Legislative Audit Division

State of Montana

Report to the Legislature

January 2003

Financial Audit

For the Fiscal Year Ended June 30, 2002

State of Montana

Basic Financial Statements

We performed a financial audit of the Basic Financial Statements of the state of Montana for the fiscal year ended June 30, 2002. The report contains the Basic Financial Statements of the state of Montana for fiscal year 2001-02, which were prepared by the Department of Administration's Administrative Financial Services Division. We issued an unqualified opinion on these financial statements. The opinion means the reader can rely on the financial statement information presented.

This report also contains our report on compliance and internal control over financial reporting, which discusses a reportable condition concerning reconciliation of cash between accounting and bank records.

This report contains no recommendations to the Department of Administration.

Direct comments/inquiries to:
Legislative Audit Division
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

02-01

FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2003, will be issued by March 31, 2004. The Single Audit Report for the two fiscal years ended June 30, 2001, was issued on March 26, 2002. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

Legislative Audit Division
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

January 2003

The Legislative Audit Committee
of the Montana State Legislature:

This financial audit report contains our independent auditor's report on the Basic Financial Statements of the state of Montana for the fiscal year ended June 30, 2002. The Basic Financial Statements were prepared by the Administrative Financial Services Division of the Department of Administration. We performed the audit to express an opinion on the state's Basic Financial Statements. Any findings disclosed by our audit were discussed with appropriate management personnel and will be reported as part of our scheduled financial-compliance audits of state agencies.

Our report on consideration of the state of Montana's internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, and grants which is required by *Government Auditing Standards* and Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations is on page A-1. The Independent Auditor's Report is on page B-1 followed by the Basic Financial Statements, which include Management's Discussion and Analysis, the financial statements and accompanying notes, and the Budgetary Comparison Schedule and accompanying notes. We issued an unqualified opinion on the basic financial statements which means the reader can rely on the presented information. Department officials reviewed and agreed with the contents of this report.

All members of the financial-compliance audit staff contributed to this audit. We thank the Department of Administration director and staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

(Signature on File)

Scott A. Seacat
Legislative Auditor

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For additional information on the Basic Financial Statements contact:

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF BASIC FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Legislative Audit Committee
of the Montana State Legislature:

We have audited the basic financial statements of the state of Montana as of and for the fiscal year ended June 30, 2002, and have issued our report thereon dated December 31, 2002. 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.

Compliance

As part of obtaining reasonable assurance about whether the state of Montana's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards.* However, we noted certain immaterial instances of noncompliance, which we have reported to the management of the state of Montana during the course of our audit work.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the state of Montana's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the state of Montana's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition noted is described below.

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> The Department of Administration is responsible for reconciling activity in all bank accounts for the state of Montana. The state converted to a new accounting system in fiscal year 2000. Since the conversion, the department has been unable to reconcile bank activity to the accounting records. The ability to promptly reconcile bank records to the accounting records is a key control which management needs to ensure the accounting records accurately reflect the cash balances.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to the management of the state of Montana during the course of our audit work.

This report is intended for the information and use of the Legislative Audit Committee, state of Montana management, the Montana State Legislature, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Respectfully submitted,

(Signature on File)

James Gillett, CPA
Deputy Legislative Auditor

December 31, 2002

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

To the Legislative Audit Committee
of the Montana State Legislature:

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 Montana, as of and for the year ended June 30, 2002, which collectively comprise the state's basic financial statements, as follows:

Statement of Net Assets
Statement of Activities
Balance Sheet - Governmental Funds
Reconciliation of the Balance Sheet - Governmental Funds - to the Statement of Net Assets
Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds - to the Statement of Activities
Statement of Net Assets - Proprietary Funds
Statement of Revenues, Expenses, and Changes in Fund Net Assets - Proprietary Funds
Statement of Cash Flows - Proprietary Funds
Statement of Fiduciary Net Assets - Fiduciary Funds
Statement of Changes in Fiduciary Net Assets - Fiduciary Funds
Combining Statement of Net Assets - Component Units
Combining Statement of Activities - Component Units

These financial statements are the responsibility of the state of Montana'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 Montana State Lottery, which represents .12 and 2.55 percent, respectively, of the assets and revenues of the aggregate remaining fund information. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Montana State Lottery, is based on the report 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

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financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report 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 Montana, as of June 30, 2002, 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.

Management's Discussion and Analysis and the Budgetary Comparison Schedule on pages C-1 through C-8 and C-76 through C-78, respectively, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We 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.

As described in Note 2, the state of Montana has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, as of June 30, 2002.

In accordance with *Government Auditing Standards*, we have issued our report dated December 31, 2002, on our consideration of the state of Montana's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report, on page A-1, is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Respectfully submitted,

(Signature on File)

James Gillett, CPA
Deputy Legislative Auditor

December 31, 2002

State of Montana
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2002

INTRODUCTION

Management of the State of Montana provides this *Management's Discussion and Analysis* of the State of Montana's Comprehensive Annual Financial Report (CAFR) for readers of the State's financial statements. This narrative overview and analysis of the financial activities of the State of Montana is for the fiscal year ended June 30, 2002. We encourage readers to consider this information in conjunction with the additional information that is furnished in the State's financial statements, which follow.

Because the State of Montana is implementing new reporting standards of the Governmental Accounting Standards Board's Statement No. 34 for this fiscal year, which involves significant changes in content and structure, much of the information is not easily comparable to prior years. However, in future years, comparisons will be more meaningful and will go further in explaining the State's financial position and results of operations.

FINANCIAL HIGHLIGHTS –PRIMARY GOVERNMENT

Government-wide Highlights
The assets of the State exceeded its liabilities at the end of fiscal year 2002 by $2.9 billion (reported as net assets). Of this amount, $157.3 million (reported as unrestricted net assets) may be used to meet the government's general obligations to citizens and creditors. Component units reported net assets of $653.7 million.

Fund Highlights
As of the close of fiscal year 2002, the State's governmental funds reported combined ending fund balances of $2.1 billion. Of this amount, $554 million is available for spending at the government's discretion (reported as unreserved fund balance). The remaining amount of $1.52 billion is restricted for specific purposes, such as education. At the end of the fiscal year, unreserved fund balance for the General Fund was $81.3 million.

Long-term Debt
The State's total long-term debt obligations decreased by $41.8 million (or 9.3 percent) during the fiscal year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the State of Montana's basic financial statements. The State's basic financial statements include three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The report also contains additional required supplementary information (budgetary schedules). These components are described below:

Basic Financial Statements
The basic financial statements include two kinds of financial statements that present different views of the State – the *government-wide financial statements* and the *fund financial statements and combining major component unit financial statements.* These financial statements also include the *notes to the financial statements* that explain some of the information in the financial statements and provide more detail.

Government-wide Financial Statements

The *government-wide financial statements* provide a broad view of the State's operations in a manner similar to a private-sector business. The statements provide both short-term and long-term information about the State's financial position, which assists in assessing the State's economic condition at the end of the fiscal year. These are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year, even if cash involved has not been received or paid. The government-wide financial statements include two statements.

The *Statement of Net Assets* presents all of the government's assets and liabilities, with the difference between the two reported as "net assets." Over time, increases or decreases in the State's net assets may serve as a useful indicator of whether the financial position of the State is improving or deteriorating.

The *Statement of Activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the State.

Both of the above financial statements have separate sections for three different types of state programs or activities. These three types of activities are:

Governmental Activities – The activities in this section are mostly supported by taxes and intergovernmental revenues (federal grants). Most services normally associated with state government fall into this category, including education (support for both K-12 public schools and higher education), general government, health services, legal and judiciary services, museums, natural resources, public safety and defense, regulatory services, social services, and transportation.

Business-type Activities – These functions are normally intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. The business-type activities of the State include the Unemployment Insurance Fund and the Industrial Development Bond Program that assists Montana's small businesses and local governments in obtaining long-term fixed-rate financing through private Montana lending institutions.

Discretely Presented Component Units – These are operations for which the State has financial accountability but they have certain independent qualities as well. For the most part, these entities operate similar to private sector businesses and the business-type activities described above. The State has three authorities and two universities that are reported as discretely presented component units of the State.

Fund Financial Statements (Reporting the State's Major Funds)

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The State, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The fund financial statements focus on individual parts of the state government, reporting the State's operations in more detail than the government-wide statements. All of the funds of the State can be divided into three categories. It is important to note that these fund categories use different accounting approaches and should be interpreted differently. The three categories of funds are:

Governmental Funds Financial Statements – Most of the basic services provided by the State are financed through governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, the governmental fund financial statements focus on near-term inflows and outflows of spendable resources. They also focus on the balances of spendable resources

available at the end of the fiscal year. Such information may be useful in evaluating the government's near-term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the State's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the State.

The State has five governmental funds that are considered major funds for presentation purposes. That is, each major fund is presented in a separate column in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances. The State's five major governmental funds are – the General Fund, the State Special Revenue Fund, the Federal Special Revenue Fund, the Coal Severance Tax Fund, and the Land Grant Fund.

Proprietary Funds Financial Statements – When the State charges customers for the service 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 report activities that provide supplies and services to the general public. An example is the State Lottery. Internal service funds report activities that provide supplies and services for the State's other programs and activities such as the Motor Pool.

Fiduciary Funds – These funds are used to account for resources held for the benefit of parties outside the state government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of these funds are not available to support the State's own programs. Fiduciary funds use the accrual basis of accounting.

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 the fund financial statements. The notes to the financial statements can be found immediately following the component unit financial statements.

Required Supplementary Information
The basic financial statements are followed by a section of required supplementary information. This section includes a budgetary comparison schedule, which includes the reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund, as presented in the governmental fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net Assets
As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The State's combined net assets (government and business-type activities) totaled $2.9 billion at the end of fiscal year 2002.

The largest portion of the State's net assets reflects its investment in capital assets such as land, buildings, equipment and infrastructure (roads, bridges, and other immovable assets), less any related debt used to acquire those assets that is still outstanding. The State uses these capital assets to provide services to citizens; consequentially, these assets are not available for future spending. Although the State's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the State's net assets (66.4%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets may be used to meet the State's ongoing obligations to citizens and creditors. Internally imposed designations of resources are not presented as restricted net assets.

At the end of the current fiscal year, the State is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities.

Net Assets as of June 30, 2002
(expressed in thousands)

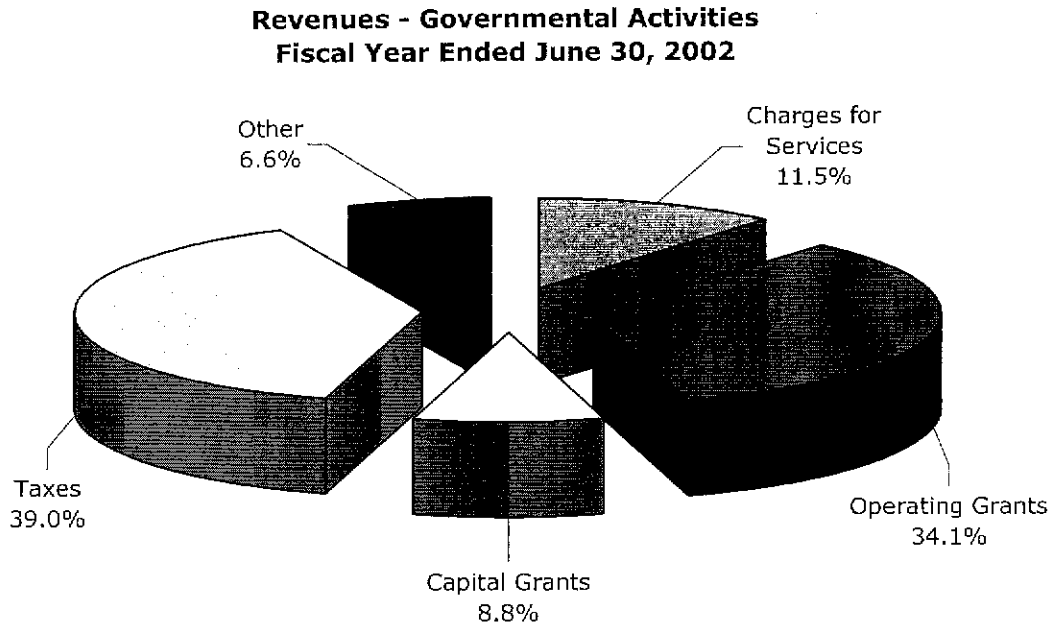
	Governmental Activities	Business-type Activities	Total Primary Government
Current and Other Assets	$2,627,061	$309,293	$2,936,354
Capital Assets	1,038,746	14,658	1,053,404
Total Assets	3,665,807	323,951	3,989,758
Long-term Liabilities	356,517	14,890	371,407
Other Liabilities	613,027	75,632	688,659
Total Liabilities	969,544	90,522	1,060,066
Invested in Capital Assets, Net of Related Debt	814,026	12,496	826,522
Restricted	1,742,193	203,710	1,945,903
Unrestricted	140,044	17,223	157,267
Total Net Assets	$2,696,263	$233,429	$2,929,692

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the State's net assets changed during the fiscal year:

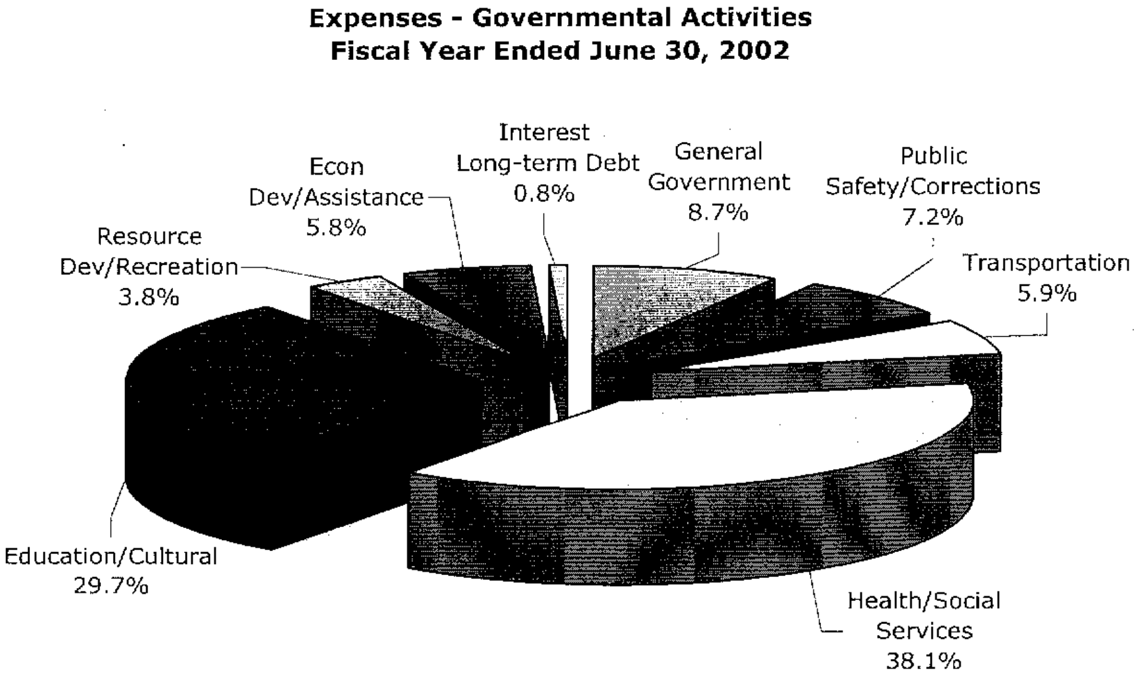
Changes in Net Assets
For Fiscal Year Ended June 30, 2002
(expressed in thousands)

	Governmental Activities	Business-type Activities	Total Primary Government
Revenues:			
Program Revenues			
Charges for Services	$ 364,614	$189,771	$ 554,385
Operating Grants	1,080,374	29,335	1,109,709
Capital Grants	280,489	602	281,091
General Revenues			
Taxes	1,238,151	12,907	1,251,058
Other	207,193	17,419	224,612
Total Revenues	3,170,821	250,034	3,420,855
Expenses:			
General Government	248,089	-	248,089
Public Safety/Corrections	205,983	-	205,983
Transportation	169,282	-	169,282
Health/Social Services	1,086,012	-	1,086,012
Educational/Cultural	845,324	-	845,324
Resource Dev/Recreation	108,642	-	108,642
Econ Dev/Assistance	164,761	-	164,761
Interest on Long-term Debt	22,763	-	22,763
Unemployment Insurance	-	83,944	83,944
Liquor Stores	-	38,074	38,074
State Lottery	-	26,585	26,585
Economic Dev Bonds	-	3,251	3,251
Hail Insurance	-	2,045	2,045
Gen Gov't Services	-	11,134	11,134
Prison Funds	-	5,444	5,444
MUS Group Insurance	-	34,594	34,594
Total Expenses	2,850,856	205,071	3,055,927
Increase (decrease) in Net Assets Before Transfers	319,965	44,963	364,928
Transfers	26,756	(26,756)	-
Change in Net Assets	346,721	18,207	364,928
Net Assets, Beg of Year (restated)	2,349,542	215,222	2,564,764
Net Assets, End of Year	$2,696,263	$233,429	$2,929,692

Governmental Activities
The following chart depicts revenues of the governmental activities for the fiscal year:



The following chart depicts expenses of the governmental activities for the fiscal year:



Business-type Activities
Net assets of the business-type activities increased by $18.2 million during the fiscal year. The majority of this increase is because in fiscal year 2002 the Unemployment Insurance Program received $18.5 million from the Reed Act. These dollars may be used to fund Wagner Peyser activities, unemployment insurance administration, or pay unemployment benefits.

FINANCIAL ANALYSIS OF THE STATE'S INDIVIDUAL FUNDS

As the State completed the year, its governmental funds reported fund balances of $2.1 billion. Of this total amount, $554 million, or 26.4%, constitutes unreserved fund balance, which is available for spending at the government's discretion. The remainder of fund balance is reserved and is not available for new spending because it has already been dedicated for various commitments.

General Fund
The General Fund is the chief operating fund of the State. At the end of the current fiscal year, unreserved fund balance of the General Fund was $81.3 million. Total fund balance diminished during the fiscal year by $93.2 million, primarily because of lower tax collections and the slowing of the economy.

<u>General Fund Budgetary Highlights</u>
Differences between the original budget and the final budget were relatively minor ($45 million) and can be briefly summarized as follows:

1. The Department of Natural Resources and Conservation received a supplemental appropriation of $3.3 million to fight fires.
2. Office of Public Instruction moved $34.9 million of their budget for special education from FY2003 to FY2002. This program has a biennial appropriation that is split into two fiscal years, but the agency was required to transfer the entire appropriation from FY2003 into FY2002, even though they only needed $4,000 in FY2002.
3. Agencies requested $696,325 in carry forward authority for 30 percent of their reverted appropriations in FY2002 per 17-7-304(4), MCA.
4. Department of Public Health and Human Services requested $3.9 million in authority be moved from FY2003 to FY2002 to cover shortfalls in Medicaid hospital, physician services and mental health services, and child support enforcement services.
5. Department of Public Health and Human Services requested $1.2 million of their biennial appropriation for the Mental Health Program be moved from FY2003 to FY2002 to cover expenditures in FY2002.
6. Department of Justice requested $200,000 of their biennial appropriation for major litigation be moved from FY2003 to FY2002 to cover FY2002 expenditures. They also requested $112,894 of their biennial appropriation for prisoner per diem costs be moved from FY2003 to FY2002 to cover FY2002 expenditures.

