BASIC FINANCIAL STATEMENTS

BASIC FINANCIAL STATEMENTS

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STATE OF ARIZONA
STATEMENT OF NET ASSETS
JUNE 30, 2007
(Expressed in Thousands)

	PRIMARY GOVERNMENT			
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL PRIMARY GOVERNMENT	COMPONENT UNITS
ASSETS				
Current Assets:				
Cash	$ 8,569	$ 149,582	$ 158,151	$ 19,554
Cash with U.S. Treasury	-	1,029,326	1,029,326	-
Cash and pooled investments with State Treasurer	3,228,764	256,286	3,485,050	90,626
Restricted cash and pooled investments with State Treasurer	-	130,137	130,137	-
Cash held by trustee	-	-	-	62,129
Collateral investment pool	-	132,606	132,606	-
Short-term investments	-	99,076	99,076	92,818
Restricted investments held by trustee	-	-	-	19,660
Receivables, net of allowances:				
Taxes	573,411	75,851	649,262	-
Interest	101,374	4,159	105,533	8,816
Loans and notes	20,802	11,732	32,534	-
Other	128,464	103,545	232,009	83,178
Internal balances	117,128	(117,128)	-	-
Due from U.S. Government	530,500	68,373	598,873	-
Due from local governments	61	122	183	-
Due from others	89	-	89	-
Inventories, at cost	12,746	30,392	43,138	11,218
Other current assets	20,998	5,592	26,590	2,626
Total Current Assets	4,742,906	1,979,651	6,722,557	390,625
Noncurrent Assets:				
Restricted assets:				
Cash	2,644	18,417	21,061	-
Cash and pooled investments with State Treasurer	1,207,257	-	1,207,257	-
Cash held by trustee	2,965	105,649	108,614	-
Investments	3,250	38,647	41,897	-
Investments held by trustee	-	31,136	31,136	145,122
Receivables, net of allowances:				
Loans and notes	966,137	38,373	1,004,510	682,375
Other	-	6,239	6,239	-
Securities held in escheat	60,268	-	60,268	-
Investments	-	494,057	494,057	80,896
Endowment investments	2,539,257	316,294	2,855,551	-
Other noncurrent assets	-	16,512	16,512	49,011
Capital assets:				
Infrastructure, land, and other non-depreciable	14,345,024	288,747	14,633,771	30,180
Depreciable buildings, property and equipment, net of accumulated depreciation	1,467,393	2,805,954	4,273,347	115,005
Total Noncurrent Assets	20,594,195	4,160,025	24,754,220	1,102,589
Total Assets	25,337,101	6,139,676	31,476,777	1,493,214

The Notes to the Financial Statements are an integral part of this statement.

(Continued)

STATE OF ARIZONA
STATEMENT OF NET ASSETS
JUNE 30, 2007
(Expressed in Thousands)

	PRIMARY GOVERNMENT			
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL PRIMARY GOVERNMENT	COMPONENT UNITS
LIABILITIES				
Current Liabilities:				
Accounts payable and other current liabilities	$ 514,466	$ 111,731	$ 626,197	$ 46,517
Payable for securities purchased	51,105	1,463	52,568	-
Accrued liabilities	699,354	74,423	773,777	25,276
Obligations under securities loan agreements	-	132,606	132,606	-
Tax refunds payable	20,279	-	20,279	-
Due to U.S. Government	6,947	9	6,956	-
Due to local governments	358,957	9,304	368,261	-
Due to others	126,862	72,260	199,122	-
Unearned deferred revenue	67,264	105,879	173,143	-
Current portion of accrued insurance losses	52,272	30,856	83,128	2,572
Current portion of long-term debt	247,167	89,253	336,420	32,855
Current portion of other long-term liabilities	143,271	9,998	153,269	5,848
Total Current Liabilities	2,287,944	637,782	2,925,726	113,068
Noncurrent Liabilities:				
Unearned deferred revenue	39,946	29,870	69,816	2,629
Contracts payable	-	18,031	18,031	-
Accrued insurance losses	291,833	370,292	662,125	10,590
Funds held for others	-	53,268	53,268	-
Long-term debt	3,791,365	1,902,488	5,693,853	836,923
Other long-term liabilities	8,314	54,568	62,882	7,203
Total Noncurrent Liabilities	4,131,458	2,428,517	6,559,975	857,345
Total Liabilities	6,419,402	3,066,299	9,485,701	970,413
NET ASSETS				
Invested in capital assets, net of related debt	13,500,218	1,180,518	14,680,736	35,714
Restricted for:				
Federal grants	40,737	-	40,737	-
Capital projects	1,003,824	8,505	1,012,329	-
Unemployment Compensation	-	1,075,038	1,075,038	-
Debt service	38,804	11,119	49,923	9,948
Permanent funds and University funds:				
Expendable	21,290	210,635	231,925	-
Nonexpendable	3,467,467	199,471	3,666,938	-
Loans and other financial assistance: expendable	-	71,211	71,211	273,096
Other purposes	169,972	12	169,984	-
Unrestricted	675,387	316,868	992,255	204,043
Total Net Assets	$ 18,917,699	$ 3,073,377	$ 21,991,076	$ 522,801

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
STATEMENT OF FINANCIAL POSITION
UNIVERSITIES - AFFILIATED COMPONENT UNITS
JUNE 30, 2007
(Expressed in Thousands)

ASSETS		
Cash and cash equivalent investments	$	95,132
Receivables:		
Pledges receivable		180,666
Other receivables		18,389
Total receivables		199,055
Investments:		
Investments in securities		982,338
Investments held in trust for Universities		8,924
Other investments		70,429
Total investments		1,061,691
Net direct financing leases		111,081
Property and equipment, net of accumulated depreciation		279,144
Other assets		44,853
Total Assets		1,790,956
LIABILITIES		
Liability under Universities' endowment trust agreements		100,184
Bonds payable		475,040
Unearned revenue		29,893
Other liabilities		57,416
Total Liabilities		662,533
NET ASSETS		
Permanently restricted		653,720
Temporarily restricted		398,173
Unrestricted		76,530
Total Net Assets	$	1,128,423

The Notes to the Financial Statements are an integral part of this statement.

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STATE OF ARIZONA
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

		PROGRAM REVENUES		
	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS
FUNCTIONS/PROGRAMS				
PRIMARY GOVERNMENT:				
Governmental Activities:				
General government	$ 802,659	$ 200,495	$ 104,323	$ 72
Health and welfare	9,789,699	76,869	6,903,461	-
Inspection and regulation	175,609	158,022	19,754	-
Education	5,984,196	47,615	1,238,158	-
Protection and safety	1,401,513	91,477	155,121	-
Transportation	583,304	158,019	70,879	354,024
Natural resources	193,862	65,835	44,334	159
Intergovernmental revenue sharing	2,864,543	-	-	-
Interest on long-term debt	191,674	-	-	-
Total Governmental Activities	21,987,059	798,332	8,536,030	354,255
Business-type Activities:				
Universities	2,960,790	1,069,339	832,411	27,981
Unemployment Compensation	248,111	325,081	50,167	-
Industrial Commission Special Fund	23,669	42,741	-	-
Lottery	363,508	462,200	-	-
Other	176,486	151,100	795	-
Total Business-type Activities	3,772,564	2,050,461	883,373	27,981
Total Primary Government	$ 25,759,623	$ 2,848,793	$ 9,419,403	$ 382,236
COMPONENT UNITS:				
Water Infrastructure Finance Authority	$ 30,033	$ 20,545	$ 12,710	$ -
University Medical Center	428,327	442,569	-	-
Arizona Power Authority	28,607	28,301	-	-
Total Component Units	$ 486,967	$ 491,415	$ 12,710	$ -

General Revenues:
Taxes:
Sales
Income
Tobacco
Property
Motor vehicle and fuel
Other
Unrestricted investment earnings
Unrestricted grants and contributions
Gain on sale of trust land
Miscellaneous
Contributions to permanent endowments
Transfers
Total General Revenues, Contributions, Gains, and Transfers
Change in Net Assets
Net Assets - Beginning, as restated

Net Assets - Ending

The Notes to the Financial Statements are an integral part of this statement.

NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS			
PRIMARY GOVERNMENT			
GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL PRIMARY GOVERNMENT	COMPONENT UNITS
$ (497,769)		$ (497,769)	
(2,809,369)		(2,809,369)	
2,167		2,167	
(4,698,423)		(4,698,423)	
(1,154,915)		(1,154,915)	
(382)		(382)	
(83,534)		(83,534)	
(2,864,543)		(2,864,543)	
(191,674)		(191,674)	
(12,298,442)		(12,298,442)	
	$ (1,031,059)	(1,031,059)	
	127,137	127,137	
	19,072	19,072	
	98,692	98,692	
	(24,591)	(24,591)	
	(810,749)	(810,749)	
(12,298,442)	(810,749)	(13,109,191)	
			$ 3,222
			14,242
			(306)
			17,158
6,537,584	79,223	6,616,807	-
4,636,447	-	4,636,447	-
358,205	-	358,205	-
43,736	-	43,736	-
1,826,893	-	1,826,893	-
529,629	-	529,629	-
261,099	103,362	364,461	31,037
11,711	-	11,711	-
451,501	-	451,501	-
212,253	77,841	290,094	8,330
-	4,815	4,815	-
(876,456)	876,456	-	-
13,992,602	1,141,697	15,134,299	39,367
1,694,160	330,948	2,025,108	56,525
17,223,539	2,742,429	19,965,968	466,276
$ 18,917,699	$ 3,073,377	$ 21,991,076	$ 522,801

STATE OF ARIZONA
STATEMENT OF ACTIVITIES
UNIVERSITIES - AFFILIATED COMPONENT UNITS
JUNE 30, 2007
(Expressed in Thousands)

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
REVENUES				
Contributions	$ 16,907	$ 111,155	$ 74,611	$ 202,673
Rental revenue	30,506	-	-	30,506
Sales and services	23,424	-	-	23,424
Net investment income	8,728	70,802	35,365	114,895
Net assets released from restrictions	112,219	(96,597)	(15,622)	-
Capital lease revenue	22,295	-	-	22,295
Other revenues	26,380	4,728	717	31,825
Total Revenues	240,459	90,088	95,071	425,618
EXPENSES				
Program services:				
Payments to Universities	82,537	-	-	82,537
Leasing related expenses	6,680	-	-	6,680
Payments on behalf of Universities	20,116	-	-	20,116
Other program services	17,967	-	-	17,967
Personal services, operations, and administrative expenses	47,263	-	-	47,263
Fundraising expenses	7,904	-	-	7,904
Interest	13,793	-	-	13,793
Assets expensed under capital lease agreement	19,928	-	-	19,928
Other expenses	20,674	-	-	20,674
Total Expenses	236,862	-	-	236,862
Increase in Net Assets	3,597	90,088	95,071	188,756
Net Assets - Beginning, as restated	73,069	314,368	563,459	950,896
Transfers	(136)	157	(21)	-
Cumulative effect of accounting changes	-	(6,440)	(4,789)	(11,229)
Net Assets - Ending	$ 76,530	$ 398,173	$ 653,720	$ 1,128,423

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2007
(Expressed in Thousands)

	GENERAL FUND	TRANSPORTATION & AVIATION PLANNING, HIGHWAY MAINTENANCE & SAFETY FUND	LAND ENDOWMENTS FUND	OTHER GOVERNMENTAL FUNDS	TOTAL
ASSETS					
Cash	$ 1,150	$ -	$ 28	$ 5,052	$ 6,230
Cash and pooled investments with State Treasurer	1,872,859	147,349	48,006	1,000,853	3,069,067
Receivables, net of allowances:					
Taxes	492,846	62,122	-	18,443	573,411
Interest	42,058	3,268	51,698	4,324	101,348
Loans and notes	-	7,623	979,316	-	986,939
Other	78,392	9,154	4,757	27,701	120,004
Due from U.S. Government	478,175	49,544	-	-	527,719
Due from local governments	61	-	-	-	61
Due from others	-	-	-	89	89
Due from other Funds	254,878	20,001	367	83,238	358,484
Inventories, at cost	3,053	5,757	-	156	8,966
Restricted assets:					
Cash	2,644	-	-	-	2,644
Cash and pooled investments with State Treasurer	40,210	957,037	-	210,010	1,207,257
Cash held by trustee	188	-	-	2,777	2,965
Investments	3,250	-	-	-	3,250
Securities held in escheat	60,268	-	-	-	60,268
Endowment investments	-	-	2,539,257	-	2,539,257
Other	213	8,128	-	1	8,342
Total Assets	$ 3,330,245	$ 1,269,983	$ 3,623,429	$ 1,352,644	$ 9,576,301
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable and other current liabilities	$ 272,243	$ 112,728	$ 18,112	$ 35,641	$ 438,724
Payable for securities purchased	-	-	51,105	-	51,105
Accrued liabilities	261,698	9,970	198	81,415	353,281
Tax refunds payable	20,279	-	-	-	20,279
Due to U.S. Government	6,947	-	-	-	6,947
Due to local governments	115,974	130,374	-	112,609	358,957
Due to others	126,832	-	1	29	126,862
Due to other Funds	63,087	175,721	13,269	11,056	263,133
Unavailable deferred revenue	486,143	7,623	1,033,700	1,203	1,528,669
Unearned deferred revenue	53,943	-	51,987	1,280	107,210
Matured notes payable	-	3,309	-	-	3,309
Total Liabilities	1,407,146	439,725	1,168,372	243,233	3,258,476
Fund Balances:					
Reserved for:					
Budget stabilization fund	673,531	-	-	-	673,531
Highway construction	-	769,407	-	207,081	976,488
Other construction	-	-	-	5,288	5,288
School facilities improvements	4,931	-	-	-	4,931
Permanent funds	-	-	2,454,564	-	2,454,564
Continuing appropriations	162,657	54,267	493	39,842	257,259
Debt service	-	-	-	34,421	34,421
Other fund balance reservations	272	25,757	-	-	26,029
Unreserved	1,081,708	(19,173)	-	-	1,062,535
Unreserved reported in:					
Non-major special revenue funds	-	-	-	822,779	822,779
Total Fund Balances	1,923,099	830,258	2,455,057	1,109,411	6,317,825
Total Liabilities and Fund Balances	$ 3,330,245	$ 1,269,983	$ 3,623,429	$ 1,352,644	$ 9,576,301

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS
JUNE 30, 2007
(Expressed in Thousands)

Total fund balances - governmental funds		$ 6,317,825
Amounts reported for governmental activities in the Statement of Net Assets are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		15,743,932
Certain receivables are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		1,528,669
Internal service funds are used by management to charge the costs of certain activities to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the Statement of Net Assets.		(191,921)
The allocation of the internal service fund accumulated net loss results in an amount due from business-type activities, which is not reported in the governmental funds.		20,416
Deferred issue costs are reported as current expenditures in the governmental funds. However, deferred issue costs are amortized over the life of the bonds and are included in the governmental activities in the Statement of Net Assets.		8,025
Long-term debt is not due and payable from current financial resources and, therefore, is not reported in the governmental funds. These amounts consist of:		
Revenue bonds	(2,328,840)	
Grant anticipation notes	(282,860)	
Certificates of participation	(959,865)	
Capital leases	(233,658)	
Installment purchase contracts	(10,644)	
Premium on debt	(225,071)	
Deferred amount on refundings	14,266	(4,026,672)
Accrued liabilities for AHCCCS programmatic costs and reimbursements are not due and payable from current financial resources and, therefore, are not reported in the governmental funds.		(330,383)
Accrued interest on long-term obligations is not due and payable from current financial resources and, therefore, is not reported in the governmental funds.		(14,839)
Other long-term liabilities are not due and payable from current financial resources and, therefore, are not reported in the governmental funds. Those liabilities consist of:		
Compensated absences		(139,893)
Other long-term assets are not available to pay for current-period expenditures and, therefore, are not reported in the governmental funds. Those assets consist of:		
Other non-current assets		2,540
Net assets of governmental activities		$ 18,917,699

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

	GENERAL FUND	TRANSPORTATION & AVIATION PLANNING, HIGHWAY MAINTENANCE & SAFETY FUND	LAND ENDOWMENTS FUND	OTHER GOVERNMENTAL FUNDS	TOTAL
REVENUES					
Taxes:					
Sales	$ 5,666,980	$ 262,264	$ -	$ 598,724	$ 6,527,968
Income	4,629,179	-	-	41	4,629,220
Tobacco	98,436	-	-	259,769	358,205
Property	28,433	15,303	-	-	43,736
Motor vehicle and fuel	686	1,821,718	-	6,297	1,828,701
Other	438,539	-	-	91,090	529,629
Intergovernmental	7,832,627	429,656	65	51,372	8,313,720
Licenses, fees, and permits	113,730	130,378	-	198,128	442,236
Earnings on investments	172,435	48,152	267,292	40,145	528,024
Sales and charges for services	84,465	13,372	34,778	25,703	158,318
Fines, forfeitures, and penalties	25,809	-	-	158,114	183,923
Gaming	6,751	-	-	88,020	94,771
Tobacco settlement	90,258	-	-	-	90,258
Other	120,737	10,028	33,240	100,435	264,440
Total Revenues	19,309,065	2,730,871	335,375	1,617,838	23,993,149
EXPENDITURES					
Current:					
General government	740,098	-	6	139,415	879,519
Health and welfare	9,333,871	-	5,213	340,142	9,679,226
Inspection and regulation	60,107	-	-	113,790	173,897
Education	5,296,593	-	45,428	641,492	5,983,513
Protection and safety	1,258,908	-	3,627	95,904	1,358,439
Transportation	1,188	518,692	-	4,438	524,318
Natural resources	28,610	-	7	156,975	185,592
Intergovernmental revenue sharing	1,645,335	1,217,883	-	-	2,863,218
Debt service:					
Principal	46,773	-	-	173,700	220,473
Interest and other fiscal charges	47,966	2,472	-	144,879	195,317
Capital outlay	187,812	575,286	94	228,808	992,000
Total Expenditures	18,647,261	2,314,333	54,375	2,039,543	23,055,512
Excess (Deficiency) of Revenues Over Expenditures	661,804	416,538	281,000	(421,705)	937,637
OTHER FINANCING SOURCES (USES)					
Transfers in	198,960	248,191	24	463,430	910,605
Transfers out	(1,287,356)	(297,489)	(69,145)	(130,843)	(1,784,833)
Proceeds from sale of trust land	-	-	199,089	-	199,089
Proceeds from sale of capital assets	-	10,162	-	-	10,162
Capital lease and installment purchase contracts	83,553	2,128	-	47,304	132,985
Bonds issued	-	-	-	325,000	325,000
Premium on bonds issued	-	-	-	26,201	26,201
Total Other Financing Sources (Uses)	(1,004,843)	(37,008)	129,968	731,092	(180,791)
Net Change in Fund Balances	(343,039)	379,530	410,968	309,387	756,846
Fund Balances - Beginning	2,266,138	450,728	2,044,089	800,024	5,560,979
Fund Balances - Ending	$ 1,923,099	$ 830,258	$ 2,455,057	$ 1,109,411	$ 6,317,825

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2007

(Expressed in Thousands)

Net change in fund balances - total governmental funds		$ 756,846
Amounts reported for governmental activities in the Statement of Activities are different because:		
Capital outlays are reported as expenditures in governmental funds. However, in the Statement of Activities, the cost of assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		
Capital outlay	992,000	
Infrastructure Adjustment	(57,818)	
Depreciation expense	(109,769)	824,413
The net income of internal service funds is included with governmental activities in the Statement of Activities.		39,679
Some revenues reported in the Statement of Activities are not currently available at year-end and are not reported as revenue in the governmental funds.		
Operating grants	65,654	
Income taxes	7,227	
Sales taxes	9,616	
Accrued interest on land sales contracts	21,128	
Other revenue	1,600	105,225
Trust land sales are financed with long-term mortgages. In the Statement of Activities, the gain on sale of trust land is reported, whereas in the governmental funds, the proceeds from the collection of mortgage payments are reported.		252,412
Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds.		
AHCCCS accrued programmatic costs	(93,313)	
Compensated absences	(17,964)	
Other noncurrent expenses	(4,184)	(115,461)
Certain expenditures that are reported in the governmental funds in the current year, but were incurred in prior fiscal years, are not reported in the Statement of Activities.		
Ladewig vs. State of Arizona lawsuit	76,116	
Kerr vs. Killian lawsuit	15,000	91,116

The Notes to the Financial Statements are an integral part of this statement.

(Continued)

STATE OF ARIZONA

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2007

(Expressed in Thousands)

Bond proceeds provide current financial resources to the governmental funds; however, issuing debt increases long-term liabilities in the Statement of Net Assets. In the current period, proceeds were received from:		
New bonds issued	(325,000)	
Premium on bonds issued	(26,201)	(351,201)
Repayment of long-term debt is reported as an expenditure in governmental funds, but the repayment reduces noncurrent liabilities in the Statement of Net Assets. In the current year, these amounts consist of:		
Debt service principal	220,473	
Debt premium/discount amoritization	21,089	
Amortization of bond issuance costs	959	
Amoritization of deferred amount	(3,566)	238,955
Accrued interest on long-term obligations is not due and payable from current financial resources and, therefore, is not reported in the governmental funds.		(14,839)
Some capital asset additions were financed through capital leases and installment purchase contracts. Such financing arrangements are reported as an other financing source in the governmental funds, however, these amounts are reported as liabilities in the Statement of Net Assets.		(132,985)
Change in net assets of governmental activities		$ 1,694,160

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2007
(Expressed in Thousands)

	BUSINESS-TYPE ACTIVITIES - ENTERPRISE FUNDS				
	UNIVERSITIES	UNEMPLOYMENT COMPENSATION	INDUSTRIAL COMMISSION SPECIAL FUND	LOTTERY	OTHER
ASSETS					
Current Assets:					
Cash	$ 101,390	$ -	$ 47,549	$ -	$ 643
Cash with U.S. Treasury	-	1,029,326	-	-	-
Cash and pooled investments with State Treasurer	169,268	-	1,828	59,816	25,374
Restricted cash and pooled investments with State Treasurer	-	-	-	-	130,137
Collateral investment pool	79,306	-	53,300	-	-
Short-term investments	98,979	-	-	-	97
Receivables, net of allowances:					
Taxes	-	70,433	5,418	-	-
Interest	1,293	-	2,073	-	793
Loans and notes	4,017	-	-	-	7,715
Other	82,685	8,061	1,202	4,265	7,332
Due from U.S. Government	68,229	-	-	-	144
Due from local governments	-	-	-	-	122
Due from other Funds	-	-	-	-	99,041
Inventories, at cost	19,150	-	-	3,946	7,296
Other current assets	5,181	-	-	-	411
Total Current Assets	629,498	1,107,820	111,370	68,027	279,105
Noncurrent Assets:					
Restricted assets:					
Cash	18,417	-	-	-	-
Cash held by trustee	105,649	-	-	-	-
Investments	38,647	-	-	-	-
Investments held by trustee	31,135	-	1	-	-
Receivables, net of allowances:					
Loans and notes	30,306	-	-	-	8,067
Other	6,239	-	-	-	-
Investments	196,447	-	297,610	-	-
Endowment investments	316,294	-	-	-	-
Other long-term assets	9,384	-	-	7,128	-
Capital assets:					
Infrastructure, land, and other non-depreciable	278,982	-	2,996	1,056	5,713
Depreciable buildings, property and equipment, net of accumulated depreciation	2,768,501	-	18,163	3,099	16,191
Total Noncurrent Assets	3,800,001	-	318,770	11,283	29,971
Total Assets	4,429,499	1,107,820	430,140	79,310	309,076

The Notes to the Financial Statements are an integral part of this statement.

TOTAL ENTERPRISE FUNDS	GOVERNMENTAL ACTIVITIES - INTERNAL SERVICE FUNDS
$ 149,582	$ 2,339
1,029,326	-
256,286	159,663
130,137	-
132,606	-
99,076	-
75,851	-
4,159	26
11,732	-
103,545	8,460
68,373	1,000
122	-
99,041	2,285
30,392	3,780
5,592	4,631
2,195,820	182,184
18,417	-
105,649	-
38,647	-
31,136	-
38,373	-
6,239	-
494,057	-
316,294	-
16,512	-
288,747	-
2,805,954	68,485
4,160,025	68,485
6,355,845	250,669

(Continued)

STATE OF ARIZONA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2007
(Expressed in Thousands)

	BUSINESS-TYPE ACTIVITIES - ENTERPRISE FUNDS				
	UNIVERSITIES	UNEMPLOYMENT COMPENSATION	INDUSTRIAL COMMISSION SPECIAL FUND	LOTTERY	OTHER
LIABILITIES					
Current Liabilities:					
Accounts payable and other current liabilities	91,851	-	12,756	4,125	2,999
Payable for securities purchased	-	-	1,463	-	-
Accrued liabilities	43,877	21,956	-	-	8,590
Obligations under securities loan agreements	79,306	-	53,300	-	-
Due to U.S. Government	-	9	-	-	-
Due to local governments	-	-	-	9,304	-
Due to others	28,472	10,303	-	33,485	-
Due to other Funds	-	514	-	20,701	174,538
Unearned deferred revenue	92,594	-	-	-	13,285
Current portion of accrued insurance losses	-	-	30,856	-	-
Current portion of long-term debt	89,253	-	-	-	-
Current portion of other long-term liabilities	8,785	-	-	348	865
Total Current Liabilities	434,138	32,782	98,375	67,963	200,277
Noncurrent Liabilities:					
Unearned deferred revenue	29,870	-	-	-	-
Contracts payable	-	-	-	-	18,031
Accrued insurance losses	-	-	370,292	-	-
Funds held for others	53,268	-	-	-	-
Long-term debt	1,902,466	-	-	-	22
Other long-term liabilities	54,511	-	-	-	57
Total Noncurrent Liabilities	2,040,115	-	370,292	-	18,110
Total Liabilities	2,474,253	32,782	468,667	67,963	218,387
NET ASSETS					
Invested in capital assets, net of related debt	1,133,322	-	21,159	4,155	21,882
Restricted for:					
Capital projects	8,505	-	-	-	-
Unemployment Compensation	-	1,075,038	-	-	-
Debt service	11,119	-	-	-	-
Universities Fund:					
Expendable	210,635	-	-	-	-
Nonexpendable	199,471	-	-	-	-
Loans and other financial assistance:					
Expendable	-	-	-	-	71,211
Other	-	-	-	-	12
Unrestricted (deficit)	392,194	-	(59,686)	7,192	(2,416)
Total Net Assets	$ 1,955,246	$ 1,075,038	$ (38,527)	$ 11,347	$ 90,689

Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.

Net assets of business-type activities

The Notes to the Financial Statements are an integral part of this statement.

