NEW JERSEY

COMPREHENSIVE
ANNUAL FINANCIAL REPORT
FISCAL YEAR ENDED JUNE 30, 1998

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STATE OF NEW JERSEY
COMPREHENSIVE ANNUAL FINANCIAL REPORT
FISCAL YEAR ENDED JUNE 30, 1998
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Introduction

Indian King Tavern

Photograph by Hoag Levins

A Delaware Valley landmark, the **Indian King Tavern** in Haddonfield, NJ, celebrates its 250th anniversary in the year 2000. When the foundations of the building were laid in 1750, Virginian Thomas Jefferson was seven years old. George Washington was an adventurous 18-year-old, mapping parts of the Blue Ridge Mountains. Haddonfield was a way station along the Kings Road through the heavily-forested colony of New Jersey.

In 1777, the General Assembly of New Jersey had to evacuate Trenton as that capital city was enveloped in battles between the Continental and British armies. The legislators fled south and reconvened in this second-floor meeting room of the Indian King Tavern in Haddonfield. Here, the status of New Jersey was legally changed from that of a colony to that of a free state in an independent union. The Great Seal of New Jersey was also created and adopted during the same sessions.

State of New Jersey

DEPARTMENT OF THE TREASURY
OFFICE OF MANAGEMENT AND BUDGET
PO BOX 221
TRENTON NJ 08625-0221

CHRISTINE TODD WHITMAN
Governor

JAMES A. DIELEUTERIO, JR.
State Treasurer

October 30, 1998

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, 1998. 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 presented in this report, the State ended the year in a sound fiscal position, with an Undesignated Fund Balance (surplus) of $1.3 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 organized 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 1997 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 Governmental 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.

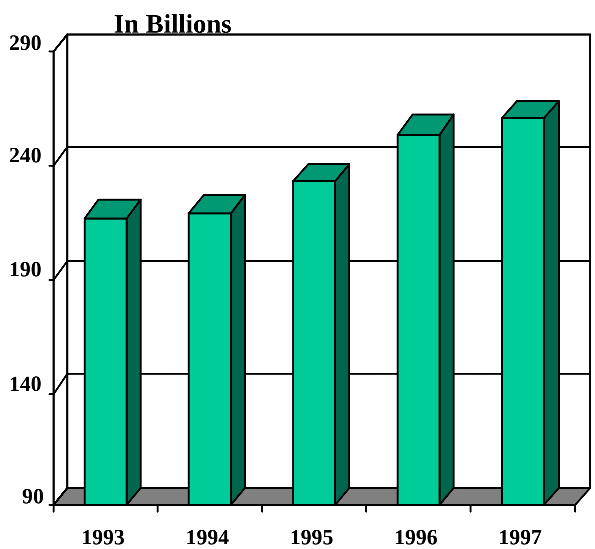
The accounting records of the various State departments are maintained on a central accounting system. The operations of this system are directed and supervised by the Office of Management and Budget. Separate accounting systems are maintained by those component units of government that are included 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.

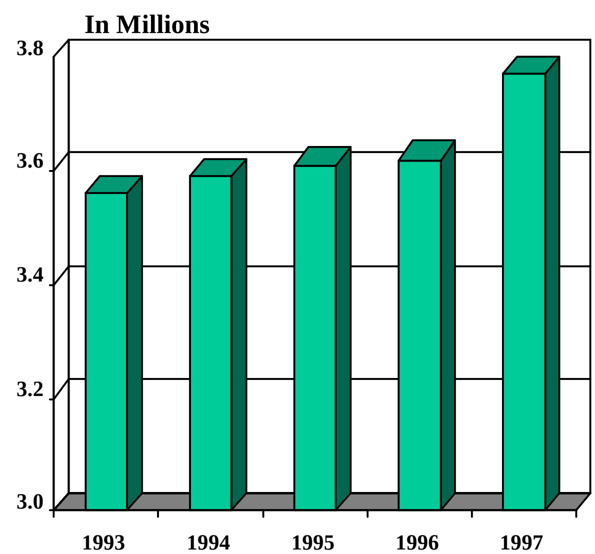
ECONOMIC CONDITION

The New Jersey economy in Calendar Year 1997 continued its positive growth trend. Employment and income growth became stronger as the year progressed. For the year, retail sales grew by 5.6 percent and total employment expanded by 2.3 percent. As demonstrated in the chart below, the State experienced employment growth of 2.3 percent driving employment to a level of 3.77 million, while personal income grew by 4.9 percent. This represents the third year of growth in excess of 4.7 percent.