The supplemental appropriations were funded from available fund balance.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets
The State's investment in capital assets for its governmental and business-type activities as of June 30, 2002, amounts to $1.4 billion, net of accumulated depreciation of $309 million, leaving a net book value of $1.1 billion. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure, and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the State, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The total increase in the State's investment in capital assets for the current fiscal year was approximately 69% in terms of net book value. The significant increase in capital assets is the inclusion of infrastructure assets and highway construction. Most of the year's capital expenditures were for construction or reconstruction of roads and bridges. Depreciation charges for the year totaled $30 million. Additional information on the State's capital assets can be found in Note 4 of the notes to the financial statements .

Debt Administration
Montana receives excellent bond ratings from both Moody's Investor Service (Aa3) and Standard and Poor's Corporation (AA-). State debt may be authorized either by a two-thirds vote of the members of each house of the legislature or by a favorable vote of a majority of the State's electors voting thereon. There is no constitutional limit on the amount of debt that may be incurred by the State. The Montana Constitution does, however, prohibit the incurring of debt to cover deficits caused by appropriations exceeding anticipated revenue. State debt may be authorized by a two-thirds vote of the members of each house of the Legislature or by a majority of the electors voting thereon.

The State of Montana's general obligation debt decreased from $236.732 million at June 30, 2001, to $214.135 million at June 30, 2002.

The ratio of general obligation debt to assessed valuation and the amount of general obligation debt per capita are:

	Amount *(in thousands)*	**Ratio Debt to 2001 Assessed Value**	**State Debt Per Capita***
General Obligation Debt	$214,135	38%	$236.88

*Based on a 2001 estimated Montana population

More detailed information regarding the State's long-term obligations is presented in Note 11 to the financial statements.

ECONOMIC CONDITION AND OUTLOOK

The unemployment rate for the State of Montana was 3.4 percent in the third quarter of 2002, which is a decrease from a rate of 3.8 percent during the third quarter of 2001. This compares favorably with the nation's average unemployment rate of 6.2 percent.

In November 2001, a significant downturn in General Fund revenues was identified, and in the last half of fiscal year 2002, revenues dropped off from regular Legislative session estimates by $153 million. The primary reasons for the decline in revenues were a sharp decline in net capital gains income due to the prolonged decline in equity markets, a sharp economic recession, and federal economic stimulus legislation that impacted state income tax revenues. The Governor directed statutory spending reductions of $23 million, and the Legislature came into special session to adopt $59 million in budget balancing actions, leaving an ending fund balance projection of $40 million.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the State of Montana's finances for all of Montana's citizens, taxpayers, customers, investors and creditors. The financial report seeks to demonstrate the State's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the State of Montana, Administrative Financial Services Division, Room 255 Mitchell Building, Capitol Complex, Helena, Montana 59620.

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STATE OF MONTANA
STATEMENT OF NET ASSETS
JUNE 30, 2002
(expressed in thousands)

	PRIMARY GOVERNMENT			
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	COMPONENT UNITS
ASSETS				
Cash/cash equivalents (Note 3)	$ 436,534	$ 222,650	$ 659,184	$ 150,917
Receivables (net)	228,701	21,969	250,670	68,659
Due from primary government	-	-	-	2,136
Due from other governments	140,365	-	140,365	-
Due from component units	1,192	974	2,166	569
Internal balances	9,777	(9,777)	-	-
Inventories	25,408	6,474	31,882	4,477
Long-term loans/notes receivable	156,274	9,241	165,515	667,517
Equity in pooled investments (Note 3)	1,167,726	-	1,167,726	3,014
Investments (Note 3)	326,981	3,600	330,581	758,330
Securities lending collateral (Note 3)	126,668	1,104	127,772	74,335
Deferred charges	448	985	1,433	8,630
Restricted assets:				
Cash/cash equivalents (Note 3)	-	-	-	1,513
Notes/loans receivable	-	45,801	45,801	-
Investments (Note 3)	-	3,706	3,706	-
Capital assets (Note 4):				
Land	266,230	800	267,030	11,148
Land improvements	9,661	222	9,883	20,805
Buildings/improvements	305,086	8,964	314,050	568,112
Equipment	229,841	9,449	239,290	118,890
Infrastructure	253,676	884	254,560	30,702
Other capital assets	66,639	1,154	67,793	118,914
Construction in progress	170,884	71	170,955	17,170
Intangible assets	37,514	1,472	38,986	6,864
Less accumulated depreciation	(300,785)	(8,358)	(309,143)	(428,474)
Total capital assets	1,038,746	14,658	1,053,404	464,131
Other assets	6,987	2,566	9,553	5,511
Total assets	3,665,807	323,951	3,989,758	2,209,739
LIABILITIES				
Accounts payable	304,639	5,990	310,629	44,156
Lottery prizes payable	-	3,044	3,044	-
Due to primary government	-	-	-	2,166
Due to other governments	3,854	-	3,854	28,685
Due to component units	2,131	5	2,136	569
Deferred revenue	79,327	2,271	81,598	17,519
Lease/installment purchase payable (Note 10)	3,652	-	3,652	2,045
Bonds/notes payable (net) (Note 11)	336,558	71,204	407,762	903,503
Property held in trust	4,454	629	5,083	4,906
Securities lending liability (Note 3)	126,668	1,104	127,772	74,335
Compensated absences payable (Note 11)	66,456	978	67,434	39,328
Estimated insurance claims (Note 8)	39,012	5,125	44,137	437,301
Early retirement benefits payable (Note 11)	336	-	336	-
Arbitrage rebate tax payable	1,451	172	1,623	1,503
Other liabilities	1,006	-	1,006	-
Total liabilities	969,544	90,522	1,060,066	1,556,016

	PRIMARY GOVERNMENT			
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	COMPONENT UNITS
NET ASSETS				
Invested in capital assets, net of related debt	$ 814,026	$ 12,496	$ 826,522	$ 259,223
Restricted for:				
Transportation	80,159	-	80,159	-
Fish, wildlife, and parks	43,889	-	43,889	-
Federal grants	23,148	-	23,148	-
Construction and debt service	6,305	-	6,305	-
Unemployment compensation	-	195,572	195,572	-
Funds held as permanent investments:				
Expendable	176,500	-	176,500	10,528
Nonexpendable	1,269,066	-	1,269,066	9,392
Housing authority	-	-	-	121,403
Reclamation	140,156	-	140,156	-
Other purposes	2,970	8,138	11,108	13,178
Unrestricted	140,044	17,223	157,267	239,999
Total net assets	$ 2,696,263	$ 233,429	$ 2,929,692	$ 653,723

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

FUNCTIONS/PROGRAMS	EXPENSES	PROGRAM REVENUES: CHARGES FOR SERVICES	PROGRAM REVENUES: OPERATING GRANTS AND CONTRIBUTIONS	PROGRAM REVENUES: CAPITAL GRANTS AND CONTRIBUTIONS	NET (EXPENSE) REVENUE
Primary government:					
Governmental activities:					
General government	$ 248,089	$ 38,368	$ 22,835	$ 27	$ (186,859)
Public safety/corrections	205,983	122,840	63,899	-	(19,244)
Transportation	169,282	32,269	5,408	280,442	148,837
Health/social services	1,086,012	40,847	761,197	-	(283,968)
Education/cultural	845,324	69,242	107,926	20	(668,136)
Resource development/recreation	108,642	45,787	16,803	-	(46,052)
Economic development/assistance	164,761	15,261	102,306	-	(47,194)
Interest on long-term debt	22,763	-	-	-	(22,763)
Total governmental activities	2,850,856	364,614	1,080,374	280,489	(1,125,379)
Business-type activities:					
Unemployment Insurance	83,944	59,771	29,335	-	5,162
Liquor Stores	38,074	45,630	-	-	7,556
State Lottery	26,585	33,670	-	-	7,085
Economic Development Bonds	3,251	13	-	-	(3,238)
Hail Insurance	2,045	301	-	-	(1,744)
General Government Services	11,134	11,202	-	602	670
Prison Funds	5,444	5,583	-	-	139
MUS Group Insurance	34,594	33,601	-	-	(993)
Total business-type activities	205,071	189,771	29,335	602	14,637
Total primary government	$ 3,055,927	$ 554,385	$ 1,109,709	$ 281,091	$ (1,110,742)
Component units:					
Authorities:					
Housing Authority	$ 46,396	$ 235	$ 241	$ -	$ (45,920)
Facility Finance Authority	231	256	-	-	25
State Compensation Insurance (New Fund)	122,285	93,259	-	-	(29,026)
State Compensation Insurance (Old Fund)	832	-	-	-	(832)
State University System:					
Montana State University	303,672	129,601	95,363	7,367	(71,341)
University of Montana	240,114	104,750	65,216	1,579	(68,569)
Total component units	$ 713,530	$ 328,101	$ 160,820	$ 8,946	$ (215,663)

The notes to the financial statements are an integral part of this statement.

	PRIMARY GOVERNMENT			
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTALS	COMPONENT UNITS
Changes in net assets:				
Net (expense) revenue	$ (1,125,379)	$ 14,637	$ (1,110,742)	$ (215,663)
General revenues:				
Taxes:				
Property	167,488	-	167,488	-
Fuel	191,248	-	191,248	-
Natural resource	96,336	-	96,336	-
Individual income	525,647	-	525,647	-
Corporate income	69,176	-	69,176	-
Other	188,256	12,907	201,163	30
Settlements	58,549	-	58,549	-
Unrestricted investment earnings	151,716	16,382	168,098	99,936
Payment from State of Montana	-	-	-	139,374
Gain (loss) on sale of capital assets	(7,532)	(3)	(7,535)	79
Miscellaneous	4,460	1,040	5,500	7,291
Transfers	26,756	(26,756)	-	-
Total general revenues and transfers	1,472,100	3,570	1,475,670	246,710
Change in net assets	346,721	18,207	364,928	31,047
Total net assets - July 1	2,347,525	209,766	2,557,291	624,113
Prior period adjustments	2,017	5,456	7,473	(1,437)
Total net assets - July 1 - as restated	2,349,542	215,222	2,564,764	622,676
Total net assets - June 30	$ 2,696,263	$ 233,429	$ 2,929,692	$ 653,723

STATE OF MONTANA
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2002
(expressed in thousands)

	GENERAL	SPECIAL REVENUE STATE	SPECIAL REVENUE FEDERAL	PERMANENT COAL SEVERANCE TAX	PERMANENT LAND GRANT	NONMAJOR	TOTALS
ASSETS							
Cash/cash equivalents (Note 3)	$ 33,941	$ 243,508	$ 34,963	$ 35,727	$ 11,892	$ 57,647	$ 417,678
Receivables (net)	117,265	74,414	8,004	8,053	5,052	4,485	217,273
Interfund loans receivable (Note 12)	80,907	44,376	241	-	-	-	125,524
Due from other governments	59	1,182	139,122	-	-	-	140,363
Due from component units	407	417	67	-	-	25	916
Due from other funds (Note 12)	19,878	12,638	1,349	3	6,835	1,252	41,955
Inventories	2,506	22,030	30	-	-	-	24,566
Equity in pooled investments (Note 3)	-	190,258	-	412,040	418,389	147,037	1,167,724
Long-term loans/notes receivable	67	119,451	911	-	-	35,846	156,275
Advances to other funds (Note 12)	160	10,305	300	46,368	-	1,698	58,831
Investments (Note 3)	-	110,716	5,267	186,108	-	16,227	318,318
Securities lending collateral (Note 3)	-	32,445	-	36,100	36,657	18,777	123,979
Other assets	3,823	1,128	1,619	-	-	4	6,574
Total assets	$ 259,013	$ 862,868	$ 191,873	$ 724,399	$ 478,825	$ 282,998	$ 2,799,976
LIABILITIES AND FUND BALANCES							
Liabilities:							
Accounts payable	113,379	85,091	76,701	-	4,937	3,652	283,760
Interfund loans payable (Note 12)	-	39,143	75,803	-	-	4,425	119,371
Advances from other funds (Note 12)	-	49,253	356	-	-	8,996	58,605
Due to other governments	18	1,425	2,411	-	-	-	3,854
Due to component units	12,471	812	856	-	408	3	14,550
Due to other funds (Note 12)	3,304	6,362	4,113	5,907	15,198	2,418	37,302
Deferred revenue	39,313	31,781	8,095	-	-	31	79,220
Property held in trust	1,285	2,536	389	-	-	191	4,401
Securities lending liability (Note 3)	-	32,445	-	36,100	36,657	18,777	123,979
Other liabilities	-	50	3	-	-	-	53
Total liabilities	169,770	248,898	168,727	42,007	57,200	38,493	725,095
Fund balances:							
Reserved for:							
Encumbrances	5,194	22,712	12,157	-	-	442	40,505
Inventories	2,506	22,030	-	-	-	-	24,536
Long-term loans	67	119,451	911	-	-	35,846	156,275
Long-term advances (Note 12)	160	10,305	300	46,367	-	1,698	58,830
Debt service	-	-	-	-	-	6,000	6,000
Trust principal (Note 14)	-	-	-	636,025	421,625	165,047	1,222,697
Fed Family Ed Loan Prog (Note 14)	-	-	12,062	-	-	-	12,062
Unreserved, designated (Note 1)	3,200	378	-	-	-	24,630	28,208
Unreserved, undesignated, reported in:							
General fund	78,116	-	-	-	-	-	78,116
Special revenue funds	-	439,094	(2,284)	-	-	-	436,810
Debt service funds	-	-	-	-	-	(2,645)	(2,645)
Capital projects funds	-	-	-	-	-	13,487	13,487
Total fund balances	89,243	613,970	23,146	682,392	421,625	244,505	2,074,881
Total liabilities and fund balances	$ 259,013	$ 862,868	$ 191,873	$ 724,399	$ 478,825	$ 282,998	$ 2,799,976

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS TO THE STATEMENT OF NET ASSETS
JUNE 30, 2002
(expressed in thousands)

Total fund balances for governmental funds		$ 2,074,881
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 not reported in the funds. (Note 4)		
Land	265,994	
Land improvements	9,566	
Buildings/improvements	302,293	
Equipment	68,211	
Infrastructure	253,676	
Other capital assets	66,639	
Construction in progress	170,127	
Intangible assets	37,308	
Less accumulated depreciation	(209,104)	964,710
Certain tax revenues are earned, but not available and therefore deferred in the funds.		8,538
Internal service funds are used by management to charge the costs of certain activities, such as insurance and central computer services, to individual funds. The assets and liabilities of the internal service funds are included in the governmental activities in the statement of net assets.		48,343
Deferred issue costs are reported as current expenditures in the funds. These costs are amortized over the life of the bonds and included in govermental activities in the statement of net assets.		448
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.		
Accrued interest	(2,344)	
Lease/installment purchase payable (Note 10)	(1,608)	
Bonds/notes payable (net) (Note 11)	(331,642)	
Compensated absences payable (Note 11)	(62,323)	
Early retirement benefits payable (Note 11)	(336)	
Arbitrage rebate tax payable (Note 11)	(1,451)	
Other liabilities	(953)	(400,657)
Net assets of governmental activities		$ 2,696,263

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

		SPECIAL REVENUE		PERMANENT			
	GENERAL	STATE	FEDERAL	COAL SEVERANCE TAX	LAND GRANT	NONMAJOR	TOTALS
REVENUES							
Licenses/permits	$ 115,644	$ 85,586	$ -	$ -	$ 907	$ 353	$ 202,490
Taxes:							
Natural resource	25,018	49,385	-	15,610	-	6,323	96,336
Individual income	518,112	-	-	-	-	-	518,112
Corporate income	68,173	-	-	-	-	-	68,173
Property	167,178	310	-	-	-	-	167,488
Fuel	-	191,235	-	-	-	13	191,248
Other (Note 1)	151,200	35,335	1	-	-	1,720	188,256
Charges for services/fines/forfeits/settlements	51,658	74,583	32,324	-	-	13,761	172,326
Investment earnings	12,991	28,762	618	47,930	36,546	19,137	145,984
Securities lending income	608	888	7	1,207	1,209	539	4,458
Sale of documents/merchandise/property	291	6,704	2	-	6,488	2,086	15,571
Rentals/leases/royalties	57	530	-	-	23,721	130	24,438
Contributions/premiums	-	6,094	-	-	-	-	6,094
Grants/contracts/donations	1,220	19,480	81	-	-	83	20,864
Federal	22,334	1,284	1,316,233	-	-	-	1,339,851
Federal indirect cost recoveries	94	-	2,667	-	-	-	2,761
Other revenues	488	3,297	532	-	9	133	4,459
Total revenues	1,135,066	503,473	1,352,465	64,747	68,880	44,278	3,168,909
Intrafund revenues	-	(481)	(1,075)	-	-	-	(1,556)
Net revenues	1,135,066	502,992	1,351,390	64,747	68,880	44,278	3,167,353
EXPENDITURES							
Current:							
General government	155,774	64,699	3,667	-	-	4,632	228,772
Public safety/corrections	129,000	29,325	29,873	-	-	1,309	189,507
Transportation	174	154,452	285,546	-	-	-	440,172
Health/social services	277,805	69,842	731,656	-	-	-	1,079,303
Education/cultural	661,586	64,549	132,357	-	2,539	3	861,034
Resource development/recreation	26,350	63,878	21,160	-	-	-	111,388
Economic development/assistance	21,550	47,730	94,136	-	-	479	163,895
Debt service:							
Principal retirement	523	1,211	182	-	-	34,842	36,758
Interest/fiscal charges	59	3,949	20	-	-	15,752	19,780
Capital outlay	1,865	22,626	11,844	-	-	28,721	65,056
Securities lending	531	778	6	1,072	1,074	475	3,936
Total expenditures	1,275,217	523,039	1,310,447	1,072	3,613	86,213	3,199,601
Intrafund expenditures	-	(481)	(1,075)	-	-	-	(1,556)
Net expenditures	1,275,217	522,558	1,309,372	1,072	3,613	86,213	3,198,045
Excess of revenue over (under) expenditures	(140,151)	(19,566)	42,018	63,675	65,267	(41,935)	(30,692)
OTHER FINANCING SOURCES (USES)							
Loan proceeds	-	727	-	-	-	1,405	2,132
Bond proceeds	-	1,785	-	-	-	-	1,785
Proceeds of refunding bonds	-	33,605	-	-	-	-	33,605
Discount on bonds/notes issued	-	(139)	-	-	-	-	(139)
Payment to refunded bond escrow agent	-	(21,037)	-	-	-	(13,719)	(34,756)
Inception of lease/installment contract	233	48	201	-	-	-	482
General capital asset sale proceeds	82	227	1	-	-	-	310
Operating transfers in (Note 12)	73,739	122,004	8,054	219	46,451	70,895	321,362
Operating transfers out (Note 12)	(33,651)	(89,367)	(53,210)	(43,120)	(54,387)	(22,994)	(296,729)
Total other financing sources (uses)	40,403	47,853	(44,954)	(42,901)	(7,936)	35,587	28,052
Excess of revenues/other sources over (under) expenditures/other uses	(99,748)	28,287	(2,936)	20,774	57,331	(6,348)	(2,640)
Fund balances - July 1 - as previously reported	182,429	581,903	32,490	661,618	415,554	254,644	2,128,638
Prior period adjustments (Note 2)	7,445	4,566	(6,408)	-	-	(3,791)	1,812
Cumulative effect of acctng change (Note 2)	-	-	-	-	(51,260)	-	(51,260)
Fund balances - July 1 - as restated	189,874	586,469	26,082	661,618	364,294	250,853	2,079,190
Increase (decrease) in inventories	(883)	(786)	-	-	-	-	(1,669)
Fund balances - June 30	$ 89,243	$ 613,970	$ 23,146	$ 682,392	$ 421,625	$ 244,505	$ 2,074,881

The notes to the financial statements are an integral part of this statement.