TOTAL ENTERPRISE FUNDS	GOVERNMENTAL ACTIVITIES - INTERNAL SERVICE FUNDS
111,731	75,743
1,463	-
74,423	1,575
132,606	-
9	-
9,304	-
72,260	-
195,753	924
105,879	-
30,856	52,272
89,253	2,672
9,998	7,666
833,535	140,852
29,870	-
18,031	-
370,292	291,833
53,268	-
1,902,488	5,879
54,568	4,026
2,428,517	301,738
3,262,052	442,590
1,180,518	59,934
8,505	-
1,075,038	-
11,119	-
210,635	-
199,471	-
71,211	-
12	-
337,284	(251,855)
$ 3,093,793	$ (191,921)
(20,416)	
$ 3,073,377	

STATE OF ARIZONA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

	BUSINESS-TYPE ACTIVITIES - ENTERPRISE FUNDS				
	UNIVERSITIES	UNEMPLOYMENT COMPENSATION	INDUSTRIAL COMMISSION SPECIAL FUND	LOTTERY	OTHER
OPERATING REVENUES					
Sales and charges for services:					
Pledged student tuition and fees, net of scholarship allowances of $191,960	$ 698,573	$ -	$ -	$ -	$ -
Pledged auxiliary enterprises, net of scholarship allowances of $9,328	300,759	-	-	-	-
Pledged educational department	70,007	-	-	-	-
Lottery	-	-	-	462,200	-
Other	-	-	-	-	147,526
Unemployment assessments	-	322,919	-	-	-
Workers' compensation assessments	-	-	24,405	-	-
Intergovernmental	603,490	6,265	-	-	795
Nongovernmental grants and contracts	94,994	-	-	-	-
Licenses, fees, and permits	-	-	-	-	665
Earnings on investments	-	-	-	-	2,909
Fines, forfeitures, and penalties	-	2,162	-	-	-
Settlement income	-	-	18,336	-	-
Other (revenues for Universities are pledged)	26,681	22	-	100	2,587
Total Operating Revenues	1,794,504	331,368	42,741	462,300	154,482
OPERATING EXPENSES					
Cost of sales and benefits	719,225	248,111	15,668	303,113	123,502
Interest on notes payable	-	-	-	-	4,040
Scholarships and fellowships	122,437	-	-	-	-
Personal services	1,847,506	-	-	6,118	29,504
Contractual services	-	-	-	11,052	9,727
Depreciation and amortization	189,951	-	1,232	260	1,888
Insurance	-	-	-	53	467
Other	-	-	-	2,478	7,274
Total Operating Expenses	2,879,119	248,111	16,900	323,074	176,402
Operating Income (Loss)	(1,084,615)	83,257	25,841	139,226	(21,920)
NON-OPERATING REVENUES (EXPENSES)					
Share of State sales tax revenues	79,223	-	-	-	-
Gifts and donations	102,580	-	-	-	-
Gain on sale of capital assets	18,589	-	-	-	1
Investment income (revenues for Universities are pledged)	55,055	43,902	41,928	-	6,379
Endowment earnings on investments	31,347	-	-	-	-
Other non-operating revenue	26,359	-	2,123	772	607
Distributions to local governments	-	-	-	(40,434)	-
Interest expense	(82,215)	-	-	-	-
Other non-operating expense	(13,540)	-	(6,769)	-	(84)
Total Non-Operating Revenues (Expenses)	217,398	43,902	37,282	(39,662)	6,903
Income (Loss) Before Contributions and Transfers	(867,217)	127,159	63,123	99,564	(15,017)
Capital grants and contributions	27,981	-	-	-	-
Contributions to permanent endowments	4,815	-	-	-	-
Transfers in	969,880	-	8,000	-	98
Transfers out	-	(2,040)	-	(99,482)	-
Change in Net Assets	135,459	125,119	71,123	82	(14,919)
Total Net Assets - Beginning, as restated	1,819,787	949,919	(109,650)	11,265	105,608
Total Net Assets - Ending	$ 1,955,246	$ 1,075,038	$ (38,527)	$ 11,347	$ 90,689

Change in net assets of enterprise funds
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.

Change in net assets of business-type activities

The Notes to the Financial Statements are an integral part of this statement.

TOTAL ENTERPRISE FUNDS	GOVERNMENTAL ACTIVITIES - INTERNAL SERVICE FUNDS
$ 698,573	$ -
300,759	-
70,007	-
462,200	-
147,526	825,352
322,919	-
24,405	-
610,550	-
94,994	-
665	-
2,909	-
2,162	-
18,336	-
29,390	55
2,785,395	825,407
1,409,619	659,431
4,040	-
122,437	-
1,883,128	31,680
20,779	33,777
193,331	11,841
520	28,751
9,752	7,926
3,643,606	773,406
(858,211)	52,001
79,223	-
102,580	-
18,590	226
147,264	333
31,347	-
29,861	700
(40,434)	-
(82,215)	(356)
(20,393)	-
265,823	903
(592,388)	52,904
27,981	3,087
4,815	-
977,978	-
(101,522)	(2,228)
316,864	53,763
2,776,929	(245,684)
$ 3,093,793	$ (191,921)
$ 316,864	
14,084	
$ 330,948	

STATE OF ARIZONA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

	BUSINESS-TYPE ACTIVITIES - ENTERPRISE FUNDS				
	UNIVERSITIES	UNEMPLOYMENT COMPENSATION	INDUSTRIAL COMMISSION SPECIAL FUND	LOTTERY	OTHER
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers	$ -	$ -	$ 18,335	$ 248,496	$ 152,237
Receipts from assessments	-	323,893	23,545	-	-
Receipts from student loans collected	36,972	-	-	-	-
Receipts from sales and services of auxiliary enterprises	300,375	-	-	-	-
Receipts from sales and services of educational departments	64,414	-	-	-	-
Receipts from interfund services / premiums	-	-	-	-	-
Receipts from student tuition and fees	687,047	-	-	-	-
Receipts from federal and local governments	704,418	6,265	-	-	722
Receipts from other Funds	-	-	-	-	39,208
Payments to suppliers, prize winners, claimants, insurance companies, or beneficiaries	(720,114)	(246,765)	(24,560)	(144,778)	(124,208)
Payments to employees	(1,831,154)	-	-	(6,131)	(29,199)
Payments to retirees	-	-	-	-	-
Payments for scholarships and fellowships	(128,216)	-	-	-	-
Payments for student loans issued	(38,143)	-	-	-	-
Payments to other Funds	-	-	-	-	(5,797)
Other receipts	28,134	2,184	-	40,594	299
Net Cash Provided (Used) by Operating Activities	(896,267)	85,577	17,320	138,181	33,262
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES					
Custodial funds received	335,218	-	-	-	-
Office rental receipts	-	-	2,124	-	-
Share of State sales tax receipts	71,170	-	-	-	-
Grants and contributions received	471,878	-	-	-	206
Transfers from other Funds	949,879	-	8,000	-	95
Custodial funds disbursed	(322,701)	-	-	-	-
Grants and contributions disbursed	(359,332)	-	-	-	-
Distributions to local governments	-	-	-	(40,434)	-
Transfers to other Funds	-	(2,283)	-	(94,456)	(65)
Other receipts (payments)	7,899	-	(2,725)	-	401
Net Cash Provided (Used) by Non-capital Financing Activities	1,154,011	(2,283)	7,399	(134,890)	637
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Proceeds from sale of capital assets	35,063	-	-	-	-
Proceeds from capital debt, installment purchase contracts and capital leases	136,341	-	-	-	-
Capital grants and contributions received	15,761	-	-	-	-
Transfers from other funds	20,000	-	-	-	-
Acquisition and construction of capital assets	(381,229)	-	(842)	(738)	(2,763)
Interest paid on capital debt, installment purchase contracts and capital leases	(81,825)	-	-	-	-
Principal paid on capital debt, installment purchase contracts and capital leases	(67,642)	-	-	-	(18)
Other receipts (payments)	(8,708)	-	(25)	-	-
Net Cash (Used) by Capital and Related Financing Activities	(332,239)	-	(867)	(738)	(2,781)

The Notes to the Financial Statements are an integral part of this statement.

TOTAL ENTERPRISE FUNDS	GOVERNMENTAL ACTIVITIES - INTERNAL SERVICE FUNDS
$ 419,068	$ -
347,438	-
36,972	-
300,375	-
64,414	-
-	824,974
687,047	-
711,405	-
39,208	-
(1,260,425)	(723,798)
(1,866,484)	(31,680)
-	(10,527)
(128,216)	-
(38,143)	-
(5,797)	-
71,211	39
(621,927)	59,008
335,218	-
2,124	-
71,170	-
472,084	-
957,974	-
(322,701)	-
(359,332)	-
(40,434)	-
(96,804)	(2,228)
5,575	1
1,024,874	(2,227)
35,063	349
136,341	-
15,761	-
20,000	-
(385,572)	(7,651)
(81,825)	(356)
(67,660)	(2,579)
(8,733)	699
(336,625)	(9,538)

(Continued)

STATE OF ARIZONA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

	BUSINESS-TYPE ACTIVITIES - ENTERPRISE FUNDS				
	UNIVERSITIES	UNEMPLOYMENT COMPENSATION	INDUSTRIAL COMMISSION SPECIAL FUND	LOTTERY	OTHER
CASH FLOWS FROM INVESTING ACTIVITIES					
Proceeds from sales and maturities of investments	386,949	-	131,804	-	-
Interest and dividends from investments	44,847	43,902	14,801	674	6,055
Change in cash collateral received from securities lending transactions	-	-	3,550	-	-
Purchase of investments	(394,110)	-	(173,364)	-	(55)
Other (payments)	-	-	(3,811)	-	(83)
Net Cash Provided (Used) by Investing Activities	37,686	43,902	(27,020)	674	5,917
Net Increase (Decrease) in Cash and Cash Equivalents	(36,809)	127,196	(3,168)	3,227	37,035
Cash and Cash Equivalents - Beginning	431,533	902,130	105,845	56,589	119,119
Cash and Cash Equivalents - Ending	$ 394,724	$ 1,029,326	$ 102,677	$ 59,816	$ 156,154
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:					
Operating income (loss)	$ (1,084,615)	$ 83,257	$ 25,841	$ 139,226	$ (21,920)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:					
Depreciation and amortization	189,951	-	1,232	260	1,888
Loss on sale of capital assets	-	-	-	7	-
Net changes in assets and liabilities:					
(Increase) in receivables, net of allowances	(9,101)	(3,325)	(760)	(679)	(1,068)
(Increase) in due from U.S. Government	-	-	-	-	(73)
(Increase) in due from local governments	-	-	-	-	(2)
Decrease in due from other Funds	-	-	-	-	34,083
(Increase) in inventories, at cost	(1,373)	-	-	(1,049)	(242)
Decrease in other assets	987	-	-	188	204
Increase (decrease) in accounts payable	(9,213)	-	102	1,599	(1,353)
Increase (decrease) in accrued liabilities	4,828	5,646	-	(1,371)	16,234
(Decrease) in due to U.S. Government	-	(1)	-	-	-
Increase (decrease) in due to others	830	-	-	-	(135)
Increase (decrease) in due to other Funds	-	-	-	-	4,043
Increase in deferred revenue	11,439	-	-	-	1,594
(Decrease) in accrued insurance losses	-	-	(9,095)	-	-
Increase (decrease) in other liabilities	-	-	-	-	9
Net Cash Provided (Used) by Operating Activities	$ (896,267)	$ 85,577	$ 17,320	$ 138,181	$ 33,262
SCHEDULE OF NONCASH INVESTING, CAPITAL AND NON-CAPITAL FINANCING ACTIVITIES					
Gifts and conveyances of capital assets	$ 13,337	$ -	$ -	$ -	$ -
Assets acquired under capital leases	34,674	-	-	-	-
Contribution of capital assets from other funds	-	-	-	-	-
Change in fair value of investments	11,643	-	27,226	(8)	(221)
Amortization of bond discount and issuance costs	(2,082)	-	-	-	-
Amortization of deferred amount on refunding and bond premium	1,366	-	-	-	-
Gain on disposal of capital assets, net	7,903	-	-	-	-
Amortization of deferred rent	4,900	-	-	-	-
Refinancing of long-term debt	208,240	-	-	-	-
Total Noncash Investing, Capital and Non-capital Financing Activities	$ 279,981	$ -	$ 27,226	$ (8)	$ (221)

The Notes to the Financial Statements are an integral part of this statement.

TOTAL ENTERPRISE FUNDS	GOVERNMENTAL ACTIVITIES - INTERNAL SERVICE FUNDS
518,753	-
110,279	333
3,550	-
(567,529)	-
(3,894)	-
61,159	333
127,481	47,576
1,615,216	114,426
$ 1,742,697	$ 162,002
$ (858,211)	$ 52,001
193,331	11,841
7	-
(14,933)	(1,576)
(73)	(1,000)
(2)	-
34,083	1,182
(2,664)	(808)
1,379	2,545
(8,865)	19,594
25,337	172
(1)	-
695	-
4,043	(1,194)
13,033	-
(9,095)	(23,095)
9	(654)
$ (621,927)	$ 59,008
$ 13,337	$ -
34,674	-
-	3,087
38,640	-
(2,082)	-
1,366	-
7,903	-
4,900	-
208,240	-
$ 306,978	$ 3,087

STATE OF ARIZONA
STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2007
(Expressed in Thousands)

	PENSION AND OTHER EMPLOYEE BENEFIT TRUST FUNDS	INVESTMENT TRUSTS	AGENCY FUNDS
ASSETS			
Cash	$ 29,465	$ -	$ 34,879
Cash and pooled investments with State Treasurer	-	-	270,062
Prepaid benefits	129,917	-	-
Short-term investments	-	-	5,096
Receivables, net of allowances:			
Accrued interest and dividends	83,657	12,463	388
Securities sold	714,828	-	-
Forward contract receivable	1,343,784	-	-
Contributions	47,710	-	-
Court fees	364	-	-
Due from other Funds	1,917	-	-
Miscellaneous receivables	8,771	-	-
Total receivables	2,201,031	12,463	388
Due from others	-	-	76,257
Investments, at fair value:			
Temporary investments	2,598,595	-	-
Temporary investments from securities lending	3,543,247	-	-
U.S. Government securities	4,760,485	1,049,028	-
Corporate bonds	2,869,522	1,192,271	-
Corporate notes	259,460	-	-
Corporate stocks	24,604,918	-	-
Real estate mortgages and contracts	597,327	-	-
Collateral investment pool	1,697,578	-	-
Repurchase agreements	-	1,719,928	-
Money market mutual funds	-	5,125	-
Other investments	241,130	44	-
Total investments	41,172,262	3,966,396	-
Custodial securities in safekeeping	-	-	2,789,482
Other assets	-	-	4,917
Property and equipment, net of accumulated depreciation	5,127	-	-
Total Assets	43,537,802	3,978,859	3,181,081
LIABILITIES			
Accounts payable and other current liabilities	1,375,800	-	189,584
Payable for securities purchased	1,528,690	-	-
Accrued liabilities	-	-	13,614
Obligation under securities loan agreements	5,240,825	-	-
Due to local governments	-	6,722	11,202
Due to others	-	-	2,966,681
Due to other Funds	1,917	-	-
Total Liabilities	8,147,232	6,722	3,181,081
NET ASSETS			
Held in trust for:			
Pension benefits	35,390,570	-	-
Pool participants	-	3,972,137	-
Total Net Assets	$ 35,390,570	$ 3,972,137	$ -

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2007
(Expressed in Thousands)

	PENSION AND OTHER EMPLOYEE BENEFIT TRUST FUNDS	INVESTMENT TRUSTS
ADDITIONS:		
Member contributions	$ 941,555	
Employer contributions	1,006,903	
Member purchase of service credit	109,910	
Court fees	3,978	
Investment income:		
Net increase in fair value of investments	4,574,527	$ 3,935
Interest income	415,804	183,650
Dividends	366,704	-
Real estate	12,508	-
Other investment income	7,954	-
Securities lending income	229,237	-
Total investment income	5,606,734	187,585
Less investment expenses:		
Investment activity expenses	61,685	2,846
Security lending expenses	219,559	-
Net investment income	5,325,490	184,739
Capital share and individual account transactions:		
Shares sold	-	5,526,293
Reinvested interest income	-	171,745
Shares redeemed	-	(4,957,937)
Net capital share and individual account transactions	-	740,101
Other additions	12,972	-
Total Additions	7,400,808	924,840
DEDUCTIONS:		
Retirement and disability benefits	2,311,045	-
Death benefits	21,590	-
Refunds to withdrawing members, including interest	103,381	-
Administrative expense	38,705	-
Dividends to investors	-	184,740
Other deductions	16,245	-
Total Deductions	2,490,966	184,740
Change in net assets held in trust for:		
Pension benefits	4,909,842	-
Pool participants	-	740,100
Net Assets - Beginning	30,480,728	3,232,037
Net Assets - Ending	$ 35,390,570	$ 3,972,137

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
COMBINING STATEMENT OF NET ASSETS
COMPONENT UNITS
JUNE 30, 2007
(Expressed in Thousands)

	WATER INFRASTRUCTURE FINANCE AUTHORITY	UNIVERSITY MEDICAL CENTER	ARIZONA POWER AUTHORITY	TOTAL
ASSETS				
Current Assets:				
Cash	$ -	$ 19,554	$ -	$ 19,554
Cash and pooled investments with State Treasurer	85,370	-	5,256	90,626
Cash held by trustee	62,129	-	-	62,129
Short-term investments	-	92,818	-	92,818
Restricted investments held by trustee	-	16,555	3,105	19,660
Receivables, net of allowances:				
Interest	8,703	-	113	8,816
Other	3,724	76,227	3,227	83,178
Inventories, at cost	-	11,218	-	11,218
Other current assets	-	-	2,626	2,626
Total Current Assets	159,926	216,372	14,327	390,625
Noncurrent Assets:				
Restricted assets:				
Investments held by trustee	-	138,575	6,547	145,122
Loans and notes receivable, net of allowances	682,375	-	-	682,375
Investments	80,896	-	-	80,896
Other noncurrent assets	3,301	5,756	39,954	49,011
Capital assets:				
Land and other nondepreciable	-	30,180	-	30,180
Depreciable buildings, property and equipment	101	319,272	1,327	320,700
Less: accumulated depreciation	(101)	(204,467)	(1,127)	(205,695)
Total Noncurrent Assets	766,572	289,316	46,701	1,102,589
Total Assets	926,498	505,688	61,028	1,493,214
LIABILITIES				
Current Liabilities:				
Accounts payable and other current liabilities	-	42,898	3,619	46,517
Accrued liabilities	6,919	17,685	672	25,276
Current portion of accrued insurance losses	-	2,572	-	2,572
Current portion of long-term debt	25,900	3,835	3,120	32,855
Current portion of other long-term liabilities	46	5,721	81	5,848
Total Current Liabilities	32,865	72,711	7,492	113,068
Noncurrent Liabilities:				
Unearned deferred revenue	2,629	-	-	2,629
Accrued insurance losses	-	10,590	-	10,590
Long-term debt	559,314	227,921	49,688	836,923
Other long-term liabilities	-	7,203	-	7,203
Total Noncurrent Liabilities	561,943	245,714	49,688	857,345
Total Liabilities	594,808	318,425	57,180	970,413
NET ASSETS				
Invested in capital assets, net of related debt	-	35,514	200	35,714
Restricted for:				
Debt service	-	9,948	-	9,948
Loans and other financial assistance	273,096	-	-	273,096
Unrestricted	58,594	141,801	3,648	204,043
Total Net Assets	$ 331,690	$ 187,263	$ 3,848	$ 522,801

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA

COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

COMPONENT UNITS

FOR THE YEAR ENDED JUNE 30, 2007

(Expressed in Thousands)

	WATER INFRASTRUCTURE FINANCE AUTHORITY	UNIVERSITY MEDICAL CENTER	ARIZONA POWER AUTHORITY	TOTAL
OPERATING REVENUES				
Sales and charges for services	$ -	$ 442,569	$ 28,301	$ 470,870
Intergovernmental	12,710	-	-	12,710
Licenses, fees, and permits	7,686	-	-	7,686
Earnings on investments	12,859	-	-	12,859
Total Operating Revenues	33,255	442,569	28,301	504,125
OPERATING EXPENSES				
Cost of sales and benefits	-	99,222	26,663	125,885
Personal services	1,024	209,136	-	210,160
Contractual services	931	66,395	-	67,326
Aid to local governments	37	-	-	37
Depreciation and amortization	8	20,170	39	20,217
Insurance	-	3,458	-	3,458
Other	28,033	24,644	1,569	54,246
Total Operating Expenses	30,033	423,025	28,271	481,329
Operating Income	3,222	19,544	30	22,796
NON-OPERATING REVENUES (EXPENSES)				
Investment income	15,671	14,571	795	31,037
Other non-operating revenue	-	8,288	42	8,330
Interest expense	-	(3,505)	(336)	(3,841)
Other non-operating expense	-	(1,797)	-	(1,797)
Total Non-Operating Revenues (Expenses)	15,671	17,557	501	33,729
Change in Net Assets	18,893	37,101	531	56,525
Total Net Assets - Beginning	312,797	150,162	3,317	466,276
Total Net Assets - Ending	$ 331,690	$ 187,263	$ 3,848	$ 522,801

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA

COMBINING STATEMENT OF FINANCIAL POSITION

UNIVERSITIES - AFFILIATED COMPONENT UNITS

JUNE 30, 2007

(Expressed in Thousands)

	ARIZONA STATE UNIVERSITY FOUNDATION	UNIVERSITY OF ARIZONA FOUNDATION	ARIZONA CAPITAL FACILITIES FINANCIAL CORPORATION	OTHER COMPONENT UNITS	TOTAL
ASSETS					
Cash and cash equivalent investments	$ 15,786	$ 63,365	$ 279	$ 15,702	$ 95,132
Receivables:					
Pledges receivable	109,570	24,683	-	46,413	180,666
Other receivables	1,267	-	6,009	11,113	18,389
Total receivables	110,837	24,683	6,009	57,526	199,055
Investments:					
Investments in securities	485,781	361,396	35,532	99,629	982,338
Investments held in trust for Universities	-	-	-	8,924	8,924
Other investments	58,295	11,073	811	250	70,429
Total investments	544,076	372,469	36,343	108,803	1,061,691
Net direct financing leases	28,815	-	46,989	35,277	111,081
Property and equipment, net of accumulated depreciation	20,198	3,980	211,498	43,468	279,144
Other assets	21,542	4,580	6,651	12,080	44,853
Total Assets	741,254	469,077	307,769	272,856	1,790,956
LIABILITIES					
Liability under Universities' endowment trust agreements	72,822	21,347	-	6,015	100,184
Bonds payable	84,095	-	300,700	90,245	475,040
Unearned revenue	4,597	-	5,705	19,591	29,893
Other liabilities	27,814	2,839	15,984	10,779	57,416
Total Liabilities	189,328	24,186	322,389	126,630	662,533
NET ASSETS					
Permanently restricted	305,516	308,815	-	39,389	653,720
Temporarily restricted	213,673	120,364	-	64,136	398,173
Unrestricted (deficit)	32,737	15,712	(14,620)	42,701	76,530
Total Net Assets	$ 551,926	$ 444,891	$ (14,620)	$ 146,226	$ 1,128,423

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA

COMBINING STATEMENT OF ACTIVITIES

UNIVERSITIES - AFFILIATED COMPONENT UNITS

JUNE 30, 2007

(Expressed in Thousands)

	ARIZONA STATE UNIVERSITY FOUNDATION	UNIVERSITY OF ARIZONA FOUNDATION	ARIZONA CAPITAL FACILITIES FINANCIAL CORPORATION	OTHER COMPONENT UNITS	TOTAL
REVENUES					
Contributions	$ 105,853	$ 60,094	$ -	$ 36,726	$ 202,673
Rental revenue	495	-	10,364	19,647	30,506
Sales and services	14,072	-	285	9,067	23,424
Net investment income	55,074	44,163	1,567	14,091	114,895
Capital lease revenue	-	-	-	22,295	22,295
Other revenues	6,202	10,711	9,507	5,405	31,825
Total Revenues	181,696	114,968	21,723	107,231	425,618
EXPENSES					
Program services:					
Payments to Universities	32,760	32,994	-	16,783	82,537
Leasing related expenses	-	-	-	6,680	6,680
Payments on behalf of Universities	-	13,100	-	7,016	20,116
Other program services	13,226	-	-	4,741	17,967
Personal services, operations, and administrative expenses	18,356	4,070	7,431	17,406	47,263
Fundraising expenses	-	4,938	-	2,966	7,904
Interest	2,245	-	8,378	3,170	13,793
Assets expensed under capital lease agreement	-	-	-	19,928	19,928
Other expenses	6,968	-	11,906	1,800	20,674
Total Expenses	73,555	55,102	27,715	80,490	236,862
Increase (Decrease) in Net Assets	108,141	59,866	(5,992)	26,741	188,756
Net Assets - Beginning, as restated	443,785	396,254	(8,628)	119,485	950,896
Cumulative effect of accounting changes	-	(11,229)	-	-	(11,229)
Net Assets - Ending	$ 551,926	$ 444,891	$ (14,620)	$ 146,226	$ 1,128,423

The Notes to the Financial Statements are an integral part of this statement.

STATE OF ARIZONA
NOTES TO THE FINANCIAL STATEMENTS
INDEX

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the State of Arizona (the State) conform to U.S. Generally Accepted Accounting Principles (GAAP) applicable to governmental units adopted by the Governmental Accounting Standards Board (GASB).

A. REPORTING ENTITY

The State is a general purpose government. The accompanying financial statements present the activities of the State (the primary government) and its component units. Component Units' footnote disclosures are presented in Note 16 – *Discretely Presented Component Unit Disclosures.*

Component Units

Component units are legally separate entities for which the State is considered to be financially accountable, or organizations that raise and hold economic resources for the direct benefit of the State. Blended component units, although legally separate entities, are in substance, part of a government's operations. Therefore, data from these units is combined with data of the primary government. Discretely presented component units of the State, except for component units affiliated with the State's Universities, are reported in a separate column in the government-wide financial statements to emphasize they are legally separate from the State. Because the component units affiliated with the Universities follow Financial Accounting Standards Board (FASB) statements, these financial statements have been reported on separate pages following the respective counterpart financial statements of the State. For financial reporting purposes, only the statement of financial position and the statement of activities for component units affiliated with the Universities are included in the State's financial statements as required by the GASB.

GASB Statement No. 14, *The Financial Reporting Entity* 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.

In addition, GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units* (GASB 39) requires that legally separate, tax-exempt entities that meet *all* of the following criteria should be discretely presented as component units: (1) The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents, (2) The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and (3) The economic resources received or held by an *individual organization* that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to that primary government.

