STATE OF ARIZONA
NOTES TO THE FINANCIAL STATEMENTS
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NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. BASIS OF PRESENTATION

The accompanying financial statements of the State of Arizona (the State) have been prepared in conformity with generally accepted accounting principles (GAAP) applicable to governmental units, except for the State Compensation Fund, which is prepared on a statutory basis of accounting.

The Governmental Accounting Standards Board (GASB) is the standard-setting body for establishing governmental accounting and financial reporting principles. GASB's Codification of Governmental Accounting and Financial Reporting Standards documents these principles. The State's significant accounting policies are as follows:

Amounts in the "Total - Memorandum Only" columns in the accompanying financial statements represent a summation of the combined financial statement line items. These are presented for analytical purposes only. Consequently, amounts shown in the "Total - Memorandum Only" columns are not comparable to a consolidation, and they do not represent the total resources available, total liabilities and fund balances or total revenues and expenditures/expenses of the State. Interfund eliminations have not been made in the aggregation of this data.

All financial information of the reporting entity is for the fiscal year ended June 30, 1999, except for the State Compensation Fund. The State Compensation Fund's financial information is for the calendar year ended December 31, 1998.

B. FINANCIAL REPORTING ENTITY

The accompanying financial statements include financial transactions of all funds, account groups, elected offices, agencies, boards, commissions and authorities. The State has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the State are such that exclusion would cause the State's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the State to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the State.

As required by generally accepted accounting principles, these financial statements present the State of Arizona (the primary government) and its component units. The component units are included in the State's reporting entity because of the significance of their operational or financial relationships with the State.

The State reporting entity does not include counties, municipalities, school districts, community colleges, the Central Arizona Water Conservation District or other political subdivisions of the State over which the State exercises little, if any, financial accountability.

1. Blended Component Units

The following component units have been presented as blended component units because the component units' governing body is substantially the same as the governing body of the State, or the component unit provides services almost entirely to the primary government. Consequently, they are reported as part of the State and blended into the fiduciary funds.

* Arizona State Retirement System (ASRS) - The ASRS is a cost-sharing, multiple-employer, public employee retirement system that provides for retirement, health insurance premium benefits, and death and survivor benefits for employees of the State and employees of participating political subdivisions and school districts. ASRS is governed by a seven-member board that is appointed by the Governor and approved by the Senate to serve three-year terms.

* Public Safety Personnel Retirement System (PSPRS) - The PSPRS is an agent, multiple-employer, public employee retirement system that benefits fire fighters and police officers employed by the State and its political subdivisions. The PSPRS is jointly administered by the Fund Manager and 162 Local Boards. The Fund Manager is a five-member board of which three members are appointed by the Governor and two members are appointed by the State Legislature. All members serve a fixed three-year term. Each eligible group participating in the system has a five member Local Board. All members serve a fixed four-year term.

* Elected Officials' Retirement Plan (EORP) - The EORP is a cost-sharing, multiple-employer, public employee retirement plan that benefits all State and county elected officials and judges (except La Paz County elected officials), and certain elected city officials. The EORP is administered by a five-member board of which three members are appointed by the Governor and two members are appointed by the State Legislature. All members serve a fixed three-year term.

* Corrections Officer Retirement Plan (CORP) - The CORP is an agent, multiple-employer, public employee retirement plan that benefits county detention officers and certain employees of the State's Department of Corrections and Department of Juvenile Corrections. The CORP is jointly administered by the Fund Manager of the PSPRS and 12 Local Boards. The Fund Manager is a five-member board. Three members are appointed by the Governor and two members are appointed by the State Legislature. Each employer participating in the CORP has a five member Local Board. All members serve a fixed four-year term.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. Discretely Presented Component Units

The State Compensation Fund, University Medical Center, the Arizona Power Authority and the Water Infrastructure Finance Authority are component units that are legally separate from the State, but are either financially accountable to the State, and/or the State is able to impose its will on the organizations.

The Component Unit - Proprietary and Fiduciary Fund Types column of the combined financial statements includes the financial data of the University Medical Center, the Arizona Power Authority and the Water Infrastructure Finance Authority. The State Compensation Fund is presented separately because it is reported on a non-GAAP basis. Individual component unit disclosures are reflected throughout the notes to these financial statements. Separately issued independent audit reports may be obtained from the addresses presented below.

* State Compensation Fund - The State Compensation Fund was established by the Legislature for the purpose of insuring employers against liability for workers' compensation; occupational disease compensation; and medical, surgical and hospital benefits. The State Compensation Fund is governed by a board of directors that consists of five members appointed by the Governor for staggered terms of five years and annually the Governor shall appoint a chairman from among the board members. The State is required by statute to review and approve the operating and capital outlay budget of the State Compensation Fund.

  State Compensation Fund
  3031 North 2nd Street
  Phoenix, Arizona 85012
  (602) 631-2000

* University Medical Center (the Center) - The Center is a 365-bed, general acute care, teaching medical facility in Tucson, Arizona. The Center is the primary teaching hospital for the College of Medicine of the University of Arizona. In 1984, the Arizona Legislature passed a bill that enabled the Arizona Board of Regents to convey the Center to a private not-for-profit, tax-exempt corporation. Although an autonomous entity was created, the teaching missions and research alliances with the University of Arizona and the State of Arizona firmly remained with the Center. Appointments of members of the Board of Directors are confirmed by the Arizona Board of Regents. The Arizona Legislature has limited both the number of Regents and the number of State employees allowed to serve on the Board of Directors.

  The University Medical Center
  1650 East Ft. Lowell, Suite 102
  Tucson, Arizona 85719
  (520) 694-2700

* Arizona Power Authority (APA) - The APA purchases the State's allocation of Hoover power and resells it to Arizona entities that are eligible purchasers under federal and state laws. Hoover power is produced by the Bureau of Reclamation at the federally owned Boulder Canyon Project hydropower plant, located near Las Vegas, Nevada. The APA is governed by a commission of five electors appointed by the Governor and approved by the Senate. The term of office of each member is six years and the members select a chairman and vice-chairman from among its membership for two-year terms.

  The Arizona Power Authority
  1810 West Adams Street
  Phoenix, Arizona 85007-2697
  (602) 542-4263

* Water Infrastructure Finance Authority (WIFA) - The WIFA is authorized to administer the Clean Water Revolving Fund and the Drinking Water Revolving Fund. The Clean Water Revolving Fund was created pursuant to the Federal Water Pollution Control Act of 1972, as amended by the Water Quality Act of 1987 (Clean Water Act) which required the State to establish the Fund to accept federal capitalization grants for publicly owned wastewater treatment projects. WIFA has entered into an agreement this year with the Environmental Protection Agency to administer the Drinking Water Revolving Fund pursuant to the Safe Drinking Water Act.. The WIFA is governed by a twelve-member board of directors appointed by the Governor. The directors serve staggered terms of five years.

  The Water Infrastructure Finance Authority
  202 East Earll Drive, Suite 480
  Phoenix, Arizona 85012
  (602) 230-9770

3. Joint Venture

As discussed in more detail in Note 14, the State participates in a joint venture. The State does not include the financial activities of this organization in its financial statements in conformity with GASB Statement 14.

4. Related Organizations

The following related organizations, for which the State appoints a voting majority of their governing boards, are not part of the reporting entity based on the criteria of GASB Statement No. 14 and therefore, financial information pertaining to these entities has not been included.

* Arizona Health Facilities Authority (the Authority) - The Authority was established to issue tax-exempt bonds for the purpose of reducing health care costs and improving health care for Arizona residents by providing less expensive financing for health care institutions. Proceeds from bond issues are loaned to various qualifying nonprofit health care institutions. The health care institutions reimburse the Authority for expenses for issuance of the bonds, pay fees

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

of the Authority, and make payments under the loans for the benefit of the holders of the bonds. The Authority is governed by a seven-member board of directors that is appointed by the Governor and approved by the Senate. The directors serve staggered terms of seven years.

* Social Service Contractors Indemnity Pool (the Pool) - The Pool is a nonprofit corporation that provides property and liability insurance coverage to social service agencies contracted by the State of Arizona. The Pool was capitalized with a one million dollar appropriation from the State, which is reflected as restricted capital in the Pool's financial statements.

* Arizona Technology Development Authority - The Arizona Technology Development Authority was established to stimulate the creation and expansion of technology related business activity, to promote new business growth in the State and provide improved employment opportunities in technology related fields. The Arizona Technology Development Authority is governed by a board of directors that consists of the Governor, the Director of the Department of Commerce, and an additional five members appointed by the Governor. The directors serve staggered terms of five years.

* Arizona International Development Authority - The Arizona International Development Authority was established to facilitate the development of international trade or commerce between this state and other countries. The Arizona International Development Authority is governed by a board of directors consisting of seven members appointed by the governor. The directors serve terms of five years.

C. FUND STRUCTURE

The State uses approximately 1,900 accounting funds. Each accounting fund is a separate accounting entity with its own self-balancing set of accounts that represent its assets, liabilities, fund equity, revenues, and expenditures or expenses, as appropriate. Governmental resources are allocated to and accounted for in individual accounting funds depending upon the purposes for which the State collects revenues or expends resources, and the means by which the State uses to control spending activities. For the purpose of preparing financial statements, the accounting funds have been combined by fund type. Transactions between funds within a fund type, if any, have not been eliminated. Account groups are used to provide accountability for certain assets and liabilities that are not recorded in the funds because they do not directly affect net expendable available financial resources. The four major fund types, two account groups and component units are described below:

1. Governmental Fund Types

The General Fund accounts for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds account for the proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to expenditures for specified purposes.

Debt Service Funds account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs.

Capital Projects Funds account for financial resources used to acquire or construct major capital facilities (other than those financed by Proprietary Funds, Non-Expendable Trust Funds, Pension Trust Funds, University Funds or Component Units).

2. Proprietary Fund Types

Enterprise Funds account for operations (a) financed and operated in a manner similar to private business enterprises, where the State intends that the cost of providing goods or services to the general public be financed or recovered primarily through service charges, or (b) where the State decides that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Internal Service Funds account for the financing of goods and services provided by one State department or agency to other State departments or agencies on a cost-reimbursement basis.

Only those applicable FASB Statements and Interpretations, APB Opinions, and ARBs issued on or before November 30, 1989, are applied unless those pronouncements conflict with or contradict GASB pronouncements.

3. Fiduciary Fund Types

Expendable Trust Funds account for assets held by the State in a trustee capacity, where principal may be expended in the course of the funds' designated operations.

Non-Expendable Trust Funds account for assets held by the State in a trustee capacity, where the State must preserve the principal intact, and may expend only income derived from the principal for the funds' designated operations.

Pension Trust Funds account for transactions of the four public employee retirement systems for which the State acts as trustee.

Investment Trust Funds account for transactions by local governments and political subdivisions that elect to participate in the State Treasurer's investment pools. The Treasurer acts as Trustee for the original deposits made into the investment pools.

Agency Funds account for the receipt and disbursement of various taxes, deposits, deductions, and property collected by the State, where the State acts as an agent for distribution to other governmental units or organizations.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

4. University Funds

University Funds account for transactions of the State's three universities. For State reporting purposes, the University Funds combine the balances of each university's separate financial statements.

The University Funds include:

* Current Operating Funds account for unrestricted resources over which the governing board retains full control in achieving the institutions' purposes and restricted resources that may be utilized only in accordance with externally restricted purposes.

* Loan funds account for loans made to assist students in financing their education.

* Endowment and similar funds account for private gifts that specify income purpose and principal protection and assets for which the universities act in a custodial manner.

* Plant funds account for institutional property investment, acquisition, renewal, replacement and debt service.

5. General Fixed Assets Account Group

Fixed assets used in Governmental and Expendable Trust Fund operations (general fixed assets) are accounted for in the General Fixed Assets Account Group, rather than in the individual funds. Fixed assets related to Proprietary Funds, Non-Expendable Trust Funds, Pension Trust Funds, University Funds and Component Units are accounted for in those funds.

6. General Long-Term Debt Account Group

The General Long-Term Debt Account Group reflects long-term liabilities expected to be retired with Governmental and Expendable Trust Fund resources. Liabilities related to Proprietary Funds, Non-Expendable Trust Funds, Pension Trust Funds, University Funds and Component Units are accounted for in those funds.

7. Component Units

The Component Units include proprietary and fiduciary type organizations that are legally separate from the State but are considered part of the reporting entity.

D. BASIS OF ACCOUNTING

1. Overview

The measurement focus of the financial statements for the Governmental Funds and Expendable Trust Funds is the flow of current financial resources, measured by the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues and other financial resources are recognized in the accounting period in which they become both measurable and available to finance operations of the fiscal year or liquidate liabilities existing at fiscal year end. Expenditures and other uses of financial resources are recognized when the related fund liability is incurred.

The measurement focus of the financial statements for the Proprietary Funds, Non-Expendable Trust Funds, Pension Trust Funds, Investment Trust Funds and Proprietary and Fiduciary Fund Types Component Units is the flow of economic resources, measured by the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recognized when they are incurred.

Agency Funds are custodial in nature, and therefore, do not present results of operations or have a measurement focus.

State Compensation Fund's financial statements are prepared on a statutory basis in accordance with accounting practices prescribed or permitted by the Arizona Department of Insurance. Prescribed statutory accounting practices include a variety of publications of the National Association of Insurance Commissioners (NAIC), as well as state laws, regulations and general administrative rules. Permitted statutory accounting practices encompass all accounting practices not so prescribed. These accounting practices differ in certain respects from generally accepted accounting principles. Under generally accepted accounting principles, the following apply:

* Non-admitted assets less applicable allowance accounts are restored to the balance sheet. Non-admitted assets include premiums receivable outstanding more than 90 days, office furniture and equipment, prepaid expenses, advances and real estate valuation allowances.

* Investment in debt securities are classified as either trading, available-for-sale or held-to-maturity. The specific accounting treatment applied to these securities is dependent upon that classification.

* Land and buildings are not classified as investments.

* Reinsurance recoverables are reclassified to assets from the liability for incurred but unpaid losses and accrued loss adjustment expense.

* Imputed rental income for office space occupied by the State Compensation Fund is eliminated against imputed rental expense.

* Policy acquisition costs are deferred over the policy life.

The measurement focus of the financial statements of the University Funds is the flow of total financial resources measured by the accrual basis of accounting in accordance with generally accepted accounting principles prescribed by the American Institute of Certified Public Accountants.

2. Revenue Recognition - Governmental Fund Types

The State recognizes tax revenues and related receivables when the taxpayer incurs the corresponding liability, and the

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

payment has been demanded, provided the State can reasonably estimate the amount of revenue to which it is entitled and can reasonably establish its collectibility, i.e., earned and collected or expected to be collected within the next 31 days. Otherwise, the State defers recognizing revenue until cash is received. Major revenues determined to be susceptible to accrual include income, sales, unemployment, and motor vehicle and fuel taxes. Any receivables not collected within the next 31 days are recorded as deferred revenue.

The State estimates the amount of taxes that will ultimately be uncollectible and excludes these from revenues. Tax refunds are based upon actual payments made within 31 days after fiscal year end and are recorded as a liability and a reduction in related revenue.

Property taxes are levied on the third Monday in August. The first half of collections are due October 1 and the second half are due the following March 1. Any property tax collections received within 31 days after fiscal year end are recognized as revenue. The lien date is the first day of January each year.

Federal grants and reimbursements are recorded as intergovernmental receivables and revenues when the State incurs the related expenditures or expenses, provided the State has complied with the terms of the grant award. Revenues from Federal entitlement awards are recorded as intergovernmental receivables and revenues when entitlement occurs.

Revenue from non-refundable licenses, permits and similar fees is recorded when cash is received. Other revenues are recorded when earned, or when the State becomes entitled to the revenue and can establish its collectibility; otherwise, the State defers recognition of revenue until cash is received.

3. Expenditure Recognition - Governmental Fund Types

The State recognizes expenditures and related liabilities in the accounting period the liability is incurred to the extent it is expected to be paid within the next 12 months, as a result of receiving property, goods or services, or when the beneficiary of a State program becomes entitled to receive benefits. Exceptions to this rule are:

* The State does not recognize a liability or the related expenditure for expected future welfare, health and similar benefits if the beneficiary is entitled to benefits solely because of a current condition.

* The State recognizes interest in the Debt Service Funds to the extent it becomes payable during the current fiscal year.

* The State recognizes compensated absences in the period they are paid. The amounts earned and to be paid in the future are recorded in the General Long-Term Debt Account Group.

* The State recognizes a liability and the related expenditures for the accrued insurance losses of the Arizona Health Care Cost Containment System as they are incurred, regardless of when these expenditures are actually paid.