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STATE OF MONTANA
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE TO THE STATEMENT OF ACTIVITIES
JUNE 30, 2002
(expressed in thousands)

Net change in fund balances - total governmental funds		$ (2,640)
Amounts reported for governmental activities in the statement of activities are different because:		
Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period. (Note 4)		
Capital outlay	354,013	
Depreciation expense	(17,451)	336,562
In the statement of activities, only the gain or loss on the sale of capital assets is reported. However, in the governmental funds, the proceeds from the sale increase financial resources. Thus, the change in net assets differs from the change in fund balance by the cost of the capital assets sold.		(7,842)
Donations of capital assets or transfers of capital assets to other funds affects net assets in the statement of activities, but these transactions do not appear in the governmental funds because they are not financial resources.		(3,682)
Inventories of governmental funds are recorded as expenditures when purchased. However, in the statement of activities, inventories are expensed when consumed.		(1,669)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.		8,526
Internal service funds are used by management to charge the costs of certain activities, such as insurance and central computer services, to individual funds. The net revenue (expense) of the internal service funds is reported with governmental activities.		(9,224)
The incurrence of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. The details of these differences is as follows:		
Loan proceeds	(2,132)	
Bond proceeds	(1,785)	
Proceeds of refunding bonds	(33,605)	
Discount on bonds/notes issued	139	
Capital lease financing	(482)	
Principal retirement	36,758	
Payment to refunded bond escrow agent	34,756	
Issuance costs	482	
Bond issuance costs amortization	(34)	
Bond refunding loss amoritzation	(93)	
Bond discount amortization	(9)	33,995

Some expenses reported in the statement of activities do not require the use of current financial resources, and therefore are not reported as expenditures in the governmental funds. The details of these differences is as follows:

Accrued interest	(2,490)	
Compensated absences	(3,471)	
Early retirement benefits	19	
Arbitrage rebate tax	(1,166)	
Other liabilities	(197)	(7,305)
Change in net assets of governmental activities		$ 346,721

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2002
(expressed in thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	UNEMPLOYMENT INSURANCE	ECONOMIC DEVELOPMENT BONDS	NONMAJOR	TOTALS	
ASSETS					
Current assets:					
Cash/cash equivalents	$ 193,761	$ 7,810	$ 21,079	$ 222,650	$ 18,855
Receivables (net)	2,373	5,617	13,980	21,970	2,738
Interfund loans receivable (Note 12)	-	-	6	6	315
Due from other funds (Note 12)	18	-	282	300	6,237
Due from component units	-	-	974	974	356
Inventories	-	-	6,474	6,474	842
Short-term investments	-	1,444	-	1,444	-
Securities lending collateral (Note 3)	-	-	1,104	1,104	2,689
Other current assets	-	-	170	170	412
Total current assets	196,152	14,871	44,069	255,092	32,444
Noncurrent assets:					
Restricted assets:					
Restricted notes/loans receivable	-	45,801	-	45,801	-
Restricted investments	-	3,706	-	3,706	-
Total restricted assets	-	49,507	-	49,507	-
Advances to other funds (Note 12)	-	-	676	676	-
Long-term investments (Note 3)	-	414	1,742	2,156	8,663
Long-term notes/loans receivable	-	9,238	3	9,241	-
Deferred charges	-	985	-	985	-
Other long-term assets	-	-	2,393	2,393	-
Capital assets (Note 4):					
Land	-	-	800	800	236
Land improvements	-	-	222	222	95
Buildings/improvements	-	-	8,964	8,964	2,793
Equipment	-	12	9,437	9,449	161,630
Infrastructure	-	-	884	884	-
Other capital assets	-	-	1,154	1,154	-
Construction in progress	-	-	71	71	757
Intangible assets	-	-	1,472	1,472	206
Less accumulated depreciation	-	(4)	(8,352)	(8,356)	(91,681)
Total capital assets	-	8	14,652	14,660	74,036
Total noncurrent assets	-	60,152	19,466	79,618	82,699
Total assets	196,152	75,023	63,535	334,710	115,143

STATE OF MONTANA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2002
(expressed in thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	UNEMPLOYMENT INSURANCE	ECONOMIC DEVELOPMENT BONDS	NONMAJOR	TOTALS	
LIABILITIES					
Current liabilities:					
Accounts payable	$ 97	$ 805	$ 5,087	$ 5,989	$ 5,762
Lottery prizes payable	-	-	1,337	1,337	-
Interfund loans payable (Note 12)	-	-	275	275	6,200
Due to component units	-	-	5	5	39
Due to other funds (Note 12)	152	4	10,218	10,374	1,051
Deferred revenue	-	18	2,217	2,235	109
Lease/installment purchase payable (Note 10)	-	-	-	-	1,291
Bonds/notes payable - net (Note 11)	-	59,330	1,055	60,385	2,075
Property held in trust	331	172	126	629	54
Securities lending liability (Note 3)	-	-	1,104	1,104	2,689
Estimated insurance claims (Note 8)	-	-	3,348	3,348	15,085
Compensated absences payable (Note 11)	-	18	473	491	2,090
Arbitrage rebate tax payable	-	72	-	72	-
Total current liabilities	580	60,419	25,245	86,244	36,445
Long-term liabilities:					
Lottery prizes payable	-	-	1,707	1,707	-
Advances from other funds (Note 12)	-	-	111	111	790
Deferred revenue	-	36	-	36	-
Lease/installment purchase payable (Note 10)	-	-	-	-	753
Bonds/notes payable - net (Note 11)	-	9,709	1,110	10,819	2,841
Estimated insurance claims (Note 8)	-	-	1,777	1,777	23,928
Compensated absences payable (Note 11)	-	16	471	487	2,043
Arbitrage rebate tax payable	-	100	-	100	-
Total long-term liabilities	-	9,861	5,176	15,037	30,355
Total liabilities	580	70,280	30,421	101,281	66,800
NET ASSETS					
Invested in capital assets, net of related debt	-	8	12,487	12,495	69,119
Restricted for:					
Unemployment Compensation	195,572	-	-	195,572	-
Other Purposes	-	2,460	5,678	8,138	-
Unrestricted	-	2,275	14,949	17,224	(20,776)
Total net assets	$ 195,572	$ 4,743	$ 33,114	$ 233,429	$ 48,343

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	UNEMPLOYMENT INSURANCE	ECONOMIC DEVELOPMENT BONDS	NONMAJOR	TOTALS	
Operating revenues:					
Charges for services	$ -	$ 12	$ 89,464	$ 89,476	$ 87,053
Investment earnings	12,200	576	688	13,464	1,126
Securities lending income	-	-	25	25	148
Financing income	-	2,893	-	2,893	-
Contributions/premiums	59,598	-	40,513	100,111	73,280
Grants/contracts/donations	29,335	-	-	29,335	-
Taxes	-	-	12,907	12,907	2
Other operating revenues	710	-	514	1,224	2,052
Total operating revenues	101,843	3,481	144,111	249,435	163,661
Operating expenses:					
Personal services	-	172	8,728	8,900	30,539
Contractual services	-	65	10,865	10,930	13,809
Supplies/materials	-	8	39,415	39,423	16,280
Benefits/claims	83,775	-	37,334	121,109	86,723
Depreciation	-	2	1,055	1,057	10,596
Amortization	-	-	187	187	592
Utilities/rent	-	38	536	574	8,509
Communications	-	8	1,040	1,048	9,304
Travel	-	5	135	140	449
Repair/maintenance	-	1	325	326	7,021
Lottery prize payments	-	-	17,104	17,104	-
Interest expense	-	2,872	134	3,006	342
Securities lending expense	-	-	22	22	132
Arbitrage rebate tax	-	47	-	47	-
Other operating expenses	-	33	1,097	1,130	1,741
Total operating expenses	83,775	3,251	117,977	205,003	186,037
Operating income (loss)	18,068	230	26,134	44,432	(22,376)
Nonoperating revenues (expenses):					
Gain (loss) on sale of capital assets	-	-	(3)	(3)	144
Federal indirect cost recoveries	-	-	-	-	4,217
Increase (decrease) value of livestock	-	-	(68)	(68)	-
Total nonoperating revenues (expenses)	-	-	(71)	(71)	4,361
Income (loss) before contributions and transfers	18,068	230	26,063	44,361	(18,015)
Capital contributions	-	-	602	602	3,833
Operating transfers in (Note 12)	-	-	120	120	3,400
Operating transfers out (Note 12)	-	-	(26,876)	(26,876)	(986)
Change in net assets	18,068	230	(91)	18,207	(11,768)
Total net assets - July 1 - as previously reported	177,577	4,490	22,583	204,650	38,154
Prior period adjustments (Note 2)	(73)	-	5,529	5,456	2,544
Cumulative effect of acctng change (Note 2)	-	23	5,093	5,116	19,413
Total net assets - July 1 - as restated	177,504	4,513	33,205	215,222	60,111
Total net assets - June 30	$ 195,572	$ 4,743	$ 33,114	$ 233,429	$ 48,343

The notes to the financial statements are an integral part of this statement.

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STATE OF MONTANA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	UNEMPLOYMENT INSURANCE	ECONOMIC DEVELOPMENT BONDS	NONMAJOR	TOTALS	
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from sales and services	$ 59,404	$ 12	$ 129,386	$ 188,802	$ 161,954
Payments to suppliers for goods and services	-	(159)	(52,957)	(53,116)	(57,993)
Payments to employees	-	(183)	(8,790)	(8,973)	(30,751)
Grant receipts	29,335	-	-	29,335	4,097
Cash payments for claims	(83,733)	-	(37,803)	(121,536)	(80,076)
Cash payments for prizes	-	-	(17,305)	(17,305)	-
Collection of payroll taxes	-	-	-	-	2
Other operating revenues	710	-	286	996	731
Net cash provided by (used for) operating activities	5,716	(330)	12,817	18,203	(2,036)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Payment of principal and interest on bonds and notes	-	(6,842)	-	(6,842)	(3,118)
Proceeds from issuance of bonds and notes	-	1,044	-	1,044	2,043
Collection of taxes	-	-	12,907	12,907	-
Transfers to other funds	-	-	(24,787)	(24,787)	(864)
Transfers from other funds	-	-	120	120	3,392
Cash payments for loans	-	-	-	-	(283)
Proceeds from interfund loans/advances	-	-	293	293	6,250
Payments of interfund loans/advances	(500)	-	(524)	(1,024)	(702)
Net cash provided by (used for) noncapital financing activities	(500)	(5,798)	(11,991)	(18,289)	6,718
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Acquisition of capital assets	-	(6)	(440)	(446)	(7,869)
Proceeds from sale of capital assets	-	-	-	-	1,080
Principal and interest payments on bonds and notes	-	-	(1,146)	(1,146)	(3,006)
Net cash used for capital and related financing activities	-	(6)	(1,586)	(1,592)	(9,795)
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of investments	-	(312)	(497)	(809)	-
Proceeds from sales or maturities of investments	-	1,363	250	1,613	7,905
Proceeds from securities lending transactions	-	-	25	25	149
Interest and dividends on investments	12,127	550	1,259	13,936	1,207
Payment of securities lending costs	-	-	(23)	(23)	(132)
Collections of principal and interest on loans	-	17,451	-	17,451	-
Cash payments for loans	-	(17,121)	-	(17,121)	-
Arbitrage rebate tax	-	(248)	-	(248)	-
Net cash provided by (used for) investing activities	12,127	1,683	1,014	14,824	9,129
Net increase (decrease) in cash and cash equivalents	17,343	(4,451)	254	13,146	4,016
Cash and cash equivalents, July 1	176,418	12,261	20,825	209,504	14,839
Cash and cash equivalents, June 30	$ 193,761	$ 7,810	$ 21,079	$ 222,650	$ 18,855

The notes to the financial statements are an integral part of this statement.

	BUSINESS-TYPE ACTIVITIES -- ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES -- INTERNAL SERVICE FUNDS
	UNEMPLOYMENT INSURANCE	ECONOMIC DEVELOPMENT BONDS	NONMAJOR	TOTALS	
Reconciliation of operating income to net cash provided by operating activities:					
Operating income (loss)	$ 18,068	$ 230	$ 26,134	$ 44,432	$ (22,376)
Adjustments to reconcile operating income to net cash provided by (used for) operating activities:					
Depreciation	-	2	1,055	1,057	10,596
Amortization	-	-	187	187	-
Taxes	-	-	(12,907)	(12,907)	-
Interest expense	-	2,872	134	3,006	342
Securities lending expense	-	-	22	22	132
Interest on investments	(12,200)	(576)	(688)	(13,464)	(1,126)
Securities lending income	-	-	(25)	(25)	(148)
Financing income	-	(2,893)	-	(2,893)	-
Federal indirect cost recoveries	-	-	-	-	4,217
Arbitrage rebate tax	-	47	-	47	-
Change in assets and liabilities:					
Decr (incr) in accounts receivable	-	-	(582)	(582)	(2,358)
Decr (incr) in due from other governments	-	-	-	-	13
Decr (incr) in due from other funds	(18)	-	66	48	1,632
Decr (incr) in due from component units	-	-	(75)	(75)	473
Decr (incr) in inventories	-	-	878	878	(102)
Decr (incr) in intangible assets	-	-	(182)	(182)	-
Decr (incr) in other assets	-	-	25	25	(82)
Incr (decr) in accounts payable	42	-	(378)	(336)	83
Incr (decr) in lottery prizes payable	-	-	(389)	(389)	-
Incr (decr) in due to other funds	(176)	(8)	(232)	(416)	(1,147)
Incr (decr) in due to component units	-	-	(10)	(10)	11
Incr (decr) in due to other governments	-	-	(51)	(51)	-
Incr (decr) in deferred revenue	-	-	(248)	(248)	53
Incr (decr) in property held in trust	-	-	55	55	35
Incr (decr) in compensated absences payable	-	(4)	125	121	1,118
Incr (decr) in estimated claims	-	-	(97)	(97)	6,598
Net cash provided by (used for) operating activities	$ 5,716	$ (330)	$ 12,817	$ 18,203	$ (2,036)
Schedule of noncash transactions:					
Capital asset acquisitions from capital leases	$ -	$ -	$ -	$ -	$ 1,002
Total noncash transactions	$ -	$ -	$ -	$ -	$ 1,002

STATE OF MONTANA
STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2002
(expressed in thousands)

	PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUNDS	PRIVATE PURPOSE TRUST FUNDS	INVESTMENT TRUST	AGENCY FUNDS
ASSETS				
Cash/cash equivalents (Note 3)	$ 126,302	$ 6,759	$ 761,216	$ 47,273
Receivables (net):				
Accounts receivable	20,538	-	-	-
Interest	24,499	68	473	57,361
Other receivables	-	-	-	645
Due from primary government	12,459	-	-	-
Due from other funds	2,274	311	-	-
Long-term loans/notes receivable	497	1,756	-	-
Total receivables	60,267	2,135	473	58,006
Investments at fair value:				
Equity in pooled investments (Note 3)	4,223,399	-	-	-
Other investments (Note 3)	920,764	-	-	-
Total investments	5,144,163	-	-	-
Securities lending collateral (Note 3)	254,736	-	-	-
Capital Assets:				
Land	35	-	-	-
Buildings/improvements	158	-	-	-
Equipment	142	-	-	-
Accumulated depreciation	(236)	-	-	-
Intangible assets	3,837	-	-	-
Total capital assets	3,936	-	-	-
Other assets	-	-	-	16,570
Total assets	5,589,404	8,894	761,689	121,849
LIABILITIES				
Accounts payable	26,335	11	473	16,848
Due to primary government	81	-	-	-
Due to other funds	310	75	-	-
Deferred revenue	20	-	-	-
Bonds/notes payable (net)	1,563	-	-	-
Property held in trust	-	3,241	-	103,049
Securities lending liability (Note 3)	254,736	-	-	-
Compensated absences payable	344	-	-	-
Other liabilities	-	-	-	1,952
Total liabilities	283,389	3,327	473	121,849
NET ASSETS				
Held in trust for pension benefits and other purposes	$ 5,306,015	$ 5,567	$ 761,216	$ -

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

	PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUNDS	PRIVATE PURPOSE TRUST FUNDS	INVESTMENT TRUST
ADDITIONS			
Contributions/premiums:			
Employer	$ 135,494	$ -	$ -
Employee	130,414	-	-
Other contributions	1,234	-	1,086,090
Net investment earnings:			
Investment earnings	(397,732)	236	21,722
Administrative investment expense	(7,397)	-	-
Securities lending income	7,183	1	394
Securities lending expense	(6,189)	(1)	(353)
Contracts/grants/donations	-	325	-
Charges for services	222	13	-
Total additions	(136,771)	574	1,107,853
DEDUCTIONS			
Benefits	287,250	8	1,114,877
Refunds	18,875	-	-
Administrative expenses:			
Personal services	1,898	67	-
Contractual services	3,678	84	-
Supplies/materials	112	9	-
Depreciation	14	-	-
Amortization	514	-	-
Utilities/rent	135	3	-
Communications	159	4	-
Travel	70	13	-
Repair/maintenance	22	-	-
Grants	-	12	-
Interest expense	43	-	-
Other operating expenses	268	-	-
Local assistance	13	-	-
Transfer to other funds	-	395	-
Total deductions	313,051	595	1,114,877
Change in net assets	(449,822)	(21)	(7,024)
Net assets - July 1 - as previously reported	5,756,333	5,617	768,240
Prior period adjustments	(496)	(29)	-
Net assets - July 1 - as restated	5,755,837	5,588	768,240
Net assets - June 30	$ 5,306,015	$ 5,567	$ 761,216

The notes to the financial statements are an integral part of this statement.