The State reports the following blended component units:

The Arizona State Retirement System (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 administered in accordance with provisions of Arizona Revised Statutes (ARS) Title 38, Chapter 5, Article 2. The ASRS is governed by a nine-member board that is appointed by the Governor and approved by the Senate to serve three-year terms.

The Public Safety Personnel Retirement System (PSPRS) is an agent, multi-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 210 local boards according to the provisions of ARS Title 38, Chapter 5, Article 4. The Fund Manager is a five-member board appointed by the Governor and approved by the Senate to 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.

The Elected Officials' Retirement Plan (EORP) is a cost-sharing, multi-employer public employee retirement plan that benefits all State and county elected officials and judges and certain elected city officials. The Fund Manager of the PSPRS administers the EORP plan according to the provisions of ARS Title 38, Chapter 5, Article 3.

The Corrections Officer Retirement Plan (CORP) is an agent, multi-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 20 local boards according to the provisions of ARS Title 38, Chapter 5, Article 6. Each employer member participating in the CORP has a five-member local board. All members serve a fixed four-year term.

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
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
3010 East Camelback Road, Suite 200
Phoenix, Arizona 85016
(602) 255-5575

The State reports the following discretely presented component units:

University Medical Center (UMC) – The UMC is the primary teaching hospital for the College of Medicine, the College of Nursing, the College of Pharmacy, the College of Public Health, and the School of Health Related Professions of the University of Arizona (U of A). The UMC was created in 1984 when the State Legislature passed a bill that allowed the Arizona Board of Regents (ABOR) to convey the UMC to a private, not-for-profit, tax-exempt corporation. Although an autonomous entity was created, the teaching missions and research alliances with the U of A and the State remained. The ABOR confirms all members of the UMC's Board of Directors, and must approve all amendments to the UMC's articles of incorporation and bylaws. Complete financial statements may be obtained from the UMC's administrative offices at 655 East River Road, Tucson, Arizona 85704, (520) 694-2700.

Arizona Power Authority (APA) – The APA purchases the State's allocation of power produced at the federally owned Boulder Canyon Project hydropower plant and resells it to Arizona entities that are eligible purchasers under federal and state laws. The APA is governed by a commission of five members 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 their membership for a term of two years. All revenue bonds issued by the APA must be approved by the State Certification Board. Complete financial statements may be obtained from the APA's administrative offices at 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. The Clean Water Revolving Fund was created pursuant to the Federal Water Pollution Control Act, which required the State to establish the Clean Water Revolving Fund to accept federal capitalization grants for publicly owned wastewater treatment projects. The WIFA has also entered into an agreement 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. The ten Governor appointed directors serve staggered terms of five years and serve at the pleasure of the Governor. Complete financial statements may be obtained from the WIFA's administrative offices at 1100 West Washington Street, Suite 290, Phoenix, Arizona 85007, (602) 364-1310.

Component units of the State affiliated with the Universities are legally separate, tax-exempt organizations controlled by separate boards of directors that meet the criteria established in GASB 39, with the exception of the Collegiate Golf Foundation and Campus Research Corporation (CRC). The Collegiate Golf Foundation is included because it is a legally separate organization that the State believes would be misleading to exclude due to its financial relationship to the State. The CRC is included because the U of A appoints a majority of the board of directors and approves the budget; the U of A can thus impose its will on the CRC.

The following discretely presented component units affiliated with the Universities are reported as *major* component units of the State:

Arizona State University Foundation (ASU Foundation) – The ASU Foundation's resources are disbursed at the discretion of the Foundation's independent board of directors, in accordance with donor directions and Foundation policy.

Arizona Capital Facilities Finance Corporation (ACFFC) – The ACFFC provides facilities for either the use by students of ASU or ASU itself.

University of Arizona Foundation (U of A Foundation) – The U of A Foundation supports the U of A through various fund-raising activities and contributes funds to the U of A in support of various programs.

The following discretely presented component units affiliated with the Universities are reported as *non-major* component units of the State:

Arizona State University Alumni Association, Sun Angel Foundation, and Sun Angel Endowment – These three foundations receive funds primarily through donations and dues, and contribute funds to ASU for support of various programs.

Arizona State University Research Park, Inc. (ASU Research Park) – ASU Research Park manages a research park to promote and support research activities in coordination with ASU.

Mesa Student Housing, LLC – Mesa Student Housing, LLC provides facilities for either the use by students of ASU or ASU itself.

Collegiate Golf Foundation – This foundation operates an ASU-owned golf course.

University of Arizona Alumni Association (U of A Alumni Association) – The U of A Alumni Association was established to serve the U of A and its graduates, former students, and friends by attracting, organizing, and encouraging them to advance the U of A's missions - teaching, research, and public service.

University of Arizona Law College Association (Law Association) – The Law Association was established to provide support and financial assistance to the College of Law at the U of A. The Law Association funds provide support to the College on many levels, from endowed student scholarships to named faculty professorships.

University of Arizona Campus Research Corporation (CRC) – The CRC was established to assist the U of A in the acquisition, improvement, and operation of the U of A Science and Technology Park (Park) and related properties. The CRC currently leases from the U of A the remaining 32.00% of building space of the Park not leased to the Arizona Research Park Authority. The CRC is responsible for assisting in the development of the presently undeveloped portions of the Park and for subleasing unoccupied space, newly developed space, and space now occupied by IBM or its subtenants once the current subleases expire. The U of A is responsible for payment of operational expenses associated with the space occupied by the U of A departments, offices, and programs.

Northern Arizona University Foundation, Inc. (NAU Foundation) – The NAU Foundation receives gifts and bequests, administers and invests securities and property, and disburses payments to and on behalf of the NAU for advancement of its mission.

Northern Arizona Capital Facilities Finance Corporation (NACFFC) – The NACFFC was established for the purpose of acquiring, developing, constructing, maintaining, and operating student housing and other capital facilities and equipment for the use and benefit of the NAU's students.

Complete financial statements for each of the aforementioned component units, except for the U of A Foundation, may be obtained at the following addresses:

ASU Foundation, ASU Alumni Association, Sun Angel Foundation, Sun Angel Endowment, ASU Research Park, Collegiate Golf Foundation, ACFFC, and Mesa Student Housing, LLC – Arizona State University, Financial Services, P.O. Box 875812, Tempe, Arizona 85287-5812 or (480) 965-3601

The U of A Alumni Association – Alumni Association, University of Arizona, P.O. Box 210109, Tucson, Arizona 85721-0109

The Law Association – Law College Association, University of Arizona, P.O. Box 210176, Tucson, Arizona 85721-0176

CRC - University of Arizona Science and Technology Park, 9040 South Rita Road, Suite 302, Tucson, Arizona 85747

NAU Foundation and NACFFC – Northern Arizona University, Comptroller's Office, P.O. Box 4069, Flagstaff, Arizona 86011

The financial statements of the U of A Foundation are not publicly available. For information regarding the U of A Foundation's financial statements, contact the U of A Comptroller at the following address: University of Arizona, Financial Services, P.O. Box 3310, Tucson, Arizona 85722-3310.

Related Organizations

Related organizations are legally separate entities for which the State is not considered to be financially accountable, and that do not meet the criteria established by GASB 39. The State's accountability for these organizations does not extend beyond making the appointments, nor are the economic resources accessible to the State. As a result, financial activity for the organizations described below is not included in the State's financial statements.

Arizona Health Facilities Authority (the Authority) – ARS §36-482 established the Authority to issue tax-exempt bonds and loans 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 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, and can be removed for cause or at will by the Governor with the consent of the Senate. The State cannot abrogate the rights of the Authority until all bonds, together with the interest thereon, are fully paid and discharged and all agreements are fully performed.

Arizona International Development Authority (the Authority) – ARS §41-1553.01 established the Authority to facilitate the development of international trade or commerce between Arizona and other countries. The Authority is governed by a seven-member board of directors appointed by the Governor and approved by the Senate for five-year terms, and can be removed only for cause.

Arizona Sports and Tourism Authority (the Authority) – ARS §5-802 established the Authority to construct, finance, maintain, improve, operate, market, and promote the use of a multipurpose facility and do all things necessary to accomplish those purposes. The Authority may issue revenue bonds in such principal amounts to accomplish the above stated purposes. The Authority is governed by a nine-member board of directors of which five are appointed by the Governor and approved by the Senate and two members each by the President of the Senate and the Speaker of the House. The directors serve terms of five years, and may be re-appointed for one full subsequent term, and can be removed only for cause.

Arizona Housing Finance Authority (the Authority) – ARS §41-3902 established the Authority to issue bonds for residential dwelling units and multifamily residential rental projects in rural areas. The Authority may also establish mortgage credit certificate programs to finance residential dwelling units in rural areas. The Authority is required to notify and obtain written consent from the governing bodies of any city, town, county, tribal government, or existing corporation for any multifamily residential rental projects planned for their jurisdiction. 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 terms of seven years, and can be removed only for cause.

State Compensation Fund (the Fund) – ARS §23-981 established the Fund to provide insurance to employers for workers' compensation, occupational disease compensation, and medical, surgical, and hospital benefits. The Fund is governed by a board of directors that consists of five members appointed by the Governor for staggered terms of five years. Annually, the Governor appoints a chairman from among the board members.

Joint Ventures

As described in Note 10, the U of A participates in a joint venture. In accordance with U.S. GAAP, the financial activities of this joint venture are not included in the State's financial statements.

B. BASIS OF PRESENTATION

The basic financial statements include both government-wide statements and fund financial statements. The government-wide statements focus on the State as a whole, while the fund financial statements focus on major funds. Each presentation provides valuable information that can be analyzed and compared between years and between governments to enhance the usefulness of the information.

Government-wide statements provide information about the primary government and its component units. The statements include a statement of net assets and a statement of activities. These statements report the financial activities of the overall government, except for fiduciary activities. They also distinguish between the governmental and business-type activities of the State and between the State and its discretely presented component units. Governmental activities generally are financed through taxes and intergovernmental revenues. Business-type activities are financed in whole or in part by fees charged to external parties.

The **Statement of Net Assets** presents the State's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

> **Invested in capital assets, net of related debt** consist of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
>
> **Restricted net assets** result when constraints placed on net asset use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or voter initiative.
>
> **Unrestricted net assets** consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often have constraints on resources, which are imposed by management, but can be removed or modified.

The **Statement of Activities** presents a comparison between direct expenses and program revenues for each function of the State's governmental activities, and its different business-type activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular program or function.

The State does not allocate indirect expenses to programs or functions. Program revenues include:

- charges to customers or applicants for goods, services, privileges provided, and fines or forfeitures
- operating grants and contributions
- capital grants and contributions, including special assessments

Revenues that are not classified as program revenues, including internally dedicated resources and all taxes, are reported as general revenues.

Interfund balances have been eliminated from the government-wide financial statements to the extent that they occur within either the governmental or business-type activities. Balances between governmental and business-type activities are presented as internal balances and are eliminated in the total column. Revenues and expenses associated with reciprocal transactions within governmental or within business-type activities have not been eliminated.

Fund financial statements provide information about the State's funds, including fiduciary funds. Separate statements are presented for the governmental, proprietary, and fiduciary fund categories. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as non-major funds. Fiduciary funds are aggregated and reported by fund type.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The State reports the following major governmental funds:

The General Fund – is the State's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The Transportation and Aviation Planning, Highway Maintenance and Safety Fund – accounts for all financial transactions applicable to the general operations of the Arizona Department of Transportation (ADOT). The ADOT builds and maintains the State's highway system and the Grand Canyon Airport.

The Land Endowments Fund – holds lands granted to the State by the Federal government for the benefit of public schools and other public institutions. Principal is maintained intact and investment earnings and lease revenues are distributed to beneficiaries in accordance with State statute.

The State reports the following major enterprise funds:

The Universities – account for transactions of the State's three universities, which comprise the State's university system.

Unemployment Compensation – pays claims for unemployment to eligible recipients from employer contributions and reimbursements.

The Industrial Commission Special Fund – accounts for deposits not to exceed 2.50% of all premiums received by the State Compensation Fund and private insurance carriers during the preceding calendar year. These monies are used to provide additional awards as necessary to enable injured employees to accept the benefits of any law for promotion of vocational rehabilitation of persons disabled in industry. In addition, benefits may be paid for workers' compensation claims filed by employees of non-insured employers. The Industrial Commission (Commission) then pursues against the non-insured employer for reimbursement of all benefits paid, including assessed penalties.

The Lottery – accounts for the activities of the Arizona State Lottery.

Additionally, the State reports the following fund types:

Internal Service Funds – account for insurance coverage, employee benefits, automotive maintenance and operation, highway equipment rentals, and data processing and telecommunication services provided to State agencies on a cost-reimbursement basis. It is the policy of the State to classify immaterial proprietary fund activities in governmental funds. This policy helps to reduce the number of funds reported in the financial statements to the minimum amount needed. These funds allocate a fixed rate payroll processing charge among all agencies, allocate postage and mailing costs among all agencies, and arrange for the sale of the State's office equipment and motorized vehicles at public auctions.

Pension and Other Employee Benefit Trust Funds – account for the activities of the ASRS, the PSPRS, the EORP, and the CORP, for which the State acts as a trustee. These retirement and other post-employment benefit plans accumulate resources to pay pension, health insurance premium subsidies, and long-term disability benefits of State employees and employees of other governmental entities participating in the plans.

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, property collected by the State, and payment of the health insurance subsidy by the PSPRS, the EORP, and the CORP, where the State acts as an agent for distribution to other governments and organizations.

C. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

The government-wide, proprietary fund, and fiduciary fund financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. The agency funds are custodial in nature and do not have a measurement focus. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Grants and donations are recognized as revenues as soon as all eligibility requirements the provider imposed have been met.

Governmental funds in the fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The State considers all revenues reported in the governmental funds to be available if the revenues are collected within 31 days after year-end. Those revenues susceptible to accrual are federal reimbursements, highway user revenue tax, and state sales tax. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they are due and payable. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of long-term debt and acquisitions under capital leases are reported as other financing sources.

Under the terms of grant agreements, the State funds certain programs through a combination of grants and general revenues. Therefore, when program expenses are incurred, there are both restricted and unrestricted resources available to finance the program. The State's policy regarding whether to first apply restricted or unrestricted resources is made on a case-by-case basis.

The State's business-type activities and enterprise funds follow Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989; Accounting Principles Board Opinions; and Accounting Research Bulletins, unless those pronouncements conflict with GASB pronouncements. The State has chosen the option not to follow FASB Statements and Interpretations issued after November 30, 1989.

D. DEPOSITS AND INVESTMENTS

1. Cash and Cash Equivalents

On the Statement of Cash Flows, the amount reported as "Cash and Cash Equivalents" is equal to the total of the amounts on the Statement of Net Assets "Cash", "Cash with U.S. Treasury", "Cash and pooled investments with State Treasurer", "Cash held by trustee" and "Collateral investment pool" (for the Industrial Commission Special Fund). For purposes of the Statement of Cash Flows, the State considers only those highly liquid debt instruments with an original maturity of ninety days or less to be cash equivalents.

- *Cash (not with State Treasurer)* – includes undeposited receipts, petty cash, bank accounts, non-negotiable certificates of deposit, and demand deposits with banking institutions other than the State Treasurer.

- *Cash with U.S. Treasury* – consists of unemployment compensation contributions from Arizona employers that are deposited in a trust fund maintained by the United States Treasury.

- *Cash and pooled investments with State Treasurer* – consists of a centralized management of most State cash resources maintained by the State Treasurer. From the perspective of the various State funds, the pool functions as both a cash management pool and a demand deposit account. The operations and investments of the State Treasurer's pooled investments are described in Note 2.

- *Cash held by trustee* – consists of capital projects and bond debt service funds invested by the trustee in accordance with the applicable financing indenture, generally limited to United States Treasury securities and other Federal agency securities, certificates of deposit, commercial paper, and money market funds.

- *Collateral investment pool* – consists of cash received as collateral on securities lending transactions and investments made with that cash. The State records the collateral received as an asset. A corresponding liability is also recorded for such securities lending transactions.

2. Investment Valuation

Investments maintained by the State Treasurer are reported at fair value using Bank of New York (BONY) prices, as determined by independent, industry recognized data vendors who provide values that are either exchange based or matrix based. Rules and tolerance levels within BONY's security master database are used to determine reasonable accuracy. Equities are priced utilizing the primary market close price. In the absence of a closed price, the mid, bid, or ask price will be utilized. The State Treasurer also compares all equity prices to Bloomberg's Index Alert. All bonds are priced using an evaluated price, the closing exchange price or the most recent exchange or quoted bid, except securities with a remaining maturity of 90 days or less are priced at amortized cost (amortizing premium/accreting discount on a straight-line to maturity method). The official price is normally the last traded price.

The ASRS investments are reported at fair value determined by the custodial agents, except for real estate and commercial mortgages. The agent's determination of fair values includes, among other things, using pricing services or prices quoted by independent brokers at current exchange rates. The fair value of real estate investments is based on independent appraisals or estimated value. 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 are considered by the ASRS to be fully collectible. Short-term investments are reported at cost plus accrued interest, which approximates fair value. For investments where no readily ascertainable fair value exists, the ASRS, in consultation with its 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. Security transactions and any resulting gains or losses are accounted for on a trade date basis. Net investment income includes net appreciation (depreciation) in the 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, the EORP, and the CORP, investments are reported at fair value. 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. Directed real estate and venture capital investments are reported at cost. Investment income is recognized as earned.

E. TAXES RECEIVABLE

Taxes receivable include amounts owed by taxpayers for the 2006 and prior calendar years including assessments for underpayments, penalties, and interest. In the government-wide financial statements, a corresponding amount is recorded as revenue using the accrual basis of accounting. In the governmental fund financial statements, revenue is recorded using the modified accrual basis of accounting. The remainder is recorded as deferred revenues.

The income tax receivable is composed of individual and corporate estimated payments, withholding payments, and payments with final returns and assessments that relate to income earned through June 30, 2007. Sales and motor vehicle and fuel tax receivables represent amounts that are earned by the State in the fiscal period ended June 30, 2007, but not collected until the following month.

F. INVENTORIES

Inventories consist of expendable supplies held for consumption in all funds and merchandise intended for sale to customers in the proprietary funds. Inventories are stated at cost using the first-in, first-out method, weighted average, or lower of cost or market. In the governmental funds, inventories are accounted for using the consumption method. Under this method, inventories are recorded as expenditures as they are used.

G. PROPERTY TAX CALENDAR

Real property taxes are levied on or before the third Monday in August and become due and payable in two equal installments. The first installment is due on the first day of October and becomes delinquent after the first business day of November. The second installment is due on the first day of March of the next year and becomes delinquent after the first business day of May. A lien attaches on the first day of January preceding assessment and levy.

H. CAPITAL ASSETS

Capital assets are stated at cost at the date of acquisition or, if donated, at the estimated fair market value at the date received. Interest incurred during the construction of capital assets is only capitalized in the proprietary funds.

Most capital assets are depreciated over their useful life. However, the State utilizes an alternative accounting treatment for most infrastructure assets in which costs to maintain and preserve these assets are expensed and no depreciation expense is recorded. This approach is discussed further in the Required Supplementary Information portion of this report. The State has adopted a general policy for capitalization thresholds, depreciation, and estimated useful lives of capital assets. In addition, the State has approved alternative policies for some State agencies.

Depreciable capital assets are depreciated on a straight-line basis. Capitalization thresholds (the dollar values at which asset acquisitions are added to the capital asset accounts) and estimated useful lives of capital assets being depreciated in the government-wide financial statements and the proprietary funds are as follows:

	General State Policy		Other Authorized Agency Policies	
Asset Category	Capitalization Threshold	Estimated Useful Life (yrs)	Capitalization Threshold	Estimated Useful Life (yrs)
Land	All capitalized	Not depreciated	All capitalized	Not depreciated
Buildings	All capitalized	25-40	$0-$100,000	10-50
Improvements other than buildings	$5,000	15	$5,000-$100,000	20-50
Equipment	$5,000	3-15	$5,000	3-25
Infrastructure	All capitalized	Not depreciated	$0-$100,000	20-100

The State is trustee for approximately 9.3 million acres of land acquired through U.S. Government land grants in the early 1900's. The State acquired a substantial portion of this land at no cost and its fair market value at acquisition has not been reliably estimated. Accordingly, this land is not reported in 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 financial statements.

The State has interest in and maintains significant special collections, works of art, and historical treasures. Except for Arizona State University (ASU), all special collections, works of art, and historical treasures which are held for financial gain are capitalized at fair market value at the date of acquisition or donation. Those special collections, works of art, and historical treasures which are held for educational, research, or public exhibition purposes are not capitalized, as they are not subject to disposal for financial gain or encumbrance. Such items are inventoried for property control purposes. The ASU capitalizes all works of art and historical treasures with a unit cost of $5,000 or more.

Additional disclosures related to capital assets and assets acquired through capital leases are provided in Notes 4 and 6, respectively.

I. INVESTMENT EARNINGS

Investment earnings are composed of interest, dividends, and net changes in fair value of applicable investments.

J. SCHOLARSHIP ALLOWANCES

Student tuition and fee revenues, and certain other revenues earned by the three State Universities are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses and Changes in Fund Net Assets. A scholarship discount and allowance is the difference between the stated charge for goods and services provided and the amount that is paid by the student or third party making payment on behalf of the student. Accordingly, some types of student financial aid such as Pell grants and scholarships awarded by the Universities are considered to be scholarship allowances. These allowances are netted against applicable revenues in the Statement of Revenues, Expenses and Changes in Fund Net Assets.

K. DEFERRED REVENUE

Deferred revenue consists of payments to the State for goods and services, not yet rendered, or taxes, grants, and other non-exchange transactions for which related resources are not available to pay current liabilities. In the government-wide and proprietary fund financial statements, revenue is deferred when cash, receivables, or other assets are received prior to their being earned. In the governmental fund financial statements, revenue is deferred when that revenue is unearned or unavailable.

L. COMPENSATED ABSENCES

In the government-wide and proprietary fund financial statements, the State accrues liabilities for compensated absences as required by the GASB. In the governmental fund financial statements, liabilities for compensated absences are not accrued, because they are not considered due and payable.

In general, State employees accrue vested annual leave at a variable rate based on years of service. Except for uncovered State employees and University employees, 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. Uncovered State employees may accumulate up to 320 hours of vacation, and any vacation hours in excess of the maximum amount that are unused at December 31 are forfeited, unless an exception is authorized. University employees may accumulate up to 264 hours of vacation, and any vacation hours in excess of the maximum amount that are unused at December 31 are forfeited. Except for University employees, 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. University employees, upon termination of employment, are paid all unused vacation benefits not exceeding 176 hours (annual accrual amount), depending on years of service and full-time equivalent employment status.

Some employees accumulate compensatory leave for time worked over 40 hours per week. An employee may accumulate up to 240 hours of compensatory leave (480 if working in a public safety activity or an emergency response activity). An employee who separates from State service is paid for all unused compensatory leave at either the employee's average base salary during the last three years of employment or final base salary, whichever is higher.

For sick leave policy, see Note 11.C.

M. LONG-TERM OBLIGATIONS

In the government-wide and proprietary fund financial statements, long-term debt and long-term liabilities are reported as liabilities. Amounts due within one year are reported as current liabilities, and amounts due thereafter are reported as non-current liabilities. Premiums and discounts on revenue bonds and COPs are deferred and amortized over the life of the debt instrument using the straight-line method. Bonds and COPs are reported net of the applicable premium or discount. Bond issuance costs and deferred gains or losses on debt refundings are charged to expense in the period incurred unless those costs are deemed to be material to the State's financial statements by management, in which case, they are deferred and amortized using either the straight-line method or the effective interest method.

In the fund financial statements, governmental fund types recognize proceeds from revenue bonds, COPs, and premiums and discounts on revenue bonds and COPs as other financing sources and uses in the current period. Long-term liabilities are more fully described in Note 6.

N. NEW ACCOUNTING PRONOUNCEMENTS

GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans.* This Statement establishes uniform financial reporting standards for other postemployment benefit (OPEB) plans and supersedes the interim guidance included in GASB Statement No. 26, *Financial Reporting for Postemployment Healthcare Plans Administered by Defined Benefit Pension Plans.* The requirements of this Statement for OPEB plan reporting are effective for periods beginning after December 15, 2005. The PSPRS, the EORP, and the CORP have implemented the requirements of this standard, but they had no material effect on the financial statements. ASRS early implemented the requirements of this standard in 2006.

NOTE 2. DEPOSITS AND INVESTMENTS

A. DEPOSITS AND INVESTMENT POLICIES

The State's deposits and investments are primarily under the control of the State Treasurer, the Retirement Systems, the Universities, and the Commission. These entities maintain the majority of the deposits and investments of the primary government. The investment policies of these organizations are defined according to State statutes or a governing board or both and are described below.

The ARS §35-312, §35-313, and §35-314 authorize the State Treasurer to invest operating, trust, and permanent endowment fund monies. Monies deposited with the State Treasurer by State agencies are invested by the State Treasurer in a pooled fund. Any interest earned is allocated monthly into each respective fund based on average daily cash balances. There is no income from investments associated with one fund that is assigned to another fund.

The State statutes and the State Treasurer's investment policies designed to administer these statutes restrict investments to obligations of the U.S. Government and its agencies, obligations or other evidence of indebtedness of the State and certain local government subdivisions, negotiable certificates of deposit, bonds, debentures and notes issued by U.S. corporations, commercial paper issued by entities organized and doing business in the United States, bankers acceptances, collateralized repurchase agreements, money market mutual funds, domestic equities, and other securities. The State Treasurer is not allowed to invest in foreign investments.

The State Treasurer maintains external investment pools [the Local Government Investment Pool (LGIP), Local Government Investment Pool – Government, Local Government Investment Pool – Long Term, and the Central Arizona Water Conservation District]. The pools are not required to register (and are not registered) with the Securities and Exchange Commission under the 1940 Investment Advisors Act. The activity and performance of the pools are reviewed monthly by the State Board of Investment in accordance with 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.

State statutes authorize the retirement systems to make investments in accordance with the "Prudent Person" rule. This rule imposes the responsibility of making investments with the judgment and care that persons 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.

The ASRS invests in U.S. government and government agency obligations, real estate, commercial mortgages, corporate bonds, and equity obligations. Per ARS §38-719, no more than 80.00% of the ASRS' total assets may be invested at any given time in corporate stocks or equity equivalents, based on cost value of the stocks or equity equivalents irrespective of capital appreciation. No more than 5.00% of the voting stock of any one corporation may be owned. No more than 20.00% of the ASRS' assets may be invested in foreign equity securities, and those investments shall be made only by investment managers with demonstrated expertise in such investments. No more than 10.00% of the ASRS' assets may be invested in bonds or other evidences of indebtedness of those multinational development banks in which the U.S. is a member nation, including the International Bank for Reconstruction and Development, the African Development Bank, the Asian Development Bank, and the Inter-American Development Bank. No more than 1.00% of ASRS' assets may be invested in economic development projects authorized as eligible for such investment by the Arizona State Department of Commerce. The ASRS Board has not formally adopted more restrictive policies for the various types of risks.