The portion of the liabilities that is expected to be paid beyond 12 months is recorded in the General Long-Term Debt Account Group.

E. VALUATION POLICIES

1. Cash and Cash Equivalents

Cash and cash equivalents include undeposited receipts, petty cash, bank accounts, non-negotiable certificates of deposit and collateral investment pools related to securities lending transactions.

2. Investments

Investments are stated at fair value, except for the Arizona Power Authority and the State Compensation Fund (non-GAAP basis) Component Units which are reported at amortized cost and the Treasurer's Custodial Securities of the Agency Funds which are reported at par value.

3. Inventories

Inventories consist of expendable supplies held for consumption in all funds, and merchandise intended for sale to customers in the Proprietary Funds and University Funds. Inventories are stated at cost, using the first-in, first-out method. In Governmental Funds, inventories are accounted for using the purchase method. Under this method, inventories are recorded as an expenditure as they are purchased. However, the Arizona Department of Transportation State Highway Fund, reported as a Special Revenue Fund, is accounted for using the consumption method. Under this method, inventories are recorded as expenditures as they are used.

4. General Fixed Assets

Fixed assets capitalized in the General Fixed Assets Account Group are recorded at the time of purchase as capital outlay or other expenditures in the funds from which the expenditures are made. Such assets are capitalized at historical cost. Donated fixed assets are recorded at estimated fair market value on the date of contribution. Public domain (infrastructure) general fixed assets consisting of roads and bridges are not capitalized, as these assets are immovable and of value only to the government. The State does not record depreciation on general fixed assets.

5. Proprietary and Similar Trust Fund Fixed Assets

Fixed assets acquired in Proprietary and Similar Trust Funds are capitalized at historical cost. Donated fixed assets are recorded at estimated fair market value on the date of contribution. Depreciation is charged against operations in Proprietary and Similar Trust Funds on a straight-line basis over the estimated useful lives of the assets.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The State is trustee for approximately 9.4 million acres of land acquired through U.S. Government land grants. The State acquired a substantial portion of this land at no cost to the State, and its fair market value has not been reliably estimated. Accordingly, this land is not reported on the accompanying financial statements. A portion of the land that the State is trustee for has been sold and the buyers of the land have defaulted on the loans. The value of this land has been recorded at the sales price and properly included in the Non-Expendable Trust Funds fixed assets.

The State holds land and other assets in trust for the benefit of its public schools and other public institutions. The trust requires the principal to be held intact with only interest and rentals of property distributed for current operations. Accordingly, certain revenues, including gains on the sale of property, are added to principal rather than distributed for current operations. In addition, the State Constitution provides that certain State revenues be added to the principal of the trust. In 1999, the trust distributed all monies eligible for distribution to aid the State's educational system and other public institutions.

6. University Fixed Assets

Fixed assets capitalized in the University Funds are recorded at historical cost. Donated fixed assets are recorded at fair market value on the date of contribution. The University Funds do not record depreciation on fixed assets.

7. Leases

The State has entered into capital lease agreements for land, buildings, machinery and equipment. Although the terms of these leases vary, most are subject to annual appropriations by the Legislature. If a legislative appropriation is reasonably assured and the intent of the State is to continue the lease, a capital lease is considered non-cancelable for financial reporting purposes.

Assets acquired through capital leases are valued at cost. Capital leases for the Governmental Funds are reported in the General Long-Term Debt Account Group and the related assets are reported in the General Fixed Assets Account Group. Capital leases for the Proprietary, Similar Trust Funds and University Funds are reported in those funds as a long-term obligation, together with the related assets.

The State also leases land, buildings and equipment under operating leases. The related assets are not capitalized. Operating lease obligations are recorded when incurred as rental expenditures or expenses of the related funds.

F. BUDGETS AND BUDGETARY ACCOUNTING

1. Budget Process

Annually (or biennially for certain small agencies), no later than five days after the regular session of the Legislature convenes, the Governor must submit to the Legislature for approval a proposed operating and capital outlay budget for the succeeding fiscal year. Beginning with fiscal year 2000, the Legislature will approve biennial budgets for all State agencies. The Legislature must approve the budget by passing a general and a capital outlay appropriation bill. The budget can be amended throughout the year by special legislative appropriations and/or budget transfers. The State's budgeted expenditures may not exceed seven percent of aggregate personal income as estimated by the Economic Estimates Commission as stated in the State Constitution.

Revenues are not budgeted. Consequently, the combined Statement of Revenues and Expenditures Appropriation (Budget) to Actual-Budgetary Basis presents a comparison of budget to actual expenditures since that is the only comparison of the legally adopted budget with actual data that can be made.

Funds that have legal budgets include the General Fund, Special Revenue Funds (except for minor funds); portions of Capital Projects Funds, State appropriations to the Exposition and State Fair (an Enterprise Fund), certain Expendable, Non-Expendable and Pension Trust Funds, and State appropriations to the University Funds. However, Federal resources included in these Funds are not appropriated. State agencies are responsible for exercising budgetary control and ensuring that expenditures do not exceed appropriations. The State Department of Administration - Financial Services Division exercises oversight and does not disburse funds in excess of appropriations.

The State prepares its annual budget on the cash basis of accounting. Encumbrances as of June 30 can be liquidated during a four-week administrative period known as the 13th month. Anticipated revenue is estimated on the cash basis. The statements comparing budgeted and actual results are presented on the budgetary (or legal) basis. The State prepares a separate document, "Annual Financial Report For the Fiscal Year Ended June 30, 1999," that presents the individual funds' comparisons at the level of budgetary control, and is available from the State Department of Administration, Financial Services Division, General Accounting Office.

2. Encumbrance Accounting

Encumbrance accounting, under which purchase orders, contracts and other commitments for expenditures are recorded to reserve that portion of the applicable appropriation, is an extension of formal budgetary control. The Department of Administration - Financial Services Division is authorized to draw warrants against the available balances of appropriations for one month after the end of the fiscal year in order to pay for goods or services received but not paid for at the close of the fiscal year.

Encumbrances outstanding more than one month after year end for goods or services that were not received before year end are canceled. These can only be paid upon a subsequent appropriation by the Legislature. Encumbrances for goods and services received before year end can be paid in the subsequent year with the previous year appropriations.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

One month after year end, the remaining available appropriations lapse and no further payments may be made except for continuing appropriations allowed under Arizona Revised Statutes (ARS) §35-190. Continuing appropriations primarily relate to multi-year commitments and automatically renew without further legislative action until altered or revoked.

G. STATE COMPENSATION FUND

Other significant accounting policies relating to the State Compensation Fund (non-GAAP basis) include:

1. Policyholders' Dividends

The Board of Directors of the State Compensation Fund makes provisions for dividends to policyholders based on the Fund's overall experience. Dividends are paid to policyholders that meet premium volume and loss experience criteria established by the Board. Dividends recorded at December 31, 1998 include $81.50 million declared in March 1999. This is a permitted statutory accounting practice.

2. Reinsurance

The State Compensation Fund is assigned certain policyholders which participate in the National Council on Compensation Insurance (NCCI) assigned risk pool. All premiums collected on such policies are ceded to NCCI. All losses incurred by the Fund on such policies are recoverable from NCCI. In addition, the Fund is assigned a pro rata allocation of the liability for loss and loss expenses incurred by all NCCI policyholders in the State. Losses of other policyholders in excess of specified amounts are recoverable from other reinsurers. Contracts with these reinsurers do not relieve the Fund of its obligation to policyholders.

NOTE 2. RECONCILIATION OF FUND EQUITY - BUDGETARY BASIS TO GAAP

The accompanying "Combined Statement of Revenues and Expenditures - Appropriation (Budget) to Actual - Budgetary Basis - General, Special Revenue and Capital Projects Funds" presents comparisons of the legally adopted budget with actual data on a budgetary basis. Appropriations authorized in one fund and transferred, by legislation, to another fund have not been eliminated. Budget amounts are not presented for revenues, as the State does not have a legally adopted budget for revenues.

Actual amounts are presented for revenues, transfers in and other financing sources/uses on the "Combined Statement of Revenues and Expenditures - Appropriation (Budget) to Actual - Budgetary Basis - General, Special Revenue and Capital Projects Funds." Since the budgetary and GAAP presentations of actual data differ, a reconciliation of the two bases follows (amounts expressed in thousands):

	General Fund Actual	Special Revenue Funds Actual	Capital Projects Funds Actual
Cash Basis Fund Balance, June 30, 1999	$ 1,023,741	$ 1,174,544	$ 61,674
Basis of Accounting Differences:			
Increases to Fund Balance:			
Taxes receivable, net of allowances	389,814	11,580	2,008
Interest receivable	10,083	1,480	102
Other receivables	-	58,719	-
Other assets	(4,734)	(441)	3
Due from other Funds	8,852	3,753	-
Inventory	-	2,512	-
Decreases to Fund Balance:			
Accounts payable	17,084	64,685	38
Due to local governments	45,385	-	-
Due to others	24,841	4,000	10
Due to other Funds	213	-	-
Deferred revenue	16,298	-	-
Accrued insurance losses	32,969	-	-
Total GAAP Basis Fund Balance, June 30, 1999	$ 1,290,966	$ 1,183,462	$ 63,739

Appropriation and corresponding budgetary-basis expenditure amounts of Enterprise, Internal Service, Expendable Trust, Non-Expendable Trust and Pension Trust Funds were $321.416 and $278.249 million, respectively. No appropriation was over-expended.

NOTE 3. CASH AND INVESTMENTS

A. CASH AND CASH EQUIVALENTS

Cash and cash equivalents are under the control of the State Treasurer, the retirement systems or other administrative bodies. The State invests any temporary surpluses of cash pursuant to ARS §35-312 Investment of Treasury Monies, ARS §35-313 Investment of Trust Monies or other statutory requirements. Investments include negotiable certificates of deposit, repurchase agreements, commercial paper, bankers' acceptances and obligations issued or guaranteed by the United States Government or its agencies. Cash deposited with the State Treasurer by State agencies with a statutory authorization to invest and all general fund monies is invested by the Treasurer in a pooled fund. Any interest earned is allocated monthly into each respective fund based on average daily cash balances.

The State Treasurer invests in short-term securities and other investments. Provisions of Arizona law restrict these investments to obligations of the U.S. Government and its agencies, obligations of the State and certain local government subdivisions, interest-bearing savings accounts and certificates of deposits, collateralized repurchase agreements, certain obligations of U.S. corporations, and certain other securities.

The State Treasurer also invests in various mortgage-backed securities for seventeen of the twenty-one investment pools it manages. These securities are reported at fair value on the balance sheet. In addition, they are reported in aggregate, as U.S. Government securities. The securities are purchased to diversify the State's exposure to maturity and credit risks while providing for enhanced yields. The credit risk associated with holding these securities is minimal since all securities are rated AAA by both Standard and Poor's and/or Moody's rating service. The market risk associated with holding these securities is linked to maturity risk in that as interest rates rise, the fair value of these securities will fall and prepayment of principal balances will decelerate. When interest rates fall, the fair value of these securities will rise and prepayment of principal balances will accelerate. The mortgage-backed securities are authorized under ARS §35-313.

Statutes enacted by the Legislature authorize the retirement systems to make investments in accordance with the "Prudent Man" rule. This rule imposes the responsibility of making investments with the judgment and care that men of ordinary prudence would exercise in the management of their own affairs when considering both the probable safety of their capital and the probable income from that capital. Within this broad framework, the retirement systems have chosen to invest in short-term securities and repurchase agreements, obligations of the U.S. Government and its agencies, corporate bonds, common and preferred stocks and mortgages. The Statutes also place certain restrictions on the investment fund portfolios of the retirement systems.

GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, requires the following disclosures.

Investments maintained by the State Treasurer are reported at fair value based upon an independent outside pricing service. Investments not valued by the pricing service, with a maturity of 91 days or more and all investments with a maturity of 90 days or less that were held at the beginning of the current fiscal year are valued using a market price solicited from the selling broker or a second outside pricing service. All investments with a remaining maturity of 90 days or less, that have no available market price, and were not held at the beginning of the current fiscal year, are valued using amortized cost. If different amortized cost values exist, the weighted average amortized cost is given to like investments.

The State Treasurer also maintains external investment pools (Central Arizona Water Conservation District, Local Government Investment Pool and Local Government Investment Pool-Government) with no regulatory oversight. The pools are not required to register (and are not registered) with the Securities and Exchange Commission under the 1940 Investments Advisors Act. The activity and performance of the pools is reviewed monthly by the State Board of Investment in accordance ARS §35-311. The fair value of investments is measured on a monthly basis. Participant shares are purchased and sold based on the Net Asset Value (NAV) of the shares. The NAV is determined by dividing the fair value of the portfolio by the total shares outstanding. The State Treasurer does not contract with an outside insurer in order to guarantee the value of the portfolio or the price of shares redeemed. The State Treasurer only makes investments in external investment pools that are registered with the Securities and Exchange Commission.

The State Treasurer is not an involuntary participant in another entity's external investment pool.

The State Treasurer is not aware of any involuntary participation of local governments in the State's external investment pools. Participants meeting the criteria established under ARS §35-316 are eligible to participate in the pools and are not required to disclose the reason for requesting the account.

The investments of the State Treasurer's Custodial Securities, an Agency Fund, are recorded at par value. The investments are held by the State Treasurer for state agencies that perform a business compliance function.

The investments of the Arizona Exposition and State Fair are reported at fair value.

The Arizona State Retirement System investments are reported at fair value. Investments, other than real estate and commercial mortgages, are reported at fair values determined by the custodial agents. The agent's determination of fair values includes, among other things, using pricing services or prices

NOTE 3. CASH AND INVESTMENTS (CONTINUED)

quoted by independent brokers at current exchange rates. Commercial mortgages have been valued on an amortized cost basis, which approximates fair value. Short-term investments are reported at cost, which approximates fair value. For investments where no readily ascertainable fair value exists, management, in consultation with their investment advisors, has determined the fair values for the individual investments based on anticipated maturity dates and current interest rates commensurate with the investment's degree of risk.

The Public Safety Personnel, Elected Officials' and Corrections Officer Retirement Systems investments are reported at fair value. Fair values are determined as follows: Short-term investments are reported at fair value, which approximates cost. Equity securities are valued at the last reported sales price. Fixed-income securities are valued using the last reported sales price or the estimated fair market value as determined by an outside pricing service. Investments that do not have an established market are reported at estimated fair value.

The investments of the Universities are reported at fair value. Fair value is determined from quoted market prices. Non-participating interest bearing contracts are valued at cost.

The University Medical Center's short-term investments are reported at cost, which approximates fair value. Long-term investments are reported at fair value as determined by quoted market prices.

The investments of the Arizona Power Authority are reported at amortized cost, which approximates fair value.

The investments of the Water Infrastructure Finance Authority in Guaranteed Investment Contracts are stated at cost, since they are non-participating contracts. The other investments are stated at fair value which approximates cost.

The investments of the State Compensation Fund (non-GAAP basis) are primarily valued at amortized cost. Investments in bonds, certificates of participation and mortgages are reported at amortized cost. Investments in stocks are valued at fair value based upon National Association of Insurance Commissioners publications or from an outside pricing service.

There is no income from investments associated with one fund that is assigned to another fund.

B. UNEMPLOYMENT INSURANCE

ARS §23-703 requires that unemployment insurance contributions from Arizona employers be deposited in an unemployment trust fund account with the Secretary of the Treasury of the United States that is established and maintained pursuant to Section 1104 of the Social Security Act. The cash on deposit in the trust fund account is pooled and invested. Interest earned from investments purchased with such pooled monies is deposited in the trust fund account.

C. RESTRICTED ASSETS

University Funds report as restricted assets cash and investments for bond and loan retirement funds (including advance refunding of bonds), as well as for maintenance and replacement reserves. The Endowment and Restricted Funds also include restricted assets.

D. COLLATERAL AND INSURANCE

The State requires that deposits and investments with financial institutions be entirely covered by Federal depository insurance or, alternatively, collateralized with surety equal to at least 100% (102% for the Treasurer) of the deposits so collateralized. Cash deposited with banks is collateralized based on bank balances. Surety collateralization includes U.S. government obligations, State obligations, obligations of counties and municipalities within the State, and certain other securities.

E. DEPOSITS

At June 30, 1999, the carrying amount of the State's deposits for the Primary Government was a deficit of $182.092 million and $7.417 million for the Component Units. At June 30, 1999, the bank balance was $148.878 million for the Primary Government and $7.417 million for the Component Units. The cash deficits resulted from the State Treasurer not reducing investments until the servicing bank presented warrants for payment. For the Primary Government bank balances, $9.230 million was collateralized by Federal depository insurance. Of the remaining balance, $68.240 million was collateralized by securities held by the bank's trust division or agent in the State's name in book-entry form, and $71.408 million was either not collateralized or was collateralized with securities held in the bank's custodial account with the Federal Reserve in the bank's name in book-entry form. For the Component Units bank balances, the $7.417 million was either not collateralized or was collateralized with securities held in the bank's custodial account with the Federal Reserve in the bank's name in book-entry form.