New Jersey Personal Income
1993 - 1997



New Jersey Employment
1993 - 1997



It is expected that the New Jersey economy in Calendar Years 1998 and 1999 will continue to grow at a moderate pace with little or no inflation. High levels of employment, steady income growth, and low interest rates will continue to support consumer and business spending. 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. Employment is projected to grow by 2.0 percent in 1998 before easing in 1999 to 0.9 percent. Personal income growth is expected to remain between 4.7 percent and 5.0 percent. Retail sales will continue to increase at a slightly lower rate. Real New Jersey Gross State Product, the most complete measure of economic activity, experienced a 4.0 percent increase in 1997 and is projected to experience increases in 1998 and 1999, although at a slower rate.

FISCAL YEAR 1998 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 1998 revenue collections totaled $17.1 billion, $977.5 million above Fiscal Year 1997 revenue. Revenue changes in the State's three major taxes over Fiscal Year 1997 levels were as follows: the Sales Tax increased by $350.8 million or 7.9 percent, the Gross Income Tax increased by $765.2 million or 15.9 percent, and the Corporation Business Tax decreased by $54.8 million or 4.3 percent. Overall, Fiscal Year 1998 revenue growth for the State's three major taxes totaled $1,061.2 million. Increased revenue over Fiscal Year 1997 levels reflect the higher level of employment within the State as evidenced by the large increase in Gross Income Tax and Sales Tax revenues. Income tax collections were also driven higher by the combined effects of strong growth in the financial markets and a large one-time impact from the reduction in the Federal capital gains tax rate. Continued enhanced collection efforts by the New Jersey Division of Taxation also enabled the State to collect from delinquent taxpayers.

Collections for the State's three major taxes, as a percentage of Fiscal Year 1998 total receipts, were as follows: the Gross Income Tax represented 32.6 percent; the Sales Tax equaled 27.8 percent; and the Corporation Business Tax represented 7.2 percent. The State's three major taxes represented 67.6 percent of Fiscal Year 1998 total receipts, as compared to 65.2 percent for Fiscal Year 1997. Even with major reductions in tax rates, the total revenues have grown over the past four years by $2.2 billion.

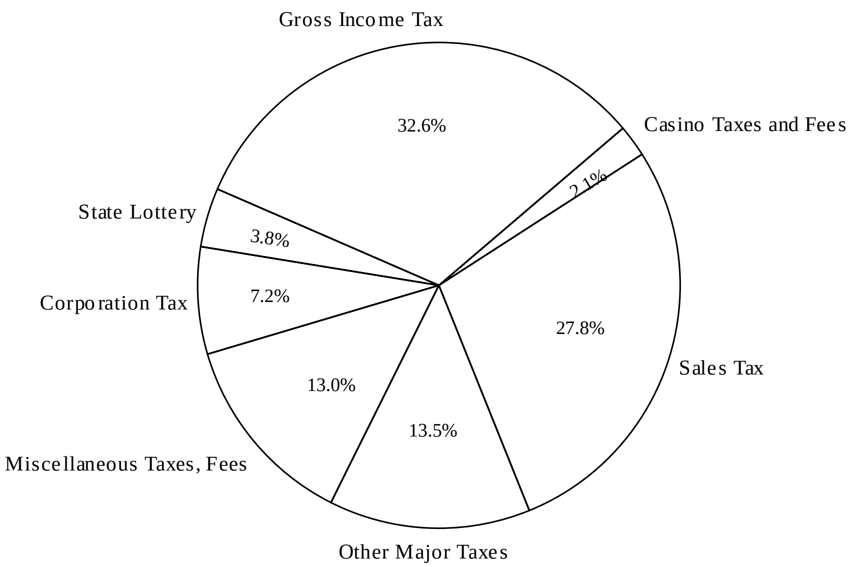
REVENUE SUMMARY BY MAJOR TAX
1994-1998
(Expressed in Millions)

