This report was prepared by the
Statewide Accounting Division of the North Carolina Office of the State Controller.

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Special appreciation is given to the chief fiscal officers and the dedicated accounting personnel throughout the State. Their efforts to contribute accurate and timely financial data for their agencies, universities, community colleges, and institutions made this report possible.
MICHAEL F. EASLEY
Governor of North Carolina
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For the Fiscal Year Ended June 30, 2006

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# Comprehensive Annual Financial Report

*For the Fiscal Year Ended June 30, 2006*

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INTRODUCTORY SECTION
The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Citizens of North Carolina

It is our pleasure to furnish you with the 2006 Comprehensive Annual Financial Report (CAFR) of the State of North Carolina in compliance with G.S. 143B-426.39. This report has been prepared by the Office of the State Controller. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the state government and this office. To the best of our knowledge and belief, this financial report is complete and reliable in all material respects. We believe all disclosures necessary to enable you to gain an understanding of the State's financial activities have been included.

Although the State budgets and manages its financial affairs on the cash basis of accounting, G.S. 143-20.1 requires the Office of the State Controller to prepare a Comprehensive Annual Financial Report (CAFR) in accordance with generally accepted accounting principles (GAAP) in the United States of America. Except for exhibits and notes clearly labeled otherwise, this CAFR has been prepared in accordance with GAAP.

For the convenience of users we have divided the CAFR into three major sections, described as follows:

- The **introductory section** includes this transmittal letter and the State's organization chart, including a listing of principal State officials.
- The **financial section** includes management discussion and analysis (MD&A), the basic financial statements (government-wide financial statements, fund financial statements, and notes), other required supplementary information, the combining and individual fund financial statements, and schedules.
- The **statistical section** includes selected financial, non-financial and demographic information, much of which is presented on a ten-year basis, as well as required supplementary information.

Management of the government is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the State are protected from loss, theft or misuse and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

In compliance with State statute, an annual financial audit of the State financial reporting entity is completed each year by the North Carolina Office of the State Auditor. The Auditor’s examination was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, and the Auditor’s opinion has been included in this report. In addition, the State coordinates the Single Audit effort of all federal funds through the State Auditor.

This letter of transmittal is intended to complement MD&A and should be read in conjunction with it. The MD&A provides an overview of the State’s financial activities addressing both governmental and business-type activities reported in the government-wide financial statements. In addition, MD&A focuses on the State’s major funds: the General Fund, the Highway Fund, the Highway Trust Fund, the Unemployment Compensation Fund, the EPA Revolving Loan Fund and the N.C. State Lottery Fund. The MD&A can be found immediately following the Independent Auditor’s Report.
Profile of the State of North Carolina

North Carolina became the 12th state of the union in 1789. North Carolina is located on the Atlantic coast and is bordered by Georgia, South Carolina, Tennessee and Virginia. The State has a land area of approximately 50,000 square miles. The State’s estimated population is 8.8 million, making it the 11th most populated state in the nation. Sixty percent of the population is found in urban areas, while forty percent is found in rural areas. The North Carolina coastline is 301 miles, the greatest distance east to west is 543 miles, and the greatest distance north to south is 188 miles. The State’s elevation rises from sea level on the eastern coastline to 6,684 feet at Mount Mitchell in the Appalachian mountain range on our western border. There are 78,844 miles of roads, with Interstate 40 crossing North Carolina east to west, and Interstates 85 and 95 crossing the State north to south. North Carolina’s capital and central state government administration is located in Raleigh, in the central piedmont. Charlotte, Raleigh, Greensboro, Durham, and Winston-Salem are North Carolina’s largest cities and there are 100 counties.

Government

North Carolina’s state government consists of an executive branch, a legislative branch, and a judicial branch. The executive branch is headed by the Governor. The Governor, Lieutenant Governor, and eight other statewide elected officers form the Council of State. The State Constitution provides that, “A Secretary of State, an Auditor, a Treasurer, a Superintendent of Public Instruction, an Attorney General, a Commissioner of Agriculture, a Commissioner of Labor, and a Commissioner of Insurance shall be elected by the qualified voters of the State….”

The legislative power of the State is vested in the General Assembly, which consists of a Senate and a House of Representatives. The Senate is composed of 50 Senators, elected on a biennial basis. The House of Representatives is composed of 120 Representatives, elected on a biennial basis.

The Courts of the Judicial Branch are split into three divisions, the Appellate Division, the Superior Court Division, and the District Court Division. Judges are elected on a non-partisan basis.

State Reporting Entity and Its Services

The State of North Carolina entity as reported in the CAFR includes all fund types of the departments, agencies, boards, commissions and authorities governed and legally controlled by the State’s executive, legislative and judicial branches. In addition, the reporting entity includes legally separate component units for which the State is financially accountable. The component units are discretely presented in the government-wide financial statements. The State’s discretely presented major component units are the University of North Carolina System; the State’s community colleges; Golden LEAF, Inc., North Carolina Housing Finance Agency, and North Carolina State Education Assistance Authority. The criteria for inclusion in the reporting entity and its presentation are defined by the Governmental Accounting Standards Board (GASB) in its GASB Codification Section 2100. These criteria are described in Note 1 of the accompanying financial statements.

The State and its component units provide a broad range of services to its citizens, including k-12 public education; higher education; health and human services; economic development; environment and natural resources; public safety, corrections, and regulation; transportation; agriculture; and general government services. The costs of these services are reflected in detail and in summary in this report.
In addition to internal controls discussed previously, the State maintains budgetary controls. The objective of these budgetary controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the General Assembly. Activities of the General Fund and most departmental special revenue funds are included in the annual appropriated budget. The State Highway Fund and the Highway Trust Fund, the State's major special revenue funds, are primarily budgeted on a multi-year basis. Capital projects are funded and planned in accordance with the time it will take to complete the project. The level of budgetary control (that is, the level at which expenditures cannot legally exceed the appropriated amount) is exercised at both the departmental and university level, with allotment control exercised by the State Controller, and on the program line-item levels requiring certain approvals by the Director of the Budget. Legislative authorization of departmental expenditures appears in the State Appropriation Bill. The certified budget is the legal expenditure authority; however, the Office of State Budget and Management (OSBM) may approve executive changes to the legal budget as allowed by law. These changes result in the final budget presented in the required supplementary information.

**Economic Condition**

The consensus revenue estimate for the upcoming fiscal year represented a very cautious stance regarding the portion of the 2005-06 revenue surplus counted as recurring. In addition, the economy-based revenue estimates for the year reflect the view that the combination of a rise in short-term interest rates to 5.25% (9.25% for prime rate) and persistently high energy prices will eventually lead to a “mid-decade slowdown” similar to 1984-86 and 1995. The result is that baseline General Fund tax growth is expected to be only 3.3%. This forecast is in line with the downward adjustments made in many states after a second year of strong April income tax payments.

The projection of slower job growth and retail sales is pretty much the same outlook adopted a year ago during the 2005-06 budget discussions. The difference this year has to do with the loss of the underpinning from the robust real estate market. As the weakness in this sector continues to filter through the economy, we think the Federal Reserve will take note and leave short-term rates at the current 5.25% level. If the economic slowdown accelerates, the Federal Reserve may begin to lower rates during the second half of the fiscal year.

An additional reason the 2006-07 economic outlook is cautious is that even if we get the change in direction of the economy and timing right, it is hard to project the magnitude of the decline. There have been numerous occasions in the past when the Federal Reserve overshot the mark and a planned slowdown turned into an outright recession. This has been especially true when the rate hikes are accompanied by external shocks such as a military engagement or a gas price spike.

Barring any unforeseen international shocks we think that a full-scale recession can be avoided. One reason has to do with stable long-term interest rates. During a typical monetary tightening phase, long-term rates will follow hikes in short-term rates for the first few moves before stabilizing as investors become comfortable that an economic slowdown and lessening of inflation pressures is underway. During the current cycle long-term rates have remained stable throughout the Federal Reserve actions. Part of the reason for the stability has been the continued supply of funds from overseas. The other reason that a full-scale recession can be avoided has to do with the fact that the sharp increase in energy prices has not translated into a major increase in “core inflation” (prices increase excluding the volatile energy and food components).

Though the risks to the economic outlook increased, the cautionary stance taken on the nonrecurring portion of the 2005-06 revenue surplus means that the State is well-positioned for the economic slowdown that is starting to unfold.

— Economic analysis prepared by David Crotts, Economist
North Carolina General Assembly, Fiscal Research Division
October 31, 2006
Issues and Observations

BEACON HR/Payroll

The State's current core business systems have limited functionality. They rely on dated technology, do not communicate well with each other, are difficult to change for new operational requirements, and are hard to operate and maintain. Moreover, they do not provide information needed for management decision-making in today's business climate, and they are at risk of failure due to old age, withdrawal of vendor support, and being run by a workforce that is rapidly reaching retirement age.

BEACON is a statewide collaborative effort aimed at transforming the way we do business in North Carolina by modernizing and standardizing key business processes in human resources, payroll, budget management, taxation, data storage and accounting. With the implementation of SAP's Enterprise Resource Planning software solution, the goal of BEACON is to build a foundation for management flexibility, increased efficiency, improved access to information, and ultimately to enhance the quality of services provided to the citizens of North Carolina.

The Office of the State Controller, Information Technology Services, the Office of State Budget and Management, the Office of State Personnel, and the Department of Transportation are overseeing the implementation effort with the full support of Governor Easley and the General Assembly. BEACON will impact many of the systems and processes utilized by state agencies and universities. Representatives from nearly every agency in the State are participating in the design of the new infrastructure.

Session Law 2004-129 appropriated $2.7 million from the IT Fund to the Office of the State Controller in 2004 to begin implementation of the recommendations found in the Statewide Business Infrastructure Study. Of the $2.7 million, $1.8 million was allocated to the HR/Payroll Initiative and $900 thousand to the Enterprise Data Warehouse Initiative. The fiscal year 2005-06 appropriation for the HR/Payroll project was $20.875 million. Funding for fiscal year 2006-07 is $44.3 million. The overall estimated cost for the HR/Payroll project is $125.5 million. The HR/Payroll project is on budget and on schedule to be operational, with the first agency group brought on-line during January 2008, and the second agency group scheduled to be on-line during April 2008.

For additional information on Beacon, you can access the Beacon website through the Office of the State Controller website at http://www.ncosc.net.

Enterprise Data Warehouse Initiative

As part of the BEACON program, the BEACON Steering Committee has identified data warehousing and business intelligence as a key technology infrastructure necessary for delivering better citizen services and more effective operations of State government. In an environment where efficiency, accountability and transparency are paramount to the operations of each and every government entity, it is essential that data formerly housed in disparate “silos” be made available for agency and enterprise reporting and analysis.

The State of North Carolina has undertaken a number of initiatives recently to allow the State to better leverage its data assets. These activities have demonstrated the clear need for a more comprehensive approach to data warehousing and business intelligence in the State. From a statewide perspective, the highest value of business intelligence and data warehousing is realized when information is globally consistent and standardized, enabling decision-makers to query across agencies to perform forecasting, trending and data analysis. The Data Warehousing Needs Assessment revealed a number of immediate opportunities for implementation of data warehousing and business intelligence that would allow agencies to better leverage their data assets to provide improved operations or services.
On July 20, 2006, the General Assembly passed House Bill 914, the State Budget Act, to replace the Executive Budget Act. This new legislation is effective July 1, 2007, and will affect budget development and management by simplifying, reorganizing, updating the current budget statutes, and making changes to conform the statutes to the state constitutional provisions governing appropriations. The State Budget Act defines key budget aspects and increases the targeted balance of the General Fund savings reserve from 5 percent to 8 percent of prior year operating appropriations expenditures. The new legislation provides that agency budgets be classified in accordance with generally accepted accounting principles as interpreted by the State Controller.

As part of the implementation of the State Budget Act, several budgetary processes and the State’s budget code structure will be reviewed and revised as appropriate. Some revisions are expected to require adjustment to the State’s budgetary and accounting systems.

The 2006 General Assembly enacted legislation that established the Government Performance Audit Committee (GPAC). The GPAC will consist of 10 members:

(i) five members of the House of Representatives appointed by the Speaker of the House of Representatives, and
(ii) five members of the Senate appointed by the President Pro Tempore of the Senate.

The GPAC committee will contract for a performance audit of the executive branch of state government. The goals of the audit are to evaluate the efficiency and effectiveness of state government, and to identify specific improvements. According to legislation, the audit may examine entire departments, agencies, or institutions, or similar programs in several departments. The results of the audit will be reported on or before February 1, 2008. A Request for Proposal (RFP) will be issued for the government performance audit.

The committee’s examination of the efficiency and effectiveness of major management policies, practices, and functions, will include the following areas:

1. Planning, budgeting, and program evaluation policies and practices, including an analysis of the compliance of the executive branch with existing planning requirements, such as the Capital Improvement Planning Act, Article 1B of Chapter 143 of the General Statutes;
2. Personnel systems operations and management;
3. State purchasing operations and management;
4. Information technology and telecommunications systems policy, organization, and management; and
5. Review of duplications and related or overlapping services or activities for the purpose of coordinating and streamlining programs to achieve consistent and clear objectives.
Other Post-Employment Benefits: Retiree Healthcare


Beginning in fiscal year 2006-07, the actuarial data will be disclosed in the notes to the State’s CAFR, based on the disclosure requirements for a cost-sharing, multiple-employer plan, and will also be presented as required supplementary information (RSI). The unfunded actuarial liability will not be recorded as an accounting liability but will be disclosed in the notes to the financial statements, and as required supplementary information.

Aon Consulting completed an actuarial valuation of retiree health benefits earned as of December 31, 2005. Aon’s report was released on December 7, 2006 by the State Health Plan. The State retiree health care benefit is currently funded on a pay-as-you-go basis, with minimal additional accumulation of funds to pay the retiree health benefit. Based on the current funding method with limited accumulation of funds, the actuarial assumptions reflect a short-term discount rate of 4.25%.

The actuarial valuation using the unit credit method indicated an accrued liability of $23.925 billion for the retiree healthcare plan ($23.786 billion unfunded), with an annual required contribution (ARC) of $2.39 billion. This accrued liability and annual required contribution are most indicative of the administration and funding of the current retiree health benefit plan and will be incorporated into the required GASB disclosures in the 2007 CAFR.

Participating employers in the retiree health care benefit plan include the primary government state employees, local education agencies (LEAs), the University of North Carolina, community colleges, and several local governments. For the fiscal year ended June 30, 2006, North Carolina’s, retiree healthcare employer contributions equaling 3.8% of payroll were $476.8 million, representing an annual increase of 25.4%. Retiree healthcare premium costs paid to the State Health Plan were $411.8 million, representing an annual increase of 14.4%. Plan net assets of $171.1 million represent an increase of $68.37 million, or 66.5% from the prior year.
Debt Affordability

The 2004 General Assembly passed legislation creating the Debt Affordability Advisory Committee. The committee is charged, on an annual basis, with advising the Governor and the General Assembly of the estimated debt capacity of the State for the upcoming 10 fiscal years.

The Committee produces the Debt Affordability Study on an annual basis. The report was created to serve as a tool for sound debt management practices by the State of North Carolina. The report provides the Governor and the General Assembly with a basis for assessing the impact of future debt issuance on the State's fiscal position and enables informed decision-making regarding both financing proposals and capital spending priorities. The report also provides a methodology for measuring, monitoring and managing the State's debt levels. The concept of Debt Affordability is widely regarded as an essential management tool. The methodology used in the study to analyze the State's debt position incorporates historical and future trends in debt levels, peer group comparisons and provides recommendations within adopted guidelines. The study also provides recommendations regarding other debt management related policies considered desirable and consistent with the sound management of the State's debt. Such recommendations were developed by incorporating management practices consistent with those utilized by the most highly rated states.

Awards and Acknowledgements

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of North Carolina for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2005. This was the 12th consecutive year (1994 to 2005) the State has received the prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to the GFOA.

Acknowledgments

In conclusion, we believe this report provides useful data to all parties using it in evaluating the financial activity of the State of North Carolina. We in the Office of the State Controller express our appreciation to the financial officers throughout the State and to the Office of the State Auditor for their dedicated efforts in assisting us in the preparation of this report. Any questions concerning the information contained in this Comprehensive Annual Financial Report should be directed to the Office of the State Controller at (919) 981-5454.

Respectfully submitted,

Robert L. Powell
State Controller

December 11, 2006
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CERTIFICATE OF ACHIEVEMENT
Certificate of Achievement for Excellence in Financial Reporting
Presented to
State of North Carolina

For its Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2005

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

President
Executive Director
# ORGANIZATION OF NORTH CAROLINA STATE GOVERNMENT
INCLUDING PRINCIPAL STATE OFFICIALS

## EXECUTIVE BRANCH

<table>
<thead>
<tr>
<th>Office</th>
<th>Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governor</td>
<td>Michael F. Easley</td>
</tr>
<tr>
<td>Lieutenant Governor</td>
<td>Beverly E. Perdue</td>
</tr>
<tr>
<td>Secretary of State</td>
<td>Elaine F. Marshall</td>
</tr>
<tr>
<td>State Auditor</td>
<td>Leslie W. Merritt, Jr.</td>
</tr>
<tr>
<td>State Treasurer</td>
<td>Richard H. Moore</td>
</tr>
<tr>
<td>Superintendent of Public Instruction</td>
<td>Dr. June St. Clair Atkinson</td>
</tr>
<tr>
<td>Attorney General</td>
<td>Roy A. Cooper, Ill</td>
</tr>
<tr>
<td>Commissioner of Agriculture</td>
<td>Steven W. Troxler</td>
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<tr>
<td>Commissioner of Labor</td>
<td>Cherie K. Berry</td>
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<tr>
<td>Commissioner of Insurance</td>
<td>James E. Long</td>
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## Cabinet Secretaries — Appointed by the Governor

<table>
<thead>
<tr>
<th>Office</th>
<th>Name</th>
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<tbody>
<tr>
<td>Administration</td>
<td>W. Britt Cobb, Jr.</td>
</tr>
<tr>
<td>Correction</td>
<td>Theodis Beck</td>
</tr>
<tr>
<td>Crime Control and Public Safety</td>
<td>Bryan E. Beatty</td>
</tr>
<tr>
<td>Cultural Resources</td>
<td>Lisbeth C. Evans</td>
</tr>
<tr>
<td>Commerce</td>
<td>James T. Fain</td>
</tr>
<tr>
<td>Environment &amp; Natural Resources</td>
<td>William G. Ross, Jr.</td>
</tr>
<tr>
<td>Health and Human Services</td>
<td>Carmen Hooker Odom</td>
</tr>
<tr>
<td>Juvenile Justice and Delinquency Prevention</td>
<td>George L. Sweat</td>
</tr>
<tr>
<td>Revenue</td>
<td>E. Norris Tolson</td>
</tr>
<tr>
<td>Transportation</td>
<td>W. Lyndo Tippett</td>
</tr>
</tbody>
</table>

## Appointed by Governor, confirmed by Legislature

<table>
<thead>
<tr>
<th>Office</th>
<th>Name</th>
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<tbody>
<tr>
<td>Office of the State Controller</td>
<td>Robert L. Powell</td>
</tr>
<tr>
<td>State Board of Education</td>
<td>Howard N. Lee</td>
</tr>
<tr>
<td>State Board of Community Colleges</td>
<td>H. Martin Lancaster President</td>
</tr>
<tr>
<td>Appointed by University Board of Governors</td>
<td>Erskine B. Bowles President</td>
</tr>
</tbody>
</table>
LEGISLATIVE BRANCH

General Assembly

Senate

President
Lieutenant Governor
Beverly E. Perdue

Speaker
James B. Black

Majority Leader
Anthony E. Rand

Minority Leader
Philip E. Berger

House of Representatives

Speaker Pro Tempore
Richard T. Morgan

Majority Leader
Joe Hackney

Minority Leader
Joe L. Kiser

JUDICIAL BRANCH

North Carolina
Supreme Court

Chief Justice
Sarah Parker

Associate Justices
Edward Thomas Brady
Robert H. Edmunds, Jr.
Paul M. Newby
Mark D. Martin
Patricia Timmons-Goodson
George L. Wainwright, Jr.

Administrative
Office of the Courts
Judge Ralph A. Walker
Director

Component Units

University of North Carolina System
The Golden LEAF, Inc.
N.C. Housing Finance Agency
Community Colleges
State Education Assistance Authority
Other Component Units

State of North Carolina Web Page
http://www.ncgov.com
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FINANCIAL SECTION
STATE OF NORTH CAROLINA
Office of the State Auditor

INDEPENDENT AUDITOR'S REPORT

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of North Carolina, as of and for the year ended June 30, 2006, which collectively comprise the State's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State of North Carolina's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the North Carolina State Lottery Fund, which is both a major fund and 3 percent, 0 percent, and 15 percent, respectively, of the assets, net assets, and revenues of the business-type activities; the financial statements of the 401(K) Supplemental Retirement Income Plan, which represent 4 percent, 5 percent, and 4 percent, respectively, of the assets, net assets, and revenues of the aggregate remaining fund information; the North Carolina Housing Finance Agency, which represent 9 percent, 3 percent, and 3 percent, respectively, of the assets, net assets, and revenues of the aggregate discretely presented component units; the financial statements of the State Education Assistance Authority, which represent 15 percent, 4 percent, and 3 percent, respectively, of the assets, net assets, and revenues of the aggregate discretely presented component units; nor the financial statements of the University of North Carolina System – University of North Carolina Health Care System – Rex Healthcare, which represent 2 percent, 2 percent, and 4 percent, respectively, of the assets, net assets, and revenues of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for those entities, are based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the 401(K) Supplemental Retirement Income Plan, the State Education Assistance Authority, and the University of North Carolina System – University of North Carolina Health Care System – Rex Healthcare were not audited in accordance with Governmental Audit Standards. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of North Carolina.
North Carolina, as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 21 to the financial statements, the State changed its method of recognizing individual income taxes and implemented Governmental Accounting Standards Board Statement No. 46, *Net Assets Restricted by Enabling Legislation*, during the year ended June 30, 2006.

In accordance with *Government Auditing Standards*, we will also issue our report dated December 11, 2006 on our consideration of the State of North Carolina’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit. The report on internal control and on compliance and other matters will be published at a later date in the State of North Carolina’s *Single Audit Report*.

The Management’s Discussion and Analysis; Schedules of Funding Progress – All Defined Benefit Pension Trust Funds; Schedule of Contributions from the Employers and Other Contributing Entities – All Defined Benefit Pension Trust Funds; Schedule of Revenues, Expenditures and Changes in Unreserved Fund Balances – Budget and Actual – General Fund; and the Notes to Required Supplementary Information – Budgetary Reporting, as listed in the table of contents, are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State of North Carolina’s basic financial statements. The introductory section, the combining fund financial statements and schedules, and the statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining fund financial statements and schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Leslie W. Merritt, Jr.  CPA, CFP
State Auditor

December 11, 2006
MANAGEMENT'S DISCUSSION AND ANALYSIS
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

The following is a narrative overview and analysis of the State of North Carolina's (the State) financial performance for the fiscal year ended June 30, 2006. Please read it in conjunction with the transmittal letter at the front of this report and with the State's financial statements, which follow this section.

Financial Highlights

Government-wide Financial Statements:
— The State's total net assets increased by $2.78 billion or 10.7% as a result of this year's operations. Net assets of governmental activities increased by $2.46 billion, or 9.9% due, in part, to higher than expected growth in tax revenues. Net assets of business-type activities increased by $319 million, or 29.2% due to the strong financial results of the Unemployment Compensation Fund. At year-end, net assets of governmental activities and business-type activities totaled $27.43 billion and $1.41 billion, respectively.
— Component units reported net assets of $13.19 billion, an increase of $1.08 billion or 9.9% from the previous year. About half of the increase ($509 million) is due to the net increase in capital assets, net of related debt for the University of North Carolina System and community colleges. The capital asset additions were financed in part by state debt proceeds.

Fund Financial Statements:
— The fund balance of the General Fund more than doubled from $953.51 million at June 30, 2005 (as restated) to $1.93 billion at June 30, 2006. The increase is explained primarily by higher than expected growth in individual income, corporate income, and sales and use taxes. In fiscal year 2006, the State changed its methodology for reporting individual income taxes, which increased beginning fund balance by $1.04 billion.
— The fund balance of the Highway Fund increased from $383.3 million at June 30, 2005 to $568.79 million at June 30, 2006, an increase of 48.4%. The fund balance growth was attributable to increases in driver's license, vehicle registration and other fees and to increases in gasoline tax collections.
— The fund balance of the Highway Trust Fund decreased substantially from negative $15.36 million at June 30, 2005 to a negative $135 million at June 30, 2006. Higher construction inflation and non-appropriated spending for the Governor's "Moving Ahead" program and other legislative initiatives contributed to the larger fund deficit.
— The net assets of the Unemployment Compensation Fund almost doubled from $258.46 million at June 30, 2005 to $507.48 million at June 30, 2006. The significant increase is explained by the State's lower unemployment rate and by a 20% surcharge on unemployment contributions.
— The N.C. Education Lottery (Lottery) began selling instant game tickets in March 2006 and Powerball tickets in May 2006. As required by statute, the Lottery's net profit of $64.59 million was transferred to the Education Lottery Fund (nonmajor special revenue fund).

Capital Assets:
— The State's investment in capital assets (net of accumulated depreciation) was $29.21 billion, an increase of 5.9% from the previous fiscal year-end.
— This year's major capital asset additions were for highway construction ($1.4 billion), highway land improvements ($479 million) and the construction of correctional facilities ($34 million). Also, construction was completed on two 1,000 bed close custody prisons.

Long-term Debt:
— The State had long-term debt (bonds and similar debt payable) outstanding of $6.52 billion, an increase of less than 1% from the previous fiscal year-end. The long-term debt balance includes $709.1 million of special obligation (non-voted) debt issued for governmental activities.
— The State maintained its AAA bond rating with Standard and Poor's and Fitch. In August 2002, Moody's downgraded the State's credit rating for general obligation debt from "AAA" to "Aa1", representing the first time since 1960 that North Carolina had less than a "AAA" rating. In September 2004, Moody's upgraded the State's outlook from stable to positive.
OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is an introduction to the State’s basic financial statements, which comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains additional required supplementary information (General Fund budgetary schedule, pension funding progress and contributions) and other supplementary information (combining financial statements) in addition to the basic financial statements. These components are described below.

Government-wide Financial Statements

The Statement of Net Assets and the Statement of Activities are two financial statements that report information about the State, as a whole, and about its activities that should help answer this question: Is the State, as a whole, better off or worse off as a result of this year’s activities? These statements include all non-fiduciary assets and liabilities using the accrual basis of accounting. The current year’s revenues and expenses are taken into account regardless of when cash is received or paid. The Statement of Net Assets (page 50) presents all of the State’s assets and liabilities, with the difference between the two reported as “net assets”. Over time, increases and decreases in net assets measure whether the State’s financial position is improving or deteriorating.

The Statement of Activities (pages 52 and 53) presents information showing how the State’s net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying events giving rise to the change occur, regardless of the timing of related cash flows. Therefore, revenues and expenses are reported in these statements for some items that will only result in cash flows in future fiscal periods (e.g. uncollected taxes and earned but unused vacation leave).

Both statements report three activities:

Governmental Activities – Most of the State’s basic services are reported under this category. Taxes and intergovernmental revenues generally fund these services.

Business-type Activities – The State charges fees to customers to help it cover all or most of the cost of certain services it provides. The State’s Unemployment Compensation Fund, the N.C. State Lottery Fund, and the EPA Revolving Loan Fund are the predominant business-type activities.

Discretely Presented Component Units – Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. A description of the component units and an address for obtaining their separately issued financial statements can be found beginning on page 72. All component units are combined and displayed in a separate discrete column in the government-wide financial statements to emphasize their legal separateness from the State. In addition, financial statements for major component units are presented in the notes to the financial statements (pages 145 and 146).

Fund Financial Statements

The fund financial statements provide more detailed information about the State’s most significant funds (i.e., major funds) – not the State as a whole. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the State uses to keep track of specific sources of funding and spending for particular purposes. In addition to the major funds, page 170 begins the individual fund data for the non-major funds. The State's funds are divided into three categories, governmental, proprietary, and fiduciary, and they use different accounting approaches.

Governmental funds – Most of the State's basic services are reported in the governmental funds, which focus on how cash and other financial assets that can readily be converted to cash flow in and out (i.e., inflows and outflows of spendable resources) and the balances left at year-end that are available for spending (i.e., balances of spendable resources). Consequently, the governmental fund financial statements provide a detailed short-term view that helps users determine whether there are more or fewer financial resources that can be spent in the near future to finance the State's programs. The State prepares the governmental fund financial statements using the modified
accrual basis of accounting and a current financial resources measurement focus. Because this information does not encompass the additional long-term focus of the government-wide statements, a reconciliation schedule, which follows each of the governmental fund financial statements, explains the relationships (or differences) between them. Information is presented separately in the governmental fund financial statements for the General Fund, the Highway Fund, and the Highway Trust Fund, all of which are considered to be major funds. Data for all other governmental funds are combined into a single aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in this report.

Proprietary funds -- When the State charges customers for the services it provides, whether to outside customers or to other agencies within the State, these services are generally reported in proprietary funds. Proprietary funds (enterprise and internal service) utilize accrual accounting; the same method used by private sector businesses. Enterprise funds are used to report activities for which fees are charged to external users for goods and services. The Unemployment Compensation Fund, the N.C. State Lottery Fund, and the EPA Revolving Loan Fund are our most significant enterprise funds. Internal service funds are used to report activities that provide goods and services to the State's other programs and activities on a cost-reimbursement basis, such as the State Property Fire Insurance Fund, the Motor Fleet Management Fund, Computing Services Fund, and the State Telecommunications Services Fund. Because the State's internal service funds predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. Information is presented separately in the proprietary fund financial statements for the Unemployment Compensation Fund, the N.C. State Lottery Fund, and the EPA Revolving Loan Fund, all of which are considered to be major funds. Conversely, separately aggregated columns are presented for the nonmajor enterprise funds and the internal service funds. Individual fund data for the nonmajor enterprise funds and internal service funds is provided in the form of combining statements elsewhere in this report.

Fiduciary funds -- Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to the support the State's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. The State's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets. These funds include pension and other employee benefit trust funds, private-purpose trust funds, investment trust funds, and agency funds.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found beginning on page 70 of this report.

Required Supplementary Information

Following the basic financial statements and notes to the financial statements is Required Supplementary Information (RSI), which accompanies the basic financial statements. The RSI is mandated by the GASB and includes General Fund budgetary comparison schedules reconciling the statutory to the generally accepted accounting principles (GAAP) fund balances at fiscal year-end, and pension plan trend information related to funding progress and contributions.

Other Supplementary Information

Other supplementary information includes the introductory section, the combining financial statements for non-major governmental funds, non-major enterprise funds, internal service funds, fiduciary funds, and non-major discretely presented component units.
FINANCIAL ANALYSIS OF THE STATE AS A WHOLE

Over time, increases or decreases in net assets serve as a useful indicator of whether a government’s financial position is improving or deteriorating. The State’s combined net assets increased $2.78 billion or 10.7% over the course of this fiscal year’s operations. The net assets of the governmental activities increased $2.46 billion or 9.9% and business-type activities increased $319.02 million or 29.2%. The following table was derived from the government-wide Statement of Net Assets:

<table>
<thead>
<tr>
<th>Net Assets</th>
<th>June 30, 2006 and 2005</th>
<th>(dollars in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Governmental Activities</td>
<td>Business-type Activities</td>
</tr>
<tr>
<td>Current and other non-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>current assets</td>
<td>$15,171,216</td>
<td>$12,809,752</td>
</tr>
<tr>
<td>Capital assets, net</td>
<td>29,195,235</td>
<td>27,542,758</td>
</tr>
<tr>
<td>Total assets</td>
<td>44,350,451</td>
<td>40,352,510</td>
</tr>
<tr>
<td>Long-term liabilities</td>
<td>7,281,649</td>
<td>7,027,869</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>9,814,902</td>
<td>8,152,804</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>16,096,551</td>
<td>15,180,673</td>
</tr>
</tbody>
</table>

Net assets:

|            | | | | | | |
| Invested in capital assets, | | | | | | |
| net of related debt | 28,035,283 | 26,435,216 | 44,196 | 44,007 | 28,079,479 | 26,479,223 |
| Restricted | 890,602 | 1,314,397 | 1,286,477 | 970,615 | 2,177,079 | 2,265,012 |
| Unrestricted | (1,491,985) | (2,777,776) | 80,002 | 77,033 | (1,411,953) | (2,700,743) |
| Total net assets | $27,433,900 | $24,917,837 | $1,410,675 | $1,091,655 | $28,544,575 | $26,063,492 |

The largest component of the State’s net assets ($28.08 billion) reflects its investment in capital assets (land, buildings, machinery and equipment, state highway system, and other capital assets), less related debt still outstanding that was used to acquire or construct those assets. Restricted net assets are the next largest component ($2.18 billion). Net assets are restricted when constraints placed on their use are 1) externally imposed by creditors, grantors, contributors, or loans or regulations of other governments or 2) legally imposed through constitutional provisions. The remaining portion, unrestricted net assets, consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

The government-wide statement of net assets for governmental activities reflects a negative $1.49 billion unrestricted net asset balance. The State of North Carolina, like many other state and local governments, issues general obligation debt and distributes the proceeds to local governments and component units. The proceeds are used to construct new buildings and renovate and modernize existing buildings on the State's community college and university campuses, assist county governments in meeting their public school building capital needs, and to provide grants and loans to local governments for clean water and natural gas projects. Of the $6.45 billion of bonds and certificates of participation outstanding at June 30, 2006, $5.49 billion is attributable to debt issued as state aid to component units (universities and community colleges) and local governments. The balance sheets of component unit and local government recipients reflect ownership of the related constructed capital assets without the burden of recording the debt obligation. The policy of selling general obligation bonds and funneling the cash proceeds to non-primary government (non-State) entities has been in place for decades. However, by issuing such debt, the State is left to reflect significant liabilities on its statement of net assets (reflected in the unrestricted net asset component) without the benefit of recording the capital assets constructed or acquired with the proceeds from the debt issuances. Additionally, as of June 30, 2006, the State’s governmental activities have significant unfunded liabilities for compensated absences in the amount of $374.8 million (see Note 7 to the financial statements). These unfunded liabilities also contribute to the negative unrestricted net asset balance for governmental activities.
The following financial information was derived from the government-wide Statement of Activities and reflects how the State’s net assets changed during the fiscal year:

**Changes in Net Assets**

*For the Fiscal Years Ended June 30, 2006 and 2005*  
*(dollars in thousands)*

<table>
<thead>
<tr>
<th></th>
<th>Governmental Activities</th>
<th>Business-type Activities</th>
<th>Total Primary Government</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
<td>2006</td>
</tr>
<tr>
<td>Revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Program revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Charges for services</td>
<td>$1,988,001</td>
<td>$1,672,482</td>
<td>$1,402,464</td>
</tr>
<tr>
<td>Operating grants and contributions</td>
<td>11,509,844</td>
<td>11,380,864</td>
<td>54,985</td>
</tr>
<tr>
<td>Capital grants and contributions</td>
<td>914,090</td>
<td>1,011,451</td>
<td>258</td>
</tr>
<tr>
<td>General revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxes</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income tax</td>
<td>9,336,745</td>
<td>8,589,320</td>
<td>-</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>1,306,193</td>
<td>1,143,458</td>
<td>-</td>
</tr>
<tr>
<td>Sales and use tax</td>
<td>5,033,040</td>
<td>4,621,098</td>
<td>-</td>
</tr>
<tr>
<td>Gasoline tax</td>
<td>1,514,626</td>
<td>1,354,999</td>
<td>-</td>
</tr>
<tr>
<td>Franchise tax</td>
<td>628,029</td>
<td>913,033</td>
<td>-</td>
</tr>
<tr>
<td>Highway use tax</td>
<td>577,237</td>
<td>580,118</td>
<td>-</td>
</tr>
<tr>
<td>Insurance tax</td>
<td>442,297</td>
<td>442,228</td>
<td>-</td>
</tr>
<tr>
<td>Beverage tax</td>
<td>233,315</td>
<td>220,782</td>
<td>-</td>
</tr>
<tr>
<td>Inheritance tax</td>
<td>133,158</td>
<td>135,107</td>
<td>-</td>
</tr>
<tr>
<td>Other taxes</td>
<td>482,552</td>
<td>309,991</td>
<td>-</td>
</tr>
<tr>
<td>Tobacco settlement</td>
<td>140,969</td>
<td>143,588</td>
<td>-</td>
</tr>
<tr>
<td>Unrestricted investment earnings</td>
<td>123,170</td>
<td>76,864</td>
<td>-</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>37,248</td>
<td>53,488</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>34,384,514</strong></td>
<td><strong>32,325,569</strong></td>
<td><strong>1,466,811</strong></td>
</tr>
<tr>
<td>Expenses:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General government</td>
<td>1,039,813</td>
<td>914,471</td>
<td>-</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>8,215,445</td>
<td>7,698,357</td>
<td>-</td>
</tr>
<tr>
<td>Higher education</td>
<td>3,472,024</td>
<td>3,575,576</td>
<td>-</td>
</tr>
<tr>
<td>Health and human services</td>
<td>13,491,119</td>
<td>13,364,916</td>
<td>-</td>
</tr>
<tr>
<td>Economic development</td>
<td>647,434</td>
<td>621,247</td>
<td>-</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>676,049</td>
<td>567,252</td>
<td>-</td>
</tr>
<tr>
<td>Public safety, corrections and regulation</td>
<td>2,304,900</td>
<td>2,106,556</td>
<td>-</td>
</tr>
<tr>
<td>Transportation</td>
<td>1,791,865</td>
<td>1,795,585</td>
<td>-</td>
</tr>
<tr>
<td>Agriculture</td>
<td>112,467</td>
<td>80,787</td>
<td>-</td>
</tr>
<tr>
<td>Interest on long-term debt</td>
<td>264,287</td>
<td>249,433</td>
<td>-</td>
</tr>
<tr>
<td>Unemployment compensation</td>
<td>-</td>
<td>849,945</td>
<td>824,934</td>
</tr>
<tr>
<td>N.C. State Lottery</td>
<td>-</td>
<td>153,125</td>
<td>-</td>
</tr>
<tr>
<td>EPA Revolving Loan</td>
<td>-</td>
<td>11,414</td>
<td>7,170</td>
</tr>
<tr>
<td>Regulatory commissions</td>
<td>-</td>
<td>28,526</td>
<td>25,974</td>
</tr>
<tr>
<td>Insurance programs</td>
<td>-</td>
<td>10,051</td>
<td>13,535</td>
</tr>
<tr>
<td>North Carolina State Fair</td>
<td>-</td>
<td>10,497</td>
<td>10,759</td>
</tr>
<tr>
<td>Other business-type activities</td>
<td>-</td>
<td>10,255</td>
<td>9,753</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td><strong>32,006,103</strong></td>
<td><strong>30,974,280</strong></td>
<td><strong>1,079,813</strong></td>
</tr>
<tr>
<td>Increase (decrease) in net assets before contributions and transfers</td>
<td>2,389,411</td>
<td>1,351,289</td>
<td>386,988</td>
</tr>
<tr>
<td>Contributions to permanent funds</td>
<td>4,674</td>
<td>2,288</td>
<td>-</td>
</tr>
<tr>
<td>Transfers</td>
<td>67,978</td>
<td>(11,620)</td>
<td>(87,978)</td>
</tr>
<tr>
<td>Increase (decrease) in net assets</td>
<td>2,462,063</td>
<td>1,341,957</td>
<td>319,020</td>
</tr>
<tr>
<td>Net assets - beginning - restated</td>
<td>24,971,837</td>
<td>23,629,886</td>
<td>1,091,655</td>
</tr>
<tr>
<td>Net assets - ending</td>
<td><strong>27,433,900</strong></td>
<td><strong>24,971,837</strong></td>
<td><strong>1,410,675</strong></td>
</tr>
</tbody>
</table>

**Governmental Activities**

For fiscal year 2006, revenues outpaced expenses and when combined with transfers from the State’s business-type activities, an increase of $2.46 billion in net assets resulted for governmental activities. Total revenues increased 6.4% in fiscal year 2006 to $34.39 billion. The increase in revenues is attributable mostly to higher than expected growth in individual income, corporate income, and sales and use tax collections. Additionally, the legislature increased driver’s license, vehicle registration, and other motor vehicle fees, effective October 1, 2005. Gasoline tax collections were higher because of increases in the motor fuels tax rate. Gasoline taxes are indexed to the wholesale price of fuel, which increased rapidly because of Hurricane Katrina. Net transfers-in were much higher in fiscal year 2006 due to the new State lottery.
The following chart reflects the dollar change in the revenues by source of governmental activities between fiscal years 2005 and 2006:

**Dollar Change in Governmental Activities Revenues by Source Between Fiscal Years 2005 and 2006**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Charges for services</td>
<td>$316</td>
<td>$318</td>
<td>$2</td>
</tr>
<tr>
<td>Operating grants and contributions</td>
<td>$123</td>
<td>$125</td>
<td>$2</td>
</tr>
<tr>
<td>Capital grants and contributions</td>
<td>$767</td>
<td>$767</td>
<td>0</td>
</tr>
<tr>
<td>Individual income tax</td>
<td>$163</td>
<td>$160</td>
<td>($3)</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>$412</td>
<td>$412</td>
<td>0</td>
</tr>
<tr>
<td>Sales and use tax</td>
<td>$316</td>
<td>$318</td>
<td>$2</td>
</tr>
<tr>
<td>Gasoline tax</td>
<td>$160</td>
<td>$160</td>
<td>0</td>
</tr>
<tr>
<td>Other revenues</td>
<td>$226</td>
<td>$226</td>
<td>0</td>
</tr>
</tbody>
</table>

Total expenses increased by only 3.3% to $32.01 billion, primarily because of minimal growth (less than 1%) in the State's largest functional area, health and human services (HHS). For comparison, HHS expenses increased by 14.1% in 2005 and 10.5% in 2004.

Several factors helped to curb HHS spending. The General Assembly froze the reimbursement rates for most Medicaid service providers to the level authorized in fiscal year 2005. Moreover, the new Medicare Part D prescription drug plan resulted in lower costs to the State for drugs funded by Medicaid. Effective January 1, 2006, Medicare Part D, not Medicaid provides for outpatient prescription drug coverage to dual eligibles (i.e., individuals who are both Medicare and Medicaid eligible). However, because of a clawback provision, State's are required to pay most of their estimated savings to the Medicare program to help finance Part D coverage for low-income beneficiaries. State's are required to pay the federal government 90% of their estimated savings in calendar year 2006 and 75% in subsequent years. Another contributing factor to the slower HHS growth is related to the number of Disproportionate Share Hospital (DSH) payments. Due to the late approval of the State plan and new DSH methodology, only six months of DSH payments were made in fiscal year 2006. Additionally, expenses in prior years were much higher because of new initiatives to the Medicaid program. No new programs or initiatives were added to the Medicaid program for the 2006 fiscal year.

Despite enrollment increases, higher education expenses fell in fiscal year 2006 due to larger distributions of higher education bond proceeds in the prior year. Distributions of bond proceeds to colleges and universities were $725 million in fiscal year 2005 compared to $291 million this year. Primary and secondary education expenses continued to grow because of enrollment increases and teacher pay raises and bonuses.

The following chart reflects the dollar change in the functional expenses of governmental activities between fiscal years 2005 and 2006:
Dollar Change in Governmental Activities Functional Expenses Between Fiscal Years 2005 and 2006

The following chart depicts the total expenses and total program revenues of the State’s governmental functions. This format identifies the extent to which each governmental function is self-financing through fees and intergovernmental aid or draws from the general revenues of the State.

Expenses - Governmental Activities Fiscal Year Ended June 30, 2006

Business-type activities reflect an increase in net assets of $319.02 million or 29.2%, primarily because of the strong financial results of the Unemployment Compensation Fund. For fiscal year 2006, the Unemployment Compensation Fund had an operating income (excess of operating revenues over operating expenses) of $253 million. The Unemployment Compensation Fund and the EPA Revolving Loan Fund comprise 90.9% of the total net assets of business-type activities. The N.C. State Lottery Fund has no net assets since its net profits are distributed to the State’s governmental activities, as required by statute. A more detailed discussion of the State’s business-type enterprise activities is provided in the following section (see Enterprise Funds).
FINANCIAL ANALYSIS OF THE STATE’S FUNDS

The State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The focus of the State’s governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. As of the end of the fiscal year, the State’s governmental funds reported combined ending fund balances of $5.23 billion, a 28% increase from the prior fiscal year-end (as restated). The majority of the increase is related to the revenue growth in the General Fund and Highway Fund (major governmental funds) and to a $64.59 million transfer from the N.C. State Lottery Fund (major enterprise fund) to the Education Lottery Fund (nonmajor special revenue fund). The lottery funds are required by statute to be used for educational purposes. The major governmental funds are discussed individually below.

General Fund

The General Fund is the chief operating fund of the State. The fund balance of the General Fund more than doubled from $953.51 million at June 30, 2005 (as restated) to $1.93 billion at June 30, 2006. The increase is explained primarily by higher than expected growth in individual income, corporate income, and sales and use taxes. For individual income taxes, withholding tax collections grew by 8% and collections of estimated taxes and final payments grew by 21%. The withholding growth rate is similar to that of a pre-recession economy and reflects both job and wage growth. Increases in estimated and final payments also reflect changes in non-wage income. The growth in sales and use taxes occurred despite other offsetting factors, such as higher gas prices and a rise in short-term interest rates. The robust real estate market and improving job market helped to offset these negatives. Corporate income taxes, which are highly volatile over the business cycle, grew primarily because of improved demand for products and services.

For the fiscal year ended June 30, 2006, the State changed its methodology for reporting individual income taxes, which increased beginning fund balance by $1.04 billion (see Note 21). A more detailed analysis of the General Fund is provided in the budgetary highlights section below.

2005-06 General Fund Budgetary Highlights

The enacted General Fund budget was founded upon an overall nominal economic (real growth plus inflation) growth rate of 4.8% for 2005-06. The appropriated budget included provisions that were designed to increase General Fund revenues. The most significant revenue adjustment was the continuation of two temporary tax increases that were scheduled to expire in 2003. In 2001, the General Assembly temporarily raised the State sales tax rate by a half-cent to 4.5% and the highest individual income tax rate from 7.75% to 8.25%. The 2005-06 budget continued the State sales tax rate at 4.5% and the 8.25% income tax bracket. In addition, the General Assembly approved tax changes to comply with the Streamlined Sales Tax Agreement by equalizing rates of telecommunications, satellite television, candy, and funeral services. North Carolina has now satisfied the terms of the agreement. The budget also included a 25 cents per pack increase in the cigarette tax effective September 1, 2005. The following table summarizes the 2006 revenue enhancements (dollars in millions).

Revenue Enhancements – 2006 Fiscal Year

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maintain State sales tax at 4.5%</td>
<td>$417.1</td>
</tr>
<tr>
<td>Maintain top income tax rate at 8.25%</td>
<td>39.8</td>
</tr>
<tr>
<td>Change tobacco tax rate</td>
<td>118.8</td>
</tr>
<tr>
<td>Change sales, use, and excise taxes</td>
<td>54.9</td>
</tr>
<tr>
<td>Other changes</td>
<td>(7.4)</td>
</tr>
<tr>
<td><strong>Total 2006 enhancements</strong></td>
<td><strong>$623.2</strong></td>
</tr>
</tbody>
</table>
The majority of funding increases for 2006 were for education, human services, and employee benefit programs. The budget provided full funding for enrollment increases in the public schools ($135 million), the University of North Carolina System ($74.2 million), and the community college system ($7.8 million). In addition, the budget included disadvantaged student supplemental funding ($22.3 million) and low wealth funds ($20 million) to enhance public school instructional programs and student achievement throughout the State. Funds were also provided to support at-risk children. These funds include an additional 3,200 slots for the Governor’s More-at-Four Program ($16.6 million), which prepares at-risk four-year-old children for success in school. It also provided funds for ABC teacher bonuses earned in the 2004-05 school year ($100 million).

The budget provided $360 million in 2005-06 to support employee benefit programs. Specifically, it contained a 2.25% recurring compensation increase for all staff on the teacher salary schedule, a 2% or $850 flat amount (whichever is greater) for other state employees, as well as an additional 2% increase for community college faculty and professional staff. In addition, the State Health Plan received funds to cover increased employee health care premiums ($108.6 million). Finally, the budget included $25 million to continue repayment of funds withheld from the Retirement System in 2000-01 due to the budget crisis.

State funding for the Medicaid Program totaled $2.3 billion in 2005-06 and the total Medicaid budget was $8.8 billion. The General Assembly reduced General Fund appropriations for the Medicaid Program by $118.8 million in fiscal year 2005-06. The most significant reduction resulted from freezing Medicaid rates for most Medicaid service providers ($62.5 million). Other reductions include improved utilization management of in-home personal care services, increased recipient co-payments, and further implementation of drug utilization management. The General Assembly also clarified that counties are responsible for paying 15% of the federal Medicare Part D clawback payments under the Medicare Modernization Act of 2004.

General Fund Budget Variances

The original General Fund budget, including state appropriations and appropriations supported by departmental receipts, serves as a starting point or plan for the Governor to execute the General Fund budget pursuant to the powers granted by the Executive Budget Act. At the state level in North Carolina, it is not unusual for the budget to change during the fiscal year in relation to budget adjustments made to accommodate departmental receipts. The General Fund budget supported by state appropriation, is a subset of the General Fund financial schedule presented in the CAFR as required supplementary information. The current CAFR schedule reflects all spending required to support the State's General Fund activities and the funding to support those activities, including state tax and nontax revenues, federal revenues, student tuition, and other fees, licenses, and fines.

Under current state budget management practice, particularly related to departmental federal receipts, primary emphasis is placed on comparisons of the final authorized budget and actual spending.

At the state level, budgetary cuts related to state appropriations are implemented by decreasing allowable actual expenditures, as opposed to decreasing the state appropriation through a formal legislative process. The Governor and state agencies maintain legal authority to spend the dollars originally appropriated to them; however, in recent years the actual spending has been limited by the collection of tax and nontax revenue. In extremely rare cases, the General Assembly has held special sessions to formally amend the state appropriation budget.

The portion of the original budget comprising departmental receipts is not intended to be the sole controlling point to manage the State's General Fund budget. The final budget includes amendments for departmental receipts collected during the fiscal year as allowed by law. General Fund departmental receipts are typically authorized for expenditure within the activity that generated the receipt. Historically, final estimated receipts have varied significantly from the original estimate at the beginning of the fiscal year. State agencies by law must spend departmental receipts prior to spending tax and nontax supported appropriations. If departmental receipts are higher than expected, appropriated dollars may go unspent and be re-appropriated in a subsequent fiscal year.
Variances – Original and Final Budget

In general, the variances between original and final budget are attributable to the timing and length of the budget preparation process. The original budget for the 2005-06 fiscal year was prepared approximately 18 months prior to the final budget existing at June 30, 2006. The final budget reflects all budget revisions made throughout the fiscal year to adjust for known facts. Furthermore, it cannot be assumed that each agency accurately prepares their budget. Consequently, when the original budget is compared to the final budget, it would be expected that significant variances can occur.

The federal funds budget variance between original and final budget was $1.4 billion. The Department of Public Instruction (DPI) was the primary contributor to the variance, which occurred because of gross understatements of the original federal budget during the continuation budget process. DPI was in the midst of a department-wide reorganization in which the federal funds budget was to be allocated among several different divisions upon completion of the reorganization. As a result, DPI made a one time decision to not estimate its federal funds for fiscal year 2005-06, but to wait until the actual federal fund budget awards were posted by fiscal year 2005-06 budget revisions during the fiscal year.

The budget increase for intra-governmental transactions revenue is primarily attributable to the following: $198.9 million of statewide encumbrance carry forward amounts from fiscal year 2004-2005 and $143 million of Department of Health and Human Services (DHHS) Medicaid Disproportionate Share. None of these amounts were included in the original budget.

The budget increase for contributions, gifts, and grants of $498.3 million is attributable primarily to DHHS’s budgeting of state match throughout the fiscal year, as opposed to including a reasonable original budget estimate. The budget increase for Universities of $237.2 million is attributed to underestimated tuition amounts and the budgeting of fiscal year 2004-05 carry-forward amounts.

For expenditures, the variances between the original budget and final budget are related to the corresponding revenue budget variances. As revenue budget accounts are increased, a corresponding increase occurs in the expenditure budget accounts. In addition to those increases, agency expenditure budgets were also increased by the allocation of statewide reserves, such as the legislative salary increase, hospitalization, retirement, and salary adjustment.

Variances - Final Budget and Actual Results

Actual revenues collected exceeded final budget for several reasons. First, the revenue forecast was on the conservative side of “most likely”. Secondly, this forecast was prepared months prior to the beginning of the fiscal year and as the time period between a fiscal year and forecast preparation increases, forecasted amounts become less accurate. Finally, the economy performed much better than anticipated. Strong employment and income growth fueled individual income and sales tax collections that exceeded expectations. In addition, corporate collections continued to surge due to strong corporate profits and improvement in the business climate.

Departmental federal funds actually received by agencies were $1.32 billion less than the final budget. The three agencies primarily responsible for this variance were DPI ($813.1 million), DHHS ($348 million), and the Department of Crime Control and Public Safety ($117.7 million). Actual federal draw downs are reflective of the actual expenditures of these federal funds. Therefore, if qualifying costs are not incurred by an agency, the actual drawdown of federal funds could be significantly less than what has been budgeted. This was the situation in fiscal year 2005-06.

For expenditures, the variances between final budget and actual expenditures for primary and secondary education, health and human services, and public safety, corrections, and regulation occurred because actual departmental revenues were less than the budgeted revenues; therefore, expenditures that depended on the receipt of these funds could not be made.
Highway Fund

The Highway Fund dates back to 1921, which is when the N.C. General Assembly first imposed the gasoline tax. It accounts for most of the activities of the North Carolina Department of Transportation (DOT), including the maintenance and construction of the State's primary and secondary road systems, the State Highway Patrol, the Division of Motor Vehicles (DMV), and transit and rail. The primary revenue sources of the Highway Fund are federal funds, three-fourths of gasoline taxes, vehicle registration fees, and driver's license fees.

The fund balance of the Highway Fund increased from $383.3 million at June 30, 2005 to $568.79 million at June 30, 2006, an increase of 48.4%. Total revenues increased by $125.71 million or 4.7% primarily because of increases in gasoline taxes and fees, licenses, and fines. The legislature increased motor vehicle license and registrations fees effective October 1, 2005. These fees include driver's license, vehicle registration, and other fees collected by DMV. Gasoline tax collections rose due to the June 2005 rate increase from 26.6 to 27.1 cents per gallon and a second increase in January 2006 from 27.1 to 29.9 cents per gallon. Gasoline taxes are indexed to the wholesale price of fuel over a six-month period, which increased rapidly following Hurricane Katrina.

Total expenditures decreased by $79.46 million or 3.1%. This was due to a decrease in costs due to natural disasters compared to the previous fiscal year. In 2005, several major storms affected the western part of the state resulting in significant damage to the road network. DOT also implemented efficiency in cash management initiatives to counteract cash constraints due to escalating inflation. This approach was implemented to offset the effects of construction cost inflationary factors that have averaged 13.5% over the last several years compared to an historical rate of 3.5%. Transfers-in decreased from $222.16 million in 2005 to $85.91 million in 2006. Prior to 2002, State match for federal aid projects resulted from interfund transfers from the Highway Trust Fund to the Highway Fund. Due to legislative changes and improved accounting software, the state match is allocated directly from the Highway Trust Fund, eliminating the need for the transfers. The remaining transfer is for projects that were funded prior to this change. As these projects are completed, the transfer balance will continue to decrease.

In September 2004, the State Board of Transportation approved a new long-range plan that prioritizes transportation investment for the next 25 years. The Statewide Transportation Plan provides a blueprint for greater investment in maintenance, preservation, and modernization of the State’s existing highway system as well as other transportation options such as rail and public transportation. The share of transportation dollars spent on new highway projects will drop from 45% to 26%. The highway needs of the State's growing population will be accommodated in part by maintaining and upgrading existing roads and by increasing anti-congestion measures such as synchronized traffic signals.

The centerpiece of the plan is the Recommended Investment Scenario (Scenario), which outlines priorities from the estimated $57 billion, in today's dollars, expected to be available over the next 25 years for transportation investment. Based on the Scenario, the DOT will be able to meet an additional 10% of its maintenance and preservation needs and nearly 25% more modernization infrastructure needs. Additionally, the scenario proposes increasing DOT’s investment in other transportation modes. The plan also identifies $122 billion in total transportation needs and states that DOT will only be able to meet one half of the State’s 25-year transportation needs at its current funding levels, regardless of how DOT’s resources are allocated. Implementation of the Scenario will be gradual.

Highway Trust Fund

Legislation creating the Highway Trust Fund was passed by the General Assembly in 1989. It was established to provide a dedicated funding mechanism to meet highway construction needs in North Carolina. The Highway Trust Fund also provides extra money for the State's municipalities to adequately maintain their streets and it pays the debt service on the State's general obligation bonds issued for highway purposes.
The principal revenue sources of the Highway Trust Fund are highway use taxes, one-fourth of gasoline taxes, and various title and registration fees. The enabling legislation also specifies that a designated amount will be transferred each year to the General Fund (see Note 9 to the financial statements). The amounts transferred to the General Fund for fiscal years 2006 and 2005 were $252.55 million and $243.77 million, respectively. The amount to be transferred for fiscal year 2007 was reduced to $55 million. The General Assembly enacted legislation during the 2005-06 Session that repealed the requirement for the General Fund to repay the $125 million (plus interest) advanced from the Highway Trust Fund during the 2002-03 fiscal year. In the prior fiscal year, this advance was reclassified to a transfer to the General Fund.

The fund balance of the Highway Trust Fund decreased substantially from negative $15.36 million at June 30, 2005 to negative $135 million at June 30, 2006. Higher construction inflation and non-appropriated spending for the Governor’s “Moving Ahead” (see below) and Senate Bill 1005 initiatives, contributed to the larger fund deficit. Total revenues increased by $45.2 million or 4.4%, primarily because of increases in gasoline taxes and fees, licenses, and fines. The legislature increased motor vehicle license and registrations fees effective October 1, 2005. These fees include title fees and other fees collected by DMV. However, due to a decrease in new vehicle sales, title fee collections were only marginally above the previous year and Highway Use Tax collections were down slightly from the previous year.

Total expenditures decreased by $188.81 million or 17.9%. This was due to a decrease in contract lettings and lower expenditures in the “Moving Ahead” and Senate Bill 1005 initiatives. The Department implemented efficiency in cash management initiatives as discussed previously.

In 2003, the General Assembly passed the Governor’s “Moving Ahead” transportation initiative to allow, over two years, the use of $630 million of Highway Trust Fund cash balances for highway preservation, modernization, and maintenance. More than 2,200 miles of highway are being improved through “Moving Ahead”. Additionally, it allows $70 million for public transit, rail, ferry, bicycle, and pedestrian projects. Through June 30, 2006, “Moving Ahead” cumulative expenditures totaled $420.3 million of the $700 million authorized. For fiscal years 2006 and 2005, transportation expenditures increased by $132.5 million and $227.6 million, respectively, due to the advancement of the Governor’s “Moving Ahead” transportation initiative.

Bond proceeds of $300 million were realized in September 2004 to reimburse the Highway Trust Fund for expenditures of prior years. These bonds constitute the remaining portion of the $950 million highway bond authorization approved by the voters in November 1996 (Note: $250 million of such bonds were issued in 1997 and $400 million were issued in 2003). For fiscal year 2006, the debt service on highway bonds was $93.56 million.

The State’s enterprise funds or business-type activities provide the same type of information found in the government-wide financial statements, but in more detail. The major enterprise funds are discussed individually below.

Unemployment Compensation Fund

The net assets of the Unemployment Compensation Fund (Trust Fund) increased by $249.02 million during the current fiscal year, an increase of 96.4% from the prior fiscal year-end. The net asset growth is explained by the State’s lower unemployment rate and by a 20% surcharge on unemployment contributions that became effective January 1, 2005, as required by state statute. The surcharge, which is projected to remain in effect through December 31, 2007, was assessed because of the fund’s low reserves in prior years. The State’s unemployment rate fell from 5.4 percent in June 2005 to 4.6 percent in June 2006. The State had a net gain of 93,400 jobs, or 2.4% increase, from July 2005 to July 2006, ranking among the national leaders and outpacing the Southeast region. Declines in manufacturing jobs have been more than offset by growth in professional and business services, financial activities, and education and health services. The State unemployment rate is down significantly from the recession peak in 2002, when the rate climbed to 6.7%.
The operating income (excess of operating revenues over operating expenses) was $253 million this year versus $244.32 million in 2005. Unemployment benefit expenses increased 3.7% in fiscal year 2006 to $848.36 million. At June 30, 2006, the short-term debt balance was zero compared to $113.69 million in 2005. To ensure timely payment of unemployment benefits, the State received repayable advances from its Federal Unemployment Account and issued tax anticipation notes (see attached Note 6 to the financial statements). The State was able to save millions of dollars in interest payments by selling tax anticipation notes instead of borrowing exclusively from the federal government. The use of short-term borrowing came about in early 2002 when an economic downturn caused the State to pay significantly more in unemployment benefits than it received in employer contributions. In May 2006, the State officially ended borrowing from the federal government to cover unemployment benefits. The Trust Fund’s cash and cash equivalent balances now equal $166.7 million.

The 2003 Session of the General Assembly enacted legislation to help preserve the integrity of the unemployment insurance tax system. Session Law 2003-67 (Senate Bill 326) clarifies that an employer cannot avoid an undesirable unemployment insurance rate by shifting employees to a newly created company with a more desirable tax rate. This practice is known as State unemployment tax avoidance or “SUTA dumping.”

**N.C. State Lottery Fund**

The N.C. Education Lottery (Lottery) began operations after July 1, 2005; therefore, the financial statements reflect only a partial fiscal year. The first full time, permanent employee was hired in December 2005. The first lottery tickets (instant game) began selling on March 30, 2006, and the first on-line (Powerball) game tickets began selling on May 30, 2006. The Lottery borrowed $4 million from the State Treasurer in February 2006 to help cover start-up expenses before the start of ticket sales. These funds were repaid to the State Treasurer in April 2006.

Since the 2005-06 fiscal year was a start-up period, the Lottery had a significant number of initial purchases and one time expenditures for temporary employees. Temporary employees were needed to help operate the Lottery until the permanent staff was hired. As required by the enabling legislation, the Lottery's net profit of $64.59 million was transferred to the Education Lottery Fund (nonmajor special revenue fund).

The budget for 2006-2007 was approved by the Lottery Commission to provide $401 million to the Education Lottery Fund. The Lottery is on schedule to complete phase two of its start-up operations by the end of October 2006. Phase one of Lottery operations involved the implementation of instant and Powerball games. Phase two will include both Pick 3 and Pick 5 daily games.

As established in the enabling legislation, lottery funds are to be distributed for educational purposes as follows:
1. 50% to support reduction of class size in early grades and to support prekindergarten programs for at-risk four-year-olds who would otherwise not be served in high-quality settings *(Note: to this point, these programs have been funded by the General Fund).*
2. 40% for public school construction.
3. 10% to the State Education Assistance Authority to fund college and university scholarships.

**EPA Revolving Loan Fund**

The net assets of the EPA Revolving Loan Fund increased by $66.75 million during the current fiscal year, which was a 9.4% increase from the prior fiscal year-end. Operating income was $10.9 million (excess of operating revenues over operating expenses). Net nonoperating revenues were $47.4 million, consisting primarily of federal capitalization grants and investment earnings. The $8.7 million transferred in from other governmental funds (i.e., special revenue funds) consisted of clean water bond proceeds and additional funds to meet a required federal match.
Capital Asset and Debt Administration

Capital Assets

As of June 30, 2006, the State’s investment in capital assets was $29.21 billion, an increase of 5.85% from the previous fiscal year-end (see table below).

Capital Assets as of June 30

(Net of depreciation, dollars in thousands)

<table>
<thead>
<tr>
<th></th>
<th>Governmental Activities</th>
<th>Business-type Activities</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land</td>
<td>$9,439,616</td>
<td>$8,913,829</td>
<td>$3,147</td>
</tr>
<tr>
<td>Buildings</td>
<td>1,824,190</td>
<td>1,652,941</td>
<td>14,698</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>566,018</td>
<td>554,484</td>
<td>2,482</td>
</tr>
<tr>
<td>Infrastructure:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State highway system</td>
<td>15,368,302</td>
<td>14,247,222</td>
<td></td>
</tr>
<tr>
<td>Other infrastructure</td>
<td>77,240</td>
<td>79,958</td>
<td>28,972</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>105,256</td>
<td>108,045</td>
<td>1,457</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>60,485</td>
<td>60,485</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1,718,128</td>
<td>1,960,204</td>
<td>2,293</td>
</tr>
<tr>
<td>Total percent change between fiscal years 2005 and 2006</td>
<td>5.87% (2.96)% 5.85%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This year’s major capital asset additions were for highway construction ($1.4 billion), highway land improvements ($479 million) and the construction of correctional facilities ($34 million).

The largest component of capital assets is the State highway system. North Carolina has a 79 thousand mile highway system, making it the second largest state-maintained highway system in the nation. The most recent report on the condition of the State highway system (December 2004) noted that while the system continues to grow, the traditional highway maintenance funds necessary to maintain it have not changed significantly when adjusted for inflation.

The 2002-2003 Session of the General Assembly authorized the issuance of up to $300 million of special indebtedness to finance the repair and renovation of state facilities and related infrastructure that are supported by the State’s General Fund. Of the $300 million, approximately $157 million will be allocated to the University of North Carolina System. Each of the 16 constituent institutions of the UNC System will receive a portion of the proceeds for repairs and renovations. The remaining $143 million of the proceeds will be used to make repairs and renovations to various state facilities. At year-end, the authorized but unissued repair and renovation debt was $175 million.

In fiscal year 2006, the N.C. Department of Correction completed construction on Maury Correctional Institution (Maury) in Greene County and Bertie Correctional Institution (Bertie) in Bertie County, both of which are 1,000 bed close custody prisons. Maury began accepting inmates in April 2006. Bertie has an inmate occupancy date of August 2006. Total construction and design costs for Maury and Bertie were $82.3 million and $84.2 million, respectively. Another 1,000 bed close custody prison is under construction in Columbus County, with an estimated completion date of February 2008. The total estimated cost of this facility is $104.3 million. The primary funding sources for all three prisons were certificates of participation.

The Department of Correction is undertaking construction initiatives to address a prison cell shortfall and to allow for the implementation of sentencing reform. The State’s correctional facility population has more than doubled since 1980 to approximately 38,000 inmates as of November 2006. The rapid growth in inmates is attributable to increases in the State’s population, increases in length of stay in correctional facilities, and changes in criminal laws.
As further detailed in Note 20(F) to the financial statements, the State has commitments of $1.43 billion for the construction of highway infrastructure, which are expected to be financed by gasoline tax collections, motor vehicle fees, and federal funds. Other commitments for the construction and improvement of state government facilities totaled $580 million, which are expected to be financed primarily by debt proceeds (certificates of participation), state appropriations, and federal funds.

More detailed information about the State’s capital assets is presented in Note 5 to the financial statements.

**Long-term Debt**

At year-end, the State had total long-term debt (bonds and similar debt payable) outstanding of $6.52 billion, an increase of 0.5% from the previous fiscal year-end (see table below).

**Outstanding Debt as of June 30**

(dollars in thousands)

<table>
<thead>
<tr>
<th></th>
<th>Governmental Activities</th>
<th>Business-type Activities</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
<td>2006</td>
</tr>
<tr>
<td>General obligation bonds</td>
<td>$5,738,815</td>
<td>$5,698,535</td>
<td>$5,738,815</td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>255,045</td>
<td>265,045</td>
<td>263,845</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>454,060</td>
<td>475,170</td>
<td>454,060</td>
</tr>
<tr>
<td>Notes payable</td>
<td>60,841</td>
<td>37,107</td>
<td>62,298</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$6,508,761</td>
<td>$6,475,857</td>
<td>$6,519,018</td>
</tr>
</tbody>
</table>

Total percent change between fiscal years 2005 and 2006: 0.51% (3.59%) 0.50%

During the 2005-06 fiscal year, the State issued $370 million in general obligation bonds and entered into installment financing contracts (e.g., notes payable) exceeding $30 million. The new general obligation debt consisted of $300 million in higher education bonds (see next page) and $70 million in clean water bonds for providing grants and loans to local government units. The majority of the installment contracts were for the financing of energy conservation improvements at the N.C. Museum of Art and the downtown state government complex. Under these contracts, energy savings are guaranteed to exceed costs. The State is authorized to finance up to $100 million for energy conservation projects, of which $76.1 million remains authorized but unissued as of October 31, 2006. The State has undertaken these projects to reduce the use of energy, water, and other utilities in state facilities in order to provide its citizens with an example of energy efficiency.

The State’s general obligation bonds are secured by the full faith, credit, and taxing power of the State. The revenue bonds issued by the State are secured solely by specified revenue sources. The certificates of participation (COPs) and lease-purchase revenue bonds issued by the N.C. Infrastructure Finance Corporation, a blended component unit of the State, are secured by lease and installment payments made by the State, and in the event of default, by a security interest in the leased facilities pursuant to a leasehold deed of trust (as applicable). The COPs issued for repair and renovation projects are not secured by a lien upon or security interest in the projects or any other property of the State. Installment financing contracts are secured by a lien on facilities or equipment.

The debt service payments on COPs, lease-purchase revenue bonds, and installment financing contracts are subject to appropriation by the General Assembly. If the State defaulted on its repayments, no deficiency judgment could be rendered against the State, but the state property that serves as security could be disposed of to generate funds to satisfy the debt. Failure to repay the debt would have negative consequences for the State’s credit rating. Article 9 of Chapter 142 of the General Statutes prohibits the issuance of special indebtedness (e.g., COPs and lease-purchase revenue bonds) except for projects specifically authorized by the General Assembly. The use of alternative financing methods provides financing flexibility to the State and permits the State to take advantage of changing financial and economic environments.
Higher Education Authorization

The 1999-2000 Session of the General Assembly authorized the issuance of up to $3.1 billion of higher education improvement bonds, which were subsequently approved by the voters of the State. The $3.1 billion bond authorization represents the largest debt authorization in the State's history. The proceeds of these general obligation bonds are being used solely to construct new buildings and to renovate and modernize existing buildings on the State's 58 community college and 16 University of North Carolina campuses. These improvements are needed to meet enrollment demands and to ensure that the State's college and university buildings meet modern code requirements and are equipped to prepare graduates for twenty-first century jobs. The bond legislation passed by the General Assembly specifies the amount of bond funding that will flow to each community college and university campus. At year-end, the authorized but unissued higher education bonds were $403.5 million.

Recent Debt Legislation

The State budget bill for fiscal year 2006-07 authorized the issuance of up to $672.1 million of special indebtedness (e.g., COPs) to finance the following projects:

- $40 million to construct new buildings and renovate existing buildings at the N.C. Museum of Art.
- $20 million to complete the Central Region Psychiatric Hospital for the N.C. Department of Health and Human Services (DHHS).
- $24.8 million for facility costs of a new Secondary State Data Center.
- $45.8 million for facility costs of a new Center City Classroom Building at the University of North Carolina at Charlotte.
- $101 million for facility costs for the DHHS Public Health Laboratory and Office of the Chief Medical Examiner.
- $145.5 million for facility costs of the Eastern Regional Psychiatric Hospital for DHHS.
- $132.2 million for facility costs of the Regional Medical Center and Mental Health Center of the N.C. Department of Correction.
- $162.8 million for facility costs of the Western Regional Psychiatric Hospital for DHHS.

Additional legislation was enacted during the 2005-06 session of the General Assembly that authorized the issuance of special indebtedness of up to $20 million for the purchase of State game lands and up to $20 million for the construction of a parking facility in downtown Raleigh.

The previous session of the General Assembly authorized the N.C. Department of Transportation to issue "GARVEE" bonds or other eligible debt financing instruments to finance federal-aid highway projects. These bonds are Grant Anticipation Revenue Vehicles, authorized by federal law, that permit states to use anticipated future federal highway funds to finance highway project construction. According to the Federal Highway Administration, candidate projects for GARVEE financing are typically larger projects that have the following characteristics:

- They are large enough to merit borrowing rather than pay-as-you-go grant funding, with the costs of delay outweighing the costs of financing;
- They do not have access to a revenue stream (such as local taxes or tolls) and other forms of repayment (such as state appropriations) are not feasible; and
- The sponsors (generally state DOT's) are willing to reserve a portion of federal aid highway funds in future years to satisfy debt service requirements.

Total debt would be constrained by the amount of federal aid authorized in the prior federal fiscal year, which was approximately $953 million for federal fiscal year 2005, the last year for which data is available. More than a dozen other states are already using this type of financing, which Congress authorized in 1995.
Debt Affordability Advisory Committee

During the 2003-04 Session, the General Assembly created a Debt Affordability Advisory Committee (Committee) to annually advise the Governor and the General Assembly on the estimated debt capacity of the State for the upcoming ten fiscal years. The Committee is responsible for preparing an annual debt affordability study and establishing guidelines for evaluating the State's debt burden. The Committee is required to report its findings and recommendations to the Governor, the General Assembly, and the Fiscal Research Division of the General Assembly by February 1 of each year.

In February 2006, the State Treasurer completed the most recent Debt Affordability Study for North Carolina. The report provides the Governor and the General Assembly with a basis for assessing the impact of future debt issuance on the State's fiscal position and enables informed decision-making regarding both financing proposals and capital spending priorities. A secondary purpose of the report is to provide a methodology for measuring, monitoring and managing the State's debt levels, thereby protecting, and perhaps enhancing North Carolina's bond ratings.

The Committee adopted the following target and ceiling guidelines as the preferred measure used to determine the amount of net tax-supported debt that can be prudently authorized by the State:

- Net Tax-Supported Debt Service as a percentage of General Tax Revenues should be targeted at no more than 4% and not exceed 4.75%.

The definition of net tax-supported debt excludes obligations of component units, Highway Fund debt paid from Highway Fund revenues, non-tax-supported special indebtedness paid from trust funds, and other self-supporting debt such as revenue bonds and short-term tax anticipation notes.

According to the report, all of the State's debt ratios are below median levels for all 50 states and for a group of six states rated "triple A" by all three rating agencies. Thus, the study concludes that North Carolina's debt is considered low and is manageable at current levels. Credit rating agencies consider a debt affordability study as a positive factor when evaluating issuers and assigning credit ratings.

Credit Ratings

Credit ratings are the rating agencies' assessment of a governmental entity's ability and willingness to repay debt on a timely basis. Credit ratings are an important factor in the public credit markets and can influence interest rates a borrower must pay.

The State's general obligation bonds are rated AAA by Fitch Ratings and AAA with a "stable" outlook by Standard & Poor's Ratings Services, the highest ratings attainable. Moody's Investors Service (Moody's) rates the State's general obligation bonds at Aa1 with a "positive outlook", one half step below their highest rating of Aaa. All three agencies base their prime ratings on the State's strong, diverse economic base, its sound financial management, and low debt levels.

In August 2002, Moody's downgraded the State's credit rating for general obligation debt from "AAA" to "Aa1", representing the first time since 1960 that North Carolina had less than a AAA rating. While Moody's praised the strength of executive powers available to insure a balanced budget, it advised that the primary reasons for the downgrade were the State's continued budget pressure, reliance on non-recurring revenues, and weakened balance sheet. Also, Moody's commented that the task of restoring structural budget balance and rebuilding reserves faces political and economic obstacles. In September 2004, Moody's revised the State's outlook from stable to positive and noted the following:

"This rating reflects the State's slowly stabilizing economy, its improving tax revenues, its conservative debt policy, and its effective financial management. While general fund balances remain negative, flexible cash reserves outside the general fund are ample, and pension funding is exceptionally strong. Moody's expects that the state will continue to take actions to restore structural balance and rebuild reserves."
The COPs and lease-purchase revenue bonds issued by the North Carolina Infrastructure Finance Corporation are rated "AA+" by Standard & Poor's, "AA+" by Fitch, and "Aa2" by Moody's.

**Limitations on Debt**

The Constitution of North Carolina (Article 5, Section 3) imposes limitations upon the increase of certain state debt. It restricts the General Assembly from contracting debts secured by a pledge of the faith and credit of the State, unless approved by a majority of the qualified voters of the State, except for the following purposes:

1. To fund or refund a valid existing debt;
2. To supply an unforeseen deficiency in the revenue;
3. To borrow in anticipation of the collection of taxes due and payable within the current fiscal year to an amount not exceeding 50 percent of such taxes;
4. To suppress riots or insurrections; or to repel invasions;
5. To meet emergencies immediately threatening the public health or safety, as conclusively determined in writing by the Governor; and
6. For any other lawful purpose, to the extent of two-thirds of the amount by which the State's outstanding indebtedness shall have been reduced during the preceding biennium.

More detailed information about the State's long-term liabilities is presented in Note 7 to the financial statements.

**Next Year's Budget and Rates**

The General Assembly and the Governor adopted a conservative revenue forecast for fiscal year 2006-07. The baseline growth estimate was 3.1%, well below the economic growth forecasts of North Carolina's university and bank economists.

Tax changes include reducing the State sales tax rate from 4.5% to 4.25% effective December 1, 2006, reducing the top income tax rate from 8.25% to 8% effective January 1, 2007, increasing the cigarette tax from 30 cents to 35 cents per pack effective July 1, 2006, and capping the gasoline tax at current levels. In addition, a $195.2 million reduction in the transfer from the Highway Trust Fund to the General Fund is recommended for fiscal year 2006-07. This reduction would repay the $125 million one time borrowing made to offset a budget shortfall as well as the $80 million inflationary increase adopted in fiscal year 2002-03.
Conditions Expected to Impact Future Operations

State Health Plan
The State Health Plan made available a Preferred Provider Organization (PPO) option to all eligible participants, effective October 1, 2006, as an alternative to the State’s indemnity plan. The indemnity plan was the only option that had been offered prior to this time. The PPO option provides for improved health benefits at a lower cost to the State. PPO plans contract with various physicians, hospitals, and other providers to form medical care networks. For the State Health Plan, PPO members receive services at lower premiums and reduced out-of-pocket costs when they use in-network providers. Approximately 330,000 eligible participants selected the new PPO plan offerings during the recent enrollment period. The State Health Plan provides coverage to approximately 600,000 teachers, state employees, and retirees, with a budget of approximately $2 billion.

Escheats Fund
Legislation passed in 2005 authorized the State Treasurer to diversify the investments of the Escheats Fund. Previously, the Fund was limited to participating in the Long Term Investment Portfolio. The State Constitution mandates that proceeds of the Escheat Fund shall be used to aid needy and worthy North Carolina students enrolled in public institutions of higher education. The continuing demand on resources at the universities and community colleges has necessitated regular tuition increases. The establishment of a modern investment allocation strategy aimed at increasing returns was identified as a way to enhance the Fund’s constitutionally provided purpose. Under the new provisions, the State Treasurer is authorized to invest up to 20% of the assets of the Escheats Fund in private equity investments. As of June 30, 2006, $20 million has been invested into a Real Estate Investment Fund. In fiscal year 2007, investments into public equity and alternative investments funds are expected.

Repayment of Escrowed Retirement Trust Funds
The State withheld $212.5 million in contributions to the Teachers’ and State Employees’ Retirement System, the Consolidated Judicial Retirement System, and the Legislative Retirement System to balance the State budget in 2001. The State committed to repaying the funds by 2008. As of June 30, 2006, approximately $138 million had been repaid. The budget for 2006-07 included another payment to the escrowed debt of $30 million. The balance of the debt is now $44.9 million.

Providing Retirement Benefits
It is widely anticipated that the progression of the baby boomer cohort from full-time career status into retirement will have significant economic, social, and political impact throughout the country. Predicting specific ramifications of this phenomenon is difficult. In North Carolina we anticipate some impact to the State’s public sector workforce, as boomers increasingly leave active service and retire, and to the state and local government retirement systems. The impact to the retirement systems could be both financial and administrative.

Administratively, the significant increase in the number of retirements to process and maintain will challenge current operations. The total number of members receiving a retirement benefit in the state and local system is approximately 173,000 (includes system retirees, beneficiaries, and members receiving a disability retirement allowance). That number is projected to increase to 345,000 by the year 2025 - an approximate 100% increase in the total number of state and local retirees maintained by the agency over the next 18 years. To help address this need, the Retirement Systems Division is currently increasing organizational efficiencies by implementing a $34 million replacement of its information technology system that will go-live in October 2007.

Financially, the North Carolina retirement systems are expected to continue the trend of robust fiscal health (the system’s funding has averaged 109% for the last 6 years). Any substantive cost increases will not primarily be driven by the cost of providing an actual pension, since employees and employers fund the pension over an employee’s service career. However, a significant increase in cost may come from providing cost of living adjustments (COLAs) for a significantly larger retiree pool since those are not pre-funded.
Health Care Benefits for Retirees and Beneficiaries

Based on a unit credit cost method and the State's pay-as-you-go approach as of December 31, 2005, the actuarial results are as follows:

<table>
<thead>
<tr>
<th>Funding method</th>
<th>Not advance funded</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actuarial cost method</td>
<td>Unit credit</td>
</tr>
<tr>
<td>Actuarial accrued liability</td>
<td>$23.9 billion</td>
</tr>
<tr>
<td>Assets</td>
<td>$0.1 billion</td>
</tr>
<tr>
<td>Unfunded accrued liability</td>
<td>$23.8 billion</td>
</tr>
<tr>
<td>Annual required contribution</td>
<td>$2.4 billion</td>
</tr>
</tbody>
</table>

The claims cost of 2006 benefits, on a cash basis, was $539 million. The General Assembly and the Governor are responsible for managing the State's postemployment health care obligations. Any significant changes in benefit or eligibility provisions would be reflected in subsequent actuarial valuations. Additional information about the State's postemployment health care benefits is presented in the letter of transmittal and in Note 13A to the financial statements.