F. INVESTMENTS

The following tables summarize the credit risk of the State's investments (expressed in thousands). Category A includes investments that are insured or registered, or for which securities are held by the State or the State's agent in the State's name. Category B includes uninsured and unregistered investments for which securities are held by the counterparty's agent or trust department in the State's name. Category C includes uninsured and unregistered investments for which securities are held by the counterparty, or by its agent or trust department but not in the State's name.

NOTE 3. CASH AND INVESTMENTS (CONTINUED)

Primary Government

Type of Deposit or Investment	Category A	Category B	Category C	Reported Amount
U.S. Government securities	$ 7,545,821	$ -	$ 17,830	$ 7,563,651
Corporate stocks	16,944,323	2,757,255	-	19,701,578
Corporate debt	8,845,768	46	-	8,845,814
State and local government securities	445,499	-	-	445,499
Repurchase agreements	350,083	-	-	350,083
Other investments	168,950	9,215	75,662	253,827
Subtotal	$ 34,300,444	$ 2,766,516	$ 93,492	37,160,452
United States Treasury Pooled Investment				919,819
Guaranteed Investment Contracts				7,395
Mutual Funds				69,463
Mutual Fund - Benchmark Portfolio				7,268
Other Investments - not categorized				125,898
Short-Term Investment Fund				1,694,259
Mortgages				215,448
Real Estate				41,827
Joint Venture				14,000
Collateral Investment Pool				1,133,806
Investments Held by Broker/Dealers Under Security Loan Program:				
U.S. Government Obligations				538,982
Corporate Obligations - Domestic				49,987
Preferred and Common Stock - Domestic				65,243
Preferred and Common Stock - Foreign				391,022
Component Units Investment in Primary Government's Investment Pool				(42,008)
Total Investments				42,392,861
Deposits				(182,092)
Total Cash and Investments				$ 42,210,769

Component Units

Type of Deposit or Investment	Category A	Category B	Category C	Reported Amount
U.S. Government securities	$ 985	$ -	$ -	$ 985
Repurchase agreements	7,147	-	-	7,147
Other investments	103	135,276	13,987	149,366
Subtotal	$ 8,235	$ 135,276	$ 13,987	157,498
Investment in Primary Government's Investment Pool				42,008
Total Investments				199,506
Deposits				7,417
Total Cash and Investments				$ 206,923

At June 30, 1999, the State had no commitments to resell securities under yield maintenance agreements.

During the year ended June 30, 1999, the State did not make significant investments in types of investments beyond those enumerated in the tables above.

NOTE 3. CASH AND INVESTMENTS (CONTINUED)

State Compensation Fund (Non-GAAP Basis)

The following table (expressed in thousands) summarizes the types of investments of the State Compensation Fund. The State Compensation Fund provided no information as to the amount of insurance or collateralization of their deposits and investments.

Type of Deposit or Investment	Carrying Amount
U.S. Government securities	$ 801,492
Corporate debt	560,760
Corporate stock	238,136
Foreign Securities	11,245
Other investments	492,742
Deposits	31,310
Total Cash and Investments	$ 2,135,685

G. SECURITIES LENDING

GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions* requires reporting cash received as collateral on securities lending transactions and investments made with that cash as assets. A corresponding liability is also recorded for such securities lending transactions.

1. Industrial Commission

State statutes and the Industrial Commission (the Commission) policies permit the Commission to enter into securities lending transactions with its custodial bank. There were no significant violations of legal or contractual provisions, and there were no borrower or lending agent losses to the securities lending agent. The custodial bank, Northern Trust, manages the securities lending operations through a contractual agreement with the Commission and splits the fees received with the Commission. There was no credit risk (i.e., lenders exposure to the borrowers of its securities) related to the securities lending transactions at June 30, 1999. Northern Trust's indemnification responsibilities include performing appropriate borrower and collateral investment credit analysis, demanding adequate types and levels of collateral, and complying with applicable Department of Labor and Federal Financial Institutions Examinations Council regulations concerning securities lending. Securities are loaned for collateral that may include cash, U.S. Government securities and irrevocable letters of credit. Domestic securities are loaned for collateral valued at 102% of the market value of securities loaned plus accrued interest. International securities are loaned for collateral valued at 105% of the market value of the securities loaned plus accrued interest. The market value at June 30, 1999, for loaned securities collateralized by cash and non-cash collateral was $37.138 million and $2.142 million, respectively. As part of the securities lending transactions, Northern Trust received cash and non-cash collateral valued at $38.453 million and $2.218 million, respectively at June 30, 1999. Non-cash collateral cannot be pledged or sold unless the borrower defaults. Securities lent at year-end for cash collateral are presented as unclassified in the preceding schedule of custodial risk; securities lent for securities collateral are classified according to the category for the collateral received on the securities lent.

All securities loans can be terminated on demand by either the lender or the borrower. The average term of the loans are twenty-three days and cash open collateral is invested in a short-term investment pool, the Core Collateral Section, which had an average weighted maturity of twenty-eight days as of June 30, 1999. Cash collateral may also be invested separately in "term loans", in which case the investments match the loan term. Cash open loans can be terminated on demand by either lender or borrower and there was no dividends or coupon payments owing on securities lent. Securities lending earnings are credited to participating clients on approximately the fifteenth day of the following month. Investments made with cash collateral received are classified as an asset on the Balance Sheet. A corresponding liability is recorded as the Commission must return the cash collateral to the borrower upon expiration of the loan. At June 30, 1999, the Commission had $38.453 million outstanding as payable for securities lending.

2. Arizona State Retirement System

The Arizona State Retirement System (ASRS) is permitted by Title 38, Chapter 5, Article 2 of the Arizona Revised Statutes to enter into securities lending transactions. The ASRS enters into agreements with brokers to loan securities and have the same securities redelivered at a later date. It is the policy of the ASRS to receive as collateral at least 102% of the market value of the loaned securities and maintains collateral at no less than 100% for the duration of the loan. During fiscal year 1998, statutes were amended to allow for other than cash collateral. The ASRS records the collateral received and the same amount as an obligation for the securities on loan. Any cash collateral received is invested in short-term investments. The ASRS receives a negotiated fee for its loan activities. Investments made with cash collateral received are classified as an asset on the Combining Statement of Plan Net Assets. A corresponding liability is recorded as the ASRS must return the cash collateral to the borrower upon expiration of the loan. At June 30, 1999, the ASRS had $1.09 billion outstanding as payable for securities on loan.

Due to the flow of securities to and from transfer agents and the security loan program, securities occasionally cannot be delivered for a sale or received for a purchase, resulting in a "failed" transaction. Securities with trade dates in June and settlement dates in July result in "outstanding" transactions. Since these securities have contractually changed ownership,

NOTE 3. CASH AND INVESTMENTS (CONTINUED)

receivables and payables result from these transactions. Such transactions resulted in a receivable for securities sold of $100.375 million and a payable for securities purchased of $376.542 million at June 30, 1999.

3. Public Safety Personnel Retirement System, Elected Officials' Retirement Plan and Corrections Officer Retirement Plan

The Public Safety Personnel Retirement System (PSPRS), Elected Officials' Retirement Plan (EORP) and the Corrections Officer Retirement Plan (CORP) are permitted by Title 38, Chapter 5, Articles 3, 4 and 6 of the Arizona Revised Statutes to enter into securities lending transactions. The PSPRS, EORP and CORP are parties to securities lending agreements with a bank. The bank, on behalf of the PSPRS, EORP and CORP, enters into agreements with brokers to loan securities and have the same securities returned at a later date. The loans are fully collateralized, primarily by cash. Collateral is marked-to-market on a daily basis. Non-cash collateral can be sold only upon borrower default. The PSPRS, EORP and CORP require collateral of at least 102% of the market value of the loaned U.S. Government or corporate security. Securities on loan are carried at fair value. As of June 30, 1999, the fair value of securities on loan were (expressed in millions):

PSPRS	$ 886.760
EORP	75.170
CORP	110.618

The PSPRS, EORP and CORP receive a negotiated fee for its loan activities and is indemnified for broker default by the securities lending agent. The PSPRS, EORP and CORP participate in a collateral investment pool. All security loans can be terminated on demand by either the pool participants or the borrower. All term loans have a matched collateral investment. Cash collateral received for open loans is invested for a longer term, however, at least 20% of total collateral investments must be invested on any overnight basis and at least 30% of total collateral investments must be invested with a maturity of seven days or less. Additionally, no more than 20% of the total collateral investments will be invested in instruments maturing in over 91 days. In lending securities, investments of cash collateral for open loans as of June 30, 1999, are not matched in maturity and have a weighted average maturity of eight days. The PSPRS, EORP and CORP have no credit risks under this program and have experienced no defaults or losses on these loans. Investments made with cash collateral received are classified as an asset on the Combining Statement of Plan Net Assets. A corresponding liability is recorded as the PSPRS, EORP and CORP must return the cash collateral to the borrower upon expiration of the loan. At June 30, 1999, the PSPRS, EORP and CORP had $904.878, $76.868 and $113.607 million outstanding, respectively, as payable for securities on loan.

4. State Compensation Fund (Non-GAAP Basis)

The State Compensation Fund (the Fund) participates in a securities lending program in which securities are loaned to approved broker/dealers for specified periods of time. All securities on loan are collateralized by cash or cash equivalents of at least 102% of their fair value. The collateral is maintained by the Fund's investment trustee who is not a party to the security lending agreement. The Fund had invested securities on loan with a fair value of approximately $341.257 million and a reported value of $320.896 million at December 31, 1998. The Fund is not reporting on its Combined Balance Sheet the assets and liabilities required by GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions*.

H. DERIVATIVES

Derivatives are financial instruments (securities or contracts) whose value is dependent on reference rates or indices such as stock or bond prices, interest rates or currency exchange rates. ASRS internal investment managers use derivatives to hedge currency risk, reduce transaction costs, obtain market exposure, and enhance returns.

The principle categories of derivatives employed and their uses during the year were as follows:

Category	**Purpose**
Foreign exchange forward contracts	Hedge currency risk of investment denominated in foreign currencies.
Futures	Reduce transaction costs; obtain market exposure; enhance returns.
SWAPS	Interest rate risk management; enhance returns.

Generally, derivatives are subject to both market risk and counterparty risk. The derivatives utilized by ASRS internal investment managers typically have no greater market risk than their physical counterparts, and in many cases are offset by exposure elsewhere in the portfolio.

The ASRS believes that it is unlikely that any of the derivatives used by its internal investment managers could have a material adverse effect on the financial conditions of the System.

NOTE 3. CASH AND INVESTMENTS (CONCLUDED)

I. STATE TREASURER'S SEPARATELY ISSUED FINANCIAL STATEMENTS

The State Treasurer issues a separately published Annual Financial Report. The report provides additional information relating to the State Treasurer's total investing activities and the Internal and External Participants of the Investment Trust Funds. The Investment Trust Funds report on the activities of the Local Government Investment Pools and Central Arizona Water Conservation District Investment Account. A copy of the State Treasurer's Office Annual Financial Report can be obtained from their office at 1700 W. Washington, Phoenix, Arizona 85007-2812. The Treasurer's financial statements are audited by the Auditor General's Office.

NOTE 4. RECEIVABLES / DEFERRED REVENUE

A. TAXES RECEIVABLE

Taxes receivable represent amounts owed by taxpayers for the 1998 and prior calendar years including assessments for underpayment, penalties and interest totaling approximately $140.255 million at June 30, 1999. Taxes receivable are accrued when they are earned, measurable, and available.

The income tax receivable is composed of individual and corporate estimated payments, withholding payments, payments with final returns and assessments that relate to income earned through June 30, 1999. Sales and motor vehicle and fuel tax receivable represent amounts that are earned by the State in the fiscal period ended June 30, 1999, but not collected until the following month.

The following table summarizes taxes receivable at June 30, 1999 (expressed in thousands):

Type of Tax	General Fund	Special Revenue Funds	Capital Projects Funds	Trust and Agency Funds
Sales	$ 290,369	$ 1,412	$ -	$ -
Income - individual and corporate	331,260	-	-	-
Insurance premium	21,497	-	-	-
Motor vehicle and fuel	3,964	165,884	-	-
Luxury	5,257	10,168	2,009	-
Unemployment	-	-	-	46,409
Allowance for uncollectible taxes	(178,698)	-	-	-
Net Taxes Receivable	$ 473,649	$ 177,464	$ 2,009	$ 46,409

B. DEFERRED REVENUE

Deferred revenue consists of payments to the State for goods and services not yet rendered. Delinquent taxes not collected within 31 days after June 30, 1999, have been deferred and, consequently, are not included in current year revenues. Federal grant revenue not available in the next 31 days is deferred. Funds with deferred revenue of $10 million or more consist of the following (expressed in thousands):

Revenue Source	General Fund	Trust and Agency Funds	University Funds	State Compensation Fund
Taxes	$ 68,459	$ -	$ -	$ -
Land leases	8,332	16,934	-	-
Student services	-	-	121,861	-
Public assistance overpayments	15,265	-	-	-
Food stamps	17,805	-	-	-
Federal grants and reimbursements	16,917	-	-	-
Unemployment Insurance contributions	-	12,413	-	-
Policyholders' advance premiums	-	-	-	38,263
Other	11,090	320	-	-
Total	$ 137,868	$ 29,667	$ 121,861	$ 38,263

NOTE 5. GOVERNMENTAL RECEIVABLES / PAYABLES

A. GOVERNMENTAL RECEIVABLES

Due from U.S. Government of $199.840 million in the General Fund represents receivables from Federal financial assistance programs and $45.978 million in the Special Revenue Funds consists principally of amounts owed to the Arizona Department of Transportation for reimbursement of highway construction costs from the U.S. Department of Transportation.

B. GOVERNMENTAL PAYABLES

Due to local governments in the General Fund and Special Revenue Funds ($127.497 and $136.034 million, respectively) represents primarily sales and motor vehicle and fuel tax collections that have not yet been remitted by the State to the respective local governments as of June 30, 1999.

NOTE 6. FIXED ASSETS

A. GENERAL FIXED ASSETS ACCOUNT GROUP

A summary of changes in the general fixed assets account group follows (expressed in thousands):

Asset	Balance July 1, 1998	Adjustments	Additions	Deletions	Balance June 30, 1999
Land	$ 67,301	$ 12,311	$ 12,777	$ 5,491	$ 86,898
Buildings and improvements	931,136	(23,176)	50,979	287	958,652
Other improvements	83,648	10,755	3,383	60	97,726
Furniture, vehicles and equipment	305,305	1,774	43,651	18,465	332,265
Subtotal	1,387,390	1,664	110,790	24,303	1,475,541
Construction in progress	227,422	24,826	61,820	40,897	273,171
Total General Fixed Assets	$ 1,614,812	$ 26,490	$ 172,610	$ 65,200	$ 1,748,712

The July 1, 1998 balance was adjusted as a result of previously unreported and misclassified fixed assets.

B. PROPRIETARY AND SIMILAR TRUST FUNDS FIXED ASSETS

Proprietary and Similar Trust Funds fixed assets consisted of the following as of June 30, 1999 (expressed in thousands):

	Primary Government				
Asset	Enterprise Funds	Internal Service Funds	Similar Trust Funds	Component Units	Combined Total
Land	$ 5,867	$ -	$ 8,984	$ -	$ 14,851
Buildings and improvements	52,994	2,912	1,925	143,280	201,111
Other improvements	3,577	-	224	-	3,801
Furniture, vehicles and equipment	21,286	164,666	1,076	106,750	293,778
Construction in progress	37	53	450	2,885	3,425
Subtotal	83,761	167,631	12,659	252,915	516,966
Less: accumulated depreciation	(36,930)	(105,235)	(1,189)	(133,554)	(276,908)
Total	$ 46,831	$ 62,396	$ 11,470	$ 119,361	$ 240,058

Fixed assets of the Proprietary and Similar Trust Funds are capitalized in the fund in which they are utilized and depreciated on a straight line basis over their useful lives. The estimated lives of fixed assets are as follows:

	Years
Building and improvements	40
Other improvements	15
Furniture, vehicles and equipment	5-15

NOTE 6. FIXED ASSETS (CONCLUDED)

State Compensation Fund's fixed assets consisted of the following as of December 31, 1998 (reported on non-GAAP basis, expressed in thousands):

Asset	Balance December 31, 1998
Furniture, vehicles and equipment	$ 8,610
Less: accumulated depreciation	(6,925)
Total	$ 1,685

C. UNIVERSITY FIXED ASSETS

The University fixed assets consist of the following (expressed in thousands):

Asset	Balance June 30, 1999
Land	$ 204,763
Buildings and improvements	1,762,003
Other improvements	33,024
Furniture, vehicles and equipment	988,383
Subtotal	2,988,173
Construction in progress	43,728
Total	$ 3,031,901

Universities' construction projects included in construction in progress have a total estimated cost of $239.022 million, a cost to date of $43.728 million and a remaining cost to complete of $195.294 million.

