247,841	522,066	340,625	7,295	1,309,828
Miscellaneous	--	2,043	--	--	2	2,045
Inter-Departmental	--	1,369,064	--	--	6,263	1,375,327
Total	$ 6,336,564	$ 5,125,821	$ 4,053,380	$ 446,901	$ 373,318	$ 16,335,984

FUND BALANCES

The State ended Fiscal Year 1997 with an undesignated fund balance of $1.1 billion for the major governmental funds. The Surplus Revenue Fund is used to account for revenues reserved for appropriation, a) in the event that anticipated revenues in the General Fund are estimated to be less than those certified by the Governor upon approval of the annual Appropriations Act or, b) in the event that the State Legislature finds that an appropriation from this fund is preferable to raising revenue through a modification of the tax structure. The Surplus Revenue Fund was established by P.L. 1990, c. 44. The significant increase in the Surplus Revenue Fund was the result of revenues realized in excess of the Appropriation Act anticipation. The following table presents a comparison of the components of the undesignated fund balances at the end of Fiscal Year 1997 and Fiscal Year 1996:

Fund	Fiscal Year 1997	Fiscal Year 1996	Increase/Decrease
General Fund	$ 280,576,653	$ 441,983,394	$ (161,406,741)
Surplus Revenue Fund	388,377,360	272,315,911	116,061,449
Property Tax Relief Fund	439,041,694	152,913,044	286,128,650
Casino Revenue Fund	--	12,828,028	(12,828,028)
Total	$ 1,107,995,707	$ 880,040,377	$ 227,955,330

Fiscal Year 1998 Revenue Projections

The Fiscal Year 1998 revenue projections are based on estimates of moderate overall economic growth. Total resources are projected at $17.3 billion. Included in the Gross Income Tax forecast is a deduction for residential property taxes paid by homeowners and tenants, and a refundable tax credit for property taxpayers. Effective January 1, 1997, 75 percent of a homeowner's, tenant's, or property taxpayer's property taxes, not in excess of $7,500, can be deducted. The Fiscal Year 1998 Corporation Business Tax forecast provides for changes in the rate for S Corporations to two percent, or one-half percent for S Corporations with $100,000 or less of annual income. The State's three major taxes are expected to comprise 63.0 percent of the Fiscal Year 1998's total resources and 67.0 percent of total revenue.

Fiscal Year 1998 Appropriations

The total Fiscal Year 1998 appropriation is $16.8 billion. Of the $16.8 billion appropriated in Fiscal Year 1998 from the General Fund, the Property Tax Relief Fund, the Casino Control Fund, the Casino Revenue Fund and the Gubernatorial Elections Fund, $6.8 billion (40.5%) is appropriated for State Aid to Local Governments, $3.9 billion (23.2%) is appropriated for Grants-in-Aid, $5.1 billion (30.3%) for Direct State Services, $0.5 billion (3.0%) for Debt Service on State General Obligation Bonds, and $0.5 billion (3.0%) for Capital Construction.

State Aid represents the largest portion of Fiscal Year 1998 appropriations. In Fiscal Year 1998, $6.8 billion will be distributed to municipalities, counties, and school districts. Major State Aid programs are: Aid to School Districts ($5,308.0 million), Unrestricted Aid to Municipalities and Counties ($819.8 million), Aid to Municipalities and Counties for Human Services programs ($416.4 million), and Aid to County Colleges ($140.1 million).

Direct State Services represent the second largest portion of the State's Fiscal Year 1998 appropriation. In Fiscal Year 1998, $5.1 billion has been appropriated. These funds support the operating costs of the Executive Departments, the Judiciary and the State Legislature. The largest appropriations are for the following departments: State Higher Education Institutions ($754.5 million), Human Services ($628.3 million), Corrections ($651.6 million), and Law and Public Safety ($339.2 million).

The Grants-in-Aid total Fiscal Year 1998 appropriation is $3.9 billion. These funds are distributed to individuals, public agencies, or private agencies as direct benefits or to provide services. The largest grants-in-aid programs are: Human Services programs ($1,939.8 million), Health and Senior Services programs ($941.9 million), Homestead Rebates ($325.0 million), Public Transportation ($165.9 million) and Higher Education ($271.2 million).

Debt Service for General Obligation Bonds is $0.5 billion. This amount reflects the cost of financing various infrastructure and environmental projects that have been approved through prior voter referenda.