Requests for Information

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the State's finances and to demonstrate the State's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the North Carolina Office of the State Controller, Accounting and Financial Reporting Section, 1410 Mail Service Center, Raleigh, N.C. 27699-1410. In addition, this financial report is available on the Office of the State Controller's internet home page at http://www.nocos.net/financial/financial.html.
Basic
Financial
Statements
GOVERNMENT-WIDE
FINANCIAL STATEMENTS
### STATEMENT OF NET ASSETS

**June 30, 2006**

**(Dollars in Thousands)**

#### Primary Government

<table>
<thead>
<tr>
<th>Assets</th>
<th>Governmental Activities</th>
<th>Business-type Activities</th>
<th>Total</th>
<th>Component Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents (Note 3)</td>
<td>$4,674,651</td>
<td>$451,447</td>
<td>$5,126,098</td>
<td>$2,601,756</td>
</tr>
<tr>
<td>Investments (Note 3)</td>
<td>1,041,445</td>
<td>57,453</td>
<td>1,098,898</td>
<td>3,548,020</td>
</tr>
<tr>
<td>Securities lending collateral (Note 3)</td>
<td>5,367,553</td>
<td>266,780</td>
<td>5,634,333</td>
<td>—</td>
</tr>
<tr>
<td>Receivables, net (Note 4)</td>
<td>3,394,647</td>
<td>406,921</td>
<td>3,801,568</td>
<td>927,829</td>
</tr>
<tr>
<td>Due from component units (Note 17)</td>
<td>12,758</td>
<td>—</td>
<td>12,758</td>
<td>58,817</td>
</tr>
<tr>
<td>Due from primary government (Note 17)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>143,726</td>
</tr>
<tr>
<td>Internal balances</td>
<td>13,620</td>
<td>(13,620)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Inventories</td>
<td>162,467</td>
<td>501</td>
<td>162,968</td>
<td>78,556</td>
</tr>
<tr>
<td>Prepaid items</td>
<td>14,439</td>
<td>2,213</td>
<td>16,652</td>
<td>15,677</td>
</tr>
<tr>
<td>Advances to component units (Note 17)</td>
<td>25,364</td>
<td>—</td>
<td>25,364</td>
<td>—</td>
</tr>
<tr>
<td>Notes receivable, net (Note 4)</td>
<td>342,149</td>
<td>545,570</td>
<td>887,719</td>
<td>3,787,120</td>
</tr>
<tr>
<td>Endowment investments (Note 3)</td>
<td>57,741</td>
<td>—</td>
<td>57,741</td>
<td>2,096,982</td>
</tr>
<tr>
<td>Investment in joint venture</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>8,319</td>
</tr>
<tr>
<td>Deferred charges</td>
<td>—</td>
<td>107</td>
<td>107</td>
<td>23,725</td>
</tr>
<tr>
<td>Securities held in trust</td>
<td>43,911</td>
<td>—</td>
<td>43,911</td>
<td>—</td>
</tr>
<tr>
<td>Pension assets (Note 11)</td>
<td>471</td>
<td>—</td>
<td>471</td>
<td>—</td>
</tr>
<tr>
<td>Capital assets-nondepreciable (Note 5)</td>
<td>11,218,229</td>
<td>5,440</td>
<td>11,223,669</td>
<td>1,871,530</td>
</tr>
<tr>
<td>Capital assets-depreciable, net (Note 5)</td>
<td>17,941,006</td>
<td>47,589</td>
<td>17,988,595</td>
<td>6,873,809</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>44,330,451</td>
<td>1,770,401</td>
<td>46,100,852</td>
<td>22,033,866</td>
</tr>
</tbody>
</table>

#### Liabilities

| Accounts payable and accrued liabilities | 1,296,093 | 44,072 | 1,340,165 | 608,306 |
| Medical claims payable | 983,145 | — | 983,145 | 4,917 |
| Unemployment benefits payable | — | 17,792 | 17,792 | — |
| Tax refunds payable | 1,183,801 | — | 1,183,801 | — |
| Obligations under securities lending | 5,367,553 | 266,780 | 5,634,333 | — |
| Interest payable | 87,542 | 33 | 87,575 | 51,457 |
| Short-term debt (Note 6) | — | — | — | — |
| Due to component units (Note 17) | 143,726 | — | 143,726 | 58,817 |
| Due to primary government (Note 17) | — | — | — | 12,759 |
| Unearned revenue | 498,444 | 16,957 | 515,401 | 132,378 |
| Advance from primary government (Note 17) | — | — | — | 25,364 |
| Obligations under reverse repurchase agreements | — | — | — | 4,015 |
| Deposits payable | 60 | 28 | 88 | 11,700 |
| Funds held for others | 54,538 | — | 54,538 | 679,255 |
| Long-term liabilities (Note 7): | 549,362 | 587 | 549,949 | 972,610 |
| Due within one year | 6,732,287 | 13,477 | 6,745,764 | 6,140,929 |
| **Total Liabilities** | 16,886,551 | 359,726 | 17,246,277 | 8,842,686 |

#### Net Assets

| Invested in capital assets, net of related debt | 28,035,283 | 44,196 | 28,079,479 | 6,332,775 |

**Restricted for:**

- Nonexpendable:
  - Environment and natural resources | 56,645 | — | 56,645 | — |
  - Higher education | 527 | — | 527 | 1,420,266 |
  - Health and human services | 200 | — | 200 | — |

- Expendable:
  - Primary and secondary education | 7,332 | — | 7,332 | — |
  - Higher education | 540,069 | — | 540,069 | 2,475,959 |
  - Health and human services | 153,023 | — | 153,023 | 5,798 |
  - Economic development | 1,831 | — | 1,831 | 381,901 |
  - Environment and natural resources | 34,348 | — | 34,348 | — |
  - Public safety, corrections, and regulation | 54,093 | — | 54,093 | — |
  - Transportation | 11,864 | — | 11,864 | — |
  - Unemployment compensation | 507,477 | — | 507,477 | — |
  - EPA revolving loan | — | 775,269 | 775,269 | — |
  - Other purposes | 30,670 | 3,731 | 34,401 | 32 |

**Unrestricted:**

(1,491,985) | 80,002 | (1,111,983) | 2,574,547 |

**Total Net Assets**

$27,433,900 | $1,410,675 | $28,844,575 | $13,191,180 |

*The accompanying Notes to the Financial Statements are an integral part of this statement.*
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# Statement of Activities

For the Fiscal Year Ended June 30, 2008

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Functions/Programs</th>
<th>Expenses</th>
<th>Program Revenues</th>
<th>Capital Grants and Contributions</th>
<th>Net (Expense) Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Primary Government:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Governmental Activities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General government</td>
<td>$1,039,513 $339,053</td>
<td>$215,409 $1,711</td>
<td>(483,340)</td>
<td></td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>8,215,445 23,959</td>
<td>1,163,672</td>
<td>—</td>
<td>(7,027,814)</td>
</tr>
<tr>
<td>Higher education</td>
<td>3,472,024 300</td>
<td>22,038</td>
<td>—</td>
<td>(3,449,686)</td>
</tr>
<tr>
<td>Health and human services</td>
<td>13,491,119 295,479</td>
<td>9,139,441 14,582</td>
<td>(4,041,817)</td>
<td></td>
</tr>
<tr>
<td>Economic development</td>
<td>647,434 26,506</td>
<td>375,654</td>
<td>—</td>
<td>(245,274)</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>676,049 151,698</td>
<td>94,056 77,723</td>
<td>(352,572)</td>
<td></td>
</tr>
<tr>
<td>Public safety, corrections, and regulation</td>
<td>2,304,900 411,188</td>
<td>223,663 15,520</td>
<td>(1,654,529)</td>
<td></td>
</tr>
<tr>
<td>Transportation</td>
<td>1,781,865 725,311</td>
<td>256,466 803,487</td>
<td>3,399</td>
<td></td>
</tr>
<tr>
<td>Agriculture</td>
<td>112,467 14,507</td>
<td>13,445 1,087</td>
<td>(83,448)</td>
<td></td>
</tr>
<tr>
<td>Interest on long-term debt</td>
<td>264,287</td>
<td>—</td>
<td>—</td>
<td>(264,287)</td>
</tr>
<tr>
<td>Total Governmental Activities</td>
<td>32,005,103</td>
<td>1,985,001</td>
<td>11,503,844</td>
<td>914,090</td>
</tr>
<tr>
<td><strong>Business-type Activities:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unemployment Compensation</td>
<td>849,945 1,101,357</td>
<td>5,910</td>
<td>—</td>
<td>257,322</td>
</tr>
<tr>
<td>N.C. State Lottery</td>
<td>153,125 216,906</td>
<td>806</td>
<td>—</td>
<td>64,569</td>
</tr>
<tr>
<td>EPA Revolving Loan</td>
<td>11,414 15,237</td>
<td>54,514</td>
<td>—</td>
<td>58,337</td>
</tr>
<tr>
<td>Regulatory commissions</td>
<td>28,526 33,550</td>
<td>850</td>
<td>—</td>
<td>5,874</td>
</tr>
<tr>
<td>Insurance programs</td>
<td>16,051 14,860</td>
<td>852</td>
<td>—</td>
<td>(339)</td>
</tr>
<tr>
<td>North Carolina State Fair</td>
<td>10,497 12,581</td>
<td>109</td>
<td>—</td>
<td>2,193</td>
</tr>
<tr>
<td>Other business-type activities</td>
<td>10,255 7,973</td>
<td>1,042</td>
<td>258</td>
<td>386,994</td>
</tr>
<tr>
<td>Total Business-type Activities</td>
<td>1,079,813 1,402,494</td>
<td>84,055</td>
<td>258</td>
<td>386,994</td>
</tr>
<tr>
<td>Total Primary Government</td>
<td>$33,084,918 $3,390,465</td>
<td>$11,587,829 $914,090</td>
<td>(17,212,174)</td>
<td></td>
</tr>
<tr>
<td><strong>Component Units:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Golden LEAF, Inc.</td>
<td>$28,773 $5</td>
<td>$48,444 $ —</td>
<td>—</td>
<td>19,676</td>
</tr>
<tr>
<td>University of North Carolina System</td>
<td>6,650,114 3,903,663</td>
<td>929,272 32,747</td>
<td>(1,784,432)</td>
<td></td>
</tr>
<tr>
<td>Community Colleges</td>
<td>1,502,874 242,164</td>
<td>452,649 60,971</td>
<td>(747,090)</td>
<td></td>
</tr>
<tr>
<td>N.C. Housing Finance Agency</td>
<td>251,870 244,466</td>
<td>32,086</td>
<td>—</td>
<td>24,664</td>
</tr>
<tr>
<td>State Education Assistance Authority</td>
<td>249,312 154,206</td>
<td>38,717</td>
<td>—</td>
<td>(58,389)</td>
</tr>
<tr>
<td>Other component units</td>
<td>195,104 58,702</td>
<td>20,344 715</td>
<td>(117,343)</td>
<td></td>
</tr>
<tr>
<td>Total Component Units</td>
<td>$8,878,047 $4,601,206</td>
<td>$1,521,494 $94,433</td>
<td>(2,660,914)</td>
<td></td>
</tr>
</tbody>
</table>

The accompanying Notes to the Financial Statements are an integral part of this statement.
STATEMENT OF ACTIVITIES (continued)

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Primary Government</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Governmental</td>
<td>Business-type</td>
<td>Total</td>
<td>Component</td>
</tr>
<tr>
<td></td>
<td>Activities</td>
<td>Activities</td>
<td></td>
<td>Units</td>
</tr>
<tr>
<td>Changes in Net Assets:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net (expense) revenue</td>
<td>$(17,596,168)</td>
<td>$386,994</td>
<td>$(17,212,174)</td>
<td>$(2,660,914)</td>
</tr>
<tr>
<td>General Revenues:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxes:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income tax</td>
<td>9,336,745</td>
<td>—</td>
<td>9,336,745</td>
<td>—</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>1,306,193</td>
<td>—</td>
<td>1,306,193</td>
<td>—</td>
</tr>
<tr>
<td>Sales and use tax</td>
<td>5,033,040</td>
<td>—</td>
<td>5,033,040</td>
<td>—</td>
</tr>
<tr>
<td>Gasoline tax</td>
<td>1,514,626</td>
<td>—</td>
<td>1,514,626</td>
<td>—</td>
</tr>
<tr>
<td>Franchise tax</td>
<td>628,029</td>
<td>—</td>
<td>628,029</td>
<td>—</td>
</tr>
<tr>
<td>Highway use tax</td>
<td>577,237</td>
<td>—</td>
<td>577,237</td>
<td>—</td>
</tr>
<tr>
<td>Insurance tax</td>
<td>442,297</td>
<td>—</td>
<td>442,297</td>
<td>—</td>
</tr>
<tr>
<td>Beverage tax</td>
<td>233,315</td>
<td>—</td>
<td>233,315</td>
<td>—</td>
</tr>
<tr>
<td>Inheritance tax</td>
<td>133,156</td>
<td>—</td>
<td>133,156</td>
<td>—</td>
</tr>
<tr>
<td>Other taxes</td>
<td>482,552</td>
<td>—</td>
<td>482,552</td>
<td>—</td>
</tr>
<tr>
<td>Tobacco settlement</td>
<td>140,969</td>
<td>—</td>
<td>140,969</td>
<td>—</td>
</tr>
<tr>
<td>Unrestricted investment earnings</td>
<td>123,170</td>
<td>—</td>
<td>123,170</td>
<td>—</td>
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<tr>
<td>State operating aid</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3,132,005</td>
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<tr>
<td>State capital aid</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>489,979</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>37,248</td>
<td>4</td>
<td>37,252</td>
<td>10,628</td>
</tr>
<tr>
<td>Contributions to permanent funds</td>
<td>4,874</td>
<td>—</td>
<td>4,874</td>
<td>—</td>
</tr>
<tr>
<td>Contributions to endowments</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>109,747</td>
</tr>
<tr>
<td>Transfers</td>
<td>87,978</td>
<td>(87,978)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Total general revenues, contributions and transfers</td>
<td>20,081,231</td>
<td>(87,974)</td>
<td>19,993,257</td>
<td>3,742,357</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>2,462,063</td>
<td>318,020</td>
<td>2,781,083</td>
<td>1,081,443</td>
</tr>
<tr>
<td>Net assets — July 1, as restated (Note 22)</td>
<td>24,971,837</td>
<td>1,091,655</td>
<td>26,063,492</td>
<td>12,109,737</td>
</tr>
<tr>
<td>Net assets — June 30</td>
<td>$27,433,900</td>
<td>$1,410,675</td>
<td>$28,844,575</td>
<td>$13,191,180</td>
</tr>
</tbody>
</table>
FUND FINANCIAL STATEMENTS
## BALANCE SHEET
### GOVERNMENTAL FUNDS

**June 30, 2006**

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Assets</th>
<th>General Fund</th>
<th>Highway Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>Total Governmental Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents (Note 3)</td>
<td>$2,421,376</td>
<td>$599,757</td>
<td>$21,766</td>
<td>$1,577,952</td>
<td>$4,610,851</td>
</tr>
<tr>
<td>Investments (Note 3)</td>
<td>2,014</td>
<td>—</td>
<td>—</td>
<td>1,018,515</td>
<td>1,020,529</td>
</tr>
<tr>
<td>Securities lending collateral (Note 3)</td>
<td>3,763,630</td>
<td>532,421</td>
<td>23,001</td>
<td>1,009,392</td>
<td>5,328,444</td>
</tr>
<tr>
<td>Receivables, net: (Note 4)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxes receivable</td>
<td>1,790,815</td>
<td>107,306</td>
<td>37,855</td>
<td>2,317</td>
<td>1,938,293</td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>258,855</td>
<td>10,588</td>
<td>392</td>
<td>24,217</td>
<td>294,052</td>
</tr>
<tr>
<td>Intergovernmental receivable</td>
<td>1,061,100</td>
<td>56,789</td>
<td>2,529</td>
<td>7,445</td>
<td>1,127,863</td>
</tr>
<tr>
<td>Interest receivable</td>
<td>13,835</td>
<td>391</td>
<td>518</td>
<td>7,433</td>
<td>22,177</td>
</tr>
<tr>
<td>Other receivables</td>
<td>—</td>
<td>2,102</td>
<td>—</td>
<td>—</td>
<td>2,102</td>
</tr>
<tr>
<td>Due from other funds (Note 9)</td>
<td>5,690</td>
<td>75,495</td>
<td>105</td>
<td>57,927</td>
<td>139,217</td>
</tr>
<tr>
<td>Due from component units (Note 17)</td>
<td>2,438</td>
<td>—</td>
<td>—</td>
<td>9,240</td>
<td>11,678</td>
</tr>
<tr>
<td>Inventories</td>
<td>73,343</td>
<td>74,991</td>
<td>—</td>
<td>33,618</td>
<td>182,152</td>
</tr>
<tr>
<td>Prepaid items</td>
<td>—</td>
<td>—</td>
<td>991</td>
<td>3,841</td>
<td>3,841</td>
</tr>
<tr>
<td>Advances to component units (Note 17)</td>
<td>—</td>
<td>3,622</td>
<td>—</td>
<td>21,742</td>
<td>25,364</td>
</tr>
<tr>
<td>Notes receivable, net (Note 4)</td>
<td>6,578</td>
<td>1,102</td>
<td>107</td>
<td>334,362</td>
<td>342,149</td>
</tr>
<tr>
<td>Securities held in trust</td>
<td>565</td>
<td>4,546</td>
<td>—</td>
<td>38,800</td>
<td>43,911</td>
</tr>
<tr>
<td>Endowment investments (Note 3)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>57,741</td>
<td>57,741</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>$9,400,239</td>
<td>$1,455,488</td>
<td>$89,895</td>
<td>$4,201,892</td>
<td>$15,147,514</td>
</tr>
</tbody>
</table>

### Liabilities and Fund Balances

**Liabilities:**

- Accounts payable and accrued liabilities:
  - Accounts payable: $79,077
  - Accrued payroll: 6,529
  - Intergovernmental payable: 602,461
  - Medical claims payable: 983,145
  - Tax refunds payable: 1,183,801
  - Obligations under securities lending: 3,763,630
  - Interest payable: 655
  - Due to fiduciary funds (Note 9): 42,541
  - Due to other funds (Note 9): 14,190
  - Due to component units (Note 17): 48,446
  - Deferred revenue: 749,622
  - Deposits payable: 51
  - Funds held for others: 903

**Total Liabilities:** $7,475,041

**Fund Balances:**

- Reserved (Note 10): 155,418
- Unreserved/Designated: 655,731
- Unreserved/Undesignated, reported in:
  - General Fund: 1,113,049
  - Special Revenue Funds: 514,786
  - Capital Projects Funds: —
  - Permanent Funds: —

**Total Fund Balance:** $1,925,196

**Total Liabilities and Fund Balances:** $9,400,239

*The accompanying Notes to the Financial Statements are an integral part of this statement.*
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS

June 30, 2006

(Dollars in Thousands)

Total fund balances - governmental funds (see Exhibit B-1) $ 5,233,485

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 funds (see Note 5). These consist of:
  
  Cost of capital assets (excluding internal service funds) .......................................... $ 29,494,748
  
  Less: Accumulated depreciation (excluding internal service funds) .......................... (431,249)
  
  Net capital assets ........................................................................................................ 29,063,499

- **Some assets**, such as receivables, are not available soon enough to pay for current-period expenditures and thus, are offset by deferred revenue in the governmental funds.

- **Pension assets**, resulting from contributions in excess of the annual required contribution are not financial resources and, therefore, are not reported in the funds (see Note 11).

- **Long-term debt instruments**, such as bonds and notes payable, are not due and payable in the current period and, therefore, the outstanding balances are not reported in the funds (see Note 7). Also, unamortized debt premiums, discounts, and losses on refundings are reported in the Statement of Net Assets but are not reported in the funds. These balances consist of:
  
  General obligation bonds payable ................................................................................. (5,738,815)
  
  Lease-purchase revenue bonds payable ......................................................................... (255,045)
  
  Certificates of participation payable ............................................................................ (454,060)
  
  Unamortized debt premiums (to be amortized as interest expense) ......................... (313,253)
  
  Less: Unamortized debt discounts (to be amortized as interest expense) ............... 721
  
  Less: Unamortized loss on refunding (to be amortized as interest expense) .......... 103,059
  
  Notes payable ............................................................................................................. (60,841)
  
  Capital leases payable ................................................................................................. (26,879)
  
  Net long-term debt ...................................................................................................... (6,745,113)

- **Other liabilities** not due and payable in the current period and, therefore, not reported in the funds (see Note 7 as applicable) consist of:
  
  Accrued interest payable ................................................................................................. (86,887)
  
  Compensated absences (excluding internal service funds) .......................................... (370,934)
  
  Obligations for workers compensation ....................................................................... (5,266)
  
  Arbitrage rebate payable ............................................................................................. (508)
  
  Deferred death benefit payable .................................................................................... (340)
  
  Cost settlement payable ............................................................................................... (154,000)
  
  Net pension obligation ................................................................................................ 1,827
  
  Total other liabilities ................................................................................................... 619,562

- **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 (see Exhibit B-3).

Total net assets - governmental activities (see Exhibit A-1) $ 27,433,900

The accompanying Notes to the Financial Statements are an integral part of this statement.
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Revenues:</th>
<th>General Fund</th>
<th>Highway Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>Total Governmental Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxes:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income tax</td>
<td>$ 9,493,714</td>
<td>$ 993,667</td>
<td>1,114,743</td>
<td>$ 1,735</td>
<td>$ 9,495,449</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>1,208,356</td>
<td>—</td>
<td>—</td>
<td>98,199</td>
<td>1,306,555</td>
</tr>
<tr>
<td>Sales and use tax</td>
<td>5,007,567</td>
<td>—</td>
<td>—</td>
<td>26,836</td>
<td>5,034,403</td>
</tr>
<tr>
<td>Gasoline tax</td>
<td>—</td>
<td>1,114,743</td>
<td>372,072</td>
<td>27,927</td>
<td>1,514,742</td>
</tr>
<tr>
<td>Franchise tax</td>
<td>628,665</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>628,665</td>
</tr>
<tr>
<td>Highway use tax</td>
<td>—</td>
<td>—</td>
<td>577,237</td>
<td>—</td>
<td>577,237</td>
</tr>
<tr>
<td>Insurance tax</td>
<td>431,729</td>
<td>—</td>
<td>—</td>
<td>10,588</td>
<td>442,317</td>
</tr>
<tr>
<td>Beverage tax</td>
<td>232,987</td>
<td>—</td>
<td>—</td>
<td>328</td>
<td>233,315</td>
</tr>
<tr>
<td>Inheritance tax</td>
<td>133,248</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>133,248</td>
</tr>
<tr>
<td>Other taxes</td>
<td>336,820</td>
<td>—</td>
<td>—</td>
<td>148,734</td>
<td>485,554</td>
</tr>
<tr>
<td>Federal funds</td>
<td>9,905,679</td>
<td>993,667</td>
<td>—</td>
<td>415,976</td>
<td>11,315,422</td>
</tr>
<tr>
<td>Local funds</td>
<td>574,300</td>
<td>14,778</td>
<td>1,976</td>
<td>19,447</td>
<td>610,501</td>
</tr>
<tr>
<td>Investment earnings</td>
<td>262,904</td>
<td>38,343</td>
<td>3,018</td>
<td>79,749</td>
<td>364,014</td>
</tr>
<tr>
<td>Interest earnings on loans</td>
<td>—</td>
<td>7</td>
<td>—</td>
<td>5,398</td>
<td>5,405</td>
</tr>
<tr>
<td>Sales and services</td>
<td>95,178</td>
<td>813</td>
<td>—</td>
<td>164,547</td>
<td>260,538</td>
</tr>
<tr>
<td>Rental and lease of property</td>
<td>7,942</td>
<td>13,399</td>
<td>1,434</td>
<td>3,207</td>
<td>25,982</td>
</tr>
<tr>
<td>Fees, licenses, and fines</td>
<td>501,018</td>
<td>597,326</td>
<td>106,348</td>
<td>200,877</td>
<td>1,405,569</td>
</tr>
<tr>
<td>Tobacco settlement</td>
<td>136,453</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>136,453</td>
</tr>
<tr>
<td>Contributions, gifts, and grants</td>
<td>17,633</td>
<td>1,946</td>
<td>868</td>
<td>98,489</td>
<td>118,936</td>
</tr>
<tr>
<td>Funds escheated</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>108,075</td>
<td>108,075</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>131,843</td>
<td>13,288</td>
<td>2,053</td>
<td>13,888</td>
<td>161,052</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>29,105,236</strong></td>
<td><strong>2,788,510</strong></td>
<td><strong>1,065,006</strong></td>
<td><strong>1,421,960</strong></td>
<td><strong>34,380,712</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenditures:</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Current:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General government</td>
<td>869,092</td>
<td>—</td>
<td>—</td>
<td>94,807</td>
<td>963,899</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>7,954,919</td>
<td>—</td>
<td>—</td>
<td>257,079</td>
<td>8,211,998</td>
</tr>
<tr>
<td>Higher education</td>
<td>3,060,173</td>
<td>—</td>
<td>—</td>
<td>411,431</td>
<td>3,471,604</td>
</tr>
<tr>
<td>Health and human services</td>
<td>13,230,073</td>
<td>—</td>
<td>—</td>
<td>87,998</td>
<td>13,318,071</td>
</tr>
<tr>
<td>Economic development</td>
<td>242,953</td>
<td>—</td>
<td>—</td>
<td>400,557</td>
<td>643,510</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>249,692</td>
<td>—</td>
<td>—</td>
<td>376,750</td>
<td>626,442</td>
</tr>
<tr>
<td>Public safety, corrections, and regulation</td>
<td>1,694,345</td>
<td>—</td>
<td>—</td>
<td>397,251</td>
<td>2,291,596</td>
</tr>
<tr>
<td>Transportation</td>
<td>—</td>
<td>2,446,816</td>
<td>770,733</td>
<td>—</td>
<td>3,217,549</td>
</tr>
<tr>
<td>Agriculture</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>8,370</td>
<td>110,626</td>
</tr>
<tr>
<td>Capital outlay</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>270,882</td>
<td>270,882</td>
</tr>
<tr>
<td>Debt service:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Principal retirement</td>
<td>312,524</td>
<td>—</td>
<td>54,675</td>
<td>747</td>
<td>367,946</td>
</tr>
<tr>
<td>Interest and fees</td>
<td>248,168</td>
<td>—</td>
<td>38,883</td>
<td>1,037</td>
<td>286,088</td>
</tr>
<tr>
<td>Debt issuance costs</td>
<td>508</td>
<td>—</td>
<td>—</td>
<td>1,137</td>
<td>1,645</td>
</tr>
<tr>
<td><strong>Total expenditures</strong></td>
<td><strong>26,164,703</strong></td>
<td><strong>2,448,816</strong></td>
<td><strong>864,291</strong></td>
<td><strong>2,308,046</strong></td>
<td><strong>33,785,856</strong></td>
</tr>
<tr>
<td>Excess revenues over (under) expenditures</td>
<td>940,533</td>
<td>339,694</td>
<td>200,715</td>
<td>(868,086)</td>
<td>594,565</td>
</tr>
</tbody>
</table>

Other Financing Sources (Uses):

| Bonds issued | — | — | — | — | — |
| Other debt issued | 3,857 | 3,000 | — | 23,831 | 30,688 |
| Premium on debt issued | — | — | — | 16,338 | 16,338 |
| Capital leases | — | — | — | 26,745 | 26,745 |
| Sale of capital assets | 8,313 | 5,773 | 571 | 5,474 | 20,131 |
| Insurance recoveries | 411 | 5,303 | — | 923 | 6,537 |
| Transfers in (Note 9) | 625,932 | 85,906 | 1,321 | 1,071,483 | 1,784,222 |
| Transfers out (Note 9) | (820,013) | (255,040) | (322,243) | (520,999) | (1,718,555) |
| **Total other financing sources (uses)** | **17,889** | **155,158** | **320,351** | **983,755** | **1,336,076** |

Net change in fund balances:

| 958,333 | 184,536 | (119,636) | 107,699 | 1,130,932 |
| 953,509 | 383,302 | (15,362) | 2,766,045 | 4,087,494 |
| 13,356 | 947 | — | 756 | 15,059 |
| **Fund balances — June 30** | **$1,925,198** | **$568,785** | **$134,998** | **$2,874,500** | **$5,233,485** |

The accompanying Notes to the Financial Statements are an integral part of this statement.
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

For the Fiscal Year Ended June 30, 2006

Exhibit B-2a

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net change in fund balances - total governmental funds (see Exhibit B-2)</td>
<td>$1,130,932</td>
</tr>
<tr>
<td>Amounts reported for governmental activities in the Statement of Activities are different because:</td>
<td></td>
</tr>
<tr>
<td><strong>Capital outlays</strong> are reported as expenditures in governmental funds. However, in the Statement of Activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:</td>
<td></td>
</tr>
<tr>
<td>Capital outlays (including construction-in-progress)</td>
<td>$2,200,513</td>
</tr>
<tr>
<td>Less: Depreciation expense (excluding internal service funds)</td>
<td>(564,014)</td>
</tr>
<tr>
<td>Net capital outlay adjustment</td>
<td>1,636,499</td>
</tr>
<tr>
<td><strong>Proceeds from the sale of capital assets</strong> increase financial resources in the funds, whereas in the Statement of Activities only the gain or loss on the sale is reported. This adjustment reduces the proceeds by the book value of the capital assets sold.</td>
<td>(37,207)</td>
</tr>
<tr>
<td><strong>Donations of capital assets</strong> do not appear in the governmental funds because they are not financial resources, but increase net assets in the Statement of Activities.</td>
<td>14,582</td>
</tr>
<tr>
<td><strong>Long-term debt</strong> proceeds provide current financial resources to governmental funds, while the repayment of the related debt principal consumes those financial resources. These transactions, however, have no effect on net assets. Also, governmental funds report the effect of premiums and similar items when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. In the current period, these amounts consist of:</td>
<td></td>
</tr>
<tr>
<td>Debt issued or incurred:</td>
<td></td>
</tr>
<tr>
<td>Bonds and similar debt issued</td>
<td>(400,688)</td>
</tr>
<tr>
<td>Capital lease financings</td>
<td>(26,746)</td>
</tr>
<tr>
<td>Premiums on debt issued</td>
<td>(15,700)</td>
</tr>
<tr>
<td>Principal repayments:</td>
<td></td>
</tr>
<tr>
<td>Bonds, notes, and similar debt</td>
<td>367,783</td>
</tr>
<tr>
<td>Capital leases</td>
<td>163</td>
</tr>
<tr>
<td>Net debt adjustments</td>
<td>(75,187)</td>
</tr>
<tr>
<td><strong>Some revenues</strong> in the Statement of Activities do not provide current financial resources and, therefore, are deferred in the funds. Also, revenues related to prior periods that became available during the current period are reported in the funds but are eliminated in the Statement of Activities. This amount is the net adjustment.</td>
<td>(51,751)</td>
</tr>
<tr>
<td><strong>Some expenses</strong> reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not recognized in the funds. Also, some payments related to prior periods are recognized in the funds but are eliminated in the Statement of Activities. In the current period, the net adjustments consist of:</td>
<td></td>
</tr>
<tr>
<td>Accrued interest</td>
<td>(1,375)</td>
</tr>
<tr>
<td>Compensated absences (excluding internal service funds)</td>
<td>(53,499)</td>
</tr>
<tr>
<td>Workers compensation</td>
<td>234</td>
</tr>
<tr>
<td>Arbitrage rebate</td>
<td>(508)</td>
</tr>
<tr>
<td>Deferred death benefit</td>
<td>60</td>
</tr>
<tr>
<td>Cost settlement</td>
<td>(149,000)</td>
</tr>
<tr>
<td>Net pension obligation</td>
<td>481</td>
</tr>
<tr>
<td>Amortization of deferred amounts</td>
<td>24,403</td>
</tr>
<tr>
<td>Net expense accruals</td>
<td>(179,204)</td>
</tr>
<tr>
<td><strong>Inventories</strong> of governmental funds are recorded as expenditures when purchased but in the Statement of Activities are recorded as expenses when consumed.</td>
<td>15,059</td>
</tr>
<tr>
<td><strong>Internal service funds</strong> are used by management to charge the costs of certain activities to individual funds. The net revenues of internal service funds are included with governmental activities in the Statement of Activities (see Exhibit B-4).</td>
<td>8,340</td>
</tr>
<tr>
<td>Change in net assets - governmental activities (see Exhibit A-2)</td>
<td>$2,462,063</td>
</tr>
</tbody>
</table>

The accompanying Notes to the Financial Statements are an integral part of this statement.
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS

June 30, 2006
(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Business-type Activities -</th>
<th>Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment Compensation Fund</td>
<td>EPA Revolving Loan Fund</td>
</tr>
</tbody>
</table>

**Assets**

**Current Assets:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents (Note 3)</td>
<td>$166,745</td>
<td>$221,983</td>
<td>$18,500</td>
<td>$42,812</td>
<td>$446,990</td>
</tr>
<tr>
<td>Investments (Note 3)</td>
<td>—</td>
<td>4,268</td>
<td>—</td>
<td>49,454</td>
<td>53,722</td>
</tr>
<tr>
<td>Securities lending collateral (Note 3)</td>
<td>12,738</td>
<td>190,362</td>
<td>16,064</td>
<td>47,616</td>
<td>266,780</td>
</tr>
<tr>
<td>Receivables: (Note 4)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable, net</td>
<td>24,919</td>
<td>10,047</td>
<td>7,140</td>
<td>42,106</td>
<td></td>
</tr>
<tr>
<td>Intergovernmental receivables</td>
<td>—</td>
<td>103</td>
<td>—</td>
<td>103</td>
<td></td>
</tr>
<tr>
<td>Interest receivable</td>
<td>49</td>
<td>3,910</td>
<td>184</td>
<td>4,170</td>
<td></td>
</tr>
<tr>
<td>Premiums receivable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,257</td>
<td></td>
</tr>
<tr>
<td>Contributions receivable, net</td>
<td>359,285</td>
<td>—</td>
<td>—</td>
<td>359,285</td>
<td></td>
</tr>
<tr>
<td>Notes receivable, net (Note 4)</td>
<td>—</td>
<td>32,429</td>
<td>—</td>
<td>32,429</td>
<td></td>
</tr>
<tr>
<td>Due from fiduciary funds (Note 9)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Due from other funds (Note 9)</td>
<td>59</td>
<td>—</td>
<td>—</td>
<td>59</td>
<td></td>
</tr>
<tr>
<td>Due from component units (Note 17)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Inventories</td>
<td>—</td>
<td>501</td>
<td>—</td>
<td>501</td>
<td></td>
</tr>
<tr>
<td>Prepaid items</td>
<td>—</td>
<td>2,213</td>
<td>—</td>
<td>2,213</td>
<td></td>
</tr>
<tr>
<td><strong>Total current assets</strong></td>
<td><strong>563,795</strong></td>
<td><strong>453,035</strong></td>
<td><strong>44,795</strong></td>
<td><strong>150,820</strong></td>
<td><strong>1,212,445</strong></td>
</tr>
</tbody>
</table>

**Noncurrent Assets:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Restricted/designated cash and cash equivalents (Note 3)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,627</td>
<td>1,627</td>
</tr>
<tr>
<td>Investments (Note 3)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>462</td>
<td>462</td>
</tr>
<tr>
<td>Restricted investments (Note 3)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3,269</td>
<td>3,269</td>
</tr>
<tr>
<td>Notes receivable, net (Note 4)</td>
<td>—</td>
<td>513,141</td>
<td>—</td>
<td>513,141</td>
<td></td>
</tr>
<tr>
<td>Deferred charges</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>107</td>
<td>107</td>
</tr>
<tr>
<td>Capital assets-nondepreciable (Note 5)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>5,440</td>
<td>5,440</td>
</tr>
<tr>
<td>Capital assets-depreciable, net (Note 5)</td>
<td>—</td>
<td>110</td>
<td>625</td>
<td>46,854</td>
<td>47,589</td>
</tr>
<tr>
<td><strong>Total noncurrent assets</strong></td>
<td>—</td>
<td>513,251</td>
<td>625</td>
<td>57,759</td>
<td>571,635</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>563,795</strong></td>
<td><strong>966,286</strong></td>
<td><strong>51,420</strong></td>
<td><strong>208,579</strong></td>
<td><strong>1,784,080</strong></td>
</tr>
</tbody>
</table>

**Liabilities**

**Current Liabilities:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts payable and accrued liabilities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable</td>
<td>12,638</td>
<td>100</td>
<td>9,927</td>
<td>842</td>
<td>23,507</td>
</tr>
<tr>
<td>Accrued payroll</td>
<td>—</td>
<td>1</td>
<td>2</td>
<td>107</td>
<td>110</td>
</tr>
<tr>
<td>Intergovernmental payable</td>
<td>3,194</td>
<td>15</td>
<td>—</td>
<td>—</td>
<td>3,209</td>
</tr>
<tr>
<td>Claims payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>11,969</td>
<td>11,969</td>
</tr>
<tr>
<td>Other payables</td>
<td>—</td>
<td>—</td>
<td>5,277</td>
<td>—</td>
<td>5,277</td>
</tr>
<tr>
<td>Unemployment benefits payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>17,792</td>
<td>17,792</td>
</tr>
<tr>
<td>Obligations under securities lending</td>
<td>12,738</td>
<td>190,362</td>
<td>16,064</td>
<td>47,616</td>
<td>266,780</td>
</tr>
<tr>
<td>Interest payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>33</td>
<td>33</td>
</tr>
<tr>
<td>Due to other funds (Note 9)</td>
<td>—</td>
<td>8</td>
<td>13,628</td>
<td>45</td>
<td>13,679</td>
</tr>
<tr>
<td>Unearned revenue</td>
<td>9,956</td>
<td>—</td>
<td>—</td>
<td>7,001</td>
<td>16,957</td>
</tr>
<tr>
<td>Deposits payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>28</td>
<td>28</td>
</tr>
<tr>
<td>Notes Payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>112</td>
<td>112</td>
</tr>
<tr>
<td>Bonds payable - current</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>280</td>
<td>280</td>
</tr>
<tr>
<td>Compensated absences - current</td>
<td>—</td>
<td>39</td>
<td>—</td>
<td>156</td>
<td>195</td>
</tr>
<tr>
<td><strong>Total current liabilities</strong></td>
<td><strong>56,318</strong></td>
<td><strong>190,525</strong></td>
<td><strong>44,896</strong></td>
<td><strong>68,189</strong></td>
<td><strong>359,928</strong></td>
</tr>
</tbody>
</table>

**Noncurrent Liabilities:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Notes payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,345</td>
<td>1,345</td>
</tr>
<tr>
<td>Bonds payable, net</td>
<td>—</td>
<td>382</td>
<td>624</td>
<td>8,520</td>
<td>9,522</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,706</td>
<td>2,706</td>
</tr>
<tr>
<td><strong>Total noncurrent liabilities</strong></td>
<td>—</td>
<td>382</td>
<td>624</td>
<td>12,571</td>
<td>13,477</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td><strong>56,318</strong></td>
<td><strong>190,907</strong></td>
<td><strong>54,420</strong></td>
<td><strong>80,760</strong></td>
<td><strong>373,405</strong></td>
</tr>
</tbody>
</table>

**Net Assets**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Invested in capital assets, net of related debt</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>43,461</td>
<td>43,461</td>
</tr>
<tr>
<td>Restricted for:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital outlay</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,629</td>
<td>2,629</td>
</tr>
<tr>
<td>Other purposes</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,102</td>
<td>1,102</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>507,477</td>
<td>775,289</td>
<td>625</td>
<td>80,627</td>
<td>1,363,018</td>
</tr>
<tr>
<td><strong>Total Net Assets</strong></td>
<td>$507,477</td>
<td>$775,379</td>
<td>($625)</td>
<td>$127,819</td>
<td>$1,410,675</td>
</tr>
</tbody>
</table>

The accompanying Notes to the Financial Statements are an integral part of this statement.
<table>
<thead>
<tr>
<th>Governmental Activities — Internal Service Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 83,800</td>
</tr>
<tr>
<td>20,916</td>
</tr>
<tr>
<td>39,109</td>
</tr>
<tr>
<td>9,774</td>
</tr>
<tr>
<td>28</td>
</tr>
<tr>
<td>15,699</td>
</tr>
<tr>
<td>1,080</td>
</tr>
<tr>
<td>315</td>
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<tr>
<td>13,448</td>
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<td>184,527</td>
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<td></td>
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<td>4,109</td>
</tr>
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<td>91,627</td>
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<td>95,736</td>
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<tr>
<td>260,263</td>
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<tr>
<td></td>
</tr>
<tr>
<td>3,888</td>
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<tr>
<td>429</td>
</tr>
<tr>
<td>118</td>
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<td>39,109</td>
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<td>1,224</td>
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<td>6,778</td>
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<td>326</td>
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<tr>
<td>52,810</td>
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<td></td>
</tr>
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<td></td>
</tr>
<tr>
<td></td>
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<tr>
<td>3,535</td>
</tr>
<tr>
<td>3,535</td>
</tr>
<tr>
<td>56,445</td>
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<tr>
<td>95,736</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>108,082</td>
</tr>
<tr>
<td>203,818</td>
</tr>
</tbody>
</table>

*Exhibit B-3*
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Business-type Activities — Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment Compensation Fund</td>
</tr>
<tr>
<td>EPA Revolving Loan Fund</td>
</tr>
<tr>
<td>N.C. State Lottery Fund</td>
</tr>
<tr>
<td>Other Enterprise Funds</td>
</tr>
<tr>
<td>Total Enterprise Funds</td>
</tr>
</tbody>
</table>

### Operating Revenues:

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employer unemployment contributions</td>
<td>$1,067,977</td>
<td>$—</td>
<td>$—</td>
<td>$—</td>
<td>$1,067,977</td>
</tr>
<tr>
<td>Federal funds</td>
<td>33,380</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>33,380</td>
</tr>
<tr>
<td>Sales and services</td>
<td>—</td>
<td>2,628</td>
<td>215,428</td>
<td>993</td>
<td>219,049</td>
</tr>
<tr>
<td>Sales and services used as security for bonds, net</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,377</td>
<td>2,377</td>
</tr>
<tr>
<td>Interest earnings on loans</td>
<td>—</td>
<td>12,609</td>
<td>—</td>
<td>—</td>
<td>12,609</td>
</tr>
<tr>
<td>Rental and lease earnings</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>5,537</td>
<td>5,537</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>—</td>
<td>—</td>
<td>1,478</td>
<td>45,014</td>
<td>46,492</td>
</tr>
<tr>
<td>Insurance premiums</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>14,860</td>
<td>14,860</td>
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<tr>
<td>Miscellaneous</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>183</td>
<td>183</td>
</tr>
<tr>
<td><strong>Total operating revenues</strong></td>
<td><strong>1,101,357</strong></td>
<td><strong>15,237</strong></td>
<td><strong>216,066</strong></td>
<td><strong>68,964</strong></td>
<td><strong>1,402,464</strong></td>
</tr>
</tbody>
</table>

### Operating Expenses:

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal services</td>
<td>—</td>
<td>3,107</td>
<td>5,700</td>
<td>26,725</td>
<td>35,532</td>
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<tr>
<td>Supplies and materials</td>
<td>—</td>
<td>13</td>
<td>252</td>
<td>1,530</td>
<td>1,796</td>
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<tr>
<td>Services</td>
<td>—</td>
<td>913</td>
<td>25,541</td>
<td>14,013</td>
<td>40,467</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>424</td>
<td>424</td>
</tr>
<tr>
<td>Depreciation/amortization</td>
<td>—</td>
<td>21</td>
<td>76</td>
<td>2,983</td>
<td>3,080</td>
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<tr>
<td>Lottery prizes</td>
<td>—</td>
<td>—</td>
<td>118,974</td>
<td>—</td>
<td>118,974</td>
</tr>
<tr>
<td>Claims</td>
<td>848,359</td>
<td>—</td>
<td>—</td>
<td>9,811</td>
<td>9,811</td>
</tr>
<tr>
<td>Unemployment benefits</td>
<td></td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>848,359</td>
</tr>
<tr>
<td>Insurance and bonding</td>
<td>—</td>
<td>—</td>
<td>4</td>
<td>3,705</td>
<td>3,709</td>
</tr>
<tr>
<td>Other</td>
<td>—</td>
<td>250</td>
<td>2,142</td>
<td>3,718</td>
<td>6,110</td>
</tr>
<tr>
<td><strong>Total operating expenses</strong></td>
<td><strong>848,359</strong></td>
<td><strong>4,304</strong></td>
<td><strong>152,889</strong></td>
<td><strong>62,909</strong></td>
<td><strong>1,088,261</strong></td>
</tr>
<tr>
<td><strong>Operating income (loss)</strong></td>
<td><strong>252,998</strong></td>
<td><strong>10,933</strong></td>
<td><strong>64,217</strong></td>
<td><strong>6,055</strong></td>
<td><strong>334,203</strong></td>
</tr>
</tbody>
</table>

### Nonoperating Revenues (Expenses):

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Noncapital grants</td>
<td>1,913</td>
<td>40,260</td>
<td>—</td>
<td>222</td>
<td>42,395</td>
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<tr>
<td>Noncapital gifts</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>163</td>
<td>163</td>
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<tr>
<td>Investment earnings</td>
<td>3,997</td>
<td>14,254</td>
<td>808</td>
<td>2,066</td>
<td>21,125</td>
</tr>
<tr>
<td>Interest and fees</td>
<td>(782)</td>
<td>(31)</td>
<td>(31)</td>
<td>(433)</td>
<td>(1,246)</td>
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<tr>
<td>Insurance recoveries</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>389</td>
<td>389</td>
</tr>
<tr>
<td>Gain (loss) on sale of equipment</td>
<td>—</td>
<td>(2)</td>
<td>(2)</td>
<td>4</td>
<td>2</td>
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<tr>
<td>Miscellaneous</td>
<td>(804)</td>
<td>(7,108)</td>
<td>(405)</td>
<td>(1,974)</td>
<td>(10,291)</td>
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<tr>
<td><strong>Total nonoperating revenues (expenses)</strong></td>
<td><strong>4,324</strong></td>
<td><strong>47,404</strong></td>
<td><strong>372</strong></td>
<td><strong>437</strong></td>
<td><strong>52,537</strong></td>
</tr>
</tbody>
</table>

### Income (loss) before contributions and transfers:

- **257,322**
- **58,337**
- **64,589**
- **6,492**
- **386,740**
- **258**
- **258**
- **10,841**
- **8,686**
- **2,155**

### Change in net assets:

- **249,022**
- **88,750**
- **3,248**
- **319,020**

### Net assets — July 1, as restated (Note 22):

- **258,455**
- **708,629**
- **124,571**
- **1,091,655**

### Net assets — June 30:

- **$507,477**
- **$775,379**
- **$127,819**
- **$1,410,675**

The accompanying Notes to the Financial Statements are an integral part of this statement.
### Governmental Activities

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<tr>
<th>Funds</th>
<th></th>
</tr>
</thead>
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<td>8</td>
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<td></td>
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<td>18,666</td>
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<td>569</td>
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<td>45,255</td>
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<td>14,447</td>
</tr>
<tr>
<td></td>
<td>105,173</td>
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<tr>
<td></td>
<td>511</td>
</tr>
<tr>
<td></td>
<td>26,966</td>
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<tr>
<td></td>
<td>1,242</td>
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<tr>
<td></td>
<td>9,850</td>
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<tr>
<td></td>
<td>37,978</td>
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<tr>
<td></td>
<td>241,442</td>
</tr>
<tr>
<td></td>
<td>6,413</td>
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<td></td>
<td>1,838</td>
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<td></td>
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<tr>
<td></td>
<td>132</td>
</tr>
<tr>
<td></td>
<td>(952)</td>
</tr>
<tr>
<td></td>
<td>(1,432)</td>
</tr>
<tr>
<td></td>
<td>(414)</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,999</td>
</tr>
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<td></td>
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</tr>
<tr>
<td></td>
<td>2,501</td>
</tr>
<tr>
<td></td>
<td>(160)</td>
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<tr>
<td></td>
<td>8,340</td>
</tr>
<tr>
<td></td>
<td>195,478</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>$</td>
<td>203,818</td>
</tr>
</tbody>
</table>
## STATEMENT OF CASH FLOWS
### PROPRIETARY FUNDS
For the Fiscal Year Ended June 30, 2006
(Dollars in Thousands)

### Business-type Activities — Enterprise Funds

<table>
<thead>
<tr>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Receipts from customers</td>
<td>$1,077,312</td>
<td>$2,628</td>
<td>$190,805</td>
<td>$65,684</td>
</tr>
<tr>
<td>Receipts from federal agencies</td>
<td>33,380</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Receipts from other funds</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Payments to suppliers</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Payments to employees</td>
<td>—</td>
<td>(1,010)</td>
<td>(7,975)</td>
<td>(21,972)</td>
</tr>
<tr>
<td>Payments for prizes, benefits and claims</td>
<td>(851,488)</td>
<td>—</td>
<td>(108,109)</td>
<td>(9,186)</td>
</tr>
<tr>
<td>Payments to other funds</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(226)</td>
</tr>
<tr>
<td>Other receipts (payments)</td>
<td>—</td>
<td>(134)</td>
<td>—</td>
<td>(1,371)</td>
</tr>
<tr>
<td>Net cash flows provided (used) by operating activities</td>
<td>259,204</td>
<td>(1,521)</td>
<td>70,054</td>
<td>7,315</td>
</tr>
</tbody>
</table>

### Cash Provided From (Used For)
#### Noncapital Financing Activities:
- Grant receipts (refunds) .................................................. 1,913 40,179  —  222 42,314
- Proceeds from short-term borrowing .................................. 333,319 —  — — 333,319
- Principal payments from short-term borrowing ..................... (447,006) — — — (447,009)
- Interest expense and issuance cost .................................. (782) — (31) — (813)
- Transfers from other funds ........................................... 6,666  — — 2,087 10,773
- Transfers to other funds ............................................. (8,300) (273) (51,042) (5,657) (85,272)
- Gifts ................................................................. — — — 163 163
- Total cash provided from (used for) noncapital financing activities ...........................................(120,859) 48,592 (51,073) (3,185) (126,525)

### Cash Provided From (Used For)
#### Capital Financing Activities:
- Acquisition and construction of capital assets .................... — — (700) (752) (1,452)
- Proceeds from the sale of capital assets ........................... — — — — 149
- Capital contributions .................................................. — — — — 40
- Principal paid on capital debt ....................................... — — — (270) (270)
- Interest paid on capital debt ....................................... — — — (364) (364)
- Payment to bond escrow agent ....................................... — — — (46) (46)
- Insurance recoveries .................................................. — — — 389 389
- Total cash provided from (used for) capital financing activities .................................................. — — (700) (854) (1,554)

### Cash Provided From (Used For)
#### Investment Activities:
- Purchase of non-State Treasurer investments ..................... — — — (179) (179)
- Purchase into State Treasurer investment pool ..................... — (1,684) — — (12,000) (13,684)
- Redemptions from State Treasurer investment pool .................. — 2 — — — 2
- Loan issuances ......................................................... — (85,438) — — (85,438)
- Loan repayments — interest .......................................... — 12,101 — — 12,101
- Loan repayments — principal ........................................ — 31,970 — — 31,970
- Investment earnings ................................................... 3,168 6,908 219 1,185 11,480
- Total cash provided from (used for) investment activities ........ 3,168 (36,141) 219 (10,994) (43,748)

- Net increase (decrease) in cash and cash equivalents ............ 141,513 10,930 18,500 (7,718) 163,225
- Cash and cash equivalents at July 1, as restated ................. 25,232 211,033 — — 51,957 288,222
- Cash and cash equivalents at June 30 .............................. $166,745 $221,963 $18,500 $44,239 $451,447

The accompanying Notes to the Financial Statements are an integral part of this statement.
| Governmental Activities — Internal Service Funds |
|---|---|
| $ | 49,811 |
| | 208,308 |
| | (166,632) |
| | (45,012) |
| | (1,169) |
| | (11,157) |
| | 133 |
| | 34,282 |
| | 2,501 |
| | (160) |
| | 2,341 |
| | (32,763) |
| | 2,173 |
| | 132 |
| | (30,458) |
| | 916 |
| | 916 |
| | 7,081 |
| | 56,719 |
| | $ 63,800 |
# STATEMENT OF CASH FLOWS
## PROPRIETARY FUNDS
For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Business-type Activities — Enterprise Funds</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating income (loss)</td>
<td>$252,998</td>
<td>$10,933</td>
<td>$64,217</td>
<td>$6,055</td>
<td>$334,203</td>
</tr>
<tr>
<td>Adjustments to reconcile operating income</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>to net cash flows from operating activities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation/amortization</td>
<td>—</td>
<td>21</td>
<td>—</td>
<td>76</td>
<td>3,080</td>
</tr>
<tr>
<td>Interest earnings on loans classified as investing activity</td>
<td>—</td>
<td>(12,609)</td>
<td>—</td>
<td>—</td>
<td>(12,609)</td>
</tr>
<tr>
<td>Restatements and adjustments to cash</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>45</td>
</tr>
<tr>
<td>Nonoperating miscellaneous income (expense)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>13</td>
<td>13</td>
</tr>
<tr>
<td>(Increases) decreases in assets:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receivables</td>
<td>3,848</td>
<td>—</td>
<td>(10,047)</td>
<td>(2,853)</td>
<td>(9,052)</td>
</tr>
<tr>
<td>Due from other funds</td>
<td>63</td>
<td>—</td>
<td>—</td>
<td>1</td>
<td>54</td>
</tr>
<tr>
<td>Due from fiduciary funds</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Due from component units</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
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<td>Inventories</td>
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<td>—</td>
<td>74</td>
<td>74</td>
</tr>
<tr>
<td>Prepaid items</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(483)</td>
<td>(483)</td>
</tr>
<tr>
<td>Increases (decreases) in liabilities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable and accrued liabilities</td>
<td>3,574</td>
<td>37</td>
<td>15,206</td>
<td>741</td>
<td>19,558</td>
</tr>
<tr>
<td>Due to other funds</td>
<td>—</td>
<td>(1)</td>
<td>78</td>
<td>10</td>
<td>87</td>
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<td>Unemployment benefits payable</td>
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<td>—</td>
<td>—</td>
<td>(3,507)</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>—</td>
<td>98</td>
<td>524</td>
<td>693</td>
<td>1,315</td>
</tr>
<tr>
<td>Unearned revenue</td>
<td>2,228</td>
<td>—</td>
<td>—</td>
<td>85</td>
<td>2,313</td>
</tr>
<tr>
<td>Deposits payable</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(49)</td>
<td>(49)</td>
</tr>
<tr>
<td>Total cash provided from operations</td>
<td>$259,204</td>
<td>$(1,521)</td>
<td>$70,054</td>
<td>$7,315</td>
<td>$335,052</td>
</tr>
</tbody>
</table>

## Noncash Investing, Capital, and Financing Activities:

Noncash distributions from the State Treasurer

<table>
<thead>
<tr>
<th>Description</th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-Term Investment Portfolio and/or other agents</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>$2,361</td>
<td>$2,361</td>
</tr>
<tr>
<td>Donated assets (fair market value)</td>
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<td>—</td>
<td>—</td>
<td>218</td>
<td>218</td>
</tr>
<tr>
<td>Transferred assets</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>68</td>
<td>68</td>
</tr>
<tr>
<td>Assets acquired through the assumption of liability</td>
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<td>190,362</td>
<td>16,064</td>
<td>47,616</td>
<td>266,780</td>
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<td>Change in fair value of investments</td>
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<td>(3,270)</td>
</tr>
<tr>
<td>Description</td>
<td>Amount</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-------------</td>
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<td></td>
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<tr>
<td>$</td>
<td>6,413</td>
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<td>26,986</td>
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<td>7,327</td>
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<td></td>
<td>(125)</td>
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<tr>
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<td>1,744</td>
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<td>(346)</td>
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<td></td>
<td>532</td>
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<tr>
<td></td>
<td>3,857</td>
<td></td>
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<tr>
<td>$</td>
<td>34,282</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>(1,145)</td>
<td></td>
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<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>39,109</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>(1,740)</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>
## STATEMENT OF FIDUCIARY NET ASSETS

### FIDUCIARY FUNDS

**June 30, 2006**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Assets</th>
<th>Pension and Other Employee Benefit Trust Funds</th>
<th>Investment Trust Fund</th>
<th>Private-Purpose Trust Funds</th>
<th>Agency Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents (Note 3)</td>
<td>$487,927</td>
<td>$6,655</td>
<td>$97,714</td>
<td>$2,543,046</td>
</tr>
<tr>
<td>Investments (Note 3):</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Annuity contracts</td>
<td>923,867</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. government securities</td>
<td></td>
<td></td>
<td>1,564</td>
<td></td>
</tr>
<tr>
<td>State and municipal securities</td>
<td></td>
<td>99</td>
<td></td>
<td></td>
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<tr>
<td>Corporate bonds</td>
<td></td>
<td></td>
<td>50,827</td>
<td></td>
</tr>
<tr>
<td>Corporate stocks</td>
<td></td>
<td></td>
<td>1,008</td>
<td></td>
</tr>
<tr>
<td>Mutual funds</td>
<td>3,058,476</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td></td>
<td></td>
<td>65,497</td>
<td></td>
</tr>
<tr>
<td>State Treasurer investment pool</td>
<td>68,334,472</td>
<td>192,963</td>
<td></td>
<td>38,477</td>
</tr>
<tr>
<td>Securities lending collateral (Note 3)</td>
<td>14,134,334</td>
<td>147,199</td>
<td>676</td>
<td>1,737,212</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxes receivable</td>
<td></td>
<td></td>
<td></td>
<td>200,000</td>
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<tr>
<td>Accounts receivable</td>
<td>35,402</td>
<td></td>
<td></td>
<td>3,224</td>
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<tr>
<td>Intergovernmental receivables</td>
<td>13,050</td>
<td></td>
<td></td>
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<tr>
<td>Interest receivable</td>
<td>2,278</td>
<td>1,214</td>
<td>2</td>
<td>288</td>
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<tr>
<td>Contributions receivable</td>
<td>113,133</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Due from other funds (Note 9)</td>
<td>28,717</td>
<td></td>
<td></td>
<td>12,871</td>
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<tr>
<td>Notes receivable</td>
<td>169,044</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Inventories</td>
<td></td>
<td></td>
<td></td>
<td>301</td>
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<tr>
<td>Sureties</td>
<td></td>
<td></td>
<td>988,443</td>
<td>96,901</td>
</tr>
<tr>
<td>Capital assets-depreciable, net</td>
<td>29</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>87,292,229</strong></td>
<td><strong>348,031</strong></td>
<td><strong>1,153,955</strong></td>
<td><strong>4,674,622</strong></td>
</tr>
</tbody>
</table>

| Liabilities | | | | |
| Accounts payable and accrued liabilities: | | | | |
| Accounts payable | 8,985 | | | 941 |
| Intergovernmental payables | | | | 639,233 |
| Benefits payable | 328,408 | | | |
| Medical claims payable | 170,465 | | | |
| Obligations under securities lending | 14,134,334 | 147,199 | | 1,737,212 |
| Due to other funds (Note 9) | 28 | | | |
| Unearned revenue | 6,312 | | | |
| Deposits payable | | | | 1,682 |
| Funds held for others | | | | 2,295,554 |
| Compensated absences | 119 | | | |
| **Total Liabilities** | **14,648,651** | **147,199** | **676** | **4,674,622** |

| Net Assets | | | | |
| Held in trust for: | | | | |
| Employees' pension and other benefits | 72,643,579 | | | |
| Pool participants | | 200,832 | | |
| Individuals, organizations and other governments | | | 1,153,319 | |
| **Total Net Assets** | **$72,643,579** | **$200,832** | **$1,153,319** | **$** |

*The accompanying Notes to the Financial Statements are an integral part of this statement.*
# STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

## FIDUCIARY FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Pension and Other Employee Benefit Trust Funds</th>
<th>Investment Trust Fund</th>
<th>Private-Purpose Trust Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Additions:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employer</td>
<td>$ 2,833,806</td>
<td>$</td>
</tr>
<tr>
<td>Members</td>
<td>1,584,177</td>
<td></td>
</tr>
<tr>
<td>Trustee deposits</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Other contributions</td>
<td>47,399</td>
<td></td>
</tr>
<tr>
<td><strong>Total contributions</strong></td>
<td>4,465,385</td>
<td></td>
</tr>
<tr>
<td>Investment income:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment earnings (loss)</td>
<td>5,632,740</td>
<td>21,724</td>
</tr>
<tr>
<td>Less investment expenses</td>
<td>(998,292)</td>
<td>(10,917)</td>
</tr>
<tr>
<td><strong>Net investment income (loss)</strong></td>
<td>4,634,448</td>
<td>10,807</td>
</tr>
<tr>
<td>Pool share transactions:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reinvestment of dividends</td>
<td>10,807</td>
<td></td>
</tr>
<tr>
<td>Net share purchases/(redemptions)</td>
<td></td>
<td>(273,118)</td>
</tr>
<tr>
<td><strong>Net pool share transactions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other additions:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>4,793</td>
<td></td>
</tr>
<tr>
<td>Interest earnings on loans</td>
<td>7,912</td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>1,898</td>
<td></td>
</tr>
<tr>
<td><strong>Total other additions</strong></td>
<td>14,603</td>
<td></td>
</tr>
<tr>
<td><strong>Total additions</strong></td>
<td>9,416,436</td>
<td>(251,504)</td>
</tr>
</tbody>
</table>

| Deductions:                                   |                       |                           |
| Claims and benefits                           | 5,189,664             |                           |                           |
| Medical insurance premiums for retirees       | 411,760               |                           |                           |
| Refund of contributions                       | 142,283               |                           |                           |
| Distributions paid and payable                | 10,807                |                           |                           |
| Payments in accordance with trust arrangements| 114,845               |                           |                           |
| Administrative expenses                       | 96,765                |                           |                           |
| Other deductions                              | 173                   |                           |                           |
| **Total deductions**                          | 5,840,625             | 10,807                    | 114,851                   |
| Change in net assets                          | 3,575,811             | (262,311)                 | 26,057                    |
| Net assets — July 1                           | 89,067,767            | 463,143                   | 1,127,262                 |
| Net assets — June 30                          | $ 72,643,578          | $ 200,832                 | $ 1,153,319               |

The accompanying Notes to the Financial Statements are an integral part of this statement.
# NOTES TO THE FINANCIAL STATEMENTS

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<th>Description</th>
<th>Page</th>
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<td></td>
<td>C. Measurement Focus and Basis of Accounting</td>
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<td>78</td>
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<td>E. Investments</td>
<td>78</td>
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<td></td>
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<td>78</td>
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</tr>
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<td></td>
<td>H. Inventories and Prepaid Items</td>
<td>78</td>
</tr>
<tr>
<td></td>
<td>I. Restricted/Designated Assets</td>
<td>78</td>
</tr>
<tr>
<td></td>
<td>J. Capital Assets</td>
<td>78</td>
</tr>
<tr>
<td></td>
<td>K. Tax Refund Liabilities</td>
<td>79</td>
</tr>
<tr>
<td></td>
<td>L. Compensated Absences</td>
<td>79</td>
</tr>
<tr>
<td></td>
<td>M. Long-Term Liabilities</td>
<td>79</td>
</tr>
<tr>
<td></td>
<td>N. Sureties</td>
<td>80</td>
</tr>
<tr>
<td></td>
<td>O. Net Assets/Fund Balance</td>
<td>80</td>
</tr>
<tr>
<td></td>
<td>P. Revenues and Expenses</td>
<td>80</td>
</tr>
<tr>
<td></td>
<td>Q. Food Stamps</td>
<td>80</td>
</tr>
<tr>
<td>2</td>
<td>Stewardship, Compliance, and Accountability</td>
<td>81</td>
</tr>
<tr>
<td>3</td>
<td>Deposits and Investments</td>
<td>82</td>
</tr>
<tr>
<td></td>
<td>A. Deposits and Investments with State Treasurer</td>
<td>82</td>
</tr>
<tr>
<td></td>
<td>B. Deposits Outside the State Treasurer</td>
<td>87</td>
</tr>
<tr>
<td></td>
<td>C. Investments Outside the State Treasurer</td>
<td>88</td>
</tr>
<tr>
<td>4</td>
<td>Receivables</td>
<td>94</td>
</tr>
<tr>
<td>5</td>
<td>Capital Assets</td>
<td>96</td>
</tr>
<tr>
<td>6</td>
<td>Short-Term Debt</td>
<td>100</td>
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<tr>
<td>7</td>
<td>Long-Term Liabilities</td>
<td>101</td>
</tr>
<tr>
<td></td>
<td>A. Changes in Long-Term Liabilities</td>
<td>101</td>
</tr>
<tr>
<td></td>
<td>B. Bonds, Certificates of Participation, and Notes Payable</td>
<td>103</td>
</tr>
<tr>
<td></td>
<td>C. Bonds Authorized but Unissued</td>
<td>103</td>
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<tr>
<td></td>
<td>D. Demand Bonds</td>
<td>103</td>
</tr>
<tr>
<td></td>
<td>E. Interest Rate and Basis Swaps</td>
<td>107</td>
</tr>
<tr>
<td></td>
<td>F. Swaptions</td>
<td>113</td>
</tr>
<tr>
<td></td>
<td>G. Debt Service Requirements</td>
<td>114</td>
</tr>
<tr>
<td></td>
<td>H. Bond Defeasances</td>
<td>116</td>
</tr>
<tr>
<td></td>
<td>I. Bond Redemptions</td>
<td>116</td>
</tr>
<tr>
<td>8</td>
<td>Lease Obligations—Operating and Capital</td>
<td>117</td>
</tr>
<tr>
<td>9</td>
<td>Interfund Balances and Transfers</td>
<td>118</td>
</tr>
<tr>
<td></td>
<td>A. Interfund Balances</td>
<td>118</td>
</tr>
<tr>
<td></td>
<td>B. Interfund Transfers</td>
<td>119</td>
</tr>
<tr>
<td>10</td>
<td>Fund Balance Reserves and Designations</td>
<td>120</td>
</tr>
<tr>
<td>11</td>
<td>Retirement Plans</td>
<td>121</td>
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<tr>
<td></td>
<td>A. Plan Descriptions and Contribution Information</td>
<td>121</td>
</tr>
<tr>
<td></td>
<td>B. Summary of Significant Accounting Policies and Plan Asset Matters</td>
<td>124</td>
</tr>
<tr>
<td></td>
<td>C. Actuarial Methods and Assumptions</td>
<td>124</td>
</tr>
<tr>
<td></td>
<td>D. Annual Pension Cost and Net Pension Obligation</td>
<td>125</td>
</tr>
<tr>
<td></td>
<td>E. Optional Retirement Plan</td>
<td>127</td>
</tr>
<tr>
<td></td>
<td>F. Special Separation Allowance</td>
<td>127</td>
</tr>
</tbody>
</table>

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**DETAIL NOTES ON ALL FUNDS AND ACTIVITIES**
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A. Financial Reporting Entity

The accompanying government-wide financial statements present the State of North Carolina and its component units. The State of North Carolina, as primary government, consists of all organizations that make up its legal entity. All funds, organizations, agencies, boards, commissions, and authorities that are not legally separate are, for financial reporting purposes, part of the primary government. The primary government has a separately elected governing body (the General Assembly) and the primary government must be both legally separate and fiscally independent. Component units are legally separate entities for which the State is financially accountable. Accountability is defined as the State’s substantive appointment of a majority of the component unit’s governing board. Furthermore, to be financially accountable, the State must be able to impose its will upon the component unit or there must be a possibility that the component unit may provide specific financial benefits to, or impose specific financial burdens on, the State. Financial accountability also exists when an organization is fiscally dependent upon the State. The State’s defined benefit pension plans, deferred compensation plans, and other employee benefit plans, being fiduciary in nature, were not evaluated as potential component units but instead are reported as fiduciary funds.

The State’s component units are either blended or discretely presented. The blended component unit is so intertwined with the State that it is, in substance, the same as the State and, therefore, is reported as if it was part of the State primary government. The “Component Units” column in the accompanying financial statements includes the financial data of the State’s discretely presented component units. They are combined and reported in a separate column in the government-wide financial statements to emphasize their legal separateness from the State.

Blended Component Unit

The North Carolina Infrastructure Finance Corporation

The North Carolina Infrastructure Finance Corporation (Corporation) was created by the General Assembly and organized as a separate not-for-profit corporation. It is managed by a three-member board appointed by the State Treasurer. The Corporation is authorized to issue tax-exempt debt to finance the acquisition, construction, repair and renovation of State facilities and related infrastructure. The debt obligations are secured by lease-purchase agreements or installment financing contracts with the State, which constitute the imposition of a financial burden on the State. The substance of the financing agreements is that the assets and debt are those of the State (lessee). The Corporation is reported with the State’s governmental funds since it provides services entirely to the State.

Discretely Presented Component Units - Major

The Golden LEAF (Long-term Economic Advancement Foundation), Inc.

The Golden LEAF, Inc. (Foundation) is a legally separate not-for-profit corporation ordered to be created by the Consent Decree and Final Judgment in the State of North Carolina vs. Philip Morris, et al. The Foundation was established to receive and distribute fifty percent of the tobacco settlement funds allocated to North Carolina, such funds to be used to provide economic impact assistance to economically affected or tobacco-dependent regions of North Carolina. The Foundation is governed by a fifteen-member board, all of whom are appointed by either the Governor, President Pro Tempore of the Senate, or the Speaker of the House. The State assigned fifty percent of its share of the settlement to the Foundation, creating a financial benefit/burden relationship.

University of North Carolina System

The Board of Governors of the consolidated University of North Carolina (UNC) System is a legally separate body, composed of thirty-two members elected by the General Assembly. The Board of Governors establishes system-wide administrative policies while budgetary decisions are exercised at the State level. Within the consolidated System are UNC-General Administration, which is the administrative arm of the Board of Governors; the sixteen constituent universities; and the University of North Carolina Health Care System (UNCHCS). Each of the sixteen universities, in turn, is governed by its own separate board of trustees that is responsible for the operations of that campus only. UNCHCS is governed by a separate board of directors. Funding for the UNC System is accomplished by State appropriations, tuition and fees, sales and services, federal grants, state grants, and private donations and grants.

Also included in the System are the financial data of the universities’ significant fund-raising foundations (and similarly affiliated organizations). Although the universities do not control the timing or amount of receipts from their foundations, the majority of resources (or income thereon) that the foundations hold and invest are restricted to the activities of the respective universities by the donors. Because these restricted resources held by the foundations can only be used by, or for the benefit of, the specific universities, the foundations are considered component units of the universities and are included in the universities’ financial statements. The foundations are private not-for-profit organizations that report under Financial Accounting Standards Board pronouncements. As such, certain revenue recognition criteria and presentation features are different from that of the Governmental Accounting Standards Board. The foundations’ financial statement formats were modified to make them compatible with the universities’ financial statement formats.
NOTES TO THE FINANCIAL STATEMENTS

The following constituent institutions comprise the UNC System for financial reporting purposes:

- UNC General Administration
- Appalachian State University
- East Carolina University
- Elizabeth City State University
- Fayetteville State University
- North Carolina Agricultural and Technical State University
- North Carolina Central University
- North Carolina School of the Arts
- North Carolina State University
- University of North Carolina at Asheville
- University of North Carolina at Chapel Hill
- University of North Carolina at Charlotte
- University of North Carolina at Greensboro
- University of North Carolina at Pembroke
- University of North Carolina at Wilmington
- Western Carolina University
- Winston-Salem State University
- University of North Carolina Health Care System

The following are the State’s 58 community colleges:

- Avance Comm. College
- Beaufort County Comm. College
- Blue Ridge Comm. College
- Caldwell Comm. College and Tech. Institute
- Carteret Comm. College
- Central Carolina Comm. College
- Cleveland Comm. College
- College of The Albemarle
- Davidson County Comm. College
- Edgecombe Comm. College
- Forsyth Technical Comm. College
- Guilford Technical Comm. College
- Haywood Comm. College
- James Sprunt Comm. College
- Lenoir Comm. College
- Mayland Comm. College
- Mitchell Comm. College
- Nash Comm. College
- Piedmont Comm. College
- Randolph Comm. College
- Roanoke-Chowan Comm. College
- Rockingham Comm. College
- Sampson Comm. College
- South Piedmont Comm. College
- Southwestern Comm. College
- Surry Comm. College
- Vance-Grassville Comm. College
- Wayne Comm. College
- Wilkes Comm. College
- Asheville-Buncombe Technical Comm. College
- Bladen Community College
- Brunswick Comm. College
- Cape Fear Comm. College
- Catawba Valley Comm. College
- Central Piedmont Comm. College
- Coastal Carolina Comm. College
- Craven Comm. College
- Durham Technical Comm. College
- Fayetteville Technical Comm. College
- Gaston College
- Halifax Comm. College
- Isothermal Comm. College
- Johnston Comm. College
- Martin Comm. College
- McDowell Technical Comm. College
- Montgomery Comm. College
- Pamlico Comm. College
- Pitt Comm. College
- Richmond Comm. College
- Robeson Comm. College
- Rowan-Cabarrus Comm. College
- Sandhills Comm. College
- Southeastern Comm. College
- Stanly Comm. College
- Tri-County Comm. College
- Wake Technical Comm. College
- Western Piedmont Comm. College
- Wilson Technical Comm. College

Community Colleges

There are currently 58 community colleges located throughout the State of North Carolina. Each is a separate component unit of the reporting entity and is legally separate. The State does not appoint a voting majority of each community college board of trustees. However, the State is financially accountable for these institutions because the State Board of Community Colleges (the Board) approves the budgeting of state and federal funds, the associated budget revisions, and the selection of the chief administrative officer of each individual community college. The Board is comprised of state officials or their appointees. Each community college is similar in nature and function to all of the others, and the operations of no single community college are considered major in relation to the operations of all community colleges in the system. Therefore, aggregated financial information is presented in this CAFR for all community colleges.

The aggregated financial information for community colleges also includes the financial data of the institutions’ significant fund-raising foundations. Although the community colleges do not control the timing or amount of receipts from their foundations, the majority of resources (or income thereon) that the foundations hold and invest are restricted to the activities of the respective community colleges by the donors. Because these restricted resources held by the foundations can only be used by, or for the benefit of, the specific community colleges, the foundations are considered component units of the community colleges and are included in the community colleges’ financial statements. The foundations are private not-for-profit organizations that report under Financial Accounting Standards Board pronouncements. As such, certain revenue recognition criteria and presentation features are different from that of the Governmental Accounting Standards Board. The foundations’ financial statement formats were modified to make them compatible with the community colleges’ financial statement formats.

North Carolina Housing Finance Agency

The North Carolina Housing Finance Agency is a legally separate organization established to administer programs to finance construction of low and moderate income housing. The Agency has a thirteen-member board of directors, with twelve appointed by either the Governor or the General Assembly. The thirteenth member is elected by the other twelve. The State has the ability to impose its will since it can significantly influence the programs, projects, activities, and level of services of the Agency.

State Education Assistance Authority

The State Education Assistance Authority is a legally separate authority created to provide a system of financial assistance, consisting of grants, loans, work-study or other employment, and other aids, to qualified students to obtain an education beyond the high school level by attending public or private educational institutions. The Authority is governed by a seven-member board of directors, all of whom are appointed by the Governor. The State provides significant operating subsidies to the Authority; therefore, a financial benefit/burden relationship exists between the State and the Authority.
NOTES TO THE FINANCIAL STATEMENTS

Discretely Presented Component Units - Other

North Carolina Phase II Tobacco Certification Entity, Inc.
The North Carolina Phase II Tobacco Certification Entity, Inc. (Entity) is a legally separate organization established to serve as the certification entity for the State for the National Tobacco Grower Settlement Trust. Under the settlement, tobacco companies agreed to create a trust fund for tobacco growers and quota holders in 14 grower states, including North Carolina. The Entity is governed by a fourteen-member board. Three members serve by virtue of their positions as state officials and nine members are appointed by either the Governor, President Pro Tempore of the Senate, or the Speaker of the House. The State has the ability to impose its will since appointed members may be removed without cause. The Tobacco Buyout Bill enacted in October 2004 ended the trust agreement that the Entity was formed to oversee. The Entity made a final payment to quota and tobacco owners in late 2005. Management believes that it will take approximately two years from the date of final payment to finalize any outstanding issues related to open payment years and to cease operations.

North Carolina Global TransPark Authority
The North Carolina Global TransPark Authority (formerly North Carolina Air Cargo Airport Authority) is a legally separate authority created to administer the development of the North Carolina Global TransPark. Of the twenty-member governing board, nineteen are voting members. Seven of the voting members are appointed by the Governor and six are appointed by the General Assembly. The State has obligated itself to provide significant funding to the Authority; therefore, a financial benefit/burden relationship exists between the State and the Authority. Also included in the Authority are the financial data of its blended component unit, the North Carolina Global TransPark Foundation (Foundation). The Authority appoints a majority of the Foundation’s governing board and receives financial benefits from the Foundation.

North Carolina State Ports Authority
The North Carolina State Ports Authority is a legally separate authority established to operate the State’s port facilities in Wilmington and Morehead City. It is governed by an eleven-member board, all of whom are appointed by either the Governor or the General Assembly. The State has obligated itself to provide significant funding to the Authority; therefore, a financial benefit/burden relationship exists between the State and the Authority.

North Carolina Railroad Company
The North Carolina Railroad Company is a legally separate, for-profit corporation owned by the State for the purpose of promoting trade, industry, and transportation within North Carolina and advancing the economic interests of the State. The Railroad is governed by a fourteen-member board, all of whom are elected by shares held by the State. A financial benefit/burden relationship exists between the State and the Railroad. Also, the State is financially accountable since the State’s intent in owning the Railroad’s stock is to directly enhance its ability to provide governmental services.

North Carolina Agricultural Finance Authority
The North Carolina Agricultural Finance Authority is a legally separate authority created to administer the financing of low-interest loans to farmers. The Authority is governed by a ten-member board, one of whom is a state official and nine of whom are appointed by either the Governor or the General Assembly. A financial benefit/burden relationship exists between the State and the Authority.

North Carolina Partnership for Children, Inc.
The North Carolina Partnership for Children, Inc. is a legally separate organization established to develop a comprehensive long-range strategic plan for early childhood development. A twenty-six-member board governs the Partnership. Certain elected state officials appoint twenty-two of the members, while four members serve ex officio by virtue of their state positions. The State provides significant operating subsidies to the Partnership creating a financial benefit/burden relationship.

Regional Economic Development Commissions:

Northeastern North Carolina Regional Economic Development Commission
The Northeastern North Carolina Regional Economic Development Commission is a legally separate organization created to facilitate economic development and tourism in northeastern North Carolina. The Commission consists of seventeen members, including the Secretary of Commerce and the Secretary of the Department of Environment and Natural Resources (or their designees), five members appointed by the Governor, five by the Speaker of the House, and five by the President Pro Tempore of the Senate. The State provides significant program and operating support to the Commission, creating a benefit/burden relationship.

Southeastern North Carolina Regional Economic Development Commission
The Southeastern North Carolina Regional Economic Development Commission is a legally separate organization created to build economic strength in southeastern North Carolina. The Commission consists of fifteen members, with three appointed by the Governor, two by the Lieutenant Governor, five by the Speaker of the House, and five by the President Pro Tempore of the Senate. The State provides significant program and operating support to the Commission, creating a benefit/burden relationship.

Western North Carolina Regional Economic Development Commission
The Western North Carolina Regional Economic Development Commission is a legally separate organization created to improve economic opportunity in western North Carolina with sensitivity to the resources of that region. The Commission consists of fifteen members, with five appointed by the N.C. House of Representatives, five by the N.C. Senate, three by the Governor, and two by the Lieutenant Governor. The State provides significant program and operating support to the Commission, creating a benefit/burden relationship.
Notes to the Financial Statements

North Carolina Turnpike Authority

The North Carolina Turnpike Authority was created to study, design, plan, construct, finance, and operate a system of toll roads, bridges, and/or tunnels supplementing the traditional non-toll transportation system serving the citizens of the State. The Turnpike Authority is governed by a nine member board consisting of four members appointed by the General Assembly, four members appointed by the Governor, and the Secretary of Transportation. The State has the ability to impose its will since appointed members may be removed without cause.

Availability of Financial Statements

Complete financial statements for the following component units can be obtained from the Office of the State Auditor, 2 South Salisbury Street, 20601 Mail Service Center, Raleigh, N.C. 27699-0601.

- Constituent institutions in the UNC System
- Community colleges
- North Carolina Turnpike Authority
- North Carolina State Ports Authority
- North Carolina Partnership for Children, Inc.
- North Carolina Agricultural Finance Authority
- North Carolina Global Transpax Authority

Complete financial statements for the following component units can be obtained from the respective administrative offices of those units listed below:

- The Golden LEAF, Inc.
  107 SE Main Street
  Rocky Mount, NC 27801
- N.C. Housing Finance Agency
  P.O. Box 28066
  Raleigh, N.C. 27611-8066
- State Education Assistance Authority
  P.O. Box 2688
  Chapel Hill, N.C. 27515-2688
- North Carolina Railroad Company
  2809 Highwoods Boulevard, Suite 100
  Raleigh, NC 27604-1000
- N.C. Phase II Tobacco Certification Entity, Inc.
  3125 Popularwood Ct., Suite 112
  Raleigh, N.C. 27604
- Northeastern N.C. Regional Economic Development Commission
  119 West Water Street
  Edenton, N.C. 27932
- Southeastern N.C. Regional Economic Development Commission
  P.O. Box 2556
  Elizabethtown, N.C. 28937
- Western N.C. Regional Economic Development Commission
  3 General Aviation Dr.
  Fletcher, N.C. 28732

The North Carolina Infrastructure Finance Corporation does not issue separate financial statements.

B. Basis of Presentation

The accompanying financial statements of the State of North Carolina financial reporting entity have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”) as applicable to governments. The Governmental Accounting Standards Board (GASB) establishes standards of financial accounting and reporting for state and local governmental entities. Private sector standards of accounting and financial reporting issued on or before November 30, 1989 generally are followed in both the government-wide and proprietary fund financial statements to the extent those pronouncements do not conflict with or contradict GASB pronouncements. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The State has elected not to follow subsequent private-sector guidance. The financial statements of the North Carolina Railroad Company (Railroad), a for-profit corporation (discretely presented component unit), have been prepared in accordance with FASB pronouncements.

The financial statements are presented as of and for the fiscal year ended June 30, 2006, except for the USS North Carolina Battleship Commission whose statements are as of and for the fiscal year ended September 30, 2005, and the North Carolina Deferred Compensation Plan, the 401(k) Supplemental Retirement Income Plan, and the North Carolina Railroad Company whose statements are as of and for the fiscal year ended December 31, 2005.

The basic financial statements include both government-wide (based on the State as a whole) and fund financial statements as follows:

Government-wide Financial Statements

The statement of net assets and the statement of activities display information on all the nonfiduciary activities of the primary government (the State) and its component units. Fiduciary activities are excluded from the government-wide statements because they cannot be used to support the State's own programs. As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are interfund services provided and used between functions. Elimination of these charges would misstate both the expenses of the purchasing function and the program revenues of the selling function. These statements distinguish between the governmental and business-type activities of the State. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.
NOTES TO THE FINANCIAL STATEMENTS

The statement of activities demonstrates the degree to which the direct expenses of a given function or identifiable activity are offset by program revenues. Direct expenses are those that are clearly associated with a specific function or identifiable activity. Certain charges to other funds or programs for "centralized" expenses also include an overhead markup that is included in direct expenses. Program revenues include (a) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or identifiable activity (including fees, fines and forfeitures and certain grants and contracts that are essentially contracts for services) and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program or identifiable activity (including restricted investment earnings or losses). Revenues that are not classified as program revenues, including all taxes, are presented as general revenues. Unrestricted resources internally dedicated by the State's governing body (General Assembly) are reported as general revenues rather than as program revenues. The State does not allocate general government (indirect) expenses to other functions.

Fund Financial Statements

The fund financial statements provide information about the State's funds, including its fiduciary funds. Separate statements for each fund category—governmental, proprietary, and fiduciary—are presented. The emphasis of fund financial statements is on major governmental and major enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

The State reports the following major governmental funds:

General Fund
This 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.

Highway Fund
This fund accounts for most of the activities of the Department of Transportation, including the construction and maintenance of the State's primary and secondary road systems. In addition, it supports areas such as the N.C. Ferry System, the Division of Motor Vehicles, public transportation, and railroad operations. The fund provides revenue to other State agencies to support initiatives such as the State Highway Patrol and driver's education. The principal revenues of the Highway Fund are motor fuels taxes, motor vehicle registration fees, driver's license fees, and federal aid. A portion of the motor fuels taxes is distributed to municipalities for local street projects.

Highway Trust Fund
This fund was established by legislation (Chapter 692 of the 1989 Session Laws) to provide a dedicated funding mechanism to meet highway construction needs for North Carolina. Taxes were increased for the specific purpose of improving identified primary transportation corridors within the State and for the completion of urban loops around seven major metropolitan areas. Additionally, this fund provides supplemental allocations for secondary road construction and supplemental assistance to municipalities for local street projects. The fund also makes transfers to the General Fund and the Highway Fund. The principal revenues of the Highway Trust Fund are highway use taxes, motor fuels taxes, and various title and registration fees.

The State reports the following major enterprise funds:

Unemployment Compensation Fund
This fund accounts for the State's unemployment insurance program, which is part of a national system established to provide temporary benefit payments to eligible unemployed workers. The unemployment benefits are financed primarily by State unemployment insurance taxes, distributions of federal unemployment insurance taxes, and federal funding for the unemployment benefits of civilian and military employees. The unemployment taxes collected from employers are transferred to the United States Treasury and deposited into North Carolina's Unemployment Insurance Trust Fund.

N.C. State Lottery Fund
This fund accounts for the activities of the N.C. Education Lottery Commission, which began ticket sales on March 30, 2006. The net profits of the fund are transferred periodically to the Education Lottery Fund, a nonmajor special revenue fund.

EPA Revolving Loan Fund
This fund accounts for the activities of the State's clean water and drinking water revolving loan programs, which provide low cost loans to units of local government for the construction of wastewater facilities and drinking water infrastructure. These programs are financed primarily by federal capitalization grants from the United States Environmental Protection Agency (EPA), interest earnings on loans, loan repayments, and State funds (i.e., bond proceeds and State appropriations).

Additionally, the State reports the following fund types:

Internal Service Funds
These funds account for workers compensation and state property fire insurance coverages, motor fleet management services, mail services, temporary staffing services, computing and telecommunication services, and surplus property services provided to other departments or agencies of the State and its component units, or to other governments, on a cost-reimbursement basis.

Pension and Other Employee Benefits Trust Funds
These funds account for resources held in trust for the members and beneficiaries of the State's defined benefit pension plans, Internal Revenue Code (IRC) Section 401(k) plan, IRC Section 457 plan, other defined contribution plans, death benefit plan, disability income plan, State health plan, and retiree health benefit fund.
NOTES TO THE FINANCIAL STATEMENTS

Investment Trust Fund
This fund accounts for the external portion of the Investment Pool sponsored by the Department of State Treasurer.

Private-purpose Trust Funds
These funds account for resources held in trust for insurance carriers, designated beneficiaries by the Administrative Office of the Courts, and other departmental trust funds in which the principal and income benefit individuals, private organizations, or other governments.