In October 1996, the Federal Government conveyed to Arizona State University a portion of the former Williams Air Force Base which is used by the University as the ASU East Campus. The property transfer is conditional upon the use of the property for educational purposes in accordance with the terms of the deed. The appraised fair value of the property conveyed was $56.4 million and consisted of 61 multi-purpose use buildings and 177 single family residences valued at $45.3 million, site improvements valued at $3.5 million and 279.1 acres of land valued at $7.6 million.

Arizona State University recorded this conveyed property at the time of title transfer at its appraised value. This was the initial conveyance in what the University anticipates to be a two-phase transfer of title to the property it occupies as the East Campus. The appraised fair value of the property yet to be conveyed is $33.3 million and includes 4 multi-purpose use buildings, 390 single family residences and 312.9 acres of land. The University will record these remaining assets at the time they are conveyed by the Federal Government. As of September 3, 1999, only the initial conveyance totaling $56.4 million had occurred.

NOTE 7. RETIREMENT PLANS

The State contributes to the four plans described below. The four plans are considered part of the State's financial reporting entity and are included in the State's financial statements as Pension Trust Funds.

A. PLAN DESCRIPTIONS

The State participates in the Arizona State Retirement System (ASRS), the Public Safety Personnel Retirement System (PSPRS), the Elected Officials' Retirement Plan (EORP) and the Corrections Officer Retirement Plan (CORP). Benefits are established by state statutes and provide retirement, death, long-term disability, survivor and health insurance premium benefits to State employees, public school employees and employees of counties, municipalities and certain other State political subdivisions.

The **ASRS** is a cost-sharing, multiple-employer defined benefit pension plan that benefits employees of the State, its political subdivisions and public schools. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of ARS Title 38, Chapter 5, Article 2.

The **PSPRS** is an agent, multiple-employer defined benefit pension plan that benefits fire fighters and police officers employed by the State or certain local governments. The PSPRS, acting as a common investment and administrative agent, is governed by a five-member board, known as the Fund

NOTE 7. RETIREMENT PLANS (CONTINUED)

Manager, and 166 local boards according to the provisions of ARS Title 38, Chapter 5, Article 4.

The **EORP** is a cost-sharing, multiple-employer defined benefit pension plan that benefits all elected State and county officials and judges (except La Paz County elected officials), and certain elected city officials. The EORP is governed by the Fund Manager of PSPRS according to the provisions of ARS Title 38, Chapter 5, Article 3.

The **CORP** is an agent, multiple-employer defined benefit pension plan that benefits town, city and county detention officers and certain employees of the Arizona Department of Corrections and the Arizona Department of Juvenile Corrections. The CORP is governed by the Fund Manager of PSPRS according to the provisions of ARS Title 38, Chapter 5, Article 6.

Each plan issues a publicly available financial report that includes its financial statements and required supplementary information. A report may be obtained by writing or calling the applicable plan.

Arizona State Retirement System
3300 North Central Avenue
P.O. Box 33910
Phoenix, Arizona 85067-3910
(602) 240-2000 or (800) 621-3778

Public Safety Personnel Retirement System, Elected Officials' Retirement Plan or the Corrections Officer Retirement Plan
1020 East Missouri Avenue
Phoenix, Arizona 85014
(602) 255-5575

The number of participating government employers as of June 30, 1999, are shown below:

Employer	ASRS	PSPRS	EORP	CORP
Cities and towns	62	118	16	-
Counties and county agencies	14	19	15	10
State	1	1	1	1
Special districts	41	25	-	-
School districts	221	-	-	-
Charter schools	79	-	-	-
Community college districts	10	-	-	-

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As part of the Pension Trust Funds, the financial statements are prepared using the accrual basis of accounting under which expenses are recorded when the liability is incurred and revenues are recorded in the accounting period in which they are earned and become measurable. Employee contributions are recognized in the period in which contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Contributions from employees and employers for service through June 30 are accrued. These contributions are considered to be fully collectible and, accordingly, no allowance for uncollectible receivables is reflected in the financial statements.

For the ASRS, investments are reported at fair value and cost. Security transactions and any resulting gains or losses are accounted for on a trade-date basis. Investments, other than real estate and commercial mortgages, are reported at fair values determined by the custodial agents. The agent's determination of fair values includes, among other things, using pricing services or prices quoted by independent brokers at current exchange rates. Commercial mortgages have been valued on an amortized cost basis which approximates fair value. No allowance for loan loss has been provided as all loans and bonds are considered by management to be fully collectible.

Short-term investments are reported at cost which approximates fair value. For investments where no readily ascertainable fair value exists, management, in consultation with their investment advisors, has determined the fair values for the individual investments based on anticipated maturity dates and current interest rates commensurate with the investment degree of risk. Net investment income includes net appreciation in fair value of investments, interest income, dividend income and total investment expense, which includes investment management and custodial fees and all other significant investment related costs.

For the PSPRS, EORP and the CORP, investments are reported at fair value and at cost. Fair values are determined as follows: Short-term investments are reported at fair value, which approximates cost. Equity securities are valued at the last reported sales price. Fixed-income securities are valued using the last reported sales price or the estimated fair market value as determined by one of the world's largest and most prominent fixed-income broker/dealers. Investments that do not have an established market are reported at estimated fair value. Investment income is recognized as earned.

Statutes enacted by the Arizona State Legislature restrict the four retirement plans from investing more than five percent of each plan's total assets in securities issued by any one institution, agency or corporation, other than securities issued as direct obligations of or fully guaranteed by the United States Government. As of June 30, 1999, the four retirement plans are in compliance with the state statutes.

NOTE 7. RETIREMENT PLANS (CONTINUED)

C. FUNDING POLICY

The contribution requirements of plan members and the State are established by Title 38, Chapter 5 of the Arizona Revised Statutes. These contribution requirements may be amended by the Arizona State Legislature.

Cost-sharing plans - For the year ended June 30, 1999, active ASRS members and the State were each required by statute to contribute at the actuarially determined rate of 3.34 percent (2.85 percent retirement and 0.49 percent long-term disability) of the members' annual covered payroll. The State's contributions to ASRS for the years ended June 30, 1999, 1998 and 1997 were $42.112, $41.685, and $40.622 million, respectively, for the primary government and $727, $735 and $12 thousand, respectively, for the component units, which were equal to the required contributions for the year.

In addition, active EORP members were required by statute to contribute 7.00 percent of the members' annual covered payroll. The State was required to contribute a designated portion of certain fees collected by the Supreme Court plus additional contributions of 8.9 percent of the members' annual covered payroll, as determined by actuarial valuation. The State's contributions to EORP for the years ended June 30, 1999, 1998 and 1997 were $1.180 million, $681 thousand and $338 thousand, respectively, which were equal to the required contributions for the year.

Agent plans - For the year ended June 30, 1999, active PSPRS members were required by statute to contribute 7.65 percent of the members' annual covered payroll and the participating State agencies were required to contribute at actuarially determined rates of 0.00 - 10.74 percent. Active CORP members were required by statute to contribute 8.50 percent of the members' annual covered payroll and the participating State agencies were required to contribute at actuarially determined rates of 1.87 - 3.72 percent.

D. ANNUAL PENSION COST

The State's annual pension cost and related actuarial data for the two agent, multiple-employer defined benefit pension plans for the year ended June 30, 1999, follows (expressed in thousands):

	PSPRS	CORP
Contribution rates:		
State	0.00%-10.74%	1.87%-3.72%
Plan members	7.65%	8.50%
Annual pension cost	$4,348	$13,500
Contribution made	$4,348	$13,500
Actuarial valuation date	6/30/99	6/30/99
Actuarial cost method	entry age	entry age
Actuarial assumptions:		
Investment rate of return	9%	9%
Projected salary increases/ includes inflation at	6.5%-9.5% 5.5%	5.5%-9.5% 5.5%
Cost-of-living adjustment	none	none
Amortization method	level percent open	level percent open
Remaining amortization period from 7/1/99	Open 20 years	Open 20 years
Asset valuation method	4-year smoothed market	4-year smoothed market

NOTE 7. RETIREMENT PLANS (CONTINUED)

E. TREND INFORMATION

An analysis of the most recent actuarial valuations for each of the agent, multiple-employer defined benefit plans is as follows (expressed in thousands):

Contributions Required and Contributions Made

	Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
PSPRS	6/30/99	$ 4,348	100%	$ 0
	6/30/98	5,345	100	0
	6/30/97	5,528	100	0
CORP	6/30/99	13,500	100%	0
	6/30/98	13,355	100	0
	6/30/97	12,945	100	0

F. FUNDING PROGRESS

The following schedule describes the funding progress for each of the agent, multiple-employer defined benefit plans for the fiscal year as indicated (expressed in thousands):

Plan	Actuarial Valuation Date	Actuarial Value of Plan Assets	Actuarial Accrued Liability	Funding Excess	Funded Ratio	Annual Covered Payroll	Funding Excess as Percentage of Covered Payroll
PSPRS	6/30/99	$ 497,050	$ 397,860	$ 99,190	124.9%	$ 61,994	160.0%
	6/30/98	436,811	363,284	73,527	120.2	56,711	129.7
	6/30/97	405,428	340,714	64,714	119.0	53,737	120.4
CORP	6/30/99	457,404	345,460	111,944	132.4	243,211	46.0%
	6/30/98	374,549	316,710	57,839	118.3	204,778	28.3
	6/30/97	303,962	272,513	31,449	111.5	193,952	16.2

There has been a significant benefit enhancement for CORP members. The benefit accrual rate was increased from 2.2% of the member's base salary to 2.5% for each year of credited service. This benefit change applies to members retiring subsequent to July 21, 1997, and may have a significant impact on the funding level for CORP. Beginning July 21, 1997, the member contribution rate increased to eight and one-half percent (8.50%) of salary.

G. UNIVERSITIES' DEFINED CONTRIBUTION PLANS

University faculty, academic professionals and administrative officers at the three universities (Arizona State University, Northern Arizona University, and University of Arizona) may select one of five retirement plans: the Arizona State Retirement System (ASRS), Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), Fidelity Investments Tax-Exempt Services Company (Fidelity) or Aetna Life Insurance and Annuity Company (Aetna). The ASRS is a defined benefit plan (described above) and the other four plans are defined contribution plans. The four defined contribution plans are administered by independent insurance and annuity companies approved by the Arizona Board of Regents. In addition, University of Arizona employees hired before July 1, 1972, have the option to participate in the defined contribution plan administered by the ASRS. Eligible classified staff belong to the Arizona State Retirement System. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings.

The Arizona State Legislature establishes and may amend active plan members' and the Universities' contribution rates. For the year ended June 30, 1999, plan members and the three Universities were each required by statute to contribute an amount equal to seven percent of an employee's compensation, except for an 8.24 percent contribution for the ASRS plan. Contributions to these plans for the year ended June 30, 1999, were as follows (expressed in thousands):

NOTE 7. RETIREMENT PLANS (CONCLUDED)

Plan	University Contributions	Employee Contributions	Total Contributions
TIAA/CREF	$ 20,257	$ 20,257	$ 40,514
VALIC	2,933	2,933	5,866
Fidelity	1,974	1,974	3,948
Aetna	751	751	1,502
ASRS	355	304	659

H. UNIVERSITY MEDICAL CENTER DEFINED CONTRIBUTION PLAN

The University Medical Center (UMC) has an Employee Pension Plan (the Plan) for employees of the UMC. The Plan is a defined contribution plan covering all employees of the UMC subject to minimum employment requirements, as defined in the Plan Agreement. The UMC makes contributions to the Plan in amounts equal to (a) 5.5 percent of total compensation plus (b) 5.4 percent of compensation in excess of 80 percent of the FICA wage base. Such contributions are allocated to each participant as defined in the Plan Agreement. Retirement plan expense, net of participant forfeitures was approximately $4.300 million for the year ended June 30, 1999.

I. POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described, the ASRS makes available group health insurance coverage to eligible retired and disabled members and their dependents. Retired and disabled members of the ASRS, PSPRS, EORP and CORP may participate if they are no longer eligible for health insurance benefits through their former employer.

This program is administered in accordance with ARS §38-782 and §38-783. Health insurance premiums are withheld from benefit payments and remitted to health insurance carriers. Approximately 32,000 coverage agreements currently exist for retired and disabled members and their dependents. The ASRS remitted approximately $34.9 million to health insurance carriers for premium payments during the fiscal year.

NOTE 8. EMPLOYEE BENEFITS

A. COMPENSATED ABSENCES

1. Annual Leave

In general, State employees accrue vested annual leave at a variable rate based on years of service. An employee forfeits accumulated annual leave in excess of 240 hours at the end of a calendar year, unless the Director of the Department of Administration authorizes an exception. An employee who separates from State service is paid for all unused and unforfeited annual leave at the employee's rate of pay at the time of separation.

2. Compensatory Leave

Some employees accumulate compensatory leave for time worked over 40 hours per week. Compensatory leave is treated like annual leave except that the employee must use any compensatory leave before using annual leave.

B. SICK LEAVE

Sick leave includes any approved period of paid absence granted an employee due to illness, injury or disability. Most State employees accrue sick leave at the rate of eight hours per month without an accumulation limit. Effective July 1, 1998, State employees are eligible to receive payment for an accumulated sick leave balance of 500 hours or more with a maximum of 1500 hours upon retirement directly from State service. (See Note 15.D)

C. DEFERRED COMPENSATION PLAN

The State offers its employees a Deferred Compensation Plan (the Plan) established in accordance with Section 457 of the Internal Revenue Code. All assets and income of the Plan are held in trust for the exclusive benefit of the participants and their beneficiaries. Assets of the Plan are administered by a private corporation under contract with the State. Consequently, the Plan's assets and liabilities are excluded from the State's financial statements.

NOTE 9. LONG-TERM DEBT

A. REVENUE BONDS

Primary Government

1. Arizona Department of Transportation

The Arizona Department of Transportation (ADOT) issued Highway Revenue Bonds in 1990, 1991, 1992 and 1993. These bonds are secured by a prior lien on and a pledge of motor vehicle and related fuel fees and taxes of the State Highway Fund, a special revenue fund. Arizona Revised Statutes prohibit the total principal amount of Arizona Highway Revenue Bonds, excluding refunded bonds, to exceed $800 million.

The ADOT also issued Transportation Excise Tax Revenue Bonds in 1988, 1989, 1991, 1992, 1993, 1995 and 1998. These bonds are secured by transportation excise taxes collected by the Arizona Department of Revenue on behalf of Maricopa County.

Bonds payable are due in varying annual principal amounts plus varying semiannual interest amounts, except for the 1988 Series A Capital Appreciation Bonds, which are due in annual installments of $21.500 million in 2002 through 2004 with the balance of $8.500 million due in 2005.

Bonds aggregating approximately $405.800 million ($240.585 million of Highway Revenue Bonds and $165.215 million of Transportation Excise Tax Revenue Bonds, respectively) are subject to redemption prior to their maturity dates, at the option of the Transportation Board, in whole at any time, or in part at various interest payment dates. These bonds may be redeemed at various redemption prices ranging from 100 percent to 102 percent of principal, plus accrued interest to the date fixed for redemption. Bonds aggregating approximately $870.805 million are not subject to redemption prior to maturity.

The Bond Resolution adopted by the Transportation Board on July 25, 1986 established a debt service reserve requirement equal to the maximum annual interest due in the current year or future years on any series of outstanding Transportation Excise Tax Revenue Bonds. The Second Supplemental Transportation Excise Tax Revenue Bond Resolution adopted by the Transportation Board on September 22, 1988, gives the Board the option, which it has elected, of acquiring debt service reserve insurance policies in lieu of the debt service reserve requirement. Accordingly, no debt service reserve is reflected in the accompanying financial statements. The policies (aggregating $70.064 million at June 30, 1999) were issued by Financial Guaranty Insurance Company, except for the 1989 Series A Subordinated Bonds and the 1993 Series Subordinated Bonds policies, which were issued by MBIA Insurance Corporation, and the 1995 Series A and Series B Subordinated Bonds policies, which were issued by AMBAC Assurance Corporation. These policies are noncancelable and insure payment, up to the policy amount, of the bond interest on their respective payment dates. The policies shall terminate on the earlier of July 1, 2005 or the date when no respective bonds are outstanding under the bond resolution. The premiums on these insurance policies are recorded as expenditures in the year of payment.