Capital Construction appropriations for Fiscal Year 1998 total $0.5 billion. Of this amount, $380.3 million is the appropriation to the New Jersey Transportation Trust Fund Authority. This amount represents an increase of $75.8 million over the prior fiscal year. Appropriations totaling $66.8 million for environmental projects represent the four percent State Constitutional dedication of the Corporation Business Tax.

SERVICE EFFORTS AND ACCOMPLISHMENTS

The following sections highlight various service efforts and accomplishments the State has achieved during Fiscal Year 1997 as well as some of the goals the State hopes to achieve for Fiscal Year 1998.

Fiscal Year 1997

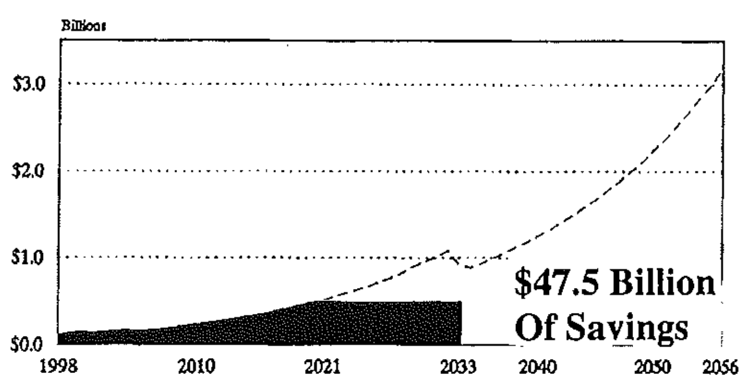
As part of the Fiscal Year 1997 Budget, the State enacted several policies which affected the State's Gross Income Tax and Corporation Business Tax. For the Gross Income Tax, a deduction for residential property taxes paid by homeowners and tenants was enacted. For property taxpayers, a refundable tax credit has been provided. Effective January 1, 1996, 50 percent of a homeowner, tenant, or property taxpayer's property taxes, not in excess of $5,000, can be deducted. Effective January 1, 1997, 75 percent of a homeowner, tenant or property taxpayer's property taxes, not in excess of $7,500, can be deducted. A reduction in the Corporation Business Tax rate from 9.0 percent to 7.5 percent became effective for those corporations that have net income of $100,000 or less. Also effective July 1, 1996, a corporation's sales became double weighted in calculating receipt factors in determining a multi-state corporation's New Jersey State Corporation Business Tax liability.

During June 1997, the Pension Security Plan was passed which enacted various reform measures involving seven of the State's pension fund systems and the Local Government's unfunded pension liability of the Public Employees' and the Police and Firemen's Retirement Systems. A major provision involves fully funding the State's unfunded pension liability of $3.2 billion and the projected unfunded liability of $1.0 billion by bringing the assets to full market value, recognizing surplus assets within the normal contribution accounts and issuing $2.75 billion of pension obligation bonds to refinance the remaining State's liability at interest rates below the pension systems' actuarially assumed rate. Prior pension policy called for the amortization of the State's unfunded liability to occur through Fiscal Year 2056 at a cost of $57.8 billion. The amortization of the pension obligation bonds occurs through Fiscal Year 2029 at a cost of $10.3 billion. Therefore, future taxpayers may reap savings of $47.5 billion from Fiscal Year 2030 through Fiscal Year 2056.

Another measure in the Pension Security Plan involves the reallocation of surplus assets within the pension systems to offset the State's normal contribution for Fiscal Years 1997 and 1998. This cost avoidance enables the State to realize $601 million in savings and the local governmental entities participating in the Public Employees' and the Police and Firemen's Retirement Systems to reap $107 million in savings. The Pension Security Plan also allows the State to reap budgetary savings in future years should investment gains exceed actuarial assumptions.

Other Pension Security Plan provisions benefit the members directly. During Calendar Years 1998 and 1999, Public Employees' Retirement System and Teachers' Pension and Annuity Fund members will have their contributions reduced by 1/2 of 1 percent with future reductions possible.