STATE OF MONTANA
COMBINING STATEMENT OF NET ASSETS
COMPONENT UNITS
JUNE 30, 2002
(expressed in thousands)

	AUTHORITIES			
	HOUSING AUTHORITY	FACILITY FINANCE AUTHORITY	STATE COMPENSATION INSURANCE (NEW FUND)	STATE COMPENSATION INSURANCE (OLD FUND)
ASSETS				
Cash/cash equivalents (Note 3)	$ 4,938	$ 1,808	$ 22,025	$ 5,406
Receivables (net)	16,014	190	11,690	2,431
Due from primary government	-	-	5	1
Due from component units	-	-	516	-
Inventories	-	-	-	-
Long-term loans/notes receivable	641,024	252	52	-
Equity in pooled investments (Note 3)	-	-	-	-
Investments (Note 3)	148,988	-	496,155	109,352
Securities lending collateral (Note 3)	-	-	57,563	16,600
Deferred charges	6,703	-	-	-
Restricted cash/cash equivalents	-	-	-	-
Capital assets (Note 4):				
Land	-	-	-	-
Land improvements	-	-	-	-
Buildings/improvements	-	-	-	-
Equipment	88	2	3,094	-
Infrastructure	-	-	-	-
Other capital assets	-	-	-	-
Construction in progress	-	-	-	-
Intangible assets	107	-	3,098	-
Less accumulated depreciation	(41)	(1)	(1,903)	-
Total capital assets	154	1	4,289	-
Other assets	175	1	1,673	-
Total assets	817,996	2,252	593,968	133,790
LIABILITIES				
Accounts payable	4,373	9	4,209	231
Due to primary government	34	1	795	3
Due to other governments	-	-	-	-
Due to component units	-	-	-	516
Deferred revenue	-	-	584	611
Lease/installment purchase payable (Note 10)	-	-	291	-
Bonds/notes payable (net) (Note 11)	689,923	-	-	-
Property held in trust	525	-	2,141	-
Securities lending liability (Note 3)	-	-	57,563	16,600
Compensated absences payable (Note 11)	81	8	1,270	63
Estimated insurance claims (Note 8)	-	-	346,400	90,901
Arbitrage rebate tax payable	1,503	-	-	-
Total liabilities	696,439	18	413,253	108,925
NET ASSETS				
Invested in capital assets, net of related debt	154	1	4,289	-
Restricted for:				
Funds held as permanent investments:				
Expendable	-	-	-	-
Nonexpendable	-	-	-	-
Housing authority	121,403	-	-	-
Other purposes	-	-	-	13,178
Unrestricted	-	2,233	176,426	11,687
Total net assets	$ 121,557	$ 2,234	$ 180,715	$ 24,865

The notes to the financial statements are an integral part of this statement.

STATE UNIVERSITY SYSTEM		
MONTANA STATE UNIVERSITY	UNIVERSITY OF MONTANA	TOTALS
$ 72,481	$ 44,259	$ 150,917
24,018	14,316	68,659
1,360	770	2,136
-	53	569
2,876	1,601	4,477
17,765	8,424	667,517
-	3,014	3,014
2,261	1,574	758,330
-	172	74,335
-	1,927	8,630
1,513	-	1,513
4,212	6,936	11,148
11,834	8,971	20,805
269,400	298,712	568,112
74,991	40,715	118,890
30,702	-	30,702
60,436	58,478	118,914
9,768	7,402	17,170
2,608	1,051	6,864
(234,575)	(191,954)	(428,474)
229,376	230,311	464,131
2,185	1,477	5,511
353,835	307,898	2,209,739
17,694	17,640	44,156
1,217	116	2,166
19,812	8,873	28,685
53	-	569
8,486	7,838	17,519
412	1,342	2,045
96,592	116,988	903,503
738	1,502	4,906
-	172	74,335
21,674	16,232	39,328
-	-	437,301
-	-	1,503
166,678	170,703	1,556,016
132,372	122,407	259,223
4,508	6,020	10,528
4,722	4,670	9,392
-	-	121,403
-	-	13,178
45,555	4,098	239,999
$ 187,157	$ 137,195	$ 653,723

STATE OF MONTANA
COMBINING STATEMENT OF ACTIVITIES
COMPONENT UNITS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

		PROGRAM REVENUES		
FUNCTIONS/PROGRAMS	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS
Authorities:				
Housing Authority	$ 46,396	$ 235	$ 241	$ -
Facilty Finance Authority	231	256	-	-
State Compensation Insurance (New Fund)	122,285	93,259	-	-
State Compensation Insurance (Old Fund)	832	-	-	-
State University System:				
Montana State University	303,672	129,601	95,363	7,367
University of Montana	240,114	104,750	65,216	1,579
Total component units	$ 713,530	$ 328,101	$ 160,820	$ 8,946

General revenues:
Other taxes
Unrestricted investment earnings
Payment from State of Montana
Gain (loss) on sale of capital assets
Miscellaneous
Payment between component units
Total general revenues
Change in net assets
Total net assets - July 1
Prior period adjustments
Total net assets - July 1 - as restated
Total net assets - June 30

The notes to the financial statements are an integral part of this statement.

NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS						
HOUSING AUTHORITY	FACILITY FINANCE AUTHORITY	STATE COMPENSATION INSURANCE (NEW FUND)	STATE COMPENSATION INSURANCE (OLD FUND)	MONTANA STATE UNIVERSITY	UNIVERSITY OF MONTANA	TOTALS
$ (45,920)	$	$	$	$	$	$ (45,920)
	25					25
		(29,026)				(29,026)
			(832)			(832)
				(71,341)		(71,341)
					(68,569)	(68,569)
(45,920)	25	(29,026)	(832)	(71,341)	(68,569)	(215,663)
-	-	2	28	-	-	30
52,421	70	33,241	10,295	2,724	1,185	99,936
500	-	-	-	80,965	57,909	139,374
-	-	(14)	-	93	-	79
4	-	123	-	-	7,164	7,291
-	-	7,408	(7,408)	-	-	-
52,925	70	40,760	2,915	83,782	66,258	246,710
7,005	95	11,734	2,083	12,441	(2,311)	31,047
114,552	2,139	168,981	22,782	176,191	139,468	624,113
-	-	-	-	(1,475)	38	(1,437)
114,552	2,139	168,981	22,782	174,716	139,506	622,676
$ 121,557	$ 2,234	$ 180,715	$ 24,865	$ 187,157	$ 137,195	$ 653,723

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State of Montana
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Year Ended June 30, 2002

NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements for the State of Montana have been prepared in accordance with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

A. Reporting Entity

For financial reporting purposes, the State of Montana has included all funds which comprise the State of Montana (the primary government) and its component units. The component units are entities for which the State is financially accountable, or whose relationship with the State is such that exclusion would cause the State's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the State to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the State.

Discrete Component Units
These component units are entities which are legally separate from the State because they possess corporate powers, but are financially accountable to the State, or whose relationships with the State are such that exclusion would cause the State's financial statements to be misleading or incomplete. Complete financial statements of the individual component units, which issue separate financial statements, can be obtained from their respective administrative offices. The component unit columns of the combined financial statements include the financial data of these entities:

Housing Authority – This authority, which is a legally separate entity, is governed by a quasi-judicial board appointed by the Governor. It was created in 1975 to facilitate the availability of decent, safe, and sanitary housing to persons and families of lower income. The board issues negotiable notes and bonds to fulfill its purposes. The total amount of notes and bonds outstanding at any time may not exceed $975 million. Neither the faith and credit nor taxing power of the State of Montana may be pledged for the amounts so issued. The authority is audited annually by the Legislative Auditor. The report is issued under separate cover and available at 301 South Park, Room 204, Helena, MT 59620-0545.

Facility Finance Authority – This authority, which is a legally separate entity, is governed by a quasi-judicial board appointed by the Governor with the advice and consent of the Senate. The authority assists all eligible, non-profit Montana health care and other community-based service providers to obtain and maintain access to the broadest range of low-cost capital financing as possible. The board issues revenue bonds to fulfill its purposes. Neither the faith and credit nor taxing power of the State of Montana may be pledged for the amounts so issued. Individual audit reports are issued by the Legislative Auditor every two years. The report is issued under separate cover and available at 2401 Colonial Drive, 3rd Floor, PO Box 200506, Helena, MT 59620-0506.

State Compensation Insurance Fund (New and Old) – The fund is a nonprofit, independent public corporation governed by a board appointed by the Governor. The fund provides workers compensation insurance. The fund consists of two separate entities: the New Fund and the Old Fund. The New Fund covers claims incurred after June 30, 1990, and is financed by member (employer) premiums. The Old Fund covers claims incurred before July 1, 1990. In 1999, the 56th Legislature determined that the Old Fund was adequately funded and discontinued the Old Fund Liability Tax. Administrative operations and budgets are reviewed by the Governor and the legislature. The fund is audited annually by the Legislative Auditor. The report is issued under separate cover and available at 5 South Last Chance Gulch, Helena, MT 59601.

Universities and Colleges – The State Board of Regents has responsibility for the following institutions: The University of Montana - Missoula and the units under it including Montana Tech of the University of Montana, The University of Montana - Western and The University of Montana - Helena College of Technology; and Montana State University - Bozeman and the units under it including Montana State University - Billings, Montana State University - Northern, and the Montana State University College of Technology - Great Falls. All units are funded through state appropriations, tuition, federal grants, and private donations and grants. Individual audit reports are issued by the Legislative Auditor annually. The reports are issued under separate cover and are available at the President's Office on each of the campuses or by contacting the Commissioner of Higher Education, 2500 Broadway, PO Box 203101, Helena, MT 59620.

Though the following organizations perform functions related to the higher education units, they are not considered part of Montana's reporting entity: (1) Community Colleges which are considered part of local units of government; (2)

the Montana Higher Education Student Assistance Corporation, a private non-profit corporation; (3) the Student Assistance Foundation of Montana, a private non-profit corporation; and (4) private foundations supporting public education, over which the State exercises neither financial nor administrative control (see Note 15). Entities such as local school districts and local authorities of various kinds are considered part of local units of government and have not been included. The State's support of local public education systems is reported in the General Fund.

Fiduciary Fund Component Units

Teachers Retirement System (Pension Trust Fund) – This retirement system is a legally separate entity with a board appointed by the Governor. Its purpose is to provide retirement, disability, death and lump-sum payments to members of Montana's public teaching profession. The administrative costs of the Teachers Retirement System are paid from investment earnings of the fund. The system is funded from employer and employee contributions and investment earnings. The board is a discretely presented component unit. The system is audited annually by the Legislative Auditor. Its report is issued under separate cover and is available at 1500 Sixth Avenue, PO Box 200139, Helena, MT 59620-0139.

Public Employees Retirement Board (Pension and Other Employee Benefit Trust Funds) – The board, appointed by the Governor, administers ten separate retirement systems for the purpose of providing retirement, disability, death, and lump-sum payments to each system member. These legally separate entities include the Public Employees Defined Benefit, Public Employees Defined Contribution, the associated education funds, the Municipal Police Officers, the Game Wardens and Peace Officers, the Sheriffs, the Judges, the Highway Patrol Officers and the Firefighters Unified Retirement Systems, as well as the Volunteer Firefighters Compensation Act. The board also administers the State of Montana Deferred Compensation Program.

The Public Employees Retirement System (PERS) is funded from employer and employee contributions, investment earnings and state contributions for city, county, and local governments. The PERS also accounts for the administrative costs, paid from investment earnings, of the system. The Municipal Police Officers Retirement System is funded from member, state, and city contributions. The Game Wardens and Peace Officers Retirement System is funded by employer and employee contributions. The Sheriffs Retirement System is funded by member and county contributions. The Judges Retirement System is funded by member and state contributions. The Highway Patrol Officers Retirement System is funded by member and state contributions. The Firefighters Unified Retirement System is funded by employer and employee contributions as well as a portion of insurance premium taxes collected by the State. The Volunteer Firefighters Compensation Act is funded by contributions of a percentage of fire insurance premium taxes collected. The State of Montana Deferred Compensation Program is funded from member contributions and investment earnings.

The board is a discretely presented component unit responsible for the ten separate public employee retirement systems and the Deferred Compensation Program. These are reported as pension and other employee benefit trust funds. The board is audited annually by the Legislative Audit Division. Its report is issued under separate cover and is available at 100 N Park, PO Box 200131, Helena, MT 59620-0131.

B. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) report information on all of the non-fiduciary activities of the State of Montana and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which are normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the State of Montana is reported separately from certain legally separately component units for which the State is financially accountable.

The Statement of Activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Certain indirect costs are included in the program expense reported for the individual functions and activities. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function, and grants and contributions restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not properly included among program revenues are reported as general revenues.

Separate fund financial statements are provided for governmental, proprietary, and fiduciary funds. Fiduciary fund statements are only reported on the fund financial statements. Major individual governmental and major individual enterprise funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide, proprietary fund, and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are reported when earned; expenses are recorded when a liability is incurred regardless of the timing of the related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenues as soon as all of the eligibility requirements imposed by the provider are met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Revenues are considered to be available if they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures as well as expenditures relating to compensated absences and claims and judgments are recorded only when payment is due. Significant intrafund transactions and balances have been eliminated.

The State uses funds to report on its financial position and the results of its operations. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

The financial activities of the State of Montana are classified into fund categories as described below:

Governmental Funds
General Fund – To account for all governmental financial resources except those required to be accounted for in another fund.

Special Revenue Funds – To account for the proceeds of specific revenue sources restricted to expenditure for specified purposes other than major capital projects.

Debt Service Funds – To account for resources accumulated for payment of principal and interest on general long-term obligation debt.

Capital Projects Funds – To account for resources used for the acquisition or construction of major capital facilities, other than those financed by proprietary or trust funds.

Permanent Funds – To account for resources that are permanently restricted to the extent that only earnings, not principal, may be used for the purposes of supporting the government's programs.

Proprietary Funds
Enterprise Funds – To account for operations: (1) financed and operated similar to private business enterprises, where the intent of the legislature is to finance or recover costs primarily through user charges; (2) where the legislature has decided periodic determination of revenue earned, expenses incurred, or net income is appropriate; (3) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; (4) when laws or regulations require that the activities' costs of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The primary focus of fee revenues charged by enterprise funds is users outside of the primary government.

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

The State of Montana reports two employee group benefits funds. The MUS Group Insurance Fund primarily charges its fees to Montana State University and the University of Montana. The universities are reported as discretely presented component units, which the State considers to be external users, and as such, reports the MUS Group Insurance Fund as an enterprise fund. The Employee Group Benefits Fund charges its fees to funds of the primary government, and as such, is reported as an internal service fund.

Fiduciary Funds
Trust and Agency Funds – To account for assets held by the State in a trustee capacity or as an agent for individuals, private organizations, or other governments. These assets cannot be used to support the government's own programs. These include: (1) pension (and other employee benefit) trust funds; (2) agency funds, (3) investment trust funds, and (4) private purpose trust funds.

The State reports the following funds as major as defined under GASB 34:

Major Governmental Funds
The General Fund is the State's primary operating fund, as defined above.

The State Special Revenue Fund accounts for all activities funded from state sources, which are restricted either legally or administratively for particular costs of an agency, program, or function.

The Federal Special Revenue Fund accounts for all activities funded from federal sources used in the operation of state government.

The Coal Tax Trust Permanent Fund, created by Article IX, Section 5 of the Montana State Constitution, receives 50% of all coal tax collections. The principal in this fund can be expended only upon affirmative vote of three-fourths of each house of the legislature.

The Land Grant Permanent Fund accounts for lands granted to the State for support of public schools and state institutions.

Major Proprietary Funds
The Unemployment Insurance Fund accounts for employer contributions deposited with the Secretary of the Treasury of the United States to the credit of the State's unemployment trust fund. Unemployment benefits are paid from this fund to eligible recipients.

The Economic Development Bonds Fund accounts for the Economic Development Bond Act programs and the Municipal Finance Consolidation Act programs. These programs assist Montana's small businesses and local governments in obtaining long-term, fixed-rate financing through private Montana lending institutions.

Private sector standards of accounting and financial reporting issued prior to December 1, 1989, are generally followed by both the government-wide and proprietary fund financial statements to the extent they do not conflict with or contradict guidance of GASB. Governments also have the option of following subsequent private sector guidance for their business-type activities and enterprise funds. The State has elected not to follow subsequent private sector guidance.

As a general rule, material interfund revenues have been eliminated from the government-wide financial statements. These have not been eliminated where their elimination would distort the direct costs and program revenues of the functions involved.

Amounts reported as program revenues include: (1) Charges to customers or applicants for goods, services, or privileges provided; (2) Operating grants and contributions; (3) Capital grants and contributions, including special assessments. Internally dedicated resources and all taxes are reported as general revenues.

The State does not allocate indirect expenses to functions in the Statement of Activities.

D. Proprietary Activity Accounting and Financial Reporting

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues generally result from providing services and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses for enterprise and internal service funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as non-operating.

E. Cash/Cash Equivalents

For all funds, except the Housing Authority in the component unit proprietary funds, cash and cash equivalents consist of funds deposited by individual funds in the State Treasurers pooled cash account, cash deposits in checking accounts, cash invested in the Short Term Investment Pool (STIP), undeposited cash held by individual state agencies, and investments categorized as cash equivalents, which are short-term, highly liquid investments with original maturities of three months or less. The Housing Authority considers cash and cash equivalents to be cash held by the State Treasurer, cash held by trustees, and cash invested in STIP (See Note 3).

F. Receivables

This classification, net of estimated uncollectibles, consists primarily of receivables for goods sold and services provided; short-term loans and notes; interest and dividends; taxes due within 60 days of fiscal year-end; and income, withholding, and inheritance taxes that are past due. An allowance for uncollectible taxes is provided based upon historical analysis. The allowance for uncollectible taxes at June 30, 2002, was $13.4 million.

G. Inventories

Inventories of materials and supplies are stated at cost. The State allows agencies to use any generally accepted inventory pricing method, but specifies the first-in, first-out method should be appropriate for most agencies. Governmental funds use the "purchase method," meaning inventory purchases are recorded as expenditures. At fiscal year-end, significant amounts of inventory are shown as a reservation of fund balance, indicating they do not constitute available expendable resources. An exception is the Federal Special Revenue Fund food stamp inventory balance, which is offset by deferred revenue.

Proprietary and fiduciary funds report using the "consumption method," meaning inventories are expensed as used.

H. Investments

In accordance with the Montana Constitution and the statutorily mandated "Prudent Expert Rule," the State of Montana invests in various types of securities for each portfolio it manages. Certain securities including asset-backed securities, variable-rate instruments, zero-coupon bonds, preferred stocks, and mortgage-backed securities are purchased for portfolio diversification and a competitive rate of return. Most investments are reported at fair value in the balance sheet or statement of net assets. Investments are reported by type in the disclosure of custodial credit risk for each investment portfolio (See Note 3 on Cash/Cash Equivalents and Investments).

I. Equity in Pooled Investments

The Montana Board of Investments manages the State's Unified Investment Program, which includes several internal investment pools. Participation in the pools is restricted to permanent funds, private purpose trust funds, investment trust funds, pension trust funds, higher education units, and specific trusts established within the State Special Revenue Fund. The participant investments in the pools are reported at fair value in the balance sheet within the individual funds (See Note 3 on Cash/Cash Equivalents and Investments).

J. Capital Assets

Capital asset valuation is based on actual historical cost or, in the case of donations, fair market value on the date donated. General government infrastructure capital assets are capitalized and reported in the government-wide financial statements. Infrastructure assets of primary government and component unit proprietary activities are capitalized. Interest incurred during the construction of capital assets for proprietary funds and higher education units is capitalized. The State has chosen to use the depreciation approach for infrastructure assets and is reporting accumulated depreciation in the Statement of Net Assets and depreciation expense in the Statement of Activities for these assets. The State is only reporting the current year highway system infrastructure construction/acquisitions. Other than land, all other highway related infrastructure will be added prior to the end of the phase-in period allowed under GASB 34. Other infrastructure has been capitalized and depreciated without regard to the phase-in period.

Capital assets in proprietary, private purpose trust, and pension trust funds are accounted for within their respective funds and are depreciated. Depreciation is on a straight-line basis with estimated useful lives of 25 to 60 years for buildings, 7 to 20 years for building improvements, 3 to 10 years for equipment, and 10 to 50 years for infrastructure. State agencies are also required to extend or shorten the useful lives of capital assets to reflect their actual experience or industry standards when appropriate.