The carrying basis of the 1988 Series A Capital Appreciation Bonds increases as a result of accretion of the original issuance discount. At June 30, 1999, the carrying basis was $53.887 million. At maturity on July 1, 2005, the carrying basis will equal the maturity amount of $73.000 million.

On July 16, 1998, the ADOT issued $174.545 million in Transportation Excise Tax Revenue Bonds (1998 Series A) to (i) advance refund portions of the Transportation Board's outstanding Subordinated Bonds, (ii) finance acquisition of land and the design and construction of certain controlled access highways within Maricopa County, Arizona and (iii) pay costs of issuing the 1998 Series Bonds. The 1998 Series A Bonds are due July 1, 1999 through 2005.

Net proceeds totaled $177.826 million (after receipt of $4.359 million of reoffering premium and payment of $1.078 million in underwriting fees). Net proceeds of $28.714 million were used to advance refund $27.390 million of the 1989 Series A, Subordinated Transportation Excise Tax Revenue Bonds (Refunded Bonds). State and Local Government securities were purchased with these proceeds and were deposited in an irrevocable trust with an escrow agent to provide for the partial future debt service payments on the above-referenced bonds. As a result, the Refunded Bonds will be considered defeased and the liability for these bonds will be removed from the General Long-Term Debt Account Group. The ADOT advance refunded the Refunded Bonds to reduce its total debt service payments over the next three years by $738 thousand and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of $711 thousand.

In prior years, the ADOT refinanced various bond issues through advance refunding arrangements. Under the terms of the refunding bond issues, sufficient assets to pay all principal and interest on the refunded bond issues have been placed in irrevocable trust accounts at commercial banks and invested in U.S. Government Securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded.

As of June 30, 1999, the principal balance of defeased, refunded bonds is $776.993 million, which accordingly is not included as a liability in the accompanying financial statements.

2. Universities

a. University of Arizona

Cash and securities on deposit with trustees, restricted for retirement of bonded indebtedness and renewals and replacements, are $358 thousand and $369 thousand respectively, at June 30, 1999, as required by the bond indentures. In addition, $18.147 million was held by trustees

NOTE 9. LONG-TERM DEBT (CONTINUED)

for payment of future construction costs, and at June 30, 1999, the University also directly held proceeds totaling $1.990 million of the 1998 System Revenue Bonds for payment of future construction costs.

In fiscal years 1977, 1990, 1992, 1993 and 1998, the University refunded in advance of maturity certain outstanding revenue bonds. At June 30, 1999, the outstanding principal balance of the refunded bonds was $102.260 million that will be paid by investments held in trust with a carrying value of $82.218 million. These amounts are not included in the accompanying financial statements.

b. Northern Arizona University

In prior years, the University defeased certain revenue bonds by either placing the proceeds of new bonds, or cash and investments accumulated in the sinking fund, in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the accompanying financial statements. At June 30, 1999, $4.985 million of such bonds outstanding are considered defeased.

c. Arizona State University

In prior years, certain system revenue bonds of the University were in substance defeased through an advance refunding by depositing sufficient U.S. Government securities to pay all future debt service in an irrevocable trust. Accordingly, liabilities for these defeased bonds are not included in the accompanying financial statements. The principal amount of all refunded bonds outstanding at June 30, 1999, is $75.730 million.

The housing revenue bonds are payable from housing revenues as defined in the bond indentures. The Series 1992, 1992A and 1993 System Revenue Refunding Bonds, and the outstanding Series 1989 and 1991 System Revenue Bonds are payable from Main Campus tuition, fees, certain auxiliary enterprise revenues, and certain other revenues as defined in the bond indentures.

Securities and cash restricted for bond retirement funds and maintenance and replacement reserves held by trustees at June 30, 1999, totaled $17.445 million.

Component Units

3. Arizona Power Authority

In prior years, Arizona Power Authority (APA) defeased various issues of bonds by purchasing United States government securities which were deposited in an irrevocable trust with an escrow agent to provide future debt service on the maturity dates defeased. As a result, these bonds are considered to be defeased and the liability has been removed from the Hoover Uprating Fund. Accordingly, these trust account assets and related liabilities are not included in the accompanying financial statements. As of June 30, 1999, $99.450 million of bonds outstanding are considered to be defeased.

The remaining bonds, totaling $68.945 million, bear interest rates from 4.9 % to 5.4 % are due serially from 2002 through 2017.

4. University Medical Center

In January 1991, the University Medical Center issued $50.655 million of Hospital Revenue Bonds (the Series 1991 Bonds). The proceeds of the Series 1991 Bonds were used for the construction of an imaging center, a 110 bed tower for expanded programs, an emergency room, a parking facility, and the expansion and renovation of the surgical suites and other existing facilities.

In March 1992, the University Medical Center issued $28.405 million of Hospital Revenue Bonds (the Series 1992 Bonds) and in May, 1993, the University Medical Center issued $54.750 million of Hospital Revenue Refunding Bonds (the Series 1993 Bonds). The proceeds of the Series 1992 Bonds and the Series 1993 Bonds were used to advance refund a portion of the Series 1986, 1987 and 1991 Bonds.

The University Medical Center is subject to certain financial covenants under the Master Trust Indenture (the Indenture), with which the Center is in compliance as of and for the year ended June 30, 1999. In addition, the Indenture places certain restrictions on the incurrence of additional indebtedness and the sale or acquisition of property.

The University Medical Center has established and maintains separate funds for borrowings not yet expended for construction. These funds are held by the trustee and are reflected in "Investments held by trustee" in the accompanying combined balance sheets, consisting principally of guaranteed investment contracts.

The bonds or other obligations of the University Medical Center do not constitute general obligations of the Arizona Board of Regents, the University of Arizona, the State of Arizona or any political subdivision thereof.

5. Water Infrastructure Finance Authority

The Water Infrastructure Finance Authority (WIFA) issued Financial Assistance Revenue Bonds in 1991, 1992, 1995, 1996, 1997 and 1998. WIFA also issued Capitalization Revenue Bonds in 1991, 1992, 1995, 1996 and 1997. The bonds are callable and interest is payable semiannually. The bonds are special obligations of the WIFA payable solely from and secured by the WIFA's assets. The bonds are not obligations, general, specific or otherwise, of the State or any other political subdivision thereof other than the WIFA.

NOTE 9. LONG-TERM DEBT (CONTINUED)

6. Summary of Revenue Bonds

The following schedule summarizes revenue bonds outstanding at June 30, 1999 (expressed in thousands):

Revenue Bonds Outstanding	Dates Issued	Maturity Dates	Interest Rates	Amount Authorized	Amount Issued	Outstanding Balance at June 30, 1999
Primary Government:						
Department of Transportation	1990-1998	2000-2011	3.90-8.80 %	$ 2,358,623	$ 2,358,623	$ 1,257,492
University Revenue Bonds	1961-1998	2000-2019	2.70-9.40	833,901	833,901	559,109
Proprietary and Fiduciary Fund Types						
Component Units:						
Arizona Power Authority	1993	2002-2017	4.90-5.40	68,945	68,945	67,433
University Medical Center	1991-1993	1999-2021	5.53-6.86	133,810	133,810	77,078
Water Infrastructure Finance Authority	1991-1998	2005-2017	2.90-6.55	158,930	158,930	144,656

Future debt service principal payments on revenue bond issues for fiscal years ended June 30 are summarized below (expressed in thousands):

	Principal						
	Primary Government			Proprietary and Fiduciary Fund Types Component Units			
Fiscal Year	ADOT	Universities	Total Primary Government	University Medical Center	Arizona Power Authority	Water Infrastructure Finance Authority	Total Component Units
2000	$ 157,540	$ 27,750	$ 185,290	$ 2,280	$ -	$ 6,080	$ 8,360
2001	156,030	27,640	183,670	2,420	-	6,585	9,005
2002	157,740	29,990	187,730	2,580	-	7,985	10,565
2003	165,085	31,710	196,795	2,715	1,450	8,075	12,240
2004	172,765	33,432	206,197	2,860	2,320	8,180	13,360
Thereafter	448,332	408,587	856,919	64,223	63,663	107,751	235,637
Total	$ 1,257,492	$ 559,109	$ 1,816,601	$ 77,078	$ 67,433	$ 144,656	$ 289,167

Principal and interest debt service payments on revenue bonds outstanding at June 30, 1999 are as follows (expressed in thousands):

	Annual Debt Service					
	Primary Government			Proprietary and Fiduciary Fund Types Component Units		
Fiscal Year	Total Principal	Total Interest	Total Primary Government	Total Principal	Total Interest	Total Component Units
2000	$ 185,290	$ 97,232	$ 282,522	$ 8,360	$ 15,620	$ 23,980
2001	183,670	87,023	270,693	9,005	15,186	24,191
2002	187,730	77,111	264,841	10,565	14,678	25,243
2003	196,795	67,999	264,794	12,240	14,151	26,391
2004	206,197	58,591	264,788	13,360	13,528	26,888
Thereafter	856,919	247,933	1,104,852	235,637	102,471	338,108
Total	$ 1,816,601	$ 635,889	$ 2,452,490	$ 289,167	$ 175,634	$ 464,801

Changes in Revenue Bonds for Fiscal Year 1999 are summarized below (expressed in thousands):

	Primary Government	Component Units	Total Bonds Outstanding
Balance at July 1, 1998, as restated	$ 1,842,569	$ 296,158	$ 2,138,727
New Bonds Issued	178,296	-	178,296
Bonds Retired	(204,264)	(6,991)	(211,255)
Balance at June 30, 1999	$ 1,816,601	$ 289,167	$ 2,105,768

NOTE 9. LONG-TERM DEBT (CONTINUED)

B. CERTIFICATES OF PARTICIPATION

The State has issued Certificates of Participation (COPs) to finance construction or improvements of office buildings that are primarily leased to State agencies. The COPs mature serially at six-month intervals. The State lease payments are made to a trustee. The lease provides that the obligation of the State to make lease payments is subject to annual appropriation by the State Legislature.

The State is recording the COPs at the outstanding balance less cash with trustee except for the Universities and the Industrial Commission that are recorded at the outstanding balance. The cash with trustee is a reserve for the COPs.

Capitalized interest costs include interest incurred during the construction of an asset.

The 1985 COPs for the Industrial Commission were issued to refund the 1984 certificates that were issued to finance the cost of acquiring and constructing a building. The lease agreement provides that the title will pass to the Industrial Commission at the end of the lease term, once the COPs are completely redeemed. The refunded amount was $17.500 million. This amount is considered paid and is not included in the outstanding amounts.

The February 1992, June 1992 and November 1992 (in part) COPs for the Department of Administration were issued to refund the August 1986, October 1988 and December 1986 certificates, respectively. The total amount refunded was $161.530 million. This amount is considered paid and is not included in the outstanding amounts.

The December 1993 COPs for the Department of Administration was issued to refund the December 1989 and October 1990 certificates. The total amount refunded was $31.815 million. This amount is considered paid and is not included in the outstanding amounts.

A summary of the COPs issued as of June 30, 1999, is as follows (expressed in thousands):

Project	Issue Date	Maturity Date	Interest Rates
Arizona State University:			
Towers Project	1991	2010	6.89 %
West Campus – Refinancing	1993	2009	5.18
Industrial Commission Special Fund	1985	2005	4.20 – 5.00
Department of Revenue/ Department of Economic Security	1992	2005	5.00 - 6.50
Capitol Centre/RTC	1992	2007	3.00 - 6.10
Arizona Municipal Financing Program	1992	2004	3.40 - 6.10
University of Arizona:			
Telecommunications	1991	2012	4.60 - 6.50
Educational	1992	2007	3.20 - 6.25
Residence Life	1994	2014	4.10 - 5.80
Maingate Admin.	1994	2024	4.25 - 6.00
Alumni Foundation	1997	2008	3.80 - 4.50
School for the Deaf and Blind / Game and Fish	1993	2011	2.75 - 5.00
Prisons*	1991	2005	4.50 - 6.40
AHCCCS	1994	2005	6.66

NOTE 9. LONG-TERM DEBT (CONTINUED)

Project	Amount Authorized and Issued	Outstanding Balance	Cash with Trustee	Net COP Liability
Arizona State University:				
Towers Project	$ 4,500	$ 3,520	$ 446	$ 3,074
West Campus - Refinancing	46,905	43,440	5,447	37,993
Industrial Commission Special Fund	17,500	10,800	3,177	7,623
Department of Revenue/				
Department of Economic Security	22,125	18,855	2	18,853
Capitol Centre/RTC	32,895	17,230	6	17,224
Arizona Municipal Financing Program	129,640	105,560	12,692	92,868
University of Arizona:				
Telecommunications	25,995	16,899	3,907	12,992
Educational	4,670	3,240	486	2,754
Residence Life	16,725	14,890	1,943	12,947
Maingate Admin.	16,170	15,385	1,224	14,161
Alumni Foundation	2,965	2,710	313	2,397
School for the Deaf and Blind/Game and Fish	31,250	23,970	2	23,968
Prisons *	55,080	42,055	5,041	37,014
AHCCCS	12,642	8,319	-	8,319
Total	$ 419,062	$ 326,873	$ 34,686	$ 292,187

* The Prisons issue was a sales-leaseback transaction involving two prison units that are a portion of the Eyman Complex at the Arizona State Prison in Florence, Arizona. The proceeds of the issue were used to reimburse the General Fund for the ENSCO settlement.

Principal and interest debt service requirements on COPs outstanding at June 30, 1999, are as follows (expressed in thousands):

	Annual Debt Service		
Fiscal Year	Total Principal	Total Interest	Total Amount Required
2000	$ 20,970	$ 18,353	$ 39,323
2001	22,157	17,237	39,394
2002	23,559	16,028	39,587
2003	22,678	14,720	37,398
2004	23,922	13,444	37,366
Thereafter	213,587	57,518	271,105
Total	$ 326,873	$ 137,300	$ 464,173

Changes in COPs for Fiscal Year 1999 are summarized below (expressed in thousands):

Balance at July 1, 1998	$ 360,181
New COPs Issued	-
COPs Retired	(33,308)
Balance at June 30, 1999	$ 326,873

NOTE 9. LONG-TERM DEBT (CONTINUED)

C. LEASES AND INSTALLMENT PURCHASES

1. Leases

The total operating lease expenditures for the fiscal year-ended June 30, 1999, were $41.944 million for the primary government and $1.495 million for the Component Units. The future minimum lease payments for long-term operating leases as of June 30, 1999, are summarized below (expressed in thousands):

	Primary Government				
Fiscal Year	Governmental & Expendable Trust Funds	Proprietary Funds	University Funds	Component Units	Total
2000	$ 24,756	$ 57	$ 497	$ 1,342	$ 26,652
2001	18,905	57	121	849	19,932
2002	13,167	57	99	749	14,072
2003	7,169	57	70	507	7,803
2004	3,285	24	-	36	3,345
Thereafter	4,897	-	-	14	4,911
Total Future Minimum Payments	$ 72,179	$ 252	$ 787	$ 3,497	$ 76,715

Many operating leases are for buildings and land leased by State agencies. Although these leases are considered to be long-term, they are cancelable under certain circumstances.

* An agency must be able to cancel the lease if the monies are not appropriated to cover the lease expenditures.

* If an agency is ordered to move into State-owned property and a 60-day notice is given, the lease can be canceled without penalty.

* In situations where the use of the leased property is dependent on the use of Federal monies, the lease must be cancelable in the event Federal funds are no longer available.

The State has incurred capital leases for the acquisition of telephone systems, copy machines and other equipment.

The future minimum lease payments for long-term capital leases (all primary government) as of June 30, 1999, are summarized below (expressed in thousands):

Fiscal Year	General Long-Term Debt Account Group	University Funds	Total
2000	$ 1,537	$ 1,627	$ 3,164
2001	1,509	1,154	2,663
2002	1,494	879	2,373
2003	1,425	712	2,137
2004	1,174	439	1,613
Thereafter	6,263	1,058	7,321
Total Future Minimum Payments	13,402	5,869	19,271
Less: Interest and Executory Costs	3,085	938	4,023
Net Liability at June 30, 1999	$ 10,317	$ 4,931	$ 15,248

NOTE 9. LONG-TERM DEBT (CONCLUDED)

2. Installment Purchases

The State has installment purchase contracts payable for acquisitions of computer and other equipment. Installment purchases for the Governmental Funds are reported in the General Long-Term Debt Account Group and the related assets are reported in the General Fixed Assets Account Group. Installment purchases for the Proprietary and University Funds are reported in those funds as a long-term obligation, together with the related assets.

