

New Jersey Comprehensive Annual Financial Report



**For The Fiscal Year
Ended June 30, 2013**



State of New Jersey



Comprehensive Annual Financial Report Fiscal Year Ended June 30, 2013

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Governor

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Lieutenant Governor

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**STATE OF NEW JERSEY
 COMPREHENSIVE ANNUAL FINANCIAL REPORT
 FISCAL YEAR ENDED JUNE 30, 2013
 TABLE OF CONTENTS**

INTRODUCTION	Page
Letter of Transmittal	1
Certificate of Achievement	7
FINANCIAL SECTION	
Independent Auditor’s Report	11
Management’s Discussion and Analysis	16
Basic Financial Statements	
Government-wide Financial Statements	
Statement of Net Position	30
Statement of Activities	32
Governmental Funds Financial Statements	
Balance Sheet	34
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position	35
Statement of Revenues, Expenditures and Changes in Fund Balances.....	36
Reconciliation of the Changes in Fund Balances of Governmental Funds to the Statement of Activities.....	37
Proprietary Funds Financial Statements	
Statement of Net Position	38
Statement of Revenues, Expenses and Changes in Fund Net Position	39
Statement of Cash Flows	40
Fiduciary Funds Financial Statements	
Statement of Fiduciary Net Position	42
Statement of Changes in Fiduciary Net Position	44
Component Units Financial Statements	
Statement of Net Position.....	46
Statement of Activities	48
Index to the Notes to the Financial Statements	50
Notes to the Financial Statements	51
Required Supplementary Information	
Budgetary Comparison Schedule	106
Budgetary Comparison Schedule – Budget to GAAP Reconciliation Major Funds	109
Notes to Required Supplementary Information	111
Schedule of Funding Progress All Pension Trust Funds	112
Combining Financial Statements	
Governmental Funds - Major Fund – General Fund	
Balance Sheet	114
Statement of Revenues, Expenditures and Changes in Fund Balances.....	132

	Page
Governmental Funds – Non-Major Funds	
Balance Sheet – By Fund Type	150
Statement of Revenues, Expenditures and Changes in Fund Balances – By Fund Type	151
Special Revenue Funds	
Balance Sheet	152
Statement of Revenues, Expenditures and Changes in Fund Balances	172
Capital Projects Funds – Non-Major Funds	
Balance Sheet	192
Statement of Revenues, Expenditures and Changes in Fund Balances	196
Fiduciary Funds	
Agency Funds	
Statement of Fiduciary Net Position	200
Statement of Changes in Assets and Liabilities	204
Pension and Other Employee Benefits Trust Funds	
Statement of Fiduciary Net Position	208
Statement of Changes in Fiduciary Net Position	212
Private Purpose Trust Funds	
Statement of Fiduciary Net Position	216
Statement of Changes in Fiduciary Net Position	218
Component Units	
Statement of Net Position – Non-Major Component Units	220
Statement of Activities – Non-Major Component Units	221
Authorities	
Statement of Net Position	222
Statement of Activities	226
Colleges and Universities	
Statement of Net Position	230
Statement of Activities	234
Description of Funds	237
Other Information	
Capital Assets	
Schedule of Changes in Gross Capital Assets by Function	265
Schedule of Gross Capital Assets by Function	266
Schedule of Changes in Accumulated Depreciation by Function	269
Schedule of Accumulated Depreciation by Function	270
Accumulated Depreciation as a Percentage of Capital Assets	272
Long-Term Debt	
Schedule of Long-Term Debt	274
Budgetary Schedules	
Budgetary Comparison Schedule Non-Major Governmental Funds	276
Budgetary Comparison Schedule-Budget to GAAP Reconciliation – Non-Major Funds	280
Schedule of Anticipated Revenue	282
Schedule of Appropriated Revenue	291
Schedule of Appropriations and Expenditures	292
STATISTICAL SECTION	
Statistical Section Index	313