During fiscal year 2002, the capitalization limit for buildings and building/land improvements was raised to $25,000. The capitalization threshold for infrastructure was set at $500,000. Agencies are allowed to capitalize additions to collections and land acquisitions at any cost. The capitalization limit for other capital assets remains at $5,000. Purchases under these thresholds are recorded as expenditures/expenses in the current period.

K. Deferred Revenue

Deferred revenues arise when a potential revenue does not meet both the measurable and available criteria for recognition in the current period. Deferred revenues also arise when resources are received by the government before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the State has a legal claim to the resources, the liability for deferred revenue is removed and revenue is recognized.

L. Long-Term Obligations

Long-term obligations expected to be financed from governmental funds are reported in the government-wide financial statements. Long-term debt is recognized as a liability of a governmental fund when due, or when resources have

been accumulated in the debt service fund for payment early in the following year. For other long-term obligations, only that portion expected to be financed from current expendable available financial resources is reported as a fund liability of a governmental fund in the fund financial statements. The remaining portion of such obligations is reported in the government-wide financial statements.

Long-term liabilities expected to be financed from proprietary fund operations are accounted for in those funds.

M. Capital Leases

A capital lease is generally defined by Statement of Financial Accounting Standards No. 13, "Accounting for Leases", as one which transfers benefits and risks of ownership to the lessee. Leases meeting the criteria of a capital lease, as defined, are recorded at inception as expenditures and other financing sources in governmental fund types and as assets and liabilities at the present value of the future minimum lease payments, using the interest rates stated in the leases.

N. Bond Discounts/Premiums/Issuance Costs

In the governmental funds as presented in the fund financial statements, bond premiums and discounts, as well as issuance costs, are recognized in the current period. Bond proceeds are reported as an other financing source, net of any premium or discount. Issuance costs are reported as debt service expenditures whether or not they are withheld from the net bond proceeds. In proprietary fund types and in governmental funds as presented in the government-wide financial statements, bond premiums and discounts are deferred and amortized over the life of the bonds, which approximates the effective interest method. Bonds payable are recorded net of any applicable premium or discount, while issuance costs are reported as deferred charges.

O. Compensated Absences

Full-time state employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Teachers employed by the State do not receive vacation leave. Vacation leave may be accumulated and carried over from one year to the next. The carryover is limited to two times the maximum number of days earned annually. Sick leave is earned at the rate of 12 days per year with no limit on accumulation. Each contribution year, an employee may contribute a maximum of 40 hours of sick leave to a nonrefundable sick leave pool. Based on a review, the adjusted ending balance of the pool for June 30, 2001, was 2,564.5 hours. For fiscal year 2002, 992 hours were contributed to the sick leave pool and 2,081.5 hours were withdrawn leaving a balance of 1,475 hours in the pool. No liability is reported in the accompanying financial statements because these hours are nonrefundable to participants except by grants approved through an application process.

Vested or accumulated leave for proprietary and fiduciary funds is recorded as an expense and liability of those funds in the fund financial statements. For governmental funds, the liability is not expected to be liquidated with expendable financial resources. The expenditure and liability for the governmental funds is reported only in the government-wide financial statements. Upon retirement or termination, an employee is paid for 100 percent of unused vacation leave and 25 percent of unused sick leave.

P. Advances to Other Funds

Noncurrent portions of long-term interfund receivables are reported as advances and are offset equally by a fund balance reserve account in the fund financial statements, which indicates that they do not constitute expendable available financial resources. The transaction is recognized by the receiving fund as Advances From Other Funds.

Q. Fund Equity

In the fund financial statements, reservations represent those portions of fund equity or net assets not appropriated for expenditure or legally segregated for a specific future use. Designated fund balances represent tentative plans for the future use of financial resources. In fiscal year 2002, the General Fund designated fund balance represents the 2001 Legislature's desire to set aside $3.2 million for contingencies related to cost increases in electricity and natural gas expenditures significantly greater than those appropriated or to support litigation to secure affordable electricity and natural gas. The State Special Revenue Fund designated fund balance represents management's desire to improve the Smith River Corridor. The Debt Service Funds designated fund balances represent management's desire to maintain fund balance in relation to bonds payable.

R. Property Taxes

Real property taxes are levied in October and are payable in two installments on November 30 and May 31. These taxes attach as an enforceable lien immediately if not paid when due. The State recognizes property tax revenues as available if they are collectible within 60 days after fiscal year-end. Material delinquent and total uncollected current year property taxes receivable are recorded as receivables (net of uncollectibles).

Personal property tax levies are set each August, and notices are normally mailed the following March or April. Half of mobile home taxes are due in 30 days and the remaining half on September 30. Taxes on all other types of personal property are to be paid in full 30 days after receipt of the notice. Personal property taxes attach as an enforceable lien immediately if not paid when due. Property taxes are collected by each of Montana's 56 counties. The counties then remit the State's portion to the State Treasury. The majority of these taxes help fund public school systems and higher education.

S. Other Taxes

On the Statement of Revenues, Expenditures and Changes in Fund Balances for Governmental Funds, the revenue category "Other Taxes" in the general, state special revenue, and nonmajor funds consists of the following taxes (in thousands):

	General Fund	State Special Revenue Fund	Capital Projects Fund	Totals
Video Gaming	$ 43,645	$ -	$ -	$ 43,645
Insurance Premium	43,930	-	-	43,930
Inheritance	13,769	-	-	13,769
University System Millage	920	11,451	-	12,371
Cigarette/Tobacco	10,083	1,504	1,718	13,305
Accommodations	39	11,873	-	11,912
Telephone License	19,826	-	-	19,826
Alcoholic Beverage	4,010	1,428	-	5,438
Electrical Energy	7,420	-	-	7,420
Public Contractor	3,537	-	-	3,537
Livestock	-	2,385	-	2,385
Public Service Commission	-	2,250	-	2,250
Freight Line	1,490	-	-	1,490
Fire Protection	2,367	2,159	-	4,526
Agriculture Sales	-	1,291	-	1,291
Consumer Counsel	-	829	-	829
Miscellaneous	164	165	-	329
Total Other Taxes	$151,200	$35,335	$1,718	$188,253

NOTE 2 — OTHER ACCOUNTING ISSUES

The State made changes in its accounting practices to report in conformance with the new governmental reporting model as defined by GASB statements 34 through 38. All changes reported in the accompanying financial statements that resulted in the restatement of beginning fund equity were made to correct errors of prior periods and changes in accounting principle.

NOTE 3 — CASH/CASH EQUIVALENTS AND INVESTMENTS

This footnote details the following Balance Sheet classifications (in thousands):

Cash/Cash Equivalents	$1,753,166
Equity in Pooled Investments	$5,394,139
Investments	$2,013,381

Carrying amounts and fair values (Bank Balance for Cash Deposits) for the State's cash/cash equivalents and investments are presented in Tables 1 through 4.

A. General

(1) Cash and cash equivalents consist of funds deposited by individual funds in the State Treasurer pooled cash account, cash deposits in checking accounts, cash invested in the Short Term Investment Pool, undeposited cash held by individual state agencies, and investments categorized as cash equivalents.

Cash deposited with the State Treasurer pooled cash account is invested by the Montana Board of Investments (BOI) in short-term securities and other investments. Because these funds are immediately available to the individual funds, their investment in the pooled cash account is reported as a cash equivalent. In addition to the State Treasurer pooled cash account, there is a short-term investment pool (STIP) maintained by the BOI. This investment fund provides individual state agencies and local governments an opportunity to invest excess cash in a money market fund. Because these pooled funds are invested in short-term, highly liquid investments, the individual funds investments in the STIP are reported as a cash equivalent.

Although STIP, an external investment pool, is not registered with the Securities and Exchange Commission (SEC) as an investment company, the BOI has as policy that STIP will, and does, operate in a manner consistent with the SEC Rule 2a7 of the Investment Company Act of 1940. In meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values. Investments held are reported at fair value, annually, and the difference between amortized cost and fair value is reflected as an unrealized gain or loss in the investments managed. The portfolio is carried at amortized cost or book value. State agencies that are allowed to retain their investment earnings within their funds are only allowed to invest in STIP. Local government participation in STIP is also voluntary. Separately issued external investment pool financial statements may be obtained by contacting the Montana Board of Investments, 2401 Colonial Drive, 3rd Floor, PO Box 200126, Helena, MT 59620-0126.

Deposits with financial institutions are categorized to indicate the level of risk assumed by the State. Category 1 consists of deposits that are insured or collateralized with securities held by the State or by its agent in the State's name. Category 2 consists of deposits collateralized with securities held by the pledging financial institution's trust department or agent in the State's name. Category 3 deposits are uncollateralized. The State's Cash Deposits are categorized in Table 1.

The State's cash equivalents and investments are categorized to indicate the risk level assumed by the State in Table 2 - Cash Equivalents, Table 3 - Equity in Pooled Investments, and Table 4 - Investments to disclose the level of risk assumed by the State at fiscal year-end.

Category 1 includes investments that are insured or registered securities held by the State or its agent in the State's name. Category 2 includes uninsured and unregistered investments where the securities are held by the counter party's trust department or agent in the State's name. Category 3 includes uninsured and unregistered investments in which the securities are held by the counter party, or by its trust department or agent, but not in the State's name. None of the State's cash equivalents or investments are classified in Category 3 at fiscal year-end. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

(2) The State invests in certain types of securities including asset-backed securities, variable-rate instruments, zero-coupon bonds, preferred stocks (convertible equity securities), and mortgage-backed securities, in addition to other long-term investment securities, to provide a diversified investment portfolio and an overall competitive rate of return. All securities are reported by investment portfolio and type in Table 2 - Cash Equivalents, Table 3 - Equity in Pooled Investments, and Table 4 - Investments.

Asset-backed securities represent debt securities collateralized by a pool of non-mortgage assets such as trade and loan receivables, equipment leases, credit cards, etc. These securities have less credit risk than do securities not backed by pledged assets, while market risk for asset-backed securities is the same as market risk for similar non asset-backed securities.

Variable-rate instruments pay a variable rate of interest until maturity. The variable rate floats with the 91-day treasury bill or the London Interbank Offered Rate (LIBOR). Variable-rate instruments have credit risk identical to similar fixed-rate securities; however, their market risk (income) is more sensitive to interest rate changes. Their market risk (value/price) may be less volatile than fixed-rate securities because their value will usually remain near par as a result of interest rates being periodically reset to maintain a current market yield.

Zero-coupon bonds and preferred stocks include securities whose structure differs from the basic convertible security structure. These include PENs (Participating Equity Notes), PERCs (Preferred Equity Redemption Coupons), DECS (Dividend Enhanced Common Stock), and ACES (Automatically Convertible Equity Securities). PENs are corporate bonds offering the investor a choice at maturity of receiving the greater of the bond's par value or the value of a preset ratio of an established index. PERCs reflect an investor's acceptance of a cap in a security's price appreciation in exchange for a higher income yield. DECS and ACES are issued and traded at a premium to the underlying common stock in exchange for a higher dividend yield. The State's investment policy requires convertible debt and zero-coupon bonds to be rated at a specific level at time of purchase as a credit risk control measure. These securities carry market

risk and the potential for change in market value. Market value changes may occur due to interest rate changes, declines in the value of underlying common stock, or the triggering of a call feature and other factors.

Mortgage-backed securities reflect participation in a pool of residential mortgages. These securities include structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). Some REMICs are principal-only strips (POS) and interest-only strips (IOS). These securities are based on the cash flows from the principal and interest payments on underlying mortgages, respectively. These securities have credit risk as measured by major credit rating services. The State's investment policy requires these investments to be rated investment grade at the time of purchase. Market risk for these securities is caused by changes in the price or principal value of the securities due to changes in interest rates.

As of June 30, 2002, investments in Enron and Burlington presented legal and higher credit risk to the State.

(3) Under the provisions of state statutes, the State has, via a Securities Lending Authorization Agreement, authorized the State's agent to lend the State's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the State receives a fee and the agent must initially receive collateral equal to 102% to 105% of the fair value of the securities on loan and maintain collateral equal to not less than 100% of the fair value of the loaned security. During fiscal year 2002, the State's agent loaned, on behalf of the State, certain securities held by the agent and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. The State's agent does not have the ability to pledge or sell collateral securities unless the borrower defaults. The State retains all rights and risks of ownership for the loaned securities. On June 30, 2002, the State had no credit risk exposure to borrowers.

B. Cash/Cash Equivalents

(1) Cash Deposits – The State requires collateralization based on the average daily bank balance in the depository bank holding the main state bank account. For other depository banks, State statutes require collateralization at 50% of the bank balance. The cash deposits amount includes both primary government and component unit deposits.

Table 1 - Cash Deposits *(in thousands)*

Risk Category		Carrying Amount	Bank Balance	Fund
1	Insured (FDIC)	$ 1,621	$ 1,621	Various
	Collateral Held by State/State's Agent	9,996	9,996	Various
2		489	489	Various
3		317	317	Various
Uncategorized:				
	Undeposited Cash	3,552		
	Cash in U.S. Treasury	193,603		
	Less Outstanding Warrants	(52,682)		
	Total Cash Deposits	$156,896		

As of June 30, 2002, the carrying amount of deposits for component units was $59,114,091, and the bank balance was $57,286,461. Of the bank balance, $57,286,461 was fully insured or collateralized with securities held by the component units or their agents in the unit's name, and $94,713 was collateralized with securities held by the pledging institution's trust department or its agent in the respective component unit's name.

(2) Cash Equivalents – consists of cash in the State Treasury invested by individual funds in the Short Term Investment Pool (STIP) and the Treasurer Cash Pool in identifiable securities and investments considered to be cash equivalents. Cash equivalents, except for the Housing Authority in the component unit proprietary fund, generally are short-term, highly liquid investments with original maturities of three months or less. The Housing Authority considers cash and cash equivalents to be cash held by the State Treasurer, other cash deposits, and cash invested in STIP. Cash equivalents may be under the control of the Board of Investments (the board) or other agencies, as allowed by law.

Table 2 - Cash Equivalents *(in thousands)*

	Risk Category 1					
	Securities Not on Loan	On Loan for* Securities Collateral	Not* Categorized	Carrying Amount	Fair Value	Fund
Commercial Paper	$ 9,995	$ -	$ -	$ 9,995	$ 9,995	Various
Asset-backed Securities	912,374	-	-	912,374	912,371	Various
Government Securities	104,135	-	-	104,135	105,571	Various
Repurchase Agreements	59,000	-		59,000	59,000	Various
Variable-rate	491,045	-	-	491,045	491,222	Various
Direct Investments:						
Money Markets				19,721	19,721	Various
Guaranteed Investment Contracts				-	-	Various
Total Cash Equivalents				$1,596,270	$1,597,880	
Securities Lending Collateral Investment Pool			$ -	$ -	$ -	

* At June 30, 2002, no securities were loaned for securities or cash collateral under a security lending agreement with the State's agent.

As of June 30, 2002, local governments invested $761,215,876 in the STIP.

As of June 30, 2002, component units of the State of Montana had investments in cash equivalents with a book value and fair value of $273,290,129.

C. Equity in Pooled Investments

These securities consist of investments held by pooled investment funds. The Montana Common Stock Pool (MTCP), Trust Funds Bond Pool (TFBP), Retirement Funds Bond Pool (RFBP), Montana International Equity Pool (MTIP), and Montana Private Equity Pool (MPEP) were created to allow qualifying funds to participate in diversified investment pools. Participation is restricted to permanent funds, private-purpose trust funds, investment trust funds, pension trust funds, higher education units, and specific trusts established within the State Special Revenue Fund. Purchases are subject to statutory restrictions for quality and size of holdings.

Table 3 - Equity In Pooled Investments *(in thousands)*

	Risk Category 1				
	Securities Not on Loan	On Loan for Securities Collateral*	Not Categorized*	Carrying Amount	Fair Value
MTCP:					
Corporate Stocks	$1,802,361	$ -	$ 20,924	$1,823,285	$1,877,185
SPIFF	5,982	-	-	5,982	5,869
TFBP:					
Corporate Asset-backed	2,714	-	-	2,714	2,824
Corporate Stocks	689,693	-	9,229	698,922	700,892
US Govt. Mortgage-backed	52,444	-	-	52,444	53,775
US Govt. Direct/Indirect	176,648	18,002	78,776	273,426	298,283
Yankee Bonds	74,095	-	-	74,095	74,991
State and Local Government	17,551	-	-	17,551	17,553
RFBP:					
Corporate Asset-backed	1,357	-	-	1,357	1,412
Corporate Stocks	1,094,407	-	8,964	1,103,371	1,109,175
US Govt. Mortgage-backed	60,870	-	-	60,870	63,326
US Govt. Direct/Indirect	251,439	-	140,150	391,589	433,208
Yankee Bonds	88,899	-	5	88,904	91,125
State and Local Government	1,130	-	-	1,130	1,130
MTIP:					
BOI Internal International	116,630	-	28,137	144,767	143,563
Pyford International	81,721	-	15,783	97,504	89,775
Schroder Capital Management	106,946	68	9,009	116,023	112,533
SG Pacific Asset Management	74,349	-	10,231	84,580	83,734
MPEP:					
Private Equities	160,649	-	-	160,649	175,506
State Street SPIFF	23,461	-	-	23,461	21,846
Total Pooled Investments	4,883,346	18,070	321,208	5,222,624	5,357,705
Other Pool Assets (Net)	-	-	-	36,434	36,434
Total - Equity in Pooled Investments	$4,883,346	$18,070	$321,208	$5,259,058	$5,394,139
Securities Lending Collateral Investment Pool			$358,146	$ 358,146	$ 358,146

* At June 30, 2002, these underlying securities, with fair values of $18,816,095 and $343,856,304, respectively, were loaned for securities and cash under a security lending agreement with the State's agent.

As of June 30, 2002, component units of the State of Montana had equity in pooled investments with a book value of $3,195,123,554 and a fair value of $4,226,413,018.

D. Investments

Long-term investments are primarily administered by three state agencies. Article 8 of Montana's Constitution, with supporting statutes, authorizes the Board of Investments (BOI) to manage the State's unified investment program. State law specifies which agencies may hold investments outside the administration of the BOI. The BOI, as the State's primary administrator of long-term investments, actively manages 82% of those investments; the Board of

Housing, 7%; and the Department of Administration's Public Employees Retirement Board, 10% for the State's Deferred Compensation Plan. Additionally, the Department of Natural Resources and Conservation manages 1% of total investments for bond-related activities.

The BOI must employ the "Prudent Expert Rule" in managing the State's investment portfolio. Investments are presented in the Balance Sheet at fair value. Investment fair values for publicly traded securities are determined primarily by reference to market prices supplied to the BOI's custodial bank or trustee. Amortized cost, or carrying value, represents the original cost, adjusted for premium and discount amortization where applicable.

The Board of Investments continued to invest in leveraged buyouts in fiscal year 2002. The board's total leveraged buyout commitment, administered by Kohlberg, Kravis, Roberts and Companies (KKR), amounts to $125 million, as of June 30, 2002. The KKR leveraged buyout invested balance for the Montana Private Equity Pool (MPEP) amount to $90,962,263 on June 30, 2002.

On May 18, 2001, the board approved that $50 million be invested with Lexington Partners LP Fund V, a secondary leveraged buyout market fund. As of June 30, 2002, the MPEP invested balance totaled $4,896,324.

On January 19, 2001, the board approved a staff recommendation to commit $25 million in the leveraged buyout fund of Madison Dearborn Partners IV. As of June 30, 2002, the MPEP invested balance totaled $858,233.