Agency Funds
These funds account for sales tax collections held on behalf of local governments, resources held by the Administrative Office of the Courts for distribution to designated beneficiaries, the Investment Pool's securities lending assets and liabilities allocated to participating component units, insurance company receivership assets, and other resources held by the State in a purely custodial capacity for individuals, private organizations, or other governments. Insurance company receivership assets are held by the Commissioner of Insurance exclusively in his capacity as Receiver. These assets belong to insurance companies and other entities in receivership and are not the property of the State.

C. Measurement Focus and Basis of Accounting

Government-wide, Proprietary, and Fiduciary Fund Financial Statements

The government-wide, proprietary, and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, except for agency funds which do not have a measurement focus. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of the timing of related cash flows.

Lottery games are sold to the public by contracted retailers. For Powerball, revenue is recognized at the time of sale. For instant games, revenue is recognized at the time a pack of tickets is settled. For Powerball, prize expense is recorded at fifty percent of sales. For instant games, prize expense is accrued based on the final production prize structure percentage provided by the gaming vendor for each game and recorded on the value of packs settled. For instant games with prize tickets, the final prize structure percentage used is adjusted to eliminate the value of the prize tickets.

Nonexchange transactions, in which the State receives (or gives) value without directly giving (or receiving) equal value in exchange, include taxes; fines and forfeitures; grants, entitlements, and similar items; and donations. Recognition standards are based on the characteristics and classes of nonexchange transactions. Income taxes, sales taxes, and other similar taxes on earnings or consumption are recognized as revenues, net of estimated refunds and uncollectible amounts, in the accounting period when the underlying exchange transaction has occurred. Franchise taxes, other taxes, and fines and forfeitures are recognized as revenues, net of estimated refunds and uncollectible amounts, in the accounting period when an enforceable legal claim to the assets arises and the use of resources is required or is first permitted. Grants, entitlements, and donations are recognized as revenues, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection. Amounts received before all eligibility requirements have been met are reported as deferred revenues. Grants and similar aid to other organizations are recognized as expenses as soon as recipients have met all eligibility requirements. Amounts paid before all eligibility requirements have been met are reported as prepaid items.

Governmental Fund Financial Statements

Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets and liabilities are generally included on the balance sheet. The operating statement presents increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in spendable resources. General capital asset acquisitions are reported as expenditures and proceeds of general long-term debt are reported as other financing sources.

Under the modified accrual basis of accounting, revenues are recognized when both measurable and available. Generally, the State considers revenues reported in the governmental funds to be available if they are collected with thirty-one days after year-end. Exceptions are individual income tax revenues and federal and county funds accrued for the matching share of medicaid claims payable, which the State considers to be available if they are collected within twelve months after year-end. Furthermore, in the circumstance where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., refunds payable and applied refunds). Principal revenue sources considered susceptible to accrual include taxes, federal funds, local funds, and investment earnings. Other revenues are considered to be measurable and available only when cash is received by the State.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, compensated absences, obligations for workers' compensation, and arbitrage rebate liabilities, which are recognized as expenditures when payment is due. Pension contributions to cost-sharing pension plans are recognized as expenditures in the period to which the payment relates, even if payment is not due until the subsequent period.
D. Cash and Cash Equivalents

This classification includes undeposited receipts; petty cash; deposits held by the State Treasurer in the Short-term Investment portfolio (see Note 3); and demand and time deposits with private financial institutions, excluding certificates of deposit. The Short-term Investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and also may withdraw cash at any time without prior notice or penalty.

E. Investments

This classification includes deposits held by the State Treasurer in certain long-term investment portfolios (see Note 3) as well as investments held separately by the State and its component units. Investments are generally reported at fair value. Additional investment valuation information is provided in Note 3. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

F. Securities Lending

Cash and securities received as collateral on securities lending transactions are reported as assets in the accompanying financial statements. Liabilities resulting from the securities lending transactions are also reported. Certain component units of the State deposit funds with the State Treasurer's Investment Pool, which participates in securities lending activities. The component units' position in the pool and related securities lending assets and liabilities are reported in an agency fund. Additional disclosures about the State Treasurer's securities lending transactions are provided in Note 3.

G. Receivables and Payables

Receivables in all funds represent amounts that have arisen in the ordinary course of business and are shown net of allowances for uncollectible amounts.

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either “due to/over from other funds” (i.e., current portion of interfund loans) or “advances to/over from other funds” (i.e., the non-current portion of interfund loans). All other outstanding balances between funds related to services provided and used, reimbursements, and transfers are classified as “due to/over from other funds.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

In the fund financial statements, advances between funds (and to component units) and notes receivable are offset by a reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

H. Inventories and Prepaid Items

The inventories of the State and component units are valued at cost using either the first-in, first-out, last invoice cost, or average cost method. These inventories consist of general supplies and materials. Institutions of the UNC system and community colleges also use these valuations along with the retail inventory method for some bookstore operations. The State Highway Fund (special revenue fund) accounts for its maintenance and construction inventories using the average cost method.

Except for maintenance and construction inventories of the State Highway Fund, inventories in the State's governmental funds are recorded as expenditures when purchased. In the fund financial statements, inventories are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources. All other inventories of the State and its component units are recognized as expenses or expenditures when consumed.

Certain payments to vendors and grantees reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

I. Restricted/Designated Assets

In the enterprise funds, unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. These assets are also classified as noncurrent since they cannot be used for current operations (i.e., are restricted for the acquisition/construction of capital assets). Unrestricted assets that are internally designated for capital purposes are also classified as noncurrent. Certain other assets are classified as restricted because their use is limited by statute.

J. Capital Assets

Capital assets, which include property, plant, equipment; easements; and infrastructure assets (e.g., State highway network, utility systems, and similar items), are reported in the government-wide financial statements and the fund financial statements for proprietary funds. Purchased or constructed capital assets are reported at cost or estimated historical cost. The State highway network constructed prior to July 1, 2001 is recorded at estimated historical cost. Since July 1, 2001 the State highway network is recorded at cost. The initial estimated historical cost of the network is based on construction expenditures reported by the Department of Transportation less amounts estimated for the cost of right-of-ways and land
improvements. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend its useful life are not capitalized. Donated capital assets are recorded at their estimated fair value at the date of donation.

Generally, capital assets are defined by the State and component units as assets with an initial value or cost greater than or equal to $5,000 and an estimated useful life of two or more years. Exceptions are certain component units (The Golden LEAF, Inc., N.C. Housing Finance Agency, N.C. Phase II Tobacco Certification Entity, Inc., N.C. Railroad Company, and N.C. Regional Economic Development Commissions), which maintain minimum thresholds of $1,000 or below.

The value of assets constructed by the State and its component units for their own use includes all material direct and indirect construction costs that are increased as a result of the construction. In proprietary funds and component units, interest costs incurred (if material) are capitalized during the period of construction.

The depreciation methods and estimated useful lives used by the state and component units are as follows:

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Method</th>
<th>Estimated Useful Life</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings</td>
<td>Straight-line</td>
<td>10-50 years</td>
</tr>
<tr>
<td>Machinery and Equipment</td>
<td>Straight-line</td>
<td>2-25 years</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>Units of output for motor vehicles</td>
<td>90,000 miles</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>Straight-line</td>
<td>2-25 years</td>
</tr>
<tr>
<td>General infrastructure</td>
<td>Straight-line</td>
<td>10-75 years</td>
</tr>
<tr>
<td>State highway network</td>
<td>Composite</td>
<td>50 years</td>
</tr>
</tbody>
</table>

For the State highway network, depreciation is based on a weighted average of the estimated useful lives of dissimilar assets in the network (e.g., subsurface foundations, roadway surfaces, bridges, traffic control devices, guardrails, markings, signage, etc.).

K. Tax Refund Liabilities

Tax refund liabilities consist primarily of accrued income and sales and use tax refunds due to taxpayers. During the calendar year, the State collects employee withholdings and taxpayers' payments for income taxes. At June 30, the State estimates the amount it owes taxpayers for income tax overpayments during the preceding six months. Sales and use tax refund liabilities are also estimated at June 30. These liabilities are recorded as “Tax refunds payable.”

L. Compensated Absences

Employees of the State and component units are permitted to accumulate earned but unused vacation pay benefits. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. Also, when determining the vacation pay liability due within one year, leave is considered taken on a last in, first out (LIFO) basis. In governmental funds, a liability for these amounts is reported only as payments come due each period upon the occurrence of relevant events such as employee resignations and retirements. The State's policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year end is converted to sick leave.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not part of the 30 day maximum applicable to regular vacation leave and is not subject to conversion to sick leave.

There is no liability for unpaid accumulated sick leave because the State has no obligation to pay sick leave upon employee termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

M. Long-Term Liabilities

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the columns for governmental activities, business-type activities, and component units. These amounts are also reported as liabilities in the fund financial statements for proprietary funds. Debt premiums of the State are deferred and amortized over the life of the debt using the effective interest method, if material. Losses on the State’s refundings are deferred and amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter, using the effective interest method. Losses on refundings of the NC Housing Finance Agency are deferred and amortized using the straight-line method. Debt premiums, discounts, and losses on refundings of the University of North Carolina System (component unit) are generally deferred and amortized using the straight-line method, if material. Long-term debt is reported net of the applicable debt premium, discount, and/or deferred loss on refunding. Debt issuance costs of the State’s governmental activities and the University of North Carolina System (component unit) are generally expensed. Debt issuance costs of the State’s business-type activities and the NC Housing Finance Agency and the NC State Education Assistance Authority (component units) are deferred and amortized over the life of the debt using the straight-line method.
NOTES TO THE FINANCIAL STATEMENTS

Capital appreciation bonds are those bonds that are issued at stated interest rates (which may be zero) significantly below their effective interest rate, resulting in a substantial discount (deep discount). The implicit interest (i.e., discount) is not paid until the bonds mature. Therefore, the net value of the bonds accrete (i.e., the discount is reduced) over the life of the bonds. This deep-discount debt is reported in the government-wide financial statements at its net or accreted value rather than at face value.

In the fund financial statements, governmental fund types recognize debt premiums, as well as debt issuance costs, during the current period. The face amount of the debt issued and premiums received are reported as other financing sources. Issuance costs, whether or not withheld from the actual proceeds received, are reported as debt service expenditures.

N. Sureties

Sureties include various assets, including securities from insurance companies and bail bondsmen doing business within North Carolina, that have been placed in safekeeping with a financial institution or the State Treasurer, as required by applicable general statutes.

O. Net Assets/Fund Balance

Net assets are reported as restricted when constraints placed on them are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or are imposed by law through constitutional provisions. Constraints placed on net asset use by enabling legislation are not reported as net asset restrictions since such constraints are not legally enforceable. An Attorney General Advisory Opinion referenced that the Governor, pursuant to his constitutional authority under Article III, Section 3(3), may use resources restricted by enabling legislation in his discretion to meet a budget shortfall. Legal enforceability means that the State can be compelled by an external party, such as citizens, public interest groups, or the judiciary to use resources created by enabling legislation only for the purposes specified by the legislation. Situations where the State's internal governing body (General Assembly) places restrictions on existing resources or earmarks existing revenue sources are considered to be constraints that are internally imposed. Such internally dedicated net assets are reported as unrestricted.

Under some programs, the State has the option of using either restricted or unrestricted resources to make certain payments. When both restricted and unrestricted resources are available for use, generally it is the State's policy to use receipts first (which include restricted and unrestricted resources), then State appropriations as necessary. Receipts are defined as all funds collected by an agency or institution other than State appropriations. The decision to use restricted or unrestricted receipts to fund a payment is transactional-based within the departmental management system in place at the agency or institution. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are (a) externally restricted for a specific use, (b) not available for appropriation or expenditure because the underlying asset is not an available financial resource, or (c) for encumbrances, which represent commitments related to unperformed contracts for services and undelivered goods. Designations of fund balance represent tentative management plans that are subject to change (See Note 10, Fund Balance Reserves).

P. Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items and capital contributions. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Proprietary fund operating revenues 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. Nonoperating revenues, such as noncapital grants and investment earnings, result from nonexchange transactions or ancillary activities. Capital contributions are reported separately, after nonoperating revenues and expenses.

Q. Food Stamps

In accordance with GASB Statement No. 24, Accounting and Financial Reporting for Certain Grants and Other Financial Assistance, the State recognizes distributions of food stamp benefits as revenue and expenditures in the general fund, whether the benefits are distributed directly or through agents and whether the benefits are in paper or electronic form. Expenditures are recognized when the benefits are distributed to the individual recipients by the State or its agents; revenue is recognized at the same time. Revenue, expenditures, and balances of food stamps are measured based on face value.
NOTE 2: STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Fund Balance / Net Assets Deficit

Component Unit

At June 30, 2006, the following component unit reported a net assets deficit: N. C. Turnpike Authority, $3.915 million.
A. Deposits and Investments with State Treasurer

Unless specifically exempt, every agency of the State and certain component units are required by General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. Certain local governmental units that are not part of the reporting entity are also allowed to deposit money with the State Treasurer. Expenditures for the primary government and certain component units are made by warrants issued by the agencies and drawn on the State Treasurer. The State Treasurer processes these warrants each day when presented by the Federal Reserve Bank. General Statute 147-69.1 authorizes the State Treasurer to invest all deposits in obligations of or fully guaranteed by the United States; obligations of certain federal agencies; specified repurchase agreements; obligations of the State of North Carolina; time deposits with specified financial institutions; prime quality commercial paper with specified ratings; specified bills of exchange or time drafts; asset-backed securities with specified ratings; and corporate bonds and notes with specified ratings.

General Statute 147-69.2 authorizes the State Treasurer to invest the deposits of certain special funds, including the pension trust funds, the State Health Plan, the Disability Income Plan of N.C., the Escheats Fund, the Public School Insurance Fund, the State Education Assistance Authority, and trust funds of the University of North Carolina System, in the investments authorized in General Statute 147-69.1; general obligations of other states; general obligations of North Carolina local governments; asset-backed securities bearing specific ratings; and obligations of any company incorporated within or outside the United States bearing specific ratings. The deposits of the pension trust funds may be invested in all of the above plus certain insurance contracts; group trusts; individual, common or collective trusts of banks and trust companies; real estate investment trusts; limited partnership interest in limited liability partnerships or limited liability companies; and certain stocks and mutual funds.

External Investment Pool

To ensure that these and other legal and regulatory limitations are met, all cash deposited with the State Treasurer, except for the UNC Hospitals, Escheats Fund, and bond proceeds investment accounts, is maintained in the Investment Pool. This pool, a governmental external investment pool, consists of the following individual investment portfolios:

- **Short-term Investment** – This portfolio may hold any of the investments authorized by General Statute 147-69.1. The Short-term Investment portfolio is the primary cash management account for the State and is managed in such a manner as to be readily convertible into cash. The primary participants of this portfolio are the General Fund and the Highway Funds. Other participants include the remaining portfolios listed below, universities and various boards, commissions, community colleges, and school administrative units that make voluntary deposits with the State Treasurer.

**Long-term Investment** – This portfolio may hold the fixed-income investments authorized by General Statutes 147-69.1 and 147-69.2. Since the deposits in this fund are typically not needed for day-to-day operations, the investment vehicles used generally have a longer term and higher return than those held in the Short-term Investment portfolio. The primary participants of the portfolio are the pension trust funds.

**Equity Investment** – This portfolio holds an equity-based trust. The State's pension trust funds are the sole participants in the portfolio.

**Real Estate Investment** – This portfolio holds investments in real estate-based trust funds and group annuity contracts. The State's pension trust funds are the sole participants in the portfolio.

**Alternative Investment** – This portfolio holds investments in limited partnerships and equities received in the form of distributions from its primary investments. The State's pension trust funds are the sole participants in the portfolio.

All of the above investment portfolios operate like individual investment pools, except that an investment portfolio may hold shares in other investment portfolios at the discretion of the State Treasurer and subject to the legal limitations discussed above. To this extent, the deposits are commingled; and therefore, the State Treasurer considers all investment portfolios to be part of a single pool, the Investment Pool. The Investment Pool contains deposits from funds and component units of the reporting entity (internal portion) as well as deposits from certain legally separate organizations outside the reporting entity (external portion). This pool is not registered with the Securities and Exchange Commission and is not subject to any formal oversight other than that of the legislative body.

At year-end, the condensed financial statements for the Investment Pool maintained by the State Treasurer were as follows (dollars in thousands):
NOTES TO THE FINANCIAL STATEMENTS

Statement of Net Assets
June 30, 2006

Assets:
Cash and cash equivalents.............. $ 320,050
Other assets.................................. 411,008
Investments................................... 98,791,063
Total assets.................................. $99,522,121

Liabilities:
Distributions payable...................... 8,844
Other payables................................ 25,000
Obligations under securities lending..... 21,667,015
Total liabilities................................ 21,700,859

Net Assets:
Internal:
Primary government....................... 75,552,556
Component units........................... 2,027,864
External............................................. 200,832
Total net assets............................ $77,821,262

Statement of Operations and Changes in Net Assets
For the Fiscal Year Ended June 30, 2006

Revenues:
Investment income........................ 5,918,457

Expenses:
Securities lending......................... 853,022
Investment management................... 138,335
Total expenses.............................. 991,357

Net increase in net assets resulting from operations................. 4,927,100

Distributions to participants:
Distributions paid and payable........... (4,927,100)

Share transactions:
Reinvestment of distributions............ 4,928,231
Net share redemptions..................... (1,439,071)
Total increase in net assets............... 3,489,160

Net assets:
Beginning of year.......................... 74,332,102
End of year.................................... $77,821,262

The external portion of the Investment Pool is presented in the State's financial statements as an investment trust fund. Each fund and component unit's share of the internal equity in the Investment Pool is reported in the State's financial statements as an asset of those funds or component units. Equity in the Short-term Investment portfolio is reported as cash and cash equivalents while equity in the Long-term Investment, Equity Investment, Real Estate Investment, and Alternative Investment portfolios is reported as investments. The internal equity of the pool differs from the amount of assets reported by the funds and component units due to the typical banker/customer outstanding and in-transit items. Additionally, each fund reports its share of the assets and liabilities arising from securities lending transactions. The State reports the assets and liabilities arising from securities lending transactions for component units as part of the State's agency funds, rather than allocate them to the component units.

Investments in nonparticipating contracts, such as nonnegotiable certificates of deposit, are reported at cost. Other investments held in the Short-term Investment portfolio are reported at amortized cost, which approximates fair value. All other investments are reported at fair value. Fair values are determined daily for the Long-term Investment and Equity Investment portfolios and quarterly for the Real Estate Investment and Alternative Investment portfolios. The fair value of fixed income securities is based on future principal and interest payments discounted using current yields for similar instruments. Investments in real estate trusts, limited partnerships, and the equity trust are valued using market prices provided by the third party professionals. Participants' shares sold and redeemed are determined in the same manner as is used to report investments, and the State Treasurer does not provide or obtain legally binding guarantees to support share values.

Net investment income earned by the Investment Pool is generally distributed on a pro rata basis. However, in accordance with legal requirements, the General Fund receives all investment income earned by funds created for purposes of meeting appropriations. For the fiscal year ended June 30, 2006, $50.31 million of investment income associated with other funds was credited to the General Fund.

Deposits

Custodial Credit Risk. For deposits, custodial credit risk is the risk that in the event of a bank failure, the State's deposits may not be recovered. At year-end, the Investment Pool's deposits were not exposed to custodial credit risk.

The State Treasurer's deposit policy for custodial credit risk is limited to complying with the collateralization rules of the North Carolina Administrative Code (Chapter 20 N.C.A.C 7). Deposits to the Investment Pool may be made in any bank, savings and loan association or trust company in the State as approved by the State Treasurer. The North Carolina Administrative Code requires depositories to collateralize all balances that are not insured. The depositories must maintain specified security types in a third party escrow account established by the State Treasurer. The securities collateral must be governmental in origin (e.g., U.S. Treasury, U.S. agency, or state and local government obligations) or the highest grade commercial paper and bankers' acceptances. The market value of the collateral must not be less than the value of the uninsured deposits. The depositories may elect to collateralize deposits separately (dedicated method) or include deposits of the North Carolina local government units in a collateral pool with the State and certain component units (pooling method).
Investments

At year-end, the Investment Pool maintained by the State Treasurer had the following investments and maturities (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Less Than 1</th>
<th>1 to 5</th>
<th>6 to 10</th>
<th>More Than 10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt securities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>8,887,071</td>
<td>1,402,136</td>
<td>2,164,800</td>
<td>2,399,668</td>
<td>900,367</td>
</tr>
<tr>
<td>Mortgage pass-throughs</td>
<td>6,326,147</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>8,055,999</td>
<td></td>
<td>1,022,814</td>
<td>3,993,519</td>
<td>3,039,868</td>
</tr>
<tr>
<td>Securities purchased with cash collateral under securities lending program:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>11,764,962</td>
<td>1,991,216</td>
<td>9,773,746</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>4,435,041</td>
<td>4,435,041</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>5,467,012</td>
<td>450,271</td>
<td>5,016,741</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$54,790,808</td>
<td>$11,425,511</td>
<td>$21,085,510</td>
<td>$7,951,500</td>
<td>$14,348,281</td>
</tr>
</tbody>
</table>

Other securities:

| Equity based trust - domestic                              | 32,587,628      |             |        |         |              |
| Equity based trust - international                          | 7,476,717       |             |        |         |              |
| Alternative investments                                     |                 |             |        |         |              |
| Hedge funds                                                 | 901,619         |             |        |         |              |
| Private equity investment partnerships                      | 574,247         |             |        |         |              |
| Stock distributions                                         | 4,414           |             |        |         |              |
| Real estate trust funds                                     | 2,455,630       |             |        |         |              |
| Total investment securities                                 | $98,791,082     |             |        |         |              |

Also, the major investment classifications of the Investment Pool had the following attributes at year-end (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Classification</th>
<th>Principal Amount</th>
<th>Range of Interest Rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Treasuries</td>
<td>$11,075,848</td>
<td>2.25%-8.86%</td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>5,966,786</td>
<td>0.0%-7.13%</td>
</tr>
<tr>
<td>Mortgage pass-throughs</td>
<td>6,484,376</td>
<td>5.0%-9.0%</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>8,039,308</td>
<td>3.45%-9.8%</td>
</tr>
<tr>
<td>Securities purchased with cash collateral under securities lending program:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>11,764,999</td>
<td>5.07%-5.54%</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>4,435,041</td>
<td>4.67%-5.38%</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>5,467,000</td>
<td>5.02%-5.58%</td>
</tr>
<tr>
<td>Equity-based trust - domestic</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Equity-based trust - international</td>
<td>n/a</td>
<td>n/a</td>
</tr>
</tbody>
</table>

Equity-based Trust - The State Treasurer has contracted with an external party (Trustee) to create the “Treasurer of the State of North Carolina Equity Investment Fund Pooled Trust” (the Trust). The State’s pension trust funds are the only depositors in the Trust. The State Treasurer employs investment managers to manage the assets, primarily in equity and equity-based securities in accordance with the General Statutes and parameters provided by the State Treasurer. The Trustee maintains custody of the underlying securities in the name of the Trust, services the securities, and maintains all related accounting records. The Trustee also acts as a securities lending agent for the Trust, invests residual cash in a cash sweep fund, and may be temporarily employed as an investment manager. The State Treasurer maintains beneficial interest in the Trust and no direct ownership of the securities.

Interest Rate Risk. Although there is no formally adopted investment policy, as a means of managing interest rate risk, fixed income assets of the Short-term Investment portfolio are invested in a laddered maturity approach that focuses on short maturity securities with ample liquidity. The Short-term Investment portfolio had a weighted average maturity of 1.18 years as of June 30, 2006. Most of the cash and cash equivalents of the major governmental and enterprise funds are invested in this portfolio.
NOTES TO THE FINANCIAL STATEMENTS

The assets of the Long-term Investment portfolio are primarily invested in securities with maturities longer than five years. The longer maturity range is more sensitive to interest rate changes; however, the longer duration structure of the portfolio provides a better match to the long duration characteristics of the retirement systems’ liabilities. At year-end, pensions and other employee benefit plans owned 98% of the Long-term Investment portfolio and the Escheats Fund (included with other governmental funds) owned 1%.

The Long-term Investment portfolio holds investments in Government National Mortgage Association (GNMA) mortgage pass through pools. Critical to the pricing of these securities are the specific features of the cash flows from the interest and principal payments of the underlying mortgages. Therefore, these valuations are very sensitive to the potential of principal prepayments by mortgagees in periods of declining interest rates. Also, included within the Long-term Investment portfolio are U.S. government agencies and corporate bonds which carry call options in which the issuer has the option to prepay the principal at certain dates over the life of the security. As such, these types of securities are more sensitive to the decline in long-term interest rates as similar securities without call options.

Credit Risk. General Statute 147-69.1 specifies the cash investment options for the Short-term Investment portfolio. The statute limits credit risk by restricting the portfolio’s corporate obligations, asset-backed securities, and commercial paper to securities that bear the highest rating of at least one nationally recognized rating service and do not bear a rating below the highest by any nationally recognized rating service. General Statute 147-69.2 specifies the cash investment options for the Long-term Investment portfolio. The statute limits credit risk by restricting the portfolio’s asset-backed securities and corporate obligations to securities that bear one of the four highest ratings of at least one nationally recognized rating service and do not bear a rating below one of the four highest ratings by any nationally recognized rating service. In the Long-term Investment portfolio, all holdings were rated BBB (or equivalent) or higher at the time of purchase by all three nationally recognized rating agencies.

At year-end, the Investment Pool had the following credit quality distribution for securities with credit exposure (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Aaa/AAA</th>
<th>Aa/AA</th>
<th>A</th>
<th>Baa/BBB</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. agencies</td>
<td>8,887,071</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>629,264</td>
<td>2,520,314</td>
<td>3,131,702</td>
<td>1,774,719</td>
</tr>
<tr>
<td>Securities purchased with cash collateral under securities lending program:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>11,764,962</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>4,435,041</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>789,730</td>
<td>1,007,071</td>
<td>3,670,211</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>24,506,068</td>
<td>3,527,385</td>
<td>6,801,913</td>
<td>1,774,719</td>
</tr>
</tbody>
</table>

Custodial Credit Risk. For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the State Treasurer will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. At year-end, the investments purchased with cash collateral under the securities lending program of $21.67 billion were exposed to custodial credit risk since the securities were held by the counterparty and were not registered in the name of the State Treasurer. As required by contractual agreements, a third party agent holds these assets for the benefit of a dedicated Treasurer’s account. This agreement fully indemnifies the Treasurer for any third party defaults or losses. All other investments of the Investment Pool were not exposed to custodial credit risk at year-end and no custodial credit risk policy has been adopted for these investment types.
NOTES TO THE FINANCIAL STATEMENTS

Foreign Currency Risk. At year-end, the Investment Pool’s exposure to foreign currency risk was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Currency</th>
<th>Equity Based Trust - International</th>
<th>Alternative Investment - Private Equity Investment Partnerships</th>
<th>Real-Estate Trust Fund Investment Partnerships</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Euro</td>
<td>$2,007,451</td>
<td>$106,052</td>
<td>$41,410</td>
<td>$2,154,913</td>
</tr>
<tr>
<td>Japanese Yen</td>
<td>1,577,484</td>
<td>2,737</td>
<td></td>
<td>1,580,221</td>
</tr>
<tr>
<td>Pound Sterling</td>
<td>1,150,973</td>
<td></td>
<td></td>
<td>1,150,973</td>
</tr>
<tr>
<td>Swiss Franc</td>
<td>595,278</td>
<td></td>
<td></td>
<td>595,278</td>
</tr>
<tr>
<td>Hong Kong Dollar</td>
<td>217,273</td>
<td></td>
<td></td>
<td>217,273</td>
</tr>
<tr>
<td>Australian Dollar</td>
<td>189,390</td>
<td></td>
<td></td>
<td>189,390</td>
</tr>
<tr>
<td>New Taiwan Dollar</td>
<td>153,727</td>
<td></td>
<td></td>
<td>153,727</td>
</tr>
<tr>
<td>South Korean Won</td>
<td>138,140</td>
<td></td>
<td></td>
<td>138,140</td>
</tr>
<tr>
<td>Canadian Dollar</td>
<td>127,628</td>
<td></td>
<td></td>
<td>127,628</td>
</tr>
<tr>
<td>Other Currencies</td>
<td>651,449</td>
<td></td>
<td></td>
<td>651,449</td>
</tr>
<tr>
<td>Total</td>
<td>$6,808,793</td>
<td>$108,789</td>
<td>$41,410</td>
<td>$6,958,992</td>
</tr>
</tbody>
</table>

Although there is no formally adopted investment policy, the State Treasurer's investment policy permits up to 13% of the retirement systems' invested assets to be in international securities. At year-end, the retirement systems had approximately 10.2% invested in international securities.

Securities Lending

Based on the authority provided in General Statute 147-69.3(e), the State Treasurer lends securities from its Investment Pool to broker-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The Treasurer's securities custodian manages the securities lending program. During the year the custodian lent U.S. government and agency securities, GNMA's, corporate bonds and notes for collateral. The custodian is permitted to receive cash, U.S. government and agency securities, or irrevocable letters of credit as collateral for the securities lent. The collateral is initially pledged at 102% of the market value of the securities lent, and additional collateral is required if its value falls to less than 100% of the market value of the securities lent. There are no restrictions on the amount of loans that can be made. Substantially all security loans can be terminated on demand by either the State Treasurer or the borrower. The State Treasurer cannot pledge or sell the collateral securities received unless the borrower defaults.

The cash collateral received is invested by the custodian agent and held in a separate account in the name of the State Treasurer. The average maturities of the cash collateral investments are less than the average maturities of the securities lent. While cash can be invested in securities ranging from overnight to five years, the custodian agent is not permitted to make investments where the weighted average maturity of all investments exceeds 30 days. At year-end, the weighted average maturity of investments was approximately 22 days.

At year-end, the State Treasurer had no credit risk exposure to borrowers because the amounts the Treasurer owed the borrowers exceeded the amounts the borrowers owed the State. The securities custodian is contractually obligated to indemnify the Treasurer for certain conditions, the two most important are default on the part of the borrowers and failure to maintain the daily mark-to-market on the loans.

Interest rate risk and credit risk. The policies for investments purchased with cash collateral under the securities lending program are set forth in the contract with the securities custodian. Contractually, asset-backed securities must bear the highest rating of at least one nationally recognized rating service. The expected maturity shall not exceed five years and securities having a final maturity greater than two years will be in floating rate instruments with interest rate resets occurring at no greater than 90-day intervals to minimize the effect of interest rate fluctuations on their valuations. The securities pledged as collateral for repurchase agreements are limited to securities issued or guaranteed by the U.S. government or its agencies, or specified bank or corporate obligations. As directed by the State Treasurer, repurchase counterparties are limited to specific counterparties with specific dollar limits per counterparty. Corporate bonds and notes, including bank holding company obligations, rated AA must have a final maturity no greater than three years. Securities rated A must have a final maturity no greater than two years. No more than five percent of the cash collateral may be invested in a single issue.
NOTES TO THE FINANCIAL STATEMENTS

Bond Proceeds Investment Accounts

The State Treasurer has established separate investment accounts for each Bond fund issue to comply with Internal Revenue Service regulations on bond arbitration. A private investment company under contract with the State Treasurer manages these separate accounts. The investments are valued at amortized cost, which approximates fair value. In the State's financial statements, each fund's equity in these accounts is reported as investments.

At year-end, the bond proceeds investment accounts had the following investments and maturities (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Weighted Average Maturity (Days)</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Agencies</td>
<td>$277,338</td>
<td>11</td>
</tr>
<tr>
<td>Commercial paper</td>
<td>29,600</td>
<td>91</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>215,474</td>
<td>7</td>
</tr>
<tr>
<td>Total investments</td>
<td>$522,412</td>
<td></td>
</tr>
</tbody>
</table>

Interest Rate Risk and Credit Risk. As established in the contract with the private investment company, all bond proceeds are managed in compliance with General Statute 147-69.1, which limits credit risk as described above, and can only be invested in short-term maturities with the average maturity ranging between overnight to six months based on the liquidity needs of the investment accounts. As of June 30, 2006, Standard and Poor's rated investments in commercial paper and U.S. agencies as A-1 and AAA, respectively.

Custodial Credit Risk. Investments purchased with bond proceeds were exposed to custodial credit risk since the securities were held by the counterparty and were not registered in the name of the State Treasurer.

University of North Carolina (UNC) Hospitals Investment Account

The State Treasurer has contracted with an external party (Trustee) to create the University of North Carolina Hospitals at Chapel Hill Trust (Trust). The UNC Hospitals are the only depositor in the Trust. However, the Trust is a participant of a commingled equity investment fund. The Trustee manages the assets, primarily in equity and equity-based securities in accordance with the General Statutes. The Trustee maintains custody of the underlying securities in the name of the Trust, services the securities, and maintains all related accounting records. The investments are valued at fair market value.

At year-end, the UNC Hospitals investment account maintained by the State Treasurer had the following investments (settled transactions) (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other securities:</td>
<td></td>
</tr>
<tr>
<td>Equity based trust - domestic</td>
<td>$104,825</td>
</tr>
<tr>
<td>Equity based trust - international</td>
<td></td>
</tr>
<tr>
<td>Total investment securities</td>
<td>$150,377</td>
</tr>
</tbody>
</table>

Foreign Currency Risk. At year-end, the UNC Hospitals investment account's exposure to foreign currency account was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Currency</th>
<th>Carrying Value by Investment Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Euro</td>
<td>$14,529</td>
</tr>
<tr>
<td>Japanese Yen</td>
<td>10,357</td>
</tr>
<tr>
<td>Pound Sterling</td>
<td>9,829</td>
</tr>
<tr>
<td>Canadian Dollar</td>
<td>3,448</td>
</tr>
<tr>
<td>Swiss Franc</td>
<td>2,783</td>
</tr>
<tr>
<td>Australian Dollar</td>
<td>2,236</td>
</tr>
<tr>
<td>Hong Kong Dollar</td>
<td>1,744</td>
</tr>
<tr>
<td>South Korean Won</td>
<td>1,326</td>
</tr>
<tr>
<td>Swedish Krona</td>
<td>994</td>
</tr>
<tr>
<td>Other Currencies</td>
<td>4,602</td>
</tr>
<tr>
<td>Total</td>
<td>$51,846</td>
</tr>
</tbody>
</table>

Note: The totals in this table do not agree to the totals disclosed in the investment table above because this foreign currency table includes equities based on trade date while the investment table is reported on settle date.

Esechet Investment Account

Pursuant to General Statute 147-69.2(b)(12), the State Treasurer has established a separate investment account on behalf of the Esechet Fund. A real estate investment trust under contract with the State Treasurer manages the account.

At year-end, the Esechet Fund invested in a Real Estate account, which held $20 million in cash. These funds were on deposit at a private investment bank in a short-term investment fund pending transfer into the investment fund on July 3, 2006.

Custodial Credit Risk. For deposits, custodial credit risk is the risk that in the event of a bank failure, the State's deposit may not be recovered. At year-end, the deposit held at the private investment bank was exposed to custodial credit risk because it was uninsured and not fully collateralized.

B. Deposits Outside the State Treasurer

In addition to the pooled deposits maintained by the State Treasurer, other deposits are maintained outside the State Treasurer by the primary government and certain component units. As a general rule, these deposits are not covered by the rules in Chapter 20 NCAC 7 requiring collateralization of uninsured deposits.
NOTES TO THE FINANCIAL STATEMENTS

Primary Government

The majority of deposits held outside the State Treasurer were maintained by the Employment Security Commission and the various clerks of superior court. General Statute 96-6 requires that Employment Security Commission funds be deposited with the United States Treasury to the credit of North Carolina. The clerks of superior court do not have a deposit policy for custodial credit risk. At year-end, the bank balances maintained outside the State Treasurer by the primary government were exposed to custodial credit risk as follows (dollars in thousands):

Uninsured and unencumbered ................................ $ 33,640
Uninsured and collateral held by pledging bank ............... 13
Uninsured and collateral held by pledging bank's
  trust department but not in State's name .................. 233
Total ....................................................................... $ 33,886

Component Units

(University of North Carolina System and State Education Assistance Authority)

The University of North Carolina (UNC) System does not have a deposit policy for custodial credit risk. At year-end, the bank balances maintained outside the State Treasurer by the UNC System were exposed to custodial credit risk as follows (dollars in thousands):

Uninsured and unencumbered ................................ $ 177,369
Uninsured and collateral held by pledging bank ............... 286
Uninsured and collateral held by pledging bank's
  trust department or agent but not in State's name ........ 11
Total ....................................................................... $ 177,666

The State Education Assistance Authority does not have a deposit policy for custodial credit risk. At year-end, the bank balances maintained outside the State Treasurer by the State Education Assistance Authority were exposed to custodial credit risk as follows (dollars in thousands):

Uninsured and collateral held by pledging bank ............... $ 23,275
Uninsured and collateral held by pledging bank's
  trust department or agent but not in State's name .......... 6,073
Total ....................................................................... $ 30,248

C. Investments Outside the State Treasurer

Investments in participating investment contracts, external investment pools, open-end mutual funds, debt securities, equity securities, and all investments of the Deferred Compensation Plan are reported at fair value. Investments in certificates of deposit, investment agreements, bank investment contracts, real estate, real estate investment trusts, and limited partnerships are reported at cost. Detailed disclosures about investments held outside the State Treasurer are presented below.

Primary Government

At year-end, 77% of investments held outside the State Treasurer were maintained by the Supplemental Retirement Income Plan of North Carolina.

Supplemental Retirement Income Plan of North Carolina

The General Statutes place no specific investment restrictions on the Supplemental Retirement Income Plan of North Carolina (the Plan). However, in the absence of specific legislation, the form of governance over the investments would be the prudent-person or prudent-expert rule. These rules are broad statements of intent, generally requiring investment selection and management to be made with prudent, discreet, and intelligent judgment and care. The Plan does not have formal investment policies that address interest rate risk, credit risk, custodial credit risk, concentration of credit risk, or foreign currency risk.
At December 31, 2005, the Supplemental Retirement Income Plan of North Carolina had the following investments and maturities that were maintained outside the State Treasurer (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Loss Than 1</th>
<th>1 to 5</th>
<th>6 to 10</th>
<th>More Than 10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt securities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fidelity Intermediate Bond Fund</td>
<td>$209,248</td>
<td>$209,248</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prudential Stable Value Fund:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>228,378</td>
<td>25,429</td>
<td>117,001</td>
<td>31,613</td>
<td>54,335</td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>96,190</td>
<td>—</td>
<td>79,891</td>
<td>9,507</td>
<td>6,762</td>
</tr>
<tr>
<td>Collateralized mortgage obligations</td>
<td>297,945</td>
<td>42,580</td>
<td>1,731</td>
<td>858</td>
<td>262,776</td>
</tr>
<tr>
<td>State and local government</td>
<td>2,886</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,886</td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>37,225</td>
<td>—</td>
<td>5,119</td>
<td>9,561</td>
<td>31,274</td>
</tr>
<tr>
<td>Money market mutual funds</td>
<td>5,119</td>
<td>5,119</td>
<td>—</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>167,623</td>
<td>3,433</td>
<td>80,160</td>
<td>51,810</td>
<td>32,220</td>
</tr>
<tr>
<td>Foreign corporate bonds</td>
<td>26,612</td>
<td>—</td>
<td>18,290</td>
<td>3,958</td>
<td>4,364</td>
</tr>
<tr>
<td>Foreign government bonds</td>
<td>8,343</td>
<td>—</td>
<td>3,089</td>
<td>2,412</td>
<td>2,842</td>
</tr>
<tr>
<td>Other securities:</td>
<td></td>
<td>$76,561</td>
<td>$509,410</td>
<td>$106,109</td>
<td>$387,491</td>
</tr>
<tr>
<td>International mutual funds</td>
<td>123,429</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other mutual funds</td>
<td>2,106,588</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prudential Stable Value Fund:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amount guaranteed by insurance company</td>
<td>17,387</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total investment securities</td>
<td>$3,328,973</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The Prudential Stable Value Fund is a trust product and is comprised of a group annuity contract issued by The Prudential Insurance Company of America and a portfolio of assets owned by the Plan. Principal and accrued interest is guaranteed by The Prudential Insurance Company of America.

**Interest Rate Risk and Credit Risk.** The Fidelity Intermediate Bond Fund, which is unrated, had a weighted average maturity of 4.5 years as of April 30, 2006. In the above table, it is disclosed as an investment with a maturity of one to five years. Of the underlying securities in the Prudential Stable Value Fund with credit risk exposure, $230.74 million were rated BBB or above by Standard & Poor’s and $633.79 million were unrated.

**Custodial Credit Risk.** The Prudential Stable Value Fund had a custodial credit risk exposure of $865.2 million because the underlying securities were uninsured, unregistered, and held by the counterparty.

**Concentration of Credit Risk.** More than 5% of the Plan’s investment is in collateralized mortgage obligations issued by the Federal National Mortgage Association. These investments were 5.3% of the Plan’s total investments.

**Foreign Currency Risk.** The Plan owns two international mutual funds, the American Europacific Growth Fund and the T. Rowe Price International Stock Fund. These funds had a carrying value of $122.84 million and $588.56 thousand, respectively, at December 31, 2005.

**Other Primary Government Investments**

The other primary government investments held outside the State Treasurer consisted almost entirely of balances maintained by the North Carolina Public Employee Deferred Compensation Plan (the Plan) and separate investment accounts held by trustees for special obligation debt issues to comply with IRS regulations on bond arbitrage.

General Statute 143B-426.24(j) allows the Deferred Compensation Plan Board to acquire investment vehicles from any company authorized to conduct such business in this State or may establish, alter, amend and modify, to the extent it deems necessary or desirable, a trust for the purpose of facilitating the administration, investment and maintenance of assets acquired by the investment of deferred funds. All assets of the Plan, including all deferred amounts, property and rights purchased with deferred amounts, and all income attributed thereto shall be held in trust for the exclusive benefit of the Plan participants and their beneficiaries.
NOTES TO THE FINANCIAL STATEMENTS

At year-end, the other primary government investments maintained outside the State Treasurer had the following investments and maturities (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Less Than 1</th>
<th>1 to 5</th>
<th>8 to 10</th>
<th>More Than 10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt securities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>$696</td>
<td>$104</td>
<td>$406</td>
<td>$163</td>
<td>$23</td>
</tr>
<tr>
<td>U.S. Treasury STRIPS</td>
<td>873</td>
<td>185</td>
<td>688</td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>2,409</td>
<td>158</td>
<td>395</td>
<td>1,849</td>
<td>7</td>
</tr>
<tr>
<td>Mortgage pass throughs</td>
<td>154</td>
<td>—</td>
<td>24</td>
<td>2</td>
<td>128</td>
</tr>
<tr>
<td>Collateralized mortgage obligations</td>
<td>58</td>
<td>2</td>
<td>50</td>
<td>6</td>
<td></td>
</tr>
<tr>
<td>State and local government</td>
<td>108</td>
<td>—</td>
<td>99</td>
<td>8</td>
<td>1</td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>26</td>
<td>—</td>
<td>—</td>
<td>9</td>
<td>17</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>164,775</td>
<td>153,151</td>
<td>11,624</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial paper</td>
<td>588</td>
<td>588</td>
<td>—</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Annuity contracts</td>
<td>36,157</td>
<td>—</td>
<td>36,157</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Money market mutual funds</td>
<td>5,094</td>
<td>5,094</td>
<td>—</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Mutual bond funds</td>
<td>11,219</td>
<td>—</td>
<td>—</td>
<td>11,217</td>
<td>2</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>62</td>
<td>—</td>
<td>27</td>
<td>25</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>222,217</td>
<td>159,280</td>
<td>49,470</td>
<td>13,279</td>
<td>188</td>
</tr>
</tbody>
</table>

Other securities:
- Other mutual funds: 610,781
- Real estate investment trusts: 20,000
- Domestic stocks: 58,952
- Other: 557
- Total investment securities: $912,507

Interest Rate Risk and Credit Risk. The special obligation debt proceeds are generally invested in repurchase agreements. As established in the debt covenants, repurchase agreements with respect to government obligations can only be entered into with 1) a dealer recognized as a primary dealer by a Federal Reserve Bank with a short-term rating not less than P-1 from Moody’s Investors Service (Moody’s) and not less than A-1 from Standard & Poor’s (S&P) and Fitch Ratings (Fitch); or 2) any commercial bank, trust company, or national banking association rated A or better by Moody’s, S&P and Fitch, the deposits of which are insured by the Federal Deposit Insurance Corporation. There are no formally adopted investment policies or debt covenants for special obligation debt proceeds that address interest rate risk.

At year-end, the other primary government investments maintained outside the State Treasurer had the following credit quality distribution for securities with credit exposure (dollars in thousands):

<table>
<thead>
<tr>
<th>Carrying Amount by Credit Rating - Moody's/S&amp;P/Fitch</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment Type</td>
</tr>
<tr>
<td>------------------------------------------------------</td>
</tr>
<tr>
<td>U.S. agencies</td>
</tr>
<tr>
<td>Mortgage pass throughs</td>
</tr>
<tr>
<td>Collateralized mortgage obligations</td>
</tr>
<tr>
<td>State and local government</td>
</tr>
<tr>
<td>Asset-backed securities</td>
</tr>
<tr>
<td>Repurchase agreements</td>
</tr>
<tr>
<td>Commercial paper</td>
</tr>
<tr>
<td>Annuity contracts</td>
</tr>
<tr>
<td>Money market mutual funds</td>
</tr>
<tr>
<td>Mutual bond funds</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>
NOTES TO THE FINANCIAL STATEMENTS

Component Units
(University of North Carolina System and State Education Assistance Authority)

University of North Carolina System

The General Statutes place no specific investment restrictions on the University of North Carolina System (the UNC System). However, in the absence of specific legislation, the form of governance over these investments would be the prudent-person or prudent-expert rule. These rules are broad statements of intent, generally requiring investment selection and management to be made with prudent, discreet, and intelligent judgment and care. The University of North Carolina at Chapel Hill (the University) operates an Investment Fund, which is a governmental external investment pool. The University operates the Investment Fund for charitable, nonprofit foundations, associations, trusts, endowments and funds that are organized and operated primarily to support the University. Separate financial statements for the Investment Fund may be obtained from the University.

At year-end, the UNC System had the following investments and maturities that were maintained outside the State Treasurer (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Less Than 1</th>
<th>1 to 5</th>
<th>6 to 10</th>
<th>More Than 10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt securities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>43,385</td>
<td>5,533</td>
<td>16,297</td>
<td>445</td>
<td>21,111</td>
</tr>
<tr>
<td>U.S. Treasury STRIPS</td>
<td>2,337</td>
<td>—</td>
<td>2,337</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>38,033</td>
<td>13,325</td>
<td>18,135</td>
<td>2,600</td>
<td>3,973</td>
</tr>
<tr>
<td>Mortgage pass throughs</td>
<td>68,032</td>
<td>1,292</td>
<td>6,035</td>
<td>13,817</td>
<td>47,088</td>
</tr>
<tr>
<td>Collateralised mortgage obligations</td>
<td>142,218</td>
<td>—</td>
<td>2,084</td>
<td>6,026</td>
<td>134,104</td>
</tr>
<tr>
<td>State and local government</td>
<td>2,506</td>
<td>60</td>
<td>2,216</td>
<td>83</td>
<td>149</td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>1,991</td>
<td>—</td>
<td>—</td>
<td>1,426</td>
<td>563</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>672</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Money market mutual funds</td>
<td>222,445</td>
<td>220,445</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Mutual bond funds</td>
<td>175,759</td>
<td>21,651</td>
<td>37,498</td>
<td>108,313</td>
<td>8,287</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>36,476</td>
<td>2,057</td>
<td>18,522</td>
<td>1,501</td>
<td>14,396</td>
</tr>
<tr>
<td>Foreign corporate bonds</td>
<td>2,458</td>
<td>15</td>
<td>5,068</td>
<td>4,381</td>
<td>14</td>
</tr>
<tr>
<td>Total investment securities</td>
<td>761,217</td>
<td>264,792</td>
<td>108,865</td>
<td>138,574</td>
<td>229,085</td>
</tr>
</tbody>
</table>

Other securities:

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>International mutual funds</td>
<td>79,820</td>
</tr>
<tr>
<td>Other mutual funds</td>
<td>425,466</td>
</tr>
<tr>
<td>Investments in real estate</td>
<td>56,164</td>
</tr>
<tr>
<td>Real estate investment trusts</td>
<td>14,708</td>
</tr>
<tr>
<td>Limited partnerships</td>
<td>857,899</td>
</tr>
<tr>
<td>Pooled investments</td>
<td>359</td>
</tr>
<tr>
<td>Domestic stocks</td>
<td>266,709</td>
</tr>
<tr>
<td>Foreign stocks</td>
<td>37,875</td>
</tr>
<tr>
<td>Other</td>
<td>510,444</td>
</tr>
<tr>
<td>Total investment securities</td>
<td>3,081,161</td>
</tr>
</tbody>
</table>

Limited Partnerships – The limited partnership positions are primarily held by the University of North Carolina at Chapel Hill. The University uses various external money managers to identify specific investment funds and limited partnerships that meet asset allocation and investment management objectives. The University invests in these funds and partnerships to increase the yield and return on its investment portfolio given the available alternative investment opportunities and to diversify its asset holdings. These investments generally include equity and bond funds. Certain investment funds expose the University to significant amounts of market risk by trading or holding derivative securities and by leveraging the securities in the fund. The University limits the amount of funds managed by any single asset manager and also limits the amount of funds to be invested in particular security classes.

Interest Rate Risk and Credit Risk. The constituent institutions of the UNC System generally do not have formal investment policies that address interest rate risk or credit risk. At year-end, the UNC System’s investments maintained outside the State Treasurer had the following credit quality distribution for securities with credit exposure (dollars in thousands):
Notes to the Financial Statements

Carrying Amount by Credit Rating - Moody's/S&P/Fitch

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Aaa/AAA</th>
<th>Aa/AA</th>
<th>A</th>
<th>Baa/BBB</th>
<th>Ba/BB</th>
<th>and Below</th>
<th>Unrated</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. agencies</td>
<td>13,380</td>
<td>-</td>
<td>3,139</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>18,576</td>
</tr>
<tr>
<td>Mortgage pass throughs</td>
<td>4,739</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>82,907</td>
</tr>
<tr>
<td>Collateralized mortgage obligations</td>
<td>72,433</td>
<td>8,407</td>
<td>38,573</td>
<td>1,275</td>
<td>-</td>
<td>-</td>
<td>21,482</td>
</tr>
<tr>
<td>State and local government</td>
<td>2,306</td>
<td>107</td>
<td>-</td>
<td>35</td>
<td>-</td>
<td>-</td>
<td>60</td>
</tr>
<tr>
<td>Asset-backed securities</td>
<td>1,457</td>
<td>-</td>
<td>35</td>
<td>499</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Money market mutual funds</td>
<td>45,658</td>
<td>-</td>
<td>169,138</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>8,053</td>
</tr>
<tr>
<td>Mutual bond funds</td>
<td>71,871</td>
<td>50,351</td>
<td>17,013</td>
<td>5,790</td>
<td>14,629</td>
<td>-</td>
<td>6,005</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>6,362</td>
<td>1,028</td>
<td>18,140</td>
<td>10,654</td>
<td>292</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Foreign corporate bonds</td>
<td>-</td>
<td>5,028</td>
<td>37</td>
<td>47</td>
<td>4,346</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>218,306</td>
<td>78,058</td>
<td>242,938</td>
<td>18,300</td>
<td>19,267</td>
<td>115,083</td>
<td></td>
</tr>
</tbody>
</table>

Custodial Credit Risk. The constituent institutions of the UNC System generally do not have formal investment policies that address custodial credit risk. At year-end, the UNC System's investments maintained outside the State Treasurer were exposed to custodial credit risk as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Carrying Amount</th>
<th>Held by Counterparty's Trust Dept. or Agent but not in State's Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment Type</td>
<td>Held by Counterparty</td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>$ 12,620</td>
</tr>
<tr>
<td>U.S. agencies</td>
<td>$ 12,895</td>
</tr>
<tr>
<td>Mortgage pass throughs</td>
<td>$ 15,901</td>
</tr>
<tr>
<td>Collateralized mortgage obligations</td>
<td>$ 9,094</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>$ 672</td>
</tr>
<tr>
<td>Domestic corporate bonds</td>
<td>$ 14,245</td>
</tr>
<tr>
<td>Domestic stocks</td>
<td>$ 53,291</td>
</tr>
<tr>
<td>Foreign stocks</td>
<td>$ 281</td>
</tr>
<tr>
<td>Total</td>
<td>$ 119,899</td>
</tr>
</tbody>
</table>

Foreign Currency Risk. The constituent institutions of the UNC System do not have formal investment policies that address foreign currency risk. At year-end, the UNC System's investments maintained outside the State Treasurer were exposed to foreign currency risk as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Carrying Amount</th>
<th>Foreign Stocks</th>
<th>Limited Partnerships</th>
</tr>
</thead>
<tbody>
<tr>
<td>Currency</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Euro</td>
<td>$ 1,807</td>
<td>$ 21,395</td>
</tr>
<tr>
<td>Japanese Yen</td>
<td>$ 15,060</td>
<td>667</td>
</tr>
<tr>
<td>Pound Sterling</td>
<td></td>
<td>4,462</td>
</tr>
<tr>
<td>Canadian Dollar</td>
<td>$ 3,798</td>
<td>-</td>
</tr>
<tr>
<td>Singapore Dollar</td>
<td>$ 1,624</td>
<td>-</td>
</tr>
<tr>
<td>Other Currencies</td>
<td>$ 1,599</td>
<td>89</td>
</tr>
<tr>
<td>Total</td>
<td>$ 24,658</td>
<td>$ 26,613</td>
</tr>
</tbody>
</table>
NOTES TO THE FINANCIAL STATEMENTS

The State Education Assistance Authority

The State Education Assistance Authority (the Authority) is authorized by the University of North Carolina Board of Governors pursuant to General Statute 116-36.2 to invest its special funds in the same manner as the State Treasurer is required to invest, as discussed in Section A of this note.

Investments. In accordance with bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

The Authority does not have a formal investment policy that addresses interest rate risk. The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2006, for the Authority's investments (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
<th>Investment Maturities (in Years)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Less</td>
<td>1 to 5</td>
</tr>
<tr>
<td></td>
<td>Than 1</td>
<td></td>
</tr>
<tr>
<td>Debt securities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Treasuries</td>
<td>$ 12,220</td>
<td>$ —</td>
</tr>
<tr>
<td>Repurchase agreements</td>
<td>8,869</td>
<td>—</td>
</tr>
<tr>
<td>Mutual bond funds</td>
<td>29,646</td>
<td>—</td>
</tr>
<tr>
<td>Money market mutual funds</td>
<td>489</td>
<td>489</td>
</tr>
<tr>
<td></td>
<td>51,224</td>
<td>$ 489</td>
</tr>
</tbody>
</table>

Other securities:

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>International mutual funds</td>
<td>18,759</td>
</tr>
<tr>
<td>Other mutual funds</td>
<td>101,897</td>
</tr>
<tr>
<td>Domestic stocks</td>
<td>19,822</td>
</tr>
<tr>
<td>Investment contracts</td>
<td>326,611</td>
</tr>
<tr>
<td>Other</td>
<td>15,402</td>
</tr>
<tr>
<td>Total investment securities</td>
<td>$ 533,715</td>
</tr>
</tbody>
</table>

Credit Risk. The Authority has formally adopted investment policies for credit risk stating that certain investment obligations shall bear one of the two highest ratings by nationally recognized rating services. As of June 30, 2006, the Authority's investments were rated as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Carrying Amount by Credit Rating - S&amp;P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment Type</td>
</tr>
<tr>
<td>Repurchase agreements</td>
</tr>
<tr>
<td>Money market mutual funds</td>
</tr>
<tr>
<td>Mutual bond funds</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

Custodial Credit Risk. The Authority does not have a formal policy that addresses custodial credit risk. The Authority's investments were exposed to custodial credit risk as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Carrying Amount Held by Counterparty's Trust Dept. or Agent but not in State's Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Repurchase agreements</td>
<td>$ 8,869</td>
</tr>
<tr>
<td>Domestic stocks</td>
<td>19,822</td>
</tr>
<tr>
<td>Total</td>
<td>$ 28,691</td>
</tr>
</tbody>
</table>

Concentration of Credit Risk. The Authority places no limit on the amount that may be invested in any one issuer. More than 5% of the Authority's investments are in Trinity Funding, FSA Capital Management, and IXIS Funding. These investments are 33.05%, 10.7%, and 17.45%, respectively, of the Authority's investments.
NOTE 4: RECEIVABLES

Receivables at year-end are reported net of allowances for doubtful accounts as follows (dollars in thousands):

**Governmental Activities:**

<table>
<thead>
<tr>
<th></th>
<th>General Fund</th>
<th>Highway Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>Internal Service Funds(1)</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Receivables, gross (excluding notes)</td>
<td>$3,588,231</td>
<td>$184,010</td>
<td>$41,294</td>
<td>$41,473</td>
<td>$10,160</td>
<td>$3,845,168</td>
</tr>
<tr>
<td>Allowance for doubtful accounts</td>
<td>- (443,626)</td>
<td>(6,834)</td>
<td>-</td>
<td>(61)</td>
<td>-</td>
<td>- (450,521)</td>
</tr>
<tr>
<td>Receivables, net</td>
<td>$3,144,606</td>
<td>$177,176</td>
<td>$41,294</td>
<td>$41,412</td>
<td>$10,160</td>
<td>$3,384,647</td>
</tr>
<tr>
<td>Notes receivable, gross</td>
<td>$6,578</td>
<td>$1,102</td>
<td>$107</td>
<td>$375,652</td>
<td>-</td>
<td>$383,439</td>
</tr>
<tr>
<td>Allowance for doubtful accounts</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(41,290)</td>
<td>-</td>
<td>(41,290)</td>
</tr>
<tr>
<td>Notes receivable, net</td>
<td>$6,578</td>
<td>$1,102</td>
<td>$107</td>
<td>$334,362</td>
<td>-</td>
<td>$342,149</td>
</tr>
</tbody>
</table>

(1) Includes balances due from fiduciary funds.

Within governmental activities, the only significant receivables not expected to be collected within one year are $217.39 million of notes receivable in other governmental funds, $6.58 million of notes receivable in the General Fund and $5.84 million in accounts receivable in the General Fund.

**Business-Type Activities:**

<table>
<thead>
<tr>
<th></th>
<th>Unemployment Compensation Fund</th>
<th>EPA Revolving Loan Fund</th>
<th>N.C. State Lottery Fund</th>
<th>Other Enterprise Funds</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Receivables, gross (excluding notes)</td>
<td>$432,699</td>
<td>$4,013</td>
<td>$10,231</td>
<td>$8,444</td>
<td>$455,387</td>
</tr>
<tr>
<td>Allowance for doubtful accounts</td>
<td>- (48,446)</td>
<td>-</td>
<td>-</td>
<td>(20)</td>
<td>(48,466)</td>
</tr>
<tr>
<td>Receivables, net</td>
<td>$384,253</td>
<td>$4,013</td>
<td>$10,231</td>
<td>$8,424</td>
<td>$406,921</td>
</tr>
<tr>
<td>Notes receivable, gross</td>
<td>-</td>
<td>$545,570</td>
<td>-</td>
<td>-</td>
<td>$545,570</td>
</tr>
<tr>
<td>Allowance for doubtful accounts</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Notes receivable, net</td>
<td>-</td>
<td>$545,570</td>
<td>-</td>
<td>-</td>
<td>$545,570</td>
</tr>
</tbody>
</table>

Within business-type activities, the only significant receivables not expected to be collected within one year are $513.14 million of notes receivable in the EPA Revolving Loan Fund. Revenues of other enterprise funds are net of uncollectible amounts. The total amounts related to revenues of the current period are $24 thousand related to sales and services used as security for bonds.
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## Note 5: Capital Assets

**Primary Government.** A summary of changes in capital assets for the year ended June 30, 2006 is presented below (dollars in thousands).

### Governmental Activities:

<table>
<thead>
<tr>
<th></th>
<th>Balance July 1, 2005 (as restated)</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capital Assets, nondepreciable:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$8,913,829</td>
<td>$530,808</td>
<td>$(5,021)</td>
<td>$9,439,616</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>48,975</td>
<td>11,510</td>
<td>—</td>
<td>60,485</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>1,960,204</td>
<td>1,540,342</td>
<td>(1,782,418)</td>
<td>1,718,128</td>
</tr>
<tr>
<td><strong>Total capital assets-nondepreciable</strong></td>
<td>10,923,008</td>
<td>2,082,660</td>
<td>(1,787,439)</td>
<td>11,218,229</td>
</tr>
</tbody>
</table>

| **Capital Assets, depreciable:** |                                    |           |            |                       |
| Buildings              | 2,300,307                          | 263,719   | (37,043)   | 2,526,983             |
| Machinery and equipment | 1,502,431                          | 134,607   | (91,287)   | 1,545,751             |
| Intangibles            | 200,146                            | 4,215     | (5,366)    | 198,995               |
| General infrastructure | 176,331                            | 5,975     | (10,966)   | 171,340               |
| State highway system   | 19,419,720                         | 1,540,182 | (41,439)   | 20,918,463            |
| **Total capital assets-depreciable** | 23,598,935                         | 1,948,698 | (186,101) | 25,361,532            |

**Less accumulated depreciation for:**

| Buildings              | (667,366)                          | (52,863)  | 17,436     | (702,793)             |
| Machinery and equipment | (947,947)                          | (109,104) | 77,318     | (979,733)             |
| Intangibles            | (94,101)                           | (4,870)   | 5,232      | (93,739)              |
| General infrastructure | (97,273)                           | (5,889)   | 9,062      | (94,100)              |
| State highway system   | (5,172,498)                        | (418,274) | 40,611     | (5,550,161)           |
| **Total accumulated depreciation** | (6,979,185)                        | (591,000) | 149,659    | (7,420,526)           |
| **Total capital assets-depreciable, net** | 16,619,750                         | 1,357,698 | (36,442)   | 17,941,006            |

**Governmental activities**

| capital assets, net     | $27,542,758                         | $3,440,358 | $(1,823,881)| $29,159,235           |
### Business-type Activities:

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>July 1, 2005 (as restated)</td>
<td></td>
<td></td>
<td>June 30, 2006</td>
</tr>
<tr>
<td><strong>Capital Assets, nondepreciable:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$3,147</td>
<td>$-</td>
<td>$-</td>
<td>$3,147</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>1,811</td>
<td>482</td>
<td>-</td>
<td>2,293</td>
</tr>
<tr>
<td>Total capital assets-nondepreciable</td>
<td>4,958</td>
<td>482</td>
<td>-</td>
<td>5,440</td>
</tr>
<tr>
<td><strong>Capital Assets, depreciable:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>33,982</td>
<td>-</td>
<td>-</td>
<td>33,982</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>5,661</td>
<td>1,043</td>
<td>(1,505)</td>
<td>5,199</td>
</tr>
<tr>
<td>General infrastructure</td>
<td>47,304</td>
<td>218</td>
<td>-</td>
<td>47,522</td>
</tr>
<tr>
<td>Intangible Assets</td>
<td>1,569</td>
<td>-</td>
<td>(112)</td>
<td>1,457</td>
</tr>
<tr>
<td>Total capital assets-depreciable</td>
<td>88,516</td>
<td>1,261</td>
<td>(1,617)</td>
<td>88,160</td>
</tr>
<tr>
<td><strong>Less accumulated depreciation for:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>(19,472)</td>
<td>(812)</td>
<td>-</td>
<td>(19,284)</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>(3,822)</td>
<td>(253)</td>
<td>1,338</td>
<td>(2,737)</td>
</tr>
<tr>
<td>General infrastructure</td>
<td>(16,535)</td>
<td>(2,015)</td>
<td>-</td>
<td>(18,550)</td>
</tr>
<tr>
<td>Total accumulated depreciation</td>
<td>(38,829)</td>
<td>(3,080)</td>
<td>1,338</td>
<td>(40,571)</td>
</tr>
<tr>
<td>Total capital assets-depreciable, net</td>
<td>49,687</td>
<td>(1,319)</td>
<td>(279)</td>
<td>47,589</td>
</tr>
<tr>
<td><strong>Business-type activities capital assets, net</strong></td>
<td>$54,645</td>
<td>($1,337)</td>
<td>($279)</td>
<td>$53,029</td>
</tr>
</tbody>
</table>

Depreciation expense was charged to functions/programs of the primary government as follows (dollars in thousands):

**Governmental activities:**

<table>
<thead>
<tr>
<th>Function/Program</th>
<th>Amount (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>General government</td>
<td>$36,206</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>$1,977</td>
</tr>
<tr>
<td>Higher Education</td>
<td>$60</td>
</tr>
<tr>
<td>Health and human services</td>
<td>$12,640</td>
</tr>
<tr>
<td>Economic development</td>
<td>$1,205</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>$12,881</td>
</tr>
<tr>
<td>Public safety, correction, and regulation</td>
<td>$49,059</td>
</tr>
<tr>
<td>Transportation</td>
<td>$473,093</td>
</tr>
<tr>
<td>Agriculture</td>
<td>$3,680</td>
</tr>
<tr>
<td><strong>Total depreciation expense</strong></td>
<td><strong>$591,001</strong></td>
</tr>
</tbody>
</table>

**Business-type activities:**

<table>
<thead>
<tr>
<th>Function/Program</th>
<th>Amount (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Town of Butner Water and Sewer</td>
<td>$1,662</td>
</tr>
<tr>
<td>N.C. State Fair</td>
<td>$618</td>
</tr>
<tr>
<td>USS North Carolina Battleship Commission</td>
<td>$128</td>
</tr>
<tr>
<td>Agricultural Farmers Market</td>
<td>$292</td>
</tr>
<tr>
<td>EPA Revolving Loan Fund</td>
<td>$21</td>
</tr>
<tr>
<td>State Banking Commission</td>
<td>$8</td>
</tr>
<tr>
<td>ABC Commission</td>
<td>$117</td>
</tr>
<tr>
<td>Utilities Commission</td>
<td>$67</td>
</tr>
<tr>
<td>N.C. State Lottery</td>
<td>$76</td>
</tr>
<tr>
<td>Other business-type activities</td>
<td>$91</td>
</tr>
<tr>
<td><strong>Total depreciation expense</strong></td>
<td><strong>$3,080</strong></td>
</tr>
</tbody>
</table>
Component Units (University of North Carolina System and Community Colleges). Capital asset activity for the University of North Carolina System and Community Colleges for the fiscal year ended June 30, 2006, was as follows (dollars in thousands):

### University of North Carolina System:

<table>
<thead>
<tr>
<th>Capital Assets, nondepreciable:</th>
<th>Balance</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Land</strong></td>
<td>195,536</td>
<td>6,303</td>
<td>(262)</td>
<td>201,577</td>
</tr>
<tr>
<td><strong>Art, literature, and other artifacts</strong></td>
<td>99,433</td>
<td>8,824</td>
<td>(380)</td>
<td>107,877</td>
</tr>
<tr>
<td><strong>Construction in progress</strong></td>
<td>1,032,320</td>
<td>720,760</td>
<td>(653,182)</td>
<td>1,099,898</td>
</tr>
<tr>
<td><strong>Total capital assets-nondepreciable</strong></td>
<td>1,327,289</td>
<td>735,887</td>
<td>(653,824)</td>
<td>1,409,352</td>
</tr>
</tbody>
</table>

### Capital Assets, depreciable:

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Buildings</strong></td>
<td>5,208,707</td>
<td>848,363</td>
<td>(5,906)</td>
<td>6,051,164</td>
</tr>
<tr>
<td><strong>Machinery and equipment</strong></td>
<td>1,288,032</td>
<td>124,414</td>
<td>(66,489)</td>
<td>1,345,957</td>
</tr>
<tr>
<td><strong>Intangibles</strong></td>
<td>1,000</td>
<td>—</td>
<td>—</td>
<td>1,000</td>
</tr>
<tr>
<td><strong>Art, literature, and other artifacts</strong></td>
<td>1,907</td>
<td>59</td>
<td>—</td>
<td>1,966</td>
</tr>
<tr>
<td><strong>General infrastructure</strong></td>
<td>803,270</td>
<td>38,308</td>
<td>(138)</td>
<td>841,442</td>
</tr>
<tr>
<td><strong>Total capital assets-depreciable</strong></td>
<td>7,302,916</td>
<td>1,011,144</td>
<td>(72,531)</td>
<td>8,241,529</td>
</tr>
</tbody>
</table>

#### Less accumulated depreciation for:

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Buildings</strong></td>
<td>(1,585,088)</td>
<td>(151,747)</td>
<td>5,451</td>
<td>(1,731,384)</td>
</tr>
<tr>
<td><strong>Machinery and equipment</strong></td>
<td>(833,777)</td>
<td>(101,556)</td>
<td>55,337</td>
<td>(879,996)</td>
</tr>
<tr>
<td><strong>Art, literature, and other artifacts</strong></td>
<td>(800)</td>
<td>(149)</td>
<td>—</td>
<td>(949)</td>
</tr>
<tr>
<td><strong>General infrastructure</strong></td>
<td>(279,986)</td>
<td>(28,160)</td>
<td>149</td>
<td>(298,997)</td>
</tr>
<tr>
<td><strong>Total accumulated depreciation</strong></td>
<td>(2,690,651)</td>
<td>(281,612)</td>
<td>60,937</td>
<td>(2,911,326)</td>
</tr>
<tr>
<td><strong>Total capital assets-depreciable, net</strong></td>
<td>4,612,265</td>
<td>729,532</td>
<td>(11,594)</td>
<td>5,330,203</td>
</tr>
</tbody>
</table>

**University of North Carolina System capital assets, net**

|                         | $ 5,939,554 | $ 1,465,419 | $ (665,418) | $ 6,739,555 |

Capital assets of nongovernmental component units of the University of North Carolina System are excluded from the above amounts. At June 30, 2006, nongovernmental component unit foundations and similarly affiliated organizations of the University of North Carolina System had nondepreciable capital assets of $29.961 million and net depreciable capital assets of $149.873 million.
### Community Colleges:

<table>
<thead>
<tr>
<th></th>
<th>Balance July 1, 2005 (as restated)</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capital Assets, nondepreciable:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>$97,412</td>
<td>$4,692</td>
<td>$-</td>
<td>$102,104</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>355</td>
<td>-</td>
<td>-</td>
<td>355</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>232,469</td>
<td>129,651</td>
<td>(159,657)</td>
<td>202,463</td>
</tr>
<tr>
<td><strong>Total capital assets-nondepreciable</strong></td>
<td>330,236</td>
<td>134,343</td>
<td>(159,657)</td>
<td>304,922</td>
</tr>
<tr>
<td><strong>Capital Assets, depreciable:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>1,341,716</td>
<td>176,572</td>
<td>(938)</td>
<td>1,517,350</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>183,689</td>
<td>22,969</td>
<td>(7,577)</td>
<td>199,081</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>46</td>
<td>-</td>
<td>-</td>
<td>46</td>
</tr>
<tr>
<td>General infrastructure</td>
<td>68,333</td>
<td>9,964</td>
<td>(62)</td>
<td>78,235</td>
</tr>
<tr>
<td><strong>Total capital assets-depreciable</strong></td>
<td>1,593,784</td>
<td>209,505</td>
<td>(8,577)</td>
<td>1,794,712</td>
</tr>
<tr>
<td><strong>Less accumulated depreciation for:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>(409,724)</td>
<td>(35,667)</td>
<td>539</td>
<td>(444,852)</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>(111,451)</td>
<td>(13,600)</td>
<td>6,522</td>
<td>(118,529)</td>
</tr>
<tr>
<td>Art, literature, and other artifacts</td>
<td>(18)</td>
<td>(3)</td>
<td>-</td>
<td>(21)</td>
</tr>
<tr>
<td>General infrastructure</td>
<td>(33,427)</td>
<td>(3,319)</td>
<td>64</td>
<td>(36,682)</td>
</tr>
<tr>
<td><strong>Total accumulated depreciation</strong></td>
<td>(554,620)</td>
<td>(52,589)</td>
<td>7,125</td>
<td>(600,084)</td>
</tr>
<tr>
<td><strong>Total capital assets-depreciable, net</strong></td>
<td>1,039,164</td>
<td>156,916</td>
<td>(1,452)</td>
<td>1,194,628</td>
</tr>
<tr>
<td><strong>Community Colleges capital assets, net</strong></td>
<td>$1,369,400</td>
<td>$291,259</td>
<td>$(161,109)</td>
<td>$1,499,550</td>
</tr>
</tbody>
</table>

Capital assets of nongovernmental component units of community colleges are excluded from the above amounts. At June 30, 2006, nongovernmental component unit foundations and similarly affiliated organizations of community colleges had nondepreciable capital assets of $1.194 million and net depreciable capital assets of $1.780 million.
NOTE 6: SHORT-TERM DEBT

Primary Government

Beginning January 1, 2006, the State received repayable advances from the Federal Unemployment Account (FUA) to finance an operating deficit in the State's unemployment compensation fund. The tax anticipation notes issued for the period September 30, 2005 through December 31, 2005 were repaid as employer contributions became available beginning January 1, 2006. Once the tax anticipation notes were repaid in total, the State used the employer contributions to pay back the FUA borrowing as of May 31, 2006. Advances taken from January 1, 2006 through September 30, 2006, which are repaid in full on or before September 30, 2006 are considered cash flow advances and do not accrue interest provided that the State does not take additional advances from October 1, 2006 through December 31, 2006. The State does not plan to take additional FUA advances or issue tax anticipation notes through December 31, 2006.

Short-term debt activity for the fiscal year ended June 30, 2006, was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Draws</th>
<th>Repayments</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>July 1, 2005</td>
<td></td>
<td>June 30, 2006</td>
<td></td>
</tr>
<tr>
<td>FUA Advance............</td>
<td>$ 113,690</td>
<td>$ 256,185</td>
<td>$ (369,875)</td>
<td>$ —</td>
</tr>
<tr>
<td>Anticipation Notes.....</td>
<td>—</td>
<td>77,133</td>
<td>(77,133)</td>
<td>—</td>
</tr>
</tbody>
</table>

Component Units

University of North Carolina System

North Carolina State University has available commercial paper program financing for short-term credit up to $100 million to finance capital construction projects. The University's available funds are pledged to the commercial paper program financing with the anticipation of converting to general revenue bond financing in the future. As of June 30, 2006, $16 million in tax-exempt commercial paper was outstanding.

Commercial paper was issued from the University of North Carolina General Revenue Bonds, Series 2002A, to provide interim financing for the construction of capital projects. Commercial paper was redeemed with proceeds from the University of North Carolina General Revenue Refunding Bonds, Series 2005.

North Carolina A&T University borrowed $6.168 million June 1, 2006. Proceeds from the note are being used for capital construction projects. The note will be repaid from bond proceeds when the University issues bonds in the fall of 2006.

Short-term debt activity for the University of North Carolina System for the fiscal year ended June 30, 2006, was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Draws</th>
<th>Repayments</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>July 1, 2005</td>
<td></td>
<td>June 30, 2006</td>
<td></td>
</tr>
<tr>
<td>Commercial Paper</td>
<td>$ 143,141</td>
<td>$ 113,000</td>
<td>(122,727)</td>
<td>$ 133,414</td>
</tr>
<tr>
<td>Anticipation Notes.....</td>
<td>—</td>
<td>6,168</td>
<td>—</td>
<td>6,168</td>
</tr>
</tbody>
</table>
### NOTE 7: LONG-TERM LIABILITIES

#### A. Changes in Long-Term Liabilities

**Primary Government.** Long-term liability activity for the year ended June 30, 2006, was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Balance</th>
<th>Amounts Due Within One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>July 1, 2005</td>
<td>(as restated)</td>
<td></td>
<td>June 30, 2006</td>
<td></td>
</tr>
<tr>
<td><strong>Governmental activities:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds and similar debt payable:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General obligation bonds</td>
<td>$5,698,535</td>
<td>$370,000</td>
<td>($329,720)</td>
<td>$5,738,815</td>
<td>$343,615</td>
</tr>
<tr>
<td>Lease-purchase revenue bonds</td>
<td>265,045</td>
<td>-</td>
<td>(10,000)</td>
<td>255,045</td>
<td>10,000</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>475,170</td>
<td>-</td>
<td>(21,110)</td>
<td>454,060</td>
<td>21,420</td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For issuance discounts</td>
<td>(1,175)</td>
<td>-</td>
<td>454</td>
<td>(721)</td>
<td>-</td>
</tr>
<tr>
<td>On refunding</td>
<td>(119,653)</td>
<td>-</td>
<td>16,594</td>
<td>(103,059)</td>
<td>-</td>
</tr>
<tr>
<td>Add issuance premium</td>
<td>339,004</td>
<td>15,700</td>
<td>(41,451)</td>
<td>313,253</td>
<td>-</td>
</tr>
<tr>
<td>Total bonds and similar debt payable</td>
<td>6,656,926</td>
<td>385,700</td>
<td>(385,233)</td>
<td>6,657,393</td>
<td>375,035</td>
</tr>
<tr>
<td>Notes payable</td>
<td>37,107</td>
<td>30,688</td>
<td>(6,954)</td>
<td>60,841</td>
<td>26,334</td>
</tr>
<tr>
<td>Capital leases payable</td>
<td>297</td>
<td>26,745</td>
<td>(163)</td>
<td>26,879</td>
<td>982</td>
</tr>
<tr>
<td>Arbitrage rebate payable</td>
<td>-</td>
<td>508</td>
<td>-</td>
<td>508</td>
<td>-</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>320,595</td>
<td>270,792</td>
<td>(216,592)</td>
<td>374,795</td>
<td>36,679</td>
</tr>
<tr>
<td>Net pension obligation</td>
<td>2,044</td>
<td>14,544</td>
<td>(14,961)</td>
<td>1,627</td>
<td>-</td>
</tr>
<tr>
<td>Workers’ compensation</td>
<td>5,500</td>
<td>583</td>
<td>(817)</td>
<td>5,266</td>
<td>1,122</td>
</tr>
<tr>
<td>Deferred death benefit payable</td>
<td>400</td>
<td>-</td>
<td>(60)</td>
<td>340</td>
<td>210</td>
</tr>
<tr>
<td>Cost settlement payable</td>
<td>5,000</td>
<td>151,500</td>
<td>(2,500)</td>
<td>154,000</td>
<td>109,000</td>
</tr>
<tr>
<td><strong>Total Governmental activity long-term liabilities</strong></td>
<td>$7,027,869</td>
<td>$881,060</td>
<td>($627,280)</td>
<td>$7,281,649</td>
<td>$549,362</td>
</tr>
<tr>
<td><strong>Business-type activities:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonds payable:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$9,070</td>
<td>-</td>
<td>($270)</td>
<td>$8,800</td>
<td>$280</td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>9,070</td>
<td>-</td>
<td>(270)</td>
<td>8,800</td>
<td>280</td>
</tr>
<tr>
<td>Notes payable</td>
<td>1,569</td>
<td>-</td>
<td>(112)</td>
<td>1,457</td>
<td>112</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>2,379</td>
<td>2,650</td>
<td>(1,222)</td>
<td>3,807</td>
<td>195</td>
</tr>
<tr>
<td>Business-type activity long-term liabilities</td>
<td>$13,018</td>
<td>$2,650</td>
<td>($1,604)</td>
<td>$14,064</td>
<td>$587</td>
</tr>
</tbody>
</table>

For governmental activities, the compensated absences, net pension obligation, workers’ compensation, and cost settlement liabilities are generally liquidated by the General Fund. Arbitrage rebate payable is generally liquidated by other governmental funds. A portion of compensated absences is also liquidated by the Highway Fund. Internal service funds predominantly serve the governmental funds. Accordingly, long-term liabilities for them are included as part of the above totals for governmental activities. At year-end, $3.861 million of internal service funds compensated absences are included in the above amounts.
### Component Units

(University of North Carolina System, North Carolina Housing Finance Agency, and the State Education Assistance Authority). Long-term liability activity for the year ended June 30, 2006, was as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>University of North Carolina System:</th>
<th>Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Balance</th>
<th>Amounts Due Within One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonds payable:</td>
<td>July 1, 2005</td>
<td></td>
<td></td>
<td>June 30, 2006</td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$1,737,063</td>
<td>$412,160</td>
<td>$129,840</td>
<td>$2,019,383</td>
<td>$180,876</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>31,185</td>
<td>—</td>
<td>1,395</td>
<td>29,790</td>
<td>1,755</td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For issuance discounts</td>
<td>(52,499)</td>
<td>—</td>
<td>3,928</td>
<td>(48,571)</td>
<td>—</td>
</tr>
<tr>
<td>On refunding</td>
<td>(27,064)</td>
<td>(2,286)</td>
<td>2,070</td>
<td>(27,280)</td>
<td>—</td>
</tr>
<tr>
<td>Add issuance premium</td>
<td>25,043</td>
<td>21,263</td>
<td>(2,360)</td>
<td>43,946</td>
<td>—</td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>1,713,728</td>
<td>431,137</td>
<td>(127,597)</td>
<td>2,017,268</td>
<td>182,631</td>
</tr>
<tr>
<td>Notes payable</td>
<td>69,780</td>
<td>98,787</td>
<td>(39,917)</td>
<td>128,650</td>
<td>38,344</td>
</tr>
<tr>
<td>Capital leases payable</td>
<td>43,649</td>
<td>63,155</td>
<td>(3,379)</td>
<td>103,425</td>
<td>9,042</td>
</tr>
<tr>
<td>Arbitrage rebate payable</td>
<td>3,795</td>
<td>116</td>
<td>(3,622)</td>
<td>289</td>
<td>20</td>
</tr>
<tr>
<td>Amortization and life income payable</td>
<td>10,688</td>
<td>1,342</td>
<td>(1,051)</td>
<td>10,979</td>
<td>973</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>233,424</td>
<td>206,350</td>
<td>(171,384)</td>
<td>268,390</td>
<td>27,534</td>
</tr>
<tr>
<td>Total long-term liabilities</td>
<td>$2,075,064</td>
<td>$800,887</td>
<td>$346,950</td>
<td>$2,529,001</td>
<td>$258,544</td>
</tr>
</tbody>
</table>

Long-term liabilities of nongovernmental component units of the University of North Carolina System are excluded from the above amounts. At June 30, 2006, nongovernmental component unit foundations and similarly affiliated organizations of the University of North Carolina System had total long-term liabilities of $336,963 million, of which $17.178 million was due within one year and $319.785 million was due in more than one year.