Enhanced Savings Structure



• Adds $25 million from FY 1999 - FY 2004 which lowers the overall payments
• $505 million level payments from FY 2021 - FY 2033
• Total Debt Service = $12.3 billion

Beginning in Fiscal Year 1997, the Governor and the State Legislature have enacted a coherent, comprehensive policy to help the State's 1.4 million senior citizens attain the highest level of dignity and independence by consolidating all programs for older adults into the Department of Health and Senior Services. Services such as housing assistance, Medicaid, and nursing home information were provided for individually, through the Departments of Community Affairs, Human Services, and Health, respectively. Through the new Department of Health and Senior Services, all programs for seniors are coordinated so that more informed choices can be made for long-term care. As part of this program, the State is coordinating its efforts with counties and municipalities to create a new way of delivering these types of services at the local level.

To alleviate overcrowding in State prisons and county jails, the Southwoods Prison Project was initiated in an effort to add 3,000 beds to the State prison system. The Southwoods Prison Project comprises the construction of a 1,355,000 square foot medium security prison, including a poultry processing plant and a central kitchen which will service prison facilities throughout the State. Construction of Phase I, which includes the first 1,000 beds and various administrative buildings, was completed on May 16, 1997 for beneficial use and occupancy. Phase IIA, which includes the second 1,000 beds is expected to be completed during late 1997. The final stage of the project, Phase II, is expected to be completed by March 13, 1998.

On November 5, 1996, the voters of the State, through voter referendum, amended the New Jersey Constitution to provide that an amount equivalent to 4.0 percent of the revenue annually derived from the Corporation Business Tax be deposited in a special account for appropriation for the following purposes and in the following manner: 1) a minimum of 1/2 for funding State costs relating to hazardous discharge remediations; 2) a minimum of 1/3, dedicated until December 31, 2008, for funding loans and grants for underground storage tank upgrades and replacements; and 3) a minimum of 1/6 or $5.0 million, whichever is less, for funding costs related to water quality monitoring, watershed planning, and nonpoint source water pollution prevention. This resulted in $31.9 million being dedicated from the Corporation Business Tax revenues for Fiscal Year 1997. The appropriation for the fiscal year 1998 dedication is $62.4 million.

In an effort to streamline State government services, the Department of Banking has merged with the Department of Insurance. This restructure combines common functions of administration, licensing, examinations, and complaint investigations into a single, integrated department. The new Department of Banking and Insurance reduces the number of State departments to sixteen. The maximum amount of State departments permitted under the New Jersey Constitution is nineteen.

During April 1997, the New Jersey Transit Corporation issued $347.7 million in Capital Grant Anticipation Notes in order to fund the Phase I construction of a north-south mass transit system along the west side of the Hudson River to be known as the Hudson-Bergen Light Rail Transit System. Under the terms of a design, build, operate and maintain agreement that the New Jersey Transit Corporation entered into, construction on the project is expected to be completed by March 1, 2000. The Notes are expected to be paid through receipts received under a Grant Agreement between the New Jersey Transit Corporation and the Federal Government. The New Jersey Transit Corporation has also entered into a Standby Deficiency Agreement with the New Jersey Transportation Trust Fund Authority in order to provide further security for the noteholders.

In an effort to meet its customers needs, the New Jersey State Lottery implemented an option of either a lump sum award or a 20 year annuity payment plan for winners of large cash prizes. Historically, the State Lottery provided only 20 year annuity payments for its customers. The ability to select a lump sum payment as an award is seen as a customer service initiative that will spur interest from new players for the State Lottery's large cash drawings. Future General Fund revenues are expected to be positively impacted as this measure becomes more widely known.

Fiscal Year 1998

Fiscal Year 1998 will represent the first full fiscal year in which welfare reform measures under the Work First New Jersey Program were enacted. The Work First New Jersey Program consolidated and replaced various Department of Human Services programs such as aid to families with dependent children, emergency assistance, General Assistance, and the Family Development Initiative. Basic eligibility requirements, income and resource eligibility levels, time limits on benefits, and pilot and demonstration projects have been statutorily enacted under the auspices of the Commissioner of Human Services for the Work First New Jersey Program. The current overall gross cost of the programs now under Work First New Jersey Program totals approximately $1.3 billion. The State expects that the funding level for these programs will remain at $1.3 billion for the next several fiscal years. The enactment and the funding of the Work First New Jersey Program allows New Jersey to comply with new federal mandates and qualifies the State for the Federal Temporary Assistance to Needy Families Block Grant in the amount of $404 million annually. This amount is approximately $50 million to $60 million more than the State recently received under its existing program.