Introduction







State of New Jersey

CHRIS CHRISTIE
Governor

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State Treasurer

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Director

March 12, 2014

Governor Chris Christie
Members of the State Legislature
New Jersey Citizens

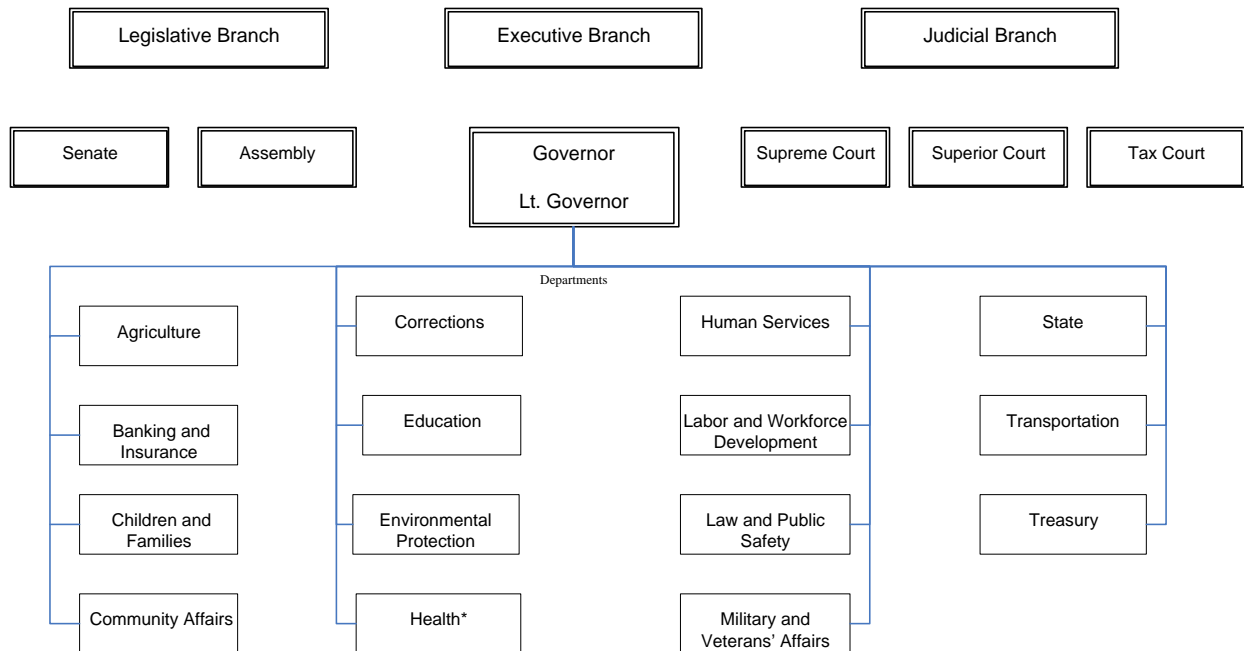
In accordance with the provisions of N.J.S.52:27B-46, it is our pleasure to transmit to you the State of New Jersey's Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2013. The Department of the Treasury's Office of Management and Budget prepared this report. The Department of the Treasury and the Office of Management and Budget are responsible for the accuracy, completeness, and fairness of all data presented, including all disclosures.

This CAFR presents the financial position and operating results of the State under generally accepted accounting principles (GAAP) applicable to State and local governments, as established by the Governmental Accounting Standards Board (GASB). The State also participates in the Government Finance Officers Association (GFOA) of the United States and Canada's Certificate of Achievement for Excellence in Financial Reporting review program.

The State operates in accordance with the standards provided in GASB Statements No. 34 and No. 35. In addition to providing traditional fund financial statements, the objective of this reporting model is to provide a single, unified, transparent picture of the State's fiscal health; thus, this CAFR clearly displays all of the State's revenues, costs, assets, and liabilities. This report also includes a Management's Discussion and Analysis section, which provides users with an objective and easy-to-read analysis of New Jersey's financial performance for the fiscal year ended June 30, 2013. We are confident that the data is accurate in all material respects and presented in a manner designed to set forth fairly the financial position and results of the State's operations, as measured by the fiscal activity of its various funds, and includes all disclosures necessary to enable the reader to gain a reasonable understanding of the State's financial affairs.