	1998	1997	1996	1995	1994
Gross Income Tax	$ 5,590.6	$ 4,825.4	$ 4,733.8	$ 4,540.0	$ 4,493.6
Sales Tax	4,766.2	4,415.4	4,318.3	4,133.3	3,778.5
Other Major Taxes	2,305.0	2,297.2	2,276.1	2,215.4	2,263.8
Miscellaneous Taxes, Fees	2,226.4	2,320.9	2,121.1	2,016.8	2,446.2
Corporation Tax	1,231.6	1,286.4	1,171.5	1,085.5	1,063.1
State Lottery	642.8	650.0	662.1	647.8	602.8
Casino Taxes and Fees	369.8	359.6	358.6	355.4	319.8
Total	$ 17,132.4	$ 16,154.9	$ 15,641.5	$ 14,994.2	$ 14,967.8

REVENUE COMPARISONS

Source of Revenue ($000)	Fiscal Year 1998	Fiscal Year 1997	Increase/Decrease Amount	Percent
Gross Income Tax	$ 5,590,579	$ 4,825,411	$ 765,168	15.9
Sales Tax	4,766,195	4,415,428	350,767	7.9
Other Major Taxes	2,304,982	2,297,155	7,827	0.3
Miscellaneous Taxes, Fees	2,226,410	2,320,852	(94,442)	(4.1)
Corporation Tax	1,231,629	1,286,447	(54,818)	(4.3)
State Lottery	642,830	650,025	(7,195)	(1.1)
Casino Taxes and Fees	369,806	359,561	10,245	2.8
	$ 17,132,431	$ 16,154,879	$ 977,552	6.1

FISCAL YEAR 1998
MAJOR REVENUE CATEGORY COLLECTIONS
AS A PERCENT OF TOTAL REVENUE COLLECTIONS



FISCAL YEAR 1998 REVENUE SUMMARY:
PERCENT DISTRIBUTION OF REVENUE COLLECTIONS

Gross Income Tax	32.6%
Sales Tax	27.8
Other Major Taxes	13.5
Miscellaneous Taxes, Fees	13.0
Corporation Tax	7.2
State Lottery	3.8
Casino Taxes and Fees	2.1
Total	**100.0**%

FISCAL YEAR 1998 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 based upon the annual Appropriations Act are divided 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 and supports the operation of the State's departments, the Executive Office, several commissions, the State Legislature, and the Judiciary. 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.

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, support for the State colleges and universities, 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 1998	Fiscal Year 1997	Increase/Decrease Amount
State Aid	$ 6,847,567	$ 6,336,564	$ 511,003
Direct State Services	5,343,201	5,125,821	217,380
Grants-in-Aid	4,047,224	4,053,380	(6,156)
Debt Service	478,894	446,901	31,993
Capital Construction	496,982	373,318	123,664
	$ 17,213,868	$ 16,335,984	$ 877,884

Fiscal Year 1998 Expenditures

Fiscal Year 1998 expenditures of $17.2 billion are $877.9 million more than the expenditures of the prior fiscal year.

State Aid represented 39.8 percent of total Fiscal Year 1998 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.