### North Carolina Housing Finance Agency:

<table>
<thead>
<tr>
<th>Bonds payable:</th>
<th>Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Balance</th>
<th>Amounts Due Within One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue bonds</td>
<td>July 1, 2005</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less deferred amounts:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For issuance discounts</td>
<td>(19,569)</td>
<td>(2,780)</td>
<td>3,306</td>
<td>(19,043)</td>
<td>—</td>
</tr>
<tr>
<td>On refunding</td>
<td>(145)</td>
<td>—</td>
<td>40</td>
<td>(105)</td>
<td>—</td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>1,292,151</td>
<td>397,220</td>
<td>(143,639)</td>
<td>1,545,732</td>
<td>178,050</td>
</tr>
<tr>
<td>Arbitrage rebate payable</td>
<td>297</td>
<td>308</td>
<td>(257)</td>
<td>348</td>
<td>144</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>583</td>
<td>347</td>
<td>(272)</td>
<td>658</td>
<td>30</td>
</tr>
<tr>
<td>Total long-term liabilities</td>
<td>$1,293,031</td>
<td>$397,875</td>
<td>$144,168</td>
<td>$1,546,738</td>
<td>$178,224</td>
</tr>
</tbody>
</table>

### State Education Assistance Authority:

<table>
<thead>
<tr>
<th>Bonds payable:</th>
<th>Balance</th>
<th>Increases</th>
<th>Decreases</th>
<th>Balance</th>
<th>Amounts Due Within One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue bonds</td>
<td>July 1, 2005</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total bonds payable</td>
<td>1,921,562</td>
<td>$806,300</td>
<td>(169,208)</td>
<td>2,558,654</td>
<td>$506,300</td>
</tr>
<tr>
<td>Arbitrage rebate payable</td>
<td>2,801</td>
<td>1,352</td>
<td>—</td>
<td>4,153</td>
<td>74</td>
</tr>
<tr>
<td>Compensated absences</td>
<td>190</td>
<td>75</td>
<td>(9)</td>
<td>256</td>
<td>9</td>
</tr>
<tr>
<td>Total long-term liabilities</td>
<td>$1,924,553</td>
<td>$807,727</td>
<td>(169,217)</td>
<td>$2,563,063</td>
<td>$506,383</td>
</tr>
</tbody>
</table>
NOTES TO THE FINANCIAL STATEMENTS

B. Bonds, Certificates of Participation, and Notes Payable

Bonds, certificates of participation, and notes payable at June 30, 2006 were as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Primary Government:</th>
<th>Interest Rates</th>
<th>Maturing Through Year</th>
<th>Original Issue Amount</th>
<th>Outstanding Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governmental activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General obligation bonds</td>
<td>2.13% - 6.90%*</td>
<td>2028</td>
<td>$6,201,384</td>
<td>$5,738,815</td>
</tr>
<tr>
<td>Lease-purchase revenue bonds</td>
<td>2.00% - 5.25%*</td>
<td>2024</td>
<td>227,045</td>
<td>255,045</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>3.25% - 5.25%*</td>
<td>2025</td>
<td>489,640</td>
<td>454,060</td>
</tr>
<tr>
<td>Notes payable</td>
<td>2.89% - 6.00%</td>
<td>2016</td>
<td>74,416</td>
<td>60,841</td>
</tr>
<tr>
<td>Business-type activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>3.38% - 4.21%*</td>
<td>2026</td>
<td>$9,905</td>
<td>8,800</td>
</tr>
<tr>
<td>Notes payable</td>
<td>0.00%</td>
<td>2019</td>
<td>1,569</td>
<td>1,457</td>
</tr>
<tr>
<td>Component Units:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>University of North Carolina System</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>1.63% - 10.00%*</td>
<td>2036</td>
<td>$2,329,204</td>
<td>$2,019,382</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>3.00% - 5.00%*</td>
<td>2035</td>
<td>31,545</td>
<td>29,790</td>
</tr>
<tr>
<td>Notes payable</td>
<td>0.91% - 9.45%*</td>
<td>2035</td>
<td>147,563</td>
<td>128,650</td>
</tr>
<tr>
<td>North Carolina Housing Finance Agency</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>2.00% - 8.25%*</td>
<td>2043</td>
<td>$3,341,066</td>
<td>$1,564,880</td>
</tr>
<tr>
<td>State Education Assistance Authority</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>3.45% - 6.35%*</td>
<td>2035</td>
<td>$2,609,850</td>
<td>$2,558,654</td>
</tr>
</tbody>
</table>

* For variable rate debt, interest rates in effect at June 30, 2006 are included. For variable rate debt with interest rate swaps, the synthetic fixed rates are included.

The full faith, credit, and taxing power of the State are pledged for the payment of principal and interest on general obligation bonds. The certificates of participation (COPs) and lease-purchase revenue bonds issued by the N.C. Infrastructure Finance Corporation, a blended component unit of the State, are secured by lease and installment payments made by the State and in the event of default, by a security interest in the leased facilities pursuant to a leasehold deed of trust (as applicable). The COPs issued for repair and renovation projects are not secured by a lien upon or security interest in the projects or in any other property of the State. All payments of the State for the COPs and lease-purchase revenue bonds are subject to appropriation by the General Assembly. Other long-term debts of the State and its component units are payable solely from certain resources of the funds to which they relate.

C. Bonds Authorized but Unissued

The amount of authorized but unissued general obligation bonds of the primary government at June 30, 2006, totaled $502.7 million as follows: higher education $403.5 million and clean water $99.2 million.

The amount of authorized but unissued debt of the primary government subject to annual appropriation requirements at June 30, 2006 totaled $622.4 million as follows: repair and renovation $175 million, universities $337.1 million, hospital $49 million, prisons $52.4 million, youth facilities $22 million, parks $20.8 million, and guaranteed energy savings contracts $26.1 million.

D. Demand Bonds

Included in bonds payable are several variable rate demand bond issues. Demand bonds are securities that contain a "put" feature that allows bondholders to demand payment before the maturity of the debt upon proper notice to the issuer's remarketing or paying agents.

Component Units

University of North Carolina System

With regards to the following demand bonds, the issuer has not entered into take out agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

The University of North Carolina at Chapel Hill - General Revenue, Series 2001B and 2001C

In 2001 the University issued two series of variable rate demand bonds in the amount of $54.97 million (2001B) and $54.97 million (2001C) that each have a final maturity date of December 1, 2025. The bonds are subject to mandatory sinking fund redemption on the interest payment date on or immediately preceding each December throughout the term of the bonds. The proceeds of these issuances were used to provide funds to refund in advance of their maturity the following issues: Ambulatory Care Clinic, Series 1990; Athletic Facilities, Series 1998; Carolina Inn, Series 1994; School of Dentistry, Series 1995; Kenan Stadium, Series 1996; and Parking System, Series...
1997C. While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the University's remarketing agents, Lehman Brothers, Inc (2001B) and UBS Financial Services, Inc. (2001C).

The University renewed its line of credit, in the amount of $107.46 million, with JP Morgan Chase Bank effective February 1, 2006. Under the line of credit agreement, the University is entitled to draw amounts sufficient to pay the principal and accrued interest on bonds delivered for purchase.

The University is required to pay a quarterly commitment fee for the line of credit of 0.1% per annum based on the unused portion of the line of credit commitment. If the University's credit rating for unsecured debt were to drop below AA3 (or its equivalent) by Moody’s Investors Service (Moody’s), AA- (or its equivalent) by Standard & Poor’s (S&P), or AA- (or its equivalent) by Fitch Ratings (Fitch), the quarterly commitment fee would increase to 0.15%. If the University’s credit rating for unsecured debt were to drop below A3 (or its equivalent) by Moody’s, A- (or its equivalent) by S&P, or A- (or its equivalent) by Fitch, the quarterly commitment fee would increase to 0.25%.

Under the line of credit agreement, the University has promised to repay loans that represent purchase drawings in equal semi-annual payments after termination of the line of credit. Interest at the rate of Prime plus 1% (Prime plus 2% after 60 days) is payable quarterly and upon draw repayment. At June 30, 2006, no purchase draws had been made under the line of credit.

The line of credit agreement expires on January 31, 2007. However, between November 3, 2006, and December 3, 2006, the University may request that the Bank extend the expiration date for another year. The Bank shall respond affirmatively or negatively within 30 days after receipt of such request.

North Carolina Central University – Revenue Bonds Series 2003A

In October of 2003, the North Carolina Capital Facilities Finance Agency issued Student Housing Facilities Revenue Demand Bonds ($21.48 million Variable Rate Revenue Demand Bonds, Series 2003A) that have a maturity date of October 1, 2034. The issuer, the North Carolina Capital Facilities Finance Agency, loaned the proceeds of the Series 2003 Bonds to the NCCU Real Estate Foundation, Inc. (Foundation). The Foundation used the proceeds to finance the costs of building a student housing facility at North Carolina Central University, to fund a debt service reserve fund for the 2003A Bonds, to pay a portion of the interest on the bonds during construction of the project, and to pay certain costs of issuance of the bonds. The 2003A Bonds are subject to mandatory sinking fund redemption at the principal amount on the interest payment dates or immediately preceding October 1, 2006.

The Student Housing Facilities Revenue Demand Bonds (Series 2003) has an Irrevocable Letter of Credit (LOC) for $21.82 million. The LOC is to secure the payment of the principal and purchase price of interest on the Series 2003 Bonds. The LOC was issued by Wachovia Bank, N.A. and expires on October 15, 2006. The LOC may be extended by request from the Foundation by delivering a notice of extension to the Trustee with a new expiration date. At June 30, 2006, the LOC rate for the bonds was 1.4% and the total amount drawn on it was $907 thousand.

The Foundation paid Wachovia Bank, N.A. a commitment fee of $109 thousand for the letter of credit on the date the bonds were issued. Additionally, the Foundation paid credit facility fees in the amount of $76 thousand during the fiscal year. If the Foundation terminates the letter of credit on or before August 1, 2006, then the Foundation must pay a termination fee of $25 thousand. The Bonds are not under a take out agreement; however, in the event of termination 100% of the unpaid principal will be due and payable plus any unpaid and accrued interest.

Under the LOC agreement, the proceeds of each drawing under the LOC to pay the portion of the purchase price of Series 2003 bonds allocable to principal will constitute a tender advance and must be reimbursed as provided in the agreement. The Foundation is required to repay each tender advance to Wachovia Bank, N.A. plus an interest rate of Prime plus 1%. The amount of any tender advance made is repaid based on the earliest to occur of the date the credit provider bonds purchased pursuant to such tender advances are remarketed, the close of business on the date that is 180 days after the tender was made, and/or the termination date.

The Student Housing Facilities Revenue Demand Bonds (Series 2003) has remarketing fees. The remarketing fee is an upfront charge to reset the interest rates on a weekly basis. The remarketing agent is Wachovia Bank, N.A. for the Series 2003A Bonds. At June 30, 2006, the remarketing fee rate for the bonds was 0.13%.

State Education Assistance Authority – Guaranteed Student Loan Revenue Bonds, Series 2005A

In October, 2005, the Authority issued Guaranteed Student Loan Revenue Bonds, Series 2005A, in the amount of $506.3 million consisting of four tranches of tax-exempt bonds totaling $471.6 million and two tranches of taxable bonds totaling $34.7 million. This series of bonds matures on September 1, 2035, but $12.4 million must be retired by mandatory sinking fund redemption on October 1, 2012. The proceeds of this issuance were used to finance student loans, refund the Authority's outstanding Series 1995A bonds, make a deposit to the operating fund, and pay issuance costs. While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven day's notice to the tender agent.

Payment of principal and interest on the Series 2005A bonds is insured by a financial guaranty insurance policy by Ambac Assurance Corporation. The Authority has entered into a
NOTES TO THE FINANCIAL STATEMENTS

standby bond purchase agreement with a commercial bank for each respective tranche. Pursuant to each agreement, the respective bank has agreed to purchase any bonds of that respective tranche that have been tendered for purchase during the term of the agreement.

With regards to the following demand bonds, the issuer has entered into take-out agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

North Carolina State University - General Revenue Bonds, Series 2003B

On June 20, 2003 the University issued tax-exempt variable rate revenue demand bonds in the amount of $45.66 million that have a final maturity date of October 1, 2027. The bonds are subject to mandatory sinking fund redemption that began on October 1, 2004. The University’s proceeds of this issuance were used to pay a portion of the costs of certain improvements on the campus of the University, to refund certain debt previously incurred for that purpose, and to pay the costs incurred in connection with the issuance of the 2003B bonds.

While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the paying agent, The Bank of New York. Upon notice from the paying agent, the remarketing agent, UBS Financial Services Inc., has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.

Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and Bayerische Landesbank, a Liquidity Facility has been established for the Trustee (The Bank of New York) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. This Agreement requires a commitment fee equal to 0.13% of the available commitment, payable quarterly in arrears, beginning on July 1, 2003 and on each October 1, January 1, April 1, and July 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Liquidity Provider Rate (the greater of the bank prime commercial lending rate and Federal Funds Rate plus 0.5%). Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each month in which Liquidity Provider Bonds are outstanding. At June 30, 2006, there were no Liquidity Provider Bonds held by the Liquidity Facility. The original Liquidity Facility expiration date has been extended and is scheduled to expire on November 30, 2015, unless otherwise extended based on the terms of the Agreement.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in twenty quarterly installments, beginning the first business day of January, April, July, or October, whichever first occurs on or following the Purchase Date along with accrued interest at the Liquidity Provider Rate. In the event the entire issue of $45.07 million of demand bonds was “put” and not resold, the University would be required to pay $11.22 million a year for 5 years under this agreement assuming an 8.75% interest rate.

University of North Carolina Hospitals - Revenue Bonds, Series 2001A and Series 2001B

On January 31, 2001, the Hospitals issued two series of tax-exempt variable rate demand bonds in the amount of $55 million (2001A) and $55 million (2001B) that have a final maturity date of February 15, 2031. The bonds are subject to mandatory sinking fund redemption that began on February 15, 2002. A portion of the proceeds was used to reimburse the Hospitals for $75 million spent allowing the UNC Health Care System to acquire controlling interest in Rex Healthcare Inc. The remaining proceeds are being used for the renovation of space vacated after the opening of the North Carolina Women’s Hospital, North Carolina Children’s Hospital, and associated support services. While initially bearing interest in a daily mode, the mode on these bonds may change to a weekly rate, a unit pricing rate, a term rate or a fixed rate.

While in daily mode, the bonds are subject to purchase on any business day upon demand by telephonic notice of tender to the remarketing agent on the purchase date and delivery to the bond tender agent, Wachovia Bank, N.A. The Hospitals’ remarketing agents, Merrill Lynch, Pierce, Fenner & Smith Incorporated (Series 2001A) and Banc of America Securities LLC (Series 2001B) have agreed to exercise their best efforts to remarket bonds for which a notice of purchase has been received. The quarterly remarketing fee is payable in arrears and is equal to either 0.05% or 0.08% of the outstanding principal amount of the bonds assigned to each agent, depending upon their performance in comparison to an established benchmark.

Under separate Standby Bond Purchase Agreements for the Series 2001A and Series 2001B (Agreements) between the Hospitals and Landesbank Hessen-Thüringen Girozentrale, a Liquidity Facility has been established for the tender agent to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. These Agreements require an adjustable facility fee based on the long-term rating of the bonds, which is calculated as a percentage of the available commitment. Payments are made quarterly in arrears, on the first business day of each July, October, January and April thereafter until the expiration date or the termination date of the Agreements. For the past fiscal year the percentage was 0.25% with the new long-term agreement that became effective.
on July 11, 2005. The percentage will remain 0.25% unless the bond ratings change.

Under the Agreements, any bonds purchased through the Liquidity Facility become Bank Bonds and shall, from the date of such purchase and while they are Bank Bonds, bear interest at the Formula Rate (Base Rate equal to the higher of the Prime Rate for such day or the sum of 0.5% plus the Federal Funds Rate) subject to a maximum rate as permitted by law. Upon remarketing of Bank Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Bank Bonds. Payment of the interest on the Bank Bonds is due quarterly (the first business day of January, April, July and October) for each period in which Bank Bonds are outstanding. At June 30, 2006, there were no Bank Bonds held by the Liquidity Facility.

Included in the Agreements is a take out provision, in case
the remarketing agent is unable to resell any bonds that are "put" within 90 days of the "put" date. In this situation, the Hospitals is required to redeem the Bank Bonds held by the Liquidity Facility. The agreements allow the Hospitals to redeem bank bonds in equal quarterly installments, on the first business day of January, April, July and October. The payments will commence with the first business day of any such month that is at least 90 days following the applicable purchase date of the Bank Bond and end no later than the fifth anniversary of such purchase date. If the take out agreement were to be exercised because the entire outstanding $104.8 million of demand bonds was "put" and not resold, the Hospitals would be required to pay $25.79 million a year for 5 years under the installment loan agreement assuming an 8.25% prime interest rate.

The current expiration date of the Agreements is December 31, 2015. The Liquidity Provider has the option to terminate its commitment on October 11, 2008, October 11, 2011, or October 11, 2014 by providing adequate notice of its intention. The Hospitals may request additional extensions of at least one year from the previous termination date. Extensions are at the discretion of Liquidity Provider.

University of North Carolina Hospitals - Revenue Refunding Bonds, Series 2003A and Series 2003B

On February 13, 2003, the Hospitals issued two series of tax-exempt variable rate demand bonds in the amount of $63.77 million (2003A) and $34.25 million (2003B) that have a final maturity date of February 1, 2029. The bonds are subject to mandatory sinking fund redemption that began on February 1, 2004. The proceeds were used to advance refund $88.33 million of the Series 1996 Bonds. While initially bearing interest in a weekly mode, the mode on these bonds may change to a daily rate, a unit pricing rate, a term rate or a fixed rate.

While in the weekly mode, the bonds are subject to purchase on demand with seven days notice to the remarketing agent and delivery to the bond tender agent, Wachovia Bank, N.A. The Hospitals’ remarketing agents, Banc of America Securities LLC (Series 2003A) and Wachovia Bank, N.A. (Series 2003B) have agreed to exercise their best efforts to remarket bonds for which a notice of purchase has been received. The quarterly remarketing fee is payable in arrears and is equal to 0.08% of the outstanding principal amount of the bonds assigned to the remarketing agent for Series 2003A and is equal to 0.07% of the outstanding principal amount of the bonds assigned to the remarketing agent for Series 2003B.

Under separate Standby Bond Purchase Agreements for the Series 2003A and Series 2003B (Agreements) between the Hospitals and Bank of America, N.A. (Series 2003A) or Wachovia Bank, N.A. (Series 2003B) a Liquidity Facility has been established for the Tender Agent to draw amounts sufficient to pay the purchase price on bonds delivered for purchase when remarketing proceeds or other funds are not available. These Agreements require a facility fee equal to 0.22% of the available commitment for Series 2003A and for Series 2003B, payable quarterly in advance, beginning on February 13, 2003, and on each February 1, May 1, August 1, and November 1 thereafter until the expiration date or the termination date of the Agreements.

Under the Agreements, any bonds purchased through the Liquidity Facility become Bank Bonds and shall, from the date of such purchase and while they are Bank Bonds, bear interest at the Bank Bond Interest Rate (for Series 2003A, the rate equals the London Interbank Offered Rate (LIBOR) plus 2.50% for the first 90 days and then equals LIBOR plus 4%; for Series 2003B, the rate equals Prime Rate for the first 90 days and then equals Prime plus 1%) subject to a maximum rate as permitted by law. Upon remarketing of Bank Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Bank Bonds. Payment of the interest on the Bank Bonds is on the first business day of each month for each period in which Bank Bonds are outstanding. At June 30, 2006, there were no Bank Bonds held by the Liquidity Facility.

Included in the Agreements is a take out provision, in case
the remarketing agent is unable to resell any bonds that are "put" within 90 days of the "put" date. In this situation, the Hospitals are required to redeem the Bank Bonds held by the Liquidity Facility. The Series 2003A agreement allows the Hospitals to redeem bank bonds in twelve equal quarterly installments beginning on the first February 1, May 1, August 1 or November 1 that occurs at least 90 days following the applicable purchase date of the Bank Bond. If the take out agreement was to be exercised because the entire outstanding $62.84 million of demand bonds was "put" and not resold, the Hospitals would be required to pay $24.26 million a year for 3 years under the installment loan agreement assuming a 9.35% interest rate (LIBOR plus 4%). The Series 2003B agreement allows the Hospitals to redeem bank bonds in 36 equal monthly installments, on the first business day of each calendar month after the loan date. Payments commence with the first business day of any such month that is at least 120 days following the applicable purchase date of the Bank Bond. If the take out agreement were to be exercised because the entire outstanding $33.76 million of demand bonds was "put" and not resold, the Hospitals would be required to pay $12.93 million a year for
three years under the installment loan agreement assuming a 9.25% interest rate (Prime plus 1%).

The current expiration date of the Series 2003A Agreement is July 1, 2008 and July 31, 2008 for the Series 2003B Agreement. The Hospitals may request additional extensions, which are approved at the discretion of the Liquidity Provider.

E. Interest Rate and Basis Swaps

Primary Government

Governmental Activities

Objective. As a means to lower its borrowing costs and increase its savings when compared to fixed-rate refunding bonds at the time of issuance in December 2002, the State entered into two interest rate swaps in connection with its $499.87 million Variable Rate General Obligation Refunding Bonds, Series 2002B-F. The intention of the swap agreements was to effectively change the State's interest rate on the bonds to a synthetic fixed rate of 3.28% (Swap 1) and 3.09% (Swap 2). For comparison, the State sold fixed rate bonds on the same day as the swaps, with the same final maturity, at an interest rate of 4.45%.

In June 2003, the State entered into a third interest rate swap agreement (Swap 3) to lower its borrowing costs and reduce its exposure to variable interest rates in connection with $355 million Variable Rate Public Improvement Bonds, Series 2002 D, E, F, and G. Effective July 1, 2003, the intention of this third swap agreement was to effectively change the interest rate on the bonds to a synthetic fixed rate of 1.06% (Swap 3) for a period of two years.

In March 2005, the State entered into basis rate swap agreements and related swapnotes with three separate counterparties to lower its borrowing costs when compared to fixed rate refunding bonds. The swap component is disclosed and valued in a separate section within this note (see section F). The bonds associated with basis swaps were as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Bonds Associated with Basis Swaps</th>
<th>Principal Amount</th>
<th>Average Coupon</th>
<th>Call Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Improvement, Series 2003A</td>
<td>$ 171,000</td>
<td>4.89%</td>
<td>3/1/2013</td>
</tr>
<tr>
<td>Public Improvement, Series 2003B</td>
<td>169,955</td>
<td>4.87%</td>
<td>4/1/2013</td>
</tr>
<tr>
<td>Public Improvement, Series 2004A</td>
<td>335,000</td>
<td>4.86%</td>
<td>3/1/2014</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$ 675,955</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Terms - Swaps 1 and 2. The bonds and the related swap agreements mature on June 1, 2019, (Swap 1) and June 1, 2017, (Swap 2) and the combined swaps' notional amount of $499.87 million matches the $499.87 million variable-rate bonds. The swaps were entered into at the same time the bonds were issued (December 2002). Starting in fiscal year 2012 the combined notional value of the swaps and the combined principal amount of the associated debt begin to decline. Under the swaps, the State pays the counterparties a fixed payment of 3.28% (Swap 1) and 3.09% (Swap 2) and receives a variable payment computed at 64% of the London Interbank Offered Rate (LIBOR). Conversely, the bonds' variable-rate coupons are closely associated with the Bond Market Association Municipal Swap Index (BMA).

Terms - Swap 3. This swap began July 1, 2003, with a notional amount of $355 million which matches the bonds outstanding, and ended on July 1, 2005. Under Swap 3, the State paid the counterparty a fixed payment of 1.06% and received a variable payment at the BMA.

Terms - 2005 Basis Swaps. The 2005 Basis swap agreements were entered into on March 9, 2005 with an effective date of March 30, 2005. The related bonds have serial maturities with Series 2003A having a final maturity on March 1, 2026, 2003B and 2004A have a final maturity on April 1, 2023, and March 1, 2023 respectively. The basis swap agreements mature on March 1, 2026. The swaps combined notional amount of $675.96 million matches the $675.96 million fixed rate bonds. Under the terms of the basis rate swap and swapnote agreement, the State will pay the BMA to the counterparties and will receive 70% of LIBOR plus a fixed spread of 69 basis points (41 attributable to basis swap and 28 basis points for the swapnote).

Fair value. Because interest rates have risen since execution of swaps 1 and 2, the swaps have positive fair values of $7.18 million (Swap 1) and $9.26 million (Swap 2) at June 30, 2006. The 2005 basis rate swaps had valuations at June 30, 2006 of: $14.06 million (Counterparty 1), $8.72 million (Counterparty 2), and $5.7 million (Counterparty 3). The market-to-market valuations were established by market quotations from the counterparties, representing estimates of the amounts that would be paid for replacement transactions.

Credit risk. The swaps' fair value represented the State's credit risk exposure to the counterparty as of June 30, 2006. The State's maximum possible loss is equivalent to the aggregate fair value of the swaps. The current counterparty ratings for each swap are presented in the table below:

<table>
<thead>
<tr>
<th>Swap Counterparty</th>
<th>Fitch Ratings</th>
</tr>
</thead>
<tbody>
<tr>
<td>Swap 1</td>
<td>AA</td>
</tr>
<tr>
<td>Swap 2</td>
<td>AA</td>
</tr>
<tr>
<td>Basis Swap Counterparty 1</td>
<td>AA</td>
</tr>
<tr>
<td>Basis Swap Counterparty 2</td>
<td>AA</td>
</tr>
<tr>
<td>Basis Swap Counterparty 3</td>
<td>AA</td>
</tr>
</tbody>
</table>

To mitigate the potential for credit risk, if the counterparty's credit quality falls to a specified rating, the counterparty will be required to collateralize a portion (up to 100%) of the fair value. For Swap 1, if the counterparty's credit quality fails to A1 as determined by Moody's Investors Service (Moody's) or A+ as determined by either Standard & Poor's (S&P) or Fitch Ratings (Fitch) and their exposure exceeds $5 million, then the swap will be collateralized by the counterparty with cash, U.S.
government or agency securities, or other collateral acceptable to the State. For Swap 2, if the credit quality falls to Aa1 (Moody’s) or AA+ (S&P) and their exposure exceeds $10 million, then the swap will be collateralized by the counterparty with cash, U.S. government or agency securities, or other collateral acceptable to the State. For the basis swaps, if the counterparty’s credit quality is rated lower than Baa1 (Moody’s), BBB+ (S&P), or BBB+ (Fitch) by two of the three rating agencies, then the swap will need to be collateralized by the counterparty with cash, U.S. government or agency securities, or other collateral acceptable to the State (Fitch credit ratings only apply to counterparty 1). If the counterparty is required to collateralize a portion of the derivative, then the collateral will be posted with a third party custodian or secured party.

An additional termination event occurs if the counterparty fails to maintain: for Swap 1, at least two ratings of at least Baa1 (Moody’s) or BBB+ (S&P and Fitch); for Swap 2, at least one rating of at least Baa3 (Moody’s) or BBB- (S&P). An additional termination event for the basis swaps occurs if counterparty 1 or 3 has one or more issues of rated, unsecured, unencumbered senior debt or long-term deposits outstanding and none of such issues has at least two ratings of at least Baa2 or higher as determined by Moody’s, BBB+ or higher as determined by S&P or BBB or higher as determined by Fitch. For counterparty 2, an additional termination event occurs if it has one or more issues of rated, unsecured, unencumbered senior debt outstanding and none of such issues has at least two ratings of Baa2 or higher (Moody’s), BBB or higher (S&P) or counterparty 2 fails to have a rating on long-term, unsecured, unencumbered senior debt.

**Basis risk and termination risk.** Swaps 1 and 2 expose the State to basis risk should the relationship between LIBOR and BMA converge, changing the synthetic rate on the bonds. The effect of this difference in basis is indicated by the difference between the intended synthetic rates of 3.28% (Swap 1) and 3.09% (Swap 2) and the synthetic rates as of June 30, 2006 of 3.79% (Swap 1) and 3.6% (Swap 2). As of June 30, 2006, the average rate on the State’s variable rate bonds was 3.93%, whereas 64% of LIBOR was 3.42%. The swaps may be terminated by the State with 15 days notice and the counterparties can only terminate the swaps if the State’s credit rating falls below Baa1 (Moody’s), or BBB+ (S&P or Fitch) for Swap 1, and on Swap 2, below Baa3 (Moody’s) or BBB- (S&P or Fitch), or an Event of Default occurs.

2005 Basis Swaps: These swaps expose the State to basis risk should the relationship between the two variable indexes BMA and LIBOR converge, which would affect the amount of interest savings realized. The State pays BMA and receives 70% of LIBOR plus 69 basis points (28 basis points relate to swaptions) on the notional amounts by counterparty. As of June 30, 2006, there was no basis risk as the State was paying BMA equal to 3.97% and receiving 4.43% (70% of LIBOR plus 69 basis points). LIBOR is 5.35% at June 30, 2006. The basis swaps and swaptions may be optionally terminated by the State with two days notice for counterparties 1 and 2 or with five days notice for counterparty 3. The counterparties can only terminate if the State, at any time during the term of the swap transaction, fails to maintain by at least two rating agencies, ratings of at least Baa2 or higher as determined by Moody’s, BBB or higher as determined by S&P or BBB or higher by Fitch (Fitch does not apply to counterparty 2).

**Market-access risk/Rollover-risk.** Swap 1 and Swap 2 are for the term of the Bonds and therefore there is no market-access risk or rollover risk. The 2005 basis rate swaps terminate at approximately the same time as the associated serial bonds mature (March 1, 2026; March 1, 2023; and April 1, 2023) and thus no rollover risk exists.

**Business-type Activities**

**Objective.** In order to protect against the potential of rising interest rates, the Town of Butner, State of North Carolina entered into an interest rate swap in connection with its $9.91 million Butner Water and Sewer System Revenue Bond Series 2001. The intention of the swap agreement was to effectively change the State’s interest rate on the bonds to a fixed rate of 4.21% (plus remarketing and liquidity fees and any difference between the variable rate received by the State (65% of LIBOR) and the rate paid by the State on the variable rate bonds).

**Terms.** The swap agreement with Bank of America, N.A. was effective April 1, 2001, based on a notional amount of $9.91 million to mature on September 1, 2025. The swap’s notional amount of $9.91 million matches the $9.91 million variable-rate bonds. Under the swap, the State pays a fixed payment of 4.21% to Bank of America, N.A. and receives a variable payment of 65% of the LIBOR (LIBOR was 5.33% at June 30, 2006). On the other hand, the bond’s variable-rate coupons (2.70% at June 30, 2006) are closely associated with the variable BMA, which was 3.97% as of June 30, 2006.

**Fair value.** Because interest rates have declined since execution of the swap, the swap has a fair value (the State would have to pay the counterparty if the State terminated the swap) of negative $385 thousand (Bank of America, N.A.) as of June 30, 2006. The swap’s negative fair value if terminated may be countered by a reduction in total interest payments required under a new swap creating a lower synthetic fixed rate. Because the coupons on the State’s variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value increase. The mark-to-market valuations were established by market quotations from the counterparty representing mid-market or average estimates/quotes of the amounts that would be paid for replacement transactions (having the effect of preserving the economic benefit to the party).

**Credit risk.** As of June 30, 2006, the State was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the State would be exposed to credit risk in the amount of the derivative’s fair value.
Basis risk and termination risk. The Swap exposes the State to basis risk (including effects of any reduction in marginal tax rates) should the relationship between LIBOR and BMA converge, changing the synthetic rate to the State on the bonds. The effect of this difference in basis is indicated by the difference between the intended synthetic rate of 4.21% and the actual synthetic rate as of June 30, 2006 of 4.71% (0.74% + 3.97%) reflecting a Bond Rate/LIBOR relationship of 17.64% compared to 65% of LIBOR the State is receiving (as of June 30). The swap may be terminated by either party if the other party fails to perform under the terms of the contract. If the swap is terminated, the associated variable-rate bonds would no longer carry synthetic interest rates. Also, if at the time of termination the swap has a negative fair value, the Town would be liable to the counterparty for that amount.

Component Units

University of North Carolina System

University of North Carolina at Chapel Hill

Swap 1

Objective. In order to protect against the risk of interest rate changes, effective October 3, 2000, the University entered into an interest rate swap agreement with Lehman Brothers Special Financing, Inc. (Lehman Brothers) related to $22 million of The University of North Carolina at Chapel Hill Variable Rate Housing System Revenue Bonds, Series 2000. This series of bonds was refunded in its entirety by the issuance of the University’s Variable Rate General Revenue Bonds, Series 2001B (2001B Bonds), and the interest rate swap agreement was amended to reflect the refunding.

Terms. Under this amended agreement, Lehman Brothers pays the University interest on the notional amount based on the BMA on a quarterly basis. On a semiannual basis, the University pays Lehman Brothers interest at the fixed rate of 5.24%. The notional amount of the swap reduces annually in conjunction with the 2001B Bonds; the reductions began in November 2002 and end in November 2025. The swap agreement matures November 1, 2025. As of June 30, 2006, rates were as follows:

<table>
<thead>
<tr>
<th>Term</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed payment to Lehman</td>
<td>5.24%</td>
</tr>
<tr>
<td>Variable payment from Lehman</td>
<td>3.61%</td>
</tr>
<tr>
<td>Net interest rate swap payments</td>
<td>1.63%</td>
</tr>
<tr>
<td>Variable rate bond coupon payments</td>
<td>3.95%</td>
</tr>
<tr>
<td>Synthetic interest rate on bonds</td>
<td>5.58%</td>
</tr>
</tbody>
</table>

Fair value. As of June 30, 2006, the swap had a fair value of negative $2.55 million. The fair value was developed by Lehman Brothers. Their method calculates the future net settlement payments required by the swap assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for LIBOR due on the date of each future net settlement on the swap.

Credit risk. As of June 30, 2006, the University was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the University would be exposed to credit risk in the amount of the derivative’s positive fair value. Should the swap have a positive fair value of more than $1 million at that point Lehman would be required to collateralize 103% of their exposure. Lehman Brothers Holdings, guarantor of Lehman Brothers Special Financing, Inc., was rated A1 by Moody’s, A+ by S&P, and A+ by Fitch for unsecured long-term debt at June 30, 2006.

Basis risk. The University receives the BMA from Lehman Brothers and pays a floating rate to its bondholders set by the remarketing agent. The University incurs basis risk when its bonds begin to trade at a yield above the BMA. Basis risk also exists since swap payments are made quarterly while bond payments are made monthly. With the alternative tax structure of the swap, a change in tax law would trigger the swap being converted from a BMA swap to a percentage of LIBOR swap. This would introduce basis risk. If the weekly reset interest rates on the University’s bonds are in excess of 65% of LIBOR, the University will experience an increase in debt service above the fixed rate on the swap to the extent that the interest rates on the bonds exceed 65% of LIBOR.

Termination risk. The swap agreement uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. Termination could result in the University being required to make an unanticipated termination payment. The swap terminates if the University or Lehman Brothers fails to perform under terms of the contract.

Swap 2

Future swap. The University entered into an interest rate swap agreement with the Bank of New York (BNY) for $150 million to be effective December 1, 2007. The University has the option to (1) issue variable rate bonds in December 2007, thereby effectively creating synthetic fixed-rate debt, or (2) unwind the swap, capturing the value of the movement of interest rates from the issuance date, and issuing traditional fixed rate bonds.

North Carolina State University

Objective. In order to protect against the potential of rising interest rates, the University entered into three separate pay-fixed, receive-variable interest rate swaps at a cost anticipated to be less than what the University would have paid to issue fixed-rate debt.
NOTES TO THE FINANCIAL STATEMENTS

Terms, fair values, and credit risk. The University’s swap agreements contain scheduled reductions to outstanding notional amounts that are expected to approximately follow scheduled or anticipated reductions in the associated bonds payable category. The terms, fair values, and credit ratings of the outstanding swaps as of June 30, 2006 were as follows (dollars in thousands).

<table>
<thead>
<tr>
<th>Associated Bond Issue</th>
<th>Notional Amounts</th>
<th>Effective Date</th>
<th>Fixed Rate Paid</th>
<th>Variable Rate Received</th>
<th>Fair Values</th>
<th>Swap Termination Date</th>
<th>Counterparty Credit Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Centennial</td>
<td>$8,600</td>
<td>10/1/1999</td>
<td>4.57%</td>
<td>67% of LIBOR</td>
<td>$(442)</td>
<td>12/01/2019</td>
<td>A1 / AA- / A+</td>
</tr>
<tr>
<td>Campus 1999A General Revenue</td>
<td>$24,655</td>
<td>6/20/2003</td>
<td>3.54%</td>
<td>BMA¹</td>
<td>2,045</td>
<td>10/01/2027</td>
<td>Aa1 / AA /AA-</td>
</tr>
<tr>
<td>Total</td>
<td>$33,255</td>
<td></td>
<td></td>
<td></td>
<td>$1,603</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

¹ Variable rate received is the BMA from June 20, 2003 to July 1, 2006; thereafter, the variable rate received will be 75% of LIBOR.

Because rates have changed since the effective dates of the swaps, the 1999A swap has a negative fair value as of June 30, 2006. The negative fair value may be countered by a reduction in total interest payments required under the variable-rate bonds, creating lower synthetic interest rates. Because the coupons on the University’s variable-rate bonds adjust to changing interest rates, the bonds do not have corresponding fair value increases. The fair values are the market values as of June 30, 2006.

As of June 30, 2006, the University was exposed to credit risk on the swap with a positive fair value. The State’s maximum possible loss is equivalent to the positive fair value of the swap. The swap agreements require termination should the University’s or the counterparty’s credit rating fall below either Baa2 as issued by Moody’s or BBB as issued by S&P or Fitch. Also, under the terms of the swap agreements, should one party become insolvent or otherwise default on its obligations, provisions permit the nondefaulting party to accelerate and terminate all outstanding transactions. To mitigate the potential for credit risk, if the counterparty’s credit quality falls below A3 as determined by Moody’s or A- as determined by S&P, the swap will be collateralized by the counterparty with cash, U.S. government or agency securities. If the counterparty is required to collateralize, then the collateral will be posted with a third party custodian or secured party. The swap agreements entered into by the University are held with separate counterparties. All the counterparties are rated A1 or better.

Future swap. The University has also entered into an interest rate swap agreement for $50 million to be effective September 1, 2008, on a General Revenue Bond Issue planned for 2008.

North Carolina Central University

In October of 2003, the North Carolina Capital Facilities Finance Agency issued Student Housing Facilities Revenue Bonds ($21.48 million Variable Rate Revenue Demand Bonds, Series 2003A). The issuer, the North Carolina Capital Facilities Finance Agency, loaned the proceeds of the Series 2003 Bonds to the NCCU Real Estate Foundation, Inc. (Foundation). The Foundation used the proceeds to finance the costs of building a student housing facility at North Carolina Central University, to fund a debt service reserve fund for the 2003A Bonds, to pay a portion of the interest on the bonds during construction of the project, and to pay certain costs of issuance of the bonds.

Objective. As a means to lower its borrowing costs and increase its savings, when compared against fixed-rate refunding bonds at the time of issuance in October 2003, effective March 24, 2004, the Foundation entered into two interest rate swaps with Wachovia Bank, N.A., in connection with its $21.48 million Variable Rate Revenue Demand Bonds, Series 2003A. The intention of the swap agreements was to effectively change the interest rate on the bonds to a synthetic fixed rate of 3.52% (Swap 1) and 2.71% (Swap 2).

Terms. The bonds and the related swap agreements mature on October 1, 2024, (Swap 1) and April 1, 2009, (Swap 2) and the combined swaps’ notional amount of $17.18 million hedges 80% of the $21.48 million variable-rate bonds. The combined notional value of the swaps and the combined principal amount of the associated debt is declining. Under the swaps, the Foundation pays Wachovia Bank, N.A. a fixed rate of 3.52% (Swap 1) and 2.71% (Swap 2) and receives a variable rate at 70% and 100% of LIBOR and BMA, respectively. The bonds’ variable-rate coupons are closely associated with the BMA.

Fair value. Because interest rates have risen since execution of the swaps, the swaps have positive fair values of $361 thousand (Swap 1) and $244 thousand (Swap 2) as of June 30, 2006. The swaps’ positive fair value may be countered by an increase in total interest payments required under the
variable rate bonds, creating a higher synthetic interest rate. Because the coupons on the Foundation's variable-rate bond are adjusted every seven days to changing interest rates, the bonds do not have a corresponding fair value increase. The mark-to-market valuations were established by market quotations from Wachovia Bank, N.A. representing estimates of the amounts that would be paid upon terminating the transactions.

**Credit risk.** As of June 30, 2006, the Foundation was exposed to credit risk because the swaps had a positive fair value. The exposed credit risk is in the amount of the derivatives' aggregate fair value. Swap 1 and Swap 2's counterparty (Wachovia Bank, N.A.) was rated Aa2 by Moody's, AA- by S&P and AA- by Fitch at June 30, 2006.

**Basis risk and termination risk.** Swap 1 exposes the Foundation to basis risk should the relationship between LIBOR and BMA converge, changing the synthetic rate on the bonds. The effect of this difference in basis is indicated by the difference between the intended synthetic rate of 3.52% and the actual rate of 3.76% (Swap 1) at June 30, 2006. As of June 30, 2006, the rate on the Foundation's Bonds was 3.98%, whereas 70% of LIBOR was 3.73%. Swap 2 exposes the Foundation to basis risk should the actual rate on the Foundation's Bond vary from the BMA. The effect of this difference in basis is indicated by the difference between the intended synthetic rate of 2.71% and the actual rate of 2.72% (Swap 2) at June 30, 2006. As of June 30, 2006, the rate on the Foundation's Bonds was 3.98%, whereas the BMA index was 3.97%. Termination could result in the Foundation being required to make an unanticipated termination payment. The swap agreements are terminated if the Foundation or Wachovia Bank, N.A. fails to perform under the terms of the contract.

**Market-access risk/Rollover-risk.** Swap 1 and Swap 2 expose the Foundation to market-access and rollover risk when the swaps mature on October 1, 2024 and April 1, 2009 respectively. When Swap 1 and Swap 2 mature, the interest rate on the underlying debt will return to a variable rate.

**University of North Carolina Hospitals**

**Objective.** In order to protect against the risk of interest rate changes, the Hospitals entered into an interest rate swap contract agreement with Bank of America, N.A. (BOA) on February 13, 2003. The agreement covers the Variable Rate Revenue Refunding Bonds, Series 2003A for $63.77 million and Series 2003B for $34.25 million. The 2003 series of bonds partially refunded Fixed Rate Revenue Bonds, Series 1996.

**Terms, fair values, and credit risk.** Under this agreement, BOA pays the Hospitals interest on the notional amount based on 67% of the arithmetic mean of the USD-LIBOR-BBA (with a designated maturity of one month) on a monthly basis. Also on a monthly basis, the Hospitals pay BOA interest at the fixed rate of 3.48%. No cash was paid or received by the Hospitals upon initiation of the agreement. The notional amount of the swap reduces annually; the reductions began in February 2004 and end in February 2029.

The swap agreement terminates February 1, 2029. As of June 30, 2006, rates were as follows:

<table>
<thead>
<tr>
<th>Terms</th>
<th>Rates</th>
<th>Rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed payment to BOA</td>
<td>3.48%</td>
<td>3.48%</td>
</tr>
<tr>
<td>Variable payment from BOA</td>
<td>3.49%</td>
<td>3.49%</td>
</tr>
<tr>
<td>Net interest rate swap payments</td>
<td>-0.01%</td>
<td>-0.01%</td>
</tr>
<tr>
<td>Variable rate bond payments</td>
<td>4.00%</td>
<td>3.99%</td>
</tr>
<tr>
<td>Synthetic interest rate on bonds</td>
<td>3.98%</td>
<td>3.94%</td>
</tr>
</tbody>
</table>

The swap agreement has a mark-to-market value of $3.01 million as of June 30, 2006. BOA develops the mark-to-market value. Their method calculates the present value of the future net settlement payments required by the swap assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for LIBOR due on the date of each future net settlement on the swap.

As of June 30, 2006, the Hospitals are exposed to credit risk equal to the market value of the swap. BOA’s current long-term ratings are AA- by Fitch, Aa1 by Moody’s, and AA by S&P. At such time that their ratings fall below A3 for Moody’s or below A- for S&P, BOA will be required to collateralize a portion of their exposure (up to 100%). The following instruments can serve as eligible collateral: cash, U.S. Treasury obligations, U.S. government agency fixed rate fixed maturity securities, U.S. government agency single class mortgage-backed securities, U.S. Treasury STRIPS and other U.S. government agency mortgage-backed securities. Posted collateral received will be entered in one or more accounts with a domestic office of a commercial bank, trust company or financial institution organized under the laws of the United States (or any state or a political subdivision thereof).

**Basis risk.** The Hospitals receive 67% of 1-month LIBOR-BBA Index from BOA and pays a floating rate to its bondholders set by the remarketing agent. The Hospitals incurred basis risk at June 30, 2006, because its bonds traded at a yield above 67% of 1-month LIBOR-BBA Index. If the relationship of the Hospitals’ bonds trade to a percentage of LIBOR greater than 67%, the Hospitals will experience an increase in debt service above the fixed rate on the swap.

**Termination risk.** The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Hospitals or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. If the swap is terminated, the associated variable-rate bonds would no longer carry synthetic interest rates. Also, if at the time of termination the swap has a negative fair value, the Hospitals would be liable to the counterparty for that amount. Termination could result in the Hospitals being required to make an unanticipated termination payment.
North Carolina Housing Finance Agency

**Objective.** The Agency has entered into interest rate swaps in connection with its $78.7 million variable-rate revenue bonds associated with several series in its 1998 Home Ownership Revenue Bond Resolution as a means to lower its borrowing costs when compared against fixed-rate bonds at the time of issuance. The intention of the swap was to effectively lower the Agency’s interest rate on the long term bonds to a fixed rate.

**Terms and fair value.** The terms and fair value of the outstanding swaps as of June 30, 2006 were as follows (dollars in thousands).

<table>
<thead>
<tr>
<th>Series</th>
<th>Counterparty</th>
<th>Credit Rating</th>
<th>Notional Amount</th>
<th>Date of Swap</th>
<th>Maturity Date of Swap</th>
<th>Fixed Rate</th>
<th>Fair Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>15</td>
<td>UBS AG</td>
<td>Aa2/AA+</td>
<td>$19,205</td>
<td>5/8/2003</td>
<td>7/1/2032</td>
<td>3.51%</td>
<td>$685</td>
</tr>
<tr>
<td>16</td>
<td>Bank of America, N.A.</td>
<td>Aa2/AA-</td>
<td>19,485</td>
<td>9/16/2003</td>
<td>7/1/2032</td>
<td>3.81%</td>
<td>266</td>
</tr>
<tr>
<td>17</td>
<td>Bank of America, N.A.</td>
<td>Aa2/AA-</td>
<td>20,000</td>
<td>12/11/2003</td>
<td>7/1/2032</td>
<td>3.73%</td>
<td>253</td>
</tr>
<tr>
<td>18</td>
<td>Goldman Sachs Mitsui Marine</td>
<td>Aa3/AA+</td>
<td>20,000</td>
<td>4/20/2004</td>
<td>1/1/2035</td>
<td>3.29%</td>
<td>1,141</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td></td>
<td>$78,890</td>
<td></td>
<td></td>
<td></td>
<td><strong>$2,345</strong></td>
</tr>
</tbody>
</table>

Under all of the swaps, the Agency pays the counterparties a fixed rate and receives a variable payment computed as 63% of LIBOR, plus 30 basis points. The bonds’ variable-rate coupons are based on the BMA, which was 4.05% as of June 30, 2006.

In total, the swaps have a positive fair value of $2.345 million as of June 30, 2006. Because the coupons on the Agency’s variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value increase. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

**Credit risk.** All of the Agency’s swaps rely upon the performance of the third parties who serve as swap counterparties, and as a result the Agency is exposed to credit risk – i.e., the risk that a swap counterparty fails to perform according to its contractual obligations. The appropriate measurement of this risk at the reporting date is the fair value of the swaps, as shown in the column labeled “Fair Values” in the table above. The Agency is exposed to credit risk in the amount of any positive net fair value exposure to each counterparty. As of June 30, 2006, the Agency was exposed to a total of $2.345 million of credit risk to 3 counterparties. To mitigate credit risk, the Agency maintains strict credit standards for swap counterparties. Additionally, credit events can trigger certain termination provisions or collateral provisions as outlined in the swap documents.

**Basis risk and termination risk.** The swaps expose the Agency to basis risk should the relationship between LIBOR and BMA converge, changing the synthetic rate on the bonds. Series 15 swap may be terminated if the counterparty’s credit rating falls below A3 as issued by Moody’s or A- as issued by Fitch or S&P. For Series 16, 17 and 18, collateral thresholds have been established if the counterparty’s ratings reach A2 for Moody’s or A for S&P. Series 16, 17 and 18 swaps may be terminated if the counterparty’s rating falls below Baa as issued by Moody’s or BBB as issued by S&P.
F. Swaptions

Objective. As a means of lowering its borrowing costs on the existing bonds in the table below and increasing its savings when compared to fixed rate refunding bonds, the State entered into basis swap and swaption contracts with three different financial institutions. Swaptions give the purchaser the right, but not the obligation, to enter into an interest rate swap on a specified future date. These swaptions and the related basis rate swap disclosed previously were entered into as an alternative to a synthetic fixed rate refunding. This swaption alternative provides an annuity to the State (69 basis points total – 28 for the swaptions). The swaptions give each counterparty the option to require the State to enter into pay-fixed, receive-variable interest rate swaps at the various call dates. If the swaptions are exercised, the State would then expect to issue variable-rate refunding bonds sufficient to retire the related issue.

<table>
<thead>
<tr>
<th>Bond Series</th>
<th>Counterparty 1</th>
<th>Counterparty 2</th>
<th>Counterparty 3</th>
<th>Series Total</th>
<th>Call Date / Swaption Exercise Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Improvement Bonds, Series 2003A</td>
<td>$85,500</td>
<td>$51,300</td>
<td>$34,200</td>
<td>$171,000</td>
<td>3/1/2013</td>
</tr>
<tr>
<td>Public Improvement Bonds, Series 2003B</td>
<td>84,977</td>
<td>50,987</td>
<td>33,991</td>
<td>169,955</td>
<td>4/1/2013</td>
</tr>
<tr>
<td>Public Improvement Bonds, Series 2004A</td>
<td>167,500</td>
<td>100,500</td>
<td>67,000</td>
<td>335,000</td>
<td>3/1/2014</td>
</tr>
<tr>
<td>Total</td>
<td>$337,977</td>
<td>$202,787</td>
<td>$135,191</td>
<td>$675,955</td>
<td></td>
</tr>
</tbody>
</table>

Terms. The swaption agreements were entered into on March 9, 2005 and mature March 1, 2026. The swaption annuity was based on the total notional amount of $675,955 million and is tied to the respective bond issues noted above. The counterparties have the right to exercise the swaption agreements 90 days prior to the call date for each series. If exercised, the State will pay the counterparties a fixed rate, and the counterparties will pay the State a variable rate (BMA) based on a declining notional amount that matches the amortization of the associated bonds by series. If the swaptions are exercised, the State intends to issue variable rate bonds in a principal amount to retire the associated bond series. The terms of the swaptions are listed below, which include counterparty credit ratings as of June 30, 2006.

<table>
<thead>
<tr>
<th>Counterparty</th>
<th>Swaption Annuity Payment Received</th>
<th>Fixed Rate Paid by the State</th>
<th>Variable Rate Received by the State</th>
</tr>
</thead>
<tbody>
<tr>
<td>Counterparty 1</td>
<td>28 Basis Points</td>
<td>4.8%</td>
<td>BMA</td>
</tr>
<tr>
<td>Counterparty 2</td>
<td>28 Basis Points</td>
<td>4.8%</td>
<td>BMA</td>
</tr>
<tr>
<td>Counterparty 3</td>
<td>28 Basis Points</td>
<td>4.8%</td>
<td>BMA</td>
</tr>
</tbody>
</table>

Fair value. As of June 30, 2006, the swaptions had fair values of negative $10.03 million (Counterparty 1), negative $5.62 million (Counterparty 2) and negative $3.66 million (Counterparty 3), which were estimated using the mark to market method. This method of valuation was established by market quotations from the counterparties representing estimates of the amounts that would be paid for replacement transactions. These values reflect a slight decline in interest rates between March 9, 2005, and June 30, 2006, however, only the State has the option to terminate the swaptions. A replacement transaction would generat any net present value savings equal to these fair value amounts.

Market-access risk. A small risk exists that the State, for some unforeseen reason, may be unable to issue the variable rate bonds. If the swaptions are exercised and refunding bonds are not issued, the series 2003 A and B and 2004A bonds would not be refunded, the basis rate swaps would continue, and the State would have to pay a termination payment on the swaptions to the counterparties. Termination values will be based on the net present value difference between BMA and 4.8% fixed rate.
G. Debt Service Requirements

The following schedules show the debt service requirements for the primary government (governmental activities and business-type activities) and component units (University of North Carolina System, North Carolina Housing Finance Agency, and the State Education Assistance Authority). The debt service requirements of variable rate debt and net swap payments are based on rates as of June 30, 2006 and assume that current interest rates remain the same for their term. As rates vary, variable-rate bond interest payments and net swap payments will vary.

Annual debt service requirements to maturity for general obligation bonds, certificates of participation, revenue bonds, and notes payable are as follows (dollars in thousands).

**Primary Government**

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>General Obligation Bonds</th>
<th>Certificates of Participation</th>
<th>Lease-Purchase Revenue Bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Principal</td>
<td>Interest</td>
<td>Interest Rate</td>
</tr>
<tr>
<td>Ending June 30</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>$343,615</td>
<td>$268,712</td>
<td>$(1,215)</td>
</tr>
<tr>
<td>2008</td>
<td>$342,715</td>
<td>$253,461</td>
<td>$(1,215)</td>
</tr>
<tr>
<td>2009</td>
<td>$339,320</td>
<td>$237,177</td>
<td>$(1,215)</td>
</tr>
<tr>
<td>2010</td>
<td>$339,200</td>
<td>$220,893</td>
<td>$(1,215)</td>
</tr>
<tr>
<td>2011</td>
<td>$339,360</td>
<td>$204,143</td>
<td>$(1,215)</td>
</tr>
<tr>
<td>2012-2016</td>
<td>$1,708,810</td>
<td>$770,067</td>
<td>$(4,693)</td>
</tr>
<tr>
<td>2017-2021</td>
<td>$1,566,240</td>
<td>$372,748</td>
<td>$(824)</td>
</tr>
<tr>
<td>2022-2026</td>
<td>$726,755</td>
<td>$83,050</td>
<td>—</td>
</tr>
<tr>
<td>2027-2031</td>
<td>$33,000</td>
<td>$1,485</td>
<td>—</td>
</tr>
<tr>
<td>Total</td>
<td>$5,738,815</td>
<td>$2,411,736</td>
<td>$(11,592)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Notes Payable</th>
<th>Revenue Bonds</th>
<th>Business-type Activities</th>
<th>Notes Payable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ending June 30</td>
<td>Principal</td>
<td>Interest</td>
<td>Principal</td>
<td>Interest</td>
</tr>
<tr>
<td>2007</td>
<td>$26,334</td>
<td>$4,527</td>
<td>$280</td>
<td>$290</td>
</tr>
<tr>
<td>2008</td>
<td>$10,060</td>
<td>$1,277</td>
<td>$295</td>
<td>$280</td>
</tr>
<tr>
<td>2009</td>
<td>$4,281</td>
<td>$801</td>
<td>$305</td>
<td>$270</td>
</tr>
<tr>
<td>2010</td>
<td>$2,594</td>
<td>$672</td>
<td>$320</td>
<td>$259</td>
</tr>
<tr>
<td>2011</td>
<td>$1,779</td>
<td>$590</td>
<td>$335</td>
<td>$248</td>
</tr>
<tr>
<td>2012-2016</td>
<td>$15,793</td>
<td>$1,924</td>
<td>$1,910</td>
<td>$1,055</td>
</tr>
<tr>
<td>2017-2021</td>
<td>—</td>
<td>—</td>
<td>$2,380</td>
<td>$691</td>
</tr>
<tr>
<td>2022-2026</td>
<td>—</td>
<td>—</td>
<td>$2,975</td>
<td>$235</td>
</tr>
<tr>
<td>Total</td>
<td>$60,841</td>
<td>$9,791</td>
<td>$8,800</td>
<td>$3,328</td>
</tr>
</tbody>
</table>

The general obligation bonds include $355 million of variable rate debt without interest rate swaps. For this debt, the variable interest rates change on a weekly basis and are based on the rate paid by each bank. The banks base their rate on what they perceive to be the market (7-day) for debt of this type given the credit standing of the unit of government. The general obligation bonds also include $499.87 million of variable rate debt with interest rate swaps (see Note 7E).
## Component Units

### University of North Carolina System

<table>
<thead>
<tr>
<th>Fiscal Year Ending June 30</th>
<th>Revenue Bonds</th>
<th>Interest Rate</th>
<th>Certificates of Participation</th>
<th>Notes Payable</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Principal</td>
<td>Interest</td>
<td>Swaps, Net</td>
<td>Principal</td>
</tr>
<tr>
<td>2007</td>
<td>$72,764</td>
<td>$91,829</td>
<td>$183</td>
<td>$1,755</td>
</tr>
<tr>
<td>2008</td>
<td>73,980</td>
<td>88,209</td>
<td>177</td>
<td>1,810</td>
</tr>
<tr>
<td>2009</td>
<td>76,660</td>
<td>84,728</td>
<td>195</td>
<td>1,870</td>
</tr>
<tr>
<td>2010</td>
<td>76,335</td>
<td>81,063</td>
<td>263</td>
<td>1,930</td>
</tr>
<tr>
<td>2011</td>
<td>77,810</td>
<td>77,800</td>
<td>254</td>
<td>2,000</td>
</tr>
<tr>
<td>2012-2016</td>
<td>405,350</td>
<td>336,556</td>
<td>1,042</td>
<td>7,350</td>
</tr>
<tr>
<td>2017-2021</td>
<td>373,509</td>
<td>247,834</td>
<td>480</td>
<td>2,435</td>
</tr>
<tr>
<td>2022-2026</td>
<td>319,610</td>
<td>167,614</td>
<td>(65)</td>
<td>3,035</td>
</tr>
<tr>
<td>2027-2031</td>
<td>164,985</td>
<td>111,504</td>
<td>(27)</td>
<td>3,820</td>
</tr>
<tr>
<td>2032-2036</td>
<td>378,380</td>
<td>46,053</td>
<td>—</td>
<td>3,785</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$2,019,383</strong></td>
<td><strong>$1,333,190</strong></td>
<td><strong>$2,502</strong></td>
<td><strong>$29,790</strong></td>
</tr>
</tbody>
</table>

### North Carolina Housing Finance Agency

<table>
<thead>
<tr>
<th>Fiscal Year Ending June 30</th>
<th>Revenue Bonds</th>
<th>Interest Rate</th>
<th>Swaps, Net</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>$178,050</td>
<td>$73,845</td>
<td>(61)</td>
</tr>
<tr>
<td>2008</td>
<td>74,735</td>
<td>66,879</td>
<td>(62)</td>
</tr>
<tr>
<td>2009</td>
<td>36,995</td>
<td>64,668</td>
<td>(61)</td>
</tr>
<tr>
<td>2010</td>
<td>38,755</td>
<td>63,101</td>
<td>(61)</td>
</tr>
<tr>
<td>2011</td>
<td>39,808</td>
<td>61,376</td>
<td>(55)</td>
</tr>
<tr>
<td>2012-2016</td>
<td>225,885</td>
<td>275,739</td>
<td>(212)</td>
</tr>
<tr>
<td>2017-2021</td>
<td>207,550</td>
<td>217,645</td>
<td>(132)</td>
</tr>
<tr>
<td>2022-2026</td>
<td>252,290</td>
<td>167,393</td>
<td>(81)</td>
</tr>
<tr>
<td>2027-2031</td>
<td>328,120</td>
<td>88,274</td>
<td>(32)</td>
</tr>
<tr>
<td>2032-2036</td>
<td>168,880</td>
<td>21,972</td>
<td>—</td>
</tr>
<tr>
<td>2037-2041</td>
<td>13,820</td>
<td>1,162</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$1,564,880</strong></td>
<td><strong>$1,102,054</strong></td>
<td><strong>(757)</strong></td>
</tr>
</tbody>
</table>

### State Education Assistance Authority

<table>
<thead>
<tr>
<th>Fiscal Year Ending June 30</th>
<th>Revenue Bonds</th>
<th>Interest Rate</th>
<th>Swaps, Net</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Principal</td>
<td>Interest</td>
<td>Swaps, Net</td>
</tr>
<tr>
<td>2007</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>2008</td>
<td>—</td>
<td>117,324</td>
<td>—</td>
</tr>
<tr>
<td>2009</td>
<td>—</td>
<td>117,324</td>
<td>—</td>
</tr>
<tr>
<td>2010</td>
<td>—</td>
<td>117,324</td>
<td>—</td>
</tr>
<tr>
<td>2011</td>
<td>—</td>
<td>117,324</td>
<td>—</td>
</tr>
<tr>
<td>2012-2016</td>
<td>—</td>
<td>540,704</td>
<td>546,804</td>
</tr>
<tr>
<td>2017-2021</td>
<td>—</td>
<td>325,000</td>
<td>415,722</td>
</tr>
<tr>
<td>2022-2026</td>
<td>—</td>
<td>—</td>
<td>352,965</td>
</tr>
<tr>
<td>2027-2031</td>
<td>—</td>
<td>270,000</td>
<td>310,197</td>
</tr>
<tr>
<td>2032-2036</td>
<td>—</td>
<td>1,422,950</td>
<td>157,733</td>
</tr>
<tr>
<td>2037-2041</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$2,558,654</strong></td>
<td><strong>$2,370,041</strong></td>
<td>—</td>
</tr>
</tbody>
</table>

For revenue bonds of the University of North Carolina System and the State Education Assistance Authority, the fiscal year 2007 principal requirements exclude demand bonds classified as current liabilities (see Note 7D).
NOTES TO THE FINANCIAL STATEMENTS

H. Bond Defeasances

The State and its component units have defeased certain bonds through current and/or advance refundings. New debt proceeds from current refundings may be used to repay the old debt immediately while new debt proceeds from advance refundings are placed into an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. Since these bonds are considered to be defeased, the liabilities for these bonds have been removed from the government-wide statement of net assets.

Component Units

University of North Carolina System

University of North Carolina at Chapel Hill

On August 30, 2005, the University issued $404.96 million in General Revenue and Revenue Refunding Bonds, Series 2005A, with an average interest rate of 4.9%. The refunding component of this bond was used to advance refund $6.25 million of outstanding Housing System Revenue Bonds, Series 1997A, with an average interest rate of 4.98%; $9.9 million of Parking System Revenue Bonds, Series 1997A, with an average interest rate of 5.6%; $8.75 million of Student Fee Revenue Bonds, Series 2000, with an average interest rate of 5.36%; and $33.31 million of General Revenue Bonds, Series 2001A, with an average interest rate of 5.23%. This advance refunding was undertaken to reduce total debt service payments by $4.16 million over the next 23 years and resulted in an economic gain of $3.42 million. At June 30, 2006, the outstanding balance was $5.85 million for the defeased Housing System Revenue Bonds, Series 1997A; $9.9 million for the defeased Parking System Revenue Bonds, Series 1997A; $8.75 million for the defeased Student Fee Revenue Bonds, Series 2000; and $33.31 million for the defeased General Revenue Bonds, Series 2001A.

State Education Assistance Authority

On October 27, 2005, the Authority issued $506.3 million in Series 2005A Student Loan Revenue Bonds with an average interest rate of 4.03%. The refunding component of this issue was used for a current refunding of $12.35 million of outstanding Series 1995A Student Loan Revenue Bonds with an average interest rate of 6.19%. The refunding was undertaken to reduce total debt service payments by $2.03 million over the next 9 years and resulted in an economic gain of $1.61 million.

Prior Year Defeasances

During prior years, the State and certain component units defeased certain general obligation and other bonds. For those defeasances involving advance refundings, the proceeds and any securities purchased with the proceeds were placed in an irrevocable trust with an escrow agent in an amount sufficient 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 government-wide statement of net assets. At June 30, 2006, the outstanding balance of prior year defeased bonds was $1.3 billion for the primary government and $79.1 million for component units.

I. Bond Redemptions

The bond series resolutions for the North Carolina Housing Finance Agency provide for various methods of redemption. Bonds are redeemed at par from prepayments of mortgage loans securing the issues, from unexpended bond proceeds of the issues, or from funds released via the related decreases in the respective debt service reserve requirements. In addition, various bond issues are redeemable at the option of the Agency with premiums ranging up to 2% for up to 12 years after the date of issue.
NOTE 8: LEASE OBLIGATIONS—OPERATING AND CAPITAL

The State and its component units have entered into various operating and capital leases for office space and for communications, computer, and other equipment. Any operating leases with scheduled rent increases are considered immaterial to the future minimum lease payments and current rental expenditures. Operating lease payments are recorded as expenditures or expenses of the related funds when incurred. For the year ended June 30, 2006, total operating lease expenditures were $65.79 million for Primary Government, $32.17 million for the University of North Carolina System, and $5.09 million for Community Colleges. Future minimum lease commitments for noncancelable operating leases and capital leases as of June 30, 2006 are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Primary Government</th>
<th>University of North Carolina System</th>
<th>Community Colleges</th>
<th>Total Future Minimum Lease Payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>$49,517</td>
<td>$19,531</td>
<td>$3,997</td>
<td>$206,280</td>
</tr>
<tr>
<td>2008</td>
<td>36,840</td>
<td>12,254</td>
<td>3,081</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>22,473</td>
<td>7,666</td>
<td>2,049</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>13,727</td>
<td>5,352</td>
<td>1,678</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>9,142</td>
<td>3,785</td>
<td>986</td>
<td></td>
</tr>
<tr>
<td>2012 - 2016</td>
<td>16,380</td>
<td>6,746</td>
<td>1,119</td>
<td></td>
</tr>
<tr>
<td>2017 - 2021</td>
<td>8,293</td>
<td>48</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2022 - 2026</td>
<td>8,082</td>
<td>26</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2027 - 2031</td>
<td>8,082</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2032 - 2036</td>
<td>8,082</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2037 - 2041</td>
<td>8,082</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2042 - 2046</td>
<td>8,082</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2047 - 2051</td>
<td>8,082</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2052 - 2056</td>
<td>1,816</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Future Minimum Lease Payments</td>
<td>$206,280</td>
<td>$55,552</td>
<td>$12,910</td>
<td></td>
</tr>
<tr>
<td>Less: Amounts Representing Interest</td>
<td>10</td>
<td>66,475</td>
<td>4,770</td>
<td></td>
</tr>
<tr>
<td>Present Value of Future Minimum Lease Payments</td>
<td>$26,879</td>
<td>$103,425</td>
<td>$9,887</td>
<td></td>
</tr>
</tbody>
</table>

At June 30, 2006, capital assets acquired under capital leases are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Primary Government</th>
<th>Component Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>University of North Carolina System</td>
<td>Community Colleges</td>
</tr>
<tr>
<td>Governmental Activities</td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>$26,745</td>
</tr>
<tr>
<td>Machinery and Equipment</td>
<td>298</td>
</tr>
<tr>
<td>Other</td>
<td>—</td>
</tr>
<tr>
<td>Less: Accumulated Depreciation</td>
<td>—</td>
</tr>
<tr>
<td>Total Capital Assets</td>
<td>$27,043</td>
</tr>
</tbody>
</table>
A. Interfund Balances

Due To/From Fiduciary Funds

The General Fund balance of $42.541 million due to fiduciary funds is composed of $12.824 million related to local sale; taxes collected in the general fund and due to the agency fund, as well as $29.717 million related to retirement contributions payable to retirement systems at year end. The other balances due to fiduciary funds are related to balances held on behalf of patients at the State’s mental health facilities.

The other balances due from fiduciary funds are primarily for services provided to pension and other employee benefit trust funds. Amounts payable to or receivable from fiduciary funds are considered interfund balances in the fund financial statements, but are not reported as internal balances in the government-wide statement of net assets.

Due To/From Other Funds

Balances due to/from other funds at June 30, 2006, consisted of the following (dollars in thousands):

<table>
<thead>
<tr>
<th>Due To Other Funds</th>
<th>General Fund</th>
<th>Highway Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>Unemployment Compensation Fund</th>
<th>Internal Service Funds</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Fund</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$ 2,970</td>
<td>$ —</td>
<td>$ 11,210</td>
<td>$ 14,180</td>
</tr>
<tr>
<td>Highway Fund</td>
<td>—</td>
<td>—</td>
<td>105</td>
<td>6,436</td>
<td>—</td>
<td>2,003</td>
<td>8,544</td>
</tr>
<tr>
<td>Highway Trust Fund</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>75,495</td>
<td>—</td>
</tr>
<tr>
<td>Other Governmental Funds</td>
<td>5,687</td>
<td>—</td>
<td>—</td>
<td>34,962</td>
<td>59</td>
<td>1,145</td>
<td>41,853</td>
</tr>
<tr>
<td>EPA Revolving Loan Fund</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>8</td>
<td>8</td>
</tr>
<tr>
<td>NC State Lottery Fund</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>13,548</td>
<td>—</td>
<td>78</td>
<td>13,626</td>
</tr>
<tr>
<td>Nonmajor Enterprise Funds</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>10</td>
<td>—</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Internal Service Funds</td>
<td>3</td>
<td>—</td>
<td>—</td>
<td>1</td>
<td>—</td>
<td>1,220</td>
<td>1,224</td>
</tr>
<tr>
<td>Total</td>
<td>$ 5,690</td>
<td>$ 75,495</td>
<td>$ 105</td>
<td>$ 57,927</td>
<td>$ 59</td>
<td>$ 15,699</td>
<td>$ 154,975</td>
</tr>
</tbody>
</table>

These balances resulted primarily from the time lag between the dates that (1) interfund goods and services are provided or reimbursable expenditures occur; (2) transactions are recorded in the accounting system, and (3) payments between funds are made. Amounts reported in the funds as interfund receivables and payables were eliminated in the governmental and business-type activities columns of the government-wide statement of net assets, except for the net residual amounts due between governmental and business-type activities, which were presented as internal balances.
B. Interfund Transfers

Transfers in/out of other funds for the fiscal year ended June 30, 2006 consisted of the following (dollars in thousands):

<table>
<thead>
<tr>
<th>Transfers Out</th>
<th>General Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>EPA Revolving Loan Fund</th>
<th>Other Enterprise Funds</th>
<th>Internal Service Funds</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Fund</td>
<td>$625,322</td>
<td>$85,908</td>
<td>$1,321</td>
<td>$1,071,463</td>
<td>$8,686</td>
<td>$2,155</td>
<td>$1,797,964</td>
</tr>
<tr>
<td>Highway Fund</td>
<td>$1,186,966</td>
<td>$594,316</td>
<td>$5,306</td>
<td>$2,068</td>
<td>$336</td>
<td>$620,313</td>
<td></td>
</tr>
<tr>
<td>Highway Trust Fund</td>
<td>253,201</td>
<td>213,760</td>
<td>102</td>
<td></td>
<td></td>
<td>255,040</td>
<td></td>
</tr>
<tr>
<td>Highway trust fund</td>
<td>68,940</td>
<td>102</td>
<td>166,494</td>
<td>3,380</td>
<td>87</td>
<td>322,243</td>
<td></td>
</tr>
<tr>
<td>Other Governmental Funds</td>
<td>329,883</td>
<td>166,494</td>
<td>87</td>
<td>1,145</td>
<td></td>
<td>520,989</td>
<td></td>
</tr>
<tr>
<td>Unemployment Compensation Fund</td>
<td>8,300</td>
<td>8,300</td>
<td>8,300</td>
<td>8,300</td>
<td></td>
<td>8,300</td>
<td></td>
</tr>
<tr>
<td>EPA Revolving Loan Fund</td>
<td>270</td>
<td>3</td>
<td>273</td>
<td></td>
<td></td>
<td>273</td>
<td></td>
</tr>
<tr>
<td>N.C. State Lottery Fund</td>
<td>17</td>
<td>63,552</td>
<td>1,029</td>
<td>64,589</td>
<td></td>
<td>64,589</td>
<td></td>
</tr>
<tr>
<td>Other Enterprise Funds</td>
<td>752</td>
<td>4,905</td>
<td>5,657</td>
<td></td>
<td></td>
<td>5,657</td>
<td></td>
</tr>
<tr>
<td>Internal Service Funds</td>
<td>129</td>
<td>31</td>
<td>180</td>
<td></td>
<td></td>
<td>180</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$252,555</td>
<td>$1,071,463</td>
<td>$1,321</td>
<td>$8,686</td>
<td>$2,155</td>
<td>$1,797,964</td>
<td></td>
</tr>
</tbody>
</table>

Transfers are primarily used to (1) transfer revenues and bond proceeds from the fund required by State statute or budget to collect the revenue to the fund required by State statute or budget to expend them, (2) provide unrestricted revenues collected in the general fund to finance operating and capital programs accounted for in other funds in accordance with budgetary authorizations, and (3) reflect reversions of State funds from other funds to the General Fund in accordance with Office of State Budget and Management requirements.

When the Highway Trust Fund was created in 1989, the revenue from the sales tax on motor vehicles was transferred from the General Fund to the Highway Trust Fund. To offset a portion of this revenue loss in the General Fund, the Highway Trust Fund is required to transfer funds to the General Fund each year. The total transfer for this fiscal year was $252.55 million.

In 1998 a suit was filed by the N.C. School Boards Association, et.al. against Richard H. Moore, State Treasurer, et.al. The court case questioned certain collections received by the Department of Revenue. On July 1, 2005 the Supreme Court concluded that these collections previously recorded as taxes were in fact civil penalties and ordered them paid into the Civil Penalty and Forfeiture Fund (other governmental funds). This resulted in a significant increase of the amount transferred from the General Fund to the Civil Penalty and Forfeiture Fund of approximately $56.57 million.

In compliance with the North Carolina State Lottery Act, House Bill 1023 (Session Law 2005), all “Net Revenues” of the NC State Lottery Fund are required to be transferred to the Education Lottery Fund (other governmental funds) for educational purposes. The total transfer for this fiscal year was $63.55 million, as set forth in General Statute 18C-164.
NOTE 10: FUND BALANCE RESERVES AND DESIGNATIONS

Reserved Fund Balance. The State’s reserved fund balances represent those portions of the fund balances that are either (a) externally restricted for a specific use, (b) not available for appropriation or expenditure because the underlying asset is not an available financial resource for current appropriation or expenditure, or (c) for encumbrances, which represent commitments related to unperformed contracts for services and undelivered goods. The reserved fund balances at June 30, 2006, are (dollars in thousands):

<table>
<thead>
<tr>
<th>Governmental Funds</th>
<th>General Fund</th>
<th>Highway Fund</th>
<th>Highway Trust Fund</th>
<th>Other Governmental Funds</th>
<th>Total Governmental Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specific encumbrances</td>
<td>$31,856</td>
<td>$10,495</td>
<td>$ —</td>
<td>$ —</td>
<td>$42,353</td>
</tr>
<tr>
<td>Inventories</td>
<td>$73,343</td>
<td>$4,833</td>
<td>$ —</td>
<td>$33,818</td>
<td>$111,994</td>
</tr>
<tr>
<td>Investments</td>
<td>$52</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$52</td>
</tr>
<tr>
<td>Permanent investments</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$57,372</td>
<td>$57,372</td>
</tr>
<tr>
<td>Notes receivable</td>
<td>$8,578</td>
<td>$1,102</td>
<td>$107</td>
<td>$334,362</td>
<td>$342,149</td>
</tr>
<tr>
<td>Compensated absences charged to federal projects</td>
<td>$ —</td>
<td>$31,871</td>
<td>$ —</td>
<td>$ —</td>
<td>$31,871</td>
</tr>
<tr>
<td>Prepaid items</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$991</td>
<td>$991</td>
</tr>
<tr>
<td>Continuing programs</td>
<td>$39,076</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$39,076</td>
</tr>
<tr>
<td>Capital projects</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$139,650</td>
<td>$139,650</td>
</tr>
<tr>
<td>Advance to component unit</td>
<td>$ —</td>
<td>$3,622</td>
<td>$ —</td>
<td>$21,742</td>
<td>$25,364</td>
</tr>
<tr>
<td>Loan and grant commitments</td>
<td>$ —</td>
<td>$3,181</td>
<td>$ —</td>
<td>$287,095</td>
<td>$290,276</td>
</tr>
<tr>
<td>Advance to other funds</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
<td>$ —</td>
</tr>
<tr>
<td>Other purposes</td>
<td>$4,511</td>
<td>$2,517</td>
<td>$ —</td>
<td>$28,378</td>
<td>$35,406</td>
</tr>
<tr>
<td>Total reserved fund balance</td>
<td>$155,419</td>
<td>$53,999</td>
<td>$3,729</td>
<td>$903,408</td>
<td>$1,116,554</td>
</tr>
</tbody>
</table>

Unreserved Designated Fund Balance. The State’s unreserved fund balance designations in the General Fund represent tentative plans for use in a future period. The State’s internal governing body (General Assembly) establishes restrictions on the use of these assets which are reported as fund balance designations. Fund balance designations in the General Fund are established based on the amount of reserves available as measured on the budgetary basis of accounting and authorized carryforwards for continuing General Fund programs. These designations totaled $656,731 million at June 30, 2006. As shown in the table below, the fund balance available to be designated was a positive $1.77 billion on a modified accrual basis at June 30, 2006 (dollars in thousands):

<table>
<thead>
<tr>
<th>Unreserved Designated Fund Balance</th>
<th>General Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disaster relief</td>
<td>$141,712</td>
</tr>
<tr>
<td>Repairs and renovations</td>
<td>$222,229</td>
</tr>
<tr>
<td>Higher education</td>
<td>$49,067</td>
</tr>
<tr>
<td>Agriculture</td>
<td>$5,491</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>$37,019</td>
</tr>
<tr>
<td>Economic development programs</td>
<td>$18,323</td>
</tr>
<tr>
<td>General government programs</td>
<td>$25,849</td>
</tr>
<tr>
<td>Health and human services programs</td>
<td>$125,457</td>
</tr>
<tr>
<td>Public safety, corrections,</td>
<td>$28,379</td>
</tr>
<tr>
<td>and regulation programs</td>
<td></td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>$3,205</td>
</tr>
<tr>
<td>Total designations</td>
<td>$656,731</td>
</tr>
<tr>
<td>Unreserved fund balance</td>
<td>$1,769,780</td>
</tr>
</tbody>
</table>
NOTE 11: RETIREMENT PLANS

The State reports ten retirement plans as pension trust funds. Section A of this note describes the seven defined benefit public employee retirement plans and one defined contribution plan administered by the State. The remaining plans, described in Note 12, are defined contribution plans administered by a third party under the auspices of the State. The State may or may not make supplementary contributions to these plans. Although the assets of the administered plans are commingled for investment purposes, each plan's assets may be used only for payment of benefits to the members of that plan and for administrative costs in accordance with the terms of the plan. The plans in this note do not issue separate financial statements, nor are they reported as part of other entities. The financial statements and other required disclosures are presented in Note 15 and in the Required Supplementary Information section of this CAFR. The State also provides an optional retirement plan for certain university employees and a special separation allowance for eligible sworn law enforcement officers.

A. Plan Descriptions and Contribution Information

1. TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina to provide pension benefits for employees of the State, its component units, and local boards of education not in the reporting entity. Membership is comprised of employees of state agencies and institutions, local boards of education, universities and community colleges and certain proprietary component units. At June 30, 2006, the number of participating local boards of education and component unit employers was 194 as shown below:

| Local boards of education       | 115 |
| Community colleges              | 58  |
| University of North Carolina System | 18  |
| Proprietary component units     | 3   |

Benefits and administrative expenses are funded by member contributions of 6% of compensation, investment income, and by an actuarially required employer contribution established by legislation. For the fiscal year ended June 30, 2006, the State made the actuarially based required contribution of 2.34% of covered payroll. Benefit and contribution provisions are established by General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

2. CONSOLIDATED JUDICIAL RETIREMENT SYSTEM

This plan is a single-employer, defined benefit plan established by the State of North Carolina to provide pension benefits for employees of the State Judicial System. Membership is comprised of judges, district attorneys and clerks of court. The plan provides retirement, disability and death benefits. Benefits and administrative expenses are funded by member contributions of 6% of compensation, investment income, and by employer contributions. For the fiscal year ended June 30, 2006, the State made a statutory contribution of 12.59% of covered payroll. This was greater than the actuarially required contribution of 12.06%. The difference of .53% was applied against the State's net pension obligation to this plan. Benefit and contribution provisions are established by General Statutes 135-57, 135-58, 135-68 and 135-69 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

3. LEGISLATIVE RETIREMENT SYSTEM

This plan is a single-employer, defined benefit plan established by the State of North Carolina to provide retirement and disability benefits for members of the General Assembly.

The benefit will not be payable while the member is employed in a position making him eligible to participate in either the Teachers' and State Employees' Retirement System, Consolidated Judicial Retirement System or the Local Governmental Employees' Retirement System. Benefits and administrative expenses are funded by member contributions of 7% of compensation, investment income, and by actuarially based employer contributions. For the fiscal year ended June 30, 2006, there was no actuarially based required contribution and none was made. Benefit and actuarially based contribution provisions are established by General Statutes 120-4.21, 120-4.19 and 120-4.20 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.
OTHER STATE ADMINISTERED SYSTEMS

The State also administers the following pension and retirement plans for persons who are not considered employees of the State or its component units.

4. FIREMEN'S AND RESCUE SQUAD WORKERS' PENSION FUND

This plan is a defined benefit pension plan established by the State of North Carolina to provide pension benefits for all eligible firemen and rescue squad workers. Membership is composed of both volunteer and locally employed firemen and emergency medical personnel who elect membership. At June 30, 2006, there were 1,491 participating fire and rescue units. This is a special funding situation in that the State is not the employer but is legally obligated to contribute to the plan.

Benefits and administrative expenses are funded by a ten dollar monthly contribution by the member, investment income and an actuarially based state appropriation. Benefit and contribution provisions are established by General Statute 58-86 and may be amended only by the North Carolina General Assembly.

5. NORTH CAROLINA NATIONAL GUARD PENSION FUND

This plan is a defined benefit plan established by the State of North Carolina to provide pension benefits for members of the North Carolina national guard. This also is a special funding situation because the State is not the employer, but is legally obligated to contribute to the plan.

Benefits and administrative expenses are funded by an actuarially based state appropriation and investment income. Benefit and contribution provisions are established by General Statute 127A-40 and may be amended only by the North Carolina General Assembly.

6. REGISTERS OF DEEDS' SUPPLEMENTAL PENSION FUND

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina to provide supplemental pension benefits for all eligible, retired county registers of deeds. Membership is composed of registers who are retired from the Local Governmental Employees' Retirement System or an equivalent local plan and have met the statutory eligibility requirements. At June 30, 2006, there were 100 registers enrolled in the plan with all 100 counties participating. An individual's benefits for the year are calculated as a share of accumulated contributions available for benefits for that year, subject to certain statutory limits. An individual's eligibility is based on minimum years of service as a register with the individual's share increasing with years of service. Because of the statutory limits noted above, not all contributions available for benefits are distributed. The State Treasurer administers the plan and Section B of this note describes the accounting and investing for the plan. The State's only cost in the plan is administration.

Benefits and administrative expenses are funded by investment income and 4.5% of the receipts collected by each County Commission under Article 1 of Chapter 161 of the North Carolina General Statutes. The statutory contribution currently has no relationship to the actuary's required contribution. Registers do not contribute. The actuarially required contribution and percentage of that contribution actually made is in the Required Supplementary Information section of this report. All benefit and contribution provisions are established by General Statute 161-50 and may be amended only by the North Carolina General Assembly.
7. **Sheriffs' Supplemental Pension Fund**

This plan is a defined contribution plan established by the State of North Carolina to provide supplemental pension benefits for all eligible, retired county sheriffs. Membership is comprised of sheriffs who are retired from the Local Governmental Employees' Retirement System and beneficiaries that meet the statutory eligibility requirements. At June 30, 2006, there were 76 sheriffs and two beneficiaries enrolled in the plan with all 100 of the State's counties eligible to participate.

An individual's benefits for the year are calculated as a share of accumulated contributions available for benefits for that year, subject to certain statutory limits. An individual's eligibility is based on minimum years of service as a sheriff with the individual's share increasing with years of service. Because of the statutory limits noted above, not all contributions available for benefits are distributed. The North Carolina Department of Justice administers the plan. If the plan purchases any investments, they are held as part of the State Treasurer's Investment Pool. **Section B** of this note describes the accounting and investing for the plan. The State's only cost in the plan is administration.

Receipts collected by each county's Clerk of Superior Court under General Statutes 7A-304(a)(3a), along with investment income, support the plan's benefits and administrative expenses. Sheriffs do not contribute to the plan. For the fiscal year ended June 30, 2006, the Clerks remitted $1.24 million. All benefit and contribution provisions are established by General Statute 143-166 and may be amended only by the North Carolina General Assembly.

8. **Local Governmental Employees' Retirement System**

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina for employees of local governments. Membership is comprised of general employees and local law enforcement officers of participating local governmental entities.

At June 30, 2006, the number of participating local governments was 924, as shown below:

- Cities ........................................ 427
- Counties .................................... 100
- Special districts ............................ 397

The plan provides retirement benefits nearly identical to the benefits that accrue to members of the Teachers' and State Employees' Retirement System. This plan also provides disability benefits for members who become totally and permanently disabled from performing their usual job. Benefits and administrative expenses are funded by employee contributions of 6% and actuarially based employer contributions. The annual required contribution (ARC) for all employers was 4.75% of covered payroll for law enforcement officers and 4.28% for general employees and firemen. Actual contributions were 5.27% of covered payroll for law enforcement officers and 4.8% for general employees and firemen. In addition, employers with an unfunded liability, established when the government initially enters the system, must make additional contributions towards that liability. The State's responsibility is administrative only. Benefit and contribution provisions are established by General Statutes 128-27 and 128-30 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains.
The following table summarizes membership information by plan at the actuarial valuation date:

<table>
<thead>
<tr>
<th>Employee Groups</th>
<th>Teachers' and State Employees</th>
<th>Judicial</th>
<th>Legislative</th>
<th>Firemen's and Rescue Squad</th>
<th>North Carolina National Guard</th>
<th>Registers of Deeds</th>
<th>Local Governmental</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirees and beneficiaries currently receiving benefits</td>
<td>134,719</td>
<td>449</td>
<td>250</td>
<td>9,495</td>
<td>2,640</td>
<td>79</td>
<td>38,448</td>
</tr>
<tr>
<td>Terminated employees entitled to benefits but not yet receiving them</td>
<td>54,003</td>
<td>44</td>
<td>86</td>
<td>151</td>
<td>4,076</td>
<td>1</td>
<td>18,240</td>
</tr>
<tr>
<td>Active plan members</td>
<td>321,513</td>
<td>497</td>
<td>170</td>
<td>33,520</td>
<td>5,853</td>
<td>99</td>
<td>123,015</td>
</tr>
<tr>
<td>Total</td>
<td>510,235</td>
<td>990</td>
<td>506</td>
<td>43,166</td>
<td>12,569</td>
<td>179</td>
<td>179,703</td>
</tr>
</tbody>
</table>

Date of valuation: 12-31-05 12-31-05 6-30-05 12-31-05 12-31-05 12-31-05

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PLAN ASSET MATTERS

Basis of Accounting

The financial statements of these plans are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

Investments/Securities Lending

Pursuant to North Carolina General Statutes, the State Treasurer is the custodian and administrator of the retirement systems. The State Treasurer maintains various investment portfolios in its Investment Pool. The investment balance of each system represents its share of the fair value of the net assets of the various portfolios within the pool. Additionally, the securities lending balance represents assets occurring from securities lending transactions that result from the systems' participation in the pool. The investments of the State Treasurer and securities ending are fully discussed in Note 3.