NEW JERSEY GOVERNMENT

One of the original thirteen colonies, the State of New Jersey was the third state to ratify the United States Constitution in 1787. Adopted on July 2, 1776, New Jersey's original State Constitution subsequently was superseded by the State Constitution of 1844. During the summer of 1947, a constitutional convention met to prepare the current State Constitution, which State voters ratified in the general election held on November 4, 1947. New Jersey's State Constitution continues to be a living document, as State voters passed an amendment creating the position of Lieutenant Governor of New Jersey, effective with the 2009 election. Effective December 8, 2011, it became lawful for the Legislature to authorize wagering on sports events at New Jersey casinos and horse racetracks, excluding events that take place in New Jersey or in which any New Jersey college team participates regardless of where the event takes place. The current status to legalize sports betting at New Jersey casinos and horse racetracks is to appeal the case to the United States Supreme Court. On November 5, 2013, New Jersey voters approved a ballot question to raise the minimum wage to \$8.25 an hour from \$7.25 an hour in January and amend the State Constitution to tie future increases to the nation's inflation rate. With the increase, New Jersey becomes the twenty-first state to establish a minimum wage higher than the federal minimum of \$7.25 an hour. The State Constitution divides the powers of government between three co-equal independent branches: Legislative, Executive, and Judicial.



* P.L. 2012 c.17 reorganized the Division of Aging from Health and Senior Services to Human Services and renamed the Department of Health and Senior Services to the Department of Health.

Legislative: The State’s bicameral Legislative Branch, which consists of a total of 120 members from 40 legislative districts with elections held in odd-numbered years, meets in annual sessions in Trenton, the State’s capital. The 40 members of the State Senate are elected to terms of four years, except for the election following a decennial census, in which case the term is for two years. The 80 members of the General Assembly are elected to terms of two years. Neither State Senators nor Assembly Members are subject to term limits. The Office of Legislative Services (OLS) is a nonpartisan agency that provides legislators with legal, fiscal, research, information, and administrative services. Key OLS positions include an executive director, a legislative counsel, the state auditor, a legislative budget and finance officer, a director of central staff, a director of data management, and a director of administration.

Executive: The Office of the Chief Executive, which oversees the entire Executive Branch, consists of the Governor, the Lieutenant Governor, Cabinet-level department heads, and staff who are responsible for carrying out the Governor’s constitutional powers and duties. Upon direct election by a plurality of the State’s voters, both the Governor and the Lieutenant Governor may serve two successive terms of four years. With the exception of the Secretary of Agriculture, who is chosen by the Board of Agriculture with the Governor’s approval, the New Jersey State Constitution grants the Governor the authority to appoint the entire cabinet as well as all Superior Court Judges and county prosecutors, subject to confirmation by the New Jersey Senate. Department heads remain in office until their successors are named and confirmed by the Senate; the only exceptions are the Attorney General and the Secretary of State, who are appointed to serve throughout the Governor’s entire term. Although the State Constitution permits a maximum of 20 departments, the State’s payroll consisted of approximately 59,800 employees in 15 departments as of January 2013. The Executive Branch also oversees the performance of 565 municipalities and 603 school districts, and the incarceration and rehabilitation of approximately 20,200 prisoners. In addition to reliable transportation and protection for the State’s citizenry and environment, the Executive Branch provides social services for one out of every six New Jersey citizens.

Judicial: New Jersey’s Supreme Court consists of a Chief Justice, who is the administrative head of all courts under the State’s jurisdiction, as well as six Associate Justices. In addition to Municipal and Tax Courts located throughout the State, there are Superior Courts, with a minimum of two Judges, in each of New Jersey’s 21 counties. After nomination by the Governor and subsequent confirmation by the State Senate, all Supreme Court Justices and Superior Court Judges serve initial terms of seven years. Should they be deemed eligible by both the Governor and the State Senate, Supreme Court Justices and Superior Court Judges acquire tenure with retirement at age 70 as mandated by the State Constitution. For purposes of judicial administration, the State is divided into 15 vicinages, each consisting of a single county or a combination of counties. The Administrative Office of the Courts provides support services. Approximately seven million new cases are filed in New Jersey’s courts every year, including six million in Municipal Court and one million in Superior Court. These cases address matters concerning civil, criminal, and family law.