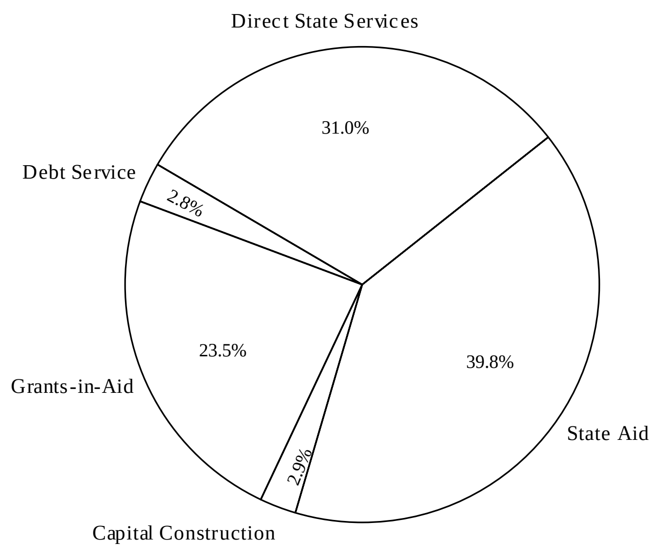
Direct State Services accounted for 31.0 percent of total Fiscal Year 1998 expenditures. Direct State Services expenditures increased between Fiscal Year 1998 and Fiscal Year 1997 by $217.4 million.

Grants-in-Aid accounted for 23.5 percent of total Fiscal Year 1998 expenditures. This is a $6.2 million decrease from the prior fiscal year.

Debt Service represented 2.8 percent of total Fiscal Year 1998 expenditures. Debt Service expenditures increased by $32.0 million.

Capital Construction represented 2.9 percent of total Fiscal Year 1998 expenditures. Construction for capital projects grew by $123.7 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 1998 EXPENDITURES BY MAJOR EXPENDITURE CATEGORY



EXPENDITURE DOLLAR
Fiscal Year 1998

State Aid	39.8%
Direct State Services	31.0
Grants-in-Aid	23.5
Debt Service	2.8
Capital Construction	2.9
Total	**100.0%**

The following table details expenditures by department for Fiscal Year 1998:

EXPENDITURES BY DEPARTMENT
STATE FUNDS
(Thousands of Dollars)

Department	State Aid	Direct State Services	Grants In-Aid	Debt Service	Capital Construction	Total
Legislative	$ --	$ 53,853	$ --	$ --	$ 91	$ 53,944
Executive		5,046	--	--	--	5,046
Judicial		365,755	-9	--	--	365,746
Agriculture	7,004	10,232	1,506	--	386	19,128
Banking & Insurance	--	40,143	--	--	--	40,143
Commerce & Economic Dev.	4,721	20,342	15,310	5,097	253	45,723
Community Affairs	875,650	29,785	44,549	--	--	949,984
Corrections	--	691,975	106,169	--	3,383	801,527
Education	5,297,364	35,765	4,395	--	1,880	5,339,404
Environmental Protection	9,242	203,114	360	82,694	73,071	368,481
Health and Senior Services	20,861	48,349	1,031,848	--	1,115	1,102,173
Human Services	376,431	623,665	2,064,659	--	8,240	3,072,995
Labor	--	70,313	25,858	--	--	96,171
Law & Public Safety	4,978	417,495	13,433	--	3,267	439,173
Military & Veterans' Affairs	--	57,294	995	--	2,239	60,528
Personnel	--	27,545	--	--	--	27,545
State & Public Defender	15,112	821,943	50,896	--	7,280	895,231
Transportation	22,227	180,011	165,767	--	380,322	748,327
Treasury	213,977	256,737	521,488	391,103	7,015	1,390,320
Miscellaneous	--	2,770	--	--	2	2,772
Inter-Departmental	--	1,381,069	--	--	8,438	1,389,507
Total	**$ 6,847,567**	**$ 5,343,201**	**$ 4,047,224**	**$ 478,894**	**$ 496,982**	**$ 17,213,868**

FUND BALANCES

The State ended Fiscal Year 1998 with an undesignated fund balance of $1.3 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 Appropriations Act anticipation. The following table presents a comparison of the components of the undesignated fund balances at the end of Fiscal Year 1998 and Fiscal Year 1997:

Fund	Fiscal Year 1998	Fiscal Year 1997	Increase/Decrease
General Fund	$ 228,263,668	$ 280,576,653	$ (52,312,985)
Surplus Revenue Fund	534,109,930	388,377,360	145,732,570
Property Tax Relief Fund	494,937,261	439,041,694	55,895,567
Casino Revenue Fund	--	--	--
Total	$ 1,257,310,859	$ 1,107,995,707	$ 149,315,152

Fiscal Year 1999 Revenue Projections

The Fiscal Year 1999 revenue projections are based on estimates of moderate overall economic growth and a normal level of growth in capital gains. Total resources are projected at $17.7 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. For Calendar Year 1998, the property tax deduction will increase to $10,000 or a $50 credit. The State’s three major taxes are expected to comprise 65.4 percent of the Fiscal Year 1999’s total resources and 69.6 percent of total revenue.