On September 22, 2000, the board approved a staff recommendation to commit $25 million in the leveraged buyout fund of Welsh Carson Anderson & Stowe IX. As of June 30, 2002, the MPEP invested balance totaled $5,810,293.

As of June 30, 2002, the board has a $195 million commitment for venture capital investments administered by Adams Street Partners, formerly Brinson Partners. The June 30, 2002, venture capital invested balance totaled $58,121,432 for MPEP.

The board committed to invest, on behalf of the retirement funds, in the S&P 500 Equity Index Fund A, managed by Barclays Global Investors. As of June 30, 2002, the pension funds had an invested balance of $465 million.

Upon receiving electorate approval, the board began investing for the State Fund in January 2001, in the S&P 500 Equity Index Fund B, managed by Barclays Global Investors. As of June 30, 2002, State Fund's invested balance totaled $74 million.

Table 4 – Investments (Risk Categories) *(in thousands)*

	Risk Category 1 Securities Not on Loan	Risk Category 2	Not Categorized*	Carrying Amount	Fair Value
Primary Government					
Corporate Bonds	$ 30,964	$ -	$ 11,169	$ 42,133	$ 43,631
Corporate Asset-backed	10,238	-	-	10,238	10,517
Government Securities	78,393	-	-	78,393	81,313
Government Mortgage-backed	12,315	-	-	12,315	12,718
Total	$131,910	$ -	$ 11,169	$ 143,079	$ 148,179
Component Units					
Corporate Bonds	$239,217	$ -	$ -	$ 239,217	$ 248,196
Corporate Asset-backed	18,442	-	-	18,442	18,697
Government Securities	78,436	44,736	89,326	212,498	219,862
Government Mortgage-backed	88,835	-	-	88,835	90,606
International Bonds	10,112	-	839	10,951	10,934
Savings & Loans	254	-	-	254	254
Repurchase Agreement	-	104,112	-	104,112	104,246
Foundations	-	-	1,281	1,281	1,139
Other Investments	-	-	216	216	215
Total	435,296	148,848	91,662	675,806	694,149
Total	$567,206	$148,848	102,831	$ 818,885	$ 842,328
Direct Investments:					
Primary Government					
Commercial Loans				186,108	186,108
Total				$ 186,108	$ 186,108
Component units					
Real Estate				$ 13,066	$ 13,600
Mortgages				324,038	330,438
Alternative Equities				539,000	446,706
Deferred Compensation				205,279	194,201
Total				1,081,383	984,945
Total Investments				$2,086,376	$2,013,381
Securities Lending Collateral Investment Pool			$109,960	$ 109,960	$ 109,960

* At June 30, 2002, the underlying securities, with fair values of $106,533,000, were loaned for cash collateral under a securities lending agreement with the State's agent.

NOTE 4 — CAPITAL ASSETS

A. Primary Government

Changes in capital asset balances for the fiscal year ended June 30, 2002, are reflected in the following table; intrafund transfers of capital assets have not been eliminated (in thousands):

Primary Government

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental Activities				
Capital Assets, Not Being Depreciated				
Land	$ 71,493	$196,510	$ (1,773)	$266,230
Construction Work in Progress	31,799	144,089	(5,004)	170,884
Capitalized Collections	53,989	10,034	(342)	63,681
Total Capital Assets, Not Being Depreciated	157,281	350,633	(7,119)	500,795
Capital Assets, Being Depreciated				
Infrastructure	95,510	158,597	(431)	253,676
Land Improvements	-	9,661	-	9,661
Buildings	300,158	16,952	(19,226)	297,884
Building Improvements	125,004	783	(118,585)	7,202
Equipment	216,855	48,381	(35,395)	229,841
Other	11,512	249	(8,803)	2,958
Total Capital Assets, Being Depreciated	749,039	234,623	(182,440)	801,222
Less Accumulated Depreciation for:				
Infrastructure	(20,835)	(2,308)	431	(22,712)
Land Improvements	-	(205)	-	(205)
Buildings	(131,617)	(8,540)	7,917	(132,240)
Building Improvements	(8,465)	(224)	2,777	(5,912)
Equipment	(130,559)	(18,929)	11,927	(137,561)
Other	(1,956)	(209)	10	(2,155)
Total Accumulated Depreciation	(293,432)	(30,415)	23,062	(300,785)
Total Capital Assets, Being Depreciated, Net	455,607	204,208	(159,378)	500,437
Intangible Assets	466	38,019	(971)	37,514
Governmental Activity Capital Assets, Net	$613,354	$592,860	$(167,468)	$1,038,746

Primary Government

	Beginning Balance	Increases	Decreases	Ending Balance
Business-type Activities				
Capital Assets, Not Being Depreciated				
Land	$ 800	$ -	$ -	$ 800
Construction Work in Progress	15	56	-	71
Total Capital Assets, Not Being Depreciated	815	56	-	871
Capital Assets, Being Depreciated				
Infrastructure	-	884	-	884
Land Improvements	-	222	-	222
Buildings	5,160	3,485	(366)	8,279
Building Improvements	689	8	(12)	685
Equipment	7,388	12,384	(10,323)	9,449
Other	1,154	-	-	1,154
Total Capital Assets, Being Depreciated	14,391	16,983	(10,701)	20,673
Less Accumulated Depreciation for:				
Infrastructure	-	(4)	-	(4)
Land Improvements	-	-	-	-
Buildings	(2,585)	(436)	290	(2,731)
Building Improvements	(424)	(35)	12	(447)
Equipment	(3,353)	(2,794)	1,967	(4,180)
Other	(995)	(1)	-	(996)
Total Accumulated Depreciation	(7,357)	(3,270)	2,269	(8,358)
Total Capital Assets, Being Depreciated, Net	7,034	13,713	(8,432)	12,315
Intangible Assets	1,735	335	(598)	1,472
Business-type Activity Capital Assets, Net	$ 9,584	$ 14,104	$ (9,030)	$ 14,658

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

	Amount
General Government	$ 899
Public Safety/Corrections	4,640
Transportation (including depreciation of the highway system maintained by the State).	3,135
Health/Social Services	3,807
Education/Cultural	1,177
Resource Development/Recreation (including depreciation of the State's dams).	3,184
Economic Development/Assistance	609
Depreciation and amortization on capital assets held by the State's internal service funds is charged to the various functions based on their usage of the assets.	11,188
Total Depreciation Expense – Governmental Activities	$28,639

B. Discretely Presented Component Units

The following table summarizes net capital assets reported by the discretely presented component units (in thousands). All component units, other than higher education units, are included under the Other caption for this schedule:

Discretely Presented Component Units

	Montana State University	University of Montana	Other	Totals
Capital Assets, Not Being Depreciated				
Land	$ 4,212	$ 6,936	$ -	$ 11,148
Construction Work in Progress	9,768	7,402	-	17,170
Capitalized Collections	7,767	14,395	-	22,162
Livestock for Educational Purposes	2,371	-	-	2,371
Total Capital Assets, Not Being Depreciated	24,118	28,733	-	52,851
Capital Assets, Being Depreciated				
Infrastructure	30,702	-	-	30,702
Land Improvements	11,834	8,971	-	20,805
Buildings	165,795	184,376	-	350,171
Building Improvements	103,605	114,336	-	217,941
Equipment	74,991	40,715	3,184	118,890
Other	50,298	44,083	-	94,381
Total Capital Assets, Being Depreciated	437,225	392,481	3,184	832,890
Less Accumulated Depreciation	(234,575)	(191,954)	(1,945)	(428,474)
Total Capital Assets, Being Depreciated, Net	202,650	200,527	1,239	404,416
Intangible Assets	2,608	1,051	3,205	6,864
Discretely Presented Component Units - Total Capital Assets, Net	$229,376	$230,311	$4,444	$464,131

NOTE 5 — RETIREMENT SYSTEMS

Defined Contribution Plans

ORP - Optional Retirement Program – Effective January 1, 1988, through June 30, 1993, eligible employees of the Montana University System (MUS) could elect to participate in the Optional Retirement Program (ORP). The ORP is a defined contribution retirement plan governed by Title 19, chapter 21 of the Montana Code Annotated. The plan is underwritten by the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF); only faculty and staff with contracts under the authority of the Board of Regents may participate. Those faculty and staff members who did not elect the ORP, participate in the Teachers Retirement System, a defined benefit plan discussed in the next section. Beginning July 1, 1993, membership in the ORP is mandatory for eligible employees new to the MUS. The MUS is the only employer contributing to this plan.

The benefits at retirement depend upon the amount of contributions, amount of investment gains and losses, and the employee life expectancy at retirement. Under the ORP, each employee enters into an individual contract with TIAA-CREF. Individuals are immediately vested with all contributions. Higher education units record employee/employer contribution expenditures in the affected higher education subfund when remitting contributions to the Commissioner of Higher Education. These monies are recorded in the Custodial Accounts Agency Fund. The Commissioner's Office then wire transfers the contributions to TIAA-CREF. The MUS is not liable for asset management or for providing benefits after the required contributions have been made to TIAA-CREF. As of June 30, 2002, 2,130 employees were members of the ORP. Required employee contributions were 7.044% of salary; required employer contributions were 4.956% of salary ,for a total of 12% of salary contributed to the ORP.

	TIAA-CREF *(in thousands)*
Covered Payroll	$ 98,750
Total Payroll	216,045
Employer Contributions	$ 4,894
Percent of Covered Payroll	4.956%
Employee Contributions	$ 6,960
Percent of Covered Payroll	7.048%

DCRP - Public Employees Retirement System – This plan is a multiple-employer, cost-sharing plan created by the 1999 Legislature and is governed by Title 19, chapters 2 & 3 of the MCA. The PERS-DCRP will be available to all active PERS members effective July 1, 2002. The plan will begin receiving contributions or revenues after the July 1, 2002, implementation date.

Eligible PERS members who are active on July 1, 2002, will have a 12-month window during which they may choose to join the PERS-DCRP or remain in the current PERS-DBRP. Members may not be active members of both the defined contribution and defined benefit retirement plans. The choice is irrevocable. Members of the defined contribution retirement plan will decide how to invest their contributions and a portion of their employer contributions in the selected investment options. The remaining portion of employer contributions will be used to maintain funding of the defined benefit plan, to provide disability benefits, and to fund an employee education program.

457 - Deferred Compensation Plan – The 457 plan was established in 1976 and is governed by Title 19, chapter 50, MCA, in accordance with Internal Revenue Service Code (IRC) 457. As of June 30, 2002, the net assets of the 457 plan were $196,419,000. All employees of the State, Montana University System, and contracting political subdivision are eligible to participate. The 457 plan is a voluntary, tax-deferred retirement plan designed to supplement state service retirement, Social Security, and other retirement plans and savings. Assets of the 457 plan are required to be held in trusts, custodial accounts, or insurance company contracts for the exclusive benefit of participants and their beneficiaries. Under the plan, eligible employees elect to defer a portion of their salary until future time periods. The compensation deferred is not available to employees until separation from service, retirement, death, or upon an unforeseeable emergency while still employed and must meet IRS-specified criteria. Participant rights are fully vested in their accounts at the time of deposit.

Defined Benefit Plans

A. General

The Public Employees Retirement Board, a discretely presented component unit of the State of Montana, administers eight defined benefit plans - Public Employees Retirement System (PERS), Highway Patrol Officers Retirement System (HPORS), Judges Retirement System (JRS), Game Wardens and Peace Officers Retirement System (GWPORS), Sheriffs Retirement System (SRS), Municipal Police Officers Retirement System (MPORS), Firefighters Unified Retirement System (FURS), and Volunteer Firefighters Compensation Act (VFCA). The board prepares a publicly issued comprehensive annual financial report that includes financial statements and required supplementary information for PERS, HPORS, JRS, GWPORS, SRS, MPORS, FURS, and VFCA.

The financial statements for PERS include activity for a defined benefit and a defined contribution retirement plan and an education fund. The defined contribution plan will be available to eligible PERS members starting July 1, 2002. The PERS received a long-term loan for $1,498,000 from the Montana Department of Administration to fund the defined contribution plan start-up and implementation costs. The education fund was established to inform the PERS members about the plan choices. The education program was funded by 0.1% of the PERS-covered payroll for fiscal year 2002.

The Teachers Retirement System (TRS) is a discretely presented component unit of the State of Montana. The system prepares a publicly issued financial report that includes financial statements and required supplementary information for TRS.

A summary of government employers participating in PERS, SRS, MPORS, HPORS, FURS, GWPORS, JRS, and TRS by employer type at June 30, 2002, follows:

Retirement System

	PERS	SRS	MPORS	HPORS	FURS	GWPORS	JRS	457	TRS
Employers									
State Agencies	34	1		1	1	5	1	34	8
Counties	55	55							
Cities/Towns	92		22		15				
Colleges/Universities	5					3		6	8
School Districts	241								378
Other	88							1	
Total	515	56	22	1	16	8	1	41	394

B. Plan Descriptions

The State contributes to and/or administers ten plans in four categories: (1) the State as the single employer; (2) the State as an employer contributor to cost-sharing multiple-employer plans; (3) the State as a nonemployer contributor to cost-sharing multiple employer plans; and (4) the State as a nonemployer contributor.

The number of years required to obtain vested rights varies among the systems. All systems provide early retirement options, death benefits, termination, and disability benefits. The post-retirement benefits of each of the systems are included in the plan descriptions below. In addition, the 1999 Legislature passed a guaranteed annual benefit adjustment (GABA) to the PERS, MPORS, GWPORS, SRS, JRS, HPORS, and FURS that will provide a maximum benefit increase of 3% each January, beginning January 2002, inclusive of all other adjustments to the member's benefit, if the recipient has been receiving a retirement benefit for at least 12 months. In addition, MPORS members hired prior to July 1, 1997, and retirees of this system, were required to make an election by December 31, 1997, for GABA coverage. For members of the JRS, HPORS, and FURS systems, the election for GABA coverage needed to be made by November 30, 2001.

The funding policies for each system provide for periodic employer and employee contributions (except VFCA) at rates specified by state law; contribution requirements are not actuarially determined. An actuary determines the actuarial implications of the funding requirement in a biennial actuarial valuation. The actuarial method used to determine the implications of the statutory funding level is the entry-age normal-cost method, with both normal cost and amortization of the unfunded accrued liability determined as a level percentage of payroll. To maintain a fund on an actuarially sound basis, the rate of contributions should fund the normal cost, in addition to amortizing the unfunded liability over a period not to exceed 30 years.

(1) State as the Single Employer

HPORS – Highway Patrol Officers Retirement System – This system, established in 1971 and governed by Title 19, chapters 2 & 6 of the Montana Code Annotated (MCA), provides retirement benefits for all members of the Montana Highway Patrol, including supervisory personnel. Rights are vested after five years of service. Member contributions are 9% of total salaries of active highway patrol officers hired prior to July 1, 1997 and not electing GABA coverage; and 9.05% for members hired after June 30, 1997, and members electing GABA coverage. The employer contribution rate is 36.33% of active officer's salaries. For members, there is no minimum age, but minimum service is 20 years for benefit eligibility. The service retirement benefit is based on a formula of 2.5% times the number of years of service times the highest average compensation. Post-retirement benefits, for non-GABA members, are in the form of minimum benefit supplements which insure the retiree's benefit is no less than 2% of a probationary highway patrol officer's salary for each year of the retiree's service, with the annual increase not to exceed 5% of the benefit nor 60% of the current base salary of a probationary officer. Members retired prior to July 1, 1991, who are at least age 55 and have been retired a minimum of five years, may be eligible for an annual lump-sum payment distributed in September. This lump-sum payment is funded by a registration fee of 25 cents per vehicle registration. The average payment in fiscal year 2002 was $2,231. This enhancement is limited to non-GABA members.

JRS – Judges Retirement System – This system, established in 1967 and governed by Title 19, chapters 2 & 5 of the MCA, provides retirement benefits for all district court judges, justices of the Supreme Court, and the Chief Water Judge. Members contribute 7% of their salaries while the State contributes 25.81% of active judges' salaries. Rights are vested after five years of membership service. For benefit eligibility, minimum service is five years, and the minimum age is 60. The monthly retirement benefit formula is 3 1/3% per year of the member's highest average compensation for the first 15 years of credited service, plus 1.785% per year for each year of credited service after 15 years. For non-GABA members, the percentages are based on the member's current salary, instead of the highest average compensation.

(2) State as an Employer Contributor to Cost-Sharing Multiple-Employer Systems

PERS-DBRP – Public Employees Retirement System - Defined Benefit Retirement Plan – This mandatory system, established in 1945 and governed by Title 19, chapters 2 & 3 of the MCA, provides retirement benefits to substantially all public employees not covered by another public system. Member contributions were 6.9% of covered compensation for fiscal year 2002. Each state agency and university system employer contributed 6.9% of PERS-covered payroll during fiscal year 2002. Participating local governments and school district employers contributed 6.8% of PERS-covered payroll. The State contributed 0.1% for local governments and school district employers from the State General Fund. Benefit eligibility is age 60 with at least 5 years of service, age 65 regardless of service, or 30 years of service, regardless of age. Actuarially reduced benefits may be taken with 25 years of service or at age 50 with at least five years of service. Monthly retirement benefits are determined by taking the greater of: (1) 2% times the number of years of service times the highest average compensation times any early retirement reduction, if necessary, or (2) a monthly annuity that is the actuarial equivalent of twice the member's accumulated regular contributions plus interest earned. Members' rights are vested after five years of membership service.

TRS – Teachers Retirement System – This mandatory system, established in 1937 and governed by Title 19, chapter 20 of the MCA, provides retirement services to all persons employed as teachers or professional staff of any public elementary or secondary school, or unit of the university system. Member and employer contributions are 7.15% and 7.47%, respectively, of earned compensation. Eligibility is met with a minimum of 25 years of service or age 60 with 5 years of creditable service. The formula for annual benefits is 1.6667% times creditable service years times the average final compensation. Rights are vested after five years of creditable service. Vested employees may retire at or after age 50 and receive reduced retirement benefits. Effective January 1, 1988, university system employees eligible to participate in the Teachers Retirement System could elect to participate in an Optional Retirement Plan established by the Board of Regents. A supplemental employer contribution to TRS is required to be amortized by July 1, 2033, for the amount that would not be paid for by contributions of university system members. The fiscal year 2002 contribution percentage of the total compensation of employees participating in the ORP program was 4.04% and the contribution was $3.96 million. The unfunded actuarial accrued liability of $495.3 million is included in the Schedules of Funding Progress.

SRS – Sheriffs Retirement System – This system, established in 1974 and governed by Title 19, chapters 2 & 7 of the MCA, covers all sheriffs and State Department of Justice criminal investigators hired after July 1, 1993. The member contribution is 9.245% of salary; the employer contribution is 9.535% of salary. Minimum years of service for normal service retirement eligibility is 20. The service retirement benefit is calculated at 2.5% of the highest average compensation for each year of membership service. Reduced benefits for early retirement may be taken with a minimum of five years of service and a minimum age of 50. Rights are vested after five years of membership service.