As of July 1, 2013, the higher education system in New Jersey includes three public research universities, eight State colleges and universities, nineteen community colleges, fourteen independent four-year colleges and universities, eight proprietary institutions with degree-granting authority, thirteen rabbinical schools and theological seminaries, and one independent two-year religious college. Effective July 1, 2013, the “New Jersey Medical and Health Sciences Education Restructuring Act” of 2012 abolished the University of Medicine and Dentistry of New Jersey (UMDNJ), transferred UMDNJ’s various schools and institutes to Rutgers University and Rowan University, respectively, and established Rowan University as a public research university. University Hospital was established as a separate non-profit legal entity of the State of New Jersey. In November 2012, New Jersey voters approved the \$750 million “Building our Future Bond Act” (P.L. 2012, c.141), and in April 2013, the State announced reauthorization of four additional higher education funding programs – the Higher Education Capital Improvement Fund (CIF); the Higher Education Facilities Trust Fund (HEFT); the Higher Education Technology Infrastructure Fund (HETI); and the Higher Education Equipment Leasing Fund (ELF). Together, these five programs will provide more than \$1.3 billion for the renewal of New Jersey’s higher education infrastructure.

COMPONENT UNITS

In accordance with the requirements of GASB Statement No. 14, *The Financial Reporting Entity*, this CAFR for fiscal year ended June 30, 2013 includes the accounts of twenty-one public authorities and twelve State colleges and universities. Public authorities are legal, separate entities that are not operating departments of the State. Governing boards are vested with the power to independently manage and set policies for the organization. Each component unit is established for a specific purpose for the benefit of the State’s citizenry. GASB Statement No. 14 provides that the State’s financial statements should emphasize the primary government and permit financial statement users to distinguish between the primary government and its component units. As a result, the transmittal letter, Management’s Discussion and Analysis, and the financial statements focus on the primary government of the State and its activities, although information pertaining to the component units is presented. For additional information, please see Note 18 – Component Units.

Executive Order No. 122, signed on July 23, 2004, was established to direct the Board of Directors for each State Authority to create an Audit Committee whose members are to assist in the oversight of the financial reporting and audit processes of the Authority. Each member of the Audit Committee is independent of the Authority, with at least one member having a background in accounting or related financial expertise. The Audit Committee must assist the Board in retaining an independent auditor to conduct an audit. The auditor selection process must be based on public, competitive bidding principles and shall take place no less than once every five years. In order to ensure the independence of the auditor selection process, an evaluation committee shall be established by the Board to conduct the solicitation and evaluation of eligible auditors. The auditor selected shall report directly to the Audit Committee or the Board. At no time shall the auditor report to any staff member of the Authority. At least twice a year, the Audit Committee shall hold a private meeting with the auditor. In carrying out these duties, the Audit Committee shall proactively assist the Board in overseeing the integrity and quality of the Authority’s financial statements, the Authority’s compliance with legal, regulatory, and ethical requirements, the auditor’s performance and ability to perform, and the performance of the Authority’s own internal audit and internal control functions.

NEW JERSEY’S ECONOMIC CONDITION

The State and nation have continued their recovery. Job gains in the State were brisk in the first half of 2013, but a sharp drop from November and December reversed much of the growth seen earlier in the year. Nonetheless, December was the 28th consecutive month in which the number of jobs in New Jersey was higher than one year earlier. Moreover, the average number of jobs in New Jersey in 2013 was 1.6 percent higher than the 2012 average, which equaled the national increase. New Jersey’s unemployment rate has moved down substantially, dropping from 9.7 percent in August 2012 to 7.3 percent in December 2013. New Jersey’s unemployment rate decline started later than the nation’s since, in contrast to the experience elsewhere, the State’s labor force participation rate rose over the course of 2012. Over the last year the State’s labor force participation rate has fallen, allowing the improved job trend to show through to a decline in unemployment. Personal income of state residents has continued to trend up, with new record highs set in both the second and third quarters of 2013. In the third quarter the annual rate of personal income earned by state residents exceeded \$500 billion for the first time.

The economic outlook for the nation remains problematic. Federal tax and spending policy is currently exerting downward pressure on demand, reflecting the tax increases effective at the start of 2013 and ongoing cuts in spending on goods and services. The roll-out of the Affordable Care Act and the changes in financial regulation and supervision mandated by the Dodd-Frank Act continue to fuel household and business uncertainty. European economies are weak and growth has moderated in China which are factors that would work to reduce foreign demand for U.S. products while increasing competition for U.S. producers. However, state and local finances are showing some signs of recovery, possibly allowing for some expansion in spending and employment by states and municipalities. Consumer spending on big-ticket items such as automobiles has continued to rise, helped in part by the marked recovery in household wealth, and homebuilding and sales have recovered somewhat and home prices have firmed. Inflation measures remain very low.