Fiscal Year 1999 Appropriations

The total Fiscal Year 1999 appropriation is $18.1 billion. Of the $18.1 billion appropriated in Fiscal Year 1999 from the General Fund, the Property Tax Relief Fund, the Casino Control Fund, the Casino Revenue Fund and the Gubernatorial Elections Fund, $7.5 billion (41.4%) is appropriated for State Aid to Local Governments, $4.9 billion (27.1%) is appropriated for Grants-in-Aid, $4.6 billion (25.4%) for Direct State Services, $0.5 billion (2.8%) for Debt Service on State General Obligation Bonds, and $0.6 billion (3.3%) for Capital Construction.

State Aid represents the largest portion of Fiscal Year 1999 appropriations. In Fiscal Year 1999, $7.5 billion will be distributed to municipalities, counties, and school districts. Major State Aid programs are: Aid to School Districts ($5,925.5 million), Unrestricted Aid to Municipalities and Counties ($869.0 million), Aid to Municipalities and Counties for Human Services programs ($333.0 million), and Aid to County Colleges ($159.8 million).

The Grants-in-Aid represent the second largest portion of the State’s Fiscal Year 1999 appropriation. In Fiscal Year 1999, $4.9 billion has been appropriated. 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 ($2,067.9 million), Higher Education ($1,044.4 million), Health and Senior Services programs ($755.4 million), Homestead Rebates ($323.6 million), and Public Transportation ($194.3 million).

The Direct State Services Fiscal Year 1999 appropriation is $4.6 billion. These funds support the operating costs of the Executive Departments, the Judiciary and the State Legislature. The largest appropriations are for the following departments: Corrections ($700.2 million), Human Services ($565.7 million), and Law and Public Safety ($317.6 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 1999 total $0.6 billion. Of this amount, $463.7 million is the appropriation to the New Jersey Transportation Trust Fund Authority, $47.2 million is for hazardous substance remediation and underground tank remediation, and $15.0 million is for shore protection.

SERVICE EFFORTS AND ACCOMPLISHMENTS

The following sections highlight various service efforts and accomplishments the State has achieved during Fiscal Year 1998 as well as some of the goals the State hopes to achieve for Fiscal Year 1999.

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, 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 the Department of Human Services for the Work First New Jersey Program. The current overall gross cost of the programs now under Work First New Jersey 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, however, to provide for contingencies, a reserve fund of $46 million was established at the end of Fiscal Year 1998. 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 received prior to the reform measures.

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. The Department of Transportation, with the consent of the State Legislature, utilized these savings by increasing its Fiscal Year 1998 capital program by $200 million. This one-time initiative was 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 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.

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 are subject to the State's Corporation Business Tax. The State's existing Sales and Use Tax, with certain exceptions, are 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 were 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 had been supplemented in recent years by excess revenue.

State School Aid to local districts in Fiscal Year 1998 totaled $5.297 billion; this included $4.724 billion in direct aid and an additional $573.3 million in aid to local districts for the employers' share of teachers' pensions and social security payments. The key item of funding was Core Curriculum Standards Aid, which is geared to support the newly adopted core curriculum standards. This includes 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 total ($2.449 billion) was distributed based on a measure of local districts' property wealth and per capita income. Core Curriculum Standards Aid represented approximately 53 percent of the formula aid amount distributed in Fiscal Year 1998.

The net increase of $445.9 million in the State School Aid appropriations for Fiscal Year 1998, includes significant funding for new initiatives including $288.0 million for Early Childhood Education, $175.0 million for Demonstrably Effective Programs, and $50.4 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 $246.2 million was added to the Budget to provide additional parity aid to these districts. On May 21, 1998, the State Supreme Court accepted the State's plan to use a nationally acclaimed reading-based program called "Success for All" and other "whole-school reforms" to assure the "thorough and efficient" education required by the State constitution.