GWPORS – Game Wardens & Peace Officers Retirement System – This system, established in 1963 and governed by Title 19, chapters 2 & 8 of the MCA, provides retirement benefits for all persons employed as a game warden, warden supervisory personnel, and state peace officers not eligible to join the SRS, HPORS and MPORS systems. The member contributes 10.56% of salary while the State contributes 9.0% of covered active employee salaries. For benefit eligibility, minimum age is 50 and minimum years of service is 20. If subject to involuntary termination, a member may retire with five years of service at age 55. The yearly retirement benefit formula is 2.5% times the number of years of service times the highest average compensation. Rights are vested after five years of membership service.

Based on current actuarial assumptions, the current normal cost is more than the statutory contribution rate; therefore, the system is not actuarially sound. Enacted legislation opened the GWPORS to all state peace officers. The active membership increased from 494 in fiscal year 2000 to 609 in fiscal year 2002. The increase in membership causes the need to reevaluate the actuarial assumptions. Changes to the actuarial assumptions may change the normal cost of the plan.

(3) State as a Nonemployer Contributor to Cost-Sharing Multiple-Employer Systems

MPORS – Municipal Police Officers Retirement System – The system, established in 1974 and governed by Title 19, chapters 2 & 9 of the MCA, covers all municipal police officers of cities covered by the plan. It is a cost-sharing defined benefit plan with a special funding situation. The member contribution is 5.8% of salary for members employed prior to July 1, 1975; 7% of salary for members employed after June 30, 1975, and prior to July 1, 1979; 8.5% of salary for members employed after June 30, 1979, and prior to July 1, 1997; and 9% for members hired on or after July 1, 1997, and members electing GABA. City contributions are 14.41% of active police officer salaries. The State contributes 29.37% of active police officer salaries. The State's contribution is funded from the General Fund. Rights are vested after five years of membership service. Minimum years of service are five for benefit eligibility at age 50, or 20 years of service at any age. The service retirement benefit is 2.5% times the number of years of service times the final average compensation. For non-GABA members, a minimum benefit adjustment is required to insure that the retired members benefit is not less than one-half of the compensation paid to newly confirmed police officers in the city that last employed the member.

FURS – Firefighters Unified Retirement System – This system, established in 1981 and governed by Title 19, chapters 2 & 13 of the MCA, provides retirement benefits for firefighters employed by first and second-class cities and other cities that wish to adopt the plan. It is a cost-sharing defined benefit plan with a special funding situation. The member

contribution is 9.5% of compensation for members hired prior to July 1, 1997; and 10.7% for new hires after June 30, 1997, and for members electing GABA coverage. City contributions are 14.36% of total annual compensation. The state contribution is 32.61% of total annual compensation for all firefighters and is paid out of the General Fund. Minimum eligibility is 20 years regardless of age. For members not electing GABA and hired prior to July 1, 1981, monthly retirement benefit is 50% of final average compensation, plus 2% per year for each year in excess of 20 years, or 2.5% of final average compensation per year. Members hired before July 1, 1981, with less than 20 years, receive a retirement benefit of 2% per year of service. Members electing GABA and hired after July 1, 1981, receive 2.5% per year of service. Post-retirement benefits, for non-GABA members, require that each retiree receive at least 50% of the salary paid a newly confirmed active firefighter. Rights are vested after five years of membership service.

(4) State as a Nonemployer Contributor

VFCA – Volunteer Firefighters Compensation Act – This compensation program, established in 1965 and governed by Title 19, chapter 17 of the MCA, provides medical benefits and pension, disability and death benefits for all volunteer firefighters who are members of eligible volunteer fire companies in unincorporated areas of the state. VFCA is a plan with a special funding situation. The state contribution is 5% of fire insurance premium taxes collected. Rights are vested after ten years of qualified service. Eligibility requirements are 55 years of age and 20 years qualified service for a full benefit, or 60 years of age and a minimum of 10 years qualified service for a partial benefit.

C. Summary of Significant Accounting Policies

The pension trust funds' financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due and when 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.

D. Method Used to Value Investments

The Montana Board of Investments (BOI) manages the investments for the retirement systems. Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Mortgages are valued on the basis of future principal and interest payments and are discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on a discounted cash flow. Investments that do not have an established market are reported at estimated fair value. These values are based on market prices supplied to the BOI by its custodial bank, State Street Bank, and various brokerage services. The retirement systems have no investments of any commercial or industrial organization whose fair value equals 5% or more of the retirement systems net assets available for benefits.

E. Long-Term Contracts for Contributions

The Public Employees Retirement System has outstanding contributions for early retirement programs:

The 1993 Montana Legislature enacted House Bill 517 - Retirement Incentive Program (RIP) providing PERS members (eligible for a service retirement) an incentive to terminate between June 25, 1993, and December 31, 1993. Local government employers participated, through election, on or before June 1, 1993. The employer purchased, on the members behalf, one year of additional service for each five years of qualified service ("1 for 5"), up to a maximum of three years, for any retirement eligible member who terminated employment during the defined time period. A total of 898 members took advantage of the program (630 from 32 state agencies, 95 from 6 universities, and 173 from 48 local government agencies).

The Montana Legislature also provided a new provision of the Employee Protection Act (EPA) (Section 19-2-706, MCA) allowing state employees, eligible for a service retirement, whose positions have been eliminated, to have their employer purchase up to three years of "1 for 5" additional service. As of June 30, 2002, 247 employees have taken advantage of the provision.

The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. Total retirement incentive contributions received, including interest, during fiscal year 2002 totaled $144,782. June 30, 2002, outstanding balances were $342,095.

F. Actuarial Data

Actuarial valuations are performed every two years. Milliman USA prepared the July 2002 actuarial reports for the retirement systems, including TRS. Employee Benefit Resources, LLP, of Helena, MT, prepared the July 1, 1998, actuarial reports for the retirement systems, excluding TRS. Milliman & Robertson, Inc., of Seattle, WA, performed the

actuarial valuation for TRS for July 1, 1998, and July 1, 2000. Milliman & Robertson, of Portland, OR, prepared the July 1, 2000, actuarial reports for the retirement systems, excluding TRS.

G. Funding Policy and Annual Pension Cost

The following tables provide information concerning funding policies and annual pension costs (in thousands):

Single Employer Systems

	HPORS	JRS
Annual Pension Cost	$3,047	$1,032
Contributions		
Employer	$2,770	$1,032
Employee	693	280
License and Registration Fees	309	
Actuarial Valuation Date	7/01/02	7/01/02
Actuarial Cost Method	Entry age	Entry age
Amortization Method	Level percentage of total salaries, open	Level percentage of total salaries, open
Remaining Amortization Period	8.7 years	30 years
Asset Valuation Method	4 year smoothed market	4 year smoothed market
Actuarial Assumptions:		
Investment Rate of Return	8.0%	8.0%
Projected Salary Increases (includes inflation factor)	4.5%	4.5%
Merit	0%-7.3%	None
Postretirement Benefit Increases	None	None

Single Employer Systems

Year Ended	Annual Pension Costs (APC)	Percentage of APC Contributed	Net Obligation
HPORS			
06/30/00	2,805	99.5%	NONE
06/30/01	3,006	101.6%	NONE
06/30/02	3,047	101.3%	NONE
JRS			
06/30/00	899	100.0%	NONE
06/30/01	944	100.0%	NONE
06/30/02	1,032	100.0%	NONE

Multiple Employer Systems

Year Ended	Annual Required Contribution (ARC)	Percentage of ARC Contributed
PERS		
06/30/00	49,695	98.7%
06/30/01	52,843	100.7%
06/30/02	55,369	100.5%
MPORS		
06/30/00	8,866	100.6%
06/30/01	9,149	100.1%
06/30/02	9,732	101.1%
FURS		
06/30/00	7,773	97.8%
06/30/01	7,854	98.6%
06/30/02	8,432	98.1%
SRS		
06/30/00	2,056	106.8%
06/30/01	2,159	103.1%
06/30/02	2,338	102.1%
GWPORS		
06/30/00	1,069	102.9%
06/30/01	1,339	101.9%
06/30/02	1,544	103.3%
TRS		
06/30/00	48,376	100.0%
06/30/01	51,524	100.0%
06/30/02	51,519	100.0%

H. Schedules of Funding Progress

Single Employer Systems

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability(AAL) Entry Age (b)	Unfunded AAL(UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as Percentage of Covered Payroll ((b-a)/c)
HPORS						
07/01/98	59,531	78,722	19,191	75.62%	6,201	309.48%
07/01/00	77,810	76,397	(1,413)	101.85%	6,952	(20.33)%
07/01/02	81,734	94,850	13,116	86.17%	7,536	174.04%
JRS						
07/01/98	31,646	29,017	(2,629)	109.06%	3,144	(83.62)%
07/01/00	42,043	27,365	(14,678)	153.64%	3,483	(421.42)%
07/01/02	44,963	30,882	(14,081)	145.60%	4,000	(352.03)%

Multiple Employer Systems

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability(AAL) Entry Age (b)	Unfunded AAL(UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as Percentage of Covered Payroll ((b-a)/c)
PERS						
07/01/98*	2,128,065	2,300,328	172,263	92.51%	660,579	26.08%
07/01/00	2,843,347	2,273,407	(569,940)	125.07%	725,692	(78.54)%
07/01/02	3,076,781	3,077,764	983	99.97%	808,747	0.12%
MPORS						
07/01/98	94,908	173,642	78,734	54.66%	17,873	440.52%
07/01/00	129,826	181,109	51,283	71.68%	20,252	253.22%
07/01/02	143,516	226,827	83,311	63.27%	22,229	374.79%
FURS						
07/01/98	89,988	169,006	79,018	53.25%	15,104	523.15%
07/01/00	123,492	162,329	38,837	76.08%	16,547	235.00%
07/01/02	136,392	197,946	61,554	68.90%	17,953	342.86%
SRS						
07/01/98	92,160	81,077	(11,083)	113.67%	20,127	(55.06)%
07/01/00	126,338	87,836	(38,502)	143.83%	21,559	(178.59)%
07/01/02	138,590	121,625	(16,965)	113.95%	24,521	(69.19)%
GWPORS						
07/01/98	23,190	22,412	(778)	103.47%	7,839	(9.92)%
07/01/00	32,966	23,922	(9,044)	137.81%	11,875	(76.00)%
07/01/02	38,730	39,109	379	99.03%	17,151	2.21%
TRS						
07/01/98*	1,809,037	2,342,690	533,653	77.2%	529,795	100.7%
07/01/00	2,247,500	2,648,300	400,800	84.9%	537,500	74.6%
07/01/02	2,484,800	2,980,100	495,300	83.4%	563,200	87.9%

* PERS July 1, 1998, results adjusted by actuary.

** TRS July 1, 1998, results adjusted for 1.5% guaranteed annual benefit adjustment and $500 minimum benefit for legislation which passed in April 1999 and the new salary scale adopted in November 1998.

Nonemployer Contributor

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability(AAL) Entry Age (b)	Unfunded AAL(UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as Percentage of Covered Payroll ((b-a)/c)
VFCA						
07/01/98	13,941	18,354	4,413	75.96%	N/A	N/A
07/01/00	17,769	16,752	(1,017)	106.07%	N/A	N/A
07/01/02	19,254	26,808	7,554	71.82%	N/A	N/A

NOTE 6 — OTHER POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described in Note 5, Retirement Systems, the following postemployment benefits are provided:

The State provides 18 to 36 months optional postemployment health care benefits in accordance with Public Law 99-272, known as the Consolidated Omnibus Budget Reconciliation Act (COBRA), to the following employees and dependents who elect to continue and pay administratively established premiums: (1) employees who are covered by the State Group Benefits Plan at the time they discontinue state employment and (2) spouses or other dependents who lose dependent eligibility. At June 30, 2002, 89 certificate holders were receiving these benefits.

In accordance with section 2-18-704, MCA, the State also provides optional postemployment health care benefits to the following employees and dependents who elect to continue coverage and pay administratively established premiums: (1) employees and dependents who retire under applicable retirement provisions and (2) surviving dependents of deceased employees. Retirement eligibility criteria differ by retirement system (See Note 5). Administratively established retiree medical premiums vary between $168 and $455 per month depending on the medical plan selected, family coverage, and Medicare eligibility. Administratively established dental premiums vary between $28.60 and $46.60 depending on the coverage selected. The State acts as secondary payor for retired Medicare-eligible claimants. As of June 30, 2002, 3,165 retirees were covered for health care benefits.

The State reimburses all validated medical claims less member obligations (annual deductibles and co-insurance of the members selected medical plan). Dental claims are reimbursed at 50% to 100% depending on the services provided. The State funds claims on a pay-as-you-go basis. During the fiscal year, expenditures of $15,910,898 were recognized for postemployment health care benefits. Premium contributions received from former employees amounted to $11,932,870 leaving $3,978,028 of claims paid in excess of premium revenue received by the State.

In accordance with section 2-18-702, MCA, the Montana University System (MUS) provides postretirement health insurance benefits to eligible employees who receive a retirement benefit from the Teachers Retirement System, Public Employees Retirement System, or an annuity under the Optional Retirement Plan and have been employed by the MUS at least 5 years. Spouses, unmarried dependent children, and surviving spouses are also eligible. Administratively established premiums vary between $183 and $506 per month and are revised annually. Medicare-eligible plan members are assumed to be insured by Medicare. After an annual $500 deductible for non-Medicare-eligible retirees, the MUS plan reimburses 75% of the first $8,000 in medical claims and 100% thereafter. After a $350 deductible for Medicare-eligible retirees, the plan reimburses 75% for the first $4,000 in medical claims and 100% thereafter. The plan automatically reduces claim reimbursement for members eligible for Medicare, even if the member is not enrolled in Medicare. As of June 30, 2002, 1,390 retirees were enrolled in the MUS plan. Funding for the retiree health plan is on a pay-as-you-go basis. Based on amounts recorded through June 2002, estimated expenditures of $5,665,612 were recognized for postemployment health care benefits. Of this amount, $4,251,665 was paid by retirees through premiums, and the balance of $1,413,947 was paid by the MUS.

NOTE 7 — DEFERRED COMPENSATION PLAN

The State of Montana Deferred Compensation Program is administered by the PERB. The Deferred Compensation plan is a voluntary, tax-deferred retirement plan designed to supplement State Service Retirement, Social Security, and other retirement plans and savings. The State of Montana has offered this plan since 1976. Internal Revenue Service Code (Section 457) and MCA (Title 19, chapter 50) govern the plan. Assets of the deferred compensation plan are required to be held in trusts, custodial accounts, or insurance company contracts for the exclusive benefit of participants and their beneficiaries.

All employees of the State, including the Montana University System and contracting agencies, are eligible to participate. The compensation deferred is not available to employees until separation from service, retirement, death, or upon an unforeseeable emergency, when still employed and meeting IRS specified criteria. Participating employees are able to direct their deferrals into two primary investment options: (1) a "fixed" or stable value option which guarantees both principal (the payroll deferrals) and a quarterly rate of earnings; and (2) a "variable" option which currently consists of 22 mutual funds and five lifestyle/profile funds. Participants are allowed to participate in both options and, under the variable option, as many of the offered funds as they choose. As of June 30, 2002, the net assets of the Plan were $196,419,000.

NOTE 8 — RISK MANAGEMENT

There are two primary government public entity risk pools and two component unit public entity risk pools that are reported within the enterprise fund type: Primary government pools include Hail Insurance and Subsequent Injury Funds; component unit pools include State Compensation Insurance (New Fund) and State Compensation Insurance (Old Fund). Unpaid claims and claim adjustment expenses are estimated based on the ultimate cost of settling the claims including the effects of inflation and other societal/economic factors. There are two primary government other than public entity risk pools reported within the internal service fund type: Group Employees Comprehensive Medical and Dental Plan and Property and Casualty Insurance Plans. There is one primary government other than public entity risk pool reported within the enterprise fund type: the Montana University System (MUS) Group Benefits Plan. In all of these funds, there are no significant reductions in insurance coverage from the prior year, nor any insurance settlements exceeding insurance coverage. These funds use the accrual basis of accounting. By statute, these funds cannot invest in common stock. Investments are recorded at fair value. Premiums and discounts are amortized using the straight-line method over the life of the securities.

A. Public Entity Risk Pools

(1) Hail Insurance – Any Montana producer engaged in growing crops subject to destruction or damage by hail may participate in the Hail Insurance program. The Hail Insurance program issued 882 policies during the 2002 growing season. This fund accounts for premium assessments paid by producers for crop acreage insured, investment and interest earnings, administrative costs, and claims paid for hail damage. Depending upon the actuarial soundness of the reserve fund and the damage in a season, producers may receive a premium refund. Anticipated investment income is considered in computing a premium deficiency, of which there is none.

A claim must be submitted to the State Board of Hail Insurance within 14 days of a loss occurrence. The claim must indicate whether the grain is stemming, in the boot, heading out, in the milk, in the stiff dough, ready to bind, or combine. If beans, peas, or other crops are damaged, the growth-stage must also be indicated. Inspection of a crop will occur as promptly as possible after claim receipt. The liability on all insured crops expires after October 1. The insurance only covers loss or damage to growing grain which exceeds 5% destruction by hail.

The fund recorded a liability of $42,330 based on estimated claims through June 30, 2002. Any crop insurance liability is paid to producers within one year of occurrence; therefore, liabilities are not discounted. The fund has no excess insurance, reinsurance, or annuity contracts.

(2) Subsequent Injury – This fund provides benefits to workers, certified as disabled at the time of hiring, who are subsequently injured on the job and entitled to benefits under the Workers Compensation or Occupational Disease Act at the time of injury. The liability of the insurer for payment of compensation benefits is limited to 104 weeks of benefits actually paid. This fund will reimburse the insurer for all benefits paid after this 104-week time period. In Montana, there are 3,051 individuals with certified disabilities.

Workers compensation insurance premium experience modification factors are influenced by the two-year limitation, and employers may experience an insurance premium reduction. Therefore, this fund provides employers with a potential incentive for hiring a person with a certified disability.

This fund makes no provision for insured events of the current year. All Montana insurers are annually assessed a percentage of their paid losses sufficient to cover paid losses reimbursed from the fund in the preceding calendar year and the expenses of administration, less other income. An estimated liability is recorded based on a projected cost analysis (case-by-case) of each injured person with a certified disability. As of June 30, 2002, the amount of this liability was estimated to be $2,100,481.

(3) State Compensation Insurance (New Fund) – Liability coverage to employers for injured employees who are insured under the Workers Compensation and Occupational Disease Acts of Montana and workers compensation claims occurring on or after July 1, 1990, are reported in the New Fund. The New Fund must insure any employer who desires coverage. At fiscal year-end, approximately 24,961 employers were insured with the New Fund. Anticipated investment income is considered for computing a premium deficiency, and employers must pay premiums to the New Fund within specified time frames.

An actuarial study prepared by Tillinghast-Towers Perrin, as of June 30, 2002, estimated the cost of settling claims that have been reported, but not settled; and claims that have been incurred, but not reported. Because actual claim costs depend on such complex factors as inflation and changes in the law, claim liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and societal factors.

A provision for inflation is implicit in the calculation of estimated future claim costs because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. As of June 30, 2002, $346,400,000 of unpaid claims and claim adjustment expenses were presented at face value. When the New Fund purchases annuity contracts, the claim is settled in full and on a final basis, and all liability of the New Fund is terminated.

Acquisition costs represent costs associated with the acquisition of new insurance contracts or renewal of existing contracts and include agent commissions and expenses incurred in the underwriting process. New Fund acquisition costs are capitalized and amortized ratably over the subsequent year. The amount of capitalized acquisition costs in fiscal years ended June 30, 2002 and 2001, were $878,000 and $389,000, respectively. For the fiscal years ended June 30, 2002 and 2001, $389,000 and $171,000 of acquisition costs were amortized, respectively.