The future minimum payments for installment purchases (all primary government) as of June 30, 1999, are summarized below (expressed in thousands):

Fiscal Year	General Long-Term Debt Account Group	Proprietary Funds	University Funds	Total
2000	$ 6,293	$ 11	$ 476	$ 6,780
2001	3,193	-	463	3,656
2002	1,740	-	442	2,182
2003	1,207	-	383	1,590
2004	418	-	9	427
Thereafter	-	-	653	653
Total Future Minimum Payments	12,851	11	2,426	15,288
Less: Interest and Executory Costs	945	-	270	1,215
Net Liability at June 30, 1999	$ 11,906	$ 11	$ 2,156	$ 14,073

3. Summary of Changes

A summary of the changes in capital leases and installment purchase obligations follows (expressed in thousands):

	Balance July 1, 1998	New Contracts	Principal Reduction	Balance June 30, 1999
General Long-Term Debt Account Group	$ 26,963	$ 5,490	$ 10,230	$ 22,223
Proprietary Funds	1,365	1	1,355	11
University Funds	6,458	3,190	2,561	7,087
Total	$ 34,786	$ 8,681	$ 14,146	$ 29,321

D. SUMMARY OF CHANGES IN THE GENERAL LONG-TERM DEBT ACCOUNT GROUP

The following is a summary of changes in the General Long-Term Debt Account Group (expressed in thousands):

Type of Debt	Balance July 1, 1998	Additions	Retirements	Balance June 30, 1999
Revenue Bonds	$ 1,257,156	$ 178,296	$ 177,960	$ 1,257,492
Certificates of Participation	224,193	116	26,063	198,246
Capital Leases	11,883	955	2,521	10,317
Installment Contracts	15,080	4,534	7,708	11,906
Subtotal	1,508,312	$ 183,901	$ 214,252	1,477,961
Compensated Absences	127,077			139,905
Total	$ 1,635,389			$ 1,617,866

NOTE 10. INTERFUND TRANSACTIONS

A. INTERFUND BALANCES AND OPERATING TRANSFERS

Interfund balances, as of June 30, 1999, and operating transfers, for the year ended June 30, 1999, are as follows:

Fund	Due From Other Funds	Due To Other Funds	Operating Transfer In	Operating Transfer Out
Primary Government:				
General Fund	$ 25,703	$ 20,968	$ 123,378	$ 973,249
Special Revenue Funds:				
General Government	8,701	6,479	23,060	11,320
Health and Welfare	10,233	660	19,047	42,144
Inspection and Regulation	4,132	386	848	7,520
Education	-	-	20	19
Protection and Safety	1,945	-	2,133	17,430
Transportation	1,677	21,191	3,679	271,310
Natural Resources	10,249	617	28,057	2,977
Total Special Revenue Funds	36,937	29,333	76,844	352,720
Debt Service Funds:				
Department of Transportation	-	-	74,192	211
Maricopa RARF	-	-	152,309	2,918
Certificates of Participation	-	-	37,286	-
Total Debt Service Funds	-	-	263,787	3,129
Capital Projects Funds:				
Maricopa RARF Financed	5,876	1,676	-	551
Other	552	215	41,300	15,567
Total Capital Projects Funds	6,428	1,891	41,300	16,118
Enterprise Funds:				
Lottery	-	10,838	-	42,980
Arizona Exposition and State Fair	-	-	-	135
Arizona Highways Magazine	-	2	-	174
Arizona Correctional Industries	55	-	-	244
Arizona Industries for the Blind	-	-	-	295
Healthcare Group of Arizona	-	-	8,000	43
Other	5	6	4,518	781
Total Enterprise Funds	60	10,846	12,518	44,652
Internal Service Funds:				
Risk Management	1	23	56	9,980
Transportation Equipment	1,775	-	-	1,289
Workers' Compensation	1	11	41	203
Technologies and Telecommunication	1,926	5	11	712
Motor Pool	957	1	-	43
Other	695	1,062	1,947	2,000
Total Internal Service Funds	5,355	1,102	2,055	14,227
Expendable Trust Funds:				
Unemployment Compensation	-	185	-	1,658
Employee Benefits	643	561	176,975	-
Energy Conservation	-	1	-	436
Other	286	619	7,051	1,189
Total Expendable Trust Funds	929	1,366	184,026	3,283
Non-Expendable Trust Funds:				
Land Endowments	523	202	-	864
Other	2,000	-	4,010	26
Total Non-Expendable Trust Funds	2,523	202	4,010	890

NOTE 10. INTERFUND TRANSACTIONS (CONCLUDED)

Primary Government (Continued):				
Pension Trust Funds:				
State Retirement	$ -	$ -	$ -	$ 6,352
Public Safety	-	-	668	1,053
Elected Officials	-	-	48	85
Corrections	-	-	-	462
Total Pension Trust Funds	-	-	716	7,952
Investment Trust Funds:				
Central Arizona Conservation District	1,029	-	-	-
Local Government Investment Pool	9,684	-	-	-
Local Government Investment Pool – Government	735	-	-	-
Total Investment Trust Funds	11,448	-	-	-
Agency Funds:				
Other Treasurer Funds	-	19,528	-	-
Other	-	4,147	-	-
Total Agency Funds	-	23,675	-	-
Total Trust and Agency Funds	14,900	25,243	188,752	12,125
University Funds	2,854	2,854	762,586	54,979
Total per Financial Statements – Primary Government	$ 92,237	$ 92,237	1,471,220	1,471,199
Component Units:				
Arizona Power Authority			-	21
Total Reporting Entity			$ 1,471,220	$ 1,471,220

B. RESIDUAL EQUITY TRANSFERS

Residual equity transfers occur when nonroutine transfers are made from one fund to another. During fiscal year 1999, funds were eliminated based upon House Bill 2323 passed during the 1998 legislative session. In addition, excess funds were transferred to the General Fund based upon Senate Bill 1001 Laws 1998 passed during the fifth special session and Senate Bill 1003 passed during the 1999 first special session. For the fiscal year ended June 30, 1999, residual equity transfers were made are as follows (expressed in thousands):

	Transfers In	Transfers Out
General Fund	$ 25,478	$ 530
Special Revenue Funds:		
General Government	333	2,308
Health and Welfare	-	2,200
Education	-	9,872
Protection and Safety	-	4,300
Natural Resources	-	1,288
Enterprise Funds:		
Lottery	-	1,500
Arizona Exposition and State Fair	-	2,000
Arizona Correctional Industries	-	1,000
Other	-	5
Internal Service Funds:		
Technology and Telecommunications	-	500
Expendable Trust Funds:		
Other	5	825
Non-Expendable Trust Funds:		
Land Endowments	523	11
Total Residual Equity Transfers	$ 26,339	$ 26,339

NOTE 11. SEGMENT INFORMATION FOR ENTERPRISE FUNDS AND PROPRIETARY AND FIDUCIARY FUND TYPES COMPONENT UNITS

A. ENTERPRISE FUNDS

The State groups its Enterprise Funds as follows:

* Industrial Commission - Administers and enforces the employment laws of the State, including the regulation of workers' compensation.

* Lottery - Accounts for lottery ticket revenues, administrative and operating expenses and distribution of revenues to other Funds.

* Arizona Exposition and State Fair - Provides rental space to a variety of entertainment and promotional lessees, and sponsors the annual State Fair.

* Arizona Highways Magazine - Publishes and markets the Arizona Highways Magazine and various other products that promote the State of Arizona.

* Arizona Correctional Industries - Employs prison inmates in its manufacturing, service and agricultural operations for the sale of goods and services primarily to other State agencies (including the Arizona Department of Corrections) and political subdivisions.

* Arizona Industries for the Blind - Accounts for the manufacturing, sale, distribution and marketing of products manufactured by employees at training centers, workshops, business enterprises and home industries programs for the training and employment of adaptable visually impaired persons.

* Healthcare Group of Arizona - Administers prepaid medical coverage primarily to small uninsured businesses with 1 - 40 employees and employees of political subdivisions.

* Arizona Beef Council - A not-for-profit organization that was created to establish a self-financed program to help develop and maintain state, national and foreign markets for beef and beef products.

* ComCare, Inc. - A nonprofit corporation responsible for the administration, coordination and delivery of comprehensive behavioral health services to residents of Maricopa County through a network of more than 130 provider agencies/individuals.

* Other Enterprise Funds - Consists of Arizona Historical Society Revolving Fund, Mines and Mineral Resources Printing Revolving Fund, Game and Fish Publications Revolving Fund, Department of Library and Archives Gift Shop Revolving Fund, Arizona State Hospital Enterprise Fund, Southern Arizona Mental Health Center Enterprise Fund, Land Department Resource Analysis Revolving Fund, State Parks Publications and Souvenirs Revolving Fund, Real Estate Printing Revolving Fund, Education Commodity Fund, Indian Affairs Commission Publications Revolving Fund, the School for the Deaf and Blind Cooperative Services Fund, the School for the Deaf and Blind Facilities Use Fund and the State Home for Veterans.

B. PROPRIETARY AND FIDUCIARY FUND TYPES COMPONENT UNITS

* University Medical Center - A 365-bed, general acute-care teaching facility in Tucson, Arizona. It is the primary teaching hospital for the College of Medicine of the University of Arizona.

* Arizona Power Authority - Purchases the State's allocation of Hoover power and resells it to Arizona entities that are eligible purchasers under federal and state laws. Hoover power is produced by the Bureau of Reclamation at the federally-owned Boulder Canyon Project hydropower plant, located near Las Vegas, Nevada.

* Water Infrastructure Finance Authority (WIFA) - The WIFA is authorized to administer the Clean Water Revolving Fund and the Drinking Water Revolving Fund. The Clean Water Revolving Fund was created pursuant to the Federal Water Pollution Control Act of 1972, as amended by the Water Quality Act of 1987 (Clean Water Act) which required the State to establish the Fund to accept federal capitalization grants for publicly owned wastewater treatment projects. WIFA has entered into an agreement this year with the Environmental Protection Agency to administer the Drinking Water Revolving Fund pursuant to the Safe Drinking Water Act.

NOTE 11. SEGMENT INFORMATION FOR ENTERPRISE FUNDS AND PROPRIETARY AND FIDUCIARY FUND TYPES COMPONENT UNITS (CONTINUED)

Enterprise Funds segment information for the fiscal year ended June 30, 1999, is shown below (expressed in thousands):

Description	Industrial Commission	Lottery	Arizona Exposition and State Fair	Arizona Highways Magazine
Operating Revenues	$ 24,100	$ 269,158	$ 9,964	$ 10,917
Operating Expenses:				
Depreciation	495	651	1,016	358
Other	10,288	223,797	9,210	11,185
Operating Income (Loss)	13,317	44,710	(262)	(626)
Net Non-Operating Income (Loss)	(405)	-	769	(52)
Operating Transfers In	-	-	-	-
Operating Transfers Out	-	(42,980)	(135)	(174)
Net Income (Loss)	$ 12,912	$ 1,730	$ 372	$ (852)
Current Assets	$ 41,364	$ 38,261	$ 7,287	$ 7,269
Current Liabilities	51,640	40,344	315	4,743
Net Working Capital	$ (10,276)	$ (2,083)	$ 6,972	$ 2,526
Property and Equipment:				
July 1, 1998, as restated	$ 18,790	$ 8,691	$ 22,530	$ 5,011
Additions	487	-	385	629
Deletions	61	15	69	1,446
June 30, 1999	$ 19,216	$ 8,676	$ 22,846	$ 4,194
Certificates of Participation	$ 9,800	$ -	$ -	$ -
Contributed Capital	$ -	$ -	$ -	$ 1,539
Residual Equity Transfer Out	$ -	$ (1,500)	$ (2,000)	$ -
Total Assets	$ 281,135	$ 48,276	$ 13,926	$ 9,689
Total Liabilities	203,962	40,667	465	4,743
Fund Equity	$ 77,173	$ 7,609	$ 13,461	$ 4,946

NOTE 11. SEGMENT INFORMATION FOR ENTERPRISE FUNDS AND PROPRIETARY AND FIDUCIARY FUND TYPES COMPONENT UNITS (CONTINUED)

Arizona Correctional Industries	Arizona Industries for the Blind	Healthcare Group of Arizona	Arizona Beef Council	ComCare	Other Enterprise Funds	Total
$ 16,703	$ 11,480	$ 20,476	$ 617	$ 106,567	$ 11,056	$ 481,038
672	555	8	5	2,952	488	7,200
15,113	11,681	28,572	669	103,321	13,645	427,481
918	(756)	(8,104)	(57)	294	(3,077)	46,357
173	1,167	283	7	(283)	23	1,682
-	-	8,000	-	-	4,518	12,518
(244)	(295)	(43)	-	-	(781)	(44,652)
$ 847	$ 116	$ 136	$ (50)	$ 11	$ 683	$ 15,905
$ 10,752	$ 4,572	$ 5,463	$ 195	$ 23,529	$ 3,460	$ 142,152
1,078	1,643	2,568	31	7,350	493	110,205
$ 9,674	$ 2,929	$ 2,895	$ 164	$ 16,179	$ 2,967	$ 31,947
$ 8,031	$ 5,304	$ 42	$ 40	$ 10,150	$ 14,447	$ 93,036
530	554	35	2	-	57	2,679
207	82	1	-	10,050	23	11,954
$ 8,354	$ 5,776	$ 76	$ 42	$ 100	$ 14,481	$ 83,761
$ -	$ -	$ -	$ -	$ -	$ -	$ 9,800
$ 3,167	$ 927	$ -	$ -	$ -	$ -	$ 5,633
$ (1,000)	$ -	$ -	$ -	$ -	$ (5)	$ (4,505)
$ 14,229	$ 7,403	$ 5,502	$ 205	$ 23,629	$ 16,187	$ 420,181
1,254	1,845	2,568	31	7,350	493	263,378
$ 12,975	$ 5,558	$ 2,934	$ 174	$ 16,279	$ 15,694	$ 156,803

NOTE 11. SEGMENT INFORMATION FOR ENTERPRISE FUNDS AND PROPRIETARY AND FIDUCIARY FUND TYPES COMPONENT UNITS (CONCLUDED)

Proprietary and Fiduciary Fund Types Component Units segment information for the fiscal year ended June 30, 1999, is shown below (expressed in thousands):

	Proprietary Fund Type		Fiduciary Fund Type	
Description	University Medical Center	Arizona Power Authority	Water Infrastructure Finance Authority	Total
Operating Revenues	$ 244,857	$ 21,549	$ 12,166	$ 278,572
Operating Expenses:				
Depreciation	17,257	44	-	17,301
Other	232,130	22,152	9,143	263,425
Operating Income (Loss)	(4,530)	(647)	3,023	(2,154)
Net Non-Operating Income (Loss)	(159)	246	-	87
Operating Transfers Out to Primary Government	-	(21)	-	(21)
Net Income (Loss)	$ (4,689)	$ (422)	$ 3,023	$ (2,088)
Current Assets	$ 95,012	$ 15,993	$ 33,581	$ 144,586
Current Liabilities	41,638	5,312	5,774	52,724
Net Working Capital	$ 53,374	$ 10,681	$ 27,807	$ 91,862
Property and Equipment:				
July 1, 1998	$ 227,380	$ 1,226	$ -	$ 228,606
Additions	24,357	11	-	24,368
Deletions	-	59	-	59
June 30, 1999	$ 251,737	$ 1,178	$ -	$ 252,915
Revenue Bonds	$ 74,798	$ 67,433	$ 144,656	$ 286,887
Contributed Capital	$ -	$ 9	$ 115,408	$ 115,417
Total Assets	$ 235,415	$ 76,915	$ 277,375	$ 589,705
Total Liabilities	138,586	72,745	150,474	361,805
Fund Equity	$ 96,829	$ 4,170	$ 126,901	$ 227,900

NOTE 12. FUND EQUITY

A. FUND BALANCES / RETAINED EARNINGS RESTATEMENT

Fund Balance and Retained Earnings at June 30, 1998, has been restated as follows (expressed in thousands):

	Primary Government			
	Special Revenue	Enterprise	Expendable Trust	Component Units
Fund Balances/Retained Earnings at June 30, 1998, as Previously Reported	$1,138,916	$ 126,650	$ 944,842	$ 106,101
Reporting Entity Addition:				
Water Infrastructure Finance Authority	-	-	-	8,470
Fund Reclassifications:				
State Parks Donations Fund	207	-	(207)	-
Veterans Services State Home Veteran Trust Fund	(60)	13,120	-	-
Prior Year Adjustment	-	-	1,723	-
Fund Balances/Retained Earnings as Restated July 1, 1998	$ 1,139,063	$ 139,770	$ 946,358	$ 114,571

1. Reporting Entity Additions

The Water Infrastructure Finance Authority (WIFA) is authorized to administer the Clean Water Revolving Fund and the Drinking Water Revolving Fund. The Clean Water Revolving Fund was created pursuant to the Federal Water Pollution Control Act of 1972, as amended by the Water Quality Act of 1987 (Clean Water Act) which required the State to establish the Fund to accept federal capitalization grants for publicly owned wastewater treatment projects. WIFA has entered into an agreement this year with the Environmental Protection Agency to administer the Drinking Water Revolving Fund pursuant to the Safe Drinking Water Act. The WIFA is considered a discrete component unit for financial reporting purposes.