Per ARS §38-848, the PSPRS, the EORP, and the CORP may not invest more than 70.00% of the respective pension fund at any given time in corporate stocks, based on cost value of such stocks irrespective of capital appreciation, and shall be restricted to stocks that, except for bank and insurance stocks, are either: 1) listed or approved on issuance for listing on an exchange registered under the Securities Exchange Act of 1934, as amended, 2) designated or approved on notice of issuance for designation on the national market system of a national securities association registered under the Securities Exchange Act of 1934, as amended, 3) listed or approved on issuance for listing on an exchange registered under the laws of this State or any other State, or 4) listed or approved on issuance for listing on an exchange registered of a foreign country with which the U.S. is maintaining diplomatic relations at the time of purchase, except that no more than 10.00% of the respective pension fund may be invested in foreign equity securities on these exchanges, based on the cost value of the stocks irrespective of capital appreciation. Not more than 5.00% of the voting stock of any one corporation shall be owned.

The Board of Regents governs the investment policies of the Universities. The Universities may invest operating funds and capital projects funds in collateralized certificates of deposits and repurchase agreements with commercial banks, U.S. Treasury securities and other Federal agency securities, or in the Local Government Investment Pool administered by the State Treasurer. For endowment investments, donor restrictions for these investments will be applied, if any. In addition, the Board of Regents has authorized the Universities to establish investment committees to make investment policies and investment decisions. The Board of Regents' policies guide the investment committees' decisions and constitute each University's investment policy.

Per ARS §23-1065, the Commission's investment committee is responsible for defining, developing, and implementing investment objectives, policies and restrictions and supervising the investment activities of the Commission. The Commission requires that their investment policy be responsive to the unpredictable nature of the incidence and severity of claims, the long periods over which losses may be paid, and the effect on both claims and losses of increases in treatment and rehabilitation costs. The investment committee may invest in any legal investment authorized under ARS §38-719.

B. CUSTODIAL CREDIT RISK – DEPOSITS AND INVESTMENTS

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the deposits or collateral securities may not be recovered from an outside party. The State Treasurer, the Retirement Systems, and the Universities' deposits with financial institutions are required by State statutes to be entirely covered by the Federal Depository Insurance Corporation (FDIC) or, alternatively, collateralized for amounts in excess of the amount insured. Surety collateral for the Universities, the ASRS, the PSPRS, the EORP, and the CORP must be equal to at least 100.00% of the bank balance required to be collateralized (102.00% for the State Treasurer). Beyond this requirement, these organizations do not have a formal policy specifically addressing custodial credit risk on deposits, except for the State Treasurer. The State statutes require surety collateral for the State Treasurer to consist of U.S. Government obligations, State obligations, and obligations of counties and municipalities within the State. As of June 30, 2007, some State agencies have uncollateralized and uninsured deposits in the amount of $2.756 million and $4.567 million in deposits collateralized with securities held by the pledging financial institution or its trust department/agent, but not in the State's name.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the value of the investment or collateral securities that are in the possession of an outside party may not be recovered. The State does not have a formal policy in regards to custodial credit risk for investments. As of June 30, 2007, the State had $34.547 million in securities that were uninsured, not registered in the State's name and held by a counterparty or a counterparty's trust department or agent but not in the State's name.

C. INTEREST RATE RISK

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The State manages interest rate risk using the segmented time distribution, weighted average maturity, and effective duration methods.

The State Treasurer manages interest rate risk by incorporating ARS §35-323, which states that the State Treasurer will invest public monies in securities with a maximum maturity of five years and operating fund monies shall not be invested for a duration of longer than three years, into their investment policy and setting forth various thresholds or parameters in accordance with each investment pool's portfolio structure. The State Treasurer's policy provides either maturity or duration limitations for the various investment pools. The interest rate risk inherent in the portfolio is monitored monthly by measuring the weighted average maturity and/or duration.

The ASU policy for operating funds limits the maximum maturity of any fixed rate issue to five years. The capital projects funds portfolio is not limited as to the overall maturity of its investments, with funds invested per the financing indentures to coincide with capital spending needs and debt service requirements, which are typically less than three years, with the additional limitation that certificates of deposit and commercial paper have maximum maturities of 360 days and 270 days, respectively.

The Commission approves and contracts with different investment managers of fixed income equities in order to manage the exposure to interest rate risk with each different fund manager focusing on different goals of yield periods or duration of maturities of their particular portion of the investment pool. Beyond this requirement, the Commission does not have a formal policy.

The following table presents the State Treasurer's, the ASU's, and the Commission's weighted average maturity in years by investment type (expressed in thousands):

Investment Type	Fair Value	Weighted Average Maturity (in years)
Bond mutual funds	$ 6,115	6.50
Certificate of deposit	4,994	.09
Commercial mortgage backed securities	3,904	32.20
Commercial paper	2,337,985	0.07
Corporate asset backed securities	6,462	6.12
Corporate collateralized mortgage obligations	58,165	19.41
Corporate notes & bonds	1,410,078	1.85
Government bonds	12,524	12.36
Government mortgage backed securities	26,216	17.62
Index linked government bonds	4,883	5.98
Money market mutual funds	62,758	0.09
Repurchase agreements	2,295,401	0.01
U.S. Agency securities	2,518,747	1.44
U.S. Agency mortgage backed securities	1,205,518	17.63
U.S. Treasury securities	788,650	1.62
U.S. Agency zeroes & strips securities	19,358	.63
Other	8,870	5.93
Total Debt Securities	$ 10,770,628	2.88

The ASRS does not have a formal policy in regards to interest rate risk, but does manage interest rate risk using effective duration. Effective duration measures the expected change in value of a fixed income security for a given change in interest rate. This method takes into account the likely timing and amounts of variable cash flows for bonds with call options and prepayment provisions. The following table presents ASRS' effective duration by investment type (expressed in thousands):

Investment Type	Fair Value	Effective Duration (in years)
Asset backed securities	$ 165,519	2.00
CMO's of government agencies	109,398	2.50
Commercial mortgage backed	531,022	4.10
Corporate bonds	1,354,427	3.40
Government agencies	500,359	4.50
Government bonds	948,615	1.80
Government mortgage backed	2,508,289	4.20
Non-government backed CMO's	125,576	2.20
Total Debt Securities	$ 6,243,205	3.24

The PSPRS, the EORP, the CORP, and the NAU do not have a formal policy in regards to interest rate risk. The U of A's investment policy limits its operating funds to having a portfolio comprised of a significant proportion of authorized securities with maturities of one year or less, and requires that a maximum maturity of any fixed rate issue may not exceed three years and the final maturity of any floating rate issue may not exceed five years. The U of A capital projects and endowment funds have no such limitations. The following table presents the interest rate risk for the PSPRS, the EORP, the CORP, the NAU, the U of A, and other State agencies utilizing the segmented time distribution (expressed in thousands):

		Investment Maturities (in years)					
Investment Type	**Fair Value**	**Less than 1**	**1-5**	**6-10**	**11-15**	**16-20**	**More than 20**
Corporate bonds	$ 651,403	$ 3,097	$ 122,607	$ 78,372	$ 60,154	$ 87,871	$ 299,302
Collateralized bond obligations (CBO's)	44,579	-	846	11,954	14,743	-	17,036
Collateralized debt obligations (CDO's)	12,128	-	-	7,999	-	-	4,129
Commercial paper	259,460	259,460	-	-	-	-	-
International fixed income fund	11,344	-	-	11,344	-	-	-
Money market mutual funds	84,606	84,606	-	-	-	-	-
Repurchase agreements	77,440	77,440	-	-	-	-	-
U.S. Agency securities	744,139	82,026	85,744	191,291	163,598	53,374	168,106
U.S. Treasury securities	596	-	177	419	-	-	-
Other investments	13,439	855	5,161	4,677	406	106	2,234
Total Debt Securities	$ 1,899,134	$ 507,484	$ 214,535	$ 306,056	$ 238,901	$ 141,351	$ 490,807

The following table presents the State's investments at fair value that are considered to be highly sensitive to interest rate changes (expressed in thousands):

Interest Rate Terms	**Corporate Securities**	**U.S. Agency Securities**	**Total**
U.S. LIBOR plus/minus fixed basis point which resets from monthly to semi-annually.	$ 1,003,576	$ 54,869	$ 1,058,445
Mortgage backed securities - when interest rates fall, mortgages are refinanced and paid off early and the reduced stream of future interest payments diminish fair value.	-	1,245,688	1,245,688
Callable step-up notes - where on certain specified dates, the issuer can call the security. If the security is not called, the interest rate is increased by a specified amount. Prevailing interest rates may go up faster than this increase in the coupon interest rate.	-	71,539	71,539
Other securities with high sensitivity to rate changes.	-	167,930	167,930
Total	$ 1,003,576	$ 1,540,026	$ 2,543,602

D. CREDIT RISK

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the holder of the investment.

The State statutes and the State Treasurer's investment policy require that commercial paper must be rated P1 by Moody's Investor Service (Moody's) or A1 or better by Standard and Poor's Ratings Service (S & P). Corporate bonds, debentures, and notes must carry a minimum Baa or better rating from Moody's or a BBB or better rating from S & P. For investments not rated by Moody's, Fitch rating information is used. There is no statute or investment policy on ratings or credit quality for obligations issued by the U.S. Government or its agencies or repurchase agreements. The underlying securities for repurchase agreements must be explicitly guaranteed by the U.S. Government.

The ASRS has not adopted a formal policy with respect to credit risk.

The PSPRS, the EORP, and the CORP's investment policy is specific as to permissible credit quality ranges, exposure levels within individual quality tiers, and the average credit quality of the overall portfolios. The fixed income portfolio must have a minimum weighted average quality rating of A3 by Moody's and A- by S & P. Fixed income investments must have a minimum quality rating of Baa3 by Moody's and BBB- by S & P at the time of purchase. Commercial paper must have a minimum quality rating of P1 by Moody's and A1 by S & P at the time of purchase. The portion of the bond portfolio in investments rated Baa3 through Baa1 by Moody's and BBB- through BBB+ by S & P must be 20.00% or less of the fair value of the fixed income portfolio.

The Universities' policies mirror that of the Board of Regents. The ASU's policy requires that capital projects and bond debt service funds are invested by the bond trustee in accordance with the applicable financing indenture, generally limited to U.S. Treasury securities and other Federal agency securities, certificates of deposit (minimum rating of P-1/A-1), commercial paper (minimum rating of P-1/A-1+), and money market funds rated AAAm or better invested in short-term debt securities. When investing endowment funds, U of A policy requires corporate bonds and notes to be of investment grade quality, rated Baa or higher by Moody's Investor Service, at the time of purchase. Beyond the requirements established by the Board of Regents, the NAU does not have a formal policy with respect to credit risk.

The Commission's investment policy requires that purchases of fixed income securities will consist of U.S. Treasury or Federal Agency obligations or those bonds rated not less than BA by Moody's or BB by S & P except for fixed income managers who have been hired to manage funds in a specialized manner (high yield).

The following table presents the State's investments which were rated by S & P and/or an equivalent national rating organization as of June 30, 2007. The ratings are presented using S & P's rating scale (expressed in thousands):

Investment Type	Fair Value	AAA	AA	A	BBB	BB	B	A1	Not Rated
Asset backed securities	$ 172,148	$ 164,487	$ 4,099	$ 2,306	$ 877	$ -	$ 379	$ -	$ -
Bond mutual funds	6,115	-	-	-	-	-	-	-	6,115
Certificates of deposit	4,994	-	4,994	-	-	-	-	-	-
CBO's	44,579	-	-	31,779	12,800	-	-	-	-
CDO's	71,490	59,362	-	8,000	4,128	-	-	-	-
CMO's of government sponsored entities	109,398	109,398	-	-	-	-	-	-	-
Commercial mortgage backed securities	534,926	531,892	1,991	280	763	-	-	-	-
Commercial paper	2,597,445	-	-	259,460	-	-	-	2,337,985	-
Corporate bonds	3,413,740	399,826	647,613	1,771,555	488,193	60,353	42,713	-	3,487
Government agencies	500,359	491,060	9,299	-	-	-	-	-	-
Government bonds	948,615	902,688	4,825	17,896	21,131	2,075	-	-	-
Government mortgage backed securities	2,529,738	2,508,289	-	-	-	-	-	-	21,449
International fixed income fund	11,344	-	-	-	-	-	-	-	11,344
Money market mutual funds	147,364	66,472	-	-	-	-	-	-	80,892
Mortgages	11,019	-	11,019	-	-	-	-	-	-
Municipal bonds	970	970	-	-	-	-	-	-	-
Non-government backed CMO's	125,576	125,545	-	31	-	-	-	-	-
U.S. Agency mortgage backed securities	885,245	885,245	-	-	-	-	-	-	-
U.S. Agency securities	3,249,671	2,515,826	14,757	-	-	-	-	718,992	96
U.S. Agency zeroes & strips	19,358	19,358	-	-	-	-	-	-	-
Other investments	21,339	2,917	632	517	-	-	-	-	17,273
Total	$15,405,433	$8,783,335	$699,229	$2,091,824	$527,892	$62,428	$43,092	$3,056,977	$ 140,656

E. CONCENTRATION OF CREDIT RISK

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The State Treasurer's, the ASRS', the U of A's, and the Commission's investment policies state that no more than 5.00% of their investments may be invested in securities issued by any one institution, agency, or corporation, other than securities issued as direct obligations of or that are fully guaranteed by the U.S. Government or mortgage backed securities and agency debentures issued by federal agencies. The PSPRS, the EORP, and the CORP's investment policy states that no more than 5.00% of their investments may be invested in securities issued by any one institution, agency, or corporation, other than securities issued as direct obligations of or that are fully guaranteed by the U.S. Government. The ASU and the NAU have no formal policy in regards to the concentration of credit risk. At June 30, 2007, more than 5.00% of the governmental activities' total investments were held in the following single issuers (expressed in thousands):

Issuer Description	Fair Value	Percentage
Federal Home Loan Mortgage Corporation	$ 902,835	12.80%
Federal Home Loan Bank	710,929	10.08%
Federal National Mortgage Association	881,437	12.50%

F. FOREIGN CURRENCY RISK

Foreign currency risk is the risk that changes in the foreign exchange rate will adversely impact the fair value of an investment or deposit. The State does not have a formal policy regarding foreign currency risk. The ASRS is the primary State agency that has foreign currency risk. Per ARS §38-719, no more than 20.00% of the ASRS assets may be invested in foreign equity securities and those investments shall be made only by investment managers with demonstrated expertise in those investments. The ASRS Board has not adopted a formal policy that is more restrictive. The following table summarizes the State's foreign currency risk as of June 30, 2007 (expressed in thousands):

	Foreign Currency Risk by Investment Type at Fair Value				
Currency	Short Term	Fixed Income	Equities	Real Estate	Total
Australian Dollar	$ 208	$ -	$ 86,454	$ -	$ 86,662
British Pound Sterling	148	-	692,300	-	692,448
Canadian Dollar	349	-	13,938	-	14,287
Czech Koruna	-	-	5,610	-	5,610
Danish Krone	529	-	26,488	-	27,017
Euro Currency	1,950	-	1,351	51	3,352
Hong Kong Dollar	205	-	53,236	58	53,499
Indonesian Rupiah	-	-	4,597	-	4,597
Japanese Yen	13,537	9,183	907,890	-	930,610
New Mexican Peso	-	1,687	-	-	1,687
New Taiwan Dollar	-	-	26,136	-	26,136
New Zealand Dollar	338	2,849	14,225	-	17,412
Norwegian Krone	288	-	21,171	-	21,459
Singapore Dollar	459	-	33,825	351	34,635
South Korean Won	-	-	81,282	-	81,282
Swedish Krona	3	-	23,196	-	23,199
Swiss Franc	492	-	345,882	-	346,374
Thailand Baht	-	-	1,980	-	1,980
Various mutual funds	4,760	13,044	91,013	-	108,817
Total	$ 23,266	$ 26,763	$ 2,430,574	$ 460	$ 2,481,063

G. UNEMPLOYMENT COMPENSATION

Pursuant to Section 904 of the Social Security Act (42 U.S.C. §1104), unemployment insurance contributions from Arizona employers are deposited in an unemployment trust fund account with the Secretary of the Treasury of the United States. 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. The Unemployment Compensation Fund, reported as a major enterprise fund, has been established for this purpose.

H. SECURITIES LENDING

Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. A corresponding liability is also recorded for such securities lending transactions.

1. Industrial Commission

State statutes and the Commission's 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 default 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., lender's exposure to the borrowers of its securities) related to the securities lending transactions at June 30, 2007. 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 102.00% of the market value of securities loaned plus accrued interest. International securities are loaned for collateral valued at 105.00% of the market value of securities loaned plus accrued interest. The market value at June 30, 2007 for loaned securities collateralized by cash and non-cash collateral was $52.205 million and $1.852 million, respectively. As part of the securities lending transactions, Northern Trust received cash and non-cash collateral valued at $53.300 million and $1.898 million, respectively at June 30, 2007. Non-cash collateral cannot be pledged or sold unless the borrower defaults. Deposit and investment risk disclosures are only reported for collateral received on securities lent.

All securities loans can be terminated on demand by either the lender or the borrower. The average term of the loans is 100 days and cash open collateral is invested in a short-term investment pool, the Core USA Collateral Section, which had an average weighted maturity of 39 days as of June 30, 2007. 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 were 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 Statement of Net Assets. A corresponding liability is recorded as the Commission must return the cash collateral to the borrower upon expiration of the loan. At June 30, 2007, the Commission had $53.300 million outstanding as payable for securities lending.

2. Arizona State Retirement System

The ASRS is permitted by ARS §38-715(D) (3), to enter into securities lending transactions. The ASRS' custodial bank enters into agreements with counterparts to loan securities and have the same securities redelivered at a later date. All securities are eligible for loan (U.S. fixed income securities, U.S. equities, and international equities) with a higher percentage of U.S. Treasuries on loan than most other security types. It is the policy of the ASRS to receive as collateral at least 102.00% of the market value of the loaned securities and maintain collateral at no less than 100.00% for the duration of the loan. At year-end, the ASRS has no credit risk exposure to borrowers because the amount the ASRS owes the borrowers exceeds the amount the borrowers owe the ASRS. The ASRS records the collateral received as an asset and the same amount as an obligation for securities on loan. Any cash collateral received is invested in short-term investments. The maturities of the investments are closely matched to those of the security loans to avoid interest rate exposure. The ASRS receives a spread for its lending activities. Investments made with cash collateral received are classified as an asset on the Statement of Fiduciary 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, 2007, the ASRS, including the Health Benefit Supplement Fund, had $3.5 billion outstanding as payable for securities on loan. The ASRS does not have the ability to pledge or sell the collateral unless there is a borrower default.

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

The EORP, the PSPRS, and the CORP are permitted by ARS Title 38, Chapter 5, Articles 3, 4, and 6, respectively, to enter into securities lending transactions. The PSPRS, the EORP, and the CORP are parties to securities lending agreements with a bank. The bank, on behalf of the PSPRS, the EORP, and the 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, the EORP, and the CORP require collateral of at least 102.00% of the fair value of the loaned U.S. Government or corporate security. Securities on loan are carried at fair value. As of June 30, 2007, the fair values of securities on loan were (expressed in millions):

PSPRS	$ 1,296.443
EORP	101.547
CORP	257.100

4. University of Arizona

During the fiscal year, the U of A engaged in securities lending transactions within its endowment funds, as authorized by the Board of Regents. The U of A entered into an agreement with Wells Fargo, the U of A's custodian, to carry out these transactions. The custodian enters into agreements with brokers to loan securities and have the same securities returned at a later date. It is the policy of the U of A to receive as collateral at least 102.00% of the market value of the loaned securities and accrued interest, and maintain collateral at no less than 100.00% for the duration of the loan. At year-end, the U of A had no credit risk to borrowers because the U of A was holding more collateral than the amount of loaned securities outstanding.

The U of A records the collateral received as an asset, which is offset by an obligation recorded under securities lending. During the fiscal year ended June 30, 2007, there were no violations of legal or contractual provisions, and there were no borrower or lending agent default losses. Wells Fargo does indemnify the U of A against losses due to borrower defaults. Collateral can be received in the form of U.S. Government securities, letters of credit, or cash. As of June 30, 2007, the custodian has received only cash collateral. This collateral may be invested in U.S. Treasury and sponsored agency obligations, repurchase agreements, bankers acceptances, commercial paper, mortgage backed securities, municipal securities, and corporate bonds or in a cash collateral investment pool, which invests in similar securities. At June 30, 2007, cash collateral received from borrowers was invested in the Enhanced Yield Business Trust and the Cash Collateral Investment Term Trust, which had a weighted average maturity of 15 days and 9 days, respectively, and represented 99.00% and 1.00% of cash collateral investments, respectively. The relationship between the maturities of the cash collateral investment pool and the U of A's securities loans is affected by the maturities of the securities loans made by other entities that use the custodian's pool, which the U of A cannot determine. However, the U of A or the borrower can terminate securities loans on demand. Other cash collateral investments are made such that their maturities will match those of the related securities loans. Such matching existed at year-end. At June 30, 2007, cash collateral investments totaled $79.306 million with a corresponding market value of securities on loan of $77.522 million. Securities lent for cash collateral included corporate stocks, corporate bonds, and U.S. government and agency notes and bonds. The U of A cannot sell or pledge securities received as collateral unless the borrower defaults. The U of A earns a negotiated fee for participating in securities lending activities.

I. DERIVATIVES

A derivative instrument is a financial instrument or other contract with all three of the following characteristics:

- It has (1) one or more underlyings and (2) one or more notional amounts or payment provisions or both. Those terms determine the amount of the settlement or settlements, and in some cases whether or not a settlement is required.

- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.

- Its terms require or permit net settlement, it can readily be settled net by means outside the contract, or it provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

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

Category	Purpose
Currency forward contracts	Hedge currency risk of investments denominated in foreign currencies.
Futures contracts	Reduce transaction costs; obtain market exposure; enhance returns.

Derivatives are reported at fair value. The fair value of currency forward contracts is determined by interpolating the spot rate and the forward rates based upon number of days to maturity. The interpolated rate is used to determine the unrealized gain/loss at the valuation date. The fair value of futures contracts is determined by calculating the difference between the closing Bloomberg market price on valuation date and the original futures trade price. Futures are settled daily.

Generally, derivatives are subject to both interest rate risk and credit risk. The derivatives utilized by ASRS internal investment managers typically have no greater interest rate risk than their physical counterparts, and in many cases are offset by exposure elsewhere in the portfolio. As of June 30, 2007, the ASRS had $1.6 billion in temporary investments held as collateral for equity and fixed income derivatives which may have a positive or negative notional value.

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.

Refer to Note 6.A.3.c for information on derivatives utilized by ASU.

J. 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, including the investment trust funds. A copy of the State Treasurer's Office Annual Financial Report can be obtained from their office location at:

Arizona State Treasurer's Office
1700 W. Washington St.
Phoenix, Arizona 85007-2812

The Treasurer's financial statements are audited by the Office of the Auditor General.