C. Actuarial Methods and Assumptions

The latest actuarial valuations are dated December 31, 2005 (June 30, 2005, for Firemen's and Rescue Squad Workers' Fund). The actuarial accrued liability and the schedule of funding progress are presented by system in the Required Supplementary Information section of this report. The actuarial value of assets for all systems is based on a five-year smoothed market value. Under this method, realized and unrealized gains and losses on investments are smoothed over five years. Below are listed the various actuarial methods and significant assumptions for these valuations that will be used to determine future annual required contributions.
NOTES TO THE FINANCIAL STATEMENTS

The valuations for the Teachers' and State Employees' system, Legislative system, and Consolidated Judicial system reflect a 3% cost of living increase for retirees in these systems. The Firemen's and Rescue Squad Workers' Fund increases retirement benefits by $2 (from $163 to $165). The National Guard system increases basic benefits from $75 to $80 and total potential benefits from $150 to $160. The Local Governmental Employee's system reflects a 2.8% cost of living increase. All of the benefit enhancements listed in this paragraph reflect legislation enacted by the North Carolina General Assembly effective July 1, 2006.

As of this valuation, the unfunded actuarial accrued liability for the Registers of Deeds' system, when amortized over 40 years is less than zero. This situation, which is not allowable under generally accepted accounting principles, is redefined by the actuary to effectively mean there is no liability to be amortized.

The projected investment returns and projected salaries for all systems, except the Legislative, include a 3.75% inflationary factor within the actuarial assumption. The assumption for the Legislative system does not identify an inflationary factor.

CURRENT FISCAL YEAR ASSUMPTIONS

Unless otherwise noted in this footnote or in the required supplementary schedules, the actuarial values, methods and significant assumptions for the current year's required contributions are the same as those presented in the table shown on the prior page. The annual required contributions (ARC) for the fiscal year ended June 30, 2006, were developed from various prior year valuations. The Teachers' and State Employees', Local Governmental Employees', Consolidated Judicial, and National Guard systems' valuations were as of December 31, 2003, the Legislative system was valued at December 31, 2004, and the Firemen's and Rescue Squad Worker's Fund was valued at June 30, 2004. These valuations used amortization periods of eight years for Legislative and nine years for all the other systems. Registers of Deeds' was valued at December 31, 2003, but effectively had no liability to be amortized. The Local Governmental Employees' system is an aggregate of numerous employers, and consequently, has various amortization periods. The rate of investment return and projected salary increases used in these valuations assumed essentially the same increases as in the most current valuations reported on the prior page.

For the fiscal year ended June 30, 2006, retirees in the Local Governmental Employees' system received a 2.5% cost of living adjustment. The Teachers' and State Employees' system, Legislative Retirement system and the Consolidated Judicial system provided a 2% cost of living increase for retirees. The Firemen's and Rescue Squad Workers' Fund increased retirement benefits from $161 to $163. All of these benefit enhancements reflect legislation enacted by the North Carolina General Assembly effective July 1, 2005. These enhancements were either reflected as liabilities in the December 31, 2004, valuations, or the systems paid for them through actuarial gains.

D. Annual Pension Cost and Net Pension Obligation

The annual pension costs and net pension obligations for the State's single-employer and special funding defined benefit plans for the current fiscal year are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Consolidated Judicial Retirement System</th>
<th>Legislative Retirement System</th>
<th>Firemen's and Rescue Squad Workers' Pension Fund</th>
<th>North Carolina National Guard Pension Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual required</td>
<td>$6,448</td>
<td>$99</td>
<td>$7,926</td>
<td>$5,944</td>
</tr>
<tr>
<td>contribution</td>
<td></td>
<td>(176)</td>
<td>(105)</td>
<td>(28)</td>
</tr>
<tr>
<td>Interest on net pension</td>
<td></td>
<td></td>
<td>49</td>
<td>58</td>
</tr>
<tr>
<td>obligation</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Adjustment to annual</td>
<td></td>
<td>6,371</td>
<td>7,870</td>
<td>5,974</td>
</tr>
<tr>
<td>required contribution</td>
<td></td>
<td>(176)</td>
<td>(56)</td>
<td>(88)</td>
</tr>
<tr>
<td>Annual pension cost</td>
<td></td>
<td>6,732</td>
<td>7,926</td>
<td>6,042</td>
</tr>
<tr>
<td>Less: Contributions</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>made</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase (decrease)</td>
<td></td>
<td>(361)</td>
<td>(56)</td>
<td>(88)</td>
</tr>
<tr>
<td>in net pension</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>obligation</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net pension (asset)</td>
<td></td>
<td>1,368</td>
<td>676</td>
<td>388</td>
</tr>
<tr>
<td>obligation beginning</td>
<td></td>
<td>(21)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>of year</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net pension (asset)</td>
<td></td>
<td></td>
<td>$620</td>
<td>$464</td>
</tr>
<tr>
<td>obligation end of year</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The following table presents the required three year trend of pension costs for the State's single-employer and special funding defined benefit plans and the annual required contributions (ARC) the State made to the Teachers' and State Employees' Retirement System (the System), a cost-sharing, multiple-employer plan. Except for (A) below, the State's statutory annual contribution to the System equals its total annual payment to the System and equals the State's pension cost in these financial statements. The State does not make any contributions to the Local Governmental Employees' System; therefore, it has no related pension cost.

### State of North Carolina's Annual Pension Cost (APC) and Annual Required Contributions (ARC) as an Employer

For the Years Ended June 30, 2004 through June 30, 2006 (dollars in thousands)

<table>
<thead>
<tr>
<th></th>
<th>Teachers' and State Employees'</th>
<th>Judicial</th>
<th>Legislative</th>
<th>Firemen's and Rescue Squad</th>
<th>North Carolina National Guard</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Primary Government:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>66,873</td>
<td>6,371</td>
<td>4</td>
<td>7,870</td>
<td>5,974</td>
</tr>
<tr>
<td>2005</td>
<td>59,021</td>
<td>6,432</td>
<td>4</td>
<td>7,460</td>
<td>1,431</td>
</tr>
<tr>
<td>2004 (A)</td>
<td>35,762</td>
<td>5,404</td>
<td>6</td>
<td>6,730</td>
<td>1,043</td>
</tr>
<tr>
<td><strong>Component units:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Universities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>35,445</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>31,037</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>3,038</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Community Colleges:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>14,990</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>13,037</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>1,211</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proprietary Funds:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>481</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>410</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>38</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Primary Government and Component Units:</strong></td>
<td>117,789</td>
<td>6,371</td>
<td>4</td>
<td>7,870</td>
<td>5,974</td>
</tr>
<tr>
<td>2005</td>
<td>103,505</td>
<td>6,432</td>
<td>4</td>
<td>7,460</td>
<td>1,431</td>
</tr>
<tr>
<td>2004</td>
<td>40,049</td>
<td>5,404</td>
<td>6</td>
<td>6,730</td>
<td>1,043</td>
</tr>
<tr>
<td><strong>Percentage of APC Contributed:</strong></td>
<td></td>
<td></td>
<td>106%</td>
<td>0%</td>
<td>101%</td>
</tr>
<tr>
<td>2006</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Percentage of ARC Contributed:</strong></td>
<td></td>
<td></td>
<td>101%</td>
<td>0%</td>
<td>101%</td>
</tr>
<tr>
<td>2006</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Net Pension (Asset) Obligation:</strong></td>
<td></td>
<td></td>
<td>$ 1,007</td>
<td>$ (17)</td>
<td>$ 620</td>
</tr>
<tr>
<td>2006</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>2005</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(A) - The State's contribution/pension cost for the Teachers' and State Employees' Retirement System equals the actuarially required contribution plus $30 million in additional appropriations mandated by the N.C. General Assembly.

Yearly pension liabilities for the systems are shown in the Required Supplementary Information section of this report. Beginning with the accounting transition year of 1997, liabilities were determined in accordance with Governmental Accounting Standards Board Statement No. 27 (GASB 27). As presented here, each system's yearly APC and net pension (asset) obligation were computed retroactively to 1993 in accordance with GASB 27 and contain the cumulative effect of applying that statement.
E. Optional Retirement Plan

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Faculty and administrators with faculty rank in universities of the UNC System may join the Program instead of the Teachers' and State Employees' Retirement System. At June 30, 2006, the Plan had 11,239 participants.

Benefits are provided by means of contracts issued and administered by the privately-operated Teachers' Insurance and Annuity Association and the College Retirement Equities Fund (TIAA/CREF), Valid, Fidelity Investments and Lincoln National Life Insurance Company. Participants' eligibility and contributory requirements are established in General Statutes 135-5.1. Participants contribute 6% of compensation and the university contributes 6.84%. There is no liability other than the universities' required contributions. The universities contributed $67.09 million for the fiscal year ended June 30, 2006. Annual covered payroll was $980.88 million and employer contributions expressed as a percentage of annual covered payroll were the required 6.84% for the fiscal year ended June 30, 2006. Employee contributions expressed as a percentage of annual covered payroll were the required 6%, with actual employee contributions of $58.85 million for the fiscal year ended June 30, 2006.

Participants are vested after five years of service, but the company must return the value of the universities' contributions to the State if termination occurs prior to five years of service. The participant chooses his/her own investment products with the company of choice.

F. Special Separation Allowance

The State provides a special separation allowance (SSA), an agent multiple-employer, defined benefit pension plan, for sworn law enforcement officers as defined by General Statutes 135-1(11b) or General Statutes 143-166.30(a)(4) that were employed by State agencies and component units and retired on a basic service retirement under the provisions of General Statutes 135-5(a). To qualify for the allowance, each retired officer must: (1) have completed 30 or more years of creditable service or have attained 55 years of age and completed five or more years of creditable service; and (2) not have attained 62 years of age; and (3) have completed at least five years of continuous service as a law enforcement officer immediately preceding a service retirement. Each eligible officer is paid an annual separation allowance equal to .85% of the officer's most recent base rate of compensation for each year of creditable service. For the fiscal year ended June 30, 2006, the State and its component units paid $12.21 million for 977 retired law enforcement officers. These benefits are funded on a pay-as-you-go basis with each employer (the State or component unit) responsible for the benefits to their former employees. There is no statewide administration of the SSA and there is no actuarial valuation performed. Funds for this allowance are appropriated annually in the budget of each affected state agency or paid from the component unit's operations. These benefits are established in General Statute 143-166.41 and may be amended only by the General Assembly.
NOTE 12: DEFERRED COMPENSATION PLANS

IRC Section 457 Plan – General Statute 143B-426.24 authorized the creation of the Board of Trustees of the North Carolina Public Employee Deferred Compensation Plan (the Board). The Board was established as an agency of the State to offer the State’s permanent employees, university employees, and the employees of certain other component units, a uniform Deferred Compensation Plan (the Plan) in accordance with Internal Revenue Code Section 457. The Plan permits each participating employee to defer a portion of his or her salary until future years by having the funds invested in various instruments that make up the North Carolina Public Employee Deferred Compensation Trust Fund. This fund is held in trust by the Plan for the exclusive benefit of participating employees and their beneficiaries. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Board. The Board has delegated the general administration of the Plan to a third party but has retained all statutory authority and fiduciary responsibility for major decisions of the Plan. The Plan is reported in the CAFR as a pension and other employee benefit trust fund. All costs of administering and funding the Plan are the responsibility of the plan participants. The Plan’s financial statements are available by contacting the N.C. Department of State Treasurer at 325 North Salisbury Street, Raleigh, NC 27603-1385.

IRC Section 401(k) Plan – Effective January 1, 1985, Chapter 135, Article 5 of the General Statutes authorized the creation of the Supplemental Retirement Income Plan of North Carolina (the Plan) in accordance with Internal Revenue Code Section 401(k). All members of the Teachers’ and State Employees’ Retirement System, Consolidated Judicial Retirement System, Legislative Retirement System, Local Governmental Employees’ Retirement System and University Optional Retirement Program are eligible to enroll in the Plan and may contribute up to 20% (limited to an Internal Revenue maximum dollar amount) of their compensation during the plan fiscal year. Members of the Plan may receive their benefits upon retirement, disability, termination, hardship, or death. All contributions and costs of administering the Plan are the responsibility of the participants.

The Plan is a defined contribution pension plan that is administered by a third party contractor. The contractor prepares financial statements based on the Plan’s fiscal year. The audited statements for the year ended December 31, 2005, are presented in this financial report as a pension and other employee benefit trust fund. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. The Plan’s financial statements are prepared using the accrual basis of accounting. Investments are reported at fair value. Securities and mutual funds are based on published quotations while bank investment contracts are stated at contract value. Notes Receivable represent loans to participants and are reported at outstanding principal balances. Prudential Retirement Services administers the Plan, and the Plan’s financial statements are available by contacting the N.C. 401(k) Plan, 150 Fayetteville Street Mall, Suite 1340, Raleigh, NC 27601.

In addition to the voluntary contribution criteria above, General Statute 143-166.30 requires state contributions to the Plan to provide benefits for all law enforcement officers employed by the State and its component units. General Statute 143-166.50 requires local governmental units with law enforcement officers to also contribute at least as much as the State. Participation begins at the date of employment. State agencies and component units are required to contribute monthly to the individual accounts of participants an amount equal to 5% of each officer’s monthly salary. The State is also required to contribute to the individual accounts of all officers on a per capita basis in equal shares. State law enforcement officers receive $50 for each court cost assessed and collected under General Statute 7A-304, while $1.25 of this assessment goes to local law enforcement officers. General Statutes allow law enforcement officers to voluntarily contribute up to 10% of their compensation within any calendar year, but current Internal Revenue Code restrictions limit the actual voluntary contribution a law enforcement officer can make. All contributions are immediately vested in the name of each participant. At December 31, 2005, 45 state agencies and component units along with 465 local governmental units outside our reporting entity contributed the required 5%. In addition, 5 state agencies and 406 local government employers contributed to the Plan on a voluntary basis.

At December 31, 2005, the Plan disclosed the following investments (at fair value) exceeding 5% of the Plan’s net assets (in thousands):

- Van Kampen Growth and Equity A ........................................... $ 642,420
- Vanguard Equity Index .......................................................... 588,178
- Growth Fund of America ...................................................... 437,201
- Fidelity Intermediate Bond Fund .............................................. 209,248
- Van Kampen Equity Income A ................................................ 196,999
- Oppen Main St Small Cap ....................................................... 127,040
- American EuroPacific Growth ................................................. 122,841

In addition, the Plan owned $887.71 million of Prudential’s Stable Value Fund. This investment exceeded 5% of net assets and is disclosed as a related party transaction because the Prudential Insurance Company is the Plan’s contractor. The Plan’s remaining investment risks are described in Note 3. The Plan also reported total member contributions of $221.54 million. The payrolls for law enforcement officers, on which the required contributions were based for the year ended December 31, 2005, amounted to $142.9 million for the state, $17.64 million for universities, and $1.69 million for the other miscellaneous component units. The required 5% employer’s contribution was made by the State for $7.15 million, by universities for $882 thousand, and by the remaining component units for $85 thousand. In addition, the State contributed $565 thousand for the required court cost assessments.
IRC Section 403(b) Plans - Employees of the UNC System and community colleges can participate in tax-sheltered annuity contracts and custodial accounts created under Internal Revenue Code (IRC) Section 403(b). Generally all employees are eligible, but the IRC does allow the establishment of a minimum contribution of $200 and the exclusion from participation of certain classes of employees. Each institution may exclude one or more of these classes if every employee within the institution meeting the class criteria is excluded from participation. The employees' eligible contributions, made through salary reduction agreements, are exempt from federal and state income taxes until the accumulated balances are received or the contributions are withdrawn. Effective January 1, 1989, contributions may be withdrawn by employees only upon separation from service, death, disability, reaching age 59 1/2 or age 55 with qualifying retirement, or due to certain financial hardships. Currently, there is no restriction on the withdrawal of the value of annuity contracts. Custodial accounts established as of December 31, 1988 can be withdrawn only in respect to hardship established as of December 31, 1988. These plans are exclusively for employees of public educational organizations and certain charitable and other non-profit institutions as defined by the IRC. Since all contributions are made voluntarily by employees, all costs are borne by the plans' participants. No direct costs are incurred by the State.
A. Health Care for Long-Term Disability Beneficiaries and Retirees

The North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan (the Plan) provides postemployment health insurance to former employees of the State, the University of North Carolina System, community colleges, certain participating proprietary component units, and Local Education Agencies (LEAs) which are not part of the reporting entity. Those former employees who are eligible to receive health care as an other postemployment benefit are long-term disability beneficiaries of the Disability Income Plan of North Carolina (DIPNC) and retirees of the Teachers' and State Employees' Retirement System (TSERS), the Consolidated Judicial Retirement System (CJRS), the Legislative Retirement System (LRS), and the University Employees' Optional Retirement Program (UEORP), with five or more years of contributory membership service in the Retirement System prior to disability or retirement. For the fiscal year ended June 30, 2006, the numbers of participants currently eligible to receive health care as an other postemployment benefit are 53,862 TSERS and DIPNC members (excluding LEA members), 311 CJRS members, 186 LRS members, 1,237 UEORP members, and 75,619 LEA members. The health insurance plan is the same as for active employees as described in Note 14, except that the coverage becomes secondary when former employees become eligible for Medicare.

The funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. These health care benefits are funded by employer contributions that are established in the biennial Appropriations Bill by the General Assembly. The State, participating component units and LEAs contributed a monthly amount equal to 3.8% of active employees' salaries to the Retiree Health Benefit Fund (the Fund). The Fund pays the full cost of coverage for long-term disability beneficiaries and retirees enrolled in the Plan. For the fiscal year ended June 30, 2006, the Fund paid $2,853 for each Medicare-eligible long-term disability beneficiary and retiree and $3,748 for each non-Medicare-eligible long-term disability beneficiary and retiree. At June 30, 2006, net assets of the Fund available for future other postemployment benefits for eligible beneficiaries were $171.13 million.

For the fiscal year ended June 30, 2006, contributions on behalf of former employees were made to the Fund as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Fund</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary government</td>
<td>$110,766</td>
</tr>
<tr>
<td>University of N. Carolina System</td>
<td>94,523</td>
</tr>
<tr>
<td>Community Colleges</td>
<td>24,342</td>
</tr>
<tr>
<td>Certain participating proprietary component units</td>
<td>781</td>
</tr>
<tr>
<td>Total contributions by the reporting entity</td>
<td>230,412</td>
</tr>
<tr>
<td>Contributions made by LEAs</td>
<td>246,510</td>
</tr>
<tr>
<td>Total contributions</td>
<td>$476,922</td>
</tr>
</tbody>
</table>

These benefits are established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly.

B. Disability Income

As discussed in Note 14, short-term and long-term disability benefits are provided to the eligible members of the Teachers' and State Employees' Retirement System and the University Employees' Optional Retirement Program through the Disability Income Plan of North Carolina (DIPNC). It is reported in this CAFR as a pension and other employee benefit trust fund. Long-term disability benefits are payable as an other postemployment benefit from DIPNC after the conclusion of the short-term disability period or after salary continuation payments cease, whichever is later, for as long as an employee is disabled. An employee is eligible to receive long-term disability benefits provided the following requirements are met: (1) the employee has five or more years of contributing membership service in the Teachers' and State Employees' Retirement System of North Carolina (Retirement System) or the University Employees' Optional Retirement Program, earned within ninety-six months prior to the end of the short-term disability period or cessation of salary continuation payments, whichever is later; (2) the employee must make application to receive long-term benefits within 180 days after the conclusion of the short-term disability period or after salary continuation payments cease or after monthly payments for Workers' Compensation cease (excluding monthly payments for permanent partial benefits), whichever is later; (3) the employee must be certified by the Medical Board to be mentally or physically disabled for the further performance of his/her usual occupation; (4) the disability must have been continuous, likely to be permanent, and incurred at the time of active employment; (5) the employee must not be eligible to receive an unreduced retirement benefit from the Retirement System; and (6) the employee must terminate employment as a permanent, full-time employee. An employee is eligible to receive an unreduced retirement benefit from the Retirement System after (1)
reaching the age of 65 and completing five years of creditable service, or (2) reaching the age of 60 and completing 25 years of creditable service, or (3) completing 30 years of creditable service, at any age.

The monthly long-term disability benefit is equal to 65% of one-twelfth of an employee’s annual base rate of compensation last payable to the participant or beneficiary prior to the beginning of the short-term disability period, plus the like percentage of one-twelfth of the annual longevity payment to which the participant or beneficiary would be eligible. The monthly benefits are subject to a maximum of $3,900 per month reduced by any primary Social Security disability benefits and by monthly payments for Workers’ Compensation to which the participant or beneficiary may be entitled, but the benefits payable shall be no less than $10 a month. When an employee qualifies for an unreduced service retirement allowance from the Retirement System, the benefits payable from DIPNC will cease, and the employee will commence retirement under the Teachers’ and State Employees’ Retirement System or the University Employees’ Optional Retirement Program.

Long-term disability income benefits are advance-funded and actuarially based using the one-year term cost method. Although the DIPNC operates on a calendar year, disability income benefits are funded by employer contributions that are established in the Appropriations Bill by the General Assembly and coincide with the state fiscal year. For the fiscal year ended June 30, 2006, the actuary recommended contribution rate was .52% of member compensation. However, the Appropriations Bill required the State, the University of North Carolina System, community colleges, certain participating component units, and LEAs to contribute .52% of active employees’ salaries to fund the disability benefits. The contributions cannot be separated between the amounts that relate to other postemployment benefits and employment benefits for active employees.

At December 31, 2005 (the most recent actuarial valuation date), DIPNC had 5,639 members, including 2,501 LEA members, who were currently eligible to receive disability benefits as an other postemployment benefit out of a total of 332,752 active plan participants. Those individuals who are receiving extended short-term disability benefit payments cannot be separated from the number of members currently eligible to receive disability benefits as an other postemployment benefit.

<table>
<thead>
<tr>
<th>Actuarial Assumptions for the calendar year ended December 31, 2005:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discount rate .................................................................. 7.25%</td>
</tr>
<tr>
<td>Rate of return on investments assumption ............................. 7.25%</td>
</tr>
<tr>
<td>Projected salary increase assumption ................................... 4.5-18.1%</td>
</tr>
<tr>
<td>Projected social security benefits increase assumption............... 3.75%</td>
</tr>
<tr>
<td>Social security assumption .................................................. 50%</td>
</tr>
<tr>
<td>The required and actual contributions made for the current fiscal year are as follows (dollars in thousands):</td>
</tr>
<tr>
<td>Annual required contribution for the reporting entity .............. $ 31,233</td>
</tr>
<tr>
<td>Annual required contribution for LEAs .................................... 33,733</td>
</tr>
<tr>
<td>Total required contributions ................................................ $ 64,966</td>
</tr>
<tr>
<td>Actual contribution made by:</td>
</tr>
<tr>
<td>Primary Government ........................................................... $ 14,861</td>
</tr>
<tr>
<td>University of North Carolina System ..................................... 12,934</td>
</tr>
<tr>
<td>Community Colleges ............................................................ 3,331</td>
</tr>
<tr>
<td>Certain participating component units .................................... 107</td>
</tr>
<tr>
<td>Total actual contribution made by the reporting entity ................ $ 31,233</td>
</tr>
<tr>
<td>Actual contribution made by LEAs .......................................... 33,733</td>
</tr>
<tr>
<td>Total actual contribution made ............................................ $ 64,966</td>
</tr>
</tbody>
</table>

The basis for estimating the actuarial liabilities for unpaid claims is discussed in Note 14. The market related actuarial value of the assets of DIPNC at December 31, 2005, was $279.29 million creating an actuarial deficit of $39.96 million. The actual fair value of the assets for DIPNC at December 31, 2005 was $275.07 million. The assets are available for future other postemployment benefits and benefits for eligible active employees.

These benefits are established by Chapter 135, Article 6, of the General Statutes and may be amended only by the North Carolina General Assembly.
NOTE 14: RISK MANAGEMENT AND INSURANCE

A. Public Entity Risk Pool

Public School Insurance Fund

The Public School Insurance Fund (the Fund) is a public entity risk pool reported within the enterprise funds. In accordance with Chapter 115C, Article 38, of the General Statutes, the purpose of the Fund is to insure the Local Education Agencies (LEAs), in order to safeguard the investment made in the public schools of North Carolina. The community colleges, which are component units, can also acquire insurance through the Fund as stated in G.S. 115D-58.11(c). The board of each LEA and the board of trustees of each community college are required to carry extended coverage against fire and lightning damage to the extent of not less than seventy-five percent (75%) of the current value for each insurable building. Additionally, the boards are to insure adequately the equipment and contents of said building. The Fund is financed by premiums collected from the LEAs and the community colleges and interest is earned on the Fund's cash balance. Each board has to give notice of its election to insure in the Fund at least 30 days prior to such insurance becoming effective and shall furnish to the State Board of Education a full and complete list of all outstanding fire insurance policies. While the said insurance policies remain in effect, the Fund shall act as co-insurer of the properties covered by such insurance. The Fund currently insures 98 out of 115 LEAs and 28 out of 58 community colleges.

Claim liabilities are based on estimates of the ultimate cost of losses that have been reported but not settled. There are no salvage claims anticipated since any salvage is adjusted in the claim settlement. There are no subrogation claims pending. Since claims are reviewed by adjusters and the actual loss projection is computed in a short time after the claim is reported, the claim adjustment expense associated with the unpaid claim liability will be reflected in the current period. The Fund does consider investment income in determining if a premium deficiency exists.

The only acquisition costs are related to proposal costs and inspection costs for new insurance. Since the Fund can only insure the LEAs and the community colleges, new contracts are immaterial. Since existing contracts are renewed once a year, the Fund's costs are for policy maintenance. Therefore, acquisition costs do not need to be amortized.

The following schedule shows the changes in the reported liability for the past two years (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Fiscal Year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
</tr>
<tr>
<td>Unpaid claims at beginning of year</td>
<td>$ 1,229</td>
</tr>
<tr>
<td><strong>Incurred claims:</strong></td>
<td></td>
</tr>
<tr>
<td>Provision for insured events of the current year</td>
<td>3,273</td>
</tr>
<tr>
<td>Increases (decreases) in provision for insured events of prior years</td>
<td>(177)</td>
</tr>
<tr>
<td>Total incurred claims</td>
<td>3,096</td>
</tr>
<tr>
<td><strong>Payments:</strong></td>
<td></td>
</tr>
<tr>
<td>Claims attributable to insured events of the current year</td>
<td>2,326</td>
</tr>
<tr>
<td>Claims attributable to insured events of the prior years</td>
<td>1,203</td>
</tr>
<tr>
<td>Total payments</td>
<td>3,529</td>
</tr>
<tr>
<td>Total unpaid claims at end of the year</td>
<td>$ 796</td>
</tr>
</tbody>
</table>

With the collection of premiums from the insured educational units, payment of valid claims becomes the responsibility of the Fund. All claims greater than $10 million per occurrence are covered by reinsurance policies. Maximum recoverable from reinsurance for any one catastrophic event is $45.5 million per occurrence. Annual aggregate limits of $15 million apply separately with respect to flood and earthquake. Coverage applies to all "all risk" perils. Boiler and machinery coverage is provided under separate contract written by the Fund. Incurred losses are reduced by estimated amounts recoverable under the Fund's reinsurance policies. Currently, there are no claims for reinsurance.

B. Employee Benefit Plans

1. State Health Plan

In accordance with Chapter 135, Article 3, Part 3, of the General Statutes, the State established the North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan, referred to as the State Health Plan (the Plan). The Plan provides comprehensive major medical care benefits for employees and retirees of the State and its participating component units, as well as their qualified dependents on a contributory basis. This care is also extended to employees and retirees of the Local Education Agencies (LEAs), and other employing units allowed by statute, which are not part of the State's reporting entity. Coverage is self-funded by contributions to the Plan, which is reported as a pension and other employee benefit trust fund. Contributions for employee
and retiree coverage are made by the State, its participating component units, LEAs, and other qualified employing units. Contributions for dependent coverage are made by employees and retirees. As described in Note 13, coverage is also extended to certain individuals as an other postemployment benefit. The Plan has contracted with third parties to process claims.

The Plan pays most expenses that are medically necessary and eligible for coverage based on usual, customary, and reasonable allowances. Claims are subject to specified annual deductible and co-payment requirements. The Plan disallows claims in excess of a lifetime maximum of $5 million.

Claim liabilities are based on estimates of the ultimate cost of claims that have been incurred (both reported and unreported). Changes in the Plan's aggregate liabilities for claims for the past two fiscal years are as follows (dollars in thousands):

2. Death Benefit Plan of North Carolina

Term life insurance (death benefits) is provided through the Death Benefit Plan, a pension and other employee benefit trust fund, to all members of the Teachers' and State Employees' Retirement System who have completed at least 12 consecutive months of membership in the System. Membership includes employees of the State, the University of North Carolina system, community colleges, and certain participating proprietary component units and Local Education Agencies (LEAs) which are not part of the reporting entity. The benefit payment is equal to the greater of (1) the compensation on which contributions were made by the member during the calendar year preceding the year in which his/her death occurs or (2) the member's highest twelve month's salary in a row during the twenty-four months prior to his/her death. The benefit is subject to a minimum of $25,000 and to a maximum of $50,000.

For the period July 1, 2005 to June 30, 2006, death benefits were funded by actuarially based employer contributions that are established in the biennial appropriation bill by the General Assembly. The State, the University of North Carolina system, community colleges, and certain participating proprietary component units and LEAs contributed .16% of active employees' salaries to fund the Death Benefit Plan for the period July 2005 to June 2006.

Changes in the aggregate liabilities for claims for the past two fiscal years are as follows (dollars in thousands):

3. Disability Income Plan of North Carolina

Short-term and long-term disability benefits are provided through the Disability Income Plan of North Carolina (DIPNC), a pension and other employee benefit trust fund, to the eligible members of the Teachers' and State Employees' Retirement System which includes employees of the State, the University of North Carolina system, community colleges, certain participating proprietary component units, and Local Education Agencies (LEAs) which are not part of the reporting entity, and the University Employees' Optional Retirement Program. Short-term benefits are payable after a waiting period of 60 continuous calendar days from the onset of disability, which is determined as the last actual day of service or the day succeeding at least 365 calendar days after the commencement of service, whichever is later. Short-term benefits are provided to currently active employees and the related liability is not measurable. As discussed in Note 13, long-term disability benefits are payable as an other postemployment benefit from DIPNC after the conclusion of the short-term disability period or after salary continuation payments cease, whichever is later, for as long as an employee is disabled. These benefits are established by Chapter 135, Article 6, of the General Statutes and may be amended only by the North Carolina General Assembly.

Claim liabilities for long-term disability benefits are actuarially estimated using the one-year term cost method. These liabilities represent the present value of future claim payments obligated to members who have become disabled. The claim liabilities are separated into the following two classifications: (1) approved claim liabilities are for long-term disabilities that have occurred, have been approved, and are in long-term payment status; and (2) incurred but not reported (IBNR) liabilities are for disabilities that have occurred but are not in payment status. The IBNR liabilities are estimated based on the historical claims experience of DIPNC.

Significant actuarial assumptions used to estimate claim liabilities are presented in Note 13. Changes in the aggregate liabilities for claims for the past two fiscal years are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Liability</th>
<th>Changes in Estimates</th>
<th>Payments</th>
<th>Balance at Fiscal Year-End</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004-05</td>
<td>1,909</td>
<td>31,222</td>
<td>(30,850)</td>
<td>2,750</td>
</tr>
<tr>
<td>2005-06</td>
<td>2,296</td>
<td>26,412</td>
<td>(25,931)</td>
<td>2,747</td>
</tr>
</tbody>
</table>
C. Other Risk Management and Insurance Activities

1. Automobile, Fire and Other Property Losses

The State is required by Chapter 58, Article 31, Part 50, of the General Statutes to provide liability insurance on every state-owned motor vehicle, which includes vehicles held by the State's participating component units. The State is self-insured for the first $500,000 of any loss through a retrospective rated plan. The plan purchases excess insurance through a private insurer to cover losses greater than $500,000. The liability limits for losses incurring in-state are $500,000 per claimant and $5 million per occurrence. For losses incurring out-of-state, the limits are $1 million per claimant and $5 million per occurrence. Covered losses include those that occur with vehicles that are not on a stationary track or rail, and federal vehicles when the Governor calls out the National Guard.

Agencies of the State and participating component units using state cars are charged premiums to cover the cost of the excess insurance and to pay for those losses falling under the self-insured retention. Premiums charged are also based on the projected losses to be incurred. The private insurer processes all claims and sets up a reserve for amounts expected to be paid for claims. Claims are paid by the private insurer after they are approved by the Attorney General's Office. Settled claims have not exceeded coverage in any of the past three fiscal years.

The State Property Fire Insurance Fund (the Fund), an internal service fund of the State, was created by Chapter 58, Article 31, of the General Statutes. The Fund insures State owned buildings and contents for fire, extended coverage, and other property losses. The Fund does not charge premiums for fire insurance for operations that are supported by the State's General Fund. Those operations that are not supported by the State's General Fund are charged for fire coverage. Agencies of the State can purchase extended coverage and other property coverage such as sprinkler leakage, business interruption, vandalism, theft, and "all risk" for buildings and contents through the Fund. For those that elect to receive any of this other coverage, the Fund charges premiums discounted from industry manual rates. The Fund insures losses up to $2.5 million per occurrence. All losses covered by the Fund are subject to a $500 per occurrence deductible except for theft, which carries a $1,000 per occurrence deductible. However, some agencies have chosen a higher deductible for a reduction in premium.

The Fund purchases excess insurance from private insurers to cover losses over the amounts insured by the Fund. If aggregate uninsured losses sustained by the Fund, in excess of $50,000 per loss, other than flood and earthquake losses and wind losses by named storms, reach $5 million in any one annual period, the Fund's deductible for the remainder of the annual period is $100,000 per occurrence. Settled claims have not exceeded coverage in any of the past three fiscal years.

Claims of $10,000 or higher are paid when the Council of State approves the request for payment. Claims less than $10,000 are paid without Council of State approval. Claims costs are recognized when they are approved by the Council of State and are outstanding for payment; when known estimates of losses are waiting to be submitted to the Council of State for approval; or when a loss occurs and can be reasonably estimated. Claims payable at June 30, 2006 are disclosed on the balance sheet as claims payable. Changes in the balances of claims liabilities for the past two fiscal years are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Liability</th>
<th>Changes in Estimates</th>
<th>Payments</th>
<th>Balance at Year-End</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004-05</td>
<td>$1,227</td>
<td>$1,451</td>
<td>$(997)</td>
<td>$1,881</td>
</tr>
<tr>
<td>2005-06</td>
<td>1,681</td>
<td>1,242</td>
<td>(1,863)</td>
<td>1,060</td>
</tr>
</tbody>
</table>
2. Medical Malpractice Protection
   
a. Professional Liability Insurance for State Medical Personnel

   All agencies of the State and participating component units are insured for tort claims up to $500,000 under the authority of the State Tort Claims Act, Chapter 143, Article 31, of the General Statutes. Organizations within the reporting entity carry excess commercial liability insurance to supplement the coverage provided by the State Tort Claims Act; however, claims involving medical malpractice are generally excluded from this coverage. The University of North Carolina at Chapel Hill Medical School (UNC-CH Medical School) and UNC Hospitals participate in the Liability Insurance Trust Fund, which is described in detail below. All other universities purchase commercial liability insurance. Chapter 237, Section 11.33, of the 1999 Session Laws of North Carolina authorized the Department of Health and Human Services, the Department of Environment and Natural Resources, and the Department of Correction to provide medical liability coverage on behalf of employees licensed to practice medicine or dentistry; all licensed physicians who are faculty members of the University of North Carolina who work on contract for the Division of Mental Health, Developmental Disabilities, and Substance Abuse Services for incidents that occur in Division programs; and on behalf of medical residents from the University of North Carolina who are in training at institutions operated by the Department of Health and Human Services. The extent of coverage is a maximum of $1 million for each individual incident and does not affect current coverage under the State Tort Claims Act. The Department of Health and Human Services, the Department of Environment and Natural Resources, and the Department of Correction purchase commercial professional liability insurance for their medical staff. Settled claims have not exceeded coverage in any of the past three fiscal years.

   Insurance coverage varies depending upon the amount of coverage and the type of policy. Typically the amount of primary coverage for medical liability is $1 million per individual, claim, or incidence, and $3 million total or aggregate. Many departments and institutions maintain excess policies to provide additional coverage above that provided by the primary policy for medical liability. The policies are written on a claims made or occurrence basis, with the majority of the policies being claims made. The claims liabilities are not measurable.

b. Self-Insurance through the Liability Insurance Trust Fund

   The Liability Insurance Trust Fund (Trust Fund) was created by Chapter 116, Article 26, of the General Statutes and the University of North Carolina Board of Governors Resolution of June 9, 1978, to provide medical malpractice protection for program participants and individual health care practitioners working as employees, agents, or officers of the program participants. The program participants are the University of North Carolina Hospitals at Chapel Hill and the University of North Carolina at Chapel Hill Physicians and Associates, both of whom are a part of the University of North Carolina system, which is a component unit of the reporting entity. Coverage is self-funded by contributions from participants and investment income. Contributions are based on the actuarially determined funding level for a given plan year.

   For the period July 1, 2005 through June 30, 2006, the Trust fund provided coverage on an occurrence basis of $3 million per individual and $7 million in the aggregate per claim. At May 1, 2005 through June 30, 2006, the Trust Fund provided coverage on an occurrence basis of $7 million per individual for each and every claim, self-insured through the Trust Fund. Effective July 1, 2005 through June 30, 2006, the Trust Fund entered into an excess of loss agreement with an unaffiliated reinsurer. Reinsurance coverage under this policy carries a $10 million aggregate limit in excess of a self-insured aggregate of $33 million subject to a $7 million per occurrence limit (sub-limit of $3 million per individual) with a $200,000 continuing underlying amount per claim. For losses occurring during the period May 1, 2004 through June 30, 2005, the Trust Fund retained 100% of the liability.

   The Trust Fund purchased a primary policy for dental residents on a claims made basis with $1 million per occurrence and $3 million annual aggregate limits of coverage. In the event the Trust Fund has insufficient funds to pay existing and future claims, it has the authority to borrow necessary amounts up to $30 million. Any such borrowing would be repaid from the assets and revenues of program participants. No borrowings have been made under this authority to date.

   The Trust Fund establishes claim liabilities based on estimates of the ultimate cost of all losses and loss adjustment expenses, including losses and loss adjustment expenses incurred but not yet reported, which are unpaid at the balance sheet date. The claims liabilities of $48,178 million and $52,230 million are the present values of the aggregate actuarially determined claims liabilities of $48,768 million and $55,296 million, discounted at 3% at June 30, 2005 and 5% at June 30, 2006, respectively. These estimates are reviewed annually, and as adjustments become necessary, such adjustments are reflected in current operations. Claims against participants are paid from the corpus of the Trust Fund. Changes in the Trust Fund’s aggregate liabilities for claims for the past two fiscal years are as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Beginning of Fiscal Year Liability</th>
<th>Current-Year Changes in Estimates</th>
<th>Claim Payments</th>
<th>Balance at Fiscal Year-End</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004-05</td>
<td>$38,085</td>
<td>$18,120</td>
<td>(6,027)</td>
</tr>
<tr>
<td>2005-06</td>
<td>48,178</td>
<td>10,453</td>
<td>(6,401)</td>
</tr>
</tbody>
</table>
3. Public Officers' and Employees' Liability Insurance

In accordance with Chapter 58, Article 32, Part 15, of the General Statutes, public officers' and employees' liability insurance is provided by private insurers for all employees of the State and participating component units except for doctors and dentists. The policy provides $5 million excess insurance over the $500,000 statutory limit payable for any one claim under the State Tort Claims Act. The first $150,000 of an award against a state agency is the responsibility of the state agency's general fund budget code or up to $500,000 if a non-general fund budget code. For general fund budget codes, any award greater than $150,000 but less than $500,000 is funded by proportionate shares of estimated lapse salaries from all agencies general fund budget codes. Since State agencies and component units are responsible for funding any tort claims of $500,000 or less from their budget and/or lapse salaries, total claims liabilities are not measurable. Employers are charged a premium for the excess insurance based on a composite rate. The employers pay the premiums directly to the private insurer. Settled claims have not exceeded coverage in any of the past three fiscal years.

4. Employee Dishonesty and Computer Fraud

Blanket public employee dishonesty and computer fraud insurance is provided for agencies of the State and its component units with a limit of $5 million per occurrence, subject to a $50,000 deductible and a 10% participation in each loss above the deductible. This coverage is placed with a private insurance company and is handled by the North Carolina Department of Insurance. Agencies of the State and its component units are charged premiums by the private insurance company. A small number of State agencies and component units of the State require faithful performance coverage in addition to employee dishonesty coverage. In these instances, separate policies have been purchased. The amounts of coverage and the deductibles vary among these separate policies. Settled claims have not exceeded coverage in any of the past three fiscal years.

5. Statewide Workers' Compensation Program

The Workers' Compensation Program (the Program) was created by Chapter 97, Article 1, of the General Statutes to provide benefits to workers injured on the job. All employees of the State and its component units are included in the Program. An injury is covered under workers' compensation if it is caused by an accident that arose out of and in the course of employment. Also, certain occupational diseases specifically designated in the North Carolina Workers' Compensation Act are compensable. Losses payable by the Program include medical claims, loss of wages, disability, and death benefits. Payments of all medical benefits are subject to approval based on a fee schedule established by the North Carolina Industrial Commission (NCIC). Loss of wages and disability benefits are payable based on 66 2/3% of an employee's average weekly salary subject to a statutory compensation rate minimum and maximum established annually by the NCIC. Death benefits are payable for 400 weeks at 66 2/3% of an employee's average weekly salary. In certain instances, death benefits may be extended beyond the 400 weeks.

The responsibility for claiming compensation is on the injured employee. If the injured employee or his representative does not notify the employer within 30 days from the date of injury, the employer can refuse compensation. A claim must be filed with the NCIC by either the employee or the employer within two years from the date of knowledge thereof; otherwise the claim is barred by law and no further compensation is allowable. When an employee is injured, the employer's primary responsibility is to arrange for and provide the necessary treatment for any work-related injury. The employer tries to provide the best possible medical care for injured employees to help them reach maximum medical improvement and return to work as soon as possible.

The State and its component units are self-insured for workers' compensation. A third-party administrator handles workers' compensation claims except for the Department of Transportation. State agencies and participating component units contribute to a fund administered by the Office of the State Controller to cover their workers' compensation claims. The third party administrator receives a per case administration fee and draws down State funds to make medical and indemnity payments on behalf of the State in accordance with the North Carolina Workers' Compensation Act.

Each state agency and participating component unit is responsible for paying claims out of its individual budget. Budgets for workers' compensation for most State agencies and participating component units are based on the prior year's loss experience. Since the related liability is not measurable, claim costs are recognized when paid. The Department of Transportation is the only state agency that sets up a reserve for claims. For the year ended June 30, 2006, workers' compensation costs were recognized as follows (dollars in thousands):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary government</td>
<td>$33,000</td>
</tr>
<tr>
<td>University of North Carolina System</td>
<td>2,283</td>
</tr>
<tr>
<td>All other component units</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$35,287</td>
</tr>
</tbody>
</table>
6. Workers’ Compensation Fund

The Workers’ Compensation Fund (the Fund) is an insurance enterprise reported within the enterprise funds. The Fund is created in the Department of Insurance (the Department) and is administered by the State Fire and Rescue Commission (the Commission) through a service contract with a third-party administrator. In accordance with Chapter 58, Article 87, of the General Statutes, the purpose of the Program is to provide workers’ compensation benefits to members of “eligible units,” which consist of volunteer fire departments or volunteer rescue/EMS units that are not part of a unit of local government and are exempt from State income tax under G.S. 105-130.11. These eligible units are not part of the reporting entity. Benefits are payable for compensable injuries or deaths which occurred on or after July 1, 1996. The Fund is financed by appropriations made to the Department for this purpose and by per capita fixed dollar amounts for each member of a participating eligible unit’s roster. The per capita fixed dollar amount is set annually by the Commission and is paid by the eligible units to the Commission on or before July 1 of each year for credit to the Fund. If payment is not received by July 1, the eligible unit shall not receive workers’ compensation coverage for that fiscal year. The appropriation for the fiscal year ended June 30, 2006 was $2 million. As of June 30, 2006, the Fund consisted of 1,239 eligible units representing approximately 43,027 members.

The liability for unpaid claims is based on an actuarial determination and represents a reasonable estimate of the ultimate cost of open claims and claim settlement expenses that are unpaid as of the fiscal year end, including incurred but not reported losses. The liability for unpaid claims is continually reviewed, and as adjustments become necessary such adjustments are included in current operations. The Program considers anticipated investment income in determining if a premium deficiency exists. The Program recognizes subrogation from third parties as a reduction to claim and claim settlement expenses incurred. As of June 30, 2006, there was no reduction for subrogation.

Acquisition costs consist of commission payments to independent insurance agents for marketing, promotional and administrative assistance with policy maintenance to eligible units. As coverage is renewed annually, acquisition costs are not amortized.

The Program maintains both specific excess of loss and aggregate reinsurance coverage. The specific excess of loss coverage provides for statutory limits above the Program’s retention of $500,000 per occurrence and a $1.5 million limit for employer’s liability above the Program’s retention of $500,000 per occurrence. Incurred losses are reduced by estimated amounts recoverable under the Program’s excess of loss and aggregate reinsurance policies. As of June 30, 2006, there are claims recoverable from reinsurers in the amount of $816,219.67.

The following schedule shows the changes in the reported liability for the past two fiscal years (dollars in thousands):

<table>
<thead>
<tr>
<th>Year</th>
<th>Beginning of Fiscal Year Liability</th>
<th>Current-Year Claims and Changes in Estimates</th>
<th>Claim Payments</th>
<th>Balance at Fiscal Year-End</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004-05</td>
<td>$9,786</td>
<td>$5,594</td>
<td>$(5,266)</td>
<td>$10,114</td>
</tr>
<tr>
<td>2005-06</td>
<td>10,114</td>
<td>6,715</td>
<td>$(5,656)</td>
<td>11,173</td>
</tr>
</tbody>
</table>

7. Health Insurance Program for Children

The Health Insurance Program for Children (the Program) is an insurance enterprise reported within the general fund. The Program was created by Chapter 108A, Article 2, Part 8, of the General Statutes to provide comprehensive health insurance coverage to uninsured low-income children who are residents of this State, including coverage for dental, hearing, and vision services and supplies.

Coverage is provided from federal funds received, State funds appropriated, and other nonappropriated funds made available for this purpose. All appropriations, allocations, premium receipts, or any other receipts, including earnings on investments, occurring or arising in connection with acute medical care benefits provided under the Program are deposited into the Child Health Insurance Fund (the Fund). Disbursements from the Fund include any and all amounts required to pay the benefits and administrative costs of the Program. For the fiscal year ended June 30, 2006, $68.16 million was appropriated from the General Fund to the North Carolina Department of Health and Human Services (DHHS) to be used for the Program.

The Program is administered by DHHS. Eligible children may be enrolled by the Division of Social Services based on the availability of funds. The North Carolina Teachers’ and State Employees’ Comprehensive Major Medical Plan (The Plan) is responsible for the administration and processing of claims for benefits under the Program, as provided under Chapter 135, Article 3, Part 5 of the General Statutes. The Plan’s self-insured indemnity program shall not incur any financial obligations for the program in excess of the amount of funds that the Plan’s self-insured indemnity program receives for the program.
Annual enrollment fees, co-payments, or other cost-sharing charges are determined by family income. However, there are no enrollment fees, deductibles, co-payments, or other cost-sharing charges for families covered under the Program whose family income is at or below 150% of the federal poverty level. A family’s total annual aggregate cost-sharing charges shall not exceed five percent of the family’s income for the year involved. The program had an enrollment of 109,466 children as of June 30, 2006, and an average enrollment of 118,965 children insured during the year.

Claim liabilities are based on estimates of the ultimate cost of claims that have been incurred (both reported and unreported). The following schedule shows the changes in the claims liability for the Program’s past two years of operation (dollars in thousands):

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Beginning Liability</th>
<th>Current-Year Claims and Changes in Estimates</th>
<th>Current-Year Claim Payments</th>
<th>Balance at Fiscal Year-End</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004-05</td>
<td>$22,354</td>
<td>$250,719</td>
<td>$(240,700)</td>
<td>$32,353</td>
</tr>
<tr>
<td>2005-06</td>
<td>32,353</td>
<td>223,718</td>
<td>(235,070)</td>
<td>21,001</td>
</tr>
</tbody>
</table>
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### Note 15: Individual Plan Financial Statements – Pension and Other Employee Benefit Trust Funds

Financial statements for Pension and Other Employee Benefit Trust Funds as of and for the fiscal year ended June 30, 2006 are presented below.

### Combining Statement of Plan Net Assets

**June 30, 2006**

(\text{Dollars in Thousands})

<table>
<thead>
<tr>
<th></th>
<th>Teachers' and State Employees' Retirement System</th>
<th>Consolidated Judicial Retirement System</th>
<th>Legislative Retirement System</th>
<th>Firemen's and Squad Rescue Workers' Pension Fund</th>
<th>North Carolina National Guard Pension Fund</th>
<th>Local Governmental Employees' Retirement System</th>
<th>401(k) Supplemental Retirement Income Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$54,258</td>
<td>$1,851</td>
<td>$115</td>
<td>$1,119</td>
<td>$1,437</td>
<td>$24,177</td>
<td>$13</td>
</tr>
<tr>
<td>Investments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Annuity contracts</td>
<td>887,710</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mutual funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Treasurer investment pool</td>
<td>51,734,288</td>
<td>401,294</td>
<td>30,066</td>
<td>301,675</td>
<td>61,963</td>
<td>15,294,646</td>
<td></td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>10,305,034</td>
<td>81,093</td>
<td>6,052</td>
<td>60,804</td>
<td>13,512</td>
<td>3,056,583</td>
<td></td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>2,687</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intergovernmental receivable</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest receivable</td>
<td>651</td>
<td>9</td>
<td>8</td>
<td>5</td>
<td>184</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions receivable</td>
<td>47,079</td>
<td></td>
<td>21</td>
<td></td>
<td>34,758</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Due from other funds</td>
<td>18,328</td>
<td>834</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Notes receivable</td>
<td>159,644</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets-depreciable, net</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>$62,162,325</td>
<td>$485,081</td>
<td>$36,254</td>
<td>$363,606</td>
<td>$76,917</td>
<td>$18,411,761</td>
<td>$3,486,630</td>
</tr>
</tbody>
</table>

|                      |                                                |                                        |                                 |                                               |                                             |                                             |                                           |
| **Liabilities**      |                                                 |                                        |                                 |                                               |                                             |                                             |                                           |
| Accounts payable and accrued liabilities: |                                 |                                        |                                 |                                               |                                             |                                             |                                           |
| Accounts payable     |                                                |                                        |                                 | 3                                             |                                             |                                              |                                           |
| Benefits payable     | 6,037                                           |                                        |                                 | 11                                            | 370                                         |                                              |                                           |
| Medical claims payable |                                                |                                        |                                 |                                               |                                             |                                              |                                           |
| Obligations under securities lending | 10,305,034                                     | 81,093                                 | 6,052                           | 60,804                                        | 13,512                                      | 3,056,583                                  |                                           |
| Due to other funds   | 10,311,071                                      | 81,093                                 | 6,052                           | 60,807                                        | 13,523                                      | 3,056,953                                  |                                           |
| Unearned revenue     |                                                |                                        |                                 |                                               |                                             |                                              |                                           |
| Compensated absences |                                                |                                        |                                 |                                               |                                             |                                              |                                           |
| **Total Liabilities**| $10,311,071                                     | $81,093                                | $6,052                           | $60,807                                       | $13,523                                     | $3,056,953                                  |                                           |

|                      |                                                |                                        |                                 |                                               |                                             |                                             |                                           |
| **Net Assets**       |                                                 |                                        |                                 |                                               |                                             |                                             |                                           |
| Held in trust for:   |                                                |                                        |                                 |                                               |                                             |                                             |                                           |
| Employees' pension and other benefits | 51,851,254                                     | 403,988                                | 39,202                          | 302,799                                       | 63,394                                      | 15,354,808                                 | $3,486,630                               |
| **Total Net Assets** | $51,851,254                                    | $403,988                               | $39,202                         | $302,799                                      | $63,394                                     | $15,354,808                                | $3,486,630                               |

A schedule of funding progress for each defined benefit plan is presented on page 160.
## NOTES TO THE FINANCIAL STATEMENTS

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 2,622</td>
<td>$ 8,441</td>
<td>$ 245,995</td>
<td>$ 136,957</td>
<td>$ 8,989</td>
<td>$ 1,378</td>
<td>$ 475</td>
<td>$ 487,027</td>
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<tr>
<td>36,157</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td>923,867</td>
</tr>
<tr>
<td>619,213</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3,056,476</td>
</tr>
<tr>
<td></td>
<td>233,499</td>
<td></td>
<td>249,671</td>
<td></td>
<td></td>
<td></td>
<td>27,370  68,334,472</td>
</tr>
<tr>
<td></td>
<td>137,925</td>
<td>191,486</td>
<td>117,477</td>
<td>147,463</td>
<td>1,182</td>
<td></td>
<td>15,723  14,134,334</td>
</tr>
<tr>
<td>4,741</td>
<td>46</td>
<td>17,293</td>
<td>9,222</td>
<td></td>
<td></td>
<td></td>
<td>35,402</td>
</tr>
<tr>
<td></td>
<td></td>
<td>13,050</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>13,050</td>
</tr>
<tr>
<td></td>
<td>28</td>
<td>926</td>
<td>425</td>
<td>35</td>
<td>4</td>
<td>1</td>
<td>2,278</td>
</tr>
<tr>
<td>1,658</td>
<td>1,170</td>
<td></td>
<td>24,748</td>
<td>3,386</td>
<td></td>
<td>313</td>
<td>113,133</td>
</tr>
<tr>
<td></td>
<td>352</td>
<td></td>
<td>8,995</td>
<td>1,208</td>
<td></td>
<td></td>
<td>29,717</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>159,644</td>
</tr>
<tr>
<td></td>
<td></td>
<td>29</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>29</td>
</tr>
<tr>
<td>664,391</td>
<td>381,461</td>
<td>468,781</td>
<td>288,602</td>
<td>419,974</td>
<td>2,564</td>
<td>43,882</td>
<td>87,292,229</td>
</tr>
</tbody>
</table>

| 180                        | 158                       | 8,644                     |                             |                               |                       |                           | 8,985   |
|                            | 2,747                     |                           |                             | 319,243                       |                       |                           | 328,408 |
|                            | 170,465                   |                           |                             |                               |                       |                           | 170,465 |
|                            | 137,925                   | 191,486                   | 117,477                     | 147,463                       | 1,182                 | 15,723                    | 14,134,334 |
|                            | 28                        |                           |                             |                               |                       |                           | 28      |
|                            | 6,312                     |                           |                             |                               |                       |                           | 6,312   |
|                            | 119                       |                           |                             |                               |                       |                           | 119     |
| 180                        | 140,830                   | 377,054                   | 117,477                     | 466,706                       | 1,182                 | 15,723                    | 14,648,651 |

| 664,211                    | 240,631                   | 91,727                    | 171,125                     | (46,732)                      | 1,382                 | 28,159                    | 72,643,578 |
| 664,211                    | 240,631                   | 91,727                    | 171,125                     | (46,732)                      | 1,382                 | 28,159                    | 72,643,578 |
## COMBINING STATEMENT OF CHANGES IN PLAN NET ASSETS

For the Fiscal Year Ended June 30, 2006  
(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Teachers' and State Employees' Retirement System</th>
<th>Consolidated Judicial Retirement System</th>
<th>Legislative Retirement System</th>
<th>Firemen's and Rescue Squad Workers' Pension Fund</th>
<th>North Carolina National Guard Pension Fund</th>
<th>Local Governmental Employees' Retirement System</th>
<th>401(k) Supplemental Retirement Income Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Additions:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employer</td>
<td>$ 315,225</td>
<td>$ 6,989</td>
<td>$ —</td>
<td>$ —</td>
<td>$ 229,399</td>
<td>$ 125,876</td>
<td></td>
</tr>
<tr>
<td>Members</td>
<td>720,014</td>
<td>3,661</td>
<td>256</td>
<td>2,670</td>
<td>—</td>
<td>280,700</td>
<td>221,539</td>
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<tr>
<td>Other contributions</td>
<td>—</td>
<td>—</td>
<td>7,926</td>
<td>6,042</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total contributions</strong></td>
<td><strong>1,035,239</strong></td>
<td><strong>10,650</strong></td>
<td><strong>256</strong></td>
<td><strong>10,599</strong></td>
<td><strong>6,042</strong></td>
<td><strong>510,099</strong></td>
<td><strong>347,415</strong></td>
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<tr>
<td><strong>Investment Income:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment earnings (loss)</td>
<td>4,085,328</td>
<td>31,745</td>
<td>2,407</td>
<td>23,795</td>
<td>4,792</td>
<td>1,191,974</td>
<td>226,795</td>
</tr>
<tr>
<td>Less investment expenses</td>
<td>(512,843)</td>
<td>(4,020)</td>
<td>(304)</td>
<td>(3,039)</td>
<td>(639)</td>
<td>(150,114)</td>
<td>—</td>
</tr>
<tr>
<td><strong>Net investment income (loss)</strong></td>
<td><strong>3,572,485</strong></td>
<td><strong>27,725</strong></td>
<td><strong>2,103</strong></td>
<td><strong>20,756</strong></td>
<td><strong>4,154</strong></td>
<td><strong>1,041,860</strong></td>
<td><strong>226,795</strong></td>
</tr>
<tr>
<td><strong>Other additions:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fees, licenses and fires</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Interest earnings on loans</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>1,881</td>
<td>—</td>
<td>—</td>
<td>(2)</td>
<td>—</td>
<td>19</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total other additions</strong></td>
<td><strong>1,881</strong></td>
<td><strong>—</strong></td>
<td><strong>—</strong></td>
<td><strong>(2)</strong></td>
<td><strong>—</strong></td>
<td><strong>19</strong></td>
<td><strong>—</strong></td>
</tr>
<tr>
<td><strong>Total additions</strong></td>
<td><strong>4,609,605</strong></td>
<td><strong>38,375</strong></td>
<td><strong>2,359</strong></td>
<td><strong>31,359</strong></td>
<td><strong>10,196</strong></td>
<td><strong>1,556,771</strong></td>
<td><strong>592,122</strong></td>
</tr>
<tr>
<td><strong>Deductions:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Claims and benefits</td>
<td>2,536,588</td>
<td>22,253</td>
<td>1,693</td>
<td>18,972</td>
<td>3,806</td>
<td>584,336</td>
<td>166,661</td>
</tr>
<tr>
<td>Medical insurance premiums for retirees</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Refund of contributions</td>
<td>82,072</td>
<td>32</td>
<td>25</td>
<td>618</td>
<td>—</td>
<td>59,516</td>
<td>—</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>7,300</td>
<td>32</td>
<td>6</td>
<td>590</td>
<td>42</td>
<td>2,758</td>
<td>1,054</td>
</tr>
<tr>
<td>Other deductions</td>
<td>1</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total deductions</strong></td>
<td><strong>2,625,961</strong></td>
<td><strong>22,317</strong></td>
<td><strong>1,724</strong></td>
<td><strong>20,160</strong></td>
<td><strong>3,848</strong></td>
<td><strong>646,610</strong></td>
<td><strong>167,715</strong></td>
</tr>
<tr>
<td>Change in net assets</td>
<td>1,983,644</td>
<td>16,058</td>
<td>635</td>
<td>11,179</td>
<td>6,348</td>
<td>910,151</td>
<td>414,407</td>
</tr>
<tr>
<td>Net assets — July 1</td>
<td>49,867,610</td>
<td>387,930</td>
<td>29,567</td>
<td>291,620</td>
<td>57,046</td>
<td>14,444,647</td>
<td>3,072,223</td>
</tr>
<tr>
<td>Net assets — June 30</td>
<td><strong>$ 51,851,254</strong></td>
<td><strong>$ 403,988</strong></td>
<td><strong>$ 30,202</strong></td>
<td><strong>$ 302,799</strong></td>
<td><strong>$ 63,394</strong></td>
<td><strong>$ 15,354,808</strong></td>
<td><strong>$ 3,486,630</strong></td>
</tr>
</tbody>
</table>
## State of North Carolina

### NOTES TO THE FINANCIAL STATEMENTS

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>$</td>
<td>$21,455</td>
<td>$1,588,639</td>
<td>$476,761</td>
<td>$65,009</td>
<td>$1,237</td>
<td>$3,219</td>
<td>$2,833,809</td>
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<td>45,039</td>
<td>310,298</td>
<td>9,704</td>
<td>23,727</td>
<td></td>
<td></td>
<td></td>
<td>1,584,177</td>
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<tr>
<td>—</td>
<td>45,039</td>
<td>31,159</td>
<td>1,922,664</td>
<td>476,761</td>
<td>65,009</td>
<td>1,237</td>
<td>3,219</td>
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<td>40,096</td>
<td>(601)</td>
<td>20,069</td>
<td>6,771</td>
<td>(422)</td>
<td>79</td>
<td>(88)</td>
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<td>—</td>
<td>(5,379)</td>
<td>(10,086)</td>
<td>(3,403)</td>
<td>(5,838)</td>
<td>(40)</td>
<td>(597)</td>
<td>(896,292)</td>
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<tr>
<td>40,096</td>
<td>(5,960)</td>
<td>9,983</td>
<td>3,368</td>
<td>(6,260)</td>
<td>39</td>
<td>(685)</td>
<td>4,936,448</td>
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<tr>
<td>—</td>
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<td>—</td>
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<td>—</td>
<td>—</td>
<td>4,793</td>
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<td>—</td>
<td>—</td>
<td>7,912</td>
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<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,898</td>
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<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>85,135</td>
<td>25,179</td>
<td>1,932,647</td>
<td>480,129</td>
<td>58,749</td>
<td>1,276</td>
<td>2,534</td>
<td>9,416,436</td>
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<td>41,023</td>
<td>26,412</td>
<td>1,698,407</td>
<td>—</td>
<td>87,884</td>
<td>785</td>
<td>844</td>
<td>5,189,664</td>
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<td>—</td>
<td>—</td>
<td>411,760</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>411,760</td>
<td>—</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>142,263</td>
<td>—</td>
</tr>
<tr>
<td>1,989</td>
<td>568</td>
<td>81,951</td>
<td>—</td>
<td>457</td>
<td>—</td>
<td>18</td>
<td>96,765</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>43,012</td>
<td>26,980</td>
<td>1,780,443</td>
<td>411,760</td>
<td>88,341</td>
<td>872</td>
<td>862</td>
<td>5,840,025</td>
</tr>
<tr>
<td>42,123</td>
<td>(1,801)</td>
<td>152,204</td>
<td>68,369</td>
<td>(29,592)</td>
<td>404</td>
<td>1,672</td>
<td>3,575,811</td>
</tr>
<tr>
<td>622,088</td>
<td>242,432</td>
<td>(60,477)</td>
<td>102,756</td>
<td>(17,140)</td>
<td>978</td>
<td>26,487</td>
<td>69,067,767</td>
</tr>
<tr>
<td>$664,211</td>
<td>$240,631</td>
<td>$91,727</td>
<td>$171,125</td>
<td>$46,732</td>
<td>$1,382</td>
<td>$28,159</td>
<td>$72,643,578</td>
</tr>
</tbody>
</table>
NOTE 16: SEGMENT INFORMATION

Primary Government. The Town of Butner water and sewer system is administered by the North Carolina Department of Health and Human Services. The State issued revenue bonds to finance upgrades to the Town’s water treatment plant, wastewater plant, sanitary sewer system, and water distribution system. This system provides water and sewer services to the State facilities in the Town of Butner as well as to other customers in southern Granville County.

Component Unit. The North Carolina Housing Finance Agency’s Home Ownership Bond Programs and Rental Bond Programs are initially funded with revenue bond proceeds. These proceeds are used to purchase single family home and rental property mortgage loans which provide the income along with investment earnings to repay the debt.

Condensed financial statements for the Town of Butner water and sewer system and the two segments of the North Carolina Housing Finance Agency as of and for the fiscal year ended June 30, 2006 are presented below (dollars in thousands).

<table>
<thead>
<tr>
<th>Town of Butner Water and Sewer</th>
<th>N.C. Housing Finance Agency</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets:</strong></td>
<td></td>
</tr>
<tr>
<td>Current assets...</td>
<td>$ 8,876</td>
</tr>
<tr>
<td>Capital assets-nondepreciable...</td>
<td>1,795</td>
</tr>
<tr>
<td>Capital assets-depreciable, net..</td>
<td>24,275</td>
</tr>
<tr>
<td>Other assets...</td>
<td>1,734</td>
</tr>
<tr>
<td>Total assets...</td>
<td>36,680</td>
</tr>
<tr>
<td><strong>Liabilities:</strong></td>
<td></td>
</tr>
<tr>
<td>Current liabilities...</td>
<td>4,614</td>
</tr>
<tr>
<td>Noncurrent liabilities...</td>
<td>9,893</td>
</tr>
<tr>
<td>Total liabilities...</td>
<td>14,507</td>
</tr>
<tr>
<td><strong>Net assets:</strong></td>
<td></td>
</tr>
<tr>
<td>Invested in capital assets, net of related debt</td>
<td>$17,237</td>
</tr>
<tr>
<td>Restricted...</td>
<td>—</td>
</tr>
<tr>
<td>Unrestricted...</td>
<td>4,936</td>
</tr>
<tr>
<td>Total net assets...</td>
<td>$22,173</td>
</tr>
</tbody>
</table>

Condensed Statement of Revenues, Expenses, and Changes in Net Assets

<table>
<thead>
<tr>
<th>Town of Butner Water and Sewer</th>
<th>N.C. Housing Finance Agency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating revenues (pledged against bonds)...</td>
<td>$2,400</td>
</tr>
<tr>
<td>Depreciation expense...</td>
<td>$ (1,662)</td>
</tr>
<tr>
<td>Other operating expenses...</td>
<td>$ (2,281)</td>
</tr>
<tr>
<td>Operating income...</td>
<td>$ (1,523)</td>
</tr>
<tr>
<td>Nonoperating revenues (expenses):</td>
<td></td>
</tr>
<tr>
<td>Investment earnings...</td>
<td>$312</td>
</tr>
<tr>
<td>Interest expense...</td>
<td>$ (433)</td>
</tr>
<tr>
<td>Other nonoperating revenues (expenses)...</td>
<td>$ (132)</td>
</tr>
<tr>
<td>Transfers out...</td>
<td>$ (238)</td>
</tr>
<tr>
<td>Change in net assets...</td>
<td>$ (2,014)</td>
</tr>
<tr>
<td>Net assets — July 1, as restated.</td>
<td>$24,187</td>
</tr>
<tr>
<td>Net assets — June 30...</td>
<td>$22,173</td>
</tr>
</tbody>
</table>

Condensed Statement of Cash Flows

<table>
<thead>
<tr>
<th>Town of Butner Water and Sewer</th>
<th>N.C. Housing Finance Agency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net cash provided (used) by:</td>
<td></td>
</tr>
<tr>
<td>Operating activities...</td>
<td>$275</td>
</tr>
<tr>
<td>Noncapital financing activities.</td>
<td>$(238)</td>
</tr>
<tr>
<td>Capital and related financing activities...</td>
<td>$(1,130)</td>
</tr>
<tr>
<td>Investing activities...</td>
<td>$158</td>
</tr>
<tr>
<td>Net increase (decrease)...</td>
<td>$(935)</td>
</tr>
<tr>
<td>Cash and cash equivalents at July 1...</td>
<td>$7,338</td>
</tr>
<tr>
<td>Cash and cash equivalents at June 30...</td>
<td>$6,403</td>
</tr>
</tbody>
</table>
# NOTE 17: COMPONENT UNITS — FINANCIAL INFORMATION

The financial statements for the University of North Carolina System and Community Colleges include their nongovernmental component unit foundations and similarly affiliated organizations. Financial statements for component units as of and for the fiscal year ended June 30, 2006 are presented below (dollars in thousands).

<table>
<thead>
<tr>
<th>Statement of Net Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td><strong>University of North Carolina</strong></td>
</tr>
<tr>
<td>LEAF, Inc.</td>
</tr>
<tr>
<td>$568</td>
</tr>
<tr>
<td><strong>Investments</strong></td>
</tr>
<tr>
<td><strong>Receivables, net</strong></td>
</tr>
<tr>
<td><strong>Due from component units</strong></td>
</tr>
<tr>
<td><strong>Due from primary government</strong></td>
</tr>
<tr>
<td><strong>Inventory</strong></td>
</tr>
<tr>
<td><strong>Prepaid items</strong></td>
</tr>
<tr>
<td><strong>Notes receivable, net</strong></td>
</tr>
<tr>
<td><strong>Endowment investments</strong></td>
</tr>
<tr>
<td><strong>Investment in joint venture</strong></td>
</tr>
<tr>
<td><strong>Deferred charges</strong></td>
</tr>
<tr>
<td><strong>Capital assets-nondepreciable</strong></td>
</tr>
<tr>
<td><strong>Capital assets-depreciable, net</strong></td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
</tr>
<tr>
<td><strong>Accounts payable and accrued liabilities</strong></td>
</tr>
<tr>
<td><strong>Medical claims payable</strong></td>
</tr>
<tr>
<td><strong>Interest payable</strong></td>
</tr>
<tr>
<td><strong>Short-term debt</strong></td>
</tr>
<tr>
<td><strong>Due to component units</strong></td>
</tr>
<tr>
<td><strong>Due to primary government</strong></td>
</tr>
<tr>
<td><strong>Unearned revenue</strong></td>
</tr>
<tr>
<td><strong>Advance from primary government</strong></td>
</tr>
<tr>
<td><strong>Obligations under reverse repurchase agreements</strong></td>
</tr>
<tr>
<td><strong>Deposits payable</strong></td>
</tr>
<tr>
<td><strong>Funds held for others</strong></td>
</tr>
<tr>
<td><strong>Due within one year</strong></td>
</tr>
<tr>
<td><strong>Due in more than one year</strong></td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
</tr>
<tr>
<td><strong>Net Assets</strong></td>
</tr>
<tr>
<td><strong>Invested in capital assets, net of related debt</strong></td>
</tr>
<tr>
<td><strong>Restricted for:</strong></td>
</tr>
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<td><strong>Nonexpendable:</strong></td>
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<td>Expendable:</td>
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<td>Higher education</td>
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<tr>
<td>Health and human services</td>
</tr>
<tr>
<td>Economic development</td>
</tr>
<tr>
<td>Other purposes</td>
</tr>
<tr>
<td><strong>Unrestricted</strong></td>
</tr>
<tr>
<td><strong>Total Net Assets</strong></td>
</tr>
</tbody>
</table>

$ 510,655 $ 9,801,715 $ 1,804,351 $ 396,270 $ 559,827 $ 318,362 $ 13,191,180
### Notes to the Financial Statements

#### Statement of Activities

<table>
<thead>
<tr>
<th></th>
<th>University of North Carolina</th>
<th>N.C. State Housing Authority</th>
<th>N.C. State Education Assistance Agency</th>
<th>Other Component</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The Golden LEAF, Inc.</td>
<td>Carolina System</td>
<td>Community Colleges</td>
<td>Agency</td>
</tr>
<tr>
<td>Total expenses</td>
<td>$28,773</td>
<td>$6,550,114</td>
<td>$1,502,874</td>
<td>$251,870</td>
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<td></td>
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<td>$249,312</td>
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<td>$195,104</td>
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<tr>
<td></td>
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<td></td>
<td></td>
<td>$8,878,047</td>
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<tr>
<td>Program revenues:</td>
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<td>Charges for services</td>
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<td>3,903,683</td>
<td>242,164</td>
<td>244,456</td>
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<td></td>
<td>154,206</td>
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<tr>
<td>Operating grants and contributions</td>
<td>48,444</td>
<td>929,272</td>
<td>452,649</td>
<td>32,068</td>
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<td></td>
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<td>38,717</td>
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<td></td>
<td>20,344</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,521,494</td>
</tr>
<tr>
<td>Capital grants and contributions</td>
<td>32,747</td>
<td>60,971</td>
<td>715</td>
<td></td>
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<tr>
<td>Net program (expense) revenue</td>
<td>19,676</td>
<td>(1,784,432)</td>
<td>(747,090)</td>
<td>24,684</td>
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<td></td>
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<td></td>
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<td>(56,389)</td>
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<td>(117,343)</td>
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<td></td>
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<td></td>
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<td>(2,860,914)</td>
</tr>
<tr>
<td>Non-tax general revenues:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State operating aid</td>
<td>68,227</td>
<td>2,131,110</td>
<td>728,340</td>
<td>10,451</td>
</tr>
<tr>
<td>State capital aid</td>
<td></td>
<td>399,737</td>
<td>68,000</td>
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</tr>
<tr>
<td>Miscellaneous</td>
<td>5,430</td>
<td>112</td>
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<tr>
<td>Total non-tax general revenues</td>
<td>68,227</td>
<td>2,535,277</td>
<td>796,452</td>
<td>10,451</td>
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<tr>
<td>Contributions to endowments</td>
<td></td>
<td>103,206</td>
<td>6,541</td>
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<tr>
<td>Change in net assets</td>
<td>87,903</td>
<td>854,051</td>
<td>55,903</td>
<td>35,115</td>
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<td>Net assets — July 1, as restated</td>
<td>422,752</td>
<td>8,747,684</td>
<td>1,748,448</td>
<td>361,155</td>
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<td>546,471</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>283,247</td>
</tr>
<tr>
<td>Net assets — June 30</td>
<td>$510,655</td>
<td>$9,601,715</td>
<td>$1,804,351</td>
<td>$396,270</td>
</tr>
<tr>
<td></td>
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<td></td>
<td>$559,827</td>
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<td>$318,362</td>
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<td>$13,191,180</td>
</tr>
</tbody>
</table>

#### Significant Balances and Transactions Between Component Units

<table>
<thead>
<tr>
<th></th>
<th>University of North Carolina</th>
<th>N.C. State Housing Authority</th>
<th>N.C. State Education Authority</th>
<th>Other Component</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The Golden LEAF, Inc.</td>
<td>Carolina System</td>
<td>Community Colleges</td>
<td>Agency</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Due from (due to) component units</td>
<td>($58,817)</td>
<td>52,303</td>
<td>4,829</td>
<td>1,510</td>
</tr>
<tr>
<td>Grant revenue (expense)</td>
<td>($8,712)</td>
<td>4,430</td>
<td>2,725</td>
<td>1,500</td>
</tr>
<tr>
<td>UNC System operating aid</td>
<td></td>
<td>(9,176)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Advances To Component Units/Advances From Primary Government

The balance of $21.742 million advanced to the N.C. Global TransPark Authority from the Escheats Fund (a special revenue fund) resulted from a $25 million advance for the purposes of the acquisition of real property in prior fiscal years. The advance is due on October 1, 2007, and will be repaid with interest at a variable rate based upon the earnings record of the Treasurer’s Long-Term Investment Fund. The balance of $3.622 million advanced to the North Carolina Turnpike Authority from the Highway Trust Fund is related to startup operating costs.

#### Intra-Entity Balances — Between Primary Government and Component Units

<table>
<thead>
<tr>
<th>Due From Component Units</th>
<th>Due From Primary Government</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>University of North Carolina</td>
</tr>
<tr>
<td></td>
<td>State</td>
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<tr>
<td></td>
<td>General Fund</td>
</tr>
<tr>
<td>Due To Component Units:</td>
<td></td>
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<tr>
<td>General Fund</td>
<td>$——</td>
</tr>
<tr>
<td>Other Governmental Funds</td>
<td>—</td>
</tr>
<tr>
<td>Due To Primary Government:</td>
<td></td>
</tr>
<tr>
<td>The Golden LEAF, Inc.</td>
<td>1,153</td>
</tr>
<tr>
<td>University of North Carolina System</td>
<td>—</td>
</tr>
<tr>
<td>Community Colleges</td>
<td>—</td>
</tr>
<tr>
<td>Other Component Units</td>
<td>1,285</td>
</tr>
<tr>
<td>Total</td>
<td>$2,438</td>
</tr>
</tbody>
</table>
NOTE 18: RELATED ORGANIZATIONS

MCNC
MCNC (formerly the Microelectronics Center of North Carolina) is a legally separate non-profit corporation fostering the advancement of education, innovation and economic development throughout North Carolina by providing high quality network infrastructure and network-based services. It is managed by a Board of Directors ranging from thirteen to twenty members. Six of the members are appointed by the Governor. Another seven members serve ex officio as follows: four are chancellors of universities in the UNC System, a component unit of the State; one is the president of MCNC; one is designated by the Board of Trustees of Duke University; and one is designated by the Board of Governors of the Research Triangle Institute. These Governor-appointed members and ex officio members may elect up to seven other board members. Any appointed director may be removed from office by the Governor for cause. Any elected director may be removed by the Board of Directors at will.

Centennial Authority
The Centennial Authority is a legally separate organization established to study, design, plan, construct, own, promote, finance, and operate a regional facility in Wake County, North Carolina, now known as the RBC Center. The RBC Center houses entertainment shows and is home to two sports teams, the National Hockey League’s Carolina Hurricanes and North Carolina State University men’s basketball. The Authority is governed by a twenty-one member board comprised of ten members appointed by the General Assembly, four members appointed by the Wake County Board of Commissioners, four members appointed by the Raleigh City Council, two members appointed jointly by the mayors of all the cities in Wake County, and the chancellor of North Carolina State University (or the Chancellor’s designee). A member may be removed by the appointing authority for cause.

North Carolina Capital Facilities Finance Agency
The North Carolina Capital Facilities Finance Agency provides the benefits of tax-exempt financing to non-profit institutions providing elementary and secondary education, private institutions of higher education, and various other entities for special purpose projects serving a public interest (see Note 20). The agency is governed by a seven member board comprised of two members appointed by the General Assembly, three members appointed by the Governor, and the State Treasurer and the State Auditor, both of whom serve ex officio.
NOTE 19: RELATED PARTY TRANSACTIONS

Primary Government

Supplemental Retirement Income Plan of North Carolina
Included in Plan assets is a stable value fund sponsored by the contractor, Prudential Retirement Services. Investment earnings in the Prudential Stable Value Fund amounted to approximately $33.5 million in 2005. The asset values of this fund are disclosed in Note 3.

North Carolina Public Employee Deferred Compensation Plan
Under the terms of an agreement effective January 1, 2004, the Plan’s Board of Trustees appointed Great-West Life & Annuity Insurance Company (Great-West), as the Plan’s third-party administrator. The Plan recognized $1.95 million in expenses related to Great-West for the year ended December 31, 2005. The portion of annuity payout contract assets attributable to contracts with Great-West at December 31, 2005 was $27.41 million.

Component Units

University of North Carolina System and Community College Foundations
The University of North Carolina (UNC) System and community colleges have separately incorporated not-for-profit foundations that are associated with constituent institutions of the UNC System or individual colleges. These organizations serve as a fundraising arm of the respective institutions through which individuals, corporations, and other organizations support institution programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific departments and the institution’s overall academic environment. These affiliated organizations are not included as component units since the economic resources received or held by an individual organization are not significant to the primary government. Therefore, the financial statements of the UNC System and community colleges do not include the assets, liabilities, net assets, or operational transactions of these foundations, except for support from each organization to constituent institutions or colleges. For the fiscal year ended June 30, 2006, this support approximated $47.23 million for the UNC System and $61 thousand for community colleges.

Related Organization

Centennial Authority
The Centennial Authority (Authority), a related organization of the State of North Carolina, was created by the 1995 General Assembly for the purpose of studying, designing, planning, constructing, owning, promoting, financing and operating a regional facility on land owned by the State. Prior to this act, the General Assembly authorized the construction by North Carolina State University (the University) of a facility to be known as the “Entertainment and Sports Arena” (ESA). This facility serves as a regional sports entertainment center and is available for cultural performances, sporting events and other activities of the University or of other entities (the Centennial Center project). With the 1995 legislation, the Centennial Center project was transferred to the Authority.

The Authority entered into a ground lease with the State of North Carolina to lease land for the ESA for a period of 99 years at an annual rent of $1. The University entered into a use agreement with the Authority. Both parties agreed that the University shall be the primary and preferred user of all areas of the ESA. The University is required to pay the greater of 10% of gross ticket revenues or $44 thousand for each men’s and $19 thousand for each women’s basketball game to compensate the Authority for facility rental and operating expenses. Rent and expense payments for miscellaneous events are negotiated on an event by event basis based on the availability of the ESA and the anticipated attendance.

In fiscal year 2003 a naming rights agreement was executed to change the name of the ESA to the “RBC Center.” As a result of this agreement, the University will receive $13.18 million over a ten-year period which began in 2003.
NOTE 20: COMMITMENTS AND CONTINGENCIES

A. No Commitment Debt

The State, by action of the General Assembly, created the North Carolina Medical Care Commission which is authorized to issue tax-exempt bonds and notes to finance construction and equipment projects for nonprofit and public hospitals, nursing homes, continuing care facilities for the elderly and related facilities. The bonds are not an indebtedness of the State and, accordingly, are not reflected in the accompanying financial statements. Each issue is payable solely from the revenues of the facility financed by that issue and any other credit support provided. Therefore, each issue is separately secured and is separate and independent from all other issues as to source of payment and security. The indebtedness of each entity is serviced and administered by a trustee independent of the State. Maturing serially to calendar year 2041, the outstanding principal of such bonds and notes as of June 30, 2006, was $5.9 billion with interest rates varying from 1.6% to 7.57%.

The North Carolina Capital Facilities Finance Agency is authorized by the State to issue tax-exempt bonds and notes to finance industrial and manufacturing facilities, pollution control facilities for industry (in connection with manufacturing) where there is a favorable impact on employment or pollution control commensurate with the size and cost of the facilities and to finance facilities and structures at private nonprofit colleges and universities, and institutions providing kindergarten, elementary and secondary education. Its authority to issue bonds and notes also includes financing private sector capital improvements for activities that constitute a public purpose. The bonds are not an indebtedness of the State and, accordingly, are not reflected in the accompanying financial statements. Each issue is payable solely from the revenues of the facility financed by that issue and any other credit support provided. Therefore, each issue is separately secured and is separate and independent from all other issues as to source of payment and security. The indebtedness of each issue is serviced and administered by a trustee independent of the State. Maturing serially to calendar year 2045, the outstanding principal of such bonds and notes as of June 30, 2006, was $1.7 billion with fixed interest rates varying from 2.4% to 7.1% and variable interest rates which can be reset weekly.

B. Litigation

_Hoke County et al. v. State of North Carolina and State Board of Education — Right to a Sound Basic Education (formerly Leandro)._ In 1994, students and boards of education in five counties in the State filed suit in Superior Court requesting a declaration that the public education system of North Carolina, including its system of funding, violates the state Constitution by failing to provide adequate or substantially equal educational opportunities, by denying due process of law, and by violating various statutes relating to public education. Five other school boards and students therein intervened, alleging claims for relief on the basis of the high proportion of at-risk and high-cost students in their counties' systems.