Under its Fiscal Year 1995 reauthorization, the New Jersey Transportation Trust Fund Authority budgeted debt service on the bonds that it issues at a rate between 7.20 percent and 8.50 percent. Since then, favorable variances have occurred which have resulted in significant debt service savings. Bonds that the New Jersey Transportation Trust Fund Authority issued have a weighted average cost of capital of 5.47 percent. The Department of Transportation, with the consent of the State Legislature, plans to utilize these savings by increasing its Fiscal Year 1998 capital program by $200 million. This one-time initiative will be achieved without reducing the Transportation Trust Fund Authority's capital program in future years, increasing its statutory debt limit, or requiring any additional State appropriations. The $200 million increase in its capital program is expected to create 7,600 jobs for the State's economy.

In an effort to curb or actually reduce the rate of growth in automobile insurance rates, several initiatives have been enacted. Strategies to reduce short-term costs involve eliminating unnecessary medical expenses, while strategies to reduce long-term costs involve attacking pervasive fraud, promoting a market fairer to consumers by eliminating automobile insurance surcharges and automatic rate increases, restricting arbitrary nonrenewals of good drivers and promoting market access in underserved urban areas called automobile insurance urban enterprise zones. The Department of Banking and Insurance has added 50 additional insurance fraud investigators. For Fiscal Year 1998, a total of $2.25 million has been appropriated for these purposes.

As a result of recent regulatory developments at the State and Federal level, legislation has been enacted to begin the transition of utilities into a competitive, free market environment. The manner in which energy producers conduct business in New Jersey and the way consumers buy and consume energy products in the State is expected to be altered dramatically. The legislation addresses the need to restructure energy taxation rates so that the continual erosion of tax revenue for annual distribution to municipalities and the State's General Fund is prevented. In its place, electric, gas and telecommunications utilities will be subject to the State's Corporation Business Tax. The State's existing Sales and Use Tax, with certain exceptions, will be applied to retail sales of electric and natural gas, and a transitional energy facility assessment will be applied for a limited time on electric and gas utilities. The assessment will be phased out over a five year period. Under companion legislation, municipalities will be guaranteed an annual State Aid distribution of at least $740 million from these replacement revenues. This amount reflects an increase from the $685 million base under the old legislation, which has been supplemented in recent years by excess revenue.

State School Aid to local districts in Fiscal Year 1997 totaled $4.870 billion; this included $4.203 billion in direct aid and an additional $667 million in aid to local districts for the employers' share of teachers' pensions and social security payments. Fiscal Year 1997 was significant in that it marked the last year in which funding was provided to local districts under the revised version of the Quality Education Act. The key item of funding was Foundation Aid totaling $2.722 billion which was distributed based on a measure of local districts property wealth and per capita income. Foundation Aid represented approximately 65 percent of the aid amount distributed in Fiscal Year 1997.

Fiscal Year 1998 marks the implementation of a new school funding formula specified by the Comprehensive Education Improvement and Financing Act of 1996. State School Aid will total $5.308 billion, a net increase of nearly $438 million. This new funding will be directed toward a new focus in education - the implementation of Core Curriculum Standards, a methodology that will guarantee that all public school students will learn the same basic educational components. Foundation Aid will be replaced by Core Curriculum Standards Aid which will be geared to support the newly adopted core curriculum standards which include seven areas of measurable, grade-appropriate levels of accomplishment: Language Arts/Literacy, Mathematics, Science, Social Studies, Visual and Performing Arts, Physical and Mental Health Education, and World Languages.

The net increase of $438 million in the State School Aid appropriation for Fiscal Year 1998, includes significant funding for new initiatives including $288 million for Early Childhood Education, $175 million for Demonstrably Effective Programs, and $50 million for the beginning of a statewide Distance Learning Network. On May 14, 1997, the State Supreme Court ruled that the new school funding law did not provide sufficient funding for the plaintiffs in the Abbott v. Burke case. As a result, an additional $246 million was added to the Budget to provide additional parity aid to these districts.

COMPONENT UNITS

The component units include the accounts of the various public authorities, colleges, and universities. These authorities are legally separate entities that are not operating departments of the State. Governing boards are vested with the power to independently manage the component units. Each component unit is established for a specific purpose for the benefit of the State's citizenry, such as economic development, public transportation, subsidized housing, environmental protection, and capital development for health and education purposes.