NOTE 3. RECEIVABLES/DEFERRED REVENUE

A. TAXES RECEIVABLE

The following table summarizes taxes receivable at June 30, 2007 (expressed in thousands):

Type of Tax	General Fund	Transportation & Aviation Planning, Highway Maintenance & Safety Fund	Unemployment Compensation Fund	Industrial Commission Special Fund	Non-Major Governmental Funds	Government-wide Total
Sales	$ 474,998	$ -	$ -	$ -	$ 2,449	$ 477,447
Income – individual and corporate	151,232	-	-	-	-	151,232
Motor vehicle and fuel	-	62,122	-	-	-	62,122
Luxury	7,563	-	-	-	15,994	23,557
Unemployment	-	-	70,433	-	-	70,433
Other	-	-	-	5,418	-	5,418
Gross taxes receivable	633,793	62,122	70,433	5,418	18,443	790,209
Allowance for uncollectible taxes	(140,947)	-	-	-	-	(140,947)
Net Taxes Receivable	$ 492,846	$ 62,122	$ 70,433	$ 5,418	$ 18,443	$ 649,262

B. DEFERRED REVENUE

At June 30, 2007, the components of deferred revenue, in terms of revenue unavailable and unearned, were as follows (expressed in thousands):

Current Deferred Revenue for Governmental Funds:	**Unavailable**	**Unearned**	**Total Deferred Revenue**
General Fund:			
Delinquent sales tax	$ 103,729	$ -	$ 103,729
Delinquent income tax	79,439	-	79,439
Tobacco settlement	46,002	-	46,002
Child support administrative reimbursements	3,813	-	3,813
Advance insurance premiums	-	45,504	45,504
Advance land lease payments	-	291	291
Public assistance overpayments	1,533	-	1,533
Vaccine & commodity food supplement	-	1,867	1,867
Advanced county Medicaid payments	-	464	464
Federal grants	251,441	-	251,441
Other	186	102	288
Transportation & Aviation Planning, Highway Maintenance & Safety Fund:			
Notes receivable for real estate mortgage loans	7,623	-	7,623
Land Endowments Fund:			
Land sales receivable	1,030,970	-	1,030,970
Land leases receivable	2,730	-	2,730
Advance land lease payments	-	17,756	17,756
Non-Major Funds:			
Public assistance overpayments	1,203	-	1,203
Advance payments for Hawaii/Arizona PMMIS Alliance	-	1,236	1,236
Other	-	44	44
Total Current Deferred Revenue for Governmental Funds	1,528,669	67,264	1,595,933
Noncurrent Deferred Revenue for Governmental Funds:			
General Fund:			
Advance land lease payments	-	5,715	5,715
Land Endowments Fund:			
Advance land lease payments	-	34,231	34,231
Total Noncurrent Deferred Revenue for Governmental Funds	-	39,946	39,946
Total Current and Noncurrent Deferred Revenue for Governmental Funds	$ 1,528,669	$ 107,210	$ 1,635,879

Current Deferred Revenue for Proprietary Funds:	**Unearned**
Universities:	
Unexpended cash advances received	$ 36,128
Auxiliary sales and services	5,763
IBM lease related to acquisition of research park	4,900
Student tuition and fees	42,838
Other deferred revenue	1,498
Deposits	1,467
Non-Major Funds:	
Policyholders' advance premiums	10,054
Magazine subscriptions	3,196
Other	35
Total Current Deferred Revenue for Proprietary Funds	$ 105,879
Noncurrent Deferred Revenue for Proprietary Funds:	
Universities:	
IBM lease related to acquisition of research park	$ 29,870
Total Noncurrent Deferred Revenue for Proprietary Funds	$ 29,870

NOTE 4. CAPITAL ASSETS

Capital asset activities for the fiscal year ended June 30, 2007 were as follows (expressed in thousands):

	Primary Government				
	Beginning Balance	Additions	Retirements	Adjustments & Reclassifications	Ending Balance
Governmental Activities:					
Non-depreciable capital assets:					
Land	$ 2,227,782	$ 165,432	$ (24,779)	$ 290	$ 2,368,725
Construction in progress	2,036,194	596,349	(482,599)	(28,786)	2,121,158
Infrastructure	9,379,755	488,033	(12,647)	-	9,855,141
Total Non-depreciable Capital Assets	13,643,731	1,249,814	(520,025)	(28,496)	14,345,024
Depreciable capital assets:					
Buildings	1,527,996	10,493	(442)	139,150	1,677,197
Improvements other than buildings	133,624	3,609	(114)	1,210	138,329
Equipment	696,119	71,984	(39,744)	4,331	732,690
Infrastructure	6,609	-	-	-	6,609
Total Depreciable Capital Assets	2,364,348	86,086	(40,300)	144,691	2,554,825
Less accumulated depreciation for:					
Buildings	(458,373)	(57,837)	376	9,592	(506,242)
Improvements other than buildings	(63,549)	(4,198)	16	2	(67,729)
Equipment	(492,423)	(59,480)	37,528	5,268	(509,107)
Infrastructure	(4,259)	(95)	-	-	(4,354)
Total Accumulated Depreciation	(1,018,604)	(121,610)	37,920	14,862	(1,087,432)
Total Depreciable Capital Assets, Net	1,345,744	(35,524)	(2,380)	159,553	1,467,393
Total Governmental Activities Capital Assets, Net	$ 14,989,475	$ 1,214,290	$ (522,405)	$ 131,057	$ 15,812,417

	Beginning Balance (As restated)	Additions	Retirements	Adjustments & Reclassifications	Ending Balance
Business-type Activities:					
Non-depreciable capital assets:					
Land	$ 143,587	$ 13,566	$ (4,451)	$ 336	$ 153,038
Construction in progress	163,030	157,927	(418)	(220,141)	100,398
Collections	34,159	1,223	(71)	-	35,311
Total Non-depreciable Capital Assets	340,776	172,716	(4,940)	(219,805)	288,747
Depreciable capital assets:					
Buildings	3,101,431	126,221	(6,476)	210,162	3,431,338
Improvements other than buildings	3,601	-	-	(1)	3,600
Equipment	1,143,858	109,225	(43,087)	-	1,209,996
Infrastructure	305,975	10,789	(291)	9,745	326,218
Total Depreciable Capital Assets	4,554,865	246,235	(49,854)	219,906	4,971,152
Less accumulated depreciation for:					
Buildings	(1,123,046)	(105,768)	2,624	18	(1,226,172)
Improvements other than buildings	(2,251)	(134)	-	-	(2,385)
Equipment	(792,684)	(76,938)	39,448	-	(830,174)
Infrastructure	(96,125)	(10,491)	165	(16)	(106,467)
Total Accumulated Depreciation	(2,014,106)	(193,331)	42,237	2	(2,165,198)
Total Depreciable Capital Assets, Net	2,540,759	52,904	(7,617)	219,908	2,805,954
Total Business-type Activities Capital Assets, Net	$ 2,881,535	$ 225,620	$ (12,557)	$ 103	$ 3,094,701

Refer to Note 8.B. for explanation of Business-type Activities restatement.

Depreciation expense was charged to governmental functions as follows (expressed in thousands):

General government	$	22,831
Health and welfare		21,093
Inspection and regulation		1,591
Education		564
Protection and safety		50,186
Transportation		16,962
Natural resources		8,383
Total Governmental Activities	$	121,610

Depreciation expense was charged to business-type activities as follows (expressed in thousands):

Lottery	$	260
Industrial Commission Special Fund		1,232
Universities		189,951
Other		1,888
Total Business-type Activities	$	193,331

NOTE 5. RETIREMENT PLANS AND OTHER POST-EMPLOYMENT BENEFITS

The State participates in the ASRS, the PSPRS, the EORP, and the 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 other State political subdivisions.

A. PARTICIPATING EMPLOYERS

The number of participating government employers as of June 30, 2007 is shown below:

Employer	ASRS	PSPRS	EORP	CORP
Cities and towns	76	134	21	-
Counties and county agencies	15	24	15	13
State	1	1	1	1
Special districts	85	51	-	-
School districts	235	-	-	-
Charter schools	172	-	-	-
Community college districts	10	-	-	-
Dispatchers	-	-	-	6

B. CONTRIBUTIONS, BENEFITS, AND REFUND PAYMENTS

The ASRS 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. Benefit and refund payments are recognized when due and payable in accordance with the terms of the retirement health benefit supplement and long-term disability plan.

PSPRS, EORP, and CORP financial statements are prepared using the accrual basis of accounting. Member and employer contributions are recognized when due, pursuant to formal commitments, as well as statutory or contractual requirements. Pension and health insurance subsidy benefits are recognized when due and payable in accordance with the terms of the Plan. Refunds are due and payable by state law within 20 days of receipt of a written application for a refund. Refunds are recorded when paid.

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, 2007, active ASRS members and the State were each required by statute to contribute at the actuarially determined rate of 9.10% (8.60% retirement and 0.50% long-term disability) of the members' annual covered payroll. The State's contributions to the ASRS for the years ended June 30, 2007, 2006, and 2005 were $171.613 million, $128.575 million, and $93.148 million, respectively, for the primary government which were equal to the required contributions for these years.

In addition, active EORP members were required by statute to contribute 7.00% 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 18.55% of the members' annual covered payroll, as determined by actuarial valuation. The State's contributions to EORP for the years ended June 30, 2007, 2006, and 2005 were $1.953 million, $2.140 million, and $1.010 million, respectively, which were equal to the required contributions for these years.

Agent plans – For the year ended June 30, 2007, active PSPRS members were required by statute to contribute 7.65% of the members' annual covered payroll and the participating State agencies were required to contribute at actuarially determined rates of 7.84 – 30.40%. Active CORP members were required by statute to contribute 8.50% of the members' annual covered payroll and the participating State agencies were required to contribute at actuarially determined rates of 4.33 – 4.66%.

D. ANNUAL PENSION COST

The State's annual pension cost and related actuarial data for each of the agent, multiple-employer defined benefit pension plans for the year ended June 30, 2007, is as follows (expressed in thousands):

	PSPRS	CORP
Contribution rates:		
State	7.84 – 30.40%	4.33 – 4.66%
Plan members	7.65%	8.50%
Annual pension cost	$19,993	$17,494
Contributions made	$19,993	$17,494
Actuarial valuation date	6/30/05	6/30/05
Actuarial cost method	projected unit credit	projected unit credit
Actuarial assumptions:		
Investment rate of return	8.50%	8.50%
Projected salary increases	5.50 – 8.50%	5.50 – 8.50%
includes inflation at	5.00%	5.00%
Cost-of-living adjustments	None	None
Amortization method	level percent open	level percent open
Remaining amortization	30 years	30 years
Asset valuation method	smoothed market value	smoothed market value

E. TREND INFORMATION

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

Contributions Required and Contributions Made

	Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
PSPRS	6/30/07	$19,993	100%	$ 0
	6/30/06	15,878	100%	0
	6/30/05	6,442	100%	0
CORP	6/30/07	17,494	100%	0
	6/30/06	17,472	100%	0
	6/30/05	12,754	100%	0

F. UNIVERSITIES' RETIREMENT PLANS

Faculty, academic professional, and administrative officers at the three universities (the ASU, the NAU, and the U of A) may select one of four retirement plans: the Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), Fidelity Investments Tax-Exempt Services Company (Fidelity), or the ASRS. The ASRS is a defined benefit plan and the other three plans are defined contribution plans. The three defined contribution plans are administered by independent insurance and annuity companies approved by the ABOR. In addition, the U of A employees hired before July 1, 1972, have the option to participate in the defined contribution plan administered by the ASRS. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. Contributions made by employees vest immediately and the Universities' contributions vest no later than after five years of full-time employment. Employees and Universities' contributions and associated returns earned on investments may be withdrawn starting upon termination of employment, death, or retirement. The distribution of employee contributions and associated investment earnings are made in accordance with the employee's contract with the applicable insurance and annuity company. Universities' contributions and associated investment earnings must be distributed to the employee in the form of an annuity paid over the employee's life.

The Arizona State Legislature establishes and may amend active plan members' and the Universities' contribution rates. For the year ended June 30, 2007, plan members and the three Universities were each required by statute to contribute an amount equal to 7.00% of an employee's compensation, except for an 8.16% contribution for the ASRS defined contribution plan.

Contributions to these plans for the year ended June 30, 2007, were as follows (expressed in thousands):

Plan	University Contributions	Employee Contributions	Total Contributions
TIAA/CREF	$ 29,529	$ 29,529	$ 59,058
VALIC	3,215	3,215	6,430
Fidelity	10,978	10,978	21,956
ASRS	100	85	185

G. POST-EMPLOYMENT BENEFITS

In addition to the pension benefits described, the ASRS administers the Health Benefit Supplement Fund (HBS) and the Long Term Disability Fund, which are defined benefit cost-sharing, multiple-employer post-employment benefit plans. Although the assets of the HBS plan are commingled with assets of the Retirement Fund, each plan's assets may be used only for the payment of benefits to the members of the plan, in accordance with terms of the plan.

The ASRS offers the Retiree Group Insurance Program and the Health Insurance Premium Benefit Program to eligible retired and disabled members. A retired member is defined as a member actively receiving an annuity benefit and a disabled member is defined as a member receiving a Long-Term Disability (LTD) benefit through the LTD program administered by the ASRS or through their former member employer's group LTD plan. The employees and member employers each contributed .50% of compensation in FY 2007.

Pursuant to ARS §38-782, the Retiree Group Insurance Program makes available group health insurance coverage to eligible retired and disabled members and their dependents. Retired and disabled members of the ASRS, University Optional Retirement Plans, the PSPRS, the EORP, and the CORP are eligible for health insurance benefits through the ASRS. As of June 30, 2007, approximately 53,970 coverage agreements currently exist for retired and disabled members and their dependents.

Pursuant to ARS §38-783, retired and disabled members with at least five years of credited service are eligible to participate in the Health Insurance Premium Benefit Program. This assistance is provided to those members who elect group coverage through either the Retiree Group Insurance Program or their former member employer.

In FY 2007 the employer's retirement contribution of 8.60% of compensation included 1.05% for the Health Premium Insurance Supplement.

The amount of the monthly subsidy the ASRS provides to retired or disabled participants is dependent upon the number of years of credited service; whether the participant is eligible for Medicare coverage; if the participant elects group insurance coverage for spouse or dependents; and if the participant lives in an area of the State where no health maintenance organization is available.

The amount of the monthly subsidy paid on a member's and their dependents' behalf toward the cost of group health insurance by the ASRS ranges from $50 to $470.

The ASRS, as the employer, made contributions to the Health Benefit Supplement Fund and the Long Term Disability Fund in the amounts of $118 thousand and $51 thousand, respectively for FY 2007. The contributions were equal to the required contributions. The projected unit credit method is the actuarial cost method used in the valuations for the funding requirements.

The State Legislature in ARS §38-783 has made the payment of the healthcare subsidy to retired and disabled participants subordinate to the payment of normal retirement benefits.

In addition to pension benefits described, the PSPRS, the CORP, and the EORP offer a health insurance premium subsidy. For the PSPRS and the CORP, the subsidy program is an agent, multi-employer defined benefit post-employment plan. For the EORP, the subsidy program is a cost-sharing, multiple-employer defined benefit post-employment plan.

The subsidized health benefits are provided and administered by the ASRS, Arizona Department of Administration or the participating employer of the retired member. The PSPRS, the EORP, and the CORP do not administer a separate healthcare plan as defined under IRC § 401(h) or an equivalent agreement. In addition, the PSPRS, the EORP, and the CORP are not statutorily authorized to maintain a separate account for the health insurance subsidy assets and benefits payments. Therefore, in accordance with GASB Statement No. 43, the health insurance subsidy is reported as an agency fund. All assets of the PSPRS, the EORP, and the CORP are available to pay both pension benefits and the health insurance subsidy.

The health insurance subsidy is funded through employer contributions based on an annual actuarial valuation determined using the projected unit credit actuarial funding method. Contributions are separately accounted for by the employer but are not segregated by contribution type. Contributions in excess of the health insurance subsidy payments are reported in the pension plan. Therefore, no accumulated assets or liabilities to participating employers are reported in the agency fund.

Pursuant to ARS §38-857 and ARS §38-906 for the PSPRS and the CORP, respectively, the fund manager shall pay part of the single or family coverage premium of any group health insurance for each retired member or survivor of the PSPRS and the CORP who receives a pension and who has elected to participate in the coverage provided or administered by a participating employer of the PSPRS or the CORP. The amount of the subsidy provided to retired participants is dependent upon whether the participant is eligible for Medicare coverage; if the participant elects group insurance coverage for spouse or dependents; and if the participant lives in an area of the State where no health maintenance organization is available. The amount of the monthly subsidy paid on a member's and their dependents' behalf toward the cost of group health insurance by the PSPRS and the CORP ranges from $100 to $470.

Pursuant to ARS §38-817 for the EORP, the benefit description is the same as the PSPRS and the CORP, except the retired member must have eight or more years of credited service to receive the full benefit. Those retired members who had between five and eight years of credited service will receive a proportionate share of the subsidies.

NOTE 6. LONG-TERM OBLIGATIONS

A. REVENUE BONDS

Governmental Activities

1. Arizona Department of Transportation

The ADOT issued Senior and Subordinated Highway Revenue Bonds to provide funds for acquisition of right-of-way and construction of federal, state, and local highways. The original amount of Highway Revenue Bonds issued in prior years and outstanding at the start of the fiscal year was $1.2 billion. During the year, Highway Revenue Bonds totaling $325.000 million were issued to finance portions of the Transportation Board's Five Year Transportation Facilities Construction Program and pay the costs of issuing the bonds.

The Highway Revenue Bonds are secured by a prior lien on and a pledge of motor vehicle and related fuel fees and taxes. On September 21, 2006, House Bill 2206, Chapter 284, became effective and eliminated the restriction that limited the principal amount of the Highway Revenue Bonds that could be outstanding at any time to $1.3 billion. Also during fiscal year 2007, the

ADOT received legislative authority to begin issuing Highway Revenue Bonds with maturities of up to 30 years in length, replacing the 20 year maturity requirement that has been in place since 1980.

The Maricopa County Regional Area Road Bond Fund is used to record all payments of principal and interest for Transportation Excise Tax Revenue Bonds issued by the ADOT. The bonds are secured by transportation excise taxes collected by the Arizona Department of Revenue on behalf of Maricopa County. There were no Transportation Excise Tax Revenue Bonds issued in prior years and outstanding at the start of the fiscal year or issued during the fiscal year.

In prior fiscal 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, redemption premium, if any, 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. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased bonds are not reflected in the accompanying financial statements. Refunded bonds for the ADOT at June 30, 2007 totaled $212.880 million.

2. School Facilities Board

In prior fiscal years, the SFB refinanced various bond issues through advance-refunding arrangements. Under the terms of the refunding bond issues, sufficient assets to pay all principal, redemption premium, if any, 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. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased bonds are not reflected in the accompanying financial statements. Refunded bonds for the SFB at June 30, 2007 totaled $446.680 million.

Business-Type Activities

3. Universities

a. University of Arizona

The U of A's bonded debt consists of various issues of system revenue bonds that are generally callable with interest payable semi-annually. Bond proceeds are used to pay for acquiring or constructing capital facilities and infrastructure. Bond proceeds are also used for refunding obligations from previously issued bonds. Payment of principal and interest on bonds is secured by a pledge of tuition and fees, sales and services, auxiliary enterprises, and other charges.

On April 12, 2007, the U of A sold System Revenue Bonds Series 2007 (2007 Bonds) for $31.010 million dated April 1, 2007. The 2007 Bonds include $23.570 million of serial bonds with interest rates ranging from 4.00% to 5.00% and maturity dates ranging from 2008 to 2028. The 2007 Bonds also include a term bond consisting of $7.440 million with an interest rate of 4.375% due June 1, 2032. The 2007 Bonds with maturity on or after June 1, 2018 are subject to optional redemption without premium. The 2007 Bonds with maturity on June 1, 2032 are subject to mandatory sinking fund redemption without premium pursuant to the debt documents. The 2007 Bonds sold at a discount of $55 thousand. The U of A realized net proceeds of $30.600 million after payment of $355 thousand for issuance costs, underwriter discounts, and bond insurance. The net proceeds were used to finance the Intercollegiate Athletics Facilities Project, the Law Commons Project, and the Residence Life Building Renewal Phase IIA and IIIA Project.

In fiscal year 2003, the U of A refunded, in advance of maturity, a portion of outstanding System Revenue Bonds Series 2000A. At June 30, 2007, the outstanding principal balance of the refunded bonds was $3.695 million, which will be paid by investments held in an irrevocable trust with a fair value of $3.745 million. Accordingly, the trust account assets and liability for these defeased bonds are not included in the accompanying financial statements.

In fiscal year 2005, the U of A refunded, in advance of maturity, a portion of outstanding System Revenue Bonds Series 1998 and the remaining portion of System Revenue Bonds Series 2000A. At June 30, 2007, the total outstanding principal balance of the refunded bonds was $28.285 million, which will be paid by investments held in an irrevocable trust with a total fair value of $29.307 million. Accordingly, the trust account assets and liability for these defeased bonds are not included in the accompanying financial statements.

b. Northern Arizona University

On December 12, 2006, the NAU sold System Revenue and Refunding Bonds Series 2006 (2006 Bonds) for $42.260 million dated December 1, 2006. The 2006 Bonds include $20.600 million of serial bonds with interest rates ranging from 4.00% to 5.00% and maturity dates ranging from June 1, 2008 to June 1, 2027. The 2006 Bonds also include $21.660 million of term bonds, with an interest rate of 4.50% and maturing on June 1, 2031 and 2034 and are subject to annual sinking fund contributions. The bonds maturing on or after June 1, 2018 are subject to optional redemption without premium on June 1, 2017. The 2006 Bonds were sold with net original issue premium of $1.803 million and had accrued interest of $110 thousand. The NAU realized net proceeds of $43.713 million after payment of $460 thousand for issuance costs, underwriter discounts, and bond insurance. The costs associated with this issue were recorded in the current fiscal year. The 2006 Bonds have an average interest rate of 4.68%, and the refunded portion of the Series 2002 System Revenue Bonds and the Series 2003 System Revenue Bonds had average interest rates of 5.00% and 5.50%, respectively. Although the recognition of the difference between the reacquisition price and the net carrying amount of the old debt of $1.194 million, which was reported in the financial statements as a deferred charge for the year ended June 30, 2007, the NAU reduced its aggregate debt service payments by $3.658 million over the next 27 years and obtained an economic gain (i.e., the difference between the present values of the old and new debt service payments) of $2.266 million. The proceeds were used to refund $17.410 million of the Series 2002 Bonds and $23.720 million of the Series 2003 Bonds.

In prior years, the NAU 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 refunded bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the accompanying financial statements. At June 30, 2007, $41.245 million of such bonds outstanding are considered defeased.

c. Arizona State University

At June 30, 2007, the ASU held a combination of fixed and variable rate bonds. The ASU's fixed rate bonded debt consists of various issues of system revenue bonds that are generally callable at a prescribed date with interest payable semi-annually. In prior years, certain system revenue bonds of the ASU were defeased through advance-refunding by depositing sufficient U.S. Government securities to pay all future debt service in an irrevocable trust. Accordingly, the liabilities for these defeased bonds are not included in the accompanying financial statements. The principal amount of all such bonds outstanding at June 30, 2007 was $46.900 million.

The ASU has outstanding two series of variable rate demand system revenue bonds, Series 2003A and 2003B, totaling $103.000 million, with final maturities of July 1, 2034. Both series of bonds continue to bear interest at a weekly rate not to exceed 12.00% per annum based upon prevailing market conditions, as determined by the respective remarketing agents. The bonds are subject to conversion, at the option of the ABOR on behalf of the ASU, to a different or alternate adjustable rate mode, or a fixed rate pursuant to the bond indenture. The interest rate in effect on June 30, 2007 was 3.70% for the Series 2003A bonds and 3.72% for the Series 2003B bonds.

The variable rate bonds are subject to purchase on the demand of the holder at a price equal to principal plus accrued interest on seven days' notice and delivery to the remarketing agents. If the remarketing agents are unable to resell the bonds, the ASU has a Standby Purchase Agreement with Bank of America, N.A. to extend credit through the purchase of the unremarketed bonds. Assuming all of the $51.500 million Series 2003A bonds and $51.500 million Series 2003B bonds are not resold within 90 days, the ASU would be responsible to make annual installment principal payments of $20.600 million over a five year period, plus interest to be calculated as established in the Standby Purchase Agreement. The ASU has agreed to pay Bank of America, N.A. an annual commitment fee of 0.18% on the outstanding principal for the Standby Purchase Agreement. The Standby Purchase Agreement is valid through October 15, 2008. The ASU is in the process of terminating the current Standby Purchase Agreement and entering into a new agreement.

Effective January 1, 2007, the ASU entered into a swap agreement on $103.000 million, notional amount, relating to the 2003 variable rate demand system revenue bonds (2003 Bonds). The $103.000 million in bond principal is not exchanged; it is only the basis on which the interest payments are calculated. The notional amount under the swap decreases as principal payments are made on the 2003 Bonds so the notional amount equals the principal outstanding under the bonds. The intention of the swap is to effectively change the variable rate interest on the 2003 Bonds to a fixed rate of 3.91%. The swap agreement expires on July 1, 2034. Under the terms of the swap agreement, the ASU pays the counterparty interest calculated at a fixed rate of 3.91% and receives payments from the counterparty based on the BMA Municipal Swap Index that is set weekly. The BMA rate at June 30, 2007 was 3.73%. At June 30, 2007, the synthetic fixed interest rate on the bonds is shown below:

Interest Rate Swap	Terms	Rates (%)
Fixed payment to counterparty	Fixed	3.91
Variable payment from counterparty	BMA	(3.73)
Net interest rate swap payments		.18
Variable-rate bond coupon payments	Spread to BMA	3.71
Synthetic fixed interest rate on bonds		3.89

As of June 30, 2007, the swap had a fair value of $2.722 million, which represents the cost to the counterparty to terminate the swap. The fair value was developed by an independent third party, with no vested interest in the transaction, using the zero-coupon discounting method. This method calculates the future payments required by the swap, assuming the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement on the swaps.

As of June 30, 2007, the ASU was exposed to credit risk of the counterparty on the termination payment because the swap had a positive fair value. The swap counterparty was rated AA- by Fitch and Standard & Poor's and Aa3 by Moody's Investor Services as of June 30, 2007. Based on current ratings, the counterparty was not required to provide collateral. In the event a rating downgrade occurs, the counterparty may be required to provide collateral if the ASU's overall exposure exceeds predetermined levels. Collateral may be held by the ASU or a third party custodian.

The swap exposes the ASU to basis risk should the weekly BMA rate paid by the counterparty fall below the weekly interest rate due on the bonds which is also a variable rate with a spread to BMA. This basis risk can be the result of a downgrade of the ASU's rating or the pricing of the ASU's bonds by the remarketing agents at rates higher than the BMA index.

The ASU continues to pay interest to the bondholders at the variable rate provided by the bonds. However, during the term of the swap agreement, the ASU effectively pays a fixed rate on the debt. If a default occurs regarding the swap agreement, the non-defaulting party may designate a date to terminate the agreement. The ASU will revert to a variable rate if the counterparty defaults or if the swap is terminated. A termination of the swap agreement may also result in the ASU making or receiving a termination payment.

In February 2007, the ASU issued $76.260 million in system revenue bonds at an average interest rate of 4.46%. The bonds were issued primarily to fund classroom and laboratory renovations and deferred maintenance, infrastructure upgrades, land acquisition, site preparation, and construction of a new University Police Department facility. The bonds were issued at a premium with a net addition of $2.100 million for bond premium, underwriting fees, and other issuance costs.

Securities and cash restricted for bond debt service held by the trustee at June 30, 2007 totaled $24.200 million.

The ASU has pledged portions of its gross revenues towards the payment of debt related to various system revenue bonds outstanding at June 30, 2007. These pledged revenues include student tuition and fees, certain auxiliary enterprise revenue, investment income, and indirect cost recovery revenue. Pledged revenues do not include state appropriations, gifts, endowment income, or other restricted revenues.

The ASU presently plans to issue approximately $33.000 million in system revenue bonds during fiscal year 2008.

Summary of Revenue Bonds

The following schedule summarizes revenue bonds outstanding at June 30, 2007 (expressed in thousands):

Revenue Bonds Outstanding	Dates Issued	Maturity Dates	Interest Rates	Outstanding Balance at June 30, 2007
Governmental Activities:				
Department of Transportation	1994-2007	2008-2026	3.40-6.00%	$1,490,600
School Facilities Board	2001-2006	2008-2021	.14-5.75%	838,240
Proprietary Funds:				
University Revenue Bonds	1992-2007	2008-2040	2.50-6.50%	868,565

Principal and interest debt service payments on revenue bonds outstanding at June 30, 2007 are as follows (expressed in thousands):

	Annual Debt Service						
	Governmental Activities			Business-type Activities			
Fiscal Year	Total Principal	Total Interest	Total	Total Principal	Total Interest	Net Payments on Swap Agreement at .18%	Total
2008	$ 108,925	$ 117,001	$ 225,926	$ 47,865	$ 41,744	$ 186	$ 89,795
2009	114,715	111,407	226,122	46,215	37,844	186	84,245
2010	121,080	105,790	226,870	49,820	35,449	186	85,455
2011	127,520	99,277	226,797	52,035	32,978	183	85,196
2012	134,220	92,528	226,748	41,560	30,467	178	72,205
2013-2017	788,525	351,602	1,140,127	238,145	117,913	823	356,881
2018-2022	726,255	144,443	870,698	145,825	71,298	685	217,808
2023-2027	207,600	22,719	230,319	117,715	41,074	509	159,298
2028-2032	-	-	-	84,200	18,424	284	102,908
2033-2037	-	-	-	42,740	3,453	38	46,231
2038-2042	-	-	-	2,445	244	-	2,689
Total	$ 2,328,840	$ 1,044,767	$ 3,373,607	$ 868,565	$ 430,888	$ 3,258	$ 1,302,711

B. GRANT ANTICIPATION NOTES

Grant Anticipation Notes are issued by the Transportation Board and secured by revenues received from the Federal Highway Administration under a grant agreement and certain other federal-aid revenues. The original amount of Grant Anticipation Notes issued in prior years and outstanding at the start of the fiscal year was $325.430 million.