The suit is similar to a number of suits in other states, some of which resulted in holdings that the respective systems of public education funding were unconstitutional under the applicable state law. The State filed a motion to dismiss, which was denied. On appeal, the North Carolina Supreme Court upheld the present funding system against the claim that it unlawfully discriminated against low wealth counties, but remanded the case for trial on the claim for relief based on the Court's conclusion that the constitution guarantees every child the opportunity to obtain a sound basic education. Trial on the claim of one plaintiff-county was held in the fall of 1999. On October 26, 2000 the trial court, in Section Two of a projected three-part ruling, concluded that at-risk children in North Carolina are constitutionally entitled to such pre-kindergarten educational programs as may be necessary to prepare them for higher levels of education and the “sound basic education” mandated by the Supreme Court. On March 26, 2001, the Court issued Section Three of the three-part ruling, in which the judge ordered all parties to investigate certain school systems to determine why they are succeeding without additional funding. The State filed a Notice of Appeal to the Court of Appeals, which resulted in the Court's decision to re-open the trial and call additional witnesses. That proceeding took place in the fall of 2001. On April 4, 2002, the Court entered Section Four of the ruling, ordering the State to take such actions as may be necessary to remedy the constitutional deficiency for those children who are not being provided with access to a sound basic education and to report to the Court at 90-day intervals remedial actions being implemented. On July 30, 2004, the North Carolina Supreme Court affirmed the majority of the trial court's orders, thereby directing the executive and legislative branches to take corrective action necessary to ensure that every child has the opportunity to obtain a sound, basic education. The Supreme Court did agree with the State that the trial court exceeded its authority in ordering pre-kindergarten programs for at-risk children. The State is now undertaking measures to respond to the trial court's directives. The magnitude of state resources which may ultimately be required cannot be determined at this time; however, the total cost could exceed $100 million.

_N.C. School Boards Association, et al. v. Richard H. Moore, State Treasurer, et al._ — Use of Administration Payments. On December 14, 1998, plaintiffs, including county school boards of Wake, Durham, Johnston, Buncombe, Edgecombe and Lenoir Counties, filed suit in Superior Court requesting a declaration that certain payments to state administrative agencies must be distributed to the public schools on the theory that such amounts are civil penalties which under the North Carolina Constitution must be paid to the schools.
On December 14, 2001, the Superior Court of Wake County granted summary judgment in favor of the plaintiffs on all issues, concluding that the funds in dispute are civil fines or penalties required by Article IX, Section 7 of the Constitution to be remitted to the public schools in the county where the violation occurred. The court further determined a three-year statute of limitations to be applicable, making the order retroactive to December 1995. This case was argued in the Court of Appeals in February, 2003. The North Carolina Court of Appeals rendered a decision in September 2003 substantially favorable to the State. On July 1, 2005, the Supreme Court reversed the Court of Appeals in part, concluding that a majority of the funds in dispute are civil penalties required to be paid into the Civil Penalty and Forfeiture Fund for the benefit of public schools. Based upon information supplied by the defendant state agencies, the amount owed could be as much as $770 million. The case is now pending in Superior Court while the parties discuss a negotiated resolution.

Southeast Compact Commission — Disposal of Low-level Radioactive Waste. North Carolina and seven other southeastern states created the Southeast Interstate Low-level Radioactive Waste Management Compact to plan and develop a site for the disposal of low-level radioactive waste generated in the member states. North Carolina was assigned responsibility for development of the first disposal site, with costs to be distributed equitably among the Compact members. In 1997, the Compact Commission discontinued funding of the development of the North Carolina site, alleging that the State was not actively pursuing the permitting and development of the proposed site. North Carolina withdrew from the Compact in 1999. The Compact subsequently asked the United States Supreme Court to accept its Complaint against North Carolina demanding the repayment, with interest, of $80 million of Compact payments expended on the permitting of the site, plus $10 million of future lost income, interest and attorney fees. The Supreme Court denied this motion in August 2001. On August 5, 2002 the Compact, with the addition of four member states as plaintiffs, filed a new motion requesting the United States Supreme Court to accept the claim under its original jurisdiction. On June 16, 2003, the Court accepted jurisdiction of the case and the State filed an answer and motion to dismiss on August 21, 2003. On November 17, 2003, the motion to dismiss was denied, and the U.S. Supreme Court appointed a Special Master with authority to determine when additional pleadings will be filed in the case. The Special Master heard oral arguments on dispositive motions filed by both sides on September 3, 2004 and in September, 2006 allowed the State’s motions as to several claims. The parties will continue to litigate the remaining claims.

Philip Morris USA Inc. v. Tolson — Refund of Corporate Income Tax. On June 13, 2000, Philip Morris filed a complaint in Wake County Superior Court for a refund of approximately $30 million in corporate income taxes paid for 1989 through 1991. An order of the Augmented Tax Review Board in the 1970’s allowed it to apportion its income under a modified formula, which included a more favorable property factor. When the law changed in 1989 to move to double weighting of the sales factor, Philip Morris incorporated this change into its formula. The Board’s order did not permit double weighting. Philip Morris argued that the principle of in pari materia required incorporation of the amendment, and that failure to allow double weighting violated the equal protection and separation of powers clauses. The Wake County Superior Court ruled that Philip Morris was required to use the formula approved by the Board without double weighting the sales factor unless the statutory formula (without the modified property factor) produced a more favorable result. Philip Morris appealed this ruling to the North Carolina Court of Appeals. The Court of Appeals issued a unanimous opinion affirming the superior court. Philip Morris has filed a notice of appeal and petition for discretionary review with the North Carolina Supreme Court.

State Employees Association of North Carolina v. State; Stone v. State — Diversion of Employer's Retirement System Contribution. On May 22, 2001, SEANC filed an action in Wake County Superior Court demanding repayment of approximately $129 million in employer retirement contributions to the Retirement Systems. The Governor withheld, and subsequently used, the withheld funds under his constitutional authority to balance the state budget. The trial court dismissed the action on May 23, 2001, and the North Carolina Court of Appeals affirmed this dismissal on December 3, 2002. The Supreme Court, on June 13, 2003, reversed the Court of Appeals on issues related to class standing and remanded with instructions to consider procedural issues raised but not addressed by the Court of Appeals. The Court of Appeals remanded the case to the Superior Court of Wake County without opinion and without considering any remaining issues.

In June 2002, the Stone case was filed in Wake County Superior Court on behalf of individual state employees and retirees seeking repayment of the withheld employer contribution and a prohibition against future diversions. A class comprised of all members of the Retirement System has been certified and the case is currently proceeding through class notification and toward trial. On September 6, 2006, the trial court issued an interlocutory order in response to cross-motions for summary judgment. The court’s order found the diversion of funds to be in violation of the constitution, but did not direct any repayment of funds.

Goldston v. State of North Carolina — Highway Trust Fund Transfers. On November 14, 2002, a lawsuit was filed in Wake County Superior Court demanding that $80 million transferred by the Governor from the Highway Trust Fund to the General Fund for purposes of balancing the state budget be returned to the Highway Trust Fund. The suit further
alleges that actions of the General Assembly regarding the transfer of funds from the Highway Trust Fund to the General Fund constitute a borrowing by the State of Highway Trust Fund cash surplus and are unlawful and unconstitutional. The lawsuit requests a declaration that taxes collected for purposes of Highway Trust Fund expenditures cannot be used for other purposes. Summary Judgment was granted in favor of the State on all issues and Plaintiffs has filed a notice of appeal. On September 20, 2005, the North Carolina Court of Appeals upheld the trial court’s order. The plaintiff filed a petition for discretionary review with the North Carolina Supreme Court, and the Court agreed on March 2, 2006 to review a portion of the Court of Appeals’ decision and oral argument is scheduled for October 16, 2006.

Diana Coley, et al. v. State of North Carolina, et al. — Refund of Income Tax. On April 25, 2003, Plaintiffs filed suit in the Superior Court of Wake County against the State of North Carolina and the Secretary of Revenue challenging the constitutionality of retroactively applying the 2001 increase in the highest rate of North Carolina’s state income tax to the entire 2001 tax year. Plaintiffs seek refunds, for themselves and a proposed class of similarly situated taxpayers, of all taxes paid for the year 2001 in excess of the prior 7.75% maximum rate, on the theory that a retroactive midyear tax increase violates the state and federal constitutions. Plaintiffs claim the total amount of taxes involved exceeds $76 million, plus interest. On June 30, 2004, the trial court granted summary judgment in favor of the State on all issues. Plaintiffs appealed to the Court of Appeals. The Court of Appeals issued a 2-1 opinion sustaining the constitutionality of the tax. Plaintiffs appealed to the North Carolina Supreme Court. Arguments were heard in the Supreme Court in March 2006. The Supreme Court upheld the Court of Appeals decision on June 30, 2006. A petition for rehearing was denied on August 17, 2006.

DirecTV, Inc. and EchoStar Satellite Corporation v. State of North Carolina et al. — Refund of Sales Tax. Effective January 1, 2002, the legislature enacted a provision to impose the sales tax on satellite TV service providers. On September 30, 2003, DirecTV and EchoStar filed a complaint in Wake County Superior court for a refund of state sales tax paid, which currently amounts to approximately $70 million. Plaintiffs claim this tax, which was not imposed on cable television providers, is unconstitutional under the Commerce Clause because it discriminates against interstate commerce. It is the State’s position that the sales tax does not violate the Commerce Clause. Although cable providers are not subject to this tax, they are subject to city and county franchise taxes. The tax on satellite companies was enacted to equalize the tax burden on these various forms of entertainment. In 2005, the trial court allowed summary judgment in the State’s favor. Plaintiffs appealed to the North Carolina Court of appeals. Oral arguments were heard on May 9, 2006. On August 1, 2006, the Court of Appeals unanimously affirmed the decision and upheld the constitutionality of the tax.

Leslie J. Dunn, et al. v. The State of North Carolina, et al. — Tax on Municipal Bonds. On February 9, 2004, Plaintiffs, on behalf of a class of all others similarly situated, filed suit in Forsyth County Superior Court alleging that the State’s imposition and collection of state income tax on interest received by certain taxpayers on municipal bonds issued by non-North Carolina state and local governments constitutes a violation of the Commerce Clause of the United States Constitution and seeking class certification. An order certifying a class has been entered by the superior court. The State has appealed the scope of the class certification to the North Carolina Court of Appeals. On October 17, 2006, the Court of Appeals unanimously affirmed the order certifying the class.

Wal-Mart Stores East, Inc. v. Tolson and Sam’s East, Inc. v. Tolson — Refund of Corporate Income Tax. On March 17, 2006, the Plaintiffs filed complaints seeking a refund of over $33.5 million in corporate income taxes in Wake County Superior Court (06 CVS 3928 and 06 CVS 3929). Plaintiffs are challenging the Secretary’s authority to require them to file a “combined return” on various statutory and constitutional grounds. Defendant has filed a motion to dismiss under Rule 12(b)(6) and Plaintiffs have filed a motion for summary judgment. On August 31, 2006, Defendant’s Motion to Dismiss was heard before Judge Horton who has been assigned to hear the actions as exceptional cases.

State of North Carolina v. Philip Morris, Inc., et al., 98 CVS 14377 — Master Settlement Agreement (“MSA”) Payments. On April 20, 2006, the State of North Carolina filed a Motion for Declaratory Order in the North Carolina Business Court against defendants Philip Morris, Inc., R.J. Reynolds Tobacco Company, and Lorillard Tobacco Company. The Motion is seeking a declaration that (1) in 2003, North Carolina continuously had a Qualifying Statute in full force and effect and “diligently enforced” its provisions throughout that year in accordance with the MSA; (2) North Carolina is not subject to a Non-Participating Manufacturers’ Adjustment for 2003; and (3) defendants are obligated not to withhold or pay into a disputed payments account any payments due, or seek any offset of any payments made, on the basis that North Carolina is subject to a Non-Participating Manufacturers’ Adjustment for 2003. If the State is unable to ultimately prevail in the diligent enforcement litigation, the State may be unable to recover a portion of this year’s MSA payment.

Petroleum Traders Corporation (PTC) v. State. Petroleum Traders Corporation (PTC) brought a Declaratory Judgment
NOTES TO THE FINANCIAL STATEMENTS

action in Wake County Superior Court on July 19, 2006, seeking a declaration that the North Carolina e-procurement fee is a tax and is unconstitutional under provisions of the state and national constitutions. PTC claims to have paid over $1 million itself in e-procurement fees. PTC also seeks to have the action proceed as a class action, allegedly involving potential refunds in excess of $100 million. The State has moved to dismiss the complaint, and the motion is expected to be heard this year.

Other Litigation. The State is involved in numerous other claims and legal proceedings, many of which are normal for governmental operations. A review of the status of outstanding lawsuits involving the State by the North Carolina Attorney General did not disclose other proceedings that are expected to have a material adverse effect on the financial position of the State.

C. Federal Grants

The State receives significant financial assistance from the Federal Government in the form of grants and entitlements, which are generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of the resources for eligible purposes. Under the terms of the grants, periodic audits are required and certain costs may be questioned as not being appropriate expenditures. During the fiscal year ending June 30, 2006, the U.S. Department of Health and Human Services (USDHHS) notified the state Department of Health and Human Services (DHHS) of a disallowance of $95 million in federal funds under Title IV-E of the Social Security Act. This disallowance has been appealed by DHHS to the USDHHS Departmental Appeals Board.

Any disallowance as a result of questioned costs could become a liability of the State. As of June 30, 2006, the State is unable to estimate what liabilities may result from such audits except for the $154 million settlement balance with the U.S. Department of Justice and the U.S. Department of Health and Human Services which is included in the long-term liabilities footnote (Note 7).

D. Highway Construction

The State may be liable for approximately $51.55 million to contractors for highway construction claims that the State has contested. The State may also be liable for an additional $10.31 million in contested rights-of-way acquisition costs to property owners in condemnation proceedings. These costs have not been included in project-to-date costs. Also, the State is contingently liable for outstanding contractors’ claims in the amount of $114.37 million.

E. USDA-Donated Commodities

The State has custodial responsibility for $2.81 million of U.S. Department of Agriculture donated food commodities for which the State is liable in the event of loss.

F. Construction and Other Commitments

At June 30, 2006, the State had commitments of $1.43 billion for construction of highway facilities. Of this amount, $776.74 million relates to the Highway Fund, and $651.29 million relates to the Highway Trust Fund. The other commitments for construction and improvements of state government facilities totaled $580.24 million (including $442.92 million for the Department of Environment and Natural Resources and $86.72 million for the Department of Correction).

At June 30, 2006, the University of North Carolina System (component unit) had outstanding construction commitments of $506.96 million (including $107.66 million for North Carolina State University, $84.97 million for North Carolina Agricultural and Technical State University, $56.82 million for East Carolina University, $36.23 million for University of North Carolina - Wilmington, $36.29 million for Appalachian State University and $35.55 million for University of North Carolina - Charlotte).

At June 30, 2006, community colleges (component units) had outstanding construction commitments of $153.49 million (including $39.56 million for Wake Technical Community College, $15.09 million for Blue Ridge Community College, $14.75 million for Sandhills Community College, $11.76 million for College of the Albemarle, $9.04 million for Cape Fear Community College, and $8.17 million for Central Piedmont Community College).

At June 30, 2006, The Golden LEAF, Inc. (component unit) had outstanding commitments of $61.9 million.

G. Tobacco Settlement

In 1998, North Carolina, along with forty-five other states, signed the Master Settlement Agreement (MSA) with the nation’s largest tobacco companies to settle existing and potential claims of the states for damages arising from the use of the companies’ tobacco products. Under the MSA, the tobacco companies are required to adhere to a variety of marketing, advertising, lobbying, and youth access restrictions, support smoking cessation and prevention programs, and provide payments to the states in perpetuity. The amount that North Carolina will actually receive from this settlement remains uncertain, but projections are that the State will receive approximately $4.6 billion through the year 2025. In the early
NOTES TO THE FINANCIAL STATEMENTS

years of MSA, participating states received initial payments that were distinct from annual payments. The initial payments were made for five years: 1998 and 2000 through 2003. The annual payments began in 2000 and will continue indefinitely. However, these payments are subject to a number of adjustments including an inflation adjustment and a volume adjustment. Some adjustments (e.g., inflation) should result in an increase in the payments while others (e.g., domestic cigarette sales volume) may decrease the payments. Also, future payments may be impacted by continuing and potential litigation against the tobacco industry and changes in the financial condition of the tobacco companies. At year-end, the State recognizes a receivable and revenue for the tobacco settlement based on the underlying domestic shipment of cigarettes. This accrual estimate is based on the projected payment schedule in the MSA adjusted for historical payment trends.

In 1999, the State approved legislation to implement the terms of the MSA in North Carolina. The State created a nonprofit corporation, The Golden LEAF, Inc., to distribute 50 percent of the settlement funds received by the State of North Carolina. The legislation directed that these funds be used for the purposes of providing economic impact assistance to economically affected or tobacco-dependent regions of North Carolina. However, the Foundation’s share of the payments may be diverted by the North Carolina General Assembly prior to the funds being received by the North Carolina State Specific Account. The Golden LEAF, Inc. is reported as a discretely presented component unit.

In 2000, the State enacted legislation that established the Health and Wellness Trust Fund and the Tobacco Trust Fund and created commissions charged with managing these funds. Each fund will receive 25 percent of the tobacco settlement payments. The purpose of the Health and Wellness Trust Fund is to finance programs and initiatives to improve the health and wellness of the people of North Carolina. An eighteen-member Health and Wellness Trust Fund Commission will administer the Fund. The primary purpose of the Tobacco Trust Fund is to compensate the tobacco-related segment of North Carolina’s economy for the economic hardship it is expected to experience as a result of the MSA. An eighteen-member Tobacco Trust Fund Commission will administer the Fund. The Health and Wellness Trust Fund and Tobacco Trust Fund are reported as special revenue funds.

H. Other Contingencies

As of June 30, 2006, the North Carolina Global TransPark Authority (component unit) had a loan outstanding including accrued interest payable totaling $30.47 million to the Escheat Fund (special revenue fund). The loan is due on October 1, 2007. The current amount of operating cash held by the Authority is not sufficient to pay the balance due to the Escheat Fund and as such, substantial doubt about the Authority’s ability to continue as a going concern exists. In addition, if the Authority declares bankruptcy all funding received to date from the Federal Aviation Administration (FAA) is required to be paid back. As of June 30, 2006, the Authority has received approximately $20.1 million from the FAA.
NOTE 21:  CHANGES IN FINANCIAL ACCOUNTING AND REPORTING

CHANGE IN METHOD OF APPLYING PREVIOUSLY IMPLEMENTED ACCOUNTING PRINCIPLE

For the fiscal year ended June 30, 2006, the State changed its methodology, as it regards individual income taxes, for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions. Specifically, the State now reports an estimate of underpayments of individual income taxes whereas before this change it did not. In addition, the State has changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds).

For the purpose of reporting underpayments, the State changed the availability period for recognizing individual income tax revenues in the governmental fund financial statements. The availability period for individual income taxes was extended from thirty-one days to twelve months after yearend (see Note 1). Furthermore, in the circumstance where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).

The change in methodology as described above results in a more accurate estimate of overpayments of individual income taxes and also allows for the accounting recognition of both underpayments and overpayments of individual income taxes in the period when taxable income is earned by taxpayers (see Note 22).

CHANGES RESULTING FROM ADOPTION OF NEW ACCOUNTING PRINCIPLES

For the fiscal year ended June 30, 2006, the State implemented the following pronouncements issued by the Governmental Accounting Standards Board (GASB):

- GASB Statement No. 44, Economic Condition Reporting: The Statistical Section.
- GASB Statement No. 46, Net Assets Restricted by Enabling Legislation, an amendment of GASB Statement No. 34.

GASB Statement No. 44 enhances and updates the statistical section that accompanies the basic financial statements. This pronouncement adds new information that users have identified as important and eliminates certain previous requirements. The statistical section now includes trend information on fund balances and principal employers and government-wide, accrual-based information required by GASB Statement No. 34. It also now includes revenue capacity information and information about operating indicators and capital assets. Finally, this pronouncement improves the understandability and usefulness of the statistical section by requiring governments to augment their schedules with certain narrative explanations.

GASB Statement No. 46 provides clarifications regarding the meaning of the phrase legally enforceable as it applies to restrictions imposed on net asset use by enabling legislation. This pronouncement also specifies the accounting and financial reporting requirements if legal enforceability is reevaluated. During the fiscal year, the State determined that constraints placed on net asset use by enabling legislation are not legally enforceable. An Attorney General Advisory Opinion referenced that the Governor, pursuant to his constitutional authority under Article III, Section 5(3), may use resources restricted by enabling legislation in his discretion to meet a budget shortfall. Such amounts previously reported as restricted are reclassified to unrestricted net assets.

GASB Technical Bulletin No. 2006-1 clarifies how state and local governmental entities should report payments received from the federal government under the retiree drug subsidy provisions of Medicare Part D. Such payments made to the State Health Plan constitute on-behalf payments for fringe benefits. In the statement of changes in plan net assets, the State Health Plan displays payments from the federal government as "Other contributions" (see Note 15).

GASB Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries, and GASB Statement 47, Accounting for Termination Benefits, have no material impact on the State's financial statements as the items to which these pronouncements would apply are immaterial.
NOTE 22: FUND EQUITY RECLASSIFICATIONS AND RESTATEMENTS

The following table reconciles the beginning fund equity as previously reported to the beginning fund equity as restated (dollars in thousands). The adjustments in the Change in Application of GASB 33 column result from the change in methodology for applying GASB Statement No. 33 to individual income taxes as discussed in Note 21. The amounts in the Other Adjustments column are due primarily to the correction of errors related to prior periods.

<table>
<thead>
<tr>
<th>Primary Government</th>
<th>Fund Equity as Previously Reported</th>
<th>Change in Application of GASB 33</th>
<th>Other Adjustments</th>
<th>Fund Equity as Restated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Major Governmental Funds:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Fund</td>
<td>$78,809</td>
<td>$1,035,504</td>
<td>$3,186</td>
<td>$953,509</td>
</tr>
<tr>
<td>Highway Fund</td>
<td>369,431</td>
<td>-</td>
<td>13,871</td>
<td>383,302</td>
</tr>
<tr>
<td>Highway Trust Fund</td>
<td>(2,909)</td>
<td>-</td>
<td>(12,453)</td>
<td>(15,362)</td>
</tr>
<tr>
<td>Other Governmental Funds:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Special Revenue Funds</td>
<td>2,494,795</td>
<td>-</td>
<td>3,186</td>
<td>2,497,981</td>
</tr>
<tr>
<td>Capital Projects Funds</td>
<td>209,514</td>
<td>-</td>
<td>-</td>
<td>209,514</td>
</tr>
<tr>
<td>Permanent Funds</td>
<td>58,550</td>
<td>-</td>
<td>-</td>
<td>58,550</td>
</tr>
<tr>
<td>Total Governmental Funds</td>
<td>3,050,572</td>
<td>1,035,504</td>
<td>1,418</td>
<td>4,087,494</td>
</tr>
<tr>
<td>Internal Service Funds</td>
<td>198,301</td>
<td>-</td>
<td>(2,823)</td>
<td>195,478</td>
</tr>
<tr>
<td>Governement-wide adjustments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital assets</td>
<td>27,419,071</td>
<td>-</td>
<td>30,555</td>
<td>27,449,626</td>
</tr>
<tr>
<td>Unavailable deferred revenues</td>
<td>354,265</td>
<td>-</td>
<td>(5,214)</td>
<td>349,051</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>(7,028,062)</td>
<td>-</td>
<td>3,355</td>
<td>(7,024,707)</td>
</tr>
<tr>
<td>Accrual of interest payable</td>
<td>(85,512)</td>
<td>-</td>
<td>-</td>
<td>(85,512)</td>
</tr>
<tr>
<td>Pension assets</td>
<td>407</td>
<td>-</td>
<td>-</td>
<td>407</td>
</tr>
<tr>
<td>Total Government-wide adjustments</td>
<td>20,660,169</td>
<td>-</td>
<td>28,696</td>
<td>20,688,865</td>
</tr>
<tr>
<td>Total Governmental Activities</td>
<td>$23,909,042</td>
<td>$1,035,504</td>
<td>$27,291</td>
<td>$24,971,837</td>
</tr>
</tbody>
</table>

Business-type Activities - Enterprise Funds:

|Business-type Activities - Enterprise Funds:| | | | |
|Unemployment Compensation Fund | $258,455 | - | - | $258,455 |
|EPA Revolving Loan Fund | 708,629 | - | - | 708,629 |
|N.C. State Lottery Fund | - | - | - | - |
|Other enterprise funds | 124,526 | - | 45 | 124,571 |
|Total Business-type Activities - Enterprise Funds | $1,091,610 | - | 45 | $1,091,655 |

Component Units:

|Component Units| | | | |
|The Golder LEAF, Inc. | $422,752 | - | - | $422,752 |
|University of North Carolina System | 8,746,529 | - | 1,135 | 8,747,664 |
|Community Colleges | 1,729,524 | - | 18,924 | 1,748,448 |
|NC Housing Finance Agency | 361,155 | - | - | 361,155 |
|State Education Assistance Authority | 546,471 | - | - | 546,471 |
|Other component units | 283,021 | - | 229 | 283,247 |
|Total Component Units | $12,089,452 | - | 20,285 | $12,109,737 |
NOTE 23: SUBSEQUENT EVENTS

Primary Government

Repair and Renovation Certificates of Participation

On August 16, 2006, the State sold $100 million of repair and renovation certificates of participation, Series 2006A. The certificates are dated August 16, 2006 and will bear interest from that date. Interest will be payable semiannually on each June 1 and December 1, commencing December 1, 2006. The certificates will mature, subject to the redemption provisions, from June 1, 2007 to 2026 inclusive, and were issued at coupon rates ranging from 4% to 5%. Pursuant to Session Law 2003-284 and the State of North Carolina Capital Facilities Finance Act, Article 9 of Chapter 142, the certificates were issued for the purpose of financing the repair and renovation of state facilities and related infrastructure that are supported from the State’s General Fund and to pay certain costs incurred in connection with the execution and delivery of the 2006A Certificates.

Capital Improvement Certificates of Participation

On October 18, 2006, the State sold $200 million of Capital improvements certificates of participation, Series 2006A. The certificates are dated October 18, 2006 and will bear interest from that date. Interest will be payable semiannually on each February 1 and August 1, commencing February 1, 2007. The certificates will mature, subject to the redemption provisions, from February 1, 2008 to 2027 inclusive, and were issued at coupon rates ranging from 4% to 5%. Pursuant to the provisions of Article 9 of Chapter 142 of the North Carolina General Statutes (the “State Capital Facilities Finance Act”), and Session Laws 2003-314, 2004-126, 2004-179, 2005-276, 2006-66, 2006-146 and 2006-231 which authorized a total of $1.41 billion of various state projects and related infrastructure. These certificates were issued for the purpose of providing funding in varying amounts for the authorized projects and to pay certain costs incurred in connection with the execution and delivery of the 2006A Certificates.

Settlement Agreement

Subsequent to June 30, 2006, a settlement agreement was reached between the United States of America, through the United States Department of Justice and on behalf of the Office of Inspector General of the United States Department of Health and Human Services and the State of North Carolina for the Medicaid Disproportionate Share Hospital program. The settlement agreement was signed by all parties on August 17, 2006. The State agreed to pay $151.5 million. Of that amount, fifty-one hospitals identified in the settlement paid the State $91.5 million during September 2006. The first payment to the Centers for Medicare and Medicaid Services was made on September 27, 2006, in the amount of $106.5 million. The second payment is due by September 30, 2007 in the amount of $15 million plus accrued interest; the third payment is due by September 30, 2008 in the amount of $15 million plus accrued interest; and the final payment is due by September 30, 2009 in the amount of $15 million plus accrued interest. Interest shall begin accruing as of January 1, 2007 at the rate of 5.01%.

Town of Butner Water and Sewer

The authority to operate the Butner Water and Sewer System had been transferred from the Department of Health and Human Services (DHHS) to South Granville Water and Sewer Authority (SGWASA) effective as of January 1, 2006.

On July 5, 2006, the rights to the Town of Butner intangible asset, nitrogen credits were transferred to SGWASA and sold. The Town of Butner intangible asset, nitrogen credits amounting to $1.46 million and the note payable amounting to $1.46 million supporting the intangible asset, will be retired in fiscal year 2007.

Enacted legislation, Senate Bill 491 approved as of July 23, 2006, provides for the conveyance to SGWASA, from DHHS, on January 1, 2007, all the remaining assets that make up the water and sewer system providing that SGWASA “make arrangements to retire, assume or otherwise satisfy” the remaining bond payable, amounting to $8.8 million entered into by the State and secured by the assets and revenue of the water and sewer system.

SGWASA will also continue to make monthly payments to the Town of Butner from its water and sewer revenue to provide for the funding of the operation of the Town.

Component Units

Appalachian State University

The University participated in the University of North Carolina System Pool Revenue and Refunding Bonds, Series 2006A issuance. The Bonds were sold on November 30, 2006, and $42.7 million will be used by the University for a new dining facility, renovate a residence hall, refund the 2000 housing bonds, refund a portion of the 2002A housing bonds, and refund a portion of the 2003A Student Recreation Center Bonds.
NOTES TO THE FINANCIAL STATEMENTS

North Carolina State University Commercial Paper

On August 16, 2006, the University borrowed $44 million through the commercial paper financing program for construction projects.

North Carolina Housing Finance Agency, Bond Purchase Agreement

On August 31, 2006, the Agency signed a bond purchase agreement under the 1998 Home Ownership Trust Indenture for Series 25A amounting to $65 million. The Agency will deliver these bonds on September 26, 2006.

State Education Assistance Authority, Bond Issuance

On August 8, 2006 the State Education Assistance Authority (the Authority) issued $346 million State of North Carolina Education Assistance Authority Tax-Exempt Guaranteed Student Loan Revenue Bonds 2006 Series Q (Senior Lien), $30 million State of North Carolina Education Assistance Authority Tax-Exempt Guaranteed Student Loan Revenue Bonds 2006 Series Q (Subordinate Lien) and $194 million State of North Carolina State Education Assistance Authority Guaranteed Student Loan Revenue Bonds 2006 Series R (Senior Lien). The proceeds from these issuances will be used to fund student loans.
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REQUIRED SUPPLEMENTARY INFORMATION
# REQUIRED SUPPLEMENTARY INFORMATION

## SCHEDULES OF FUNDING PROGRESS

### ALL DEFINED BENEFIT PENSION TRUST FUNDS

**June 30, 2006**

(Expressed in Thousands)

<table>
<thead>
<tr>
<th>Retirement System</th>
<th>Valuation Date</th>
<th>Actuarial Value of Assets</th>
<th>Actuarial Accrued Liability (AAL)</th>
<th>Unfunded AAL (UAAL)</th>
<th>Funded Ratio (a) / (b)</th>
<th>Annual Covered Payroll (b-a)(c)</th>
<th>UAAL as a Percentage of Covered Payroll (b-a)(c)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Teachers' and State Employees'</td>
<td>12-31-05</td>
<td>$49,670,182</td>
<td>$46,624,668</td>
<td>$(3,045,514)</td>
<td>106.5%</td>
<td>$10,990,239</td>
<td>(27.7)%</td>
</tr>
<tr>
<td></td>
<td>12-31-04</td>
<td>$47,383,509</td>
<td>$43,827,854</td>
<td>$(3,555,655)</td>
<td>106.1%</td>
<td>$10,366,137</td>
<td>(34.3)%</td>
</tr>
<tr>
<td></td>
<td>12-31-03</td>
<td>$45,117,508</td>
<td>$41,733,701</td>
<td>$(3,383,807)</td>
<td>106.1%</td>
<td>$10,082,153</td>
<td>(36.6)%</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$43,226,837</td>
<td>$39,863,983</td>
<td>$(3,362,854)</td>
<td>106.4%</td>
<td>$9,734,448</td>
<td>(34.6)%</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$42,104,086</td>
<td>$37,713,663</td>
<td>$(4,390,423)</td>
<td>111.6%</td>
<td>$9,494,603</td>
<td>(46.2)%</td>
</tr>
<tr>
<td></td>
<td>12-31-00</td>
<td>$39,773,747</td>
<td>$35,248,770</td>
<td>$(4,524,977)</td>
<td>112.8%</td>
<td>$9,001,354</td>
<td>(50.3)%</td>
</tr>
<tr>
<td>Consolidated Judicial</td>
<td>12-31-05</td>
<td>$382,501</td>
<td>$355,498</td>
<td>$(27,003)</td>
<td>107.6%</td>
<td>$51,018</td>
<td>(52.9)%</td>
</tr>
<tr>
<td></td>
<td>12-31-04</td>
<td>$363,110</td>
<td>$334,727</td>
<td>$(28,383)</td>
<td>108.6%</td>
<td>$49,368</td>
<td>(58.4)%</td>
</tr>
<tr>
<td></td>
<td>12-31-03</td>
<td>$340,857</td>
<td>$316,649</td>
<td>$(24,008)</td>
<td>107.6%</td>
<td>$49,465</td>
<td>(48.9)%</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$323,384</td>
<td>$301,031</td>
<td>$(22,353)</td>
<td>107.4%</td>
<td>$48,432</td>
<td>(46.2)%</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$311,221</td>
<td>$285,692</td>
<td>$(25,529)</td>
<td>108.9%</td>
<td>$47,773</td>
<td>(53.4)%</td>
</tr>
<tr>
<td></td>
<td>12-31-00</td>
<td>$291,807</td>
<td>$269,181</td>
<td>$(22,626)</td>
<td>108.4%</td>
<td>$43,546</td>
<td>(52.0)%</td>
</tr>
<tr>
<td>Legislative</td>
<td>12-31-05</td>
<td>$28,381</td>
<td>$21,524</td>
<td>$(6,857)</td>
<td>131.9%</td>
<td>$3,681</td>
<td>(188.3)%</td>
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<tr>
<td></td>
<td>12-31-04</td>
<td>$27,478</td>
<td>$20,686</td>
<td>$(6,782)</td>
<td>132.8%</td>
<td>$3,658</td>
<td>(185.4)%</td>
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<tr>
<td></td>
<td>12-31-03</td>
<td>$26,327</td>
<td>$20,046</td>
<td>$(6,281)</td>
<td>131.3%</td>
<td>$3,692</td>
<td>(170.1)%</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$25,304</td>
<td>$19,243</td>
<td>$(6,061)</td>
<td>131.5%</td>
<td>$3,688</td>
<td>(165.2)%</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$24,231</td>
<td>$18,551</td>
<td>$(5,680)</td>
<td>130.6%</td>
<td>$3,891</td>
<td>(153.9)%</td>
</tr>
<tr>
<td></td>
<td>12-31-00</td>
<td>$22,314</td>
<td>$17,733</td>
<td>$(4,581)</td>
<td>125.8%</td>
<td>$3,785</td>
<td>(121.0)%</td>
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<tr>
<td>Firemen's and Rescue Squad Workers'</td>
<td>6-30-05</td>
<td>$274,265</td>
<td>$285,356</td>
<td>$11,091</td>
<td>96.1%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
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<td></td>
<td>6-30-04</td>
<td>$261,148</td>
<td>$273,826</td>
<td>$12,678</td>
<td>95.4%</td>
<td>N/A</td>
<td>N/A</td>
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<tr>
<td></td>
<td>6-30-03</td>
<td>$249,925</td>
<td>$260,707</td>
<td>$10,782</td>
<td>95.9%</td>
<td>N/A</td>
<td>N/A</td>
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<tr>
<td></td>
<td>6-30-02</td>
<td>$239,918</td>
<td>$249,316</td>
<td>$9,398</td>
<td>96.2%</td>
<td>N/A</td>
<td>N/A</td>
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<tr>
<td></td>
<td>6-30-01</td>
<td>$225,276</td>
<td>$230,796</td>
<td>$5,520</td>
<td>97.6%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>6-30-00</td>
<td>$202,751</td>
<td>$240,335</td>
<td>$37,584</td>
<td>84.4%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>North Carolina National Guard</td>
<td>12-31-05</td>
<td>$59,204</td>
<td>$81,803</td>
<td>$22,599</td>
<td>72.4%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>12-31-04</td>
<td>$54,069</td>
<td>$93,388</td>
<td>$39,319</td>
<td>57.9%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>12-31-03</td>
<td>$51,316</td>
<td>$58,752</td>
<td>$7,436</td>
<td>87.3%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$46,769</td>
<td>$58,943</td>
<td>$12,174</td>
<td>79.3%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$46,314</td>
<td>$52,235</td>
<td>$5,921</td>
<td>88.7%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>12-31-00</td>
<td>$43,886</td>
<td>$49,495</td>
<td>$5,609</td>
<td>88.7%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Registers of Deeds'</td>
<td>12-31-05</td>
<td>$28,242</td>
<td>$11,788</td>
<td>$(16,454)</td>
<td>239.6%</td>
<td>$5,357</td>
<td>(306.6)%</td>
</tr>
<tr>
<td>NOTE 2</td>
<td>12-31-04</td>
<td>$24,262</td>
<td>$12,240</td>
<td>$(12,022)</td>
<td>198.2%</td>
<td>$5,549</td>
<td>(216.6)%</td>
</tr>
<tr>
<td></td>
<td>12-31-03</td>
<td>$20,439</td>
<td>$11,886</td>
<td>$(8,553)</td>
<td>172.0%</td>
<td>$5,178</td>
<td>(165.2)%</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$16,325</td>
<td>$11,673</td>
<td>$(4,652)</td>
<td>139.9%</td>
<td>$4,767</td>
<td>(97.6)%</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$12,887</td>
<td>$11,648</td>
<td>$(1,239)</td>
<td>110.6%</td>
<td>$4,736</td>
<td>(26.2)%</td>
</tr>
<tr>
<td></td>
<td>12-31-99</td>
<td>$9,227</td>
<td>$10,859</td>
<td>$1,632</td>
<td>85.0%</td>
<td>$4,406</td>
<td>37.0%</td>
</tr>
<tr>
<td>Local Governmental Employees'</td>
<td>12-31-05</td>
<td>$14,395,849</td>
<td>$14,482,208</td>
<td>$43,359</td>
<td>99.4%</td>
<td>$4,241,351</td>
<td>2.0%</td>
</tr>
<tr>
<td></td>
<td>12-31-04</td>
<td>$13,377,297</td>
<td>$13,466,189</td>
<td>$88,892</td>
<td>99.3%</td>
<td>$4,088,170</td>
<td>2.2%</td>
</tr>
<tr>
<td></td>
<td>12-31-03</td>
<td>$12,364,380</td>
<td>$12,455,503</td>
<td>$91,123</td>
<td>99.3%</td>
<td>$3,868,476</td>
<td>2.3%</td>
</tr>
<tr>
<td></td>
<td>12-31-02</td>
<td>$11,393,460</td>
<td>$11,462,706</td>
<td>$69,246</td>
<td>99.4%</td>
<td>$3,746,396</td>
<td>1.9%</td>
</tr>
<tr>
<td></td>
<td>12-31-01</td>
<td>$10,764,032</td>
<td>$10,835,460</td>
<td>$72,428</td>
<td>99.3%</td>
<td>$3,597,769</td>
<td>2.0%</td>
</tr>
<tr>
<td></td>
<td>12-31-00</td>
<td>$9,892,805</td>
<td>$9,967,548</td>
<td>$74,743</td>
<td>99.3%</td>
<td>$3,344,615</td>
<td>2.2%</td>
</tr>
</tbody>
</table>

**NOTE 1**

A negative UAAL denotes excess actuarial assets

**NOTE 2**

No valuation was done for 12-30-00

A- Change in the actuary's computation of the 5-year smoothed market value of assets.

N/A - Not applicable

The information presented in these required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information for the latest actuarial valuations is presented on page 124.
### REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF CONTRIBUTIONS FROM THE EMPLOYERS AND OTHER CONTRIBUTING ENTITIES ALL DEFINED BENEFIT PENSION TRUST FUNDS**

For the Six-Year Period 2001 to 2006 (July 1 to June 30)

(Expressed in Thousands)

<table>
<thead>
<tr>
<th>Retirement System</th>
<th>State Fiscal Year</th>
<th>Annual Required Contribution</th>
<th>Percentage Contributed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Teachers' and State Employees'</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>$ 269,587</td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>2005</td>
<td>237,170</td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>2004</td>
<td>23,135</td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>2003</td>
<td>—</td>
<td></td>
<td>NR</td>
</tr>
<tr>
<td>2002</td>
<td>196,003</td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>2001</td>
<td>513,907</td>
<td></td>
<td>75%</td>
</tr>
</tbody>
</table>

| Consolidated Judicial            |                   |                               |                        |
| 2006                             | $ 6,448           |                               | 100%                   |
| 2005                             | 6,513             |                               | 100%                   |
| 2004                             | 5,583             |                               | 100%                   |
| 2003                             | 5,993             |                               | 100%                   |
| 2002                             | 7,003             |                               | 100%                   |
| 2001                             | 9,071             |                               | 75%                    |

| Legislative                      |                   |                               |                        |
| 2006                             | —                 |                               | NR                     |
| 2005                             | —                 |                               | NR                     |
| 2004                             | —                 |                               | NR                     |
| 2003                             | —                 |                               | NR                     |
| 2002                             | 858               |                               | 97%                    |
| 2001                             | 861               |                               | 71%                    |

| Firemen's and Rescue Squad Workers' |                   |                               |                        |
| 2006                             | $ 7,926           |                               | 100%                   |
| 2005                             | 7,521             |                               | 100%                   |
| 2004                             | 8,801             |                               | 100%                   |
| 2003                             | 6,856             |                               | 100%                   |
| 2002                             | 10,027            |                               | 100%                   |
| 2001                             | 12,105            |                               | 92%                    |

| North Carolina National Guard    |                   |                               |                        |
| 2006                             | $ 5,944           |                               | 102%                   |
| 2005                             | 1,412             |                               | 111%                   |
| 2004                             | 1,176             |                               | 100%                   |
| 2003                             | 1,132             |                               | —                      |
| 2002                             | 1,542             |                               | 58%                    |
| 2001                             | 2,075             |                               | 100%                   |

| Registers of Deeds'             |                   |                               |                        |
| 2006                             | —                 |                               | NR                     |
| 2005                             | 29                |                               | 10.458%                |
| 2004                             | 286               |                               | 1.158%                 |
| 2003                             | 1,722             |                               | 197%                   |
| 2002                             | 1,722             |                               | 128%                   |
| 2001                             | 1,826             |                               | 98%                    |

| Local Governmental Employees'    |                   |                               |                        |
| 2006                             | $ 226,665         |                               | 100%                   |
| 2005                             | 216,097           |                               | 100%                   |
| 2004                             | 208,092           |                               | 100%                   |
| 2003                             | 233,753           |                               | 100%                   |
| 2002                             | 192,170           |                               | 100%                   |
| 2001                             | 179,238           |                               | 100%                   |

NR- No contribution was required or made.

Note 1- The State made additional contributions not related to the ARC. The amounts were disclosed in the 2004 CAFR.

Note 2- The State made $284 thousand in additional contributions not related to the ARC.

Note 3- For Registers, significant fees and collections are contributed. They are not directly related to the ARC.

The information presented in these required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information for the latest actuarial valuations is presented on page 124.
## REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN UNRESERVED FUND BALANCE — BUDGET AND ACTUAL (BUDGETARY BASIS — NON-GAAP)**

### GENERAL FUND

For the Fiscal Year Ended June 30, 2006

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Revenues:</th>
<th>Budgeted Amounts</th>
<th>Variance with Final Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Original</td>
<td>Final</td>
</tr>
<tr>
<td><strong>Taxes:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income</td>
<td>8,839,760</td>
<td>8,839,760</td>
</tr>
<tr>
<td>Corporate income</td>
<td>905,940</td>
<td>905,940</td>
</tr>
<tr>
<td>Sales and use</td>
<td>4,692,700</td>
<td>4,692,700</td>
</tr>
<tr>
<td>Franchise</td>
<td>493,800</td>
<td>493,800</td>
</tr>
<tr>
<td>Insurance</td>
<td>441,700</td>
<td>441,700</td>
</tr>
<tr>
<td>Beverage</td>
<td>195,950</td>
<td>195,950</td>
</tr>
<tr>
<td>Inheritance</td>
<td>137,900</td>
<td>137,900</td>
</tr>
<tr>
<td>Other</td>
<td>260,774</td>
<td>260,774</td>
</tr>
<tr>
<td><strong>Non-Tax:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>161,726</td>
<td>161,726</td>
</tr>
<tr>
<td>Investment income</td>
<td>74,800</td>
<td>74,800</td>
</tr>
<tr>
<td>Disproportionate share receipts</td>
<td>100,000</td>
<td>100,000</td>
</tr>
<tr>
<td>Other</td>
<td>238,691</td>
<td>238,691</td>
</tr>
<tr>
<td><strong>Transfers in:</strong></td>
<td>252,558</td>
<td>252,558</td>
</tr>
<tr>
<td><strong>Departmental:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal funds</td>
<td>8,741,557</td>
<td>10,105,989</td>
</tr>
<tr>
<td>Local funds</td>
<td>977,982</td>
<td>1,048,968</td>
</tr>
<tr>
<td>Inter-agency grants and allocations</td>
<td>22,007</td>
<td>58,081</td>
</tr>
<tr>
<td>Intra-governmental transactions</td>
<td>1,446,246</td>
<td>1,825,350</td>
</tr>
<tr>
<td>Sales and services</td>
<td>78,785</td>
<td>88,348</td>
</tr>
<tr>
<td>Rental and lease of property</td>
<td>7,319</td>
<td>8,122</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>472,023</td>
<td>327,985</td>
</tr>
<tr>
<td>Contributions, gifts and grants</td>
<td>92,092</td>
<td>590,372</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>83,706</td>
<td>96,061</td>
</tr>
<tr>
<td><strong>Universities:</strong></td>
<td>780,830</td>
<td>1,018,064</td>
</tr>
<tr>
<td><strong>Total Revenues:</strong></td>
<td>29,518,846</td>
<td>31,983,639</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenditures:</th>
<th>Budgeted Amounts</th>
<th>Variance with Final Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Original</td>
<td>Final</td>
</tr>
<tr>
<td><strong>Current:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General government</td>
<td>1,011,356</td>
<td>622,842</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>7,657,836</td>
<td>9,036,931</td>
</tr>
<tr>
<td>Community Colleges</td>
<td>1,012,194</td>
<td>1,111,392</td>
</tr>
<tr>
<td>Health and human services</td>
<td>14,221,530</td>
<td>15,016,023</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>389,209</td>
<td>426,101</td>
</tr>
<tr>
<td>Economic development</td>
<td>165,232</td>
<td>173,733</td>
</tr>
<tr>
<td>Public safety, corrections, and regulation</td>
<td>1,719,009</td>
<td>2,091,679</td>
</tr>
<tr>
<td>Transportation</td>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>Agriculture</td>
<td>75,179</td>
<td>87,501</td>
</tr>
<tr>
<td>Capital outlay</td>
<td>54,960</td>
<td>54,960</td>
</tr>
<tr>
<td>Debt service</td>
<td>581,838</td>
<td>567,469</td>
</tr>
<tr>
<td>Universities</td>
<td>2,995,426</td>
<td>3,154,928</td>
</tr>
<tr>
<td><strong>Total Expenditures:</strong></td>
<td>29,883,996</td>
<td>32,363,759</td>
</tr>
<tr>
<td><strong>Excess revenues over (under) expenditures</strong></td>
<td>(365,123)</td>
<td>(360,120)</td>
</tr>
<tr>
<td>Transfers to reserves</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Unreserved fund balances (budgetary basis) at July 1, 2005</td>
<td>478,509</td>
<td>478,509</td>
</tr>
<tr>
<td>Unreserved fund balances (budgetary basis) at June 30, 2006</td>
<td>113,386</td>
<td>98,389</td>
</tr>
</tbody>
</table>
BUDGETARY REPORTING

A. General Fund Budgetary Process

The State of North Carolina operates on a biennial budget cycle with separate annual departmental certified budgets adopted by the General Assembly on the cash basis of accounting for the General Fund.

The accompanying budgetary comparison schedule discloses the annual original budget and final budget for the General Fund. Actual amounts in the schedule are presented on the budgetary basis. Since the budgetary basis differs from generally accepted accounting principles (GAAP), a reconciliation between the budgetary basis and the GAAP basis is presented in section C below.

The legal level of budgetary control is essentially at the object level. However, departments and institutions may make changes at their discretion within the budget of each purpose between and among objects for supplies and materials, current obligations and services, fixed charges and other expenses, and capital outlay. Also, Chapter 116, Article 1, Part 2A of the General Statutes authorized the sixteen universities within the University of North Carolina System to apply for special responsibility status, which sets the legal level of budgetary control at the institution’s budget code level. A budget code is a convention used in the State’s accounting system to distinguish the type of fund and the responsible department or institution. Budget codes are also used to segregate certain purposes within departments or institutions. Institutions with special responsibility status must still have certain budget revisions, primarily those associated with unanticipated revenues, approved by the Office of State Budget and Management (OSBM). Additionally, universities must maintain programs and services in accordance with the guidelines established by the Board of Governors of the consolidated University of North Carolina System. All sixteen universities have applied for and received special responsibility status.

Generally, unexpended appropriations at the end of the fiscal year lapse and are reappropriated in the next fiscal year. However, in certain circumstances the OSBM will allow a department to carry forward appropriations for specifically identified expenditures that will be paid in the next fiscal year. This is accomplished by the department writing a check to itself and recording a budgetary expenditure. The check is deposited in the next fiscal year as a budgetary receipt.

A detailed listing of appropriation and departmental budget information is available for public inspection in the separately published “Budgetary Compliance Report” prepared by the Office of the State Controller, 3512 Bush Street, Raleigh, NC 27609-7509 and through the Office of State Budget and Management, 116 West Jones Street, Raleigh, NC 27603-8005.

B. Special Fund Budgetary Process

The major special revenue funds, which are the Highway Fund and Highway Trust Fund, do not have annual appropriated budgets.

C. Reconciliation of Budget/GAAP Reporting Differences

The Schedule of Revenues, Expenditures and Changes in Unreserved Fund Balances – Budget and Actual (Budgetary Basis – Non-GAAP) – General Fund, presents comparisons of the legally adopted budget (which is more fully described in section A, above) with actual data on a budgetary basis. Accounting principles applied to develop data on a budgetary basis differ significantly from those principles used to present financial statements in conformity with generally accepted accounting principles (GAAP). The following describes the major differences between budgetary financial data and GAAP financial data.

**Entity differences.** Certain funds not included in the annual budgetary statements but which have the characteristics of governmental funds are presented in the General Fund for GAAP purposes.

**Basis differences.** Budgetary funds are accounted for on the cash basis of accounting, while under GAAP the governmental funds use the modified accrual basis. Accrued revenues and expenditures are recognized in the GAAP financial statements.

**Timing differences.** A significant variance between budgetary practices and GAAP is the authorized carryforward of appropriated funds, which is described in section A.

The following table presents a reconciliation of resulting entity, basis, and timing differences in the fund balances (budgetary basis) at June 30, 2006 to the fund balances on a modified accrual basis (GAAP). Amounts are expressed in thousands.
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

Unreserved fund balance (budgetary basis),

<table>
<thead>
<tr>
<th>Description</th>
<th>General Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 30, 2006</td>
<td>$749,386</td>
</tr>
</tbody>
</table>

Reserved fund balance (budgetary basis),

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Savings</td>
<td>628,793</td>
</tr>
<tr>
<td>Repairs and renovation</td>
<td>222,229</td>
</tr>
<tr>
<td>Disproportionate share</td>
<td>19,304</td>
</tr>
<tr>
<td>Disaster relief</td>
<td>141,712</td>
</tr>
<tr>
<td>One North Carolina Fund</td>
<td>1,083</td>
</tr>
<tr>
<td>Job Development Investment Grant</td>
<td>7,798</td>
</tr>
</tbody>
</table>

Fund balance (budgetary basis) = $1,770,305

Reconciling Adjustments:

Entity Differences:

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary government</td>
<td>232,759</td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
</tbody>
</table>

Basis Differences:

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Accrued revenues</td>
<td></td>
</tr>
<tr>
<td>Taxes receivable</td>
<td>1,790,815</td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>256,876</td>
</tr>
<tr>
<td>Federal funds, net</td>
<td>774,658</td>
</tr>
<tr>
<td>Other receivables</td>
<td>210,775</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>Tax refunds payable</td>
<td>(1,183,801)</td>
</tr>
<tr>
<td>Deferred revenue</td>
<td>(674,748)</td>
</tr>
<tr>
<td>Total accrued revenues</td>
<td>1,174,325</td>
</tr>
</tbody>
</table>

Accrued expenditures:

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Medical claims payable</td>
<td>(962,144)</td>
</tr>
<tr>
<td>Accounts payable and accrued liabilites</td>
<td>(480,337)</td>
</tr>
<tr>
<td>Other payables</td>
<td>(63,711)</td>
</tr>
<tr>
<td>Total accrued expenditures</td>
<td>(1,506,192)</td>
</tr>
</tbody>
</table>

Other Adjustments:

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Notes receivable</td>
<td>6,578</td>
</tr>
<tr>
<td>Inventories</td>
<td>73,343</td>
</tr>
<tr>
<td>Investments</td>
<td>52</td>
</tr>
</tbody>
</table>

Timing Differences:

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorized carryforward for</td>
<td></td>
</tr>
<tr>
<td>specific encumbrances</td>
<td>31,958</td>
</tr>
<tr>
<td>Authorized carryforward for</td>
<td></td>
</tr>
<tr>
<td>designated programs</td>
<td>142,170</td>
</tr>
</tbody>
</table>

Fund balance (GAAP basis) = $1,925,198

D. Budgetary Reserves

The North Carolina General Assembly has established several accounts in the General Fund as reserved fund balances for budgetary purposes. Funds that are transferred to these accounts from the unreserved credit balance of the General Fund can be used only for their intended purposes and on a budgetary basis are not available for appropriation.

Savings Reserve Account (General Statute 143-15.2 through 143-15.3B). One-fourth of any unreserved credit balance (budgetary basis) remaining in the General Fund at the end of each fiscal year will be transferred to the Savings Reserve account until the account contains funds equal to 5% of the amount appropriated the preceding year for the General Fund operating budget. Therefore, at the end of the fiscal year, $316.15 million was transferred to the Savings Reserve bringing the balance of this reserve to $628.79 million at June 30, 2006.

Repairs and Renovations Reserve Account (General Statute 143-15.2 through 143-15.3B). This reserve account provides for a portion of the State's continuing capital needs. The reserve balance is based on 3% of the estimated replacement value of all State buildings supported from the General Fund. The funds in this account shall be used only for the repair and renovation of State facilities and related infrastructure that are supported from the General Fund. In accordance with Session Law 2006-66, Senate Bill 1741, Section 2.2(b) the State Controller was directed to transfer $222.23 million from the unreserved credit balance to the Repairs and Renovations Reserve Account on June 30, 2006. At the end of the fiscal year 2005-2006, the balance of this reserve was $222.23 million.

Disproportionate Share Reserve Account (1997 General Assembly, Senate Bill 352, Section 11). Disproportionate share payments are Medicaid payments made to hospitals which serve a disproportionate share of indigent patients. This account was established to reserve for future appropriation any excess collection of disproportionate share revenues above those budgeted as departmental receipts or non-tax revenues. At the end of the fiscal year 2005-2006, the remaining balance of this reserve was $19.3 million.

Disaster Relief Reserve. The 1996 Second Extra Session, Section 7.9, Chapter 18 of House Bill 53 authorized the Director of Budget to create the Disaster Relief Reserve. During fiscal year 2004-2005 $248.17 million was transferred to the Disaster Relief Reserve to fund recovery from the effects of the 2004 Hurricane Season. This $248.17 million was funded from required agency, university, and community college transfers, a Savings Reserve transfer, and transfers of funds from the unreserved credit balance. At the end of the fiscal year 2005-2006, the remaining balance of this reserve was $141.71 million.

One North Carolina Reserve. The Office of State Budget and Management, after consultation with Joint Legislative Commission on Governmental Operations on November 4, 2003, established the One North Carolina Reserve. This reserve was funded by a transfer from the unexpended legislative increase appropriation of $1.5 million. During the fiscal year an establishment of $0.4 million was expended. However, since that time no further One North Carolina funds have been disbursed. Therefore, for fiscal years 2003-2004 through 2005-2006 the balance has remained at $1.08 million.

Job Development Investment Grant Program Reserve (JDIG). In accordance with Session Law 2004-124, House Bill 1414, Section 6.12(a), Article I of Chapter 143 of the General Statutes was amended by adding a new section requiring the establishment of a JDIG Reserve in the General Fund. It is the intent of the General Assembly to annually appropriate funds to this reserve in amounts sufficient to meet anticipated cash requirements for each fiscal year of the Job Development Investment Grant Program established pursuant to General Statute 143B-437.52. Funds in the amount of $4.5 million were
The following schedule summarizes current year changes in the budgetary reserve accounts. Amounts are expressed in thousands.

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Savings[1]</td>
<td>$312,641</td>
<td>$316,152</td>
<td>$628,793</td>
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<tr>
<td>Repairs and renovations</td>
<td>125,000</td>
<td>222,229</td>
<td>222,229</td>
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<tr>
<td>Disproportionate share</td>
<td>19,304</td>
<td>19,304</td>
<td>19,304</td>
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<tr>
<td>Disaster relief</td>
<td>211,679</td>
<td>69,967</td>
<td>141,712</td>
</tr>
<tr>
<td>One North Carolina</td>
<td>1,083</td>
<td>1,083</td>
<td>1,083</td>
</tr>
<tr>
<td>Job Development Investment Grant</td>
<td>2,542</td>
<td>9,000</td>
<td>7,798</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$672,249</strong></td>
<td><strong>$547,381</strong></td>
<td><strong>$1,020,919</strong></td>
</tr>
</tbody>
</table>

[1] Note: An additional $5.79 million was transferred by the State Controller on December 5, 2006, to the Savings Reserve account from the General Fund unreserved fund balance. This additional transfer will satisfy the 2006 fiscal year end Savings Reserve account requirements of General Statute 143-15.2 through 143-15.3B.


At the end of fiscal year 2005-2006, the balance of this reserve was $7.8 million.
COMBINING FUND STATEMENTS AND SCHEDULES
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NONMAJOR
GOVERNMENTAL
FUNDS
### COMBINING BALANCE SHEET
### NONMAJOR GOVERNMENTAL FUNDS

**June 30, 2006**

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Assets</th>
<th>Special Revenue Funds</th>
<th>Capital Projects Funds</th>
<th>Permanent Funds</th>
<th>Total Nonmajor Governmental Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$1,336,214</td>
<td>$240,604</td>
<td>$1,134</td>
<td>$1,577,752</td>
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<tr>
<td>Investments</td>
<td>989,983</td>
<td>28,532</td>
<td></td>
<td>1,018,515</td>
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<tr>
<td>Securities lending collateral</td>
<td>975,533</td>
<td>886</td>
<td>32,673</td>
<td>1,009,392</td>
</tr>
<tr>
<td>Receivables, net:</td>
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<td></td>
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<tr>
<td>Taxes receivable</td>
<td>2,317</td>
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<tr>
<td>Accounts receivable</td>
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<td>24,217</td>
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<td>Intergovernmental receivable</td>
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<td>3</td>
<td>7,433</td>
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<td>Due from other funds</td>
<td>49,541</td>
<td>8,386</td>
<td></td>
<td>57,927</td>
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<tr>
<td>Due from component units</td>
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<td>Inventories</td>
<td>33,818</td>
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<td>Prepaid items</td>
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<td>Advances to component units</td>
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<td>Notes receivable, net</td>
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<td>Securities held in trust</td>
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<td>Endowment investments</td>
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<td></td>
<td></td>
<td>57,741</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>$3,831,264</strong></td>
<td><strong>$278,765</strong></td>
<td><strong>$91,863</strong></td>
<td><strong>$4,201,892</strong></td>
</tr>
</tbody>
</table>

### Liabilities and Fund Balances

**Liabilities:**

| Accounts payable               | $61,359               | $24,104               |                | $85,463                           |
| Accrued payroll                | 813                   |                        |                | 813                               |
| Intergovernmental payable      | 9,105                 | 653                    |                | 9,758                             |
| Claims payable                 | 32,632                |                        |                | 32,632                            |
| Obligations under securities lending | 975,533 | 886                       | 32,973         | 1,009,392                         |
| Due to fiduciary funds         | 47                    |                        |                | 47                                |
| Due to other funds             | 41,815                | 38                     |                | 41,853                            |
| Due to component units         | 95,280                |                        |                | 95,280                            |
| Deferred revenue               | 13,282                |                        |                | 13,282                            |
| Deposits payable               | 8                     | 1                      |                | 9                                 |
| Funds held for others          | 38,863                |                        |                | 38,863                            |
| **Total Liabilities**          | **1,268,737**         | **25,682**             | **32,973**     | **1,327,392**                     |

**Fund Balances:**

| Reserved                       | 706,386               | 139,650                | 57,372         | 903,408                           |
| Unreserved                     | 1,856,141             | 113,433                | 1,518          | 1,971,092                         |
| **Total Fund Balances**        | **2,562,527**         | **253,083**            | **68,890**     | **2,874,500**                     |

| Total Liabilities and Fund Balances | $3,831,264 | $278,765 | $91,863 | $4,201,892 |
## COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
### NONMAJOR GOVERNMENTAL FUNDS

For the Fiscal Year Ended June 30, 2006

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Revenues:</th>
<th>Special Revenue Funds</th>
<th>Capital Projects Funds</th>
<th>Permanent Funds</th>
<th>Total Nonmajor Governmental Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxes:</td>
<td></td>
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<tr>
<td>Individual income tax</td>
<td>$1,735</td>
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<td>Corporate income tax</td>
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<td>96,199</td>
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<tr>
<td>Sales and use tax</td>
<td>26,836</td>
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<td>26,836</td>
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<tr>
<td>Gasoline tax</td>
<td>27,927</td>
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<td>27,927</td>
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<tr>
<td>Insurance tax</td>
<td>10,568</td>
<td></td>
<td></td>
<td>10,568</td>
</tr>
<tr>
<td>Beverage tax</td>
<td>328</td>
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<td>328</td>
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<tr>
<td>Other taxes</td>
<td>146,734</td>
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<td>146,734</td>
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<tr>
<td>Federal funds</td>
<td>395,586</td>
<td>20,390</td>
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<td>415,976</td>
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<tr>
<td>Local funds</td>
<td>19,447</td>
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<td>19,447</td>
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<td>Investment earnings</td>
<td>76,436</td>
<td>1,502</td>
<td>(189)</td>
<td>79,749</td>
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<td>Interest: earnings on loans</td>
<td>5,398</td>
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<td>5,398</td>
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<tr>
<td>Sales and services</td>
<td>163,421</td>
<td>1,057</td>
<td>69</td>
<td>164,547</td>
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<td>Rental and lease of property</td>
<td>3,158</td>
<td>49</td>
<td></td>
<td>3,207</td>
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<tr>
<td>Fees, licenses, and fines</td>
<td>196,308</td>
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<td>4,589</td>
<td>200,877</td>
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<tr>
<td>Contributions, gifts, and grants</td>
<td>24,595</td>
<td>73,858</td>
<td>36</td>
<td>98,489</td>
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<tr>
<td>Funds escheated</td>
<td>108,075</td>
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<td></td>
<td>108,075</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>13,506</td>
<td>362</td>
<td></td>
<td>13,868</td>
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<tr>
<td><strong>Total revenues</strong></td>
<td><strong>1,320,257</strong></td>
<td><strong>97,218</strong></td>
<td><strong>4,485</strong></td>
<td><strong>1,421,960</strong></td>
</tr>
</tbody>
</table>

| Expenditures:                                 |                       |                        |                |                                   |
| Current:                                      |                       |                        |                |                                   |
| General government                            | 94,807                |                        |                | 94,807                           |
| Primary and secondary education               | 257,079               |                        |                | 257,079                          |
| Higher education                              | 411,372               | 33                     | 26             | 411,431                          |
| Health and human services                     | 87,989                |                        | 9              | 87,998                           |
| Economic development                          | 400,557               |                        |                | 400,557                          |
| Environment and natural resources             | 375,281               | 35                     | 1,434          | 376,750                          |
| Public safety, corrections, and regulation    | 397,251               |                        |                | 397,251                          |
| Agriculture                                   | 8,370                 |                        |                | 8,370                            |
| Capital outlay                                |                        | 270,882                |                | 270,882                          |
| Debt service                                  |                       |                        |                |                                   |
| Principal retirement                          | 747                   |                        |                | 747                              |
| Interest and fees                             | 902                   | 135                    |                | 1,037                            |
| Debt issuance costs                           | 1,137                 |                        |                | 1,137                            |
| **Total expenditures**                        | **2,035,492**         | **271,085**            | **1,489**      | **2,308,046**                    |
| Excess revenues over (under) expenditures     | (715,235)             | (173,867)              | **3,016**      | (886,086)                        |

| Other Financing Sources (Uses):               |                       |                        |                |                                   |
| Bonds issued                                  | 370,000               |                        |                | 370,000                          |
| Other debt issued                             |                        | 23,831                 |                | 23,831                           |
| Premium on debt issued                        | 16,338                |                        |                | 16,338                           |
| Capital leases                                | 26,745                |                        |                | 26,745                           |
| Sale of capital assets                        | 5,464                 | 10                     |                | 5,474                            |
| Insurance recoveries                          | 923                   |                        |                | 923                              |
| Transfers in                                  | 875,654               | 195,129                | 680            | 1,071,463                        |
| Transfers out                                 | (516,099)             | (1,534)                | (3,358)        | (520,989)                        |
| **Total other financing sources (uses)**      | **779,025**           | **217,436**            | **(2,676)**    | **793,736**                      |
| Net change in fund balances                   | 63,780                | 43,569                 | 340            | 107,699                          |
| Fund balances — July 1, as restated           | 2,497,981             | 209,514                | 58,550         | 2,766,045                        |
| Increase (decrease) in reserve for related assets | 756                  |                        |                | 756                              |
| Fund balances — June 30                       | **2,562,527**         | **253,083**            | **58,890**     | **2,874,500**                    |
NONMAJOR SPECIAL REVENUE FUNDS

The special revenue funds are maintained to account for those financial resources which are restricted by legal, regulatory or administrative action to finance particular functions or activities of the State.

The following are included in the nonmajor special revenue funds:

- Escheat Fund
- Health and Wellness Trust Fund
- Tobacco Trust Fund
- Clean Water Funds
- Public School Bond Fund
- Higher Education and Public Improvement Bond Funds
- Public School Building Capital Fund
- Clean Water Management Trust Fund
- N.C. Infrastructure Finance Corporation
- Natural Gas Funds
- Prison Enterprises Fund
- Educational Materials and School Buses Fund
- Employment Security Commission Funds
- Highway Patrol Fund
- Employment and Training Administration Fund
- Leaking Petroleum Underground Storage Tank Cleanup Fund
- Ecosystem Enhancement Funds
- Wildlife Resources Commission Fund
- Natural Heritage Trust Fund
- Wireless 911 Fund
- Parks and Recreation Trust Fund
- Education Lottery Funds
- Departmental Funds
### COMBINING BALANCE SHEET
#### NONMAJOR SPECIAL REVENUE FUNDS
#### June 30, 2006
#### (Dollars in Thousands)

<table>
<thead>
<tr>
<th>Assets</th>
<th>Escheat Fund</th>
<th>Health and Wellness Trust Fund</th>
<th>Tobacco Trust Fund</th>
<th>Clean Water Funds</th>
<th>Public School Bond Fund</th>
<th>Higher Education and Public Improvement Bond Funds</th>
<th>Public School Building Capital Fund</th>
<th>Clean Water Management Trust Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$223,222</td>
<td>$46,941</td>
<td>$5,100</td>
<td>$40,095</td>
<td>$10,132</td>
<td>$203</td>
<td>$125,007</td>
<td>$175,139</td>
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<td>Securities lending collateral</td>
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<td>4,375</td>
<td>26,191</td>
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<td>Taxes receivable</td>
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</tr>
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<td>Accounts receivable</td>
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<td>Intergovernmental receivable</td>
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<td>Interest receivable</td>
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<td>513</td>
<td>573</td>
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<tr>
<td>Due from component units</td>
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<tr>
<td>Prepaid items</td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Advances to component units</td>
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<tr>
<td>Notes receivable, net</td>
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<tr>
<td>Securities held in trust</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>$925,379</td>
<td>$87,403</td>
<td>$9,491</td>
<td>$243,671</td>
<td>$12,085</td>
<td>$470,823</td>
<td>$257,377</td>
<td>$325,974</td>
</tr>
</tbody>
</table>

#### Liabilities and Fund Balances

##### Liabilities:
- Accounts payable and accrued liabilities:
  - Accounts payable: $19 $2 $15 $558 $518
  - Accrued payroll
  - Intergovernmental payable: 32,632
  - Claims payable: 334,534
  - Obligations under securities lending: $34,534 $15 $4,375 $26,191
  - Due to fiduciary funds
  - Due to other funds: $24,726 $2 $24,805 $8
  - Due to component units: $11,394 $115,964
  - Deferred revenue
  - Deposits payable
  - Funds held for others: $151,108

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>$403,305</th>
<th>$40,290</th>
<th>$4,390</th>
<th>$26,780</th>
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</thead>
<tbody>
<tr>
<td>Total Liabilities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

##### Fund Balances:
- Reserved for:
  - Inventories
  - Notes receivable: 115,964
  - Prepaid items
  - Loan and grant commitments: 16,895
  - Advance to component unit: 21,742
  - Other purposes

- Unreserved:
  - Undesignated: $500,332 $47,113 $5,101 $84,032 $12,085 $394,208 $125,520 $35,402

| Total Fund Balances | $522,074 | $47,113 | $5,101 | $216,891 $12,085 $394,208 $125,520 $174,866 |
|---------------------|----------|---------|--------|----------|---------|----------|---------|
| Total Liabilities and Fund Balances | $925,379 | $87,403 | $9,491 | $243,671 $12,085 $470,823 $257,377 $325,974 |
### Exhibit C-3

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>$</td>
<td>$ 2,334</td>
<td>$ 20,701</td>
<td>$ 66,249</td>
<td>$ 11,113</td>
<td>$ 17,343</td>
<td>$ 68</td>
<td>$ 18,988</td>
<td>$ 45,393</td>
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<tr>
<td>141,680</td>
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Continued
# COMBINING BALANCE SHEET
## NONMAJOR SPECIAL REVENUE FUNDS
### June 30, 2006

(Dollars in Thousands)

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<th>Wildlife Resources Commission Fund</th>
<th>Natural Heritage Trust Fund</th>
<th>Wireless 911 Fund</th>
<th>Parks and Recreation Trust Fund</th>
<th>Education Lottery Funds</th>
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<td>Funds held for others</td>
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## COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
### NONMAJOR SPECIAL REVENUE FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

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<th>Health and Wellness Trust Fund</th>
<th>Tobacco Trust Fund</th>
<th>Clean Water Funds</th>
<th>Public School Bond Fund</th>
<th>Higher Education and Public Improvement Bond Funds</th>
<th>Public School Building Capital Fund</th>
<th>Clean Water Management Trust Fund</th>
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<td>Beverage tax</td>
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<td><strong>Total other financing sources</strong></td>
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<td>(124,684)</td>
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<td>52,978</td>
<td>(4,150)</td>
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<td>Fund balances — June 30</td>
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### Exhibit C-4

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Continued
## COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES  
### NONMAJOR SPECIAL REVENUE FUNDS  
#### For the Fiscal Year Ended June 30, 2006  
### Exhibit C-4  
#### (Dollars in Thousands)  

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<th>Revenues:</th>
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<tr>
<td>Wildlife Resources Commission Fund</td>
<td>Natural Heritage Trust Fund</td>
<td>Wireless 911 Fund</td>
<td>Parks and Recreation Trust Fund</td>
<td>Education Lottery Funds</td>
<td>Departmental Funds</td>
<td>Total Nonmajor Special Revenue Funds</td>
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<td><strong>Taxes:</strong></td>
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<td>98,199</td>
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<td>10,568</td>
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<td>Beverage tax</td>
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<td><strong>Interest earnings on loans:</strong></td>
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<td><strong>Sales and services:</strong></td>
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<td>113,194</td>
<td>196,308</td>
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<td>(6,843)</td>
<td>(3,753)</td>
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<tr>
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<td>2,193</td>
<td>9,904</td>
<td>13,632</td>
<td>63,558</td>
<td>48,897</td>
<td>63,750</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Fund balances — July 1, as restated:</strong></td>
<td>14,930</td>
<td>24,592</td>
<td>7,633</td>
<td>39,039</td>
<td>—</td>
<td>347,748</td>
<td>2,497,981</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Increase (decrease) in:</strong></td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Reserve for related assets:</strong></td>
<td>1,123</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(52)</td>
<td>756</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Fund balances — June 30:</strong></td>
<td>$ 10,222</td>
<td>$ 26,785</td>
<td>$ 17,537</td>
<td>$ 52,671</td>
<td>$ 63,558</td>
<td>$ 396,291</td>
<td>$ 2,562,527</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
### COMBINING SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN UNRESERVED FUND BALANCES — BUDGET AND ACTUAL (BUDGETARY BASIS — NON-GAAP)

**NONMAJOR SPECIAL REVENUE FUNDS**

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Revenues:</th>
<th>Employment and Training Administration Fund</th>
<th>Clean Water Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Budgeted Amounts</td>
<td>Variance with Final</td>
</tr>
<tr>
<td></td>
<td>Original</td>
<td>Final</td>
</tr>
<tr>
<td><strong>Departmental:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal funds</td>
<td>$97,094</td>
<td>$162,778</td>
</tr>
<tr>
<td>Local funds</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Inter-agency grants and allocations</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Intra-governmental transactions</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Sales and services</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Sale, rental and lease of property</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Contributions, gifts and grants</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total revenues:</strong></td>
<td>$97,095</td>
<td>$162,778</td>
</tr>
</tbody>
</table>

| Expenditures:                      |          |       |        |        |          |       |        |        |
| Current:                           |          |       |        |        |          |       |        |        |
| General government                 | —        | —      | —      | —      | —        | —     | —     | —      |
| Health and human services          | —        | —      | —      | —      | —        | —     | —     | —      |
| Environment and natural resources  | —        | —      | —      | —      | —        | —     | —     | —      |
| Economic development               | $97,095  | $162,778 | $119,383 | $43,395 | $750     | 6,482 | 435   | 6,047  |
| Primary and secondary education     | —        | —      | —      | —      | —        | —     | —     | —      |
| Public safety and corrections      | —        | —      | —      | —      | —        | —     | —     | —      |
| Debt service                       | —        | —      | —      | —      | —        | —     | —     | —      |
| Principal retirement               | —        | —      | —      | —      | —        | —     | —     | —      |
| Interest and fees                  | —        | —      | —      | —      | —        | —     | —     | —      |
| **Total expenditures:**            | $97,095  | $162,778 | $119,383 | $43,395 | $750     | 6,482 | 435   | 6,047  |
| Excess revenues over (under) expenditures | $—       | $—      | 21     | 21     | $—       | $(4,194) | 1,665 | $5,679 |
| Unreserved fund balances (budgetary basis) at July 1, 2005 | $5        | 5,812 |
| Restatements                       | —        | —      | —      | —      | —        | —     | —     | —      |
| Unreserved fund balances (budgetary basis) at June 30, 2006 | $26      | $7,497 |
### Employment Security Commission Funds

<table>
<thead>
<tr>
<th>Budgeted Amounts</th>
<th>Variance with Final Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Original</td>
</tr>
<tr>
<td><strong>$159,306</strong></td>
<td>189,490</td>
</tr>
<tr>
<td><strong>15,195</strong></td>
<td>18,695</td>
</tr>
<tr>
<td><strong>6,788</strong></td>
<td>4,188</td>
</tr>
<tr>
<td><strong>20,072</strong></td>
<td>45,555</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
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<td></td>
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<tr>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>1,205</strong></td>
<td>2,305</td>
</tr>
<tr>
<td><strong>202,566</strong></td>
<td>260,233</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Highway Patrol Fund

<table>
<thead>
<tr>
<th>Budgeted Amounts</th>
<th>Variance with Final Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Original</td>
</tr>
<tr>
<td><strong>$327</strong></td>
<td></td>
</tr>
<tr>
<td><strong>331</strong></td>
<td></td>
</tr>
<tr>
<td><strong>$4</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
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<td></td>
</tr>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>1,205</strong></td>
<td></td>
</tr>
<tr>
<td><strong>202,566</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| **$10,015**      |          |       |        |                |                |

1,480

Continued
| Revenues: | Wildlife Resources Commission Fund | | Education Lottery Funds | | Variance with Final Budget | Variance with Final Budget |
|---|---|---|---|---|---|
| | Budgeted Amounts | Variance | Budgeted Amounts | Variance |
| | Original | Final | Actual | | Original | Final | Actual |
| Departmental: | | | | | | | |
| Federal funds | $8,522 | $12,386 | $12,329 | $(57) | $ | $ | $ | $ |
| Local funds | 13 | 168 | 171 | 3 | | | | |
| Inter-agency grants and allocations | 266 | 33 | 21 | (12) | | | | |
| Intra-governmental transactions | 41,143 | 97,408 | 96,388 | (1,020) | | | | |
| Sales and services | 1,619 | 2,171 | 3,301 | 1,130 | | | |
| Sale, rental and lease of property | 165 | 206 | 206 | | | | | |
| Fees, licenses and fines | 18,056 | 19,649 | 19,651 | 2 | | | | |
| Contributions, gifts and grants | 85 | 247 | 211 | (36) | | | | |
| Miscellaneous | 12 | 331 | 349 | 18 | | | | |
| Total revenues | 69,881 | 132,599 | 132,627 | 28 | | | | |
| Expenditures: | | | | | | | |
| Current: | | | | | | | |
| General government | | | | | | | |
| Health and human services | | | | | | | |
| Environment and natural resources | 69,881 | 140,938 | 136,311 | 4,627 | | | | |
| Economic development | | | | | | | |
| Primary and secondary education | | | | | | | |
| Public safety and corrections | | | | | | | |
| Debt service | | | | | | | |
| Principal retirement | | 650 | 650 | | | | | |
| Interest and fees | 783 | 783 | | | | | | |
| Total expenditures | 69,881 | 142,371 | 137,744 | 4,627 | | | | |
| Excess revenues over (under) expenditures | $ | $(9,772) | $(5,117) | $4,655 | | | | | |

Unreserved fund balances (budgetary basis) at July 1, 2005: 13,033

Restatements:

Unreserved fund balances (budgetary basis) at June 30, 2006: $7,916 $50,000
<table>
<thead>
<tr>
<th>Departmental Funds</th>
<th>Variance with Final Budget</th>
<th>Totals - Budgeted Special Revenue Funds</th>
<th>Variance with Final Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Budgeted Amounts</strong></td>
<td><strong>Original</strong></td>
<td><strong>Final</strong></td>
<td><strong>Actual</strong></td>
</tr>
<tr>
<td>$ 51,917</td>
<td>$ 45,358</td>
<td>$ 65,774</td>
<td>$ 20,416</td>
</tr>
<tr>
<td>110</td>
<td>580</td>
<td>9</td>
<td>(571)</td>
</tr>
<tr>
<td>1,973</td>
<td>5,251</td>
<td>1,494</td>
<td>(3,757)</td>
</tr>
<tr>
<td>152,327</td>
<td>208,668</td>
<td>136,725</td>
<td>(71,943)</td>
</tr>
<tr>
<td>4,549</td>
<td>8,998</td>
<td>6,795</td>
<td>(2,163)</td>
</tr>
<tr>
<td>89</td>
<td>87</td>
<td>102</td>
<td>15</td>
</tr>
<tr>
<td>83,422</td>
<td>95,569</td>
<td>91,423</td>
<td>(4,146)</td>
</tr>
<tr>
<td>414</td>
<td>2,234</td>
<td>1,924</td>
<td>(310)</td>
</tr>
<tr>
<td>2,393</td>
<td>3,175</td>
<td>4,710</td>
<td>1,535</td>
</tr>
<tr>
<td>297,194</td>
<td>369,900</td>
<td>308,956</td>
<td>(60,944)</td>
</tr>
</tbody>
</table>

| 75,407 | 205,473 | 137,340 | 68,133 | 75,407 | 205,473 | 137,340 | 68,133 |
| 105,562 | 91,258 | 66,472 | 24,786 | 105,562 | 91,258 | 66,472 | 24,786 |
| 52,032 | 61,604 | 43,217 | 18,387 | 121,913 | 202,542 | 179,528 | 23,014 |
| 32,594 | 82,979 | 42,717 | 40,262 | 333,005 | 512,472 | 412,323 | 100,149 |
| — | — | — | — | 50,000 | — | 50,000 |
| 31,341 | 42,247 | 39,001 | 3,246 | 224,519 | 278,104 | 238,863 | 39,241 |
| — | — | — | — | 650 | 650 | — |
| — | — | — | — | 783 | 783 | — |
| 299,936 | 483,561 | 323,747 | 154,814 | 860,406 | 1,341,282 | 1,035,959 | 305,323 |
| $ 258 | $(113,861) | (19,791) | $ 93,870 | $ 258 | $(127,627) | $ 36,717 | $ 184,344 |

| 229,752 | 254,980 |
| 6,301 | 6,301 |

$216,262 $297,998
NONMAJOR CAPITAL PROJECTS FUNDS

The Capital Projects funds are maintained to account for those financial resources received and used for the acquisition, construction or improvement of major governmental general fixed assets which are financed principally by transfers from the General Fund or lease purchase revenue bonds and certificates of participation.

The following activities are included in the nonmajor capital projects funds:

- Capital Projects Fund
- N.C. Infrastructure Finance Corporation
- State Energy Contracts
# COMBINING BALANCE SHEET
## NONMAJOR CAPITAL PROJECTS FUNDS

**June 30, 2006**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Assets</th>
<th>Capital Projects Fund</th>
<th>N.C. Infrastructure Finance Corporation</th>
<th>State Energy Contracts</th>
<th>Total Nonmajor Capital Projects Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$238,550</td>
<td>$2,054</td>
<td>$—</td>
<td>$240,804</td>
</tr>
<tr>
<td>Investments</td>
<td>$—</td>
<td>13,756</td>
<td>14,776</td>
<td>28,532</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>886</td>
<td>$—</td>
<td>$—</td>
<td>886</td>
</tr>
<tr>
<td>Receivables, net:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intergovernmental receivable</td>
<td>353</td>
<td>$—</td>
<td>$—</td>
<td>353</td>
</tr>
<tr>
<td>Interest receivable</td>
<td>4</td>
<td>$—</td>
<td>$—</td>
<td>4</td>
</tr>
<tr>
<td>Due from other funds</td>
<td>$—</td>
<td>8,386</td>
<td>$—</td>
<td>8,386</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>$239,793</strong></td>
<td><strong>$24,196</strong></td>
<td><strong>$14,776</strong></td>
<td><strong>$278,765</strong></td>
</tr>
</tbody>
</table>

**Liabilities and Fund Balances**

**Liabilities:**

Accounts payable and accrued liabilities:

- Accounts payable: $10,657, $13,447, $—, $24,104
- Intergovernmental payable: 653, $—, $—, 653
- Obligations under securities lending transactions: 886, $—, $—, 886
- Due to other funds: 25, 13, $—, 38
- Deposits payable: 1, $—, $—, 1

**Total Liabilities:** 12,222, 13,460, $—, 25,682

**Fund Balances:**

Reserved for:

- Capital projects: 34,388, 105,262, $—, 139,650

Unreserved:

- Undesignated: 193,183, (94,526), 14,776, 113,433

**Total Fund Balances:** 227,571, 10,736, 14,776, 253,083

**Total Liabilities and Fund Balances:** $239,793, $24,196, $14,776, $278,765
## COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
### NONMAJOR CAPITAL PROJECTS FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Capital Projects Fund</th>
<th>N.C. Infrastructure Finance Corporation</th>
<th>State Energy Contracts</th>
<th>Total Nonmajor Capital Projects Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal funds</td>
<td>20,390 $</td>
<td>$</td>
<td>$</td>
<td>$ 20,390 $</td>
</tr>
<tr>
<td>Investment earnings</td>
<td>73</td>
<td>911</td>
<td>518</td>
<td>1,502</td>
</tr>
<tr>
<td>Sales and services</td>
<td>1,057</td>
<td>$</td>
<td>$</td>
<td>$ 1,057</td>
</tr>
<tr>
<td>Rental and lease of property</td>
<td>49</td>
<td>$</td>
<td>$</td>
<td>$ 49</td>
</tr>
<tr>
<td>Contributions, gifts, and grants</td>
<td>73,858</td>
<td>$</td>
<td>$</td>
<td>$ 73,858</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>362</td>
<td>$</td>
<td>$</td>
<td>$ 362</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td>95,789</td>
<td>911</td>
<td>518</td>
<td>97,218</td>
</tr>
<tr>
<td><strong>Expenditures:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Higher education</td>
<td>33</td>
<td>$</td>
<td>$</td>
<td>33</td>
</tr>
<tr>
<td>Environment &amp; natural resources</td>
<td>35</td>
<td>$</td>
<td>$</td>
<td>35</td>
</tr>
<tr>
<td>Capital outlay</td>
<td>152,675</td>
<td>108,643</td>
<td>9,564</td>
<td>270,882</td>
</tr>
<tr>
<td>Debt service:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest and fees</td>
<td>$</td>
<td>126</td>
<td>$</td>
<td>9</td>
</tr>
<tr>
<td><strong>Total expenditures</strong></td>
<td>152,743</td>
<td>108,769</td>
<td>9,573</td>
<td>271,085</td>
</tr>
<tr>
<td>Excess revenues over (under) expenditures</td>
<td>56,854</td>
<td>(107,858)</td>
<td>(9,055)</td>
<td>(173,867)</td>
</tr>
<tr>
<td><strong>Other Financing Sources (Uses):</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other debt issued</td>
<td>$</td>
<td>$</td>
<td>$</td>
<td>23,831</td>
</tr>
<tr>
<td>Sale of capital assets</td>
<td>10</td>
<td>$</td>
<td>$</td>
<td>10</td>
</tr>
<tr>
<td>Transfers in</td>
<td>113,693</td>
<td>81,436</td>
<td>$</td>
<td>195,129</td>
</tr>
<tr>
<td>Transfers out</td>
<td>(610)</td>
<td>(924)</td>
<td>$</td>
<td>(1,534)</td>
</tr>
<tr>
<td><strong>Total other financing sources (uses):</strong></td>
<td>113,093</td>
<td>80,512</td>
<td>23,831</td>
<td>217,436</td>
</tr>
<tr>
<td>Net change in fund balances</td>
<td>56,139</td>
<td>(27,346)</td>
<td>14,776</td>
<td>43,569</td>
</tr>
<tr>
<td>Fund balances — July 1</td>
<td>171,432</td>
<td>38,082</td>
<td>$</td>
<td>209,514</td>
</tr>
<tr>
<td>Fund balances — June 30</td>
<td>$ 227,571</td>
<td>$ 10,736</td>
<td>$ 14,776</td>
<td>$ 253,083</td>
</tr>
</tbody>
</table>
NONMAJOR PERMANENT FUNDS

Permanent funds are used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs—that is, for the benefit of the government or its citizenry.