Authorities

Hackensack Meadowlands Development Commission
New Jersey Development Authority For Small Business, Minorities And Women's Enterprise
New Jersey Economic Development Authority
New Jersey Educational Facilities Authority
New Jersey Health Care Facilities Financing Authority
New Jersey Higher Education Assistance Authority - NJ Class
New Jersey Highway Authority
New Jersey Housing And Mortgage Finance Agency
New Jersey Redevelopment Authority
New Jersey Sports and Exposition Authority
New Jersey Transit Corporation
New Jersey Turnpike Authority
New Jersey Wastewater Treatment Trust
New Jersey Water Supply Authority
South Jersey Port Corporation
South Jersey Transportation Authority

Colleges And Universities

The College of New Jersey
Thomas A. Edison State College
Jersey City State College
Kean College of New Jersey
Montclair State University
New Jersey Institute of Technology
The William Paterson University of New Jersey
Ramapo College of New Jersey
Rowan University
Rutgers, The State University
Richard Stockton College of New Jersey
University of Medicine And Dentistry of New Jersey

Combined operating revenues and expenses for the State's authorities amounted to $2.5 billion and $3.0 billion, respectively, for Fiscal Year 1997. Total operations along with other financing sources and uses contributed to a total combined fund balance at fiscal year end of $2.7 billion.

For Fiscal Year 1997, combined revenues for the state colleges and universities were $2.4 billion. Combined expenditures totaled $3.1 billion. Total operations along with other financing sources and uses contributed to a total combined fund balance at fiscal year end of $3.0 billion.

GENERAL FIXED ASSETS

The general fixed assets of the State are used in the performance of general governmental functions and exclude the fixed assets of the component units. As of June 30, 1997, the general fixed assets of the State amounted to $2.4 billion. This amount represents the actual or estimated cost of the assets. Depreciation of general fixed assets is not recognized in the State's accounting system. Infrastructure assets, consisting primarily of highways, roads, and bridges, are not recorded in the general fixed assets.

DEBT ADMINISTRATION

As of June 30, 1997, outstanding General Obligation Debt totaled $3.4 billion. General Obligation Debt must be approved by voter referendum and is used primarily to finance various environmental projects, transportation infrastructure, and correctional and institutional construction.

The State's Master Lease Program is used primarily to finance various departmental equipment needs at tax-exempt rates by issuing Certificates of Participation. Beginning in Fiscal Year 1996 the State modified the Master Lease Program and began using a line of credit as the preferred method of financing various departmental equipment needs. As of June 30, 1997, outstanding Certificates of Participation totaled $16.3 million and the State's outstanding balance on its line of credit totaled $21.8 million.

The State first began issuing Tax and Revenue Anticipation Notes during Fiscal Year 1992, in order to provide effective cash flow management of imbalances which occur in the timing of collections and disbursements of State revenues and expenditures. The State Treasurer is authorized to issue these types of instruments without constituting a general obligation of the State, or a debt, or a liability within the meaning of the State Constitution. All short-term notes that are issued must be retired within twelve months of their issuance date. The State has issued and retired short-term notes in prior fiscal years that have ranged from a high of $1.800 billion in Fiscal Year 1992 to a low of $450 million in Fiscal Year 1996. Beginning in Fiscal Year 1996, the State began issuing commercial paper as the sole instrument for meeting its cash flow needs. During Fiscal Year 1997, the State issued $600 million in commercial paper. The entire amount was retired on June 13, 1997.

The State funds its capital appropriations by authorizing the issuance of long-term bonds. The following table sets forth the trend of the State's tax-supported long-term indebtedness for the last five years:

LONG TERM DEBT
(Amount in Billions)

Fiscal Year	Authorized-Unissued	Principal Amount of Outstanding Long-Term Debt
1997	$ 1.9	$ 3.4
1996	1.6	3.7
1995	1.5	3.6
1994	1.4	3.6
1993	1.4	3.6

As of June 30, 1997, Standard and Poor's Corporation, Moody's Investors Service and Fitch Investors Service rate the State's long-term general obligation debt AA+, Aa1 and AA+, respectively. The State's Certificates of Participation are rated AA- by Standard and Poor's and A1 by Moody's.