As unemployment stays high and capacity utilization remains low, underlying inflation is expected to be low and is not likely to be a serious concern until after spending and employment growth move higher. Enhanced availability of credit, continued improvement in financial market stability, and gains in consumer and business confidence continue to be critical factors necessary for a more pronounced economic turnaround in the nation and in New Jersey.

New Jersey is subject to many of the same forces as the nation. The recovery process from Superstorm Sandy will continue to affect the State; the expectation is that as time passes the rebuilding process will provide some noticeable stimulus. Looking forward, the economic expansion in the nation and the State looks to be ongoing. Longer-term interest rates moved up somewhat in the middle part of 2013 as markets anticipated the December 18, 2013 announcement by the Federal Reserve that it will reduce its volume of monthly purchases of securities. However, the Federal Reserve has also made it clear that such reductions will not immediately lead to a more fundamental tightening of policy, and the transition in Federal Reserve leadership will likely not mean significant change in its policies.

New Jersey's housing sector is on the path to recovery. 2013 saw a 34.9 percent increase in the number of permits granted in the State. Home resales have also increased substantially, and prices have begun to move up somewhat. Motor vehicle sales continue to grow, with purchases of new cars in 2013 9.5 percent higher than in 2012.

New Jersey payroll employment is anticipated to average about 1.2 percent higher in 2014 than in 2013 and grow another 2.1 percent in 2015. The unemployment rate is expected to average 7.0 percent in 2014 and 6.3 percent in 2015. Personal income is expected to grow around 3.9 percent in 2014 and 4.7 percent in 2015.

BUDGET AND ACCOUNTING

Legal Level of Control

The State's annual Appropriations Act includes the General Fund, as well as certain Special Revenue Funds (Casino Control, Casino Revenue, Gubernatorial Elections, and Property Tax Relief). The departments maintain legal control at the appropriation line item level and exercise budgetary control by individual appropriations and allocations within annual appropriations to various programs and major expenditure objects. Program classifications represent a lower level operating program function, consisting of closely related activities with identifiable objectives or goals. Revisions to the annual Appropriations Act, reflecting program changes or interdepartmental transfers of an administrative nature, may be effected during the budget year with certain Executive and Legislative Branch approvals. Language, located in the "General Provisions" section of the State's annual Appropriations Act, enables management to amend a department's budget with approval by the Director of the Office of Management and Budget; under specific conditions, additional approval by the Office of Legislative Services is required. Only the State Legislature, however, may transfer appropriations between departments.

Accounting Systems

The Office of Management and Budget directs and supervises a central accounting system, which maintains all accounting records for the various State departments. The State's annual budget provides individual appropriations to departments for specific programs and purposes, while component units maintain separate accounting systems.

To ensure expenditures do not exceed appropriations and allocations, the State employs encumbrance accounting. Purchase orders, contracts, and other commitments involving monetary expenditures are encumbrances. Any unencumbered and unexpended non-continuing appropriations lapse at fiscal year's end.

Consideration as to the adequacy of internal controls is paramount in developing and maintaining the State's accounting system. Internal accounting controls are designed to provide reasonable assurance regarding the safeguarding of assets against loss from unauthorized use or disposition, and guarantee 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 the evaluation of costs and benefits requires managerial estimates and judgments. All internal control evaluations occur within this framework.

RELEVANT FINANCIAL POLICIES

The New Jersey State Constitution, which mandates an annual balanced budget, directs, in part, that no money shall be drawn from the State Treasury but for appropriations made by law and that no law appropriating money for any State purpose shall be enacted if the appropriations contained therein, together with all prior appropriations made for the same fiscal period, shall exceed the total amount of the revenue on hand and anticipated to be available to meet such appropriations during such fiscal period, as certified by the Governor. Accordingly, during the fiscal year, the State may have to make several revenue and expenditure adjustments to ensure a positive fund balance. The State has had a balanced budget in every fiscal year since the adoption of the State Constitution in 1947.