The State successfully completed the refinancing of its pension obligations at the end of Fiscal Year 1997. This was accomplished through the issuance of pension obligation bonds that were used to finance the former unfunded accrued liability. The Pension Security Plan of 1997 resulted in significant cost avoidance for Direct State Services, State Aid, and local employers participating in the Public Employees Retirement System and Police and Firemen's Retirement System. The following chart reflects combined actual and projected savings of normal and unfunded accrued liability contributions for these three groups from Fiscal Year 1997 through 1999. The total cost avoidance for this period is in excess of $1.0 billion.

Pension Security Plan Cost Avoidance
for Direct State Services, State Aid and Local Employers
($ in millions)

	Fiscal 1997	**Fiscal 1998**	**Fiscal 1999**	**Fiscal 97-99**
Direct State Services and State Aid:				
Normal Contributions	$ 193	$ 348	$ 218	$ 759
Unfunded Accrued Liability Contributions	60	---	---	60
Direct State Services and State Aid Cost Avoidance	253	348	218	819
Local Pension Contribution Savings	---	66	129	195
Total Pension Security Plan Cost Avoidance	$ 253	$ 414	$ 347	$1,014

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. The total dedicated for Fiscal Years 1997 and 1998 from the Corporation Business Tax revenues was $88.3 million.

Fiscal Year 1999

State School Aid to local districts in Fiscal Year 1999 totals $5.926 billion, an increase of $602.1 million. A new $50.0 million appropriation for a school construction and renovation fund is included. This fund is supported through the dedication of a portion of the $.40 increase per pack in the cigarette tax.

The total for formula aid programs is $4.890 billion, including $2.747 billion for core curriculum standards aid, $647.9 million for special education, $302.5 million for early childhood aid, and $261.1 million for pupil transportation aid. There is an appropriation of $917.4 million for the employer's share of teachers' pensions and social security payments.

The closure of the Marlboro Psychiatric Hospital and the North Princeton Developmental Center has enabled $70.9 million to be reallocated from these institutions to community programs for the mentally ill and the developmentally disabled.

Funding in the amount of $50.0 million is included for an Open Space Local Matching Program in Fiscal Year 1999. Counties and municipalities with open space taxes and funding programs will be eligible to receive state matching funds. These funds will support the purchase of open space and the preservation of farmland. The goal is to save 300,000 acres of open space during the next four years and one million acres over the next decade. A stable funding source for New Jersey's natural resources and farmland preservation efforts was established through the enactment of legislation this summer that dedicates $98.0 million of sales tax revenues for this purpose beginning in Fiscal Year 2000, subject to voter approval.

Funding in the amount of $25 million has been appropriated to redevelop abandoned properties. Under the program, the State will assist local governments, non-profit groups, and private developers in acquiring title to properties needed for viable redevelopment plans. This program is leveraged with $300 million in bonds arranged through the New Jersey Economic Development Authority (EDA) and $100 million from the New Jersey Housing and Mortgage Finance Agency (HMFA).

There is a $47.6 million appropriation for KidCare, a program that provides health insurance for children whose parents cannot afford to purchase it. An extensive outreach plan is being initiated to increase the number of children in the program.

New Jersey has had the fastest growing economy in the Mid-Atlantic region for the past three years. To ensure the continuation of New Jersey's superior economic performance, the State has created the New Jersey Commerce and Economic Growth Commission. This independent Commission will have the flexibility to tailor economic development programs to the changing needs of New Jersey's businesses. The new Commission will be better positioned to take advantage of emerging economic growth opportunities than its predecessor, the Department of Commerce and Economic Development. Through its market-driven, results-oriented approach, the Commission will quickly respond to new opportunities by reallocating resources and finding the best people for the task. As an autonomous entity, the Commission will have greater opportunity to bring private sector resources to bear on its efforts to encourage investment and expansion. Major programs of the Commission will include: business attractions, business retention and expansion, international trade, small business and minority owned business development, and urban enterprise zones.