CASH MANAGEMENT

The State's Division of Investments was created by law in 1950 in order to centralize all functions relating to the purchases, sales, or exchanges of securities for the State's diverse funds under experienced and professional management. The statute provides investment authority to the State Investment Council and to the Director of the Division. The State Treasurer appoints the Director from a field of candidates selected by the State Investment Council. The role of the State Investment Council is to formulate investment policies and procedures to be followed by the Director. State legislation provides that the State Investment Council may issue regulations which specifically approve and authorize any form of investment. The State Investment Council has taken the position that the Division of Investments is bound by law to make prudent investments for the sole and direct financial benefit of the beneficiaries of the various funds under its supervision, and that the Division of Investments may not make any concession as to the rate, risk or terms which would benefit any other party at the expense of the beneficiaries of the funds.

Unused cash is invested primarily in the New Jersey Cash Management Fund. The fund provides the State, its authorities and agencies, local municipalities, and school districts with a vehicle for short-term investment. For the Fiscal Year ended June 30, 1997, the New Jersey Cash Management Fund's average daily annualized rate of return for participating state accounts was 5.5 percent. For "Other-than-State" participants the average daily annualized rate of return, which includes charges for administrative and operating expenses, was 5.3 percent for the Fiscal Year ended June 30, 1997.

RISK MANAGEMENT

New Jersey's risk management function is performed within the Department of the Treasury and operates to reduce the adverse impact of catastrophic loss on State operations and budgets through a combination of risk management and loss prevention techniques. The Office of Risk Management administers claims against the State and its employees under the Tort Claims Act, Workers Compensation statute, and various Federal laws, as well as claims on behalf of the State against others responsible for damage to the State, its employees, and its property.

AUDIT INFORMATION

The principal auditor of the State's reporting entity is the legislative office of the State Auditor. Their examination was conducted in accordance with generally accepted auditing standards and their opinion precedes the General Purpose Financial Statements. Outside public accounting firms have been used for the audits of separately issued component unit and college and university fund financial statements. In addition, the Office of the State Auditor conducts periodic financial and expanded scope audits of the various State agencies. This audit received an unqualified opinion for all funds contained in this Comprehensive Annual Financial Report.

CERTIFICATE OF ACHIEVEMENT FOR EXCELLENCE IN FINANCIAL REPORTING

The Government Finance Officers Association of the United States and Canada has awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of New Jersey for its Comprehensive Annual Financial Report for the year ended June 30, 1996.

In order to qualify for the Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report, the contents of which conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

We believe our current report continues to conform with the Certificate of Achievement Program requirements.

ACKNOWLEDGMENTS

Finally, we would like to express our appreciation to the many people in the Office of Management and Budget and the Office of the State Auditor whose dedicated efforts made possible the preparation of this report. We believe that their combined efforts have produced a report that will provide a means for government, the financial community, decision makers, and concerned citizens to better understand and evaluate the State's financial condition.