Grant Anticipation Notes currently outstanding are as follows (expressed in thousands):

Grant Anticipation Notes Outstanding	Dates Issued	Maturity Dates	Interest Rates	Outstanding Balance at June 30, 2007
Governmental Activities:				
Department of Transportation	2001-2005	2008-2016	2.50-5.25%	$ 282,860

Future debt service principal and interest payments on Grant Anticipation Notes issues for fiscal years ended June 30 are summarized below (expressed in thousands):

Annual Debt Service			
Governmental Activities			
Fiscal Year	Total Principal	Total Interest	Total Debt Service
2008	$ 36,565	$ 13,300	$ 49,865
2009	29,990	11,832	41,822
2010	31,350	10,468	41,818
2011	32,785	9,034	41,819
2012	34,360	7,461	41,821
2013-2017	117,810	12,613	130,423
Total	$ 282,860	$ 64,708	$ 347,568

C. CERTIFICATES OF PARTICIPATION

Governmental Activities

1. Department of Administration

The State has issued COPs to finance construction or improvements of office buildings that are primarily leased to State agencies. The State's obligation to make lease payments and any other obligations of the State under the lease are subject to, and dependent upon, annual appropriations made by the State Legislature and annual allocations of such appropriations being made by the Department of Administration for such purpose. The Department of Administration agrees to use its best efforts to budget, obtain, allocate, and maintain sufficient appropriated monies to make lease payments. In the event any such appropriation and allocation is not made, the leases will terminate and there can be no assurance that the proceeds for the re-leasing or sale of the projects will be sufficient to pay principal and interest with respect to the then outstanding COPs. The scheduled payments of principal and interest with respect to the COPs are guaranteed under certificate insurance policies. The State's obligation to make lease payments does not constitute a debt or liability of the State within the meaning of any constitutional or statutory limitation. Neither the full faith and credit nor the general taxing power of the State is pledged to make payments of principal or interest due with respect to the COPs. Such payments will be made solely from amounts derived under the terms of the lease, including lease payments, and amounts from time to time on deposit under the terms of the declaration of trust.

2. School Facilities Board

In prior fiscal years, the SFB refinanced various COPs through advance-refunding arrangements. Under the terms of the refundings, sufficient assets to pay all principal, redemption premiums, if any, and interest on the refunded COPs have been placed in irrevocable trust accounts at commercial banks and invested in U.S. securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased COPs are not reflected in the accompanying financial statements. Refunded COPs for the SFB at June 30, 2007 totaled $311.130 million.

Business-Type Activities

3. University of Arizona

On April 17, 2007, the U of A issued Refunding COPs Series 2007A, 2007B, and 2007D (2007A-D) for $12.035 million, $50.150 million, and $42.895 million, respectively, dated April 1, 2007 at a net discount of $1.684 million. The 2007A-D COPs consist of $105.080 million of serial and term certificates with interest rates ranging from 3.50% to 4.50% and maturity dates ranging from 2009 to 2031. The 2007D COPs include three term certificates consisting of $7.440 million due June 1, 2024, $8.370 million due June 1, 2027, and $12.800 million due June 1, 2031, all with an interest rate of 4.00%. The 2007A-D Certificates maturing on or after June 1, 2018 are subject to optional redemption prior to maturity without premium. The 2007D Certificates maturing on June 1, 2024, June 1, 2027, and June 1, 2031 are subject to mandatory sinking fund redemption in part on June 1 of the years 2022 through 2031 without premium. There are also extraordinary redemption dates pursuant to the debt instruments.

The U of A realized net proceeds from the 2007A-D COPs of $104.241 million after payment of $1.300 million for issuance costs, underwriter discounts, and insurance. The U of A contributed $2.145 million toward the refunding. The net proceeds and U of A's contributed funds were used for the following:

- Refund in advance a portion of the outstanding principal on the COPs Series 2001A, 2001B, and 2002A totaling $59.195 million. The advance-refunding generated a combined net present value economic gain of $2.060 million (difference between the present values of the old debt and new debt service payments) for the U of A. The advance-refunding decreases the U of A's debt service by $1.548 million in year one, $39 thousand in year two, and $300 thousand in year three. In addition, annual debt service decreases by an average of $27 thousand in years four through ten and by an average of $4 thousand in years eleven through nineteen. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $3.315 million. This difference, reported in the accompanying financial statements as a deduction from long-term debt, is being amortized to interest expense through the year 2025 using the straight-line method. The refunded COPs Series 2001A, 2001B, and 2002A will be paid by investments held in an irrevocable trust with a combined fair value of $61.139 million. Accordingly, the trust account assets and liability for these defeased COPs are not included in the accompanying financial statements.
- Current-refund the variable rate COPs Series 2004B with an outstanding principal balance of $41.400 million. At the time of the refunding, the effective rate of the refunded 2004B variable rate COPs was 3.69% and the maximum annual interest rate could not exceed 12.00%. Depending on what the future changes might have been in the variable rates of the refunded 2004B COPs, the difference in debt service payments resulting from changes in variable interest rates compared to 2007D COPs' average fixed interest rate of 4.00% over the next 24 years is ($2.393 million) to $62.528 million. The difference between the present values of the old and new debt service payments results in a range of an economic loss of $107 thousand to an economic gain of $3.254 million. The current refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $608 thousand. This difference, reported in the accompanying financial statements as a deduction from long-term debt, is being amortized to interest expense through the year 2031 using the straight-line method.

In fiscal year 2003, the U of A refunded, in advance of maturity, a portion of outstanding COPs Series 2001B. At June 30, 2007, the outstanding principal for the COPs Series 2001B was $4.645 million, which will be paid by investments held in an irrevocable trust with a fair market value of $4.675 million. Accordingly, the trust account assets and liability for these defeased COPs are not included in the accompanying financial statements.

In fiscal year 2005, the U of A refunded, in advance of maturity, a portion of outstanding COPs Series 1999 and 2001A. At June 30, 2007, the total outstanding principal balance for the COPs Series 1999 and 2001A was $22.740 million, which will be paid by investments held in an irrevocable trust with a fair value of $23.563 million. Accordingly, the trust account assets and liability for these defeased COPs are not included in the accompanying financial statements.

In fiscal year 2006, the U of A refunded, in advance of maturity, a portion of outstanding COPs Series 1999A and 1999. At June 30, 2007, the total outstanding principal balance for the COPs Series 1999A and 1999 was $3.290 million, which will be paid by investments held in an irrevocable trust with a fair value of $3.346 million. Accordingly, the trust account assets and liability for these defeased COPs are not included in the accompanying financial statements.

4. Arizona State University

At June 30, 2007, the ASU has issued fixed rate COPs. The ASU's non-bonded debt consists of various issues of COPs that are generally callable at a prescribed date with interest payable semi-annually. Certain COPs of the ASU have been defeased through advance refundings by depositing sufficient U.S. Government securities to pay all future debt service in an irrevocable trust. Accordingly, the liabilities for these defeased COPs are not included in the accompanying financial statements. The principal amount of all such COPs outstanding at June 30, 2007 was $65.400 million.

In December 2006, the ASU issued $65.890 million of refunding COPs, with an average interest rate of 4.15% to refund a portion of the outstanding 2002 COPs totaling $65.400 million with an average interest rate of 4.75%. The net proceeds of $70.800 million, after the net addition of $4.900 million for premium, underwriting fees, and other issuance costs, were used to purchase U.S. Government securities which were deposited in an irrevocable trust in order to retire the 2014 through 2026 maturities of the 2002 COPs on July 1, 2012. The refunded debt is considered defeased and related liabilities are not included in the accompanying financial statements. The issuance of the refunding COPs at a lower interest rate than the rate for the refunded debt resulted in a $2.900 million reduction in future debt service payments, with an economic gain of $2.300 million based upon the present value savings.

Securities and cash restricted for COP debt service held by the trustee at June 30, 2007 totaled $14.200 million.

A summary of the COPs issued as of June 30, 2007 is as follows (expressed in thousands):

Project	Issue Date	Final Maturity Date	Original Amount Issued	Outstanding Balance	Interest Rates
Governmental Activities:					
Department of Administration:					
Refunding Certificates of 92A, 92C, & 1091	2001	2012	$ 57,930	$ 27,120	4.00 – 5.25
Health Lab/HRIS 2002A	2002	2023	63,270	48,970	4.00 – 5.50
Refunding Certificates of 92B	2003	2011	75,295	54,045	3.13 – 5.50
Refunding Certificates of 93B	2004	2012	16,725	11,580	3.00 – 5.00
1000 Bed Prison 2004B	2004	2019	31,965	28,510	3.00 – 5.25
School Facilities Board:					
New School Construction 2003A	2003	2014	372,730	143,840	2.75 – 5.00
New School Construction 2003B	2004	2015	194,610	104,475	2.25 – 5.25
New School Construction 2004A	2004	2019	47,160	41,595	2.00 – 5.00
New School Construction 2004B	2005	2017	190,040	121,910	3.50 – 5.25
New School Construction 2004C	2005	2020	47,585	45,195	3.00 – 5.00
Refunding Certificates of 2003A	2005	2018	201,125	200,390	2.50 – 5.00
Refunding Certificates of 2003B	2005	2019	80,055	79,355	2.50 – 5.00
Refunding Certificates of 2004B	2005	2020	53,045	52,880	2.50 – 5.00
Total Governmental Activities:			$ 1,431,535	$ 959,865	
Business-Type Activities:					
Arizona State University:					
Towers Project	1991	2011	$ 4,500	$ 1,500	6.89
Downtown Center – 1999A	1999	2025	5,620	4,780	5.75
Downtown Center – 1999B	1999	2025	5,165	4,575	8.00
2002 Certificates of Participation	2002	2027	103,800	27,760	4.75
2004 West Campus – Refunding	2004	2010	22,495	17,130	2.36
2004 Certificates of Participation	2005	2031	80,275	80,275	4.89
2005A Certificates of Participation	2005	2031	110,115	110,115	4.36
2006 Certificates of Participation	2006	2031	15,810	15,810	4.52
2006 Refunding Certificates of Participation	2007	2027	65,890	65,890	4.15
University of Arizona:					
Fixed Student Union A	1999	2020	21,607	3,777	5.13 – 5.30
Parking Garage/Residence Hall	1999	2009	18,635	345	5.00
Park Student Union/Ln Svcs/6th St Gar/TEP Bldg.	2001	2012	31,695	3,565	4.00 – 4.45
Gittings Bldg/Highland Infra/Life Sci.	2001	2014	21,425	2,185	4.75 – 5.00
Student Housing, Health Bldg., UA North	2002	2022	76,965	23,580	4.13 – 5.50
Meinel Bldg & Refund COPS 1994B	2002	2023	29,845	28,320	3.10 – 5.13
Refund COPS 1997 & Portion of Series 2001B	2003	2022	10,615	10,615	3.50 – 5.00
Med. Resh. Bldg./Biomed Sci./Tech. Infstr.	2004	2031	153,960	151,315	2.62 – 5.25
Chem.Bldg./Res.Life/Pkg.Garage/Rfnd. COPS 1994A	2004	2029	42,020	39,380	3.60 – 5.25
Refund COPS 1999A	2005	2024	12,660	12,660	4.00 – 5.00
Refund COPS 1999	2005	2024	14,825	14,825	5.00
Refund COPS 2001A	2005	2022	16,330	16,330	4.13 – 5.00
Refund COPS 1999, 1999A&B, 2000A, 2001A&B, 2002A&B, 2003A&B, 2004A	2006	2025	29,460	28,500	3.25 – 5.00
Refund COPS 1999A&B, 2000A, 2001A&B, 2002A&B, 2003A&B, 2004A	2006	2025	58,650	58,290	3.63 – 5.00
Biomed Rsch Collab Bldg. Project	2006	2031	18,240	18,240	4.00 – 5.00
Refund COPs 2001A&B, 2002A, 2004B	2007	2031	105,080	105,080	3.50 – 4.50
Northern Arizona University:					
2004 Certificates of Participation	2005	2030	37,585	37,585	2.50 – 5.00
2005 Certificates of Participation	2006	2030	40,255	40,255	3.00 – 5.00
2006 Certificates of Participation	2006	2030	12,445	12,445	4.00 – 4.50
Total Business-Type Activities:			$ 1,165,967	$ 935,127	
Total Certificates of Participation			$ 2,597,502	$ 1,894,992	

Principal and interest debt service requirements on COPs outstanding at June 30, 2007 are as follows (expressed in thousands):

	Annual Debt Service					
	Governmental Activities			Business-type Activities		
Fiscal Year	Total Principal	Total Interest	Total Amount Required	Total Principal	Total Interest	Total Amount Required
2008	$ 63,215	$ 45,202	$ 108,417	$ 31,470	$ 43,156	$ 74,626
2009	65,805	42,417	108,222	31,210	41,620	72,830
2010	68,580	39,425	108,005	32,315	40,288	72,603
2011	71,680	36,120	107,800	28,605	39,186	67,791
2012	75,265	32,530	107,795	34,802	38,433	73,235
2013-2017	434,070	101,741	535,811	203,379	165,293	368,672
2018-2022	178,975	10,724	189,699	257,846	109,945	367,791
2023-2027	2,275	58	2,333	186,540	52,468	239,008
2028-2032	-	-	-	128,960	12,662	141,622
Total	$ 959,865	$ 308,217	$ 1,268,082	$ 935,127	$ 543,051	$ 1,478,178

D. LEASES

1. Leases

The State has entered into capital lease agreements for the acquisition of buildings, telephone systems, copy machines, and other equipment. Capital lease assets and liabilities are reported on the government-wide Statement of Net Assets. A lease is reported as a capital lease if one or more of the following criteria are met:

- Title to or ownership of the asset is transferred to the State at the end of the lease.
- The lease contains a bargain purchase option.
- The lease term is equal to 75.00% or more of the useful life of the leased asset. (This criterion does not apply if the beginning lease term falls within the last 25.00% of the total useful life of the asset.)
- The present value of the minimum lease payments at the inception of the lease, excluding executory costs, equals at least 90.00% of the fair market value of the leased asset. (This criterion does not apply if the beginning lease term falls within the last 25.00% of the total useful life of the asset.)

The future minimum lease payments for long-term capital leases as of June 30, 2007 are summarized below (expressed in thousands):

	Annual Debt Service	
Fiscal Year	Governmental Activities	Business-type Activities
2008	$ 27,706	$ 14,171
2009	28,872	12,432
2010	27,874	11,573
2011	25,958	11,403
2012	25,636	11,172
2013-2017	115,466	50,865
2018-2022	103,142	48,397
2023-2027	96,536	49,490
2028-2032	4,620	50,799
2033-2037	-	19,662
2038-2042	-	2,967
2043-2047	-	1,784
Total minimum lease payments	455,810	284,715
Less: amount representing interest	(118,948)	(117,935)
Less: amount representing executory costs	(94,653)	-
Obligations under Capital Leases	$ 242,209	$ 166,780

2. Capital Assets Financed through Capital Leases and Certificates of Participation

The following table summarizes the historical costs of assets acquired under capital leases and COPs (expressed in thousands):

	Governmental Activities	Business-type Activities
Land	$ 6,513	$ 5,684
Construction in progress	-	-
Buildings	442,825	1,025,219
Infrastructure	-	53,762
Improvements other than buildings	3,653	-
Equipment	69,314	24,848
	522,305	1,109,513
Less: accumulated depreciation	(138,451)	(89,442)
Carrying Value	$ 383,854	$ 1,020,071

E. LITIGATION

The *Ladewig vs. Arizona Department of Revenue* and the *Kerr vs. Killian* lawsuits have been settled as of June 30, 2007, and therefore no liability is reported in the accompanying financial statements. The State paid these settlements from the General Fund.

F. COMPENSATED ABSENCES

Compensated absences are paid from various funds in the same proportion that those funds pay payroll costs. The compensated absence liability attributable to governmental activities will be liquidated primarily by the General Fund. During fiscal year 2007, the State paid for compensated absences as follows: 83.39% from the General Fund, 10.61% from other funds, and 6.00% from other major funds.

G. CHANGES IN LONG-TERM OBLIGATIONS

The following is a summary of changes in Long-Term Obligations (expressed in thousands):

	Balance July 1, 2006	Increases	Decreases	Reclassifications	Balance June 30, 2007	Due Within One Year	Due Thereafter
Governmental Activities:							
Long-term Debt:							
Revenue bonds	$ 2,106,700	$ 325,000	$ (102,860)	$ -	$ 2,328,840	$ 108,925	$ 2,219,915
Grant anticipation notes	325,430	-	(42,570)	-	282,860	36,565	246,295
Certificates of participation	1,020,810	-	(60,945)	-	959,865	63,215	896,650
Capital leases	129,808	123,721	(11,320)	-	242,209	12,746	229,463
Installment purchase contracts	6,815	9,264	(5,435)	-	10,644	4,324	6,320
Notes payable	-	3,309	-	-	3,309	3,309	-
Premiums and discounts on debt	219,958	26,201	(21,088)	-	225,071	21,649	203,422
Deferred amounts on refundings	(17,832)	-	3,566	-	(14,266)	(3,566)	(10,700)
Total Long-term Debt	3,791,689	487,495	(240,652)	-	4,038,532	247,167	3,791,365
Other Long-term Liabilities:							
Compensated absences	134,346	241,528	(224,289)	-	151,585	143,271	8,314
Ladewig vs. Arizona Department of Revenue Settlement	76,116	-	(76,116)	-	-	-	-
Kerr vs. Killian Settlement	15,000	-	(15,000)	-	-	-	-
Total Other Long-term Liabilities	225,462	241,528	(315,405)	-	151,585	143,271	8,314
Total Long-term Obligations	$ 4,017,151	$ 729,022	$ (556,056)	$ -	$ 4,190,117	$ 390,438	$ 3,799,679
Business-type Activities:							
Long-term Debt:							
Revenue bonds	$ 802,600	$ 149,530	$ (83,565)	$ -	$ 868,565	$ 47,865	$ 820,700
Certificates of participation	946,766	171,146	(182,785)	-	935,127	31,470	903,657
Capital leases	113,388	61,220	(6,474)	(1,354)	166,780	7,567	159,213
Installment purchase contracts	10,279	1,582	(2,317)	-	9,544	2,336	7,208
Notes payable	-	-	-	1,354	1,354	332	1,022
Premiums and discounts on debt	38,331	8,611	(7,360)	-	39,582	1,575	38,007
Deferred amounts on refundings	(21,606)	(10,088)	2,483	-	(29,211)	(1,892)	(27,319)
Total Long-term Debt	1,889,758	382,001	(280,018)	-	1,991,741	89,253	1,902,488
Other Long-term Liabilities:							
Compensated absences	62,835	71,998	(70,267)	-	64,566	9,998	54,568
Total Other Long-term Liabilities	62,835	71,998	(70,267)	-	64,566	9,998	54,568
Total Long-term Obligations	$ 1,952,593	$ 453,999	$ (350,285)	$ -	$ 2,056,307	$ 99,251	$ 1,957,056

The above long-term obligations relating to governmental activities include internal service funds. Amounts for capital leases and compensated absences differ from those in the Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets because $8.551 million of capital leases and $11.692 million of compensated absences are attributable to internal service funds. These amounts are included in the reconciliation as part of internal service fund net assets.

NOTE 7. INTERFUND TRANSACTIONS

INTERFUND BALANCES AND TRANSFERS

Interfund Receivables/Payables

Interfund balances as of June 30, 2007 are as follows (expressed in thousands):

	Due To						
Due From	General Fund	Transportation & Aviation Planning, Highway Maintenance & Safety Fund	Land Endowments Fund	Non-Major Governmental Funds	Non-Major Enterprise Funds	Internal Service Funds	Total Due To
General Fund	$ -	$ -	$ 367	$ 61,022	$ 5	$ 1,693	$ 63,087
Transportation & Aviation Planning, Highway Maintenance & Safety Fund	70,271	-	-	6,414	99,036	-	175,721
Land Endowments Fund	330	-	-	12,939	-	-	13,269
Non-Major Governmental Funds	9,091	-	-	1,499	-	466	11,056
Unemployment Compensation Fund	2	-	-	512	-	-	514
Lottery Fund	19,852	-	-	849	-	-	20,701
Non-Major Enterprise Funds	154,538	20,000	-	-	-	-	174,538
Internal Service Funds	794	1	-	3	-	126	924
Total Due From	$ 254,878	$ 20,001	$ 367	$ 83,238	$ 99,041	$ 2,285	$ 459,810

Interfund balances represent (1) amounts due to and from the internal service funds for goods and services rendered, and (2) cash transferred between funds for various interfund activities subsequent to the balance sheet date. The cash is recorded in the fund which initiated the transfer, and a corresponding liability is recorded. The receiving fund records an interfund receivable.

An interfund balance of $33.900 million between the General Fund and the Transportation & Aviation Planning, Highway Maintenance & Safety Fund is not due until fiscal year 2009.

Interfund Transfers

Transfers for the year ended June 30, 2007 are as follows (expressed in thousands):

	Transferred To							
Transferred From	General Fund	Transportation & Aviation Planning, Highway Maintenance & Safety Fund	Land Endowments Fund	Non-Major Governmental Funds	Universities Fund	Industrial Commission Special Fund	Non-Major Enterprise Funds	Total Transfers Out
General Fund	$ -	$ 246,591	$ 24	$ 70,861	$ 969,880	$ -	$ -	$ 1,287,356
Transportation & Aviation Planning, Highway Maintenance & Safety Fund	32,380	-	-	265,109	-	-	-	297,489
Land Endowments Fund	310	-	-	68,835	-	-	-	69,145
Non-Major Governmental Funds	90,461	1,600	-	30,684	-	8,000	98	130,843
Unemployment Compensation Fund	17	-	-	2,023	-	-	-	2,040
Lottery Fund	73,595	-	-	25,887	-	-	-	99,482
Internal Service Funds	2,197	-	-	31	-	-	-	2,228
Total Transfers In	$ 198,960	$ 248,191	$ 24	$ 463,430	$ 969,880	$ 8,000	$ 98	$ 1,888,583

Interfund transfers represent legally authorized non-exchange transfers of funds. These transfers include: (1) legislative appropriations from the General Fund, (2) other legislative transfers, (3) statutorily required transfers, (4) transfers related to the elimination of funds, and (5) transfers for debt service.

NOTE 8. ACCOUNTING CHANGES AND RESTATEMENTS

A. FUND FINANCIAL STATEMENTS

Net Assets have been restated as follows (expressed in thousands):

	Universities
Net Assets, as previously reported	$ 1,823,202
Change in accounting principle	(3,415)
Net Assets, as restated	$ 1,819,787

B. GOVERNMENT-WIDE STATEMENTS

Government-Wide Net Assets have been restated as follows (expressed in thousands):

	Business-type Activities of Primary Government
Net Assets, as previously reported	$ 2,745,844
Change in accounting principle	(3,415)
Net Assets, as restated	$ 2,742,429

The change in accounting principle in fiscal year 2007 was due to the NAU increasing its capitalization threshold for equipment from $2,500 to $5,000.

NOTE 9. FUND DEFICIT

A. INDUSTRIAL COMMISSION SPECIAL FUND

The Industrial Commission Special Fund deficit decreased in the amount of $71.123 million from $109.650 million to $38.527 million during fiscal year 2007. The main contributor to the Special Fund deficit continues to be the insolvent carrier liability, which was $264.710 million at June 30, 2007. The Special Fund is responsible for paying all current and future Arizona workers' compensation claims of insolvent insurance carriers and self-insured plans. Some of the claims expense will be recovered over a period of years as the Special Fund receives liquidation distributions from the insolvent companies. The 2007 calendar year assessments percentage for the State Compensation Fund and privately owned insurance companies that provide workers' compensation insurance is 2.50%, the largest amount currently authorized in Arizona law. In 2005, ARS §23-1081(B) was amended to permit a surplus in the Industrial Commission Administrative Fund to be transferred to the Special Fund when the Special Fund is not actuarially sound. During fiscal year 2007, $8.000 million was transferred from the Administrative Fund to the Special Fund.

B. HEALTHCARE GROUP

The Healthcare Group (HCG) incurred an operating loss of $20.701 million in 2007 and $6.137 million in 2006. As of June 30, 2007 the HCG had a fund deficit of $23.740 million. Additionally, current liabilities exceeded current assets by $5.838 million at June 30, 2007.

Two factors were the primary contributors to the decrease in net assets in 2007 and 2006. The most significant were the $17.458 million in HMO medical costs in excess of capitation paid (reconciliation costs) for the HMO model insurance contractors in 2007 and the $3.257 million PPO medical expense in excess of PPO premium revenue.

In response to the decreases in net assets and liquidity concerns described above, the HCG has implemented the following intensive initiatives:

- In March 2007, the HCG introduced a Point-of-Service (POS) plan and began "tiering" its hospital network. When a member requires inpatient or outpatient care from a hospital provider, their coinsurance payment will be dependent upon the level or "tier" of the hospital they choose. Hospitals will be classified into tiers based on the discounts that they offer to the HCG. Members will incur less out of pocket costs if they choose a Tier 1 hospital vs. a Tier 2 or Tier 3 hospital.

- Premium, deductible, and co-payment increases were implemented effective September 1, 2007 for new and renewing HMO members, for all health plan options and tiers, with a continued emphasis on increasing the actuarially determined premium rates for groups with one employee, in order to cover the costs of their historically disproportionate consumption of services.
- The HCG reviewed and tightened pharmacy formularies and Pharmacy Benefit Managers (PBMs) at one health plan and for the PPO to encourage use of generic and lower cost drugs.
- The HCG implemented strategies to mitigate member migration/fall out due to the premium increase, elimination of $0 deductible, and increases to co-payments and coinsurance.
- The HCG eliminated 49% of its staff as of February 2008 due to an enrollment freeze passed by the Legislature effective September 19, 2007 – through reengineering of job assignments and duties.
- Contract negotiations are underway with the health plans to address increasing medical loss ratios, improve medical management practices, and include incentives for medical management by the health plan.
- The HCG is conducting ongoing and concurrent review of premium revenue and plan benefit design for implementation.

Management represents that successful implementation of these operating improvements will improve the financial performance of the HCG for fiscal year 2008; however, they anticipate a continued operating deficit of $2.000 - $8.000 million.

There can be no assurance that these operating improvements will occur or will provide sufficient cash to fund operating expenses. Additionally, if there is an adverse change in enrollment and the premium increases are not sufficient to fund the reserves for past losses and future medical claims experience costs, then the HCG will be required to further scale back administrative expenditures to the level supported by actual enrollment and/or require a subsidy from the State General Fund to cover these operating costs. There can be no assurances that the Legislature will approve such a subsidy from the State General Fund.