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

Casino Reinvestment Development Authority
Hackensack Meadowlands Development Commission
New Jersey Building Authority
New Jersey Development Authority For Small Business, Minorities
And Women's Enterprise
New Jersey Economic Development Authority
New Jersey Educational Facilities Authority
New Jersey Environmental Infrastructure Trust
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 Transportation Trust Fund Authority
New Jersey Turnpike Authority
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
Kean University of New Jersey (formerly Kean College of New Jersey)
Montclair State University
New Jersey City University (formerly Jersey City State College)
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 $3.3 billion, respectively, for Fiscal Year 1998. Total operations along with other financing sources and uses contributed to a total combined fund balance at fiscal year end of $12.9 billion.

For Fiscal Year 1998, combined revenues for the state colleges and universities were $2.6 billion. Combined expenditures totaled $3.2 billion. Total operations along with other financing sources and uses contributed to a total combined fund balance at fiscal year end of $3.3 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, 1998, the general fixed assets of the State amounted to $2.5 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, 1998, outstanding General Obligation Debt totaled $3.6 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, 1998, outstanding Certificates of Participation totaled $103.4 million and the State's outstanding balance on its line of credit totaled $25.4 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 $1.8 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 1998, the State issued $800 million in commercial paper. The entire amount was retired on June 15, 1998.

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
1998	$ 1.5	$ 3.6
1997	1.9	3.4
1996	1.6	3.7
1995	1.5	3.6
1994	1.4	3.6

As of June 30, 1998, 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 Investment 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 Investment 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 Investment 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, 1998, the New Jersey Cash Management Fund's average daily annualized rate of return for participating state accounts was 5.56 percent. For "Other-than-State" participants the average daily annualized rate of return, which includes charges for administrative and operating expenses, was 5.41 percent for the fiscal year ended June 30, 1998.

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.

YEAR 2000

A major challenge confronting most government officials is the Year 2000 data processing problem. In order to address this problem and ensure the continuation of government operations into the Year 2000 and beyond, the State established a committee to work with the departments to identify and address Year 2000 renovation efforts and funding needs. A moratorium was imposed in February 1998 on all non-Year 2000 related data processing activities to ensure availability of resources for Year 2000 compliance.

The State Office of Information Technology and the various departments are utilizing both in-house and vendor resources in renovating lines of code and in-house applications. While there can be no guarantee that all the State's mission-critical and high-priority computer systems will be Year 2000 compliant, the State is concentrating efforts so that there will not be an adverse impact upon State operations or State finances as a result. As of June 30, 1998, the testing, validation, and implementation phases of approximately 55 percent of all critical centrally maintained systems are completed. For a more complete description of this matter, refer to Note 21 in the General Purpose Financial Statements.

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 units 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, 1997.