2. Fund Reclassifications

Accounting and reporting treatment applied to a fund is determined by its measurement focus. The following funds' measurement focus changed during the fiscal year:

The State Parks Donation Fund receives monies from gifts, grants and other donations for the trail system. The State Parks Board does not act in a trustee capacity for these monies. Accordingly, the June 30, 1998 fund balance has been reclassified from an Expendable Trust Fund to a Special Revenue Fund.

The Veteran Services State Home for Veterans operates a nursing care institution for the State's Veterans. The Legislature has determined there is need to recover the costs of providing these services through user charges. Accordingly, the Veterans Services State Home for Veterans has been reclassified from a Special Revenue Fund to an Enterprise Fund. Including the effect of the change in measurement focus, the reclassification resulted in a net change of $13.120 million in fund equity from the Special Revenue Fund and the General Fixed Asset Account Group to the Enterprise Fund.

3. Prior Period Adjustment

The Veterans Services Fiduciary Division Fund asset amounts were understated by $1.723 million at June 30, 1998.

B. CHANGES IN CONTRIBUTED CAPITAL

The changes in contributed capital for fiscal year 1999 are shown below (expressed in thousands):

	Restated	Additions	Deletions	
	Beginning Balance July 1, 1998	Contributed Capital Transfers In	Contributed Capital Transfers Out	Ending Balance June 30, 1999
Enterprise Funds:				
Arizona Highways Magazine	$ 2,039	$ -	$ (500)	$ 1,539
Arizona Correctional Industries	3,146	21	-	3,167
Arizona Industries for the Blind	927	-	-	927
Internal Service Funds:				
Transportation Equipment	6,107	-	-	6,107
Technologies and Telecommunications	687	-	-	687
Motor Pool	13,954	1,998	-	15,952
Component Units:				
Arizona Power Authority	9	-	-	9
Water Infrastructure Finance Authority	79,759	35,649	-	115,408

NOTE 12. FUND EQUITY (CONCLUDED)

C. FUND BALANCES / RETAINED EARNINGS DETAIL

The following schedule details fund balances at June 30, 1999 (expressed in thousands):

	Governmental Fund Types				Fiduciary Fund Types	
	General	Special Revenue	Debt Service	Capital Projects	Trust	University
Fund Balances:						
Reserved for:						
Budget stabilization fund	$ 386,838	$ -	$ -	$ -	$ -	$ -
Highway construction	-	223,429	-	8,290	-	-
Inventory	1,267	-	-	-	-	-
Retirement benefits	-	-	-	-	28,322,613	-
Trust principal	-	-	-	-	2,033,599	-
Continuing appropriations	83,360	405,554	-	25,854	3,333	-
Debt service	-	-	35,972	-	-	-
Pool participants net assets	-	-	-	-	2,773,873	
Other	670	15,075	-	17	-	-
Unreserved:						
Restricted	-	-	-	-	-	282,551
Unrestricted:						
Designated	-	-	-	-	-	325,222
Undesignated	818,831	539,404	-	29,578	-	-
Total Fund Balances	$1,290,966	$1,183,462	$ 35,972	$ 63,739	$ 33,133,418	$ 607,773

Restricted fund balances for University Funds represents restrictions for U.S. Government grants refundable, endowments, quasi-endowments, restrictions for outstanding purchase orders, investment in joint venture and other restrictions of $28.172, $115.768, $28.762, $25.272, $14.000 and $70.577 million, respectively.

Designated fund balances for University Funds represents designations for outstanding purchase orders and other commitments, quasi-endowments, summer sessions, funding of ensuing year's budget and other designations of $34.375, $38.487, $8.973, $0.100 and $243.287 million, respectively.

The following schedule details retained earnings at June 30, 1999, (expressed in thousands):

	Proprietary Fund Types		
	Enterprise	Internal Service	Component Units
Retained Earnings (Deficits):			
Reserved for:			
Capital outlay	$ 1,912	$ -	$ 5,178
Replacement of equipment	-	9,985	-
Continuing appropriations	3,306	1,620	-
Other	79	-	948
Unreserved	145,873	(111,261)	94,864
Total Retained Earnings (Deficits)	$ 151,170	$ (99,656)	$ 100,990

D. DEFICIT FUND EQUITIES

The Internal Service Fund deficit results from the Risk Management and Workers' Compensation Funds net losses in prior years. The Risk Management and Workers' Compensation Fund deficits of $103.702 and $63.087 million, respectively, are primarily due to the State's policy of funding 60% of the actuarially determined liability. However, 100% of the liability is recorded for financial statement purposes. The Risk Management and Workers' Compensation Fund accumulated deficits at June 30, 1999, should be recovered through annual adjustments to insurance billings. The entire liability is reflected in the Internal Service Funds, rather than being allocated to other funds, to assist financial statement users in their understanding and analysis of the Risk Management and Workers' Compensation Funds.

NOTE 13. RELATED PARTY TRANSACTIONS

A. ARIZONA STATE UNIVERSITY

Not included in the accompanying financial statements are six financially interrelated organizations that are nonprofit corporations controlled by separate Boards of Directors whose goals are to support Arizona State University. Financial statements of these organizations are audited by independent auditors.

Four of these financially interrelated organizations (the Arizona State University Alumni Association, Arizona State University Foundation, Sun Angel Foundation and the Sun Angel Endowment) receive funds primarily through donations and dues, and contribute funds to the University for support of various programs.

A fifth financially interrelated organization, Price-Elliott Research Park, Inc. (Park), is developing a research park to promote and support research activities, in coordination with the University. In developing the research park, the Park has issued bonds guaranteed by the University.

As of June 30, 1999, the Park had $18.245 million of revenue bonds outstanding at an average interest rate of 5.26%. The debt service on the bonds is secured by a subordinated lien on University Main Campus revenues. Park revenues are not pledged in order to provide development flexibility to the Park.

Annual debt service on the Park bonds will be $993 thousand in fiscal 2000 and varies from a low of $898 thousand in fiscal 2004 to a high of $1.698 million in fiscal 2006. The University is obligated to pay the annual debt service, if not paid by the Park, under a debt service assurance agreement.

Beginning in fiscal 1990, the University provided operating cash advances to the Park repayable with interest to the University (1) upon the Park's total gross receipts for a fiscal year exceeding its total disbursements for that fiscal year and (2) before any Park surpluses are transferred to the Arizona State University Foundation. The last year for cash transfers to the Park was fiscal 1998. Since the Park's repayment to the University was dependent upon successful future operations and entering into of additional land leases, the transfers to the Park were recorded by the University as current year expenditures when made and not as an asset on the University's balance sheet. Total cash advances repayable to the University at June 30, 1999, including the accrued interest, totaled $8.291 million. During fiscal year 1999, the Park repaid $662 thousand to the University, with this amount being recorded as other source revenues with the timetable for future repayments dependent upon the Park entering into additional land leases.

A sixth financially interrelated organization, the Collegiate Golf Foundation, operates a University-owned golf course. Assets, net assets, and revenues for these organizations for the most recent fiscal years for which audits have been completed aggregated $202.5, $152.9, and $82.4 million, respectively, with substantially all of the net assets being donor restricted or endowment funds.

B. NORTHERN ARIZONA UNIVERSITY

The financial activities of the Northern Arizona University Foundation, Inc., are not included in the accompanying financial statements. The foundation is a nonprofit corporation controlled by a separate Board of Directors. The goals of the foundation are to promote the cause of education and the objectives of the University.

C. UNIVERSITY OF ARIZONA

The accompanying financial statements do not include the operations of the University of Arizona Foundation, Inc., the University Physicians, Inc., the Arizona Research Park Authority, and the Campus Research Corporation.

The University of Arizona Foundation, Inc. (Foundation) is a nonprofit corporation controlled by a separate Board of Directors. The principal goals of the Foundation are to support the University of Arizona through various fund-raising activities, and to contribute funds to the University for support of various programs. According to the audited financial statements of the Foundation for the year ended June 30, 1998, assets, liabilities, revenues, and expenditures totaled $219, $26, $93, and $43 million, respectively.

The University Physicians, Inc. (UPI) is a nonprofit corporation established to provide medical services and to support the University of Arizona in its teaching and research missions. UPI is controlled by a Board of Directors, comprised of the Dean, three faculty physicians, a representative of the twelve clinical department heads and three community members. The primary purpose of UPI is to assist the University's College of Medicine in achieving its teaching and research mission through the provision of patient care. According to the audited financial statements of UPI for the year ended June 30, 1998, assets, liabilities, revenues and expenditures totaled $84, $42, $116 and $118 million, respectively.

The Arizona Research Park Authority (ARPA) is a nonprofit corporation created with the permission of the Arizona Board of Regents (ABOR) and designated by Arizona law as a political subdivision of the State, governed by a separate board of directors which by law may not include officers or employees of ABOR. ARPA was established under the State's industrial development authority statute to assist in the acquisition, improvement, and operation of university research parks and related properties. In August 1994, ARPA, with the approval of ABOR, sold $98 million

NOTE 13. RELATED PARTY TRANSACTIONS (CONCLUDED)

of nontransferable special revenue bonds to International Business Machines Corporation (IBM) to enable the University to acquire from IBM a 345-acre developed industrial site (the "Research Park") near Tucson, Arizona, together with 1,000 acres of adjacent unimproved land (collectively, the University of Arizona Science and Technology Park or the "Park"). The transaction was accomplished through the following steps: (1) the University agreed to pay $98 million to IBM for title to the entire Park; (2) ARPA and Campus Research Corporation jointly agreed to lease the developed portion of the Park from the University for a period of 30 years with a prepaid rental of $98 million; (3) ARPA subleased 72% of the building space in the developed portion of the Park to IBM for periods of up to 30 years for a rental sufficient to pay debt service on ARPA's bonds; and (4) ARPA used the $98 million received from its bond sale to make the rental prepayment to the University who, in turn, applied the money to purchase the entire Park from IBM. The bonds are payable solely from lease rentals paid by IBM. If IBM defaults or cancels its lease, the bonds must be surrendered and discharged. Title to the entire Park resides in the University and neither the Park nor any payments by the University secures ARPA's bonds. Since the original transaction, IBM has reduced its leasehold to 70% of the building space for periods up to the remaining term of 25 years. Audited financial statements are not available.

The Campus Research Corporation (CRC) is a nonprofit corporation governed by a separate Board of Directors and was established to assist the University in the acquisition, improvement, and operation of the Research Park and related properties. CRC leases from the University the remaining 30% of the building space of the Research Park that is not leased to ARPA (see preceding paragraph). CRC is responsible for assisting in the development of the presently undeveloped portions of the Research Park and for subleasing to the University or to third parties currently existing unoccupied space, newly developed space, and space now occupied by IBM or its subtenants once the current subleases expire. The University is responsible for payment of operational expenses associated with the space occupied by the University departments, offices, and programs. All income received by CRC from its activities, after payment of expenses and financial reserves, will be turned over to the University.

CRC's June 30, 1998, audited financial statements disclosed:

- $7.284 million total assets, including $4.804 million of net intangible assets, $1.042 million of rents receivable, and $733 thousand of net property and equipment.
- $5.004 million total liabilities, including $4.419 million of long-term notes payable to Norwest Bank Arizona collateralized by leasehold interests.
- $2.902 million total revenues, including $1.001 million of rent revenues from the University and $1.878 million rent revenues from other tenants.
- $2.483 million total expenses, including $1.289 million of project operating costs, $377 thousand of interest, and $341 thousand of intangible assets amortization.

CRC's audited financial statements may be obtained by writing to P.O. Box 210066, Tucson, Arizona 85721-0066.

D. UNIVERSITY MEDICAL CENTER

The University Medical Center (UMC) and the University of Arizona (the University) both provide and receive services from each other under various contracts. Payments to the University by the UMC include resident and intern salaries, utilities, ground maintenance, mailroom operations and various administrative functions. Amounts paid to the University for these services were $12.624 million for the year ended June 30, 1999.

The UMC has entered into contractual agreements with the University to provide support for the academic mission of the University. Charges to the University for such services and facilities provided by the UMC were $9.516 million for the year ended June 30, 1999. These amounts are included in other operating revenue in the accompanying financial statements.

University Physicians, Inc. (UPI) is a not-for-profit corporation whose members are physicians employed by the University of Arizona and who practice at the UMC. The UMC has agreements with UPI whereby UPI provides physician and other services to the UMC.

NOTE 14. JOINT VENTURE

UNIVERSITY OF ARIZONA

The University of Arizona (the University) is a participant in the Large Binocular Telescope Corporation (LBT). LBT was formally incorporated as a not-for-profit corporation in August 1992, pursuant to a Memorandum of Understanding, as amended, executed on February 24, 1989, between the University and the Arcetri Astrophysical Observatory in Florence, Italy (Arcetri). The purpose of the joint venture is to design, develop, construct, own, operate and maintain a binocular telescope currently being constructed in Arizona. The current members of LBT are the University, Arcetri, Research Corporation, Ohio State University and LBT Beteiligungsgesellschaft (LBTB).

NOTE 14. JOINT VENTURE (CONCLUDED)

The University has committed resources equivalent to 25% of the project's construction costs and LBT's annual operating costs. As of June 30, 1999, the University has made cash contributions of $14.0 million toward the project's construction costs. The University's financial interest represents its future viewing/observation rights. Upon completion of construction, viewing rights will be divided equally among the participants in proportion to their contributions. According to the unaudited financial statements of LBT for the year ended December 31, 1998, assets, liabilities, revenues and expenditures totaled $50.0 million, $1.0 million, $15.0 million and $700 thousand, respectively.

NOTE 15. COMMITMENTS, CONTINGENCIES AND COMPLIANCE

A. RISK MANAGEMENT INSURANCE LOSSES

The Department of Administration - Risk Management Section manages the State's property, environmental, liability and workers' compensation losses. The State has determined that the management of these losses can be performed effectively and efficiently through the Risk Management Section. Consequently, all agencies and the State's three universities are required to participate in this program. The State's Risk Management Section evaluates the proper mix of purchased commercial insurance and self insurance annually.

The management and payment of these losses is accomplished through the funding mechanism of the Risk Management and Workers' Compensation Funds. As discussed in the following paragraph, an independent annual actuarial analysis is performed to evaluate the needed funding. Once the needed funding is determined, each agency is assessed an annual portion of the necessary funding based on their exposures and prior loss experience.

The State records claims liability when the reported loss is probable and reasonably estimated. On an annual basis an independent actuarial firm is engaged to estimate the State's total year-end outstanding claims liability, which takes into account recorded claims and related allocated claims adjustment expenditures, salvage, subrogation, loss development factors and an estimate for incurred but not reported claims.

Occasionally, the State agrees with claimants to purchase an annuity contract to settle these specific claims when it is determined that it is in the best interest of the State to do so. In these instances, the State requires the claimant to sign an agreement releasing the State from any further obligation. In addition, the State requires that a third party assignment company be named in the contract should the annuity company fail to perform its obligations under the annuity contract. As a result of these requirements, the likelihood that the State will be required to make future payments on these claims is remote.

There have been no significant reductions in the current fiscal year insurance coverage. There has been no settlements that have exceeded insurance premium coverage in the last three years.

The following table presents the changes in long-term claims liability balances during fiscal years ended June 30, 1998 and June 30, 1999 (expressed in thousands):

Fiscal Year	Beginning Balance	Current Year Claims and Changes in Estimates	Claims Payments	Ending Balance
Risk Management Fund:				
1998	$ 142,697	$ 3,726	$ 26,440	$ 119,983
1999	119,983	55,751	39,323	136,411
Workers' Compensation Fund:				
1998	84,416	7,193	15,544	76,065
1999	76,065	23,782	16,510	83,337

NOTE 15. COMMITMENTS, CONTINGENCIES AND COMPLIANCE (CONCLUDED)

B. LITIGATION

In *Ladewig vs. Waddell*, the plaintiff challenges the constitutionality of the deduction given for dividends received from corporations doing most of their business in Arizona. The Tax Court certified a class and found the tax to be unconstitutional. Class certification and a statute of limitations issue were appealed to the Court of Appeals and a decision is pending. Potential outcome of the case cannot be determined. The Court of Appeals may hold that only the plaintiff is entitled to refunds due to the statute of limitations. However, if class certification is affirmed, the estimated potential loss to the State is $300 to $400 million.