Accordingly, the accompanying financial statements have been prepared assuming that the HCG will continue as a going concern. The matters discussed above raise substantial doubt about the HCG's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the HCG be unable to continue as a going concern.

C. RISK MANAGEMENT FUND

Risk Management Fund (RMF) - The RMF deficit of $299.841 million is primarily due to the RMF receiving annual funding only for expected paid claims (self-insured and excess insurance expenditures, legal and other claim related expenditures, and administrative expenditures), and not being funded for non-current accrued insurance losses. Accrued insurance losses of the RMF are not considered when determining funding for each fiscal year.

NOTE 10. JOINT VENTURE

The U of A is a participant in the Large Binocular Telescope Corporation (LBT). The LBT was formally incorporated as a nonprofit corporation in August 1992, pursuant to a Memorandum of Understanding, as amended, executed on February 24, 1989, between the U of A 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 the LBT are the U of A, Arcetri Research Corporation, Ohio State University, and the LBT Beteiligungsgesellschaft.

The U of A has committed resources equivalent to 25.00% of the LBT's construction costs and annual operating costs. As of June 30, 2007, the U of A has made cash contributions of $18.159 million toward the project's construction costs. The U of A's financial interest represents its future viewing/observation rights. Upon completion of construction, these rights will be divided among the participants in proportion to their contributions. According to the audited financial statements of the LBT for the year ended December 31, 2006, assets, liabilities, revenues, and expenses totaled $118.000 million, $3.000 million, $11.000 million, and $4.000 million, respectively.

The LBT's separate audited financial statements can be obtained from the University of Arizona Comptroller at the University of Arizona, Financial Services, P.O. Box 3310, Tucson, AZ 85722-3310.

NOTE 11. 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 Industrial Commission Special Fund provides payment of workers' compensation losses which are not covered by the State Compensation Fund, the Department of Administration – Risk Management Section, private insurance carriers, or self-insured employers. The workers' compensation claims paid by the Commission encompass losses against uninsured or underinsured employers and insolvent insurance carriers and would include payments for vocational rehabilitation, medical conditions incurred prior to 1973, apportionment claims for pre-existing industrial and non-industrial related physical impairments, and compensation for loss of earnings associated with the disability.

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

The management and payment of these losses is accomplished through the funding mechanism of the Risk Management Fund (internal service fund) and the Industrial Commission Special Fund (enterprise fund). As discussed in the above paragraph, an independent annual actuarial analysis is performed to evaluate the needed funding. The Risk Management Section will assess each agency an annual portion of the necessary funding for the Risk Management Fund based on their exposures and prior loss experience. Interest and dividend earnings of investments and assessments on gross premium revenues currently fund the Commission Special Fund. To provide funding for workers' compensation claims, the Commission may direct payment to the State Treasurer an amount not to exceed one and one-half percent of all premiums received by the State Compensation Fund, private carriers and self-insured plans during the immediately preceding calendar year. Beginning in calendar year 2004, this 1.50% assessment was levied under ARS §23-1065(A) because of a deficit net assets balance resulting from an increase in accrued insurance losses due to defunct insurance carriers.

AMI Risk Consultants, Inc. was retained to evaluate the medical and compensation related liabilities of the Special Fund as of June 30, 2007. The estimated loss reserve of $401.148 million is $9.095 million lower than the $410.243 million reserve estimate at June 30, 2006. The most significant category of change was the medical and compensation claims that decreased in the amount of $10.631 million from $98.386 million at June 30, 2006 to $87.755 million at June 30, 2007. The reserves were discounted at an assumed rate of three and one-half percent for the compensation claims and zero percent for the medical claims. For medical benefits, it was assumed that the inflation in medical costs will equal the investment return earned by the Special Fund on those reserves.

The total of all three assessments for the Industrial Commission Special Fund in 2007 is 2.50%. This includes the 1.50% assessment under ARS §23-1065(A), .50% assessment under ARS §23-966(D), based on the insolvent carrier losses, and .50% assessment under ARS §23-1065(F) based on the total apportionment liability. The Commission has filed pending proof of claim requests with ancillary receivers, liquidators holding deposits and surety bonds of several insolvent companies. Since the actual amount that will ultimately be received cannot be determined, the Commission will continue to recognize receipt of insolvent carrier deposits (no insurance settlement income) as revenue at the time received rather than recording a receivable.

Occasionally, the Risk Management Section agrees with claimants to purchase an annuity contract to settle 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. 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 have been no settlements that have exceeded insurance premium coverage in the last three years.

The following table presents the changes in claims liabilities balances (short- and long-term combined) during fiscal years ended June 30, 2006 and June 30, 2007 (expressed in thousands):

Fiscal Year	Beginning Balance	Current Year Claims and Changes in Estimates	Claims Payments	Ending Balance
Risk Management Fund:				
2006	$ 301,600	$ 135,364	$ 69,764	$ 367,200
2007	367,200	46,276	69,371	344,105
Industrial Commission Special Fund:				
2006, as restated	455,655	(30,570)	14,842	410,243
2007	410,243	15,684	24,779	401,148

B. LITIGATION

In *Roosevelt Elementary School District No. 66 vs. State of Arizona* and *Somerton Elementary School District No. 11 vs. State of Arizona*, the plaintiffs are seeking a declaration that Arizona's funding of the Building Renewal Fund for school district capital resources under ARS §15-2031 is unconstitutional. The actions were originally commenced in 1999 and 2002, but they were remanded by the Arizona Court of Appeals after its decision in *Roosevelt Elem. Sch. Dist. v. State of Arizona*, 205 Ariz. 594, 74 P.3d 258 (App. 2003). On remand, plaintiffs substituted some parties, leaving the plaintiff school districts as Globe Unified School District, Williams Unified School District, and Sierra Vista Unified School District, and discovery recommenced. In October, 2006, the court granted the State summary judgment, finding that the named school districts had failed to seek emergency funding under ARS §15-2022. The court indicated that if the districts proved subsequently that they had sought emergency funding and been rejected, and had exhausted all sources of State funding available to them for their facility needs, they might reinstate their claims. Plaintiff Globe Unified School District is no longer a party. The court later agreed to stay the judgment against plaintiffs through June 1, 2007, and plaintiffs successfully sought even further continuance on the inactive calendar. The State has recommenced discovery, having served written requests for production and interrogatories. The plaintiffs are not seeking damages. However, they are seeking a declaration that would require the State to provide additional funding for building maintenance and renewal needs. The plaintiffs are likely to argue that the Legislature was required to fund according to the Building Renewal Fund Formula, which was ultimately suspended by the Legislature. The formula-calculated amounts that were not funded for just the 1999-2000, 2001-2002, and 2002-2003 fiscal years amounted to almost $186.000 million. The potential outcome is uncertain at this time. If this case were to have an unfavorable outcome, it is possible that the State could incur losses in excess of $200.000 million.

In *Mayer vs. Winkelman*, the plaintiffs have filed an action in Maricopa County Superior Court seeking an accounting, declaratory relief, and damages for breach of trust. Damages are for the value of land disposed of by the State Land Department between 1929 and 1967 for approximately 600 rights of way that were issued to governmental entities without appraisal or auction, and without the payment of any compensation. In January 2007, the court granted motions to dismiss on the ground that the plaintiffs' claims were barred by laches. An appeal was filed and in May 2008, the Court of Appeals, Division II, reversed the trial court dismissal for laches, but determined that the Lassen case, which held that the State must be compensated in money for rights of way across State lands, did not apply retroactively. A petition for review will likely be filed in the Arizona Supreme Court. The State previously moved to dismiss on statute of limitations grounds and for lack of standing and justiciability, but the motion was denied, and on appeal the Court of Appeals rejected the State's arguments. If a petition for review is filed by the plaintiffs, the State will likely cross-petition on the State's arguments rejected by the Court of Appeals. The Court of Appeals determined that Lassen does not apply retroactively. Although the State may not agree with the framing of the analysis and the extent of the effect of the ruling, there is a greater probability that there will be some limitation on the application of the Lassen decision. With respect to the State's other arguments, the State will pursue those positions. The potential outcome is uncertain at this time. If this case were to have an unfavorable outcome, it is possible that the State would have to pay the Land Endowments Fund between $500.000 million and $1.0 billion.

In *Liquid Titan vs. Arizona Department of Weights and Measures, et al.*, the plaintiff alleges defamation against the Arizona Department of Weights and Measures (ADWM), the former director, and the current director. The complaint arises from a press release issued by the ADWM relating to fuel quality and record violations. The complaint has been served with discovery. The State has answered the complaint, provided Rule 26.1 disclosure, and has prepared a draft motion for summary judgment. The State's response is to maintain that there was a reasonable basis of belief of the Director in issuing the press release. The potential outcome is uncertain at this time. If this case were to have an unfavorable outcome, the State could incur losses ranging from $9.200 million to $15.000 million.

The State has a variety of claims pending against it that arose during the normal course of its activities. Management believes, based on advice of legal counsel, losses, if any, resulting from settlement of these claims will not have a material effect on the financial position of the State. All losses for any unsettled litigation or contingencies involving workers' compensation, medical malpractice, construction and design, highway operations, employment practices, criminal justice, fidelity and surety, environmental property damage, general liability, environmental liability, building and contracts, auto liability, or auto physical damage are determined on an actuarial basis and included in the Accrued Insurance Losses of the internal service funds and the Industrial Commission Special Fund.

C. ACCUMULATED 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. Because sick leave benefits do not vest with employees, a liability for sick leave is not accrued in the financial statements. State employees are eligible to receive payment for an accumulated sick leave balance of 500 hours or more with a maximum of 1,500 hours upon retirement directly from State service. The benefit value is calculated by taking the State employee's 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 25.00% for 500 hours to a maximum of 50.00% for 1,500 hours. The maximum benefit value is $30 thousand. 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 internal service fund and accounts for the retiree accumulated sick leave.

D. UNCLAIMED PROPERTY

The State of Arizona's Uniform Unclaimed Property Act requires deposit of certain unclaimed assets into a managed agency fund. ARS §44-313 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 ARS §46-731, unclaimed utility deposits are deposited in the Utility Assistance Fund to help low income 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. Under ARS §41-2407, monies from unclaimed victim restitution payments are deposited in the Victim Compensation and Assistance Fund for the purpose of establishing, maintaining, and supporting programs that compensate and assist victims of crime. The balance is to be deposited in the General Fund. For fiscal year 2007, $2.551 million was deposited in the Utility Assistance Fund, $40.973 million was deposited in the Housing Fund, $14.899 million was deposited in the Racing Fund, $1.250 million was deposited in the Victim Restitution Fund, and $11.704 million was deposited in the General Fund. A total of approximately $491.658 million has been remitted since inception of the fund. The State is also holding securities valued at $55.023 million, and mutual funds of $5.246 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 GASB 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, 2007, this amount, reported as Due to Others in the General Fund, is $125.369 million.

E. CONSTRUCTION COMMITMENTS

The ADOT had outstanding commitments under construction contracts of approximately $873.795 million at June 30, 2007.

F. ARIZONA STATE LOTTERY

Annuities are purchased for all prizes over $400 thousand for which winners will receive the jackpot in annual installments for The Pick on-line game. These annuities are purchased from qualifying insurance companies which have the highest ratings from among A.M. Best Company, Standard & Poor's, Moody's, Duff & Phelps, or Weiss. The Lottery remains contingently liable on all annuities. Aggregate future payments to prize winners on existing annuities totaled approximately $126.954 million at June 30, 2007. Approximately $97.439 million of the total aggregate future payments at June 30, 2007 relate to annuities purchased from five separate insurance companies, of which approximately $34.112 million relates to a single insurance company.

NOTE 12. 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 settlement money is intended to compensate the State for costs it has incurred in providing health and other services to its citizens that were necessitated by the use of tobacco products. The State expects to receive settlement payments through 2025.

The State recorded tobacco settlement revenue of $90.258 million and $93.353 million in the fund statements and the government-wide statements in fiscal year 2007, respectively. Future settlement payments are subject to several adjustments, but the amounts are not presently determinable. These adjustments include a volume adjustment, which could reflect any decreasing cigarette production under a formula that also takes into account increased operating income from sales. Other factors that might affect the amounts of future payments include ongoing and future litigation against the tobacco industry and the future financial health of the tobacco manufacturers. Because the net realizable value of the future settlement payments is not measurable and there is no obligation for the tobacco companies to make settlement payments until cigarettes are shipped, the State did not record a receivable for the future payments related to cigarette sales after June 30, 2007.

NOTE 13. PUBLIC-PRIVATE PARTNERSHIP

The state of Arizona has entered into a partnership agreement with Accenture. The purpose of this partnership is to fund the Department of Revenue's technology needs. The agreement stipulates that Accenture will be paid 85.00% of the new revenue generated from the system enhancements, even if this amount is insufficient to cover the total contract cost. Accordingly, Accenture had created a system that increases the State's efficiency in collecting tax revenues. As of June 30, 2007, the State has paid Accenture $127.195 million towards the $153.730 million contract cost. Included in the $153.730 million contract cost is capitalized interest charges of $7.000 million and application support charges of $37.877 million.

NOTE 14. CONDUIT DEBT

During the year ended June 30, 2007, the Greater Arizona Development Authority (GADA) issued $36.520 million Infrastructure Revenue Bonds, Series 2006B for public infrastructure projects in the communities of the Drexel Heights Fire District, the Maricopa Fire District, the City of Show Low, the City of Somerton, the Town of Quartzite, and the Apache Junction Fire District. During the year ended June 30, 2007, the GADA issued $40.145 million Infrastructure Revenue Bonds, Series 2007A for public infrastructure projects in the communities of the City of Apache Junction, the Town of Buckeye, the Northwest Fire District, the Town of Chino Valley, the Town of Eagar, the Town of Parker, the Town of Snowflake, the Chino Valley Fire District, the Golden Ranch Fire District, and the Mayer Fire District. The GADA's bond structure allows it to lower borrowing costs for Arizona's communities by issuing and selling bonds as AAA rated tax-exempt debt and by sharing financing costs among several borrowers. Eligible applicants include cities, towns, counties, Indian tribes, and certain special districts. Principal and interest are payable semiannually. Loans are secured by the Pledged Collateral Reserve Fund, a requirement that is calculated and deposited by the GADA from the GADA Fund and an Agreement Reserve Fund, both of which are held by the Trustee. An intercept mechanism of state-shared revenues for political subdivisions enhances the security of the GADA bonds.

In previous years, the State appropriated a total of $20.000 million to the GADA for the express purpose of securing bonds issued by the GADA. As of June 30, 2007, the remaining balance in the appropriations account was $17.771 million including interest earned. Although issued in the name of the GADA, loans funded through the GADA bonds are solely the obligation of the underlying borrowers and are documented by loan repayment agreements. Pursuant to ARS §41-1554.08, the GADA's bonds do not constitute nor create a general, special, or other obligation or other indebtedness of the State or any governmental unit within the meaning of any constitutional or statutory debt limitation. The bonds do not constitute a legal debt of the State and are not enforceable against the State. The only exposure to the State is related to the *restricted* net assets of $8.055 million in the Pledged Collateral Reserve Fund. The Series 2006B and 2007A bonds do not constitute a legal debt of the State and are not enforceable against the State. At June 30, 2007, the total outstanding face value of all bonds issued by the GADA was $304.930 million.

NOTE 15. SUBSEQUENT EVENTS

On November 1, 2006, the State entered into a lease purchase agreement with Arizona Wildlife Finance Corporation (AWFC), for the purpose of construction, occupancy, and ownership of an administrative facility and related parking facilities located in Phoenix, Arizona (the project). The State began occupying the building in November 2007. The first scheduled lease payment of $481 thousand will occur in fiscal year 2008. The lease is not a general obligation or indebtedness of the State. If the State Legislature fails to appropriate monies or there is a failure to renew for any subsequent fiscal period with respect to the project, or the Arizona Game and Fish Department fails to otherwise allocate available monies for any subsequent fiscal period with respect to the project, this lease shall terminate at the end of the then current fiscal period and the State shall be relieved of any subsequent obligation under this lease. The State shall have the right, during the lease term and upon 90 days prior written notice, to purchase the AWFC's right, title, and interest in the project. On November 1, 2006, AWFC transferred its leasehold interests to Wells Fargo Bank.

In July 2007, the NAU issued approximately $38.700 million of System Revenue Bonds for the purpose of constructing a new residence hall and renovation of the NAU dining hall on the mountain campus. These bonds are secured by a first lien on certain gross revenues and are on parity with the Series 2002 System Revenue Refunding Bonds, the Series 1997 System Revenue Bonds, the Series 2002 System Revenue Bonds, the Series 2003 System Revenue Bonds, the Series 2004 System Revenue and Refunding Bonds, the Series 2005 System Revenue Bonds, and the Series 2006 System Revenue and Refunding Bonds.

On September 21, 2007, the ADOT adopted a Master Resolution relating to Transportation Excise Tax Revenue Bonds (Maricopa County Regional Area Road Fund). Also on September 21, 2007, the ADOT adopted the First Supplemental Resolution authorizing the issuance of the first series of bonds under the Master Resolution in an amount not to exceed $370.000 million. On November 6, 2007, the ADOT priced $370.000 million in Transportation Excise Tax Revenue Bonds (Maricopa County Regional Area Road Fund) 2007 Series to pay for the costs of design, right-of-way purchase, or construction of certain freeways and other routes within Maricopa County, Arizona and to pay the costs of issuing the 2007 Series Bonds. The 2007 Series Bonds were issued as senior lien bonds and mature from July 1, 2008 through July 1, 2025. Net proceeds totaled $387.404 million (after receipt of $20.429 million reoffering premium and payment of $1.897 million in underwriting fees and costs of issuance). The bonds were rated AA+ and Aa2 by Standard & Poor's Ratings Services and Moody's Investors Service, respectively.

On October 3, 2007, the SFB issued $82.880 million of State School Trust Revenue Refunding Bonds, Series 2007, with interest rates ranging from 4.00% to 5.00%, and maturity dates ranging from 2015 to 2018. The Series 2007 Bonds will not be subject to redemption prior to their stated maturity dates. The Series 2007 Bonds are being issued to refund and redeem, in advance of maturity, a portion of the Series 2004A State School Trust Revenue Bonds with a total outstanding principal balance of $88.630 million and pay the costs of issuance of the 2007 Series Bonds. The SFB realized net proceeds of $86.547 million after receipt of $5.264 million original issuance premium and payment of $1.597 million for issuance costs. The net proceeds from the sale of the 2007 Series Bonds, together with $12.304 million of cash transferred from the Debt Service Reserve Fund, were deposited into a special trust account with a depository trustee and used to purchase U.S. government securities, the maturing principal and interest income on which is calculated to be sufficient to pay the principal and interest represented by the bonds being refunded to their respective redemption dates.

On January 1, 2008, the ADOT issued Grant Anticipation Notes Series 2008A (the Series 2008A GANs) for $68.000 million, with interest rates ranging from 4.00% to 5.00% and maturity dates ranging from 2012 to 2015. The Series 2008A GANs were issued at a premium. Approximately $71.766 million of the proceeds from the issuance of the Series 2008A GANs will be used to pay a portion of the construction costs of certain controlled-access highways within Maricopa County, Arizona to be constructed by the ADOT, and for which the Series 2008A Grant Agreement has been executed with the Federal Highway Administration. The balance of the proceeds will be used to pay the cost of issuing the Series 2008A GANs.

On January 15, 2008, the U of A issued System Revenue Bonds Series 2008A (the 2008A Bonds) for $43.105 million. The 2008A Bonds include $20.915 million of serial bonds with interest rates ranging from 4.00% to 5.00% and maturity dates ranging from 2008 to 2027. The 2008A Bonds also include three term bonds consisting of $5.420 million with an interest rate of 4.25% due June 1, 2030, $6.180 million with an interest rate of 5.00% due June 1, 2033, and $10.590 million with an interest rate of 4.50% due June 1, 2040. The 2008A Bonds maturing on or after June 1, 2019 are subject to optional redemption without premium. The term bonds referred to above are subject to mandatory sinking fund redemption without premium pursuant to the debt documents. The U of A realized net proceeds of $42.713 million, after receipt of an original issue premium of $1.349 million and payment of $1.741 million of underwriters' discount, bond issuance costs, and a termination payment on an interest rate management agreement. The net proceeds will be used to fund various building, equipment, and infrastructure renovation and renewal projects and to pay the costs of issuance.

On April 10, 2008, the U of A issued System Revenue Refunding Bonds Series 2008B (the 2008B Bonds) for $18.090 million. The 2008B Bonds include $18.090 million of serial bonds with interest rates ranging from 3.50% to 4.50% and maturity dates ranging from 2009 to 2018. The 2008B Bonds are not subject to redemption prior to their stated maturity. The U of A realized net proceeds of $18.397 million after receipt of an original issue premium of $489 thousand, and payment of underwriters' discount and bond issuance costs of $182 thousand. The net proceeds were used to refund, in advance of maturity, a $17.970 million principal portion of the Series 1998 System Revenue Bonds and pay the bond issuance costs. A portion of the net proceeds will be deposited into an irrevocable trust which will acquire government obligations, which, together with the interest earned, will be sufficient to pay all future debt service of the refunded bonds. However, should the monies and interest in the trust be insufficient to pay the refunded bonds' debt service payments, the U of A will remain liable for the debt service payments of the refunded bonds.

On April 30, 2008, the State, through US Bank, NA (US Bank), issued COPs Series 2008A for $238.990 million with interest rates ranging from 3.25% to 5.00% and maturity dates ranging from 2010 to 2028. The Series 2008A COPs maturing on or after September 1, 2018 are subject to optional redemption prior to maturity, without premium. The State realized net proceeds of $238.855 million after receipt of $11.847 million reoffering premium, deposit to US Bank's Interest Account of $9.205 million capitalized interest, and payment of $2.777 million of bond insurance, underwriter's discount, and issuance costs. Upon sale of the Series 2008A COPs, US Bank (the trustee bank) immediately withdrew $206.655 million from the Acquisition Fund and purchased the Lewis Prison Complex from the State. The remaining $32.200 million will remain in the US Bank's Acquisition Fund for the Arizona State Hospital Forensic Unit. The net proceeds from the sale of the Lewis Prison Complex and the remaining issuance proceeds are being used to finance the following: (i) an approximately 4,000 bed prison expansion within the State, (ii) wastewater and water renovations and improvements at prisons throughout the State, and (iii) a new forensic unit and additional infrastructure improvements at the Arizona State Hospital.

On May 6, 2008, the ADOT issued Highway Revenue Bonds Series 2008A (the Series 2008A Bonds) for $193.950 million, with interest rates ranging from 4.13% to 5.00% and maturity dates ranging from 2024 to 2034. The Series 2008A Bonds were issued at a premium. The Series 2008A Bonds are subject to redemption, prior to maturity, at the option of the ADOT, on or after July 1, 2018 without premium. Approximately $200.000 million of the proceeds from the issuance of the Series 2008A Bonds will be used to finance portions of the ADOT's Five-Year Capital Program and pay the costs of issuing the bonds.

NOTE 16. DISCRETELY PRESENTED COMPONENT UNIT DISCLOSURES

The accounting policies of the State's component units conform to U.S. GAAP applicable to governmental units adopted by the GASB, except for those component units affiliated with the State's Universities. Because the component units affiliated with the Universities are not governmental entities, they follow FASB statements for not-for-profit organizations for financial reporting purposes. Each component unit has a June 30 year-end with the exception of the Law College Association, which has a May 31 year-end.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Measurement Focus and Basis of Accounting

The State's component units and component units affiliated with the Universities are presented using the economic resources measurement focus and the accrual basis of accounting. The State's component units follow FASB Statements and Interpretations issued on or before November 30, 1989; Accounting Principles Board Opinions; and Accounting Research Bulletins, unless those pronouncements conflict with GASB pronouncements. The State has chosen the option not to follow FASB Statements and Interpretations issued after November 30, 1989, except for the UMC, which has elected to apply the provisions of all relevant pronouncements of the FASB, including those issued after November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements.

2. Net Assets

Component units affiliated with the Universities classify net assets, revenues, expenses, gains and losses based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the component units affiliated with the Universities and changes therein are classified and reported as follows:

- *Unrestricted net assets* include assets and contributions that are not restricted by donors or for which such restrictions have expired.

- *Temporarily restricted net assets* include contributions for which donor imposed restrictions have not been met (either by the passage of time or by actions of the Foundations), charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable for which the ultimate purpose of the proceeds is not permanently restricted. Donor-restricted contributions are classified as temporarily restricted if the restrictions are satisfied in the same reporting period in which the contributions are received, except for the Foundations associated with the ASU, which classify such contributions as unrestricted.

- *Permanently restricted net assets* include contributions, charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable which require by donor restriction that the corpus be invested in perpetuity and only the board-approved payout be made available for program operations in accordance with donor restrictions.

3. Cash and Cash Equivalents

Cash and cash equivalents includes monies held in certificates of deposit, overnight money market accounts, and money market funds. Cash and cash equivalents are stated at cost, which approximates fair value.

4. Investments

Investments are recorded in accordance with Statements of Financial Accounting Standards (SFAS) No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*. Under SFAS No. 124, entities are required to report investments in equity securities that have readily determinable fair values, and all investments in debt securities at fair value. Equities, fixed income, and mutual funds are stated at fair market value based on quoted market prices. Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the increases or decreases in net assets in the Statement of Activities.

5. Income Taxes

The Foundations qualify as tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code and, accordingly, there is no provision for income taxes in the accompanying financial statements, except for the Collegiate Golf Foundation and the ACFFC. In addition, they qualify for the charitable contribution deduction and have been classified as organizations that are not private foundations. Any income determined to be unrelated business taxable income would be taxable. The ACFFC and NACFFC are exempt from taxes under the provisions of Section 501(c)(4) of the Internal Revenue Code. The ACFFC does not qualify for the charitable contribution deduction.

6. Annuities Payable and Other Trust Liabilities

Annuities payable and other trust liabilities for the U of A Foundation are stated at the actuarially computed present value of future payments to the annuitants. The excess of the fair values of assets received (classified according to their nature in the Statement of Financial Position) pursuant to annuity agreements over the actuarially computed annuities payable (using market rates in effect on the contribution date) is recorded as contributions in the year received.

7. Contributions

Contributions are recorded in accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made.* Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction.

8. Net Assets Released from Restriction

Expenses are not incurred in the temporarily restricted or permanently restricted net asset categories. As the restrictions on these net assets are met, the assets are reclassified to unrestricted net assets. The total assets reclassified are reported as net assets released from restriction in the accompanying Statement of Activities.