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, 1997

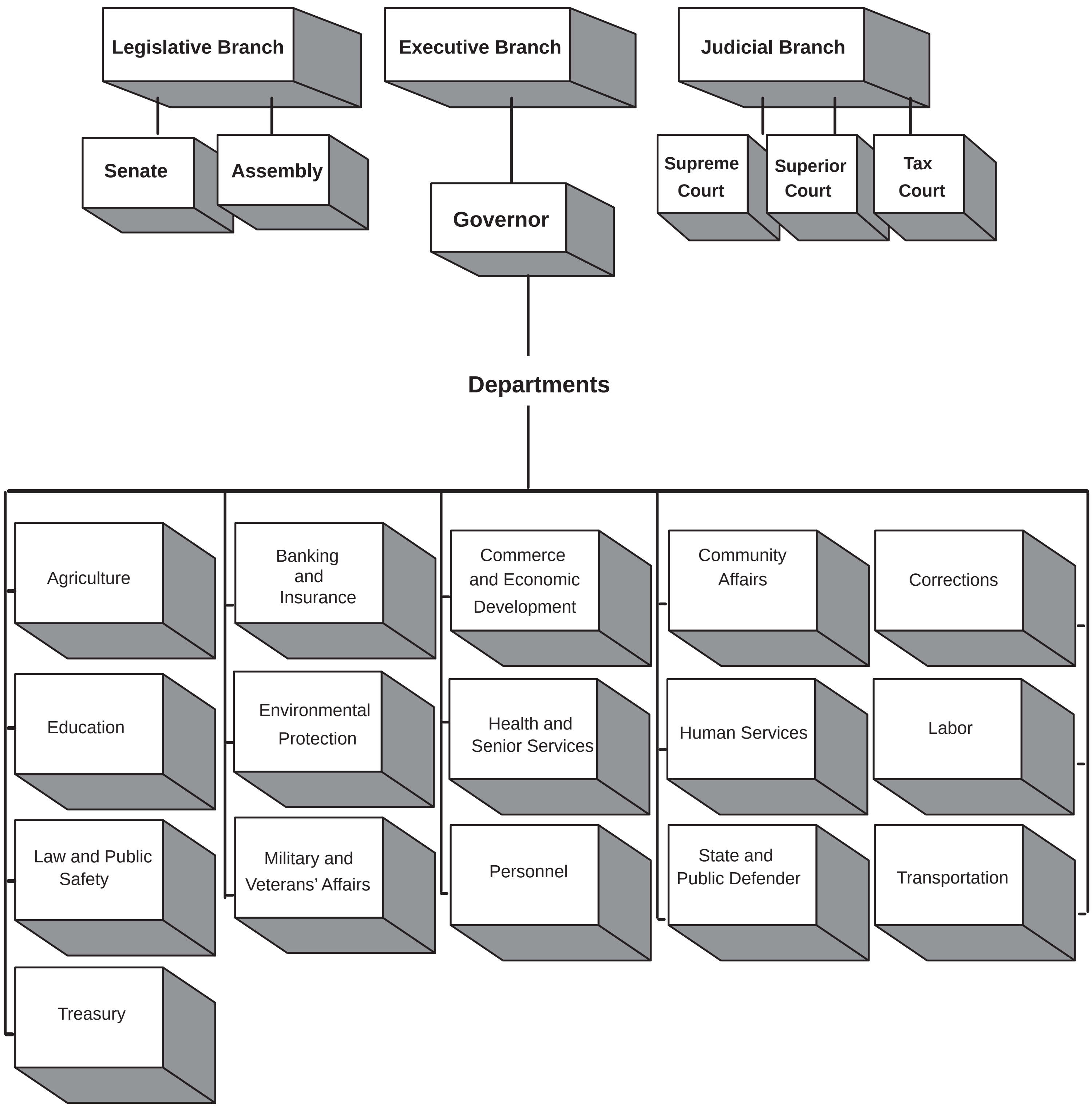
A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards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

GOVERNMENT FINANCE OFFICERS ASSOCIATION OF THE UNITED STATES AND CANADA CORPORATION SEAL CHICAGO

Douglas R Ellsworth
President

Jeffrey L. Esser
Executive Director

ORGANIZATION OF NEW JERSEY STATE GOVERNMENT



Financial

The William Trent House was built on a settlement known as Trent's Town named by the owner. Built in 1719 the classic Georgian house looks much today as it did when it was first constructed. As you walk through the building, you are drawn back to a time when Trenton was a wilderness tied closely to the Delaware River.

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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 R. 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, 1998, as listed in the table of contents. 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 the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit 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, 1998, and the results of its operations and cash flows of the nonexpendable trust funds and the proprietary fund type authorities for the year then ended in conformity with generally accepted accounting principles.

As discussed in note 2A, the State has adopted Statements 31 and 32 of the Governmental Accounting Standards Board. Implementation of Statement 31 resulted in a change from reporting investments at cost to reporting investments at fair value. As a result of implementing Statement 32, the New Jersey State Employees' Deferred Compensation Plan, which was previously reported as an agency fund, is being reported as an expendable trust fund in the financial statements.

In accordance with *Government Auditing Standards,* we have also issued our report dated October 30, 1998 on our consideration of the State of New Jersey's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

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 stated 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
October 30, 1998