The following are included in nonmajor permanent funds:

Wildlife Endowment Fund
Departmental Funds
# COMBINING BALANCE SHEET
## NONMAJOR PERMANENT FUNDS
### June 30, 2006

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th>Wildlife Endowment Fund</th>
<th>Departmental Funds</th>
<th>Total Nonmajor Permanent Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 190</td>
<td>$ 944</td>
<td>$ 1,134</td>
</tr>
<tr>
<td>Receivables, net:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>12</td>
<td>—</td>
<td>12</td>
</tr>
<tr>
<td>Interest receivable</td>
<td>—</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>32,163</td>
<td>810</td>
<td>32,973</td>
</tr>
<tr>
<td>Endowment investments</td>
<td>57,193</td>
<td>548</td>
<td>57,741</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>$ 89,558</strong></td>
<td><strong>$ 2,305</strong></td>
<td><strong>$ 91,863</strong></td>
</tr>
</tbody>
</table>

|                      |                         |                    |                                |
| **Liabilities and Fund Balances** |                     |                    |                                |
| **Liabilities:**     |                         |                    |                                |
| Obligations under securities lending | 32,163              | 810                | 32,973                         |
| **Total Liabilities**| **32,163**              | **810**            | **32,973**                     |
| **Fund Balances:**   |                         |                    |                                |
| Reserved for:        |                         |                    |                                |
| Permanent investments| 55,965                  | 1,407              | 57,372                         |
| Unreserved:          |                         |                    |                                |
| Undesignated         | 1,430                   | 88                 | 1,518                          |
| **Total Fund Balances**| **57,395**              | **1,495**          | **58,890**                     |
| **Total Liabilities and Fund Balances** | **$ 89,558** | **$ 2,305**        | **$ 91,863**                   |
## COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES

### NONMAJOR PERMANENT FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Wildlife Endowment Fund</th>
<th>Departmental Funds</th>
<th>Total Nonmajor Permanent Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment earnings</td>
<td>$ (224)</td>
<td>$ 35</td>
<td>$ (189)</td>
</tr>
<tr>
<td>Sales and services</td>
<td>69</td>
<td></td>
<td>69</td>
</tr>
<tr>
<td>Fees, licenses, and fines</td>
<td>4,569</td>
<td></td>
<td>4,569</td>
</tr>
<tr>
<td>Contributions, gifts, and grants</td>
<td>36</td>
<td></td>
<td>36</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td>4,450</td>
<td>35</td>
<td>4,485</td>
</tr>
<tr>
<td><strong>Expenditures:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Higher education</td>
<td>—</td>
<td>26</td>
<td>26</td>
</tr>
<tr>
<td>Health and human services</td>
<td>—</td>
<td>9</td>
<td>9</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>1,426</td>
<td>8</td>
<td>1,434</td>
</tr>
<tr>
<td><strong>Total expenditures</strong></td>
<td>1,426</td>
<td>43</td>
<td>1,469</td>
</tr>
<tr>
<td>Excess revenues over (under) expenditures</td>
<td>3,024</td>
<td>(8)</td>
<td>3,016</td>
</tr>
<tr>
<td><strong>Other Financing Sources (Uses):</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transfers in</td>
<td>—</td>
<td>680</td>
<td>680</td>
</tr>
<tr>
<td>Transfers out</td>
<td>(3,356)</td>
<td>—</td>
<td>(3,356)</td>
</tr>
<tr>
<td><strong>Total other financing sources (uses)</strong></td>
<td>(3,356)</td>
<td>680</td>
<td>(2,676)</td>
</tr>
<tr>
<td>Net change in fund balances</td>
<td>(332)</td>
<td>672</td>
<td>340</td>
</tr>
<tr>
<td>Fund balances — July 1.</td>
<td>57,727</td>
<td>823</td>
<td>58,550</td>
</tr>
<tr>
<td>Fund balances — June 30</td>
<td>$ 57,395</td>
<td>$ 1,495</td>
<td>$ 58,890</td>
</tr>
</tbody>
</table>
THIS PAGE INTENTIONALLY LEFT BLANK.
Proprietary Funds
NONMAJOR ENTERPRISE FUNDS

Enterprise funds are used to report activities for which a fee is charged to external users for goods or services.

The following activities are included in the nonmajor enterprise funds:

Public School Insurance
Town of Butner Water and Sewer
North Carolina State Fair
USS North Carolina Battleship Commission
Agricultural Farmers Market
Workers' Compensation
Utilities Commission
State Banking Commission
ABC Commission
Departmental Funds
### COMBINING STATEMENT OF NET ASSETS
#### NONMAJOR ENTERPRISE FUNDS

**June 30, 2006**

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Assets</th>
<th>Public School Insurance</th>
<th>Town of Butner Water and Sewer</th>
<th>North Carolina State Fair</th>
<th>USS North Carolina Battleship Commission</th>
<th>Agricultural Farmers Market</th>
<th>Workers' Compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$2,815</td>
<td>$4,776</td>
<td>$2,486</td>
<td>$1,094</td>
<td>$1,306</td>
<td>$6,097</td>
</tr>
<tr>
<td>Investments</td>
<td>36,107</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>13,347</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>22,620</td>
<td>4,095</td>
<td></td>
<td></td>
<td></td>
<td>12,649</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable, net</td>
<td></td>
<td>4</td>
<td>205</td>
<td>1</td>
<td>8</td>
<td>13</td>
</tr>
<tr>
<td>Interest receivable</td>
<td>9</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>18</td>
</tr>
<tr>
<td>Premiums receivable</td>
<td>1,257</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inventories</td>
<td></td>
<td>1</td>
<td>106</td>
<td>211</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>Prepaid items</td>
<td>2,141</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total current assets</td>
<td>64,949</td>
<td>8,876</td>
<td>2,797</td>
<td>1,376</td>
<td>1,323</td>
<td>32,124</td>
</tr>
</tbody>
</table>

| Noncurrent Assets:          |                         |                                |                           |                                         |                           |                      |
| Restricted/designated cash |                         |                                |                           |                                         |                           |                      |
| and cash equivalents        |                         | 1,627                          |                           |                                         |                           |                      |
| Investments                 |                         |                                |                           |                                         |                           |                      |
| Restricted investments      |                         |                                |                           |                                         |                           |                      |
| Deferred charges            |                         | 107                            |                           |                                         |                           |                      |
| Capital assets-nondepreciable |                       | 1,795                          | 1,379                     | 629                                      | 1,087                     |                      |
| Capital assets-depreciable, net |                 | 24,275                         | 8,824                     | 2,086                                    | 6,299                     |                      |
| Total noncurrent assets     |                         | 27,804                         | 10,203                    | 6,429                                    | 7,386                     |                      |
| Total Assets                | 64,949                  | 36,680                         | 13,000                    | 7,807                                    | 8,709                     | 32,124               |

**Liabilities**

### Current Liabilities:

- Accounts payable and accrued liabilities:
  - Accounts payable: 10, 66, 85, 25, 16, 36
  - Accrued payroll: 2, 60, 17, 10
  - Claims payable: 796
  - Obligations under securities lending: 22,620, 4,095
  - Interest payable: 33
  - Due to other funds: 1, 11
  - Unearned revenue: 3,189, 725, 2
  - Deposits payable: 28
  - Notes payable: 112
  - Bonds payable - current: 280
  - Compensated absences - current: 7
  - Total current liabilities: 25,625, 4,614, 899, 52, 33, 25,241

### Noncurrent Liabilities:

- Notes payable: 1,345
- Bonds payable, net: 8,520
- Compensated absences: 71, 28, 178, 68, 62
- Total noncurrent liabilities: 71, 9,893, 178, 68, 62
- Total Liabilities: 26,696, 14,507, 1,077, 120, 95, 25,241

**Net Assets**

- Invested in capital assets, net of related debt: 17,237, 10,203, 2,698, 7,386
- Restricted for:
  - Capital outlay: 2,629
  - Other purposes: 1,102
  - Unrestricted: 38,253, 4,956, 1,720, 1,258, 1,228, 6,883
- Total Net Assets: $38,253, $22,173, $11,923, $7,887, $8,614, $6,883
<table>
<thead>
<tr>
<th>Utilities Commission</th>
<th>Banking Commission</th>
<th>ABC Commission</th>
<th>Departmental Funds</th>
<th>Total Nonmajor Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 9,827</td>
<td>$ 6,813</td>
<td>$ 5,652</td>
<td>$ 1,746</td>
<td>$ 42,812</td>
</tr>
<tr>
<td>8,252</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>49,454</td>
</tr>
<tr>
<td>4,674</td>
<td>352</td>
<td>1,681</td>
<td>2</td>
<td>7,140</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>27</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,257</td>
</tr>
<tr>
<td>38</td>
<td>—</td>
<td>88</td>
<td>48</td>
<td>501</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,213</td>
</tr>
<tr>
<td>22,991</td>
<td>7,185</td>
<td>7,421</td>
<td>1,798</td>
<td>150,820</td>
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<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,627</td>
</tr>
<tr>
<td>—</td>
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<td>—</td>
<td>—</td>
<td>462</td>
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<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>3,269</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>107</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>550</td>
<td>—</td>
<td>5,440</td>
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<tr>
<td>94</td>
<td>76</td>
<td>3,087</td>
<td>2,130</td>
<td>46,854</td>
</tr>
<tr>
<td>94</td>
<td>76</td>
<td>3,637</td>
<td>2,130</td>
<td>57,759</td>
</tr>
<tr>
<td>23,085</td>
<td>7,241</td>
<td>11,058</td>
<td>3,928</td>
<td>208,579</td>
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<tr>
<td>46</td>
<td>185</td>
<td>348</td>
<td>25</td>
<td>842</td>
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<tr>
<td>2</td>
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<td>5</td>
<td>11</td>
<td>107</td>
</tr>
<tr>
<td>8,252</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>11,969</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
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<td>47,616</td>
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<tr>
<td>—</td>
<td>1,555</td>
<td>—</td>
<td>147</td>
<td>7,001</td>
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<tr>
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<td>—</td>
<td>—</td>
<td>—</td>
<td>28</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>112</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>280</td>
</tr>
<tr>
<td>64</td>
<td>38</td>
<td>11</td>
<td>6</td>
<td>156</td>
</tr>
<tr>
<td>8,373</td>
<td>1,786</td>
<td>376</td>
<td>190</td>
<td>68,189</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,345</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>8,520</td>
</tr>
<tr>
<td>1,288</td>
<td>741</td>
<td>217</td>
<td>53</td>
<td>2,706</td>
</tr>
<tr>
<td>1,288</td>
<td>741</td>
<td>217</td>
<td>53</td>
<td>12,571</td>
</tr>
<tr>
<td>9,661</td>
<td>2,527</td>
<td>593</td>
<td>243</td>
<td>80,760</td>
</tr>
<tr>
<td>94</td>
<td>76</td>
<td>3,637</td>
<td>2,130</td>
<td>43,461</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,629</td>
</tr>
<tr>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1,102</td>
</tr>
<tr>
<td>13,330</td>
<td>4,638</td>
<td>6,828</td>
<td>1,553</td>
<td>80,627</td>
</tr>
<tr>
<td>$ 13,424</td>
<td>$ 4,714</td>
<td>$ 10,465</td>
<td>$ 3,683</td>
<td>$ 127,819</td>
</tr>
</tbody>
</table>
### COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

**NONMAJOR ENTERPRISE FUNDS**

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Public School Insurance</th>
<th>Town of Butner Water and Sewer</th>
<th>North Carolina State Fair</th>
<th>USS North Carolina Battleship Commission</th>
<th>Agricultural Farmers Market</th>
<th>Workers' Compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Revenues:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales and services</td>
<td>$ —</td>
<td>$ —</td>
<td>$ 138</td>
<td>$ 665</td>
<td>$ 22</td>
<td>$ —</td>
</tr>
<tr>
<td>Sales and services used as</td>
<td>—</td>
<td>2,377</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>security</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rental and lease earnings</td>
<td>—</td>
<td>5</td>
<td>4,218</td>
<td>—</td>
<td>530</td>
<td>—</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>—</td>
<td>8</td>
<td>8,225</td>
<td>1,420</td>
<td>753</td>
<td>—</td>
</tr>
<tr>
<td>Insurance premiums</td>
<td>12,106</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2,752</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>—</td>
<td>10</td>
<td>—</td>
<td>101</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total operating revenues:</strong></td>
<td>12,106</td>
<td>2,400</td>
<td>12,581</td>
<td>2,186</td>
<td>1,305</td>
<td>2,752</td>
</tr>
<tr>
<td><strong>Operating Expenses:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal services</td>
<td>539</td>
<td>1,032</td>
<td>3,939</td>
<td>964</td>
<td>755</td>
<td>—</td>
</tr>
<tr>
<td>Supplies and materials</td>
<td>2</td>
<td>248</td>
<td>780</td>
<td>96</td>
<td>75</td>
<td>—</td>
</tr>
<tr>
<td>Services</td>
<td>61</td>
<td>400</td>
<td>4,164</td>
<td>738</td>
<td>310</td>
<td>693</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>299</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Depreciation/amortization</td>
<td>—</td>
<td>1,062</td>
<td>618</td>
<td>128</td>
<td>292</td>
<td>—</td>
</tr>
<tr>
<td>Claims</td>
<td>3,096</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>6,715</td>
</tr>
<tr>
<td>Insurance and bonding</td>
<td>2,489</td>
<td>2</td>
<td>145</td>
<td>18</td>
<td>40</td>
<td>955</td>
</tr>
<tr>
<td>Other</td>
<td>1</td>
<td>579</td>
<td>861</td>
<td>70</td>
<td>32</td>
<td>—</td>
</tr>
<tr>
<td><strong>Total operating expenses:</strong></td>
<td>6,186</td>
<td>3,923</td>
<td>10,497</td>
<td>2,313</td>
<td>1,504</td>
<td>8,363</td>
</tr>
<tr>
<td><strong>Operating income (loss):</strong></td>
<td>5,920</td>
<td>(1,523)</td>
<td>(2,084)</td>
<td>(127)</td>
<td>(199)</td>
<td>(6,611)</td>
</tr>
<tr>
<td><strong>Nonoperating Revenues (Expenses):</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Noncapital grants</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Noncapital gifts</td>
<td>—</td>
<td>—</td>
<td>100</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Investment earnings (loss)</td>
<td>430</td>
<td>312</td>
<td>—</td>
<td>274</td>
<td>—</td>
<td>422</td>
</tr>
<tr>
<td>Interest and fees</td>
<td>—</td>
<td>(433)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Insurance recoveries</td>
<td>—</td>
<td>28</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>361</td>
</tr>
<tr>
<td>Gain (loss) on sale of equipment</td>
<td>—</td>
<td>4</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>(960)</td>
<td>(164)</td>
<td>9</td>
<td>—</td>
<td>2</td>
<td>(540)</td>
</tr>
<tr>
<td><strong>Total nonoperating revenues (expenses):</strong></td>
<td>(530)</td>
<td>(253)</td>
<td>109</td>
<td>274</td>
<td>363</td>
<td>(118)</td>
</tr>
<tr>
<td><strong>Income (loss) before contributions and transfers:</strong></td>
<td>5,390</td>
<td>(1,778)</td>
<td>2,193</td>
<td>147</td>
<td>164</td>
<td>(5,729)</td>
</tr>
<tr>
<td>Capital contributions</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>40</td>
<td>218</td>
<td>—</td>
</tr>
<tr>
<td>Transfers in</td>
<td>—</td>
<td>—</td>
<td>136</td>
<td>—</td>
<td>—</td>
<td>2,000</td>
</tr>
<tr>
<td>Transfers out</td>
<td>—</td>
<td>(238)</td>
<td>(4,495)</td>
<td>—</td>
<td>(350)</td>
<td>—</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>5,390</td>
<td>(2,014)</td>
<td>(2,166)</td>
<td>187</td>
<td>32</td>
<td>(3,729)</td>
</tr>
<tr>
<td>Net assets — July 1, as restated</td>
<td>32,863</td>
<td>24,187</td>
<td>14,089</td>
<td>7,500</td>
<td>8,582</td>
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<td>Net assets — June 30</td>
<td>$ 38,253</td>
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<td>$ 11,923</td>
<td>$ 7,687</td>
<td>$ 8,614</td>
<td>$ 6,883</td>
</tr>
<tr>
<td>Utilities Commission</td>
<td>State Banking Commission</td>
<td>ABC Commission</td>
<td>Departmental Funds</td>
<td>Total Nonmajor Enterprise Funds</td>
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</tr>
<tr>
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<td>(433)</td>
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<td>(323)</td>
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<td>437</td>
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<td>2,166</td>
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<tr>
<td>(314)</td>
<td>(150)</td>
<td>(110)</td>
<td>—</td>
<td>(5,667)</td>
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<td>3,891</td>
<td>1,018</td>
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<td>3,248</td>
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<tr>
<td>9,533</td>
<td>3,696</td>
<td>10,074</td>
<td>3,435</td>
<td>124,571</td>
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<tr>
<td>$ 13,424</td>
<td>$ 4,714</td>
<td>$ 10,655</td>
<td>$ 3,683</td>
<td>$ 127,818</td>
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</table>
## COMBINING STATEMENT OF CASH FLOWS
### NONMAJOR ENTERPRISE FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Public School Insurance</th>
<th>Town of Butter Water and Sewer</th>
<th>North Carolina Fair</th>
<th>USS North Carolina Battleship Commission</th>
<th>Agricultural Farmers Market</th>
<th>Workers' Compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cash Flows from Operating Activities:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receipts from customers</td>
<td>$12,641</td>
<td>$2,077</td>
<td>$12,508</td>
<td>$2,188</td>
<td>$1,311</td>
<td>$2,301</td>
</tr>
<tr>
<td>Receipts from other funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payments to suppliers</td>
<td>(3,050)</td>
<td>(528)</td>
<td>(6,035)</td>
<td>(1,194)</td>
<td>(457)</td>
<td>(1,595)</td>
</tr>
<tr>
<td>Payments to employees</td>
<td>(527)</td>
<td>(1,139)</td>
<td>(3,877)</td>
<td>(937)</td>
<td>(741)</td>
<td></td>
</tr>
<tr>
<td>Payments for prizes, benefits and claims</td>
<td>(3,530)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payments to other funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other receipts (payments)</td>
<td>(1)</td>
<td>(287)</td>
<td>9</td>
<td>2</td>
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<td></td>
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<tr>
<td>Net cash flows provided (used) by operating activities</td>
<td>$5,533</td>
<td>275</td>
<td>2,605</td>
<td>57</td>
<td>115</td>
<td>(4,950)</td>
</tr>
</tbody>
</table>

| **Cash Provided From (Used For) Noncapital Financing Activities:** |                         |                                 |                     |                                          |                            |                      |
| Grant receipts (refunds)    |                         |                                 |                     |                                          |                            |                      |
| Transfers from other funds  |                         |                                 |                     |                                          |                            |                      |
| Gifts                       |                         |                                 |                     |                                          |                            |                      |
| Total cash provided from (used for) noncapital financing activities |                         |                                 |                     |                                          |                            |                      |

| **Cash Provided From (Used For) Capital Financing Activities:** |                         |                                 |                     |                                          |                            |                      |
| Acquisition and construction of capital assets |                         |                                 |                     |                                          |                            |                      |
| Proceeds from the sale of capital assets |                         |                                 |                     |                                          |                            |                      |
| Capital contributions       |                         |                                 |                     |                                          |                            |                      |
| Principal paid on capital debt |                         |                                 |                     |                                          |                            |                      |
| Interest paid on capital debt |                         |                                 |                     |                                          |                            |                      |
| Payment to bond escrow agent |                         |                                 |                     |                                          |                            |                      |
| Insurance recoveries        |                         |                                 |                     |                                          |                            |                      |
| Total cash provided from (used for) capital financing activities |                         |                                 |                     |                                          |                            |                      |

| **Cash Provided From (Used For) Investment Activities:** |                         |                                 |                     |                                          |                            |                      |
| Purchase of non-State Treasurers investments |                         |                                 |                     |                                          |                            |                      |
| Purchase into State Treasurers investment pool | (12,000)                |                                 |                     |                                          |                            |                      |
| Investment earnings (loss)   |                         |                                 |                     |                                          |                            |                      |
| Total cash provided from (used for) investment activities |                         |                                 |                     |                                          |                            |                      |

| **Reconciliation of Operating Income to Net Cash Provided From (Used For) Operating Activities:** |                         |                                 |                     |                                          |                            |                      |
| Operating income (loss)      | $5,920                   | (1,523)                         | 2,084               | (127)                                    | (199)                      | (5,611)              |
| Adjustments to reconcile operating income to net cash flows from operating activities: |                         |                                 |                     |                                          |                            |                      |
| Depreciation/amortization    |                         | 1,562                           | 618                 | 128                                      | 292                        |                      |
| Restatements and adjustments to cash |                         |                                 |                     |                                          |                            |                      |
| Nonoperating miscellaneous income (expense) |                         | 9                               | 2                   |                                          |                            |                      |
| (Increases) decreases in assets: |                         | 301                             | 117                 | 182                                      | 2                          | 2                    |
| Receivables                  |                         |                                 |                     |                                          |                            |                      |
| Due from other funds         |                         |                                 |                     |                                          |                            |                      |
| Inventories                  |                         | 160                             |                     | 17                                       | (2)                        |                      |
| Prepaid items                | (495)                   |                                 |                     |                                          |                            |                      |
| Increases (decreases) in liabilities: |                         | (436)                           | 18                  | (47)                                     | 6                          | 1,067                |
| Accounts payable and accrued liabilities |                         |                                 |                     |                                          |                            |                      |
| Due to other funds           | (1)                     | (1)                             | 7                   | (1)                                      |                            |                      |
| Compensated absences         | 12                      | (107)                           | 40                  | 25                                       | 10                         |                      |
| Unearned revenue             | 232                     | (2)                             | 108                 |                                          |                            |                      |
| Deposits payable             | (49)                    |                                 |                     |                                          |                            |                      |
| Total cash provided from (used for) operations |                         |                                 |                     |                                          |                            |                      |

| **Noncash Investing, Capital, and Financing Activities:** |                         |                                 |                     |                                          |                            |                      |
| Noncash distributions from the State Treasurer: |                         |                                 |                     |                                          |                            |                      |
| Long-Term investment Portfolio and/or other agents | $1,632                   |                                 |                     |                                          |                            | $729                 |
| Donated assets (fair market value) |                         |                                 |                     |                                          |                            |                      |
| Transferred assets           |                         |                                 |                     |                                          |                            |                      |
| Assets acquired through the assumption of a liability | $22,620                  | 4,055                           |                     |                                          |                            | 12,649               |
| Change in fair value of investments | (2,429)                 |                                 |                     |                                          |                            | (1,091)              |
### Exhibit D-3

<table>
<thead>
<tr>
<th>Utilities Commission</th>
<th>State Banking Commission</th>
<th>ABC Commission</th>
<th>Departmental Funds</th>
<th>Total Nonmajor Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>$13,504</td>
<td>$9,781</td>
<td>$7,282</td>
<td>$2,111</td>
<td>$65,684</td>
</tr>
<tr>
<td>(1,034)</td>
<td>(2,392)</td>
<td>(4,645)</td>
<td>(1,042)</td>
<td>(21,972)</td>
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<tr>
<td>(10,465)</td>
<td>(5,463)</td>
<td>(2,076)</td>
<td>(766)</td>
<td>(25,093)</td>
</tr>
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<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>(9,166)</td>
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<tr>
<td>(603)</td>
<td>(503)</td>
<td>10</td>
<td>2</td>
<td>(1,374)</td>
</tr>
<tr>
<td>1,402</td>
<td>1,403</td>
<td>569</td>
<td>306</td>
<td>7,315</td>
</tr>
</tbody>
</table>

| 222                  |                         |                |                   |                                |
| (314)                | (150)                   | (110)          |                   |                                |
|                     |                         |                |                   |                                |
| (92)                | (150)                   | (110)          | 63                | (3,185)                        |

| (26)                | (8)                     | (96)           |                   |                                |
| 122                 | 4                       | 19             |                   | 148                            |
| ---                 | ---                     | ---            |                   | 40                             |
| ---                 | ---                     | ---            |                   | (270)                          |
| ---                 | ---                     | ---            |                   | (394)                          |
| ---                 | ---                     | ---            |                   | (46)                           |
| ---                 | ---                     | ---            |                   | 389                            |
| 96                  | (4)                     | (79)           |                   | (854)                          |

| ---                  | ---                     | ---            |                   |                                |
| 305                 |                         |                |                   |                                |
| 305                 |                         |                |                   |                                |
| 1.711               | 1,249                   | 350            | 369               | (10,994)                       |
| 8.116               | 5,564                   | 5,272          | 1,377             | 51,857                         |
| $9,827              | $6,813                  | $5,682         | $1,746            | $44,239                        |

| $3,876              | $1,168                  | $501           | $164              | $5,055                         |
| 67                  | 8                       | 117            | 91                | 2,983                          |
| ---                 | ---                     | ---            | ---               | 45                             |
| ---                 | ---                     | ---            | 2                 | 13                             |
| (2,896)             | (339)                   | (72)           | 7                 | (2,853)                        |
| ---                 | ---                     | 1              | 1                 | 74                             |
| ---                 | (70)                    | ---            | ---               | (483)                          |
| (24)                | 111                     | 36             | 10                | 741                            |
| (2)                 | 5                       | 3              |                   | 10                             |
| 375                 | 273                     | 54             | 7                 | 693                            |
| ---                 | 177                     |                 | 23                | 86                             |
| ---                 |                         |                 |                   | (43)                           |
| $1,402              | $1,403                  | $569           | $306              | $7,315                         |

<table>
<thead>
<tr>
<th>$</th>
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</tr>
</thead>
<tbody>
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<td>19</td>
<td>86</td>
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<tr>
<td>8,252</td>
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<td>47,616</td>
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INTERNAL SERVICE FUNDS

The internal service funds are maintained to account for the operations of State agencies that provide services to other State agencies, component units, or other governmental units on a cost reimbursement basis.

The following activities are included in the internal service funds:

Office of the State Controller:
Workers’ Compensation Program

Office of the Governor:
Computing Services
State Telecommunications Services

Department of Administration:
Motor Fleet Management
Mail Service Center
Temporary Solutions
Surplus Property

Department of Insurance:
State Property Fire Insurance
### COMBINING STATEMENT OF NET ASSETS
#### INTERNAL SERVICE FUNDS
June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Workers' Compensation</th>
<th>State Property Fire Insurance</th>
<th>Motor Fleet Management</th>
<th>Mail Service Center</th>
<th>Temporary Solutions</th>
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<td><strong>Assets</strong></td>
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<td><strong>Current Assets:</strong></td>
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<td>Cash and cash equivalents</td>
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<td>$ 5,506</td>
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<td>Receivables:</td>
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<td>Accounts receivable, net</td>
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<td>1,558</td>
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<td>Prepaid items</td>
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<td><strong>Total current assets</strong></td>
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<td><strong>92,337</strong></td>
<td><strong>11,826</strong></td>
<td><strong>919</strong></td>
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<td><strong>Noncurrent Assets:</strong></td>
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<td>Capital assets-nondepreciable</td>
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<td>Capital assets-depreciable, net</td>
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<td><strong>89,035</strong></td>
<td><strong>304</strong></td>
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<tr>
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<td><strong>92,337</strong></td>
<td><strong>80,861</strong></td>
<td><strong>1,223</strong></td>
<td><strong>2,656</strong></td>
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<td><strong>Liabilities</strong></td>
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</tr>
<tr>
<td><strong>Current Liabilities:</strong></td>
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<tr>
<td>Accounts payable and accrued liabilities:</td>
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<td>2,229</td>
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<tr>
<td>Accrued payroll</td>
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<td>14</td>
<td>44</td>
<td>313</td>
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<td>Intergovernmental payable</td>
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<td>--</td>
</tr>
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<td>Claims payable</td>
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<td><strong>147</strong></td>
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<td><strong>Net Assets</strong></td>
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<td>3,535</td>
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<td>104</td>
<td>95,736</td>
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<td>20,545</td>
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<td>$49,811</td>
<td>$22,936</td>
<td>$1,110</td>
<td>$203,818</td>
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</table>
COMBINING STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN FUND NET ASSETS
INTERNAL SERVICE FUNDS
For the Fiscal Year Ended June 30, 2006
(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Workers' Compensation Program</th>
<th>State Property Fire Insurance</th>
<th>Motor Fleet Management</th>
<th>Mail Service Center</th>
<th>Temporary Solutions</th>
</tr>
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<tbody>
<tr>
<td>Operating Revenues:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales and services</td>
<td>$ 43,772</td>
<td>$ -</td>
<td>$ 39,818</td>
<td>$ 3,511</td>
</tr>
<tr>
<td>Rental and lease earnings</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Insurance premiums</td>
<td>-</td>
<td>-</td>
<td>18,666</td>
<td>-</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>-</td>
<td>-</td>
<td>55</td>
<td>-</td>
</tr>
<tr>
<td>Total operating revenues</td>
<td>$ 43,772</td>
<td>18,666</td>
<td>39,873</td>
<td>3,511</td>
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<tr>
<td>Operating Expenses:</td>
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<td>Personal services</td>
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<td>Supplies and materials</td>
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<td>Services</td>
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<td>Cost of goods sold</td>
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<td>Depreciation/amortization</td>
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<td>78</td>
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<td>Claims</td>
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<td>Insurance and bonding</td>
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<tr>
<td>Other</td>
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<td>Total operating expenses</td>
<td>43,881</td>
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<td>38,888</td>
<td>3,937</td>
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<td>Nonoperating Revenues (Expenses):</td>
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<td>Investment earnings</td>
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<td>Insurance recoveries</td>
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<td>-</td>
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<td>Gain (loss) on sale of equipment</td>
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<td>Miscellaneous</td>
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<td>Total nonoperating revenues (expenses)</td>
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<td>Income (loss) before contributions and transfers</td>
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<td>(426)</td>
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<td>Transfers in</td>
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<tr>
<td>Transfers out</td>
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<tr>
<td>Change in net assets</td>
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<td>8,394</td>
<td>1,061</td>
<td>(94)</td>
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<td>Net assets — July 1, as restated</td>
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<td>36,695</td>
<td>77,355</td>
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<tr>
<td>Net assets — June 30</td>
<td>$ 4,109</td>
<td>$ 45,089</td>
<td>$ 78,416</td>
<td>$ 31</td>
</tr>
<tr>
<td>Computing Services</td>
<td>State Telecommunications Services</td>
<td>Surplus Property</td>
<td>Totals</td>
<td></td>
</tr>
<tr>
<td>-------------------</td>
<td>----------------------------------</td>
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<td></td>
<td>18,666</td>
<td></td>
<td>18,666</td>
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</tr>
<tr>
<td></td>
<td>132</td>
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<td>569</td>
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</tr>
<tr>
<td><strong>58,611</strong></td>
<td><strong>72,973</strong></td>
<td><strong>1,914</strong></td>
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<td><strong>22,936</strong></td>
<td><strong>1,110</strong></td>
<td><strong>203,818</strong></td>
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</table>
COMBINING STATEMENT OF CASH FLOWS
INTERNAL SERVICE FUNDS
For the Fiscal Year Ended June 30, 2006
(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Cash Flows From Operating Activities:</th>
<th>Workers' Compensation Program</th>
<th>State Property Fire Insurance</th>
<th>Motor Fleet Management</th>
<th>Mail Service Center</th>
<th>Temporary Solutions</th>
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</thead>
<tbody>
<tr>
<td>Receipts from providers</td>
<td>$ 6,874</td>
<td>$ 6,918</td>
<td>$ 5,786</td>
<td>$ 952</td>
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<td>Receipts from other funds</td>
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<td>15,270</td>
<td>35,556</td>
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<td>8,310</td>
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<td>Payments to suppliers</td>
<td>(43,881)</td>
<td>(7,655)</td>
<td>(15,270)</td>
<td>(369)</td>
<td>(27)</td>
</tr>
<tr>
<td>Payments to employees</td>
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<td>(1,986)</td>
<td>(2,037)</td>
<td>(2,897)</td>
<td>(8,251)</td>
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<td>Payments for benefits and claims</td>
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<td>Payments to other funds</td>
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<td></td>
<td></td>
<td>(5,090)</td>
<td>(441)</td>
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<tr>
<td>Other receipts (payments)</td>
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<td></td>
<td></td>
<td>(20)</td>
<td>(26)</td>
</tr>
<tr>
<td>Net cash flows provided (used) by operating activities</td>
<td>(510)</td>
<td>10,974</td>
<td>18,968</td>
<td>(332)</td>
<td>(41)</td>
</tr>
</tbody>
</table>

| Cash Provided From (Used For)        |                               |                             |                       |                   |                    |
| Transfers from other funds           |                               |                             |                       |                   |                    |
| Transfers to other funds             |                               | (2)                        | (124)                 | (4)              |                    |
| Total cash provided (used for)       |                               | (2)                        | 896                   | 332              |                    |

| Cash Provided From (Used For)        |                               |                             |                       |                   |                    |
| Capital Financing Activities:        |                               |                             |                       |                   |                    |
| Acquisition and construction of capital assets |                               |                             |                       |                   |                    |
| Proceeds from the sale of capital assets |                             |                             |                       |                   |                    |
| Insurance recoveries                 |                               |                             |                       |                   |                    |
| Total cash provided (used for)       |                               |                             |                       |                   |                    |
| Capital financing activities         |                               |                             |                       |                   |                    |

| Cash Provided From (Used For)        |                               |                             |                       |                   |                    |
| Investment earnings                  |                               |                             |                       |                   |                    |
| Total cash provided (used for)       |                               |                             |                       |                   |                    |
| Investment activities                |                               |                             |                       |                   |                    |
| Net increase (decrease) in cash and cash equivalents | (510)                        | 11,888                     | (3,843)               | (41)             | 1,556              |
| Cash and cash equivalents at July 1   | 1,356                         | 20,066                     | 9,349                 |                   |                    |
| Cash and cash equivalents at June 30  | $ 646                         | $ 31,954                    | $ 5,506                | $                | $ 1,515            |

| Reconciliation of Operating Income to Net Cash Provided From (Used For) Operating Activities: |                               |                             |                       |                   |                    |
| Operating income (loss)               | $ (109)                       | $ 7,996                     | $ 985                 | $ (426)           | $ 325              |
| Adjustments to reconcile operating income to net cash flows from operating activities: |                               |                             |                       |                   |                    |
| Depreciation/amortization             |                               |                             |                       |                   |                    |
| Restatements and adjustments to cash  |                               |                             |                       |                   |                    |
| Nonoperating miscellaneous income (expense) |                               |                             |                       |                   |                    |
| (Increases) decreases in assets:      |                               |                             |                       |                   |                    |
| Receivables                          | 1,024                         | (135)                       | 788                   | (110)            | (209)              |
| Due from other funds                  | (1,425)                       |                             |                       |                   | (15)               |
| Due from fiduciary funds              |                               |                             |                       |                   |                    |
| Due from component units              |                               |                             |                       |                   |                    |
| Inventories                          |                               |                             |                       |                   | (6)                |
| Prepaid items                         |                               |                             |                       |                   | (101)              |
| Increases (decreases) in liabilities  |                               |                             |                       |                   |                    |
| Accounts payable and accrued liabilities |                               |                             |                       |                   |                    |
| Due to other funds                    |                               |                             |                       |                   |                    |
| Compensated absences                  |                               |                             |                       |                   |                    |
| Unearned revenue                      |                               |                             |                       |                   |                    |
| Total cash provided from (used for) operations | (510)                        | 10,974                     | 18,968                | (332)            | (41)               |

| Noncash Investing, Capital, and Financing Activities: |                               |                             |                       |                   |                    |
| Noncash distributions from the State Treasurer |                               |                             |                       |                   |                    |
| Long-Term Investment Portfolio and/or other agents |                               |                             |                       |                   |                    |
| Assets acquired through the assumption of a liability |                               |                             |                       |                   |                    |
| Change in fair value of investments |                               |                             |                       |                   |                    |
### Exhibit E-3

<table>
<thead>
<tr>
<th>Computing Services</th>
<th>Telecommunications Services</th>
<th>Surplus Property</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 1,226</td>
<td>$ 25,895</td>
<td>$ 357</td>
<td>$ 49,811</td>
</tr>
<tr>
<td>59,955</td>
<td>51,117</td>
<td>954</td>
<td>208,308</td>
</tr>
<tr>
<td>(36,530)</td>
<td>(82,710)</td>
<td>(172)</td>
<td>(168,832)</td>
</tr>
<tr>
<td>(17,956)</td>
<td>(11,133)</td>
<td>(1,433)</td>
<td>(45,012)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(1,169)</td>
</tr>
<tr>
<td>(2,998)</td>
<td>(1,143)</td>
<td>(745)</td>
<td>(11,157)</td>
</tr>
<tr>
<td>(111)</td>
<td>(24)</td>
<td>(301)</td>
<td>133</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3,988</td>
<td>1,993</td>
<td>(738)</td>
<td>34,282</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1,072</td>
<td>73</td>
<td></td>
<td>2,501</td>
</tr>
<tr>
<td>(16)</td>
<td>(10)</td>
<td>(4)</td>
<td>(160)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1,056</td>
<td>63</td>
<td>(4)</td>
<td>2,341</td>
</tr>
<tr>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>(5,917)</td>
<td>(875)</td>
<td>(6)</td>
<td>(32,763)</td>
</tr>
<tr>
<td>40</td>
<td>2</td>
<td>1</td>
<td>2,173</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td></td>
<td></td>
<td>132</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(5,873)</td>
<td>(873)</td>
<td>(5)</td>
<td>(30,458)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>916</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(849)</td>
<td>1,183</td>
<td>(747)</td>
<td>7,081</td>
</tr>
<tr>
<td>13,227</td>
<td>8,939</td>
<td>2,227</td>
<td>56,719</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>$ 12,378</td>
<td>$ 10,121</td>
<td>$ 1,480</td>
<td>$ 65,800</td>
</tr>
</tbody>
</table>

| $ 1,019           | $ (3,018)                   | $ (359)         | $ 6,413 |
| 7,011             | 2,204                       | 26              | 26,998  |
| (609)             | (2,758)                     |                 | (3,367) |
|                   |                             |                 | 2      |
| 2,535             | 3,462                       | (26)            | 7,327   |
| 4                 | 882                         | (198)           | (179)   |
| 1                 | (25)                        |                 | (24)    |
| 30                | (148)                       |                 | 52      |
| (18)              |                             |                 | (126)   |
| 432               | 1,312                       |                 | 1,744   |
|                   |                             |                 |         |
| (6,296)           | (76)                        | 14              | (8,390) |
| (406)             | 41                          | (219)           | (346)   |
| 265               | 117                         | 24              | 532     |
|                   |                             |                 |         |
|                   |                             |                 | 3,657   |
|                   |                             |                 |         |
| $ 3,968           | $ 1,993                     | (738)           | $ 34,282 |

| $                | $                            | $                | $ (1,143) |
| $                | $                            | $                | $ 39,109  |
| $                | $                            | $                | (1,710)   |
Fiduciary Funds
PRIVATE PURPOSE TRUST FUNDS

Private purpose trust funds account for resources held in trust in which the principal and income benefit individuals, private organizations, or other governments.

The following activities are included in the private purpose trust funds:

- Deposits of Insurance Carriers Fund
- Administrative Office of the Courts Trust Fund
- Departmental Funds
### COMBINING STATEMENT OF FIDUCIARY NET ASSETS
#### PRIVATE PURPOSE TRUST FUNDS

**June 30, 2006**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Assets</th>
<th>Deposits of Insurance Carriers Fund</th>
<th>Administrative Office of the Courts Trust Fund</th>
<th>Departmental Funds</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$429</td>
<td>$96,926</td>
<td>$359</td>
<td>$97,714</td>
</tr>
<tr>
<td>Investments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.S. Government securities</td>
<td>—</td>
<td>1,504</td>
<td>—</td>
<td>1,504</td>
</tr>
<tr>
<td>State and municipal securities</td>
<td>—</td>
<td>99</td>
<td>—</td>
<td>99</td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>—</td>
<td>65,497</td>
<td>—</td>
<td>65,497</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>368</td>
<td>—</td>
<td>308</td>
<td>676</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest receivable</td>
<td>1</td>
<td>—</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Sureties</td>
<td>988,443</td>
<td>—</td>
<td>—</td>
<td>988,443</td>
</tr>
<tr>
<td>Total Assets</td>
<td>989,241</td>
<td>164,086</td>
<td>668</td>
<td>1,153,995</td>
</tr>
</tbody>
</table>

| Liabilities                     |                                    |                                               |                    |         |
| Obligations under securities lending | 368                          | —                                             | 308                | 676     |
| Total Liabilities               | 368                                | —                                             | 308                | 676     |

| Net Assets                      |                                    |                                               |                    |         |
| Held in trust for:              |                                    |                                               |                    |         |
| Individuals, organizations and other governments | 988,873                 | 184,086                                       | 360                | 1,153,319 |
| Total Net Assets                | $988,873                          | $184,086                                      | $360               | $1,153,319 |
### COMBINING STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

**PRIVATE PURPOSE TRUST FUNDS**

*For the Fiscal Year Ended June 30, 2006*  
 *(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th>Deposits of Insurance Carriers Fund</th>
<th>Administrative Office of the Courts Trust Fund</th>
<th>Departmental Funds</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Additions:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contributions:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trustee deposits</td>
<td>$ 31,127</td>
<td>$ 106,595</td>
<td>$ 2</td>
<td>$ 137,724</td>
</tr>
<tr>
<td>Total contributions</td>
<td>31,127</td>
<td>106,595</td>
<td>2</td>
<td>137,724</td>
</tr>
<tr>
<td>Investment Income:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment earnings</td>
<td>28</td>
<td>3,158</td>
<td>24</td>
<td>3,210</td>
</tr>
<tr>
<td>Less investment expenses</td>
<td>(14)</td>
<td>—</td>
<td>(12)</td>
<td>(26)</td>
</tr>
<tr>
<td>Net investment income</td>
<td>14</td>
<td>3,158</td>
<td>12</td>
<td>3,184</td>
</tr>
<tr>
<td>Total additions</td>
<td>31,141</td>
<td>109,753</td>
<td>14</td>
<td>140,908</td>
</tr>
<tr>
<td><strong>Deductions:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payments in accordance with trust arrangements</td>
<td>8,696</td>
<td>106,149</td>
<td>—</td>
<td>114,845</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>6</td>
<td>—</td>
<td>—</td>
<td>6</td>
</tr>
<tr>
<td>Total deductions</td>
<td>8,702</td>
<td>106,149</td>
<td>—</td>
<td>114,851</td>
</tr>
<tr>
<td>Change in net assets</td>
<td>22,439</td>
<td>3,804</td>
<td>14</td>
<td>26,057</td>
</tr>
<tr>
<td>Net assets — July 1</td>
<td>968,434</td>
<td>160,482</td>
<td>346</td>
<td>1,127,262</td>
</tr>
<tr>
<td>Net assets — June 30</td>
<td>$ 988,873</td>
<td>$ 164,086</td>
<td>$ 360</td>
<td>$ 1,153,319</td>
</tr>
</tbody>
</table>

*Exhibit F-2*
AGENCY FUNDS

Agency funds account for resources held by the State in a purely custodial capacity for individuals, private organizations, or other governments.

The following activities are included in the agency funds:

- Local Sales Tax Collections
- Clerks of Court
- Intra-Entity Investment Fund Deposits
- Insurers in Receivership
- Other Agency Funds
## COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES

### AGENCY FUNDS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>Balance, July 1, 2005</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance, June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Local Sales Tax Collections</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$391,745</td>
<td>$2,912,601</td>
<td>$(2,890,697)</td>
<td>$413,649</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxes receivable</td>
<td>168,400</td>
<td>31,600</td>
<td></td>
<td>200,000</td>
</tr>
<tr>
<td>Due from other funds</td>
<td>10,447</td>
<td>2,377</td>
<td></td>
<td>12,824</td>
</tr>
<tr>
<td>Total Assets</td>
<td>$570,592</td>
<td>$2,946,578</td>
<td>$(2,890,697)</td>
<td>$626,473</td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable and accrued liabilities:</td>
<td>$570,592</td>
<td>$2,734,707</td>
<td>$(2,678,826)</td>
<td>$626,473</td>
</tr>
<tr>
<td>Intergovernmental payables</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>$570,592</td>
<td>$2,734,707</td>
<td>$(2,678,826)</td>
<td>$626,473</td>
</tr>
</tbody>
</table>

### Clerks of Court

<table>
<thead>
<tr>
<th></th>
<th>Balance, July 1, 2005</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance, June 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$85,736</td>
<td>$1,367,263</td>
<td>$(1,359,343)</td>
<td>$93,656</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>469</td>
<td>4,737</td>
<td></td>
<td>471</td>
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<tr>
<td>Supplies</td>
<td>82,588</td>
<td>48,481</td>
<td></td>
<td>86,901</td>
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<tr>
<td>Total Assets</td>
<td>$168,731</td>
<td>$1,420,461</td>
<td>$(1,408,184)</td>
<td>$181,028</td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable and accrued liabilities:</td>
<td>$5,879</td>
<td>$123,024</td>
<td>$(122,091)</td>
<td>$6,812</td>
</tr>
<tr>
<td>Intergovernmental payables</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Funds held for others</td>
<td>163,052</td>
<td>502,753</td>
<td></td>
<td>174,416</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>$168,731</td>
<td>$625,777</td>
<td></td>
<td>$181,028</td>
</tr>
</tbody>
</table>

### Intra-Entity Investment Fund Deposits

<table>
<thead>
<tr>
<th></th>
<th>Balance, July 1, 2005</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance, June 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$2,377,571</td>
<td></td>
<td></td>
<td>$1,989,387</td>
</tr>
<tr>
<td>Investments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Treasurer investment pool</td>
<td>46,274</td>
<td></td>
<td>(7,797)</td>
<td>38,477</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>1,879,210</td>
<td></td>
<td>(196,685)</td>
<td>1,722,525</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>$4,303,061</td>
<td></td>
<td></td>
<td>$3,750,395</td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Obligations under securities lending</td>
<td>$1,879,216</td>
<td></td>
<td>(156,685)</td>
<td>1,722,531</td>
</tr>
<tr>
<td>Funds held for others</td>
<td>2,433,845</td>
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<td>(395,881)</td>
<td>2,037,964</td>
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<td>Total Liabilities</td>
<td>$4,303,061</td>
<td></td>
<td></td>
<td>$3,750,395</td>
</tr>
</tbody>
</table>

### Insurers in Receivership

<table>
<thead>
<tr>
<th></th>
<th>Balance, July 1, 2005</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance, June 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$23,397</td>
<td></td>
<td>(1,220)</td>
<td>22,177</td>
</tr>
<tr>
<td>Investments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporate bonds</td>
<td>37,581</td>
<td>13,246</td>
<td></td>
<td>50,827</td>
</tr>
<tr>
<td>Corporate stocks</td>
<td>1,008</td>
<td></td>
<td></td>
<td>1,008</td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>12</td>
<td></td>
<td>(12)</td>
<td></td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>15,525</td>
<td></td>
<td>(12,895)</td>
<td>2,630</td>
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<td>Interest receivable</td>
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<td>131</td>
<td></td>
<td>287</td>
</tr>
<tr>
<td>Total Assets</td>
<td>$77,669</td>
<td>$13,377</td>
<td>(14,127)</td>
<td>$76,919</td>
</tr>
<tr>
<td><strong>Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Funds held for others</td>
<td>$77,669</td>
<td>$13,377</td>
<td>(14,127)</td>
<td>$76,919</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>$77,669</td>
<td>$13,377</td>
<td>(14,127)</td>
<td>$76,919</td>
</tr>
</tbody>
</table>
### COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES

#### AGENCY FUNDS

For the Fiscal Year Ended June 30, 2006

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th>Balance, July 1, 2005</th>
<th>Additions</th>
<th>Deductions</th>
<th>Balance, June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Other Agency Funds</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$21,651</td>
<td>$1,916,236</td>
<td>($1,913,700)</td>
<td>$24,187</td>
</tr>
<tr>
<td>Investments:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>467</td>
<td>—</td>
<td>—</td>
<td>467</td>
</tr>
<tr>
<td>Securities lending collateral</td>
<td>12,713</td>
<td>1,988</td>
<td>—</td>
<td>14,681</td>
</tr>
<tr>
<td>Receivables:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>11</td>
<td>112</td>
<td>—</td>
<td>123</td>
</tr>
<tr>
<td>Interest receivable</td>
<td>1</td>
<td>—</td>
<td>—</td>
<td>1</td>
</tr>
<tr>
<td>Due from other funds</td>
<td>47</td>
<td>—</td>
<td>—</td>
<td>47</td>
</tr>
<tr>
<td>Inventories</td>
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<tr>
<td>Accounts payable and accrued liabilities:</td>
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<tr>
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<td>$7,953</td>
<td>($7,498)</td>
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<tr>
<td>Deposits payable</td>
<td>1,590</td>
<td>3,857</td>
<td>(3,765)</td>
<td>1,682</td>
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<td>Funds held for others</td>
<td>14,254</td>
<td>96,704</td>
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<td><strong>Total Liabilities</strong></td>
<td>$35,191</td>
<td>$254,791</td>
<td>($250,175)</td>
<td>$39,807</td>
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</tbody>
</table>

| **Total Agency Funds**        |                       |           |            |                        |
| **Assets**                    |                       |           |            |                        |
| Cash and cash equivalents     | $2,900,090            | $6,196,100| ($6,553,144)| $2,543,046            |
| Investments:                  |                       |           |            |                        |
| Corporate bonds               | 37,581                | 13,246    | —          | 50,827                |
| Corporate stocks              | 1,008                 | —         | —          | 1,008                 |
| Certificates of deposit       | 479                   | —         | (12)       | 467                   |
| State Treasurer investment pool| 46,274               | —         | (7,797)    | 38,477                |
| Securities lending collateral | 1,891,529            | 1,968     | (155,685)  | 1,737,212            |
| Receivables:                  |                       |           |            |                        |
| Taxes receivable              | 168,400               | 31,600    | —          | 200,000               |
| Accounts receivable           | 15,025                | 4,649     | (17,650)   | 3,224                 |
| Interest receivable           | 157                   | 131       | —          | 288                   |
| Due from other funds          | 10,494                | 2,377     | —          | 12,871                |
| Inventories                   | 301                   | —         | —          | 301                   |
| Surpluses                     | 22,506                | 48,481    | (44,098)   | 26,889                |
| **Total Assets**              | $5,155,244            | $6,298,752| ($6,779,374)| $4,674,622            |
| **Liabilities**               |                       |           |            |                        |
| Accounts payable and accrued liabilities: |           |           |            |                        |
| Accounts payable              | $486                  | $7,953    | ($7,498)   | $941                  |
| Intergovernmental payables    | 682,419               | 3,002,040 | (2,945,226)| 639,233               |
| Obligations under securities lending | 1,891,529          | 1,968     | (155,685)  | 1,737,212            |
| Deposits payable              | 1,590                 | 3,857     | (3,765)    | 1,682                 |
| Funds held for others         | 2,678,820             | 612,834   | (996,100)  | 2,295,554             |
| **Total Liabilities**         | $5,155,244            | $3,628,952| ($4,109,274)| $4,674,622            |
COMPONENT UNITS
NONMAJOR COMPONENT UNITS – DISCRETELY PRESENTED

Component units are legally separate entities for which the State is financially accountable. Accountability is defined as the State’s substantive appointment of a majority of the component unit’s governing board. Furthermore, the State must be able to impose its will upon the component unit or there must be a possibility that the component unit may provide specific benefits to, or impose specific financial burdens on the State. The State has applied the criteria outlined in GASB Statement No. 14, The Financial Reporting Entity, in determining financial accountability. These component units are included in the financial reporting entity because of the significance of their operational or financial relationships with the State.

Nonmajor component units are comprised of the following entities:

- N.C. State Ports Authority
- N.C. Agricultural Finance Authority
- N.C. Global TransPark Authority
- N.C. Partnership for Children, Inc.
- Regional Economic Development Commissions
- North Carolina Railroad Company
- N.C. Phase II Tobacco Certification Entity, Inc.
- N.C. Turnpike Authority
## COMBINING STATEMENT OF NET ASSETS
### NONMAJOR COMPONENT UNITS

**June 30, 2006**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th>N.C. State Ports Authority</th>
<th>N.C. Agricultural Finance Authority</th>
<th>N.C. Global TransPark Authority</th>
<th>N.C. Partnership for Children, Inc.</th>
<th>Regional Economic Development Commissions</th>
<th>North Carolina Railroad Company</th>
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<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
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</tr>
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<td>Cash and cash equivalents</td>
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<td>$ 3,950</td>
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<td>4,307</td>
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<td>427</td>
<td>109</td>
<td>4,776</td>
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<td>360</td>
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<td>—</td>
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<td>Notes receivable, net</td>
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<tr>
<td>Deferred charges</td>
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<td>—</td>
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<tr>
<td>Capital assets-nondepreciable</td>
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<td>14,224</td>
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<td>55,104</td>
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<td>20,228</td>
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<td><strong>9,574</strong></td>
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<td><strong>87,581</strong></td>
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<td><strong>Liabilities</strong></td>
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<td>Accounts payable and accrued liabilities</td>
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<td>8,730</td>
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<tr>
<td>Advance from primary government</td>
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<td>Funds held for others</td>
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<td>Due within one year</td>
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<td>2</td>
<td>64</td>
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<td><strong>1,719</strong></td>
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<td><strong>Net Assets</strong></td>
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<td><strong>7,855</strong></td>
<td><strong>3,432</strong></td>
<td><strong>66,127</strong></td>
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</tr>
<tr>
<td>683</td>
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<td>125,854</td>
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<td>$ 3,107</td>
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<td>$ 5,798</td>
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<td>$ 32</td>
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<td>(3,915)</td>
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### COMBINING STATEMENT OF ACTIVITIES
#### NONMAJOR COMPONENT UNITS

For the Fiscal Year Ended June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th>N.C. State Ports Authority</th>
<th>N.C. Agricultural Finance Authority</th>
<th>N.C. Global TransPark Authority</th>
<th>N.C. Partnership for Children, Inc.</th>
<th>Regional Economic Development Commissions</th>
<th>North Carolina Railroad Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total expenses</td>
<td>$ 39,536</td>
<td>$ 823</td>
<td>$ 7,566</td>
<td>$ 120,033</td>
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<td>Charges for services</td>
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<td>1,195</td>
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<td>13,217</td>
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<td>774</td>
<td>6,309</td>
<td>1,662</td>
<td>925</td>
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<td>Capital grants and contributions</td>
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<td>-</td>
<td>-</td>
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<td>(113,724)</td>
<td>(4,208)</td>
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<td>Non-tax general revenues:</td>
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<td>1,600</td>
<td>118,550</td>
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<td>118,554</td>
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<td>Change in net assets</td>
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<td>4,630</td>
<td>(226)</td>
<td>10,544</td>
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<tr>
<td>Net assets — June 30</td>
<td>$ 166,437</td>
<td>$ 16,701</td>
<td>$ 57,246</td>
<td>$ 7,855</td>
<td>$ 3,432</td>
<td>$ 56,127</td>
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<tr>
<td>N.C. Phase II Tobacco Certification Entity, Inc.</td>
<td>N.C. Turnpike Authority</td>
<td>Total</td>
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<tr>
<td>-----------------------------------------------</td>
<td>-------------------------</td>
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<tr>
<td>$ 1,641</td>
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<td>2,276</td>
<td>(3,851)</td>
<td>(117,343)</td>
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<tr>
<td>2,276</td>
<td>(3,851)</td>
<td>35,115</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>209</td>
<td>(64)</td>
<td>283,247</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>$ 2,485</td>
<td>$ (3,915)</td>
<td>$ 318,362</td>
<td></td>
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</tr>
</tbody>
</table>
STATISTICAL SECTION
Index to Statistical Section

This part of the State of North Carolina's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the State's overall financial health.

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<td></td>
</tr>
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</tr>
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Sources: Unless otherwise noted, the information in these schedules is derived from the comprehensive annual financial report for the relevant year.
## NET ASSETS BY COMPONENT

### Fiscal Years 2002-2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Governmental activities:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Invested in capital assets, net of related debt</td>
<td>$28,035,283</td>
<td>$26,434,617</td>
<td>$24,706,355</td>
<td>$23,449,373</td>
<td>$22,025,039</td>
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<tr>
<td>Restricted</td>
<td>890,602</td>
<td>1,314,397</td>
<td>1,474,405</td>
<td>1,071,626</td>
<td>1,604,772</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>(1,491,985)</td>
<td>(3,839,972)</td>
<td>(3,196,354)</td>
<td>(2,210,477)</td>
<td>(1,615,102)</td>
</tr>
<tr>
<td><strong>Total governmental activities net assets</strong></td>
<td>$27,433,900</td>
<td>$23,909,042</td>
<td>$22,981,406</td>
<td>$22,310,522</td>
<td>$22,014,709</td>
</tr>
</tbody>
</table>

| **Business-type activities:** |          |          |          |          |          |
| Invested in capital assets, net of related debt | $44,196   | $44,007  | $40,277  | $38,450  | $38,267  |
| Restricted            | 1,286,477 | 970,615  | 665,547  | 863,426  | 797,437  |
| Unrestricted          | 80,002   | 76,988   | 48,295   | 56,448   | 50,479   |
| **Total business-type activities net assets** | $1,410,675 | $1,091,610 | $754,119 | $958,324 | $886,183 |

| **Primary government:** |          |          |          |          |          |
| Invested in capital assets, net of related debt | $28,079,479 | $26,478,624 | $24,746,632 | $23,487,823 | $22,063,306 |
| Restricted            | 2,177,079 | 2,285,012 | 2,139,952 | 1,935,052 | 2,402,209 |
| Unrestricted          | (1,411,983) | (3,762,954) | (3,151,059) | (2,154,029) | (1,564,623) |
| **Total primary government net assets** | $28,844,575 | $25,000,652 | $23,735,525 | $23,268,846 | $22,900,892 |

**Note:** The State of North Carolina did not begin reporting government-wide statements until implementation of GASB Statement 34 in 2002.

---

[1] For fiscal year ended June 30, 2006, the State changed its methodology for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions to individual income taxes. The State now reports an estimate of underpayments of individual income taxes. The State has also changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds). For the purpose of reporting underpayments, the availability period for General Fund individual income taxes was extended from thirty-one days to twelve months after year-end. Where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).
## Changes in Net Assets

### Fiscal Years 2002-2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Governmental activities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General government</td>
<td>$ 1,039,513</td>
<td>$ 917,209</td>
<td>$ 807,248</td>
<td>$ 773,835</td>
<td>$ 874,206</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>$ 8,215,445</td>
<td>7,698,208</td>
<td>7,223,766</td>
<td>6,865,921</td>
<td>6,802,979</td>
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<tr>
<td>Higher education</td>
<td>3,472,024</td>
<td>3,578,384</td>
<td>3,140,786</td>
<td>2,814,375</td>
<td>2,519,703</td>
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<td>Health and human services</td>
<td>13,491,119</td>
<td>13,375,794</td>
<td>11,729,904</td>
<td>10,814,411</td>
<td>10,376,807</td>
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<tr>
<td>Economic development</td>
<td>647,434</td>
<td>625,561</td>
<td>536,055</td>
<td>489,062</td>
<td>469,102</td>
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<td>Environment and natural resources</td>
<td>676,049</td>
<td>570,241</td>
<td>599,575</td>
<td>537,540</td>
<td>627,369</td>
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<tr>
<td>Public safety, corrections, and regulation</td>
<td>2,304,900</td>
<td>2,125,385</td>
<td>2,093,404</td>
<td>2,034,225</td>
<td>2,109,487</td>
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<tr>
<td>Transportation</td>
<td>1,781,865</td>
<td>1,795,490</td>
<td>1,870,578</td>
<td>1,639,866</td>
<td>1,530,870</td>
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<tr>
<td>Agriculture</td>
<td>112,467</td>
<td>111,028</td>
<td>82,394</td>
<td>73,972</td>
<td>121,729</td>
</tr>
<tr>
<td>Interest on long-term debt</td>
<td>264,287</td>
<td>249,433</td>
<td>191,228</td>
<td>151,258</td>
<td>148,585</td>
</tr>
<tr>
<td>Total governmental activities expenses</td>
<td>$32,005,103</td>
<td>$31,016,333</td>
<td>$28,274,846</td>
<td>$25,994,465</td>
<td>$25,580,849</td>
</tr>
<tr>
<td>Business-type activities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unemployment compensation</td>
<td>849,945</td>
<td>824,934</td>
<td>1,389,266</td>
<td>1,603,796</td>
<td>1,336,718</td>
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<td>N.C. State Lottery</td>
<td>153,125</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>EPA revolving loan</td>
<td>11,414</td>
<td>7,170</td>
<td>5,342</td>
<td>4,268</td>
<td>-</td>
</tr>
<tr>
<td>Regulatory commissions</td>
<td>28,526</td>
<td>-</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Insurance programs</td>
<td>16,051</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>North Carolina State Fair</td>
<td>10,497</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Other business-type activities</td>
<td>10,255</td>
<td>60,066</td>
<td>43,014</td>
<td>30,757</td>
<td>25,431</td>
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<tr>
<td>Total business-type activities expenses</td>
<td>$1,079,813</td>
<td>$892,170</td>
<td>$1,437,622</td>
<td>$1,638,819</td>
<td>$1,362,149</td>
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<tr>
<td>Total primary government expenses</td>
<td>$33,084,916</td>
<td>$31,108,503</td>
<td>$29,712,568</td>
<td>$27,833,284</td>
<td>$26,942,988</td>
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### Program Revenues:

<table>
<thead>
<tr>
<th>Governmental activities:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charges for services:</td>
</tr>
<tr>
<td>Transportation</td>
</tr>
<tr>
<td>Public safety, corrections, and regulation</td>
</tr>
<tr>
<td>General government</td>
</tr>
<tr>
<td>Other activities</td>
</tr>
<tr>
<td>Operating grants and contributions</td>
</tr>
<tr>
<td>Capital grants and contributions</td>
</tr>
<tr>
<td>Total governmental activities program revenues</td>
</tr>
<tr>
<td>Business-type activities:</td>
</tr>
<tr>
<td>Charges for services:</td>
</tr>
<tr>
<td>Unemployment compensation</td>
</tr>
<tr>
<td>N.C. State Lottery</td>
</tr>
<tr>
<td>EPA revolving loan</td>
</tr>
<tr>
<td>Regulatory commissions</td>
</tr>
<tr>
<td>Insurance programs</td>
</tr>
<tr>
<td>North Carolina State Fair</td>
</tr>
<tr>
<td>Other business-type activities</td>
</tr>
<tr>
<td>Operating grants and contributions</td>
</tr>
<tr>
<td>Capital grants and contributions</td>
</tr>
<tr>
<td>Total business-type activities program revenues</td>
</tr>
<tr>
<td>Total primary government program revenues</td>
</tr>
</tbody>
</table>

### Net (Expense) Revenue:

|Governmental activities: | $ (17,599,168) | $ (16,951,536) | $ (15,777,367) | $ (15,073,154) | $ (14,766,552) |
|Business-type activities: | 386,994 | 309,018 | (204,786) | (444,511) | (461,427) |
|Total primary government net expense | $ (17,212,174) | $ (16,642,518) | $ (15,982,173) | $ (15,517,665) | $ (15,227,979) |
### General Revenues and Other Changes in Net Assets

#### Governmental activities:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Taxes</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income tax</td>
<td>$9,336,745</td>
<td>$8,244,275</td>
<td>$7,407,455</td>
<td>$7,122,099</td>
<td>$7,234,431</td>
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<tr>
<td>Corporate income tax</td>
<td>1,306,193</td>
<td>1,143,458</td>
<td>760,180</td>
<td>921,611</td>
<td>599,382</td>
</tr>
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<td>Sales and use tax</td>
<td>5,033,040</td>
<td>4,621,096</td>
<td>4,293,040</td>
<td>4,029,403</td>
<td>3,778,873</td>
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<td>Gasoline tax</td>
<td>1,514,626</td>
<td>1,354,699</td>
<td>1,276,627</td>
<td>1,154,986</td>
<td>1,212,786</td>
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<tr>
<td>Franchise tax</td>
<td>628,029</td>
<td>613,033</td>
<td>560,708</td>
<td>584,584</td>
<td>590,992</td>
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<td>Highway use tax</td>
<td>577,237</td>
<td>580,118</td>
<td>578,346</td>
<td>552,759</td>
<td>555,320</td>
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<td>Insurance tax</td>
<td>442,297</td>
<td>442,228</td>
<td>432,975</td>
<td>417,126</td>
<td>347,893</td>
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<tr>
<td>Beverage tax</td>
<td>233,315</td>
<td>220,782</td>
<td>213,271</td>
<td>198,848</td>
<td>200,593</td>
</tr>
<tr>
<td>Inheritance tax</td>
<td>133,156</td>
<td>135,107</td>
<td>128,352</td>
<td>112,150</td>
<td>106,491</td>
</tr>
<tr>
<td>Other tax</td>
<td>482,552</td>
<td>306,991</td>
<td>313,985</td>
<td>289,261</td>
<td>278,740</td>
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<tr>
<td>Tobacco settlement</td>
<td>140,969</td>
<td>148,800</td>
<td>147,224</td>
<td>173,256</td>
<td>175,836</td>
</tr>
<tr>
<td>Federal grants not restricted to specific programs</td>
<td>-</td>
<td>-</td>
<td>136,859</td>
<td>136,859</td>
<td>139,350</td>
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<tr>
<td>Unrestricted investment earnings</td>
<td>123,170</td>
<td>78,546</td>
<td>77,225</td>
<td>103,987</td>
<td>-</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>37,248</td>
<td>53,498</td>
<td>62,601</td>
<td>41,137</td>
<td>57,484</td>
</tr>
<tr>
<td>Contributions to permanent funds</td>
<td>4,674</td>
<td>2,288</td>
<td>2,068</td>
<td>1,806</td>
<td>2,019</td>
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<tr>
<td>Transfers</td>
<td>67,978</td>
<td>(11,820)</td>
<td>(302)</td>
<td>4,918</td>
<td>47,957</td>
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<tr>
<td><strong>Total governmental activities</strong></td>
<td>20,061,231</td>
<td>17,933,291</td>
<td>16,390,814</td>
<td>15,844,790</td>
<td>15,328,149</td>
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</table>

#### Business-type activities:

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
<th>2004</th>
<th>2003</th>
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<td>Miscellaneous</td>
<td>4</td>
<td>79</td>
<td>3</td>
<td>-</td>
</tr>
<tr>
<td>Transfers</td>
<td>(67,978)</td>
<td>11,820</td>
<td>302</td>
<td>(4,918)</td>
</tr>
<tr>
<td><strong>Total business-type activities</strong></td>
<td>(67,974)</td>
<td>11,899</td>
<td>305</td>
<td>(4,918)</td>
</tr>
<tr>
<td><strong>Total primary government</strong></td>
<td>$19,993,257</td>
<td>$17,944,990</td>
<td>$16,390,919</td>
<td>$15,839,872</td>
</tr>
</tbody>
</table>

#### Change in Net Assets

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Governmental activities</td>
<td>$2,462,063</td>
<td>$981,755</td>
<td>$613,227</td>
<td>$771,636</td>
<td>$561,597</td>
</tr>
<tr>
<td>Business-type activities</td>
<td>319,920</td>
<td>320,717</td>
<td>(204,481)</td>
<td>(449,429)</td>
<td>(509,384)</td>
</tr>
<tr>
<td><strong>Total primary government</strong></td>
<td>$2,781,983</td>
<td>$1,302,472</td>
<td>$408,746</td>
<td>$322,207</td>
<td>$52,213</td>
</tr>
</tbody>
</table>

Note: The State of North Carolina did not begin reporting government-wide statements until implementation of GASB Statement 34 in 2002.

[1] For fiscal year ended June 30, 2006, the State changed its methodology for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions to individual income taxes. The State now reports an estimate of underpayments of individual income taxes. The State has also changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds). For the purpose of reporting underpayments, the availability period for General Fund individual income taxes was extended from thirty-one days to twelve months after year-end. Where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).
# FUND BALANCES OF GOVERNMENTAL FUNDS

**Table 3**

_Fiscal Years 2002-2006_  
(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>General Fund</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reserved</td>
<td>$155,418</td>
<td>$172,633</td>
<td>$197,448</td>
<td>$166,172</td>
<td>$227,767</td>
</tr>
<tr>
<td>Unreserved</td>
<td>$1,769,760</td>
<td>(251,442)</td>
<td>(393,735)</td>
<td>(333,127)</td>
<td>(578,318)</td>
</tr>
<tr>
<td>Total General Fund</td>
<td>$1,925,176</td>
<td>(78,809)</td>
<td>(196,267)</td>
<td>(166,555)</td>
<td>(348,551)</td>
</tr>
<tr>
<td><strong>All Other Governmental Funds</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reserved</td>
<td>$961,136</td>
<td>$911,966</td>
<td>$847,174</td>
<td>$672,653</td>
<td>$1,099,039</td>
</tr>
<tr>
<td>Unreserved, reported in:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Special revenue funds</td>
<td>$2,232,200</td>
<td>$2,170,533</td>
<td>$2,260,374</td>
<td>$2,041,905</td>
<td>$2,254,227</td>
</tr>
<tr>
<td>Capital projects funds</td>
<td>113,433</td>
<td>44,237</td>
<td>110,395</td>
<td>84,677</td>
<td>73,751</td>
</tr>
<tr>
<td>Permanent funds</td>
<td>1,518</td>
<td>2,645</td>
<td>2,380</td>
<td>6,903</td>
<td>226</td>
</tr>
<tr>
<td>Total all other governmental funds</td>
<td>$3,308,287</td>
<td>$3,129,381</td>
<td>$3,220,323</td>
<td>$2,806,138</td>
<td>$3,427,243</td>
</tr>
</tbody>
</table>

Note: Due to changes in the State's fund structure initiated when GASB Statement 34 was implemented, the changes in fund balance information is not available before 2002.

---

[1] For fiscal year ended June 30, 2006, the State changed its methodology for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions to individual income taxes. The State now reports an estimate of underpayments of individual income taxes. The State has also changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds). For the purpose of reporting underpayments, the availability period for General Fund individual income taxes was extended from thirty-one days to twelve months after year-end. Where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).
## CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS

**Fiscal Years 1997-2006**

(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Taxes...</td>
<td>$19,048,465</td>
<td>$17,518,730</td>
<td>$15,961,029</td>
<td>$15,394,024</td>
<td>$14,994,790</td>
</tr>
<tr>
<td>Federal funds</td>
<td>11,315,722</td>
<td>11,287,454</td>
<td>10,089,075</td>
<td>8,672,065</td>
<td>8,459,344</td>
</tr>
<tr>
<td>Local funds</td>
<td>610,501</td>
<td>767,087</td>
<td>657,954</td>
<td>586,638</td>
<td>702,076</td>
</tr>
<tr>
<td>Investment earnings</td>
<td>384,014</td>
<td>292,406</td>
<td>160,846</td>
<td>320,023</td>
<td>335,082</td>
</tr>
<tr>
<td>Interest earnings on loans</td>
<td>5,405</td>
<td>5,664</td>
<td>5,801</td>
<td>7,165</td>
<td>47,421</td>
</tr>
<tr>
<td>Sales and services</td>
<td>260,538</td>
<td>235,894</td>
<td>210,161</td>
<td>184,739</td>
<td>194,548</td>
</tr>
<tr>
<td>Rental and lease of property</td>
<td>25,982</td>
<td>38,585</td>
<td>27,848</td>
<td>22,175</td>
<td>24,359</td>
</tr>
<tr>
<td>Fees, licenses and fines</td>
<td>1,405,569</td>
<td>1,218,431</td>
<td>1,035,303</td>
<td>915,380</td>
<td>864,912</td>
</tr>
<tr>
<td>Tobacco settlement</td>
<td>136,453</td>
<td>148,641</td>
<td>146,452</td>
<td>173,256</td>
<td>175,836</td>
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<tr>
<td>Contributions, gifts, and grants</td>
<td>118,936</td>
<td>108,450</td>
<td>150,731</td>
<td>90,486</td>
<td>93,802</td>
</tr>
<tr>
<td>Funds escheated</td>
<td>108,075</td>
<td>49,684</td>
<td>55,330</td>
<td>41,369</td>
<td>90,181</td>
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<tr>
<td>Federal funds for fiscal relief</td>
<td>—</td>
<td>—</td>
<td>136,859</td>
<td>136,859</td>
<td>N/A</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>161,052</td>
<td>146,529</td>
<td>196,837</td>
<td>147,777</td>
<td>145,867</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>34,380,712</strong></td>
<td><strong>31,917,535</strong></td>
<td><strong>28,834,526</strong></td>
<td><strong>26,891,956</strong></td>
<td><strong>26,028,244</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Current:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>General government</td>
<td>963,899</td>
<td>754,175</td>
<td>711,327</td>
<td>691,287</td>
<td>809,398</td>
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<tr>
<td>Education</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
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<tr>
<td>Primary and secondary education</td>
<td>8,211,998</td>
<td>7,713,265</td>
<td>7,223,143</td>
<td>6,863,338</td>
<td>6,802,662</td>
</tr>
<tr>
<td>Higher education</td>
<td>3,471,604</td>
<td>3,576,766</td>
<td>3,140,698</td>
<td>2,813,629</td>
<td>2,519,624</td>
</tr>
<tr>
<td>Health and human services</td>
<td>13,318,071</td>
<td>13,376,364</td>
<td>11,722,721</td>
<td>10,583,184</td>
<td>10,398,398</td>
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<tr>
<td>Economic development</td>
<td>643,510</td>
<td>822,000</td>
<td>532,674</td>
<td>484,298</td>
<td>498,644</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>626,442</td>
<td>579,853</td>
<td>581,726</td>
<td>534,405</td>
<td>574,871</td>
</tr>
<tr>
<td>Public safety, corrections, and regulation</td>
<td>2,291,595</td>
<td>2,123,837</td>
<td>2,073,338</td>
<td>1,998,576</td>
<td>2,070,166</td>
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<tr>
<td>Transportation</td>
<td>3,219,549</td>
<td>3,511,161</td>
<td>3,389,042</td>
<td>2,967,551</td>
<td>2,992,197</td>
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<tr>
<td>Agriculture</td>
<td>110,626</td>
<td>82,508</td>
<td>81,488</td>
<td>81,857</td>
<td>122,337</td>
</tr>
<tr>
<td>Retiree tax judgments</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
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<tr>
<td>Capital outlay</td>
<td>270,882</td>
<td>313,932</td>
<td>385,506</td>
<td>104,379</td>
<td>126,011</td>
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<tr>
<td>Debt service:</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Principal</td>
<td>367,946</td>
<td>303,818</td>
<td>235,792</td>
<td>168,009</td>
<td>180,398</td>
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<tr>
<td>Interest</td>
<td>288,088</td>
<td>241,935</td>
<td>185,350</td>
<td>152,110</td>
<td>147,580</td>
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<tr>
<td>Debt issuance cost</td>
<td>1,845</td>
<td>7,454</td>
<td>4,830</td>
<td>1,410</td>
<td>734</td>
</tr>
<tr>
<td><strong>Total expenditures</strong></td>
<td><strong>33,785,856</strong></td>
<td><strong>33,207,069</strong></td>
<td><strong>30,267,635</strong></td>
<td><strong>27,444,013</strong></td>
<td><strong>27,242,998</strong></td>
</tr>
<tr>
<td>Excess revenues over (under) expenditures</td>
<td>594,856</td>
<td>(1,289,534)</td>
<td>(1,432,709)</td>
<td>(752,057)</td>
<td>(1,214,754)</td>
</tr>
</tbody>
</table>

### Other Financing Sources (Uses)

<table>
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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Bonds issued</td>
<td>370,000</td>
<td>1,075,140</td>
<td>1,377,560</td>
<td>711,600</td>
<td>605,000</td>
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<tr>
<td>Certificates of participation issued</td>
<td>—</td>
<td>188,385</td>
<td>258,855</td>
<td>17,500</td>
<td>—</td>
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<tr>
<td>Refunding bonds issued</td>
<td>—</td>
<td>959,665</td>
<td>326,710</td>
<td>598,350</td>
<td>—</td>
</tr>
<tr>
<td>Other debt issued</td>
<td>30,688</td>
<td>12,686</td>
<td>17,997</td>
<td>—</td>
<td>4,832</td>
</tr>
<tr>
<td>Premium on debt issued</td>
<td>16,338</td>
<td>210,116</td>
<td>137,256</td>
<td>25,017</td>
<td>14,733</td>
</tr>
<tr>
<td>Discount on debt issued</td>
<td>—</td>
<td>(264)</td>
<td>—</td>
<td>—</td>
<td>—</td>
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<tr>
<td>Payments to refunded bond escrow agent</td>
<td>—</td>
<td>(1,059,663)</td>
<td>(348,915)</td>
<td>(558,444)</td>
<td>—</td>
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<tr>
<td>Capital leases</td>
<td>26,745</td>
<td>212</td>
<td>—</td>
<td>150</td>
<td>216</td>
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<tr>
<td>Sale of capital assets</td>
<td>20,131</td>
<td>14,674</td>
<td>10,105</td>
<td>8,882</td>
<td>12,570</td>
</tr>
<tr>
<td>Insurance recoveries</td>
<td>8,537</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
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<tr>
<td>Total other financing sources (uses)</td>
<td>538,076</td>
<td>1,394,662</td>
<td>1,815,580</td>
<td>765,114</td>
<td>701,241</td>
</tr>
<tr>
<td>Net change in fund balances</td>
<td>$1,130,932</td>
<td>$105,328</td>
<td>$382,871</td>
<td>$13,057</td>
<td>$(513,513)</td>
</tr>
</tbody>
</table>

Debt service as a percentage of noncapital expenditures... 2.07% 1.80% 1.53% 1.26% 1.30%

All governmental fund types consist of the General Fund, special revenue funds, capital projects funds, and permanent funds. Years prior to 2002 do not include permanent funds.
Table 4

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>$</td>
<td>15,147,177</td>
<td>$ 14,599,104</td>
<td>$13,871,577</td>
<td>$ 13,287,609</td>
<td>$ 12,177,605</td>
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<tr>
<td></td>
<td>7,924,893</td>
<td>7,253,282</td>
<td>6,297,196</td>
<td>5,983,003</td>
<td>5,857,680</td>
</tr>
<tr>
<td></td>
<td>760,507</td>
<td>511,350</td>
<td>469,539</td>
<td>462,879</td>
<td>427,306</td>
</tr>
<tr>
<td></td>
<td>487,924</td>
<td>500,854</td>
<td>529,028</td>
<td>575,901</td>
<td>454,678</td>
</tr>
<tr>
<td></td>
<td>5,789</td>
<td>5,356</td>
<td>6,665</td>
<td>5,676</td>
<td>4,280</td>
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<tr>
<td></td>
<td>97,886</td>
<td>94,751</td>
<td>92,237</td>
<td>84,087</td>
<td>76,130</td>
</tr>
<tr>
<td></td>
<td>4,046</td>
<td>25,059</td>
<td>25,913</td>
<td>26,321</td>
<td>24,738</td>
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<td></td>
<td>896,435</td>
<td>1,046,042</td>
<td>895,892</td>
<td>828,491</td>
<td>814,690</td>
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<tr>
<td></td>
<td>140,272</td>
<td>—</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>122,871</td>
<td>79,554</td>
<td>71,787</td>
<td>61,169</td>
<td>31,805</td>
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<td></td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>165,349</td>
<td>147,616</td>
<td>172,103</td>
<td>146,794</td>
<td>182,247</td>
</tr>
<tr>
<td></td>
<td>25,791,949</td>
<td>24,233,168</td>
<td>22,379,937</td>
<td>21,461,950</td>
<td>20,051,159</td>
</tr>
</tbody>
</table>

1,035,440  | 1,229,513  | 1,039,855  | 1,115,763  | 921,406    |
9,664,812  | 6,674,757  | 6,253,838  | 5,416,468  | 4,775,741  |
N/A        | N/A        | N/A        | N/A        | N/A        |
N/A        | N/A        | N/A        | N/A        | N/A        |
9,617,423  | 8,411,025  | 7,665,461  | 7,300,262  | 6,822,624  |
453,931    | 428,819    | 370,124    | 321,613    | 294,787    |
459,170    | 371,238    | 354,025    | 332,803    | 368,402    |
1,948,423  | 1,999,894  | 1,670,703  | 1,578,985  | 1,613,757  |
2,820,290  | 2,598,605  | 2,508,886  | 2,384,455  | 2,205,494  |
88,623     | 143,936    | 72,562     | 68,573     | 65,421     |
58,579     | 440,000    | 399,000    | 400,000    | —          |
155,228    | 159,241    | 182,793    | 203,605    | 147,194    |
151,120    | 141,934    | 123,952    | 91,585     | 82,710     |
130,343    | 122,943    | 103,878    | 78,454     | 48,539     |
N/A        | N/A        | N/A        | N/A        | N/A        |
23,883,462 | 22,721,905 | 20,744,877 | 19,292,584 | 17,646,075 |
1,908,467  | 1,511,283  | 1,634,060  | 2,169,366  | 2,405,084  |
680,000    | 200,000    | 450,056    | 700,000    | 645,000    |
—         | —         | 26,182     | —          | —          |
—         | —         | —          | —          | —          |
—         | —         | —          | —          | —          |
—         | —         | (26,182)   | —          | —          |
—         | 339       | 841        | —          | 247        |
—         | —         | —          | —          | —          |
1,415,317  | 1,573,875  | 1,273,470  | 1,215,549  | 1,205,077  |
(1,427,607) | (1,576,900) | (1,307,966) | (1,217,753) | (1,190,085) |
667,710    | 197,234    | 416,370    | 697,796    | 3,040,409  |
$ 2,576,177 | $ 1,708,497 | $ 2,050,430 | $ 2,867,162 | $ 5,445,493 |
1.26%      | 1.24%      | 1.17%      | 0.94%      | 0.79%      |

[1] For fiscal years prior to 1998, health expenditures were included in the environment, health and natural resources expenditure function. In the 1998 fiscal year, health expenditures were shifted and are now reflected in the health and human services function.


[3] Fiscal years prior to 2001 do not reflect the implementation of GASB Statement No. 33, Accounting for Nonexchange Transactions. This statement provided new rules on the timing of recognition of nonexchange transactions involving financial or capital resources.