9. Use of Estimates

The preparation of the Universities-affiliated component units' financial statements in conformity with U.S. GAAP required management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

B. DEPOSITS AND INVESTMENTS

1. Component Units

a. Deposits and Investment Policies

The investments of the WIFA are stated at fair value, except guaranteed investment contracts, which are stated at cost since they are non-participating contracts. The investments of the UMC are stated at fair value.

b. Custodial Credit Risk - Deposits

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the deposits or collateral securities may not be recovered from the outside party. The UMC does not have a formal policy regarding custodial credit risk for deposits. The UMC holds deposits in excess of FDIC limits. At June 30, 2007, uninsured, uncollateralized deposits included in cash and cash equivalents were approximately $18.800 million.

c. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The WIFA does not have a formal policy regarding interest rate risk. The following table presents the interest rate risk for the WIFA utilizing the segmented time distribution method as of June 30, 2007 (expressed in thousands):

		Investment Maturities (in years)			
Investment Type	**Fair Value**	**Less than 1**	**1-5**	**6-10**	**More than 10**
Commercial paper	$ 25,523	$ 25,523	$ -	$ -	$ -
Corporate asset backed securities	167	-	167	-	-
Corporate collateralized mortgage obligations	1,197	-	-	-	1,197
Corporate notes	14,444	-	14,444	-	-
Guaranteed investment contracts	80,896	-	13,577	67,319	-
Money market mutual funds	62,129	62,129	-	-	-
U.S. Agency securities	24,895	-	24,895	-	-
U.S. Agency mortgage backed securities	13,954	-	-	-	13,954
U.S. Treasury securities	4,302	-	4,302	-	-
Total	$ 227,507	$ 87,652	$ 57,385	$ 67,319	$ 15,151

The UMC's investment policy limits the portfolio duration related to debt securities to the Lehman Brothers Intermediate Government/Credit Index. This is an index based on all publicly issued intermediate government and corporate debt securities with average maturities of four to five years. The following table presents the estimated maturities of the UMC's investments, utilizing the segmented time distribution method as of June 30, 2007 (expressed in thousands):

		Investment Maturities (in years)			
Investment Type	**Fair Value**	**Less than 1**	**1-5**	**6-10**	**More than 10**
Alternative investments	$ 1,259	$ 1,259	$ -	$ -	$ -
Commercial paper	15,527	15,527	-	-	-
Corporate fixed income	20,094	-	20,094	-	-
Guaranteed investment contracts	4,399	-	-	-	4,399
Managed futures	25,967	25,967	-	-	-
Money market mutual funds	2,263	2,263	-	-	-
Structured notes	17,925	-	17,925	-	-
U.S. Treasury securities	107,484	-	107,484	-	-
Other	15,222	14,594	-	628	-
Total	$ 210,140	$ 59,610	$ 145,503	$ 628	$ 4,399

d. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the holder of the investment. The WIFA does not have a formal policy regarding credit risk. The following table presents the WIFA's investments which were rated by S & P's and/or an equivalent national rating organization. The ratings are presented using S & P's rating scale as of June 30, 2007 (expressed in thousands):

Investment Type	**Fair Value**	**AAA**	**AA**	**A**	**A1**	**Not Rated**
Commercial paper	$ 25,523	$ -	$ -	$ -	$ 25,523	$ -
Corporate securities	15,808	4,384	4,299	7,125	-	-
Guaranteed investment contracts	80,896	80,896	-	-	-	-
Money market mutual funds	62,129	-	-	-	-	62,129
U.S. Agency securities	38,849	37,520	-	-	1,329	-
Total	$ 223,205	$ 122,800	$ 4,299	$ 7,125	$ 26,852	$ 62,129

The UMC's investment policy establishes ranges which limit the level of investments held in domestic and international equities, fixed income securities, and alternative investment strategies. Investment in fixed income securities is limited to investment grade securities with a credit rating of BBB, or equivalent, or better. The portfolio of fixed income securities must maintain an average rating of A or better at all times. The following table presents the UMC's investments which were rated by S & P's and/or an equivalent national rating organization. The ratings are presented using S & P's rating scale as of June 30, 2007 (expressed in thousands):

Investment Type	**Fair Value**	**AAA**	**AA**	**A**	**Not Rated**
Alternative investments	$ 1,259	$ -	$ -	$ -	$ 1,259
Commercial paper	15,527	-	-	-	15,527
Corporate fixed income	20,094	11,600	-	-	8,494
Guaranteed investment contracts	4,399	-	-	-	4,399
Managed futures	25,967	-	-	-	25,967
Money market mutual funds	2,263	-	-	-	2,263
Structured notes	17,925	-	15,935	1,990	-
Other	15,222	-	-	-	15,222
Totals	$ 102,656	$ 11,600	$ 15,935	$ 1,990	$ 73,131

e. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The WIFA's investment policy contains no limitations on the amount that can be invested in any one issuer. As of June 30, 2007, an investment in Bayerische Landesbank (fair value of $40.586 million) was approximately 17.84% of the WIFA's total investments, an investment in AIG Matched Funding Corp. (fair value of $25.153 million) was approximately 11.06% of the WIFA's total investments, and an investment in Royal Bank of Canada (fair value $15.158 million) was approximately 6.66% of the WIFA's total investments.

f. Foreign Currency Risk

The UMC's investment policy permits it to invest a portion of its holdings in international equities and both international alternative and managed future investments. The UMC's current holdings in international securities totaled approximately $35.384 million or 32.64% of total investments. The following table summarizes the UMC's foreign currency risk as of June 30, 2007 (expressed in thousands):

Foreign Currency Risk by Investment Type at Fair Value
(Expressed in Thousands)

Currency	Fixed Income	Equities	Total
Australian Dollar	$ 10	$ 1,759	$ 1,769
Bermuda Dollar	-	595	595
Brazil Real	-	1,604	1,604
British Pound Sterling	12	4,666	4,678
Canadian Dollar	1	2,310	2,311
Cayman Islands Dollar	-	802	802
Chinese Yuan	-	1,370	1,370
Euro	3,326	9,748	13,074
Hong Kong Dollar	-	819	819
Japanese Yen	9	3,567	3,576
Mexican Peso	-	252	252
Norwegian Krone	-	280	280
Singapore Dollar	-	414	414
South African Rand	-	815	815
Swiss Franc	1	966	967
Thailand Baht	-	297	297
Other	3	1,758	1,761
Total	$ 3,362	$ 32,022	$ 35,384

2. Universities-Affiliated Component Units

a. Investment Summary

Investments of the Universities-affiliated component units include the following amounts at June 30, 2007. All investments are stated at fair value (expressed in thousands):

	ASU Foundation	ACFFC	U of A Foundation	NAU Foundation
Money market funds and cash equivalents	$ 26,653	$ 33,701	$ -	$ -
U.S. Government / Agency obligations and mutual funds	-	-	64,621	15,104
Domestic/international equity securities and mutual funds	355,939	-	163,032	38,109
Fixed income	95,290	-	18,027	-
Corporate bonds	-	-	-	5,206
REIT fund, real estate, and timber partnerships	-	-	18,876	343
Absolute return limited partnerships	-	-	83,766	-
Other investments	66,194	2,642	13,074	-
Total Investments	$ 544,076	$ 36,343	$ 361,396	$ 58,762

b. Endowment Trust Agreement

In March 2003, the ASU Foundation and the ASU entered into a trust agreement, appointing the ASU Foundation the trustee of selected ASU Endowments. In accordance with the trust agreement, the ASU Foundation receives a management fee for providing these services. Unrealized and realized gains and losses, and interest and dividends, if any, are added to or subtracted from the recorded value of the invested trust assets managed by the ASU Foundation. The invested trust assets are separate from the ASU Foundation investments, and a corresponding liability is presented for the fair value of the invested trust assets managed for the ASU. Not included in the ASU Foundation investments held in trust total is approximately $2.1 million in cash and cash equivalents held by the ASU Foundation on behalf of the ASU at fiscal year end.

C. PROGRAM LOANS

The WIFA has made loans to local governments and others in Arizona to finance various projects pursuant to the requirements of the Clean Water and Safe Drinking Water Acts. The loans are generally payable in semi-annual installments due January 1 and July 1 of each year, including interest. However, several loans are payable monthly or quarterly. Changes in the program loans during fiscal year 2007 are as follows (expressed in thousands):

	Beginning Balance	Increases	Decreases	Ending Balance
Clean Water Fund	$ 415,588	$ 75,196	$ (28,552)	$ 462,232
Drinking Water Fund	159,347	71,066	(10,270)	220,143
Total	$ 574,935	$ 146,262	$ (38,822)	$ 682,375

Repayment of these loans will be made from pledged property taxes, net revenues from the systems, transaction privilege taxes, or from special assessments. Most loans have a .30% to 4.00% annual administrative fee.

Some program loans require a monthly or quarterly payment into a debt service reserve to assure payments of the loans. The debt service reserve is a liability of the WIFA to the borrowers and interest on the reserve accrues to the borrowers.

D. PLEDGES RECEIVABLE

Unconditional promises to give are included in the accompanying financial statements as pledges receivable and revenue of the appropriate net asset category. Unconditional promises to give are recorded at their net realizable value using various yields as determined by the university foundations. The following summarizes unconditional promises as of June 30, 2007 (expressed in thousands):

	Universities-Affiliated Component Units Net Pledges Receivable
ASU Foundation	$ 109,570
Sun Angel Foundation	5,050
U of A Foundation	24,683
Law Association	29,516

E. DIRECT FINANCING LEASE AGREEMENT

1. ASU Foundation

The ASU Foundation leases a portion of the Fulton Center building (the ASU Foundation's headquarters) to the ASU under a direct financing lease. At the end of lease, the ASU Foundation and Affiliates will gift their portion of the building to the ASU and the ASU will receive title to the building. The ASU Foundation's net investment in this direct financing lease is $28.815 million.

2. ACFFC

Pursuant to a Sublease Agreement, Nanotechnology Research, LLC, a wholly-owned subsidiary of ACFFC, leases its interest in the Research Park to the ASU, which will pay rent at times and in amounts sufficient to pay all principal and interest (after utilization of amounts held in the Capitalized Interest Accounts) on the Series 2004 Bonds, as well as all fees and expenses related to the Series 2004 Bonds. The Sublease Agreement is a net lease, and Nanotechnology is entitled to receive the rents and all other sums payable pursuant to the Sublease Agreement free from all taxes, charges, fees, and expenses, all of which will be paid by the ASU. During fiscal year 2007, the ASU remitted payments totaling $945 thousand which is recorded as rental revenue in the accompanying financial statements. There were no payments received during 2006, as sufficient funds remained in the Capitalized Interest Accounts.

The Sublease Agreement commenced on April 7, 2004, and continued until June 30, 2005, with successive automatic annual renewals for the period July 1 through June 30 of each year without action on the part of Nanotechnology or the ASU, through the period ending March 31, 2034. The Sublease Agreement is subject to early termination by Nanotechnology or the ASU upon payment in full of the Series 2004 Bonds. Upon termination or expiration of the Sublease Agreement, Nanotechnology's interest in the premises, including all buildings and improvements on the leased premises, transfers to the ASU without further consideration. Therefore, the lease is classified as a direct financing capital lease.

Lease payments are based on a variable interest rate currently determined on a weekly basis. The average interest rate approximates 4.54% at June 30, 2007. Lease payments commence once the Capitalized Interest Accounts are fully utilized, which occurred in fiscal year 2007. ACFFC's net investment in this direct financing lease is $35.000 million.

In addition, there is a $12.000 million net investment in a direct financing lease by ACFFC for the Hassayampa Academic Village facility.

F. CAPITAL ASSETS

Capital asset activity for the UMC for the fiscal year ended June 30, 2007 was as follows (expressed in thousands):

	University Medical Center				
	Beginning Balance	Additions	Retirements	Adjustments & Reclassifications	Ending Balance
Non-depreciable capital assets:					
Land	$ 6,001	$ 145	$ (530)	$ 1	$ 5,617
Construction in progress	30,071	29,244	(115)	(34,637)	24,563
Total Non-depreciable Capital Assets	36,072	29,389	(645)	(34,636)	30,180
Depreciable capital assets:					
Buildings	150,719	3,698	(426)	30,857	184,848
Improvements other than buildings	790	-	-	1	791
Equipment	119,614	10,888	(647)	3,778	133,633
Total Depreciable Capital Assets	271,123	14,586	(1,073)	34,636	319,272
Less accumulated depreciation for:					
Buildings	(97,421)	(7,166)	427	-	(104,160)
Improvements other than buildings	(351)	(51)	54	-	(348)
Equipment	(87,564)	(13,040)	645	-	(99,959)
Total Accumulated Depreciation	(185,336)	(20,257)	1,126	-	(204,467)
Total Depreciable Capital Assets, Net	85,787	(5,671)	53	34,636	114,805
Total UMC Capital Assets, Net	$ 121,859	$ 23,718	$ (592)	$ -	$ 144,985

Capital assets for the Universities-affiliated component units for the fiscal year ended June 30, 2007 include the following (expressed in thousands):

	ASU Foundation	ACFFC	CRC	NACFFC
Buildings and improvements	$ 17,374	$ 186,110	$ 13,212	$ -
Furniture, fixtures, and equipment	4,947	38,488	622	-
Construction in progress	-	2,942	-	9,209
Other property and equipment	-	509	-	-
Total cost or donated value	22,321	228,049	13,834	9,209
Less: Accumulated Depreciation	(2,123)	(16,551)	(2,407)	-
Total Property and Equipment, Net	$ 20,198	$ 211,498	$ 11,427	$ 9,209

G. LONG-TERM OBLIGATIONS

1. Component Units

a. Water Infrastructure Finance Authority

The WIFA's 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.

In prior fiscal years, the WIFA refinanced various bond issues through advance-refunding arrangements. Under the terms of the refunding bond issues, sufficient assets to pay all principal, redemption premium, if any, 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. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased bonds are not reflected in the accompanying financial statements. The amount outstanding on the refunded bonds for the WIFA at June 30, 2007 totaled $91.215 million.

The $7.480 million deferred amount on retirement of bonds is being amortized over the lives of the defeased bonds on a straight-line basis. Annual amortization is $381 thousand and $173 thousand for the Clean Water Revolving and Drinking Water Revolving Funds, respectively. Amortization has been offset against interest expense.

Bond premiums are being amortized over the life of the bonds. The amortization for the year ended June 30, 2007 is $2.236 million. Further, bond issuance costs are amortized over the life of the bond and offset to interest expense. The amortization for the year ended June 30, 2007 is $239 thousand.

b. University Medical Center

The UMC is subject to certain financial covenants under the Master Trust Indenture (the Indenture), with which the UMC is in compliance as of and for the year ended June 30, 2007. In addition, the Indenture places certain restrictions on the incurrence of additional indebtedness and the sale or acquisition of property.

The UMC has established and maintains separate funds as a bond reserve fund on outstanding bonds payable. These funds, which totaled $20.042 million at June 30, 2007, are held by the trustee and are reflected as restricted investments held by trustee in the accompanying financial statements. These principally consist of guaranteed investment contracts, collateralized by U.S. Treasury Securities, and mortgage-backed government securities. The UMC is permitted to withdraw bond reserve funds totaling $4.399 million at June 30, 2007, related to the Series 1993 Bonds, as long as it is in compliance with its financial covenants as required by the bond indenture. The UMC is currently in compliance with these covenants; however, no funds have been withdrawn from the reserve fund since its inception.

The bonds or other obligations of the UMC do not constitute general obligations of the Arizona Board of Regents, the U of A, the State, or any political subdivision thereof.

c. Arizona Power Authority

In prior years, the APA defeased various issues of bonds by purchasing U.S. Government securities which were deposited in an irrevocable trust with an escrow agent to provide future debt service until the call dates. As a result, those 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.

Summary of Revenue Bonds

The following schedule summarizes revenue bonds outstanding at June 30, 2007 (expressed in thousands):

Revenue Bonds Outstanding	Dates Issued	Maturity Dates	Interest Rates	Outstanding Balance at June 30, 2007
Component Units:				
Water Infrastructure Finance Authority	1995-2006	2008-2027	2.00-6.10%	$ 557,450
University Medical Center	1993-2007	2008-2036	4.82-5.53%	232,966
Arizona Power Authority	2001-2004	2008-2018	5.00-5.25%	52,135

Principal and interest debt service payments on revenue bonds outstanding at June 30, 2007 are as follows (expressed in thousands):

	Annual Debt Service		
	Water Infrastructure Finance Authority		
Fiscal Year	Principal	Interest	Total
2008	$ 25,900	$ 26,172	$ 52,072
2009	27,420	25,007	52,427
2010	26,845	23,820	50,665
2011	28,020	22,579	50,599
2012	33,865	21,114	54,979
2013-2017	158,240	82,728	240,968
2018-2022	152,010	44,071	196,081
2023-2027	105,150	10,875	116,025
Total	$ 557,450	$ 256,366	$ 813,816

	Annual Debt Service		
	University Medical Center		
Fiscal Year	Principal	Interest	Total
2008	$ 3,835	$ 11,689	$ 15,524
2009	4,040	11,491	15,531
2010	4,145	11,289	15,434
2011	4,295	11,082	15,377
2012	4,515	10,863	15,378
2013-2017	26,280	50,617	76,897
2018-2022	33,630	43,265	76,895
2023-2027	42,915	33,974	76,889
2028-2032	54,780	22,116	76,896
2033-2037	54,531	6,983	61,514
Total	$ 232,966	$ 213,369	$ 446,335

	Annual Debt Service		
	Arizona Power Authority		
Fiscal Year	Principal	Interest	Total
2008	$ 3,120	$ 2,611	$ 5,731
2009	3,450	2,447	5,897
2010	3,815	2,265	6,080
2011	4,220	2,064	6,284
2012	4,585	1,844	6,429
2013-2017	26,725	5,284	32,009
2018-2022	6,220	163	6,383
Total	$ 52,135	$ 16,678	$ 68,813

d. Changes in Long-Term Obligations

The following is a summary of changes in long-term obligations for the component units (expressed in thousands):

	Balance July 1, 2006, as restated	Increases	Decreases	Balance June 30, 2007	Due Within One Year	Due Thereafter
Water Infrastructure Finance Authority:						
Long-term Debt:						
Revenue bonds	$ 582,560	$ -	$ (25,110)	$ 557,450	$ 25,900	$ 531,550
Revenue bond premium	37,479	-	(2,235)	35,244	-	35,244
Deferred amounts, net	(8,034)	-	554	(7,480)	-	(7,480)
Total Long-term Debt	612,005	-	(26,791)	585,214	25,900	559,314
Other Long-term Liabilities:						
Compensated absences	59	63	(76)	46	46	-
Total Other Long-term Liabilities	59	63	(76)	46	46	-
Total Long-term Obligations	$ 612,064	$ 63	$ (26,867)	$ 585,260	$ 25,946	$ 559,314
University Medical Center:						
Long-term Debt:						
Revenue bonds	$ 236,590	$ 200	$ (3,824)	$ 232,966	$ 3,835	$ 229,131
Revenue bond premium and discounts	(1,126)	-	(84)	(1,210)	-	(1,210)
Total Long-term Debt	235,464	200	(3,908)	231,756	3,835	227,921
Other Long-term Liabilities:						
Compensated absences	10,876	2,758	(1,788)	11,846	5,721	6,125
Other	3,014	-	(1,936)	1,078	-	1,078
Total Other Long-term Liabilities	13,890	2,758	(3,724)	12,924	5,721	7,203
Total Long-term Obligations	$ 249,354	$ 2,958	$ (7,632)	$ 244,680	$ 9,556	$ 235,124
Arizona Power Authority:						
Long-term Debt:						
Revenue bonds	$ 54,960	$ -	$ (2,825)	$ 52,135	$ 3,120	$ 49,015
Revenue bond premium and discounts	2,474	-	(359)	2,115	-	2,115
Deferred amounts, net	(1,688)	-	246	(1,442)	-	(1,442)
Total Long-term Debt	55,746	-	(2,938)	52,808	3,120	49,688
Other Long-term Liabilities:						
Compensated absences	68	59	(46)	81	81	-
Total Other Long-term Liabilities	68	59	(46)	81	81	-
Total Long-term Obligations	$ 55,814	$ 59	$ (2,984)	$ 52,889	$ 3,201	$ 49,688

2. Universities-Affiliated Component Units

A summary of bonds payable as of June 30, 2007 include the following (expressed in thousands):

	Final Maturity	Amount
ASU Foundation:		
Series 2004B Variable Rate Revenue Bonds	2022	$ 11,275
Series 2004A Variable Rate Revenue Bonds	2034	22,420
Series 2003 Lease Revenue Term Bonds	2034	16,625
Series 2003 Lease Revenue Term Bonds	2028	10,575
Series 2003 Lease Revenue Term Bonds	2023	20,400
Capital Lease	2011	2,800
ACFFC:		
Series 2005A Variable Rate Demand Revenue Bonds	2045	96,700
Series 2005B Variable Rate Demand Revenue Bonds	2045	48,345
Series 2005 Tax Exempt Bonds	2035	16,005
Series 2004 Variable Rate Demand Revenue Bonds	2030	51,605
Series 2004A Variable Rate Demand Lease Revenue Bonds	2034	20,175
Series 2004B Variable Rate Demand Lease Revenue Bonds	2034	14,825
Series 2003 Serial and Term Bonds	2035	13,355
Series 2002 Bonds	2018	28,185
Series 2000 Serial and Term Bonds	2032	10,445
Unamortized bond premium		1,060
NACFFC:		
Series 2005 Variable Rate Demand Revenue Bonds	2033	35,345
North Campus Lease Revenue Serial and Term Bonds	2036	12,400

Scheduled future maturities of Universities-affiliated component units' bonds payable are as follows (expressed in thousands):

Fiscal Year	ASU Foundation	ACFFC	NACFFC
2008	$ 1,020	$ 1,945	$ 355
2009	1,723	3,060	630
2010	1,799	5,410	695
2011	1,875	6,025	760
2012	1,988	6,615	830
Thereafter	75,690	277,645	44,475
Total	$ 84,095	$ 300,700	$ 47,745

H. ACCOUNTING CHANGES AND RESTATEMENTS

Net Assets have been restated as follows (expressed in thousands):

Restatement of Net Assets	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets, June 30, 2006, as previously reported	$ 72,668	$ 279,168	$ 596,752	$ 948,588
Restriction classification	-	35,200	(35,200)	-
Prior year correction of errors	401	-	1,907	2,308
Net assets, July 1, 2007, as restated	$ 73,069	$ 314,368	$ 563,459	$ 950,896

The accompanying financial information for fiscal year 2006 has been restated to correct an error in the financial statements for the ASU Research Park in the calculation of rents receivable resulting in a $303 thousand understatement of previously reported deferred rents receivable. Additionally, there is a restatement of net assets between permanently restricted and temporarily restricted net assets for the ASU Foundation. During fiscal year 2007, the net asset balances of the Foundation's endowment funds were analyzed and reviewed in conjunction with the ASU Foundation board approved investment and spending policies, generally accepted accounting principles, and applicable Arizona Revised Statutes. As part of that process, it was determined that the net appreciation on endowed gifts previously categorized as permanently restricted net assets were, in fact, temporarily restricted. Consequently, the permanently restricted net assets of approximately $35.200 million, as of June 30, 2006, have been reclassified as temporarily restricted net assets to reflect this correction. During fiscal year 2007, the net appreciation on endowed gifts is included in temporarily restricted net investment return.

During fiscal year 2007, management of the NAU Foundation determined that there was a beneficial interest in a perpetual trust that had not been recorded as an asset of the NAU Foundation. In addition, the NAU Foundation determined that the recording of revenue received from the Educational Broadcast System (EBS) licenses lease agreements was being recorded on a cash basis rather than an accrual basis. These errors resulted in a restatement of beginning net assets of $2.005 million.

I. RELATED PARTY TRANSACTIONS

The UMC and the U of A both provide and receive services from each other under various contracts. Payments to the U of A by the UMC include mission and program support, resident and intern salaries, utilities, ground maintenance, mailroom operations, and various administrative functions. Amounts paid to the U of A for these services were approximately $24.525 million for the year ended June 30, 2007.

The UMC has entered into contractual agreements with the U of A to provide support for the academic mission of the U of A. Charges to the U of A for such services and facilities provided by the UMC were approximately $9.700 million for the year ended June 30, 2007. These amounts are included in other operating revenue in the accompanying combined financial statements.

University Physicians Healthcare (UPH) is a not-for-profit corporation whose members are physicians employed by both the UPH and the U of A, and who practice at the UMC. The UMC has agreements with the UPH whereby the UPH provides physician and medical directorship and other services to the UMC. The UMC paid the UPH approximately $9.191 million for these services for the year ended June 30, 2007.

The UMC and the UPH share certain services and facilities within the hospital. Examples include information systems, medical records, and patient scheduling. The UPH reimburses the UMC for these services pursuant to written agreements between the parties. Charges to the UPH for the above services provided by the UMC were approximately $2.900 million for the year ended June 30, 2007. These amounts are included in other operating revenue in the accompanying combined financial statements.

The UMC also has an agreement to provide healthcare services to members of an AHCCCS health plan owned by the UPH called University Family Care (UFC). The UFC, an AHCCCS funded HMO, manages approximately 15,000 members. The UMC provides healthcare services to the UFC members in the normal course of business. The UMC operates under a contract with the UFC at rates that are substantially the same as rates received from other unaffiliated AHCCCS HMOs. Such rates are generally at or below the maximum rates established by the AHCCCS. Net patient service revenue includes $7.084 million in 2007 from this payer, based on negotiated rates.

Effective July 1, 2003, the UMC became the region's sole Level I Trauma Center and entered into an arrangement with the UPH to pay trauma physician call pay. Funding for the physician call pay was derived primarily from funds designated by the State to cover trauma readiness costs. During 2007, amounts incurred for services provided by UPH physicians totaled $3.064 million, and are included in professional services – medical, within the combined financial statements. As of June 30, 2007, accrued expenses include approximately $250 thousand payable to the UPH for these services.

J. SUBSEQUENT EVENTS

On April 15, 2008, the WIFA issued Water Quality Revenue Bonds Series 2008A (the Series 2008A Bonds) for $238.710 million, with interest rates ranging from 3.00% to 5.00% and maturity dates ranging from 2010 to 2029. The WIFA realized net proceeds of $240.000 million, after receipt of an original issue premium of $19.039 million, deposit to a reserve account of $16.205 million, and payment of $1.544 million of underwriters' discount and bond issuance costs. The net proceeds will be used to fund certain loans made by the WIFA to finance water quality projects, to reimburse the WIFA monies previously loaned for those purposes, and pay the costs of issuance.

On April 29, 2008, the NACFFC issued Refunding Bonds for $36.780 million. The net proceeds will be used to refund the Series 2005 Variable Rate Demand Revenue Bonds with an outstanding principal balance of $35.345 million and pay the costs of issuance.