Sincerely,

James A. DiEleuterio, Jr.
State Treasurer

Elizabeth L. Pugh
State Comptroller

Certificate of Achievement for Excellence in Financial Reporting

Presented to

State of New Jersey

For its Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 1996

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

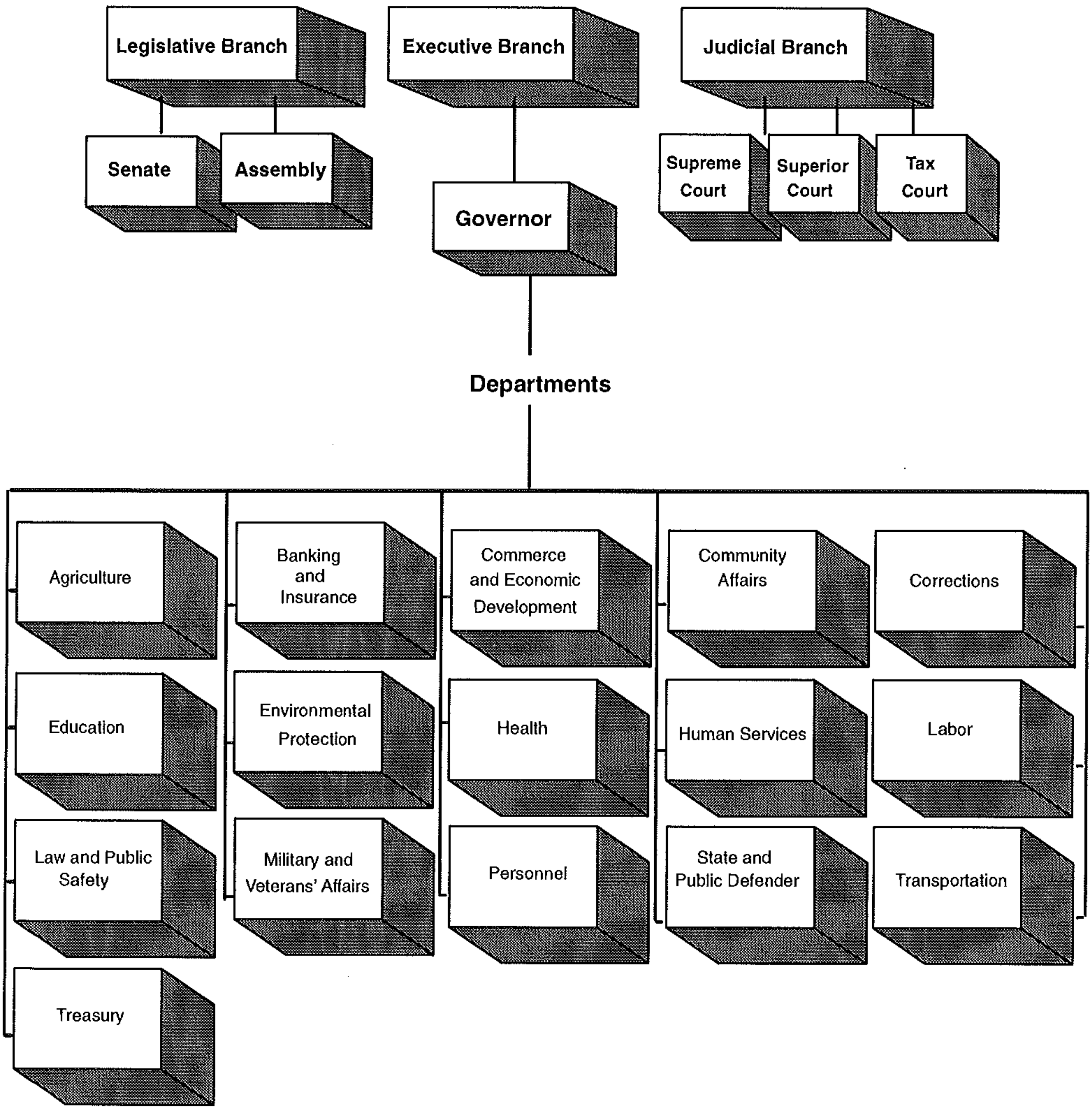
Linda K. Savitsky

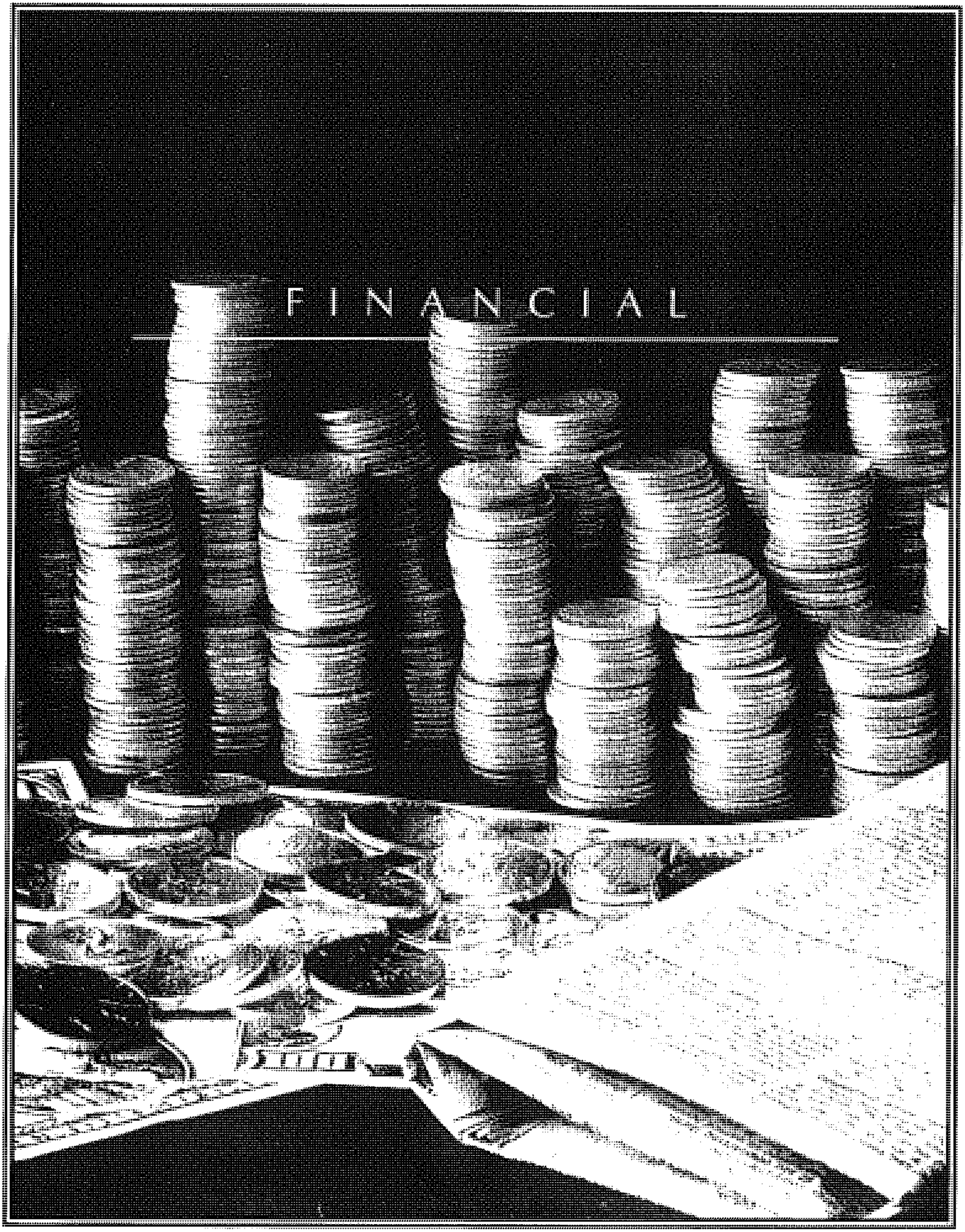
President

Jeffrey L. Esser

Executive Director

ORGANIZATION OF NEW JERSEY STATE GOVERNMENT




FINANCIAL

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The Honorable Christine Todd Whitman
Governor of New Jersey

The Honorable Donald T. DiFrancesco
President of the Senate

The Honorable Jack Collins
Speaker of the General Assembly

Mr. Albert Porroni
Executive Director
Office of Legislative Services

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying general purpose financial statements of the State of New Jersey as of and for the year ended June 30, 1997, as listed in the table of contents - financial section. These general purpose financial statements are the responsibility of the State of New Jersey's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit. We did not audit the financial statements of the Component Units - Authorities and College and University Funds. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion on the general purpose financial statements, insofar as it relates to the amounts included for the Component Units - Authorities and College and University Funds, is based upon the reports of the other auditors.

We conducted our audit in accordance with generally accepted auditing standards and 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 general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall general purpose financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based upon our audit and the reports of other auditors, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the State of New Jersey as of June 30, 1997, and the results of its operations and cash flows of the nonexpendable trust fund and the proprietary fund type authorities for the year then ended in conformity with generally accepted accounting principles.

As discussed more fully in note 2(a), the State adopted Statement 25 "Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans" and Statement 27 "Accounting for Pensions by State and Local Government Employers" of the Government Accounting Standards Board during the year ended June 30, 1997. Also, as described in note 1(g), participation in the Cash Management Fund Investment Program and the Common Pension Trust Fund Program is reflected as investments in the balance sheets of participating funds.

In accordance with Government Auditing Standards, we have also issued a report dated November 7, 1997 on our consideration of the State of New Jersey's internal control structure and a report dated November 7, 1997 on its compliance with laws and regulations.

Our audit was conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The combining and individual fund and account group financial statements and schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the general purpose financial statements of the State of New Jersey. Such information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly presented in all material respects in relation to the general purpose financial statements taken as a whole.

The introductory section and the statistical section listed in the aforementioned table of contents have not been audited by us and, accordingly, we do not express an opinion on them.

Richard L. Fair
State Auditor
November 7, 1997