Created as a “rainy day fund,” the Surplus Revenue Fund is part of the General Fund’s resources and fund balance, and accounts for excess revenues from prior fiscal years that are reserved legislatively and may be used to support current year’s appropriations 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. The Surplus Revenue Fund was designed to build fund balance during economic upswings, and to be expended during economic downturns and emergency situations. Such an example occurred during Fiscal Year 2009 when, in response to the national recession, the State drained its entire Surplus Revenue Fund to help balance its budget. As of June 30, 2013, this Fund continued to have a zero balance.

The State employs a budgetary basis of accounting for all of its annual fiscal transactions. The budgetary basis differs from the GAAP basis, which is used to present fund financial statements, in that the former: 1) recognizes encumbrances as expenditures, 2) recognizes all federal revenues related to such encumbrances, and 3) reflects only current fiscal year transactions. The GAAP basis also requires that certain grants and other financial assistance be recorded as revenues and/or expenditures.

FINANCIAL TRENDS

Revenue History

Although State-budgeted Fiscal Year 2013 revenue collections of \$30.9 billion were almost \$1.7 billion less than those collected in pre-recession Fiscal Year 2008, there was a measurable improvement of \$1.8 billion when compared to Fiscal Year 2012 revenue collections. In comparison to Fiscal Year 2008, Gross Income Tax collections in Fiscal Year 2013 were \$496.9 million less; however, they also showed a marked increase of \$980.2 million in comparison to Fiscal Year 2012. With the current Fiscal Year 2014 revenue estimate projected to be \$32.8 billion, the State’s economic recovery trend remains optimistic. The Statistical Section provides a ten-year history of State-budgeted revenue collections.

Pension and Other Postemployment Benefits (OPEB) Obligations

Pursuant to P.L. 2010, c.1, the State resumed making contributions to the pension plans on a phased-in basis over a seven-year period beginning in Fiscal Year 2012. Previously, the State had not fully funded its various pension plans for several years, and its post-retirement medical program is funded on a pay-as-you-go basis. This continued underfunding on an actuarial basis has led to the State’s current net pension obligation of \$14.5 billion and a net OPEB obligation of \$20.2 billion based on the current actuarial valuations which are as of July 1, 2012. The total unfunded actuarial accrued liability (UAAL) for State and local pension plans was \$47.2 billion as of June 30, 2012, or an increase of \$5.5 billion from June 30, 2011. The increase in the UAAL is mainly attributable to expected actuarial losses and the State’s pension contribution of 2/7th of the actuarially required amount being less than the full actuarially required amount. This increase would have been larger except for the impact of P.L. 2011, c. 78 which suspended additional cost of living adjustment (COLA) increases for current and future retirees, and the investment return of 11.78% being higher than the assumed rate of 7.90%. The total State and local OPEB unfunded actuarial accrued liability at June 30, 2012 was \$63.9 billion, or an increase of \$3.8 billion from the prior year. For updated information, Fiscal Year 2012 actuarial reports can be accessed via: <http://www.state.nj.us/treasury/pensions/actuarial-rpts.shtml>.

AUDIT INFORMATION

The principal auditor of the State's reporting entity is the Office of the State Auditor, which resides in the Legislative Branch of State government. The State Auditor's examination was conducted in accordance with generally accepted auditing standards and its opinion precedes the Basic Financial Statements. Private sector public accounting firms have been used for the audits of separately issued component units and college and university financial statements. In addition, the Office of the State Auditor conducts periodic financial and expanded scope audits of various State agencies.

Additional information regarding the State's financial status, including prior year budgets, appropriations acts, and financial reports, is available on the State's web site (<http://www.state.nj.us/treasury/omb/>).

CERTIFICATE OF ACHIEVEMENT FOR EXCELLENCE IN FINANCIAL REPORTING

The GFOA awarded the Certificate of Achievement for Excellence in Financial Reporting to the State of New Jersey for its CAFR for the fiscal year ended June 30, 2012. In order to qualify for this certificate, a governmental entity must publish an easily readable and efficiently organized comprehensive annual financial report, of which the contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. The State of New Jersey has received this award every year since 1993.

ACKNOWLEDGEMENTS

Finally, we express our grateful appreciation to the many dedicated professionals in the Office of Management and Budget and the Office of the State Auditor, whose work made possible the preparation of this report. We believe 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,



Andrew P. Sidamon-Eristoff
State Treasurer



Charlene M. Holzbaur
Director, Office of Management and Budget



Government Finance Officers Association

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, 2012

Executive Director/CEO

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