[4] Fiscal years prior to 2002 do not reflect the implementation of GASB - Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments (as amended by Statement No. 37). This statement establishes new financial reporting requirements for state and local governments throughout the United States.

[5] For fiscal year ended June 30, 2006, the State changed its methodology for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions to individual income taxes. The State now reports an estimate of underpayments of individual income taxes. The State has also changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds). For the purpose of reporting underpayments, the availability period for General Fund individual income taxes was extended from thirty-one days to twelve months after year-end. Where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).
# SCHEDULE OF REVENUES BY SOURCE — GENERAL FUND 
GAAP BASIS

**Fiscal Years 1997-2006**  
(Dollars in Thousands)

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>TAX REVENUES</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individual income tax</td>
<td>$9,493,714</td>
<td>$8,206,026</td>
<td>$7,404,956</td>
<td>$7,126,655</td>
<td>$7,219,794</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>1,208,356</td>
<td>1,065,374</td>
<td>699,441</td>
<td>922,936</td>
<td>548,046</td>
</tr>
<tr>
<td>Franchise tax</td>
<td>628,985</td>
<td>613,093</td>
<td>560,502</td>
<td>583,781</td>
<td>592,259</td>
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<tr>
<td>Beverage tax</td>
<td>232,987</td>
<td>220,782</td>
<td>213,271</td>
<td>198,848</td>
<td>200,593</td>
</tr>
<tr>
<td>Insurance tax</td>
<td>431,729</td>
<td>431,664</td>
<td>423,405</td>
<td>406,873</td>
<td>340,785</td>
</tr>
<tr>
<td>Piped natural gas</td>
<td>50,397</td>
<td>60,739</td>
<td>64,327</td>
<td>83,219</td>
<td>64,952</td>
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<tr>
<td>Intangible tax</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inheritance tax</td>
<td>133,248</td>
<td>134,419</td>
<td>129,579</td>
<td>112,605</td>
<td>104,799</td>
</tr>
<tr>
<td>Soft drink tax</td>
<td></td>
<td></td>
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<td>2</td>
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<tr>
<td>Tobacco products tax</td>
<td>187,566</td>
<td>43,381</td>
<td>44,128</td>
<td>41,899</td>
<td>41,500</td>
</tr>
<tr>
<td>License tax</td>
<td>46,035</td>
<td>44,219</td>
<td>42,418</td>
<td>44,599</td>
<td>44,432</td>
</tr>
<tr>
<td>Real estate conveyance tax</td>
<td></td>
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</tr>
<tr>
<td>Gift tax</td>
<td>16,251</td>
<td>19,924</td>
<td>16,615</td>
<td>19,328</td>
<td>13,392</td>
</tr>
<tr>
<td>Other taxes</td>
<td>27,571</td>
<td>14,114</td>
<td>13,571</td>
<td>12,508</td>
<td>17,479</td>
</tr>
<tr>
<td><strong>Total tax revenues</strong></td>
<td>17,472,086</td>
<td>15,440,257</td>
<td>13,680,503</td>
<td>13,556,140</td>
<td>12,954,216</td>
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<tr>
<td><strong>NON-TAX REVENUES</strong></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Federal Funds:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Departmental revenues</td>
<td>9,905,879</td>
<td>9,755,087</td>
<td>8,769,925</td>
<td>7,564,627</td>
<td>7,266,016</td>
</tr>
<tr>
<td>Federal Funds for Fiscal Relief:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Departmental revenues</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Local Funds:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Departmental revenues</td>
<td>574,300</td>
<td>731,388</td>
<td>636,900</td>
<td>562,498</td>
<td>682,310</td>
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<tr>
<td>Investment Earnings:</td>
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<td></td>
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</tr>
<tr>
<td>Income from General Fund investments</td>
<td>122,405</td>
<td>75,659</td>
<td>76,415</td>
<td>103,766</td>
<td>129,924</td>
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<tr>
<td>Income from securities lending</td>
<td>133,098</td>
<td>48,463</td>
<td>21,355</td>
<td>30,604</td>
<td>44,659</td>
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<tr>
<td>Departmental revenues</td>
<td>7,357</td>
<td>8,539</td>
<td>2,613</td>
<td>4,745</td>
<td>4,217</td>
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<tr>
<td>Other investment earnings</td>
<td>44</td>
<td>14</td>
<td>3</td>
<td>5</td>
<td>9,531</td>
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<tr>
<td><strong>Total</strong></td>
<td>282,904</td>
<td>132,885</td>
<td>100,336</td>
<td>139,140</td>
<td>188,331</td>
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<tr>
<td>Sales and Services:</td>
<td></td>
<td></td>
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<tr>
<td>Departmental revenues</td>
<td>94,994</td>
<td>85,592</td>
<td>76,010</td>
<td>61,316</td>
<td>61,031</td>
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<tr>
<td>Other non-tax revenues</td>
<td>184</td>
<td>168</td>
<td>182</td>
<td>198</td>
<td>228</td>
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<tr>
<td><strong>Total</strong></td>
<td>95,178</td>
<td>85,760</td>
<td>76,192</td>
<td>61,514</td>
<td>61,259</td>
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<td>Rental and Lease of Property:</td>
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<td>Proceeds from rental and lease of property</td>
<td>57</td>
<td>4,304</td>
<td>102</td>
<td>92</td>
<td>548</td>
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<td>Departmental revenues</td>
<td>7,885</td>
<td>7,072</td>
<td>6,620</td>
<td>6,140</td>
<td>6,556</td>
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<tr>
<td><strong>Total</strong></td>
<td>7,942</td>
<td>11,376</td>
<td>6,722</td>
<td>6,232</td>
<td>7,102</td>
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<td>Fees, Licenses and Fines:</td>
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<td>Court fines and fees</td>
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<td>142,798</td>
<td>138,878</td>
<td>120,381</td>
<td>109,571</td>
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<td>Secretary of State service fees</td>
<td>55,976</td>
<td>40,975</td>
<td>40,038</td>
<td>36,807</td>
<td>31,357</td>
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<td>Banking and investment fees</td>
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<td>5,185</td>
<td>4,758</td>
<td>4,485</td>
<td>4,336</td>
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<tr>
<td>Self insurer fees (Industrial Commission)</td>
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<td>14,128</td>
<td>13,777</td>
<td>13,512</td>
<td>6,799</td>
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<td>Probation supervision fees</td>
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<td>16,476</td>
<td>16,748</td>
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<td>10,833</td>
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<td>Department of insurance fees</td>
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<td>24,526</td>
<td>25,147</td>
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<td>22,854</td>
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<td>DWI service and restoration fees</td>
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<td>8,369</td>
<td>8,709</td>
<td>7,322</td>
<td>5,822</td>
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<td>Departmental revenues</td>
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<td>200,452</td>
<td>192,578</td>
<td>147,747</td>
<td>41,540</td>
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<td>Other non-tax revenues</td>
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<td>3,818</td>
<td>4,368</td>
<td>4,161</td>
<td>4,124</td>
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<td><strong>Total</strong></td>
<td>501,018</td>
<td>462,736</td>
<td>315,621</td>
<td>269,962</td>
<td>237,238</td>
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<td>Tobacco settlement</td>
<td></td>
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<tr>
<td>Tobacco settlement</td>
<td>138,453</td>
<td>148,641</td>
<td>148,452</td>
<td>173,256</td>
<td>175,636</td>
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<td>Contributions, Gifts and Grants:</td>
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<td>Departmental revenues</td>
<td>17,632</td>
<td>34,375</td>
<td>50,140</td>
<td>29,702</td>
<td>33,668</td>
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<td>Other non-tax revenues</td>
<td>1</td>
<td>105</td>
<td>234</td>
<td>1</td>
<td>30</td>
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<td><strong>Total</strong></td>
<td>17,633</td>
<td>34,480</td>
<td>50,374</td>
<td>29,703</td>
<td>33,688</td>
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<td>Miscellaneous:</td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Local sales and use tax administration</td>
<td>14,356</td>
<td>13,932</td>
<td>13,989</td>
<td>12,495</td>
<td>11,774</td>
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<td>Sales tax refunds</td>
<td>3,014</td>
<td>10,253</td>
<td>14,456</td>
<td>7,908</td>
<td>11,120</td>
</tr>
<tr>
<td>Departmental revenues</td>
<td>113,171</td>
<td>84,927</td>
<td>123,852</td>
<td>65,733</td>
<td>89,489</td>
</tr>
<tr>
<td>Other non-tax revenues</td>
<td>1,302</td>
<td>1,253</td>
<td>2,083</td>
<td>316</td>
<td>6,307</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>131,843</td>
<td>110,365</td>
<td>154,380</td>
<td>116,471</td>
<td>118,690</td>
</tr>
<tr>
<td><strong>Total non-tax revenues</strong></td>
<td>$11,833,150</td>
<td>$11,472,478</td>
<td>$10,393,761</td>
<td>$9,060,262</td>
<td>$8,770,468</td>
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<tr>
<td><strong>Total Revenues</strong></td>
<td>$29,105,236</td>
<td>$28,912,735</td>
<td>$24,274,264</td>
<td>$22,616,402</td>
<td>$21,724,866</td>
</tr>
</tbody>
</table>

**[1]** Includes $100,000 for the 2004 fiscal year.

**[2]** The 2002 amount is $21,724,866.

**[3]** The 2002 amount is $21,724,866.


Table 5

<table>
<thead>
<tr>
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<th></th>
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<th></th>
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<tbody>
<tr>
<td></td>
<td>$7,605,542</td>
<td>$7,097,514</td>
<td>$6,586,153</td>
<td>$6,124,709</td>
<td>$5,454,571</td>
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<td>712,161</td>
<td>969,280</td>
<td>920,083</td>
<td>966,759</td>
<td>889,717</td>
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<td>3,426,532</td>
<td>3,361,189</td>
<td>3,345,167</td>
<td>3,272,774</td>
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<td>746,867</td>
<td>557,544</td>
<td>567,497</td>
<td>567,869</td>
<td>534,622</td>
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<td>198,646</td>
<td>193,003</td>
<td>182,970</td>
<td>155,352</td>
<td>151,064</td>
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<td>305,791</td>
<td>273,367</td>
<td>291,202</td>
<td>283,828</td>
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<td>64,854</td>
<td>52,025</td>
<td>58,211</td>
<td>58,708</td>
<td>56,237</td>
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<td>20</td>
<td>31</td>
<td>217</td>
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</tr>
<tr>
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<td>123,094</td>
<td>162,997</td>
<td>163,808</td>
<td>144,203</td>
<td>132,195</td>
</tr>
<tr>
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<td>48</td>
<td>144</td>
<td>11,463</td>
<td>22,338</td>
<td>30,980</td>
</tr>
<tr>
<td></td>
<td>41,417</td>
<td>43,154</td>
<td>40,894</td>
<td>47,304</td>
<td>48,797</td>
</tr>
<tr>
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<td>43,674</td>
<td>42,385</td>
<td>37,202</td>
<td>38,209</td>
<td>41,080</td>
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<tr>
<td></td>
<td>20,254</td>
<td>25,084</td>
<td>19,243</td>
<td>20,722</td>
<td>12,566</td>
</tr>
<tr>
<td></td>
<td>11,152</td>
<td>10,292</td>
<td>10,973</td>
<td>1,501</td>
<td>1,515</td>
</tr>
<tr>
<td></td>
<td>13,007,776</td>
<td>12,808,158</td>
<td>12,166,951</td>
<td>11,679,679</td>
<td>10,670,535</td>
</tr>
</tbody>
</table>

|      | 6,777,503 | 4,156,189 | 5,361,839 | 5,174,408 | 5,169,286 |
|      | 4,875,237 | 432,387 | 436,659 | 436,347 | 403,145 |
|      | 383,479 | 204,083 | 248,657 | 252,162 | 224,260 |
|      | 41,082 | 7,300 | 4,018 | 58,215 | 10,257 |
|      | 320 | 251 | 81 | 137 | 241 |
|      | 285,311 | 323,646 | 365,685 | 447,669 | 340,480 |
|      | 68,276 | 69,790 | 70,035 | 87,214 | 58,744 |
|      | 405 | 278 | 350 | 319 | — |
|      | 69,141 | 70,069 | 70,386 | 67,533 | 58,744 |
|      | 573 | 1,035 | 786 | 1,811 | 1,342 |
|      | 19,080 | 7,218 | 5,773 | 4,255 | 4,651 |
|      | 17,982 | 8,283 | 6,559 | 6,066 | 5,993 |
|      | 47,221 | 97,808 | 99,908 | 93,252 | 98,819 |
|      | 29,268 | 24,236 | 20,099 | 19,267 | 17,344 |
|      | 8,794 | 4,029 | 4,332 | 3,031 | 3,337 |
|      | 7,098 | 8,360 | 4,128 | 3,556 | 3,460 |
|      | 10,453 | 10,605 | 11,168 | 11,778 | 10,859 |
|      | 20,210 | 18,433 | 18,205 | 1,096 | 6,001 |
|      | 5,706 | 5,706 | 5,896 | 6,050 | 5,949 |
|      | 40,422 | 38,300 | 110,884 | 103,296 | 104,002 |
|      | 4,066 | 4,181 | 2,652 | 3,358 | 4,075 |
|      | 239,464 | 209,674 | 277,188 | 244,674 | 254,846 |
|      | 140,272 | — | — | — | — |

|      | 53,425 | 15,462 | 17,511 | 13,205 | 14,145 |
|      | 2 | 101 | 1 | 1 | — |

|      | 53,425 | 15,462 | 17,512 | 13,206 | 14,145 |

|      | 11,568 | 10,973 | 10,293 | 10,060 | 9,178 |
|      | 11,494 | 15,046 | 10,408 | 10,636 | 15,301 |
|      | 123,230 | 108,556 | 130,518 | 115,239 | 151,906 |
|      | 816 | 54 | 744 | 455 | 465 |
|      | 147,206 | 135,908 | 152,061 | 137,269 | 174,840 |
|      | 8,486,947 | 7,401,579 | 6,687,919 | 6,527,170 | 6,421,470 |
|      | $21,770,723 | $20,209,737 | $18,856,910 | $18,206,849 | $17,092,014 |

---


[2] Fiscal years prior to 2001 do not reflect the implementation of GASB Statement No. 33, Accounting for Nonexchange Transactions. This statement provided new rules on the timing of recognition of nonexchange transactions involving financial or capital resources.

[3] For fiscal year ended June 30, 2006, the State changed its methodology for applying GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions to individual income taxes. The State now reports an estimate of underpayments of individual income taxes. The State has also changed its method to estimate overpayments of individual income taxes (i.e., income tax refunds payable and applied refunds). For the purpose of reporting underpayments, the availability period for General Fund individual income taxes was extended from thirty-one days to twelve months after year-end. Where underpayments exceed overpayments, individual income tax revenues are recognized to the extent of estimated overpayments (i.e., income tax refunds payable and applied refunds).
## PERSONAL INCOME BY INDUSTRY

For the Fiscal Years 1998-2004

(Dollars in thousands)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>$33,357,779</td>
<td>$32,754,580</td>
<td>$32,957,483</td>
<td>$33,339,686</td>
<td>$35,305,549</td>
<td>$33,669,223</td>
<td>$32,650,010</td>
</tr>
<tr>
<td>Retail trade</td>
<td>13,551,202</td>
<td>13,066,050</td>
<td>12,770,117</td>
<td>12,587,584</td>
<td>14,266,654</td>
<td>13,517,581</td>
<td>12,414,512</td>
</tr>
<tr>
<td>Services</td>
<td>56,189,445</td>
<td>52,183,987</td>
<td>50,615,389</td>
<td>48,236,817</td>
<td>34,278,925</td>
<td>31,337,093</td>
<td>28,119,353</td>
</tr>
<tr>
<td>Agricultural, forestry, fishing, etc.</td>
<td>644,207</td>
<td>620,240</td>
<td>600,946</td>
<td>618,882</td>
<td>907,049</td>
<td>827,266</td>
<td>736,696</td>
</tr>
<tr>
<td>Government</td>
<td>36,998,898</td>
<td>34,625,046</td>
<td>32,293,906</td>
<td>30,616,692</td>
<td>28,435,566</td>
<td>27,538,020</td>
<td>26,140,679</td>
</tr>
<tr>
<td>Construction</td>
<td>12,041,280</td>
<td>10,974,223</td>
<td>11,039,949</td>
<td>11,565,880</td>
<td>8,799,938</td>
<td>8,300,149</td>
<td>7,592,661</td>
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<tr>
<td>Wholesale trade</td>
<td>10,445,588</td>
<td>9,575,312</td>
<td>9,033,833</td>
<td>8,588,296</td>
<td>9,541,533</td>
<td>9,108,926</td>
<td>8,511,319</td>
</tr>
<tr>
<td>Transportation and warehousing</td>
<td>5,865,756</td>
<td>5,527,864</td>
<td>5,428,763</td>
<td>5,324,201</td>
<td>5,073,577</td>
<td>4,808,932</td>
<td>4,542,317</td>
</tr>
<tr>
<td>Finance and insurance</td>
<td>11,517,449</td>
<td>10,837,137</td>
<td>10,132,099</td>
<td>9,440,396</td>
<td>9,343,795</td>
<td>8,469,976</td>
<td>7,742,498</td>
</tr>
<tr>
<td>Mining</td>
<td>270,876</td>
<td>241,841</td>
<td>240,384</td>
<td>278,288</td>
<td>212,489</td>
<td>206,714</td>
<td>201,577</td>
</tr>
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<td>Utilities</td>
<td>1,431,754</td>
<td>1,373,889</td>
<td>1,275,087</td>
<td>[1]</td>
<td>[1]</td>
<td>[1]</td>
<td>[1]</td>
</tr>
<tr>
<td>Information</td>
<td>5,287,111</td>
<td>5,117,192</td>
<td>5,146,868</td>
<td>[1]</td>
<td>[1]</td>
<td>[1]</td>
<td>[1]</td>
</tr>
<tr>
<td>Real estate and rental and leasing</td>
<td>3,892,638</td>
<td>3,409,047</td>
<td>3,304,984</td>
<td>3,268,078</td>
<td>1,264,710</td>
<td>1,180,757</td>
<td>1,083,707</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$191,493,985</td>
<td>$180,246,408</td>
<td>$174,831,556</td>
<td>$163,864,600</td>
<td>$148,528,785</td>
<td>$138,964,639</td>
<td>$129,737,429</td>
</tr>
</tbody>
</table>

Average effective rate [2]:

- Individual income tax: 3.9% 4.0% 4.1% 4.6% 4.8% 4.7% 4.7%

[1] 2002 is the first fiscal year data was collected for this industry.

[2] Average effective rate equals individual income tax revenues divided by personal income.

Source: Bureau of Economic Analysis (Data for 2006 & 2005 is not available.)

Information prior to 1998 was not available.
### Individual Income Tax Filers and Liability by Income Level

<table>
<thead>
<tr>
<th>North Carolina Taxable Income</th>
<th>Calendar Year 2004</th>
<th>Calendar Year 1997</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of Returns</td>
<td>% of Total</td>
</tr>
<tr>
<td>0 to $15,000</td>
<td>1,915,154</td>
<td>51.7%</td>
</tr>
<tr>
<td>$15,001 to $25,000</td>
<td>503,980</td>
<td>13.6%</td>
</tr>
<tr>
<td>$25,001 to $50,000</td>
<td>679,126</td>
<td>18.4%</td>
</tr>
<tr>
<td>$50,001 to $75,000</td>
<td>298,366</td>
<td>8.1%</td>
</tr>
<tr>
<td>$75,001 to $100,000</td>
<td>125,044</td>
<td>3.4%</td>
</tr>
<tr>
<td>$100,001 to $200,000</td>
<td>124,333</td>
<td>3.4%</td>
</tr>
<tr>
<td>$200,001 and up</td>
<td>52,807</td>
<td>1.4%</td>
</tr>
<tr>
<td></td>
<td>3,698,810</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

**Note:** Due to confidentiality issues, the names of the ten largest revenue payers are not available. The categories presented are intended to provide alternative information regarding the sources of the State's revenue. Calendar year 2004 is the most recent year for which data are available.

### Individual Income Tax Rates - Last 10 Years

#### 1997-2000

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>Bracket 1</th>
<th>Bracket 2</th>
<th>Bracket 3</th>
<th>Bracket 4</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bracket 1</td>
<td>Bracket 2</td>
<td>Bracket 3</td>
<td>Bracket 4</td>
</tr>
<tr>
<td>Married - Joint:</td>
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<td></td>
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</tr>
<tr>
<td>Taxable income</td>
<td>$1-$21,250</td>
<td>$21,251-$100,000</td>
<td>&gt; $100,000</td>
<td>7.75%</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td></td>
<td>7.75%</td>
</tr>
<tr>
<td>Married - Separate:</td>
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<td></td>
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<tr>
<td>Taxable income</td>
<td>$1-$10,625</td>
<td>$10,626-$50,000</td>
<td>&gt; $50,000</td>
<td>7.75%</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td></td>
<td>7.75%</td>
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<tr>
<td>Head of Household:</td>
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</tr>
<tr>
<td>Taxable income</td>
<td>$1-$17,000</td>
<td>$17,001-$80,000</td>
<td>&gt; $80,000</td>
<td>7.75%</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td></td>
<td>7.75%</td>
</tr>
<tr>
<td>Single:</td>
<td>$1-$12,750</td>
<td>$12,751-$60,000</td>
<td>&gt; $60,000</td>
<td>7.75%</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td></td>
<td>7.75%</td>
</tr>
</tbody>
</table>

#### 2001-2006

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>Bracket 1</th>
<th>Bracket 2</th>
<th>Bracket 3</th>
<th>Bracket 4</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bracket 1</td>
<td>Bracket 2</td>
<td>Bracket 3</td>
<td>Bracket 4</td>
</tr>
<tr>
<td>Married - Joint:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable income</td>
<td>$1-$21,250</td>
<td>$21,251-$100,000</td>
<td>$100,001-$200,000</td>
<td>&gt; $200,000</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td>7.75%</td>
<td>8.25%</td>
</tr>
<tr>
<td>Married - Separate:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable income</td>
<td>$1-$10,625</td>
<td>$10,626-$50,000</td>
<td>$50,001-$100,000</td>
<td>&gt; $100,000</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td>7.75%</td>
<td>8.25%</td>
</tr>
<tr>
<td>Head of Household:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable income</td>
<td>$1-$17,000</td>
<td>$17,001-$80,000</td>
<td>$80,001-$160,000</td>
<td>&gt; $160,000</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td>7.75%</td>
<td>8.25%</td>
</tr>
<tr>
<td>Single:</td>
<td>$1-$12,750</td>
<td>$12,751-$60,000</td>
<td>$80,001-$120,000</td>
<td>&gt; $120,000</td>
</tr>
<tr>
<td>Tax rate:</td>
<td>6%</td>
<td>7%</td>
<td>7.75%</td>
<td>8.25%</td>
</tr>
</tbody>
</table>

**Temporary Rate Increase:**
Effective for the tax years January 1, 2001 through December 31, 2003, the General Assembly temporarily raised the highest individual income tax rate from 7.75% to 8.25%. This temporary increase was extended in subsequent budgets. In 2006-07, the General Assembly reduced the top rate from 8.25% to 8.0%, effective January 1, 2007.

**Income tax rate restrictions:**
The State Constitution (Article V, section 2(6)) places the following limitation on the income tax: "The rate of tax on incomes shall not in any case exceed ten percent, and there shall be allowed personal exemptions and deductions so that only net incomes are taxed".

---

**State of North Carolina**  
**Individual Income Tax Filers and Liability - Calendar Years 1997 and 2004**  
**Individual Income Tax Rates - Calendar Years 1997-2006**
## TAXABLE SALES BY BUSINESS GROUP

For the Fiscal Year 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Classification</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>General merchandise</td>
<td>$24,141,458</td>
</tr>
<tr>
<td>Food</td>
<td>17,333,935</td>
</tr>
<tr>
<td>Lumber &amp; building material</td>
<td>14,749,083</td>
</tr>
<tr>
<td>Automotive</td>
<td>5,416,622</td>
</tr>
<tr>
<td>1%, 2%, 2.5% and 3% Tax group</td>
<td>4,551,097</td>
</tr>
<tr>
<td>Furniture</td>
<td>4,367,923</td>
</tr>
<tr>
<td>Apparel</td>
<td>3,481,573</td>
</tr>
<tr>
<td>Unclassified</td>
<td>27,490,165</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$101,551,856</strong></td>
</tr>
</tbody>
</table>

Direct sales tax rate 4.5%

*Source: North Carolina Department of Revenue (Prior year data was not available.)*
## SALES TAX REVENUE PAYERS BY BUSINESS GROUP

### Fiscal Years 1998 and 2005

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>Percentage of Total</th>
<th>1998</th>
<th>Percentage of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>General merchandise</strong></td>
<td>$987,088,322</td>
<td>20.35%</td>
<td>$625,352,352</td>
<td>19.33%</td>
</tr>
<tr>
<td><strong>Food</strong></td>
<td>725,611,884</td>
<td>14.98%</td>
<td>740,721,893</td>
<td>22.90%</td>
</tr>
<tr>
<td><strong>Utilities</strong></td>
<td>669,470,423</td>
<td>13.80%</td>
<td>351,593,837</td>
<td>10.87%</td>
</tr>
<tr>
<td><strong>Lumber &amp; building material</strong></td>
<td>594,456,884</td>
<td>12.25%</td>
<td>342,385,447</td>
<td>10.59%</td>
</tr>
<tr>
<td><strong>Automotive</strong></td>
<td>254,507,573</td>
<td>5.25%</td>
<td>182,729,329</td>
<td>5.65%</td>
</tr>
<tr>
<td><strong>Furniture</strong></td>
<td>181,087,138</td>
<td>3.73%</td>
<td>142,354,550</td>
<td>4.46%</td>
</tr>
<tr>
<td><strong>Apparel</strong></td>
<td>142,766,762</td>
<td>2.94%</td>
<td>100,886,318</td>
<td>3.12%</td>
</tr>
<tr>
<td><strong>Farming</strong></td>
<td>46,272,351</td>
<td>0.95%</td>
<td>54,697,552</td>
<td>1.69%</td>
</tr>
<tr>
<td><strong>Unclassified</strong></td>
<td>1,249,760,813</td>
<td>25.77%</td>
<td>893,807,982</td>
<td>21.45%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$4,851,024,150</td>
<td>100.00%</td>
<td>$3,234,529,060</td>
<td>100.00%</td>
</tr>
</tbody>
</table>

General state sales tax rate........... 4.5% 4.0%

Information prior to 1998 is not available.

### Recent Significant Sales Tax Rate and Base Changes

<table>
<thead>
<tr>
<th>1998-99</th>
<th>Effective July 1, 1998, the State rate applicable to food purchased for home consumption was reduced from 3% to 2%. Effective May 1, 1998, food purchased for home consumption was exempted from the State sales tax.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999-00</td>
<td>Effective July 1, 1999, sales of piped natural gas became exempt from sales tax and, instead, became subject to the piped natural gas excise tax.</td>
</tr>
<tr>
<td>2001-02</td>
<td>Effective October 16, 2001, the general sales rate increased from 4% to 4.5%. Effective December 1, 2001, sales of spiritsuous liquor, other than mixed beverages, became subject to a 6% State sales and use tax. Effective January 1, 2002, gross receipts of direct-to-home satellite service to subscribers in this State became subject to a 5% State sales tax. Effective January 1, 2002, gross receipts derived from providing telecommunications services became subject to a 6% State sales and use tax. (Prior to the law change, local telecommunications services were subject to a 3% State sales tax rate and a 3.22% utility franchise tax rate, interstate long distance calls were taxed at 3.5% and interstate long distance calls were exempt.)</td>
</tr>
<tr>
<td>2003-04</td>
<td>Effective July 1, 2003, all sales of soft drinks became subject to both the State and local rates. Effective January 1, 2004, sales of closed container soft drinks sold through vending machines were taxed on only 50% of the sale price. Effective January 1, 2004, candy was exempted from the State tax and subject to only the 2% local tax. Effective for sales made on or after January 1, 2004, modular homes became subject to a 2.5% State sales and use tax rate.</td>
</tr>
<tr>
<td>2005-06</td>
<td>Effective October 1, 2005, all sales of candy became subject to the combined general State and county tax rate. Effective October 1, 2005, the sales and use tax imposed on telecommunications, direct-to-home satellite services, and spiritsuous liquor increased to 7%. Effective January 1, 2006, a 7% State sales and use tax was imposed on cable services, and satellite digital audio radio became subject to both the State general rate of tax and local rates.</td>
</tr>
</tbody>
</table>

Source: North Carolina Department of Revenue
### RATIOS OF OUTSTANDING DEBT BY TYPE

For the Fiscal Years 1997-2006  
*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Governmental Activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General obligation bonds</td>
<td>$5,738,815</td>
<td>$5,698,535</td>
<td>$4,982,880</td>
<td>$4,066,990</td>
<td>$3,467,325</td>
</tr>
<tr>
<td>Lease-purchase revenue bonds</td>
<td>255,045</td>
<td>265,045</td>
<td>218,405</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Certificates of participation</td>
<td>454,060</td>
<td>475,170</td>
<td>301,165</td>
<td>17,500</td>
<td>-</td>
</tr>
<tr>
<td>Tax judgments payable</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Claims payable</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Notes payable</td>
<td>60,841</td>
<td>34,007</td>
<td>25,008</td>
<td>9,629</td>
<td>11,753</td>
</tr>
<tr>
<td>Capital leases payable</td>
<td>26,879</td>
<td>330</td>
<td>304</td>
<td>322</td>
<td>216</td>
</tr>
<tr>
<td>Total Governmental Activities</td>
<td>$6,535,640</td>
<td>$6,473,087</td>
<td>$5,527,742</td>
<td>$4,094,441</td>
<td>$3,479,294</td>
</tr>
<tr>
<td>Business-type activities</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue bonds</td>
<td>$8,800</td>
<td>9,070</td>
<td>9,325</td>
<td>9,570</td>
<td>9,805</td>
</tr>
<tr>
<td>Notes payable</td>
<td>1,457</td>
<td>1,569</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total Business-type Activities</td>
<td>10,257</td>
<td>10,639</td>
<td>9,325</td>
<td>9,570</td>
<td>9,805</td>
</tr>
<tr>
<td>Total Primary Government</td>
<td>$6,545,897</td>
<td>$6,483,726</td>
<td>$5,537,067</td>
<td>$4,104,011</td>
<td>$3,489,099</td>
</tr>
<tr>
<td>Debt as a Percentage of Personal Income</td>
<td>2.32%</td>
<td>2.44%</td>
<td>2.22%</td>
<td>1.73%</td>
<td>1.52%</td>
</tr>
<tr>
<td>Amount of Debt per Capita</td>
<td>$742</td>
<td>$747</td>
<td>$648</td>
<td>$488</td>
<td>$419</td>
</tr>
<tr>
<td>-------</td>
<td>----------</td>
<td>----------</td>
<td>----------</td>
<td>----------</td>
<td>----------</td>
</tr>
<tr>
<td>$</td>
<td>3,038,693</td>
<td>2,509,986</td>
<td>2,451,973</td>
<td>2,123,944</td>
<td>1,514,477</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>58,744</td>
<td>440,000</td>
<td>732,000</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>20</td>
</tr>
<tr>
<td>7,870</td>
<td>8,797</td>
<td>3,270</td>
<td>4,186</td>
<td>6,083</td>
<td></td>
</tr>
<tr>
<td></td>
<td>853</td>
<td>904</td>
<td>190</td>
<td>318</td>
<td></td>
</tr>
<tr>
<td>3,046,563</td>
<td>2,578,380</td>
<td>2,896,147</td>
<td>2,860,300</td>
<td>1,520,898</td>
<td></td>
</tr>
<tr>
<td></td>
<td>9,905</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>$</td>
<td>3,056,468</td>
<td>2,578,380</td>
<td>2,896,147</td>
<td>2,860,300</td>
<td>1,520,898</td>
</tr>
<tr>
<td>1.33%</td>
<td>1.12%</td>
<td>1.26%</td>
<td>1.25%</td>
<td>0.66%</td>
<td></td>
</tr>
<tr>
<td>$</td>
<td>367</td>
<td>310</td>
<td>346</td>
<td>344</td>
<td>183</td>
</tr>
</tbody>
</table>
### RATIOS OF GENERAL BONDED AND SIMILAR DEBT OUTSTANDING

**For the Fiscal Years 1997-2006**  
*Table 11*

<table>
<thead>
<tr>
<th>Fiscal Year Ended June 30</th>
<th>General Obligation Bonds</th>
<th>Lease Purchase Revenue Bonds</th>
<th>Certificates of Participation</th>
<th>Total</th>
<th>Per Capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>$5,738,815,000</td>
<td>$255,045,000</td>
<td>$454,060,000</td>
<td>$6,447,920,000</td>
<td>$730.45</td>
</tr>
<tr>
<td>2005</td>
<td>5,698,535,000</td>
<td>265,045,000</td>
<td>475,170,000</td>
<td>6,438,750,000</td>
<td>741.51</td>
</tr>
<tr>
<td>2004</td>
<td>4,982,860,000</td>
<td>218,405,000</td>
<td>301,165,000</td>
<td>5,502,430,000</td>
<td>644.22</td>
</tr>
<tr>
<td>2003</td>
<td>4,066,990,000</td>
<td>-</td>
<td>1,750,000</td>
<td>4,068,740,000</td>
<td>483.96</td>
</tr>
<tr>
<td>2002</td>
<td>3,467,326,000</td>
<td>-</td>
<td>-</td>
<td>3,467,326,000</td>
<td>416.74</td>
</tr>
<tr>
<td>2001</td>
<td>3,042,570,000</td>
<td>-</td>
<td>-</td>
<td>3,042,570,000</td>
<td>371.67</td>
</tr>
<tr>
<td>2000</td>
<td>2,514,730,000</td>
<td>-</td>
<td>-</td>
<td>2,514,730,000</td>
<td>312.42</td>
</tr>
<tr>
<td>1999</td>
<td>2,457,650,000</td>
<td>-</td>
<td>-</td>
<td>2,457,650,000</td>
<td>321.35</td>
</tr>
<tr>
<td>1998</td>
<td>2,130,615,000</td>
<td>-</td>
<td>-</td>
<td>2,130,615,000</td>
<td>282.36</td>
</tr>
<tr>
<td>1997</td>
<td>1,522,200,000</td>
<td>-</td>
<td>-</td>
<td>1,522,200,000</td>
<td>204.91</td>
</tr>
</tbody>
</table>

*Note: Population data can be found in table 15.*
## SCHEDULE OF GENERAL OBLIGATION BONDS PAYABLE

**June 30, 2006**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th>Payable from General Fund Revenues</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total General Obligation Bonds</strong></td>
</tr>
<tr>
<td><strong>General Fund</strong></td>
</tr>
<tr>
<td>8.5 - 8.9%</td>
</tr>
</tbody>
</table>

### Bonds Authorized and Issued:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (in $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ch. 1048, 1987 session law.</td>
<td>20,499</td>
</tr>
<tr>
<td>Ch. 542, 1993 session law...</td>
<td>195,000</td>
</tr>
<tr>
<td>Ch. 631, 1995 session law...</td>
<td>1,800,000</td>
</tr>
<tr>
<td>General Statute Ch. 142.....</td>
<td>908,965</td>
</tr>
<tr>
<td>Ch. 590, 1995 session law...</td>
<td>650,000</td>
</tr>
<tr>
<td>Ch. 132, 1998 session law...</td>
<td>717,955</td>
</tr>
<tr>
<td>Ch. 3, 2000 session law......</td>
<td>2,122,800</td>
</tr>
<tr>
<td>2004 session law.............</td>
<td>1,981,165</td>
</tr>
</tbody>
</table>

| Total bonds authorized and issued | 8,396,384 |
|-----------------------------------| 7,348,014 |
| 20,499 | 195,000 |
| 450,000 | 112,000 |
| 297,000 |
| 144,000 |
| 306,000 |
| 228,000 |

**Total Bonds Outstanding** | 5,738,094 |

### Bond Maturity As Follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Principal Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006-07</td>
<td>343,263</td>
</tr>
<tr>
<td>2007-08</td>
<td>342,472</td>
</tr>
<tr>
<td>2008-09</td>
<td>339,194</td>
</tr>
<tr>
<td>2009-10</td>
<td>339,200</td>
</tr>
<tr>
<td>2010-11</td>
<td>339,360</td>
</tr>
<tr>
<td>2011-12</td>
<td>340,380</td>
</tr>
<tr>
<td>2012-13</td>
<td>342,305</td>
</tr>
<tr>
<td>2013-14</td>
<td>342,470</td>
</tr>
<tr>
<td>2014-15</td>
<td>341,715</td>
</tr>
<tr>
<td>2015-16</td>
<td>341,740</td>
</tr>
<tr>
<td>2016-17</td>
<td>339,395</td>
</tr>
<tr>
<td>2017-18</td>
<td>343,180</td>
</tr>
<tr>
<td>2018-19</td>
<td>344,255</td>
</tr>
<tr>
<td>2019-20</td>
<td>309,900</td>
</tr>
<tr>
<td>2020-21</td>
<td>229,500</td>
</tr>
<tr>
<td>2021-22</td>
<td>210,500</td>
</tr>
<tr>
<td>2022-23</td>
<td>203,455</td>
</tr>
<tr>
<td>2023-24</td>
<td>178,000</td>
</tr>
<tr>
<td>2024-25</td>
<td>98,400</td>
</tr>
<tr>
<td>2025-26</td>
<td>36,400</td>
</tr>
<tr>
<td>2026-27</td>
<td>16,500</td>
</tr>
<tr>
<td>2027-28</td>
<td>16,500</td>
</tr>
</tbody>
</table>

**Total Bonds Outstanding** | 5,738,094 |

[ * ] Capital Appreciation Bonds
Payable from General Fund Revenues

| Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement | Public Improvement |
|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| $5.0-5.4% | 6.7-6.75% | 4.5-4.7% | 5.0-5.1% | 4.5-5.0% | 4.0-5.6% | 3.0-4.0% | to 18% | to 18% | to 18% |

<table>
<thead>
<tr>
<th></th>
<th>$</th>
<th></th>
<th>$</th>
<th></th>
<th>$</th>
<th></th>
<th>$</th>
<th></th>
<th>$</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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</tr>
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| $25,000        | $2,900| $350| $60,000| $188,000| $148,000| $2,000| $88,750| $88,750| $88,750|
| $6,000         | 2,900 | 350 | 12,000| 16,000| 23,000| 2,000 |      |      |      |
| 9,500          |      |     | 12,000| 16,000| 25,000|      |      |      |      |
| 9,500          |      |     | 12,000| 16,000| 25,000|      |      |      |      |
|                |      |     | 12,000| 16,000| 25,000|      |      |      |      |
|                |      |     | 16,000| 25,000|      |      |      |      |      |
|                | 16,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 16,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 16,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 16,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 26,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 26,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 26,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                | 26,000|     |      |      | 6,250| 6,250| 6,250|      |      |
|                |      |     |      |      |      |      |      |      |      |

Continued
## SCHEDULE OF GENERAL OBLIGATION BONDS PAYABLE (continued)

### Payable from General Fund Revenues

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<td>Total bonds authorized and issued</td>
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| Accretion | — | — | — | — | — | — | — | — | — |
| Bonds retired | — | — | 620 | — | — | — | — | — | — |

| Partial defeasances | — | — | — | — | — | — | — | — | — |

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### Bond Maturity As Follows:

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| Total Bonds Outstanding | $ 88,750 | $ 20,000 | $ 18,180 | $ 39,525 | $ 100,000 | $ 100,000 | $ 100,000 | $ 100,000 | $ 100,000 | $ 100,000 |
### Table 12

#### Payable from General Fund Revenues

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Continued
### SCHEDULE OF GENERAL OBLIGATION BONDS PAYABLE (continued)

**June 30, 2006**

*(Dollars in Thousands)*

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**Bonds Authorized and Issued:**

- **Ch. 1048, 1987 session law:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Ch. 542, 1993 session law:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Ch. 631, 1995 session law:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **General Statute Ch. 142:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Ch. 590, 1995 session law:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Ch. 132, 1998 session law:** $15,255 $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Ch. 3, 2000 session law:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **2004 session law:** $—— $11,900 $59,275 $155,245 $57,470 $705,500 $16,000 $106,895

**Total bonds authorized and issued:** $15,255 $11,900 $59,275 $155,245 $57,470 $705,500 $16,000 $106,895

- **Accretion:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——
- **Bonds retired:** $6,200 $3,285 $1,435 $—— $230 $21,800 $3,200 $45
- **Partial defeasances:** $—— $—— $—— $—— $—— $—— $—— $—— $—— $——

**Bonds outstanding—6/30/2006:**

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**Bond Maturity As Follows:**

- **2006-07:** $3,100 $2,910 $11,725 $—— $65 $21,800 $3,200 $45
- **2007-08:** $3,100 $2,870 $11,580 $30,825 $70 $21,800 $3,200 $50
- **2008-09:** $2,855 $2,855 $11,545 $31,260 $70 $21,800 $3,200 $50
- **2009-10:** $—— $—— $11,515 $31,160 $9,575 $21,800 $3,200 $50
- **2010-11:** $—— $—— $11,475 $31,055 $9,555 $25,000 $—— $50
- **2011-12:** $—— $—— $—— $30,945 $9,535 $25,000 $—— $12,025
- **2012-13:** $—— $—— $—— $—— $9,510 $25,000 $—— $11,935
- **2013-14:** $—— $—— $—— $—— $9,490 $25,000 $—— $11,810
- **2014-15:** $—— $—— $—— $—— $9,370 $25,000 $—— $11,680
- **2015-16:** $—— $—— $—— $—— $—— $25,000 $—— $11,800
- **2016-17:** $—— $—— $—— $—— $—— $25,000 $—— $47,555
- **2017-18:** $—— $—— $—— $—— $—— $25,000 $—— $——
- **2018-19:** $—— $—— $—— $—— $—— $25,000 $—— $——
- **2019-20:** $—— $—— $—— $—— $—— $54,000 $—— $——
- **2020-21:** $—— $—— $—— $—— $—— $80,000 $—— $——
- **2021-22:** $—— $—— $—— $—— $—— $80,000 $—— $——
- **2022-23:** $—— $—— $—— $—— $—— $80,000 $—— $——
- **2023-24:** $—— $—— $—— $—— $—— $77,500 $—— $——
- **2024-25:** $—— $—— $—— $—— $—— $—— $—— $——
- **2025-26:** $—— $—— $—— $—— $—— $—— $—— $——
- **2026-27:** $—— $—— $—— $—— $—— $—— $—— $——
- **2027-28:** $—— $—— $—— $—— $—— $—— $—— $——

**Total Bonds Outstanding:** $9,055 $8,635 $57,840 $155,245 $57,240 $863,700 $12,800 $106,895
Table 12

<table>
<thead>
<tr>
<th>Payable from General Fund Revenues</th>
<th>Payable from Highway Trust Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clean Water Refunding Series 2005B 6-29-05</td>
<td>Highway Total Series 1997A 4-5-0%</td>
</tr>
<tr>
<td>Higher Education Series 2006A 3-30-06</td>
<td>Highway Highway Refunding Series 2003 3-5-5%</td>
</tr>
<tr>
<td>Refunding 9-14-06</td>
<td>Highway Highway Refunding Series 2004 5-0-5-5%</td>
</tr>
<tr>
<td>5% 3.875%-5.5% 4.25%-5.25%</td>
<td>Highway Highway Refunding Series 2004 3%-5%</td>
</tr>
<tr>
<td>$ 467,275 $ 70,000 $ 300,000</td>
<td>$ 756,755 $ 16,675 $ 364,000 $ 96,080 $ 280,000</td>
</tr>
</tbody>
</table>

Source: Compiled by the Department of State Treasurer.
## SCHEDULE OF SPECIAL OBLIGATION DEBT

### June 30, 2006

(Dollars in Thousands)

<table>
<thead>
<tr>
<th>Lease Purchase</th>
<th>Certificates of Participation</th>
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</thead>
<tbody>
<tr>
<td>Revenue Bonds</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>Total</strong></td>
</tr>
<tr>
<td>Special Obligation</td>
<td>Certificates of Participation</td>
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<tr>
<td>Debt</td>
<td>Bonds</td>
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<td></td>
<td>2003</td>
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<tr>
<td>Total Lease</td>
<td>Total Correctional Facilities</td>
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<td>special</td>
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<td>Bonds</td>
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<tr>
<td>502,360</td>
<td>218,405</td>
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<tr>
<td>17,500</td>
<td>283,955</td>
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<tr>
<td>General Statue Ch. 149-37.2</td>
<td>53,640</td>
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<tr>
<td>Ch. 179, 2004 session law</td>
<td>188,385</td>
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<td>Total bonds authorized and issued:</td>
<td>761,865</td>
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<tr>
<td>Bonds outstanding:</td>
<td>52,780</td>
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<tr>
<td>Bonds retired:</td>
<td>35,780</td>
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<td>June 30, 2006:</td>
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### Bond Maturity

As follows:

<table>
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<tr>
<th>Year</th>
<th>Total</th>
<th>10,000</th>
<th>8,000</th>
<th>6,000</th>
<th>4,000</th>
<th>2,000</th>
<th>1,000</th>
<th>6,510</th>
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<tr>
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<td>31,420</td>
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<td>8,000</td>
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<td>665</td>
<td>7,950</td>
<td>6,000</td>
<td>6,805</td>
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<td>2007-08</td>
<td>31,760</td>
<td>10,000</td>
<td>8,000</td>
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<td>690</td>
<td>7,950</td>
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<td>2008-09</td>
<td>32,110</td>
<td>10,000</td>
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<td>720</td>
<td>7,950</td>
<td>6,000</td>
<td>7,440</td>
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<tr>
<td>2009-10</td>
<td>32,470</td>
<td>10,000</td>
<td>8,000</td>
<td>2,000</td>
<td>720</td>
<td>7,950</td>
<td>6,000</td>
<td>7,760</td>
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<tr>
<td>2010-11</td>
<td>32,880</td>
<td>10,000</td>
<td>8,000</td>
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<td>720</td>
<td>7,950</td>
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<td>8,165</td>
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<tr>
<td>2011-12</td>
<td>33,225</td>
<td>10,000</td>
<td>8,000</td>
<td>2,000</td>
<td>720</td>
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<td>6,000</td>
<td>8,560</td>
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<tr>
<td>2012-13</td>
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<td>8,000</td>
<td>2,000</td>
<td>720</td>
<td>7,950</td>
<td>6,000</td>
<td>9,000</td>
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<tr>
<td>2013-14</td>
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<td>720</td>
<td>7,950</td>
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<td>9,455</td>
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<tr>
<td>2014-15</td>
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<td>720</td>
<td>7,950</td>
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<td>9,925</td>
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<td>2015-16</td>
<td>35,225</td>
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<td>8,000</td>
<td>2,000</td>
<td>720</td>
<td>7,950</td>
<td>6,000</td>
<td>10,425</td>
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<td>2016-17</td>
<td>35,865</td>
<td>8,650</td>
<td>8,000</td>
<td>665</td>
<td>25,990</td>
<td>1,000</td>
<td>7,945</td>
<td>6,000</td>
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<tr>
<td>2017-18</td>
<td>34,595</td>
<td>8,500</td>
<td>8,000</td>
<td>500</td>
<td>25,490</td>
<td>1,055</td>
<td>7,945</td>
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<td>2018-19</td>
<td>35,120</td>
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<td>8,000</td>
<td>500</td>
<td>27,120</td>
<td>1,110</td>
<td>7,945</td>
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<td>9,850</td>
<td>28,780</td>
<td>1,165</td>
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<td>2020-21</td>
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<td>24,000</td>
<td>19,000</td>
<td>5,000</td>
<td>26,175</td>
<td>1,220</td>
<td>7,945</td>
<td>7,000</td>
</tr>
<tr>
<td>2021-22</td>
<td>50,235</td>
<td>24,000</td>
<td>19,000</td>
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<td>26,235</td>
<td>1,290</td>
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<td>2022-23</td>
<td>50,305</td>
<td>24,000</td>
<td>19,000</td>
<td>5,000</td>
<td>26,305</td>
<td>1,360</td>
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<tr>
<td>2023-24</td>
<td>51,170</td>
<td>26,225</td>
<td>23,405</td>
<td>2,820</td>
<td>24,945</td>
<td>7,945</td>
<td>7,000</td>
<td>10,000</td>
</tr>
<tr>
<td>2024-25</td>
<td>12,520</td>
<td>2,820</td>
<td>2,820</td>
<td>2,820</td>
<td>10,000</td>
<td>10,000</td>
<td>10,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Total Bonds Outstanding</td>
<td>709,105</td>
<td>255,045</td>
<td>203,405</td>
<td>51,400</td>
<td>454,465</td>
<td>16,125</td>
<td>143,060</td>
<td>113,000</td>
</tr>
</tbody>
</table>

Source: Compiled by the Department of State Treasurer.
**PLEDGED REVENUE COVERAGE REVENUE BONDS**

For the Fiscal Years 2002-2006

**Table 14**

*(Dollars in Thousands)*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Pledged Revenue-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales and services</td>
<td>$2,377</td>
<td>$3,531</td>
<td>$3,673</td>
<td>$3,936</td>
<td>$3,581</td>
</tr>
<tr>
<td>Rental lease earnings</td>
<td>5</td>
<td>3</td>
<td>8</td>
<td></td>
<td></td>
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<tr>
<td>Fees, licenses and fines</td>
<td>8</td>
<td>14</td>
<td>14</td>
<td>13</td>
<td>17</td>
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<td>Miscellaneous revenue</td>
<td>147</td>
<td>156</td>
<td>106</td>
<td>243</td>
<td>407</td>
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<td>Less: Operating expenses</td>
<td>(2,261)</td>
<td>(2,470)</td>
<td>(2,372)</td>
<td>(2,341)</td>
<td>(2,276)</td>
</tr>
<tr>
<td>Net available revenue</td>
<td>$276</td>
<td>$1,234</td>
<td>$1,429</td>
<td>$1,851</td>
<td>$1,729</td>
</tr>
<tr>
<td>Debt service</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Principal</td>
<td>$270</td>
<td>$255</td>
<td>$245</td>
<td>$235</td>
<td>$100</td>
</tr>
<tr>
<td>Interest</td>
<td>394</td>
<td>414</td>
<td>419</td>
<td>434</td>
<td>431</td>
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<tr>
<td>Coverage</td>
<td>.42</td>
<td>1.85</td>
<td>2.16</td>
<td>2.77</td>
<td>3.28</td>
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</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Pledged Revenue-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on investments</td>
<td>$23,718</td>
<td>$17,859</td>
<td>$17,357</td>
<td>$14,887</td>
<td>$13,315</td>
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<tr>
<td>Interest on mortgage loans</td>
<td>66,515</td>
<td>69,816</td>
<td>74,650</td>
<td>83,045</td>
<td>82,769</td>
</tr>
<tr>
<td>Net increase/decrease in fair value of investments</td>
<td>(2,372)</td>
<td>544</td>
<td></td>
<td>-</td>
<td>3,926</td>
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<tr>
<td>Other revenue</td>
<td>444</td>
<td>198</td>
<td>147</td>
<td>92</td>
<td>710</td>
</tr>
<tr>
<td>Less: Operating expenses</td>
<td>(4,640)</td>
<td>(4,998)</td>
<td>(4,678)</td>
<td>(4,739)</td>
<td>(5,165)</td>
</tr>
<tr>
<td>Net available revenue</td>
<td>$83,665</td>
<td>$83,221</td>
<td>$87,476</td>
<td>$93,085</td>
<td>$55,775</td>
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<tr>
<td>Debt service</td>
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<tr>
<td>Principal</td>
<td>$175,670</td>
<td>$27,967</td>
<td>$24,245</td>
<td>$21,465</td>
<td>$15,762</td>
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<td>70,059</td>
<td>63,242</td>
<td>69,622</td>
<td>74,408</td>
<td>77,467</td>
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<td>Coverage</td>
<td>.34</td>
<td>.91</td>
<td>.93</td>
<td>.97</td>
<td>1.03</td>
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</table>

<table>
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<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Pledged Revenue-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Student loan principal collections</td>
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<td>$300,827</td>
<td>$277,552</td>
<td>$214,782</td>
<td>$133,041</td>
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<td>90,912</td>
<td>50,037</td>
<td>48,587</td>
<td>55,281</td>
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<td>4,157</td>
<td>2,886</td>
<td>2,450</td>
<td>3,121</td>
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<td>Less: Operating expenses</td>
<td>(24,627)</td>
<td>(19,395)</td>
<td>(17,823)</td>
<td>(14,781)</td>
<td>(10,692)</td>
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<td>$312,672</td>
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<tr>
<td>Principal</td>
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<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
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<td>16.69</td>
<td>10.23</td>
<td>4.84</td>
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<table>
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</tr>
</thead>
<tbody>
<tr>
<td>Pledged Revenue-</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Sales and services</td>
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<td>51,657</td>
<td>54,525</td>
<td>54,025</td>
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<td>30,133</td>
<td>32,284</td>
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<td>Non-operating revenues</td>
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<td>39,558</td>
<td>35,888</td>
<td>46,521</td>
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<td>Less: Operating expenses</td>
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<td>(1,653,952)</td>
<td>(1,604,207)</td>
<td>(1,487,632)</td>
<td>(1,460,074)</td>
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*Information prior to 2002 not available.*
## SCHEDULE OF DEMOGRAPHIC DATA


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<tr>
<td>2005</td>
<td>296,410,404 [D]</td>
<td>0.94%</td>
<td>8,683,242 [D]</td>
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<td>34,586 [E]</td>
<td>30,553 [E]</td>
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<td>10,251,650 [H]</td>
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<td>249,797 [H]</td>
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<td>2004</td>
<td>293,655,404 [D]</td>
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<td>29,246 [E]</td>
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<td>237,379 [H]</td>
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<td>249,797 [H]</td>
</tr>
<tr>
<td>2002</td>
<td>288,368,698 [D]</td>
<td>1.25%</td>
<td>8,320,146 [D]</td>
<td>1.64%</td>
<td>30,832 [E]</td>
<td>27,566 [E]</td>
<td>89.41%</td>
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<td>229,353 [H]</td>
<td>8,890,984 [H]</td>
<td>229,353 [H]</td>
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<td>2001</td>
<td>284,797,000 [D]</td>
<td>0.95%</td>
<td>8,186,268 [D]</td>
<td>1.70%</td>
<td>30,472 [E]</td>
<td>27,514 [E]</td>
<td>90.29%</td>
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<td>225,237 [H]</td>
<td>8,678,334 [H]</td>
<td>225,237 [H]</td>
</tr>
<tr>
<td>2000</td>
<td>282,125,000 [D]</td>
<td>3.46%</td>
<td>8,049,313 [D]</td>
<td>5.25%</td>
<td>29,770 [E]</td>
<td>27,055 [E]</td>
<td>90.88%</td>
<td>8,398,861 [H]</td>
<td>217,774 [H]</td>
<td>8,398,861 [H]</td>
<td>217,774 [H]</td>
</tr>
<tr>
<td>1999</td>
<td>272,691,000 [B]</td>
<td>0.90%</td>
<td>7,647,934 [C]</td>
<td>1.35%</td>
<td>27,880 [E]</td>
<td>25,504 [E]</td>
<td>91.48%</td>
<td>7,802,625 [H]</td>
<td>195,053 [H]</td>
<td>7,802,625 [H]</td>
<td>195,053 [H]</td>
</tr>
<tr>
<td>1998</td>
<td>270,248,000 [B]</td>
<td>0.92%</td>
<td>7,545,735 [C]</td>
<td>1.58%</td>
<td>26,893 [E]</td>
<td>24,661 [E]</td>
<td>91.70%</td>
<td>7,267,779 [H]</td>
<td>186,085 [H]</td>
<td>7,267,779 [H]</td>
<td>186,085 [H]</td>
</tr>
<tr>
<td>1997</td>
<td>267,784,000 [B]</td>
<td>0.96%</td>
<td>7,428,579 [C]</td>
<td>1.70%</td>
<td>25,412 [E]</td>
<td>23,468 [E]</td>
<td>92.35%</td>
<td>6,804,927 [H]</td>
<td>174,334 [H]</td>
<td>6,804,927 [H]</td>
<td>174,334 [H]</td>
</tr>
</tbody>
</table>

[C] - N.C. Office of State Planning estimate - July 1, 1991 - 1999, based on April, 1990 census population of 6,628,637 and April, 2000 census population of 8,049,313
[D] - U.S. Census estimates based on 2000 census
[E] - Bureau of Economic Analysis estimate

[F] - Since the 2006 population estimates are not available, the Office of State Controller used the growth rate of the previous year to project the 2006 amounts

[G] - Since the 2006 per capita income estimates are not available, the Office of State Controller used the U.S. Per Capita Income growth rate of the previous year to project the 2006 U.S. Per Capita Income and the previous year "N.C. as a Percentage of U.S." was used to project the "2006 Per Capita Income for North Carolina".

### Per Capita Income

#### North Carolina Compared to United States

1997 to 2006

- **Income — Thousands**
- **Percent of U.S. A.**

<table>
<thead>
<tr>
<th>Year</th>
<th>North Carolina</th>
<th>U.S.A.</th>
<th>Percent of U.S.A.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>1999</td>
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<td>2001</td>
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<tr>
<td>2002</td>
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<tr>
<td>2003</td>
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<tr>
<td>2004</td>
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<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Sources:

1. Population
2. Per Capita Income
3. Personal Income

U.S. Department of Commerce, Bureau of the Census
U.S. Department of Commerce, Bureau of Economic Analysis
Calculated from sources 1 and 2
<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Employed</th>
<th>Unemployed</th>
<th>Unemployed Percentage Rate</th>
<th>North Carolina - Other Data</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>4,394,216</td>
<td>4,193,971</td>
<td>200,245</td>
<td>4.66%</td>
<td>8,407,473</td>
</tr>
<tr>
<td>2005</td>
<td>4,308,462</td>
<td>4,076,645</td>
<td>229,837</td>
<td>5.33%</td>
<td>7,925,587</td>
</tr>
<tr>
<td>2004</td>
<td>4,206,568</td>
<td>3,977,421</td>
<td>231,147</td>
<td>5.49%</td>
<td>7,701,410</td>
</tr>
<tr>
<td>2003</td>
<td>4,152,243</td>
<td>3,882,026</td>
<td>270,217</td>
<td>6.51%</td>
<td>7,624,272</td>
</tr>
<tr>
<td>2002</td>
<td>3,964,000</td>
<td>3,715,400</td>
<td>248,600</td>
<td>6.27%</td>
<td>7,498,181</td>
</tr>
<tr>
<td>2001</td>
<td>3,999,300</td>
<td>3,802,500</td>
<td>196,800</td>
<td>4.92%</td>
<td>7,344,437</td>
</tr>
<tr>
<td>2000</td>
<td>3,941,000</td>
<td>3,805,300</td>
<td>135,700</td>
<td>3.44%</td>
<td>7,112,610</td>
</tr>
<tr>
<td>1999</td>
<td>3,826,000</td>
<td>3,724,100</td>
<td>101,900</td>
<td>2.66%</td>
<td>6,911,814</td>
</tr>
<tr>
<td>1998</td>
<td>3,776,300</td>
<td>3,661,000</td>
<td>115,300</td>
<td>3.05%</td>
<td>6,428,104</td>
</tr>
<tr>
<td>1997</td>
<td>3,799,900</td>
<td>3,657,800</td>
<td>139,100</td>
<td>3.66%</td>
<td>6,392,269</td>
</tr>
<tr>
<td>1990</td>
<td>3,471,000</td>
<td>3,339,000</td>
<td>132,000</td>
<td>3.80%</td>
<td>5,600,050</td>
</tr>
<tr>
<td>1980</td>
<td>2,759,197</td>
<td>2,607,925</td>
<td>151,272</td>
<td>5.48%</td>
<td>5,094,814</td>
</tr>
<tr>
<td>1970</td>
<td>2,054,838</td>
<td>1,984,402</td>
<td>70,436</td>
<td>3.43%</td>
<td>3,218,292</td>
</tr>
<tr>
<td>1960</td>
<td>1,680,442</td>
<td>1,605,478</td>
<td>74,964</td>
<td>4.46%</td>
<td>1,907,988</td>
</tr>
<tr>
<td>1950</td>
<td>1,512,924</td>
<td>1,463,352</td>
<td>49,572</td>
<td>3.28%</td>
<td>1,171,228</td>
</tr>
</tbody>
</table>

N/A = Data not available.

---

**Civilian Labor Force Trends**

*With Unemployment Percentages*  
**1997 to 2006**

![Graph showing civilian labor force trends with unemployment percentages from 1997 to 2006.](image)

**Sources:**

[4] Seasonally Adjusted Labor Force Data - As of June 30  
[6] Residential Housing Permits  

N.C. Employment Security Commission  
N.C. Division of Motor Vehicles  
U.S. Department of Commerce, Bureau of the Census
<table>
<thead>
<tr>
<th>Employer</th>
<th>Employees 2006</th>
<th>Rank</th>
<th>Percentage of Total State Employment</th>
<th>Employees 2001</th>
<th>Rank</th>
<th>Percentage of Total State Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>State of North Carolina</td>
<td>170,000-174,999</td>
<td>1</td>
<td>4.11%</td>
<td>160,000-164,999</td>
<td>1</td>
<td>4.27%</td>
</tr>
<tr>
<td>Federal Government</td>
<td>60,000-64,999</td>
<td>2</td>
<td>1.48%</td>
<td>60,000-64,999</td>
<td>2</td>
<td>1.64%</td>
</tr>
<tr>
<td>Wal-Mart Stores, Inc.</td>
<td>45,000-49,999</td>
<td>3</td>
<td>1.13%</td>
<td>30,000-34,999</td>
<td>3</td>
<td>0.85%</td>
</tr>
<tr>
<td>Duke University</td>
<td>25,000-29,999</td>
<td>4</td>
<td>0.65%</td>
<td>20,000-24,999</td>
<td>5</td>
<td>0.59%</td>
</tr>
<tr>
<td>Food Lion LLC</td>
<td>25,000-29,999</td>
<td>5</td>
<td>0.65%</td>
<td>25,000-29,999</td>
<td>4</td>
<td>0.72%</td>
</tr>
<tr>
<td>Wachovia Bank, NA</td>
<td>25,000-29,999</td>
<td>6</td>
<td>0.65%</td>
<td>10,000-14,999</td>
<td>9</td>
<td>0.32%</td>
</tr>
<tr>
<td>Charlotte Board of Ed.</td>
<td>15,000-19,999</td>
<td>7</td>
<td>0.41%</td>
<td>15,000-19,999</td>
<td>7</td>
<td>0.45%</td>
</tr>
<tr>
<td>Wake Public Schools</td>
<td>15,000-19,999</td>
<td>8</td>
<td>0.41%</td>
<td>10,000-14,999</td>
<td>6</td>
<td>0.32%</td>
</tr>
<tr>
<td>Charlotte Hospital Authority</td>
<td>15,000-19,999</td>
<td>9</td>
<td>0.41%</td>
<td>10,000-14,999</td>
<td>10</td>
<td>0.32%</td>
</tr>
<tr>
<td>Bank of America, NA</td>
<td>10,000-14,999</td>
<td>10</td>
<td>0.29%</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>BM Corporation</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>15,000-19,999</td>
<td>6</td>
<td>0.45%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>405,000-454,999</strong></td>
<td><strong>10.19%</strong></td>
<td><strong>355,000-404,990</strong></td>
<td><strong>9.93%</strong></td>
<td><strong>9.93%</strong></td>
<td><strong>9.93%</strong></td>
</tr>
</tbody>
</table>

**Notes:** All figures are based on 1st quarter average. Percentage of total state employment is based on the midpoints in the ranges given. Information prior to 2001 is not available.

**Source:** North Carolina Employment Security Commission
## TEACHERS AND STATE EMPLOYEES BY FUNCTION

For the Fiscal Years 2002-2006

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>General government</td>
<td>5,680</td>
<td>5,435</td>
<td>5,301</td>
<td>5,635</td>
<td>5,635</td>
</tr>
<tr>
<td>Primary and secondary education</td>
<td>156,463</td>
<td>152,746</td>
<td>147,798</td>
<td>143,428</td>
<td>140,103</td>
</tr>
<tr>
<td>Higher education:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Universities</td>
<td>55,800</td>
<td>53,560</td>
<td>51,002</td>
<td>50,787</td>
<td>49,625</td>
</tr>
<tr>
<td>Community Colleges</td>
<td>15,610</td>
<td>15,764</td>
<td>15,277</td>
<td>14,582</td>
<td>13,959</td>
</tr>
<tr>
<td>Health and human services</td>
<td>20,766</td>
<td>20,665</td>
<td>20,366</td>
<td>18,545</td>
<td>18,816</td>
</tr>
<tr>
<td>Economic development</td>
<td>2,567</td>
<td>2,366</td>
<td>2,469</td>
<td>2,466</td>
<td>2,591</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>4,616</td>
<td>4,493</td>
<td>4,341</td>
<td>4,337</td>
<td>4,750</td>
</tr>
<tr>
<td>Public safety, corrections and regulations</td>
<td>31,448</td>
<td>30,429</td>
<td>30,125</td>
<td>30,810</td>
<td>30,982</td>
</tr>
<tr>
<td>Transportation</td>
<td>14,007</td>
<td>14,379</td>
<td>14,218</td>
<td>14,438</td>
<td>14,378</td>
</tr>
<tr>
<td>Agriculture</td>
<td>1,377</td>
<td>1,339</td>
<td>1,343</td>
<td>1,275</td>
<td>1,295</td>
</tr>
<tr>
<td><strong>Totals[1]</strong></td>
<td>308,334</td>
<td>301,176</td>
<td>293,140</td>
<td>286,303</td>
<td>282,134</td>
</tr>
</tbody>
</table>

[1] Prior years 2002-2005 have been restated to include all teachers and state employees.

Source: North Carolina Office of State Budget and Management
Counts for fiscal year end 2006 are projected from prior year data.
Information prior to 2002 not available.
# OPERATING INDICATORS BY FUNCTION

For the Fiscal Years 2002-2006

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Department of Revenue</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of tax returns filed electronically</td>
<td>2,487,716</td>
<td>1,922,459</td>
<td>1,666,765</td>
<td>1,436,218</td>
<td>1,239,844</td>
</tr>
<tr>
<td>Number of tax returns processed</td>
<td>10,437,669</td>
<td>9,947,817</td>
<td>9,725,620</td>
<td>9,778,591</td>
<td>9,658,531</td>
</tr>
<tr>
<td>Number of individual refunds direct deposited</td>
<td>809,473</td>
<td>673,976</td>
<td>564,200</td>
<td>446,217</td>
<td>na</td>
</tr>
<tr>
<td>Number of individual refunds processed</td>
<td>2,634,960</td>
<td>2,732,523</td>
<td>2,654,709</td>
<td>2,664,539</td>
<td>2,595,070</td>
</tr>
<tr>
<td>Number of pieces of incoming mail</td>
<td>7,986,688</td>
<td>8,334,624</td>
<td>8,122,589</td>
<td>8,222,560</td>
<td>9,061,094</td>
</tr>
<tr>
<td>Number of pieces of outgoing mail</td>
<td>9,205,342</td>
<td>8,687,346</td>
<td>8,922,981</td>
<td>10,098,087</td>
<td>9,332,605</td>
</tr>
<tr>
<td><strong>Department of Administration</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Construction projects administered</td>
<td>71</td>
<td>226</td>
<td>181</td>
<td>213</td>
<td>205</td>
</tr>
<tr>
<td>Construction value excluding design fee (thousands)</td>
<td>$73,006</td>
<td>$873,713</td>
<td>$486,287</td>
<td>$522,060</td>
<td>$359,381</td>
</tr>
<tr>
<td><strong>Cultural Resources</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Visitation to historical sites and museums</td>
<td>2,068,910</td>
<td>2,356,046</td>
<td>2,465,484</td>
<td>2,234,241</td>
<td>1,326,603</td>
</tr>
<tr>
<td><strong>Primary and Secondary Education</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public School(K-12)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public school enrollment</td>
<td>1,368,607</td>
<td>1,346,881</td>
<td>1,325,344</td>
<td>1,303,777</td>
<td>1,285,729</td>
</tr>
<tr>
<td>Total high school graduates</td>
<td>72,580</td>
<td>74,691</td>
<td>71,853</td>
<td>69,568</td>
<td>65,681</td>
</tr>
<tr>
<td>Graduate intention to pursue further education</td>
<td>87.09%</td>
<td>84.64%</td>
<td>83.26%</td>
<td>83.63%</td>
<td>83.13%</td>
</tr>
<tr>
<td><strong>Higher Education</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Community Colleges</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of students (annualized FTE)</td>
<td>190,644</td>
<td>194,235</td>
<td>192,693</td>
<td>185,490</td>
<td>176,743</td>
</tr>
<tr>
<td>Number of certificates and degrees awarded</td>
<td>28,983</td>
<td>29,600</td>
<td>27,050</td>
<td>23,645</td>
<td>22,853</td>
</tr>
<tr>
<td><strong>Universities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of regular term students (FTE)</td>
<td>176,619</td>
<td>158,398</td>
<td>152,224</td>
<td>171,409</td>
<td>141,272</td>
</tr>
<tr>
<td>Number of certificates and degrees awarded</td>
<td>37,348</td>
<td>37,569</td>
<td>36,689</td>
<td>34,580</td>
<td>32,644</td>
</tr>
<tr>
<td><strong>Health and Human Services</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Department of Health and Human Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicaid recipients (a)</td>
<td>1,673,510</td>
<td>1,545,386</td>
<td>1,541,450</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Food stamp recipients</td>
<td>838,064</td>
<td>818,141</td>
<td>791,241</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Clients served by mental health facilities</td>
<td>16,678</td>
<td>16,884</td>
<td>16,353</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Clients served by developmental disabilities facilities</td>
<td>2,114</td>
<td>2,172</td>
<td>2,196</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Clients served by substance abuse facilities</td>
<td>3,854</td>
<td>3,633</td>
<td>3,572</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Children served through subsidized child care</td>
<td>149,946</td>
<td>155,339</td>
<td>156,534</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Participation in Special Supplemental Nutrition Program...</td>
<td>230,140</td>
<td>224,670</td>
<td>218,345</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Clients served through Work First</td>
<td>60,885</td>
<td>39,426</td>
<td>42,177</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>NC Health Choice annual enrollment</td>
<td>199,160</td>
<td>168,491</td>
<td>na</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td><strong>Economic Development</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Department of Commerce</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jobs generated company recruitment/ expansion</td>
<td>20,293</td>
<td>18,246</td>
<td>15,393</td>
<td>9,531</td>
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<td>Capital investment (thousands)</td>
<td>$3,024,914</td>
<td>$2,962,292</td>
<td>$1,863,213</td>
<td>$1,127,466</td>
<td>$2,990,123</td>
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<td>Total employed</td>
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<td>4,087,359</td>
<td>3,977,421</td>
<td>3,882,026</td>
<td>3,715,400</td>
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<td>Percentage of unemployment</td>
<td>4.56%</td>
<td>5.38%</td>
<td>5.49%</td>
<td>6.51%</td>
<td>6.27%</td>
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<td>Department of Environment and Natural Resources</td>
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<tr>
<td>Public drinking water systems in compliance</td>
<td>94%</td>
<td>93%</td>
<td>94%</td>
<td>93%</td>
<td>95%</td>
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<td>Visitation to Museum of Natural Sciences</td>
<td>622,915</td>
<td>556,422</td>
<td>913,751</td>
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<td>Visitation to NC Zoo</td>
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<td>705,030</td>
<td>676,958</td>
<td>576,093</td>
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<td>Wildlife Resources Commission</td>
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<td>Hunting licenses sold</td>
<td>204,451</td>
<td>107,242</td>
<td>107,572</td>
<td>109,511</td>
<td>114,304</td>
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<td>Fishing licenses sold</td>
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<td>331,988</td>
<td>329,314</td>
<td>302,581</td>
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<td>Vessels registered</td>
<td>363,641</td>
<td>354,096</td>
<td>361,134</td>
<td>354,863</td>
<td>358,007</td>
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<td>Department of Correction</td>
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<td>Incarcerated offenders</td>
<td>37,121</td>
<td>36,481</td>
<td>34,990</td>
<td>33,378</td>
<td>32,856</td>
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<td>Supervised offenders</td>
<td>116,513</td>
<td>117,611</td>
<td>117,196</td>
<td>118,285</td>
<td>117,374</td>
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<td>Administrative Office of the Courts</td>
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<td>Cases disposed as a % of cases filed-Superior Court</td>
<td>93.80%</td>
<td>95.52%</td>
<td>96.27%</td>
<td>93.40%</td>
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<tr>
<td>Cases disposed as a % of cases filed-District Court</td>
<td>98.10%</td>
<td>97.56%</td>
<td>95.92%</td>
<td>97.46%</td>
<td>96.76%</td>
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<td>Agriculture</td>
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<td>Department of Agriculture and Consumer Services</td>
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<td>Motor fuel dispensers tested (b)</td>
<td>109,699</td>
<td>95,735</td>
<td>103,026</td>
<td>80,390</td>
<td>85,353</td>
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<td>Rejection rate</td>
<td>10.77%</td>
<td>8.87%</td>
<td>7.22%</td>
<td>9.25%</td>
<td>9.99%</td>
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<tr>
<td>Retail scales tested (c)</td>
<td>24,896</td>
<td>27,678</td>
<td>23,335</td>
<td>29,021</td>
<td>24,021</td>
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<td>Rejection rate</td>
<td>8.28%</td>
<td>9.09%</td>
<td>8.70%</td>
<td>7.54%</td>
<td>7.07%</td>
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</table>

Notes:
(a) A significant portion of the increase in Medicaid recipients from 2005 to 2006 is the result of legislation moving children formerly covered under State Child Health Insurance Program to Medicaid for 2006. This change resulted in minimal additional cost to the Medicaid program.
(b) Governed by Gasoline and Oil Inspection Law (G.S. 119)
(c) Governed by North Carolina Weights and Measures Act (G.S. 81A)

Information prior to 2002 not available.
## CAPITAL ASSET STATISTICS BY FUNCTION

For the Fiscal Years 2002-2006

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<tr>
<td>Department of Administration</td>
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<td>7,879</td>
<td>7,961</td>
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<td>Motor Fleet vehicles</td>
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<td>16,145</td>
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<tr>
<td>Environment and Natural Resources</td>
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<td>Department of Environment and Natural Resources</td>
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<tr>
<td>Number of state park lands</td>
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<td>182,251</td>
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<td>172,763</td>
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<tr>
<td>Acres of state recreation areas</td>
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<td>12,238</td>
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<tr>
<td>Number of state natural areas</td>
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<td>17</td>
<td>17</td>
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<tr>
<td>Acres of state natural areas</td>
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<td>30,513</td>
<td>30,323</td>
<td>28,999</td>
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<td>Zoo animals (a)</td>
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<td>Boats/Trailers</td>
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<td>3,572</td>
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<td>Number of Game Lands</td>
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<td>317,467</td>
<td>325,794</td>
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<td>Acres of Game Lands</td>
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<td>Public Safety and Correction</td>
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<tr>
<td>Close security prisons</td>
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<td>Medium security prisons</td>
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<tr>
<td>Minimum security prisons</td>
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<td>37</td>
<td>36</td>
<td>36</td>
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<tr>
<td>Vehicles</td>
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<tr>
<td>Passenger/Cargo vans</td>
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<td>85</td>
<td>69</td>
<td>67</td>
<td>61</td>
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<tr>
<td>Inmate transfer vans/buses</td>
<td>481</td>
<td>418</td>
<td>398</td>
<td>391</td>
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<tr>
<td>Inmate workcrew vans/buses</td>
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<td>380</td>
<td>394</td>
<td>349</td>
<td>351</td>
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<tr>
<td>Pickup trucks</td>
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<td>275</td>
<td>325</td>
<td>248</td>
<td>277</td>
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<td>Roving patrol pickups</td>
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<td>78</td>
<td>77</td>
<td>64</td>
<td>55</td>
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<td>One ton maintenance trucks</td>
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<td>92</td>
<td>98</td>
<td>90</td>
<td>112</td>
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<td>Specialty/Other trucks (b)</td>
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<td>113</td>
<td>108</td>
<td>103</td>
<td>94</td>
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<td>Enterprise Vehicles</td>
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<tr>
<td>Passenger/Cargo vans</td>
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<td>Inmate workcrew buses</td>
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<td>Pickup trucks</td>
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<tr>
<td>One ton maintenance trucks</td>
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<td>Other/Specialty trucks</td>
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### Department of Crime Control and Public Safety

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<td>Alcohol Law Enforcement</td>
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<tr>
<td>Cars/SUV's</td>
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<td>134</td>
<td>154</td>
<td>124</td>
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<td>State Highway Patrol</td>
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<td>Cars</td>
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<td>2,283</td>
<td>2,312</td>
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<td>1,846</td>
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<td>Trucks/Vans</td>
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<td>59</td>
<td>63</td>
<td>65</td>
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<td>Motorcycles</td>
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<td>(c)</td>
<td>(c)</td>
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<td>Air craft:</td>
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### Transportation

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<th>2004</th>
<th>2003</th>
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<td>Pavement in lane-miles:</td>
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<td>Primary subsystem</td>
<td>(d)</td>
<td>14,805</td>
<td>14,760</td>
<td>14,705</td>
<td>14,670</td>
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<td>Secondary subsystem</td>
<td>(d)</td>
<td>64,204</td>
<td>64,085</td>
<td>63,910</td>
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<td>Bridges:</td>
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<td>Number of bridges</td>
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<td>Number of culverts</td>
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<td>Vehicles</td>
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<td>Heavy Equipment</td>
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### Component Units

### Higher Education

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<tbody>
<tr>
<td>Buildings</td>
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<td>1,025</td>
<td>1,064</td>
<td>1,054</td>
<td>1,043</td>
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<table>
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</thead>
<tbody>
<tr>
<td>Academic/Administrative buildings</td>
<td>930</td>
<td>918</td>
<td>893</td>
<td>873</td>
<td>866</td>
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<td>Dormitories/Auxiliary buildings</td>
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<td>585</td>
<td>537</td>
<td>524</td>
<td>510</td>
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<td>Medical</td>
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</table>

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### Notes:

(a) 500-600 fish were lost due to aquarium malfunction in 2005.
(b) Includes boom trucks, cranes, flat beds, rollbacks, yard trucks, dump trucks, semi-trucks, etc.
(c) Prior year data from the source was not available.
(d) Recent data from the source was not available, as of the date of publication.
(e) East Carolina Teaching Hospital

*Information prior to 2002 is not available.*
The following table illustrates how earned revenues (net of reinsurance) and investment income of the Public School Insurance Fund (the Fund) compare to related costs of loss (net of loss assumed by reinsurers) and other expenses assumed by the Fund for the last ten fiscal years ended June 30. The rows of the table are defined as follows:

1. Total of each fiscal year's earned contribution revenues, investment revenues, contribution revenues ceded to excess insurers or reinsurers, and amount of reported revenues net of excess insurance or reinsurance.

2. Each fiscal year's other operating costs of the Fund, including overhead and claims expense not allocable to individual claims.

3. The Fund's incurred claims (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (before the effect of loss assumed by excess insurers or reinsurers), the loss assumed by excess insurers or reinsurers, and total net amount of incurred claims and allocated claim adjustment expenses.

4. Cumulative amounts paid as of the end of successive years for each policy year.

5. The reestimated amount for loss assumed by excess insurers or reinsurers as of the end of the current year.

6. The reestimated net incurred claims and expenses based on the information available as of the end of the year. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known.

7. Comparison of the latest reestimated net incurred claims amount to the amount originally established (line 3) and indication of whether this latest estimate of claims cost is greater or less than originally thought.
As data for individual policy years mature, the correlation between original estimated and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. The columns in the table present data for successive policy years. Amounts are expressed in thousands.

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<td>6,887</td>
<td>8,136</td>
<td>9,599</td>
<td>12,255</td>
<td>10,826</td>
<td>10,219</td>
<td>12,538</td>
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<td>2,041</td>
<td>1,083</td>
<td>1,727</td>
<td>2,453</td>
<td>2,639</td>
<td>3,396</td>
<td>3,121</td>
<td>2,380</td>
<td>2,489</td>
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<td>6,313</td>
<td>5,260</td>
<td>4,660</td>
<td>5,683</td>
<td>6,960</td>
<td>8,899</td>
<td>7,405</td>
<td>7,859</td>
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<td>2,706</td>
<td>2,390</td>
<td>2,541</td>
<td>3,214</td>
<td>3,597</td>
<td>3,953</td>
<td>3,689</td>
<td>2,951</td>
<td>3,092</td>
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<td>3) Estimated claims and expenses, end of policy year:</td>
<td></td>
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<td></td>
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<td></td>
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</tr>
<tr>
<td>Incurred</td>
<td>14,351</td>
<td>8,496</td>
<td>8,615</td>
<td>21,141</td>
<td>6,449</td>
<td>4,846</td>
<td>2,690</td>
<td>12,586</td>
<td>2,093</td>
<td>3,096</td>
</tr>
<tr>
<td>Ceded</td>
<td>6,862</td>
<td>700</td>
<td>357</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td>Net incurred</td>
<td>7,489</td>
<td>7,796</td>
<td>8,258</td>
<td>21,141</td>
<td>6,449</td>
<td>4,846</td>
<td>2,690</td>
<td>12,586</td>
<td>2,093</td>
<td>3,096</td>
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<tr>
<td>4) Paid (cumulative) as of</td>
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<td>12,788</td>
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<td>4,324</td>
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<td>17,388</td>
<td>2,475</td>
<td>640</td>
<td>3,681</td>
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<tr>
<td>Four years later</td>
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<td>6,388</td>
<td>17,388</td>
<td>2,475</td>
<td>640</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Five years later</td>
<td>13,822</td>
<td>4,324</td>
<td>6,388</td>
<td>17,388</td>
<td>2,475</td>
<td>640</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Six years later</td>
<td>13,822</td>
<td>4,324</td>
<td>6,388</td>
<td>17,388</td>
<td>2,475</td>
<td>640</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Seven years later</td>
<td>13,822</td>
<td>4,324</td>
<td>6,388</td>
<td>17,388</td>
<td>2,475</td>
<td>640</td>
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<td></td>
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</tr>
<tr>
<td>Eight years later</td>
<td>13,822</td>
<td>4,324</td>
<td>6,388</td>
<td>17,388</td>
<td>2,475</td>
<td>640</td>
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<tr>
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<td>4,324</td>
<td>6,388</td>
<td>17,388</td>
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<td>640</td>
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<tr>
<td>5) Reestimated ceded claims and expenses</td>
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<tr>
<td>6) Reestimated net incurred claims and expenses:</td>
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<tr>
<td>End of policy year</td>
<td>7,489</td>
<td>7,796</td>
<td>8,258</td>
<td>21,141</td>
<td>6,449</td>
<td>4,846</td>
<td>2,690</td>
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<td>3,096</td>
</tr>
<tr>
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<td>3,543</td>
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<tr>
<td>Three years later</td>
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<tr>
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<td>3,624</td>
<td>6,031</td>
<td>17,368</td>
<td>2,475</td>
<td>4,946</td>
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<tr>
<td>Five years later</td>
<td>6,960</td>
<td>3,624</td>
<td>6,031</td>
<td>17,368</td>
<td>2,475</td>
<td>4,946</td>
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<tr>
<td>Six years later</td>
<td>6,960</td>
<td>3,624</td>
<td>6,031</td>
<td>17,368</td>
<td>2,475</td>
<td>4,946</td>
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<tr>
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<td>3,624</td>
<td>6,031</td>
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<td>4,946</td>
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<tr>
<td>Eight years later</td>
<td>6,960</td>
<td>3,624</td>
<td>6,031</td>
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<td>2,475</td>
<td>4,946</td>
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<td></td>
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</tr>
<tr>
<td>Nine years later</td>
<td>6,960</td>
<td>3,624</td>
<td>6,031</td>
<td>17,368</td>
<td>2,475</td>
<td>4,946</td>
<td></td>
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<tr>
<td>7) Increase (decrease) in estimated net incurred claims and expenses from end of policy year:</td>
<td>(529)</td>
<td>(4,172)</td>
<td>(2,227)</td>
<td>(3,773)</td>
<td>(3,974)</td>
<td></td>
<td></td>
<td>1,257</td>
<td>325</td>
<td></td>
</tr>
</tbody>
</table>
Additional copies of this document may be obtained from:

Accounting and Financial Reporting Section
North Carolina Office of the State Controller
1410 MAIL SERVICE CENTER
Raleigh, North Carolina 27699-1410

Phone requests can be made at (919) 981-5454 or (919) 981-5560 (FAX)

Internet address: http://www.ncosc.net

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