In *Kerr vs. Waddell*, federal employees have claimed an income tax refund on taxes paid on Federal employee contributions. The Board of Tax Appeals granted these claims for the years before 1991, but has denied the claim for later years. The State did not appeal. The plaintiffs appealed for years after 1990. The potential outcome cannot be determined. If this case were to have an unfavorable outcome, the State could incur losses ranging from $20 million to $100 million.

In *Roosevelt Elementary School District No. 66 vs. Jane Dee Hull*, the plaintiffs allege the defendants failed to fully fund the Building Renewal Fund established by the Students FIRST legislation. A motion to dismiss has been filed on behalf of all defendants. Briefing on that motion should be completed at the end of January 2000. The potential outcome is uncertain at this time. If the case were to have an unfavorable outcome, the State may be required to provide approximately $56 million in additional funding.

The State is also a defendant in a number of other pending lawsuits. All losses for any unsettled litigation or contingencies are determined on an actuarial basis and included in the Accrued Insurance Losses of the Internal Service Funds.

C. AUDITED FINANCIAL STATEMENTS

The four State pension plans, certain State agencies, commissions and authorities are audited by independent public accountants. Copies of these audits, as well as audits performed by the State Auditor General, are available from the State Library and Archives.

D. ACCUMULATED SICK LEAVE

Effective July 1, 1998, State employees are eligible to receive payment for an accumulated sick leave balance of 500 hours or more with a maximum of 1500 hours upon retirement directly from State service. The benefit value is calculated by taking the State hourly rate of pay at the retirement date, multiplied by the number of sick hours at the retirement date times the eligibility percentage. The eligibility percentage varies based upon the number of accumulated sick hours from 25 percent for 500 hours to a maximum of 50 percent for 1500 hours. The maximum benefit value is $30,000. The benefit is paid out in annual installments over three years. The Retiree Accumulated Sick Leave Fund is accounted for on the financial statements as an Expendable Trust Fund. The long-term portion of the accrued liability is recorded in the General Long Term Debt Account Group. Unused accumulated sick leave of employees of the State, excluding Universities, at June 30, 1999, totaled $232.470 million.

E. UNCLAIMED PROPERTY

The State of Arizona's Uniform Unclaimed Property Act requires deposit of certain unclaimed assets into a managed Agency Fund. ARS §44-323 requires a separate trust fund of not less than $100 thousand to be retained for prompt payment of claims. The excess amount, above that which is required to be retained, is required to be deposited to the General Fund where it is included as Other Revenue. Under a statute that took effect July 1, 1990, up to $1.0 million in unclaimed utility deposits is deposited in the Utility Assistance Fund to help low-income and elderly people make utility deposits and repairs. Fifty-five and twenty percent of the remaining net cash collected, after refunds, is transferred to the Department of Commerce Housing Fund to be used for low-cost housing and the State Treasurer for distribution as provided for in ARS §5-113, respectively. The balance is to be deposited in the General Fund. For fiscal year 1999, $818 thousand was deposited in the Utility Assistance Fund, $6.792 million was deposited in the Housing Fund, $2.465 million was deposited with the State Treasurer and $2.085 million was deposited in the General Fund. A total of approximately $142.213 million has been remitted since inception of the fund. In addition, the State is also holding stock valued at $11.268 million. The remittances to the General Fund and the holdings by the State represent contingencies, as claims for refunds can be made by the owners of the property. The Governmental Accounting Standards Board requires that a liability be reported to the extent that it is probable that escheat property will be reclaimed and paid to claimants. This liability is also reported as a reduction of revenue. This liability is reported in the General Fund because it is the fund to which the property ultimately escheats in Arizona. At June 30, 1999, this amount, reported as Due to Others in the General Fund, is $33.998 million.

F. CONSTRUCTION COMMITMENTS

The Arizona Department of Transportation had outstanding commitments under construction contracts of approximately $754.710 million at June 30, 1999.

NOTE 15. COMMITMENTS, CONTINGENCIES AND COMPLIANCE (CONCLUDED)

G. ARIZONA STATE LOTTERY

Annuities are purchased for all prizes over $400,000 for which winners will receive the jackpot in annual installments for the Lotto on-line game. These annuities are purchased from qualifying insurance companies that have the highest ratings from either A.M. Best Company, Standard & Poor, Moody, Duff & Phelps or Weiss. The Lottery remains contingently liable on all annuities. Aggregate future payments to prize winners on existing annuities totaled approximately $421.3 million at June 30, 1999. Approximately $319.6 million of the total aggregate future payments relates to annuities purchased from seven separate insurance companies, of which approximately $128.8 million relates to a single insurance company.
During 1991, an insurance company from which the Lottery purchased annuities in 1982 and 1983 was placed under State supervision but as of June 30, 1999, has been removed from State supervision. At June 30, 1999, remaining aggregate minimum future payments on such purchased annuities approximated $219 thousand. In 1994, an insurance company from which the Lottery purchased annuities during the period 1983 through 1989 was placed under State supervision. At June 30, 1999, remaining aggregate minimum future payments on such purchased annuities approximated $19.300 million. In 1997, an insurance company from which the Lottery purchased annuities in 1986 was placed under State supervision. At June 30, 1999, remaining aggregate minimum future payments on such purchased annuities approximated $4.140 million. During 1999, an insurance company from which the Lottery purchased annuities in 1984 was placed under State supervision. At June 30, 1999, remaining aggregate minimum future payments on such purchased annuities approximated $948 thousand. As of September 30, 1999, all four insurance companies were current in their required annuity payments. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the operations or financial position of the Lottery.

NOTE 16. COMCARE, INC.

ComCare, Inc. (ComCare), is an Arizona not-for-profit corporation dedicated to improving the health and welfare of individuals with substance abuse, behavioral/mental health disorders and serious mental illnesses. Under its contract with the Arizona Department of Health Services (ADHS), ComCare served as the sole Regional Behavior Health Authority (RBHA) for the Maricopa County under the State behavioral health system through September 18, 1998. As a RBHA, ComCare was responsible for the administration, coordination and delivery of comprehensive behavioral health services to residents of Maricopa County through a network of more than 130 provider agencies/individuals. ComCare's contract with ADHS represented approximately 95% of ComCare's revenue.

The RBHA contract between ADHS and ComCare required ComCare to maintain certain service levels and funding necessary to meet applicable legal requirements imposed on ADHS by state and federal law. Early in 1997, ADHS informed ComCare that certain actions, proposed actions and refusals to act by ComCare constituted breaches of contract regarding (i) potential failures of the State's legal responsibilities to the seriously mentally ill population, (ii) required financial standards and (iii) the adequacy of the network of subcontracted providers of behavioral health services. ComCare took the position that it was in compliance with the contract and did not modify its conduct. As a result, the Governor issued an executive order, pursuant to ARS §36-3412(E), declaring that an emergency existed in the behavioral health system. Thereafter, ComCare and ADHS began to litigate ComCare's performance under its contract with ADHS. ADHS sought a declaratory judgment that it had statutory authority to "directly operate" ComCare pursuant to ARS 36-3412(D), which provides as follows:

> The department's contracts with regional behavioral health authorities shall include terms authorizing the department to operate a regional behavioral health authority directly. These contract terms shall stipulate the circumstances under which the department could step in for direct operation. The department shall after delivering notice to the regional behavioral health authority in question, operate the regional behavioral health authority for only as long as it is necessary to assure delivery of uninterrupted care to clients and accomplish the orderly transition of those members to a new regional behavioral health authority, to other existing regional behavioral health authorities, or until the regional behavioral health authority in question reorganizes or otherwise corrects the contract performance failure.

On September 5, 1997, after extensive court proceedings in two separate venues, and with a third lawsuit having been filed, ComCare and ADHS agreed to settle all litigation. Under the terms of the settlement, the lawsuits would be dismissed and ADHS would assume direct operation of ComCare pursuant to ARS §36-3412(D). ComCare agreed to reorganize itself to effectuate the transfer of direct operation of ComCare to ADHS. Although ADHS began to directly operate ComCare following the settlement, ComCare continued observing all corporate formalities and continued to provide services and receive payments in accordance with the requirements of the contract between ADHS and ComCare.

NOTE 16. COMCARE, INC. (CONCLUDED)

ComCare's contract with ADHS expired September 18, 1998. ADHS awarded the contract to a separate unrelated entity, ValueOptions, a division of FHC Health Systems. ComCare entered into a sub-contract agreement with ValueOptions from September 19, 1998 through February 8, 1999. Under the sub-contract agreement with ValueOptions, ComCare was responsible for the same services previously covered by its contract with ADHS. The remaining 5% of ComCare's revenue stream was generated from housing grants from Department of Housing and Urban Development (HUD) and the Department of Commerce (DOC). The HUD grants were assigned to a third party beginning June 1, 1999. ComCare assigned the remaining DOC grants to a third party beginning in August 1999. Subsequent to February 8, 1999, the majority of ComCare's revenue stream ceased and ComCare disposed of the majority of its assets and terminated the majority of its employees. Revenues and expenses related to these transactions are included in the accompanying financial statements. Accordingly, the carrying values of the remaining assets are presented at estimated net realizable values and all liabilities are presented at estimated settlement amounts. Management believes these amounts approximate the ultimate liquidation amount. It is not presently determinable whether the amounts realizable from the disposition of the remaining assets or the amounts that creditors agree to accept in settlement of the obligations due them will differ materially from the amounts shown in the accompanying financial statements.

Subsequent to June 30, 1999, ComCare completed a formal plan of liquidation whereby a trust has been established to receive ComCare's net assets after settlement of liabilities. The purpose of the trust will be to distribute the net assets in accordance with ComCare's charitable purpose and for the benefit of behavioral health services as directed by the Trustee. ADHS will serve as the Policy Trustee and ValueOptions will serve as Administrative Trustee. In August 1999, ComCare transferred approximately $3.7 million to the trust. The remainder of the net assets will be transferred upon final settlement of the remaining obligations of ComCare. The accompanying financial statements do not include any adjustments relating to the ultimate recoverability and classification of asset carrying amounts or the amount and classification of ComCare's existing liabilities or other liabilities that might result from the uncertainty related to the ultimate resolution of ComCare's net assets.

NOTE 17. TOBACCO SETTLEMENT

The State is one of many states participating in the settlement of litigation with the tobacco industry over the reimbursement of healthcare costs. The State's share of the settlement agreement totals $3.151 billion, payable over 25 years. This amount includes a "Strategic Contribution Fund" payment of $263.062 million that the State earned for its role in the settlement.

The State Specific Finality is the date on which Arizona's interest in its share of the payments "vests." The State obtains State Specific Finality when: The trial court in that State has approved the master settlement agreement, the consent decree, and dismissed claims against the participating manufacturers, which has occurred in Arizona, and the time to appeal that approval has run without an appeal or, if there is an appeal, that appeal has been resolved in favor of the master settlement agreement being approved. The tobacco industry is not satisfied that the State has met this prong of the test because of litigation filed on behalf of 13 of the 15 counties in Arizona. The counties' litigation contends that they are eligible for a portion of State's share of the national tobacco settlement.

The master settlement agreement is automatically terminated with respect to any state that does not achieve State Specific Finality on or before December 31, 2001.

The State has elected not to accrue any portion of its share in the master settlement agreement on the financial statements because the amount to be distributed to the State is not measurable or available as of June 30, 1999. When the State becomes eligible for its share of the master settlement agreement, the State will accrue the amount on the balance sheet as a receivable and deferred revenue, reduced by any of the amount that has been collected.

NOTE 18. CONDUIT DEBT

In November 1998, the Greater Arizona Development Authority (GADA), part of the primary government, issued $13.270 million in Infrastructure Revenue Bonds, Series 1998 for public infrastructure projects in the communities of Avondale, Goodyear and Winslow. The State appropriated $20 million to GADA for the express purpose of securing bonds issued by the GADA. The Series 1998 Bonds were issued by GADA to make loans to the participants listed above and constitute special, limited obligations of GADA payable solely from the funds which are held in Trust by the Trustee (the Trust Estate). The Trust Estate includes debt service payments required to be made by the participants in the Series 1998 Bond Issue. The bonds do not constitute a legal debt of the GADA or the State, and accordingly have not been reported in the accompanying financial statements.

At June 30, 1999, Infrastructure Revenue Bonds outstanding aggregated $13.270 million.

NOTE 19. SUBSEQUENT EVENTS

A. PRIMARY GOVERNMENT

1. Department of Transportation

On July 21, 1999, the Department of Transportation (the Department) issued $124.695 million in Transportation Excise Tax Revenue Bonds (1999 Series) to (i) advance refund portions of the Transportation Board's Senior Bonds, (ii) finance the acquisition of land and the design and construction of certain controlled access highways within Maricopa County, Arizona and (iii) pay costs of issuing the 1999 Series Bonds. The 1999 Series Bonds are due July 1, 2000 through 2005.

Net proceeds totaled $126.690 million (after receipt of $2.112 million of reoffering premium and payment of $117 thousand in underwriting fees). Net proceeds of $4.712 million were used to advance refund $4.640 million of the 1991 Series A, Senior Transportation Excise Tax Revenue Bonds (Refunded Bonds). State and Local Government securities were purchased with these proceeds and were deposited in an irrevocable trust with an escrow agent to provide for the partial future debt service payments on the above-referenced bonds. As a result, the Refunded Bonds will be considered defeased and the liability for these bonds will be removed from the General Long-Term Debt Account Group. The Department advance refunded the Refunded Bonds to reduce its total debt service payments over the next two years by $57 thousand and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of $56 thousand.

On November 16, 1999, the Department issued $151.080 million in Highway Revenue Bonds (Series 1999) to (i) finance portions of the Board's five year capital program, (ii) advance refund portions of the Board's outstanding Senior Bonds and Subordinated Bonds and (iii) pay costs of issuing series 1999 Bonds. The Series 1999 Bonds are due July 1, 2001 through July 1, 2019.

Net proceeds totaled $151.926 million (after receipt of $1.782 million of reoffering premium and payment of $935 thousand in underwriting fees). Net proceeds of $21.409 were used to advance refund $9.065 million of the Senior Series 1990 Bonds and $11.410 million of the Subordinated 1991 Series A Bonds. State and Local Government securities were purchased with these proceeds and were deposited in an irrevocable trust with an escrow agent to provide for the partial future debt service payments on the above-referenced bonds. As a result, the Refunded Bonds will be considered defeased and the liability for these bonds will be removed from the General Long Term Debt Account Group. The ADOT advance refunded the Refunded Bonds to reduce its total debt service payments over the next three years by $491 thousand and to obtain an economic gain (difference between the present values of the debt service payment on the old and new debt) of $407 thousand.

2. University of Arizona

On August 19, 1999, the University of Arizona issued Certificates of Participation Series 1999A for $21.607 million and Series 1999B for $36.500 million. The proceeds are being used to finance a portion of the costs of constructing and equipping a new student union and bookstore facility. The Series 1999A issue consists of $19.266 million fixed rate current interest certificates and $2.341 million of fixed rate capital appreciation certificates and have interest ranging from 5 to 5.53 percent. The Series 1999B certificates are variable rate current interest certificates that initially bear interest at the rate of 3.55 percent for the initial period through March 7, 2000. Thereafter, at the option of the Arizona Board of Regents, the certificates are subject to conversion to an adjustable rate, an annual rate, or a term rate pursuant to the trust agreement. If not converted, the certificates will bear interest at a weekly rate not to exceed 12 percent determined under prevailing market conditions by the remarketing agent.

NOTE 19. SUBSEQUENT EVENTS (CONCLUDED)

B. COMPONENT UNITS

1. Water Infrastructure Finance Authority of Arizona

Effective September 8, 1999, Water Infrastructure Finance Authority of Arizona (WIFA) issued $64 million of bonds to refund Series 1991 bonds, a portion of Series 1992 bonds, a portion of Series 1995 bonds and a portion of Series 1996 bonds and the bonds and the loans from Series 1997 and 1998 were transferred into WIFA's common open pool, subject to a new Master Trust Indenture. Under the new Master Trust Indenture, loans will be originated using all of WIFA's available funds, including federal capital grants, state match monies, certain investment earnings and bond proceeds. All assets designated as pledged pursuant to the Master Indenture will secure and be the source of payment of all bonds.