Statute requires the New Fund set premiums at least annually at a level sufficient to insure adequate funding of the insurance program during the period the rates will be in effect. Statute also requires the New Fund to establish a minimum surplus above risk-based capital requirements to secure the New Fund against risks inherent in the business of insurance.

(4) **State Compensation Insurance (Old Fund)** – The liability and payment of workers compensation claims for incidents occurring before July 1, 1990, are reported in the Old Fund. Funding for claim payments was accumulated through an Old Fund Liability Tax (OFLT) imposed on employer payroll (0.5%), employee wages (0.2%), and sole proprietor and subchapter S shareholder distributive income. In 1999, the 56th Legislature determined that the fund was adequately funded and discontinued the OFLT. This fund does not compute a premium deficiency.

An actuarial study prepared by Tillinghast-Towers Perrin, as of June 30, 2002, estimated the cost of settling claims that have been reported, but not settled; and claims that have been incurred, but not reported. At June 30, 2002, $128,902,000 of unpaid claims and claim adjustment expenses were reported at a net present value of $90,900,000, discounted at a 5.5% rate. Prior to 1999, the unpaid claims and unpaid claim adjustment expenses were presented at face value. Total Old Fund surplus as of June 30, 2002, was $24,866,000 compared to $22,782,000 as of June 30, 2001.

(5) **Changes in Claims Liabilities For the Past Two Years** – As indicated above, these funds establish liabilities for both reported and unreported insured events including estimates of future payments of losses and related claim adjustment expenses. The following tables present changes (in thousands) in those aggregate liabilities during the past two years. All information in these tables is presented at face value and has not been discounted.

	Hail Insurance		**Subsequent Injury**	
Primary Government	**2002**	**2001**	**2002**	**2001**
Unpaid claims and claim adjustment expenses at beginning of year	$ 520	$ 457	$2,719	$2,279
Incurred claims and claim adjustment expenses:				
provision for insured events of the current year	2,076	2,964	-	-
Increase (Decrease) in provision for Insured events of prior years	(395)	396	(352)	379
Total incurred claims and claim adjustment expenses	1,681	3,360	(352)	379
Payments:				
Claims and claim adjustment expenses attributable to insured events of the current year	(2,034)	(2,841)	-	-
Claims and claim adjustment expenses attributable to insured events of prior years	(124)	(456)	(267)	61
Total payment	(2,158)	(3,297)	(267)	61
Total unpaid claims and claim adjust. exp. at end of the year	$ 43	$ 520	$2,100	$2,719

Component Units	State Compensation Insurance (New Fund) 2002	2001	State Compensation Insurance (Old Fund) 2002	2001
Unpaid claims and claim adjustments expenses at beginning of year	$325,900	$314,900	$148,476	$167,915
Incurred claims and claim adjustment expenses: Provision for insured events of the current year	84,370	75,465	-	-
Increase (Decrease) in provision for insured events of prior years	5,361	(1,667)	(6,690)	(5,503)
Total incurred claims and claim adjustment expenses	89,731	73,798	(6,690)	(5,503)
Payments: Claims and claim adjustment expenses attributable to insured events of the current year	(16,693)	(14,140)	-	-
Claims and claim adjustment expenses attributable to insured events of prior years	(52,538)	(48,658)	(12,884)	(13,936)
Total payments	(69,231)	(62,798)	(12,884)	(13,936)
Total unpaid claims and claim adjust. exp. at end of the year	$346,400	$325,900	$128,902	$148,476

(6) **Risk Management Trend Information** – The following table only presents risk management trend information for the State Compensation Insurance (New Fund). Only the New Fund has a three to five-year development cycle contemplated by GASB Statement 10. The State Compensation Insurance (Old Fund) does not charge a premium for its services. The Hail Insurance Fund pays claims within a calendar year cycle that parallels the growing season from spring planting to fall harvesting; therefore, it has no three to five-year development cycle. State statute limits the payment of claims and the collection of premiums (and penalties) for the Subsequent Injury Fund from any developmental cycle.

The table below illustrates how the earned revenues (net of reinsurance) of the New Fund and its investment income compare to related costs of loss (net of loss assumed by reinsurers) and other expenses assumed by the fund as of the end of the fiscal year (in thousands). Section 3 shows the fund's incurred claims and allocated claim adjustment expense (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. Section 4 shows the cumulative amounts paid as of the end of successive years for each policy year. Section 6 shows how each policy year's incurred claims increased or decreased as of the end of successive years. This annual re-estimation 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. Section 7 compares the latest re-estimated incurred claims amount to the amount originally established (Section 3) and shows 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 estimates and re-estimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. This table will be expanded and revised as data for successive policy years develops.

State Compensation Insurance (New Fund)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
1. Premiums and investment revenue										
Earned	$214,793	$231,793	$190,685	$134,771	$102,233	$87,305	$78,482	$86,786	$109,248	$105,483
Ceded	289	318	269	519	348	303	260	855	2,952	(465)
Net Earned	$214,504	$231,475	$190,416	$134,252	$101,885	$87,002	$78,222	$85,931	$106,296	$105,948
2. Unallocated expenses including overhead	$ 7,758	$ 8,890	$ 15,049	$ 18,013	$ 13,136	$15,061	$19,745	$23,189	$ 28,097	$ 32,679
3. Estimated losses and expenses end of accident year										
Incurred	$186,480	$199,890	$164,628	$ 95,067	$ 76,067	$64,983	$64,645	$65,957	$ 68,267	$ 81,560
Ceded	-	-	-	-	-	-	-	-	-	-
Net Incurred	$186,480	$199,890	$164,628	$ 95,067	$ 76,067	$64,983	$64,645	$65,957	$ 68,267	$ 81,560
4. Net paid (cumulative) as of:										
End of policy year	$ 18,347	$ 18,693	$ 18,137	$ 15,818	$ 12,589	$12,943	$13,723	$13,177	$ 14,140	$ 16,693
One year later	46,343	45,947	40,473	32,890	28,451	28,222	29,976	29,218	32,888	
Two years later	62,717	60,971	52,073	42,361	35,706	35,753	39,298	37,555		
Three years later	71,666	67,576	58,722	47,283	39,860	41,004	45,748			
Four years later	76,280	72,212	62,419	50,267	43,105	44,478				
Five years later	80,165	75,799	65,919	52,791	46,478					
Six years later	82,981	78,306	68,541	54,962						
Seven years later	85,357	80,861	70,816							
Eight years later	88,080	83,150								
Nine years later	90,094									
5. Re-estimated ceded losses and expenses	$ 272	$ -	$ -	$ -	$ 5,372	$ 106	$ 750	$ -	$ -	$ -
6. Re-estimated net incurred losses and expense:										
End of policy year	$186,480	$199,890	$164,628	$ 95,067	$ 76,067	$64,983	$63,807	$65,957	$ 68,267	$ 81,560
One year later	184,030	184,920	124,123	88,923	67,235	64,308	64,348	66,421	71,094	
Two years later	167,052	135,472	107,074	77,286	59,054	60,467	66,660	66,662		
Three years later	133,017	116,756	95,456	73,864	60,811	61,989	69,345			
Four years later	120,583	107,656	94,517	74,022	64,439	64,944				
Five years later	111,208	105,052	92,231	73,197	59,079					
Six years later	109,415	106,039	91,771	74,329						
Seven years later	111,638	105,668	92,637							
Eight years later	111,084	105,606								
Nine years later	110,921									
7. Increase (decrease) in estimated net incurred losses and expenses from end of policy year	$ (75,559)	$ (94,284)	$ (71,991)	$(20,738)	$ (16,988)	$ (39)	$ 4,700	$ 705	$ 2,827	$ -

B. Other Than Public Entity Risk Pools

(1) Group Employee Comprehensive Medical and Dental Plan – With the exception of vision care services, this plan is fully self-insured, with the State assuming the risk for claims incurred by employees of the State, elected officials, retirees, former employees covered by COBRA benefits and their dependents; vision care services are insured by the Vision Service Plan. The State contracts with Blue Cross/Blue Shield, PEAK, and New West for administration of its self-insured plans. Premiums are collected through payroll deductions, deductions through the Public Employees Retirement Division, and self-payments and are recorded as revenue in the Employee Group Benefits Internal Service Fund. At June 30, 2002, estimates for claims liabilities, which include incurred, but not reported, claims were $9,163,948 based on a formula provided by Buck Consultants, a consulting actuarial firm. A liability is reported in the accompanying financial statements for these estimated claims.

(2) Montana University System (MUS) Group Benefits Plan – This plan was authorized by the Regents to provide medical, dental, and vision insurance coverage to employees of the Montana University System, the Student Assistance Foundation (SAF), and the State Bar of Montana, as well as their dependents, retirees, and COBRA members. The MUS Group Benefits Plan is fully self-insured, with three exceptions. The three insured products are HMOs administered by New West Health Services serving some employees and dependents in Missoula, Helena, Havre, and Billings; PEAK Health Plan serving some employees and dependents in Butte; and a voluntary vision plan administered by VSP serving employees, retirees, and their dependents. Blue Cross/Blue Shield is the claims administrator for the self-insured plan. Managed Care Montana (APS) has a contract for utilization management: the utilization management program consists of hospital pre-authorization, case management, and medical necessity review. Premiums are collected from employees through payroll deductions and recorded in the MUS Group Insurance Enterprise Fund. The claims liability is calculated by Buck Consultants and estimated to be $2,982,494 as of June 30, 2002, based on prior year experience. A liability is reported in the accompanying financial statements for these estimated claims.

(3) Property & Casualty Insurance Plans – This self-insurance plan provides coverage for general liability, automobile liability, automobile physical damage, foster care liability, and state-administered foreclosure housing units. The State self-insures the $150,000 deductible per occurrence for most property insurance, as well as various deductible amounts for other state property. The State also self-insures against losses of property below $150,000 of value, with state agencies paying the first $1,000. Commercial property insurance protects approximately $2.2 billion of state-owned buildings and contents. The State's property insurance includes separate earthquake and flood protection coverage (each in the amount of $100 million) with deductibles of $1 million for earthquake and $500,000 for flood per occurrence. Premiums are collected from all state agencies, including component units, and recorded as revenue in the Administration Insurance Internal Service Fund.

An annual actuarial study, prepared by Tillinghast-Towers Perrin Company, and issued for the accident period July 1, 1991, through June 30, 2002, is the basis for estimating the liability for unpaid claims and is supported by historical loss data. The June 30, 2002, estimated claims liability of $29,848,481 is reported in the accompanying financial statements.

(4) Changes in Claims Liabilities For the Past Two Years – These funds establish liabilities for both reported and incurred, but not reported, claims. The following table presents changes in the balances of claims liabilities during the past two fiscal years (in thousands):

	Group Employees Medical & Dental		MUS Group Benefits		Prop. & Casualty Insurance	
	2002	2001	2002	2001	2002	2001
Amount of claims liabilities at the beginning of each fiscal year	$ 7,181	$ 7,080	$ 2,378	$ 2,271	$25,234	$25,347
Incurred claims:						
Provision for insured events of the current year	68,434	54,809	29,642	26,007	6,877	6,314
Increases (decreases) in provision for insured events of prior years	1,983	101	604	107	3,286	(877)
Total incurred claims	70,417	54,910	30,246	26,114	10,163	5,437
Payments:						
Claims attributable to insured events of the current year	(61,440)	(50,140)	(29,642)	(26,007)	(633)	(1,205)
Claims attributable to insured events of prior years	(6,994)	(4,669)	-	-	(4,916)	(4,345)
Total payments	(68,434)	(54,809)	(29,642)	(26,007)	(5,544)	(5,550)
Total claims liability at end of each fiscal year	$ 9,164	$ 7,181	$ 2,982	$ 2,378	$29,848	$25,234

NOTE 9 — COMMITMENTS

A. Highway Construction

At June 30, 2002, the Department of Transportation had contractual commitments of approximately $191.7 million for construction of various highway projects. Funding for these highway projects is to be provided from federal grants and matching state special revenue funds.

B. Capital Construction

At June 30, 2002, the Department of Administration, Architecture & Engineering Division, had commitments of approximately $12.1 million for capital projects construction. The primary government will fund $10.7 million of these projects, with the remaining $1.4 million coming from the state university system.

C. Proprietary Fund Commitments

Budgets are administratively established in the enterprise and internal service funds, excluding depreciation, compensated absences, and bad debt expense. Appropriations may be committed for goods/services that are not received as of fiscal year-end. These executory commitments are included in unrestricted net assets in the accompanying financial statements as follows (in thousands):

Primary Government	Amount
Enterprise Funds	
Historical Society Publications	$ 1
Internal Service Funds	
Highway Equipment	$3,529
Building and Grounds	228
Information Services Division	160
DEQ Indirect Cost Pool	81
Warrant Processing	53
FWP Equipment	35
FWP Warehouse Inventory	12
Aircraft Operation	12
Admin Supply	11
Employee Group Benefits	6
Commerce Central Services	5
Subtotal-Internal Service Funds	$4,132
Total-Primary Government	$4,133
Component Units	
Housing Authority	$ 7
Facility Finance Authority	5
Total-Component Units	$ 12

NOTE 10 — LEASES/INSTALLMENT PURCHASES PAYABLE

The State has entered into various capital and operating leases for land, buildings, equipment, and computer software. Lease contracts are required by law to contain a clause indicating continuation of the lease is subject to funding by the Legislature. It is expected, in the normal course of operations, that most of these leases will be replaced by similar leases.

A. Capital Leases/Installment Purchases

Changes in capitalized leases/installment purchases are as follows (in thousands):

Primary Government	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Governmental Activities	$5,002	$1,482	$2,832	$3,652	$1,859
Discretely Presented Component Units					
Montana State University	$ 237	$ 492	$ 317	$ 412	$ 149
University of Montana	1,013	837	508	1,342	632
State Comp Ins (New Fund)	37	306	52	291	68
Total Component Units	$1,287	$1,635	$ 877	$2,045	$ 849

Fiscal Year Ending June 30	Primary Government	Discretely Presented Component Units			
	Governmental Activities	Montana State University	University of Montana	State Comp Insurance New Fund	Totals
2003	$2,000	$171	$ 716	$ 83	$970
2004	1,231	159	442	82	683
2005	243	107	264	82	453
2006	63	11	54	57	122
2007	37	6	17	20	43
2008-2012	321	-	-	-	-
Total Minimum Pmts	$3,895	$454	$1,493	$324	$2,271
Less: Interest	243	42	151	33	226
Present Value of Minimum Payments	$3,652	$412	$1,342	$291	$2,045

B. Operating Leases

Total rental payments of primary government and discretely presented component units for operating leases in fiscal year 2002 were $9,957,000 and $534,000, respectively. Future rental payments under operating leases are as follows (in thousands):

Fiscal Year Ending June 30	Primary Government	Discretely Presented Component Units
2003	$11,269	$ 519
2004	9,070	477
2005	8,276	511
2006	7,182	171
2007	6,648	39
2008-2012	26,966	167
2013-2017	9,242	162
2018-2022	1,982	162
Total Future Rental Payments	$80,635	$2,208

NOTE 11 — STATE DEBT

A. General Information

The State has no constitutional limit on its power to issue obligations or incur debt, other than a provision that no debt may be created to cover deficits incurred because appropriations exceeded anticipated revenues. The Board of Examiners (consisting of the Governor, Secretary of State, and Attorney General) is authorized, pursuant to various enabling acts, to issue bonds and notes of the State.

B. Short-Term Debt

The Board of Examiners, upon recommendation of the Department of Administration, may issue notes in anticipation of the receipt of taxes and revenues. No notes may be issued to refund outstanding notes. The notes must be redeemed by the end of the fiscal year in which issued.

The Board of Investments (BOI) of the State of Montana is authorized to issue Municipal Finance Consolidation Act Bonds which may not aggregate more than $75 million. The purpose of the bonds is to provide funds for the BOI to make loans to eligible government units. The bonds are not in any way a debt or liability of the State of Montana. The bonds are limited obligations of the BOI, payable solely from repayments of principal and interest on loans made by the BOI to participating government units, investment income under the indenture, and an irrevocable pledge by the BOI. The BOI has no taxing power. Bondholders may elect to have their bonds purchased by the trustee on March 1 of each year until maturity. These issues are considered to be demand bonds and are included in the current portion of bonds/notes payable. The amounts issued and outstanding at June 30, 2002, were as follows (in thousands):

Series	Amount Issued	Balance June 30, 2002
1992	$6,500	$ 6,075
1994	7,500	7,005
1995	7,500	7,150
1997	10,000	9,775
1998	12,500	12,285
2000	15,000	15,000
Total		$57,290

C. Long-Term Debt

The full faith, credit, and taxing powers of the State are pledged for the payment of all general obligation debt. Revenue and mortgage bonds are secured by a pledge from the facilities to which they relate and by certain other revenues, fees, and assets of the State and the various colleges and universities. Primary government bonds and notes outstanding at June 30, 2002, were as follows (in thousands):

				Principal Payments		
Governmental Activities	Series	Amount Issued	Interest Range (%)	FY 2003	In Year of Maturity (7)	Balance June 30, 2002
General Obligation Bonds						
Water Development Program (1)	1989B	$ 500	8.55	$ 25	$ 35 (2006)	$ 125
Water Development Program (1)	1991A	750	8.0	60	90 (2007)	375
GO Refunding	1992	31,330	5.5-6.2	425	390 (2010)	3,475
Energy Conservation Program (2)	1993A	1,500	4.7-4.75	170	180 (2004)	350
Long-Range Bldg Program	1993B	3,185	4.2-4.25	290	310 (2004)	600
Renewable Resource Development (1)	1993C	750	5.55-5.65	90	95 (2004)	185
Long-Range Bldg Program	1994A	22,540	4.4-6.0	1,010	1,725 (2014)	15,930
Wastewater Treatment Works	1994B	2,200	5.1-6.1	85	180 (2016)	1,765
Long-Range Bldg Program	1994C	21,955	5.25-5.4	900	1,000 (2005)	2,850
Energy Conservation Program (2)	1994D	1,600	5.3-5.5	180	200 (2005)	570
Renewable Resource Development (1)	1994E	750	7.9-8.1	90	105 (2005)	290
Energy Conservation Program (2)	1996A	1,650	4.15-4.4	170	195 (2006)	730
Renewable Resource Development (1)	1996B	1,250	5.9-6.1	130	155 (2006)	570
Wastewater Treatment Works	1996C	2,765	4.8-5.75	120	120 (2017)	2,285
Long-Range Bldg Program	1996D	30,075	5.25-6.0	1,150	2,370 (2017)	25,080
Renewable Resource Development (1)	1996E	1,000	6.95-7.15	100	130 (2007)	580
Renewable Resource Development (1)	1997A	2,000	6.9-7.4	105	210 (2013)	1,650

Governmental Activities	Series	Amount Issued	Interest Range (%)	Principal Payments FY 2003	Principal Payments In Year of Maturity (7)	Balance June 30, 2002
Long-Range Bldg Program	1997B	12,640	4.5-5.0	755	595 (2018)	9,890
Wastewater Treatment Works	1998A	3,510	4.05-5.15	130	260 (2019)	3,150
Long-Range Bldg Program	1998B	34,545	3.9-4.85	1,320	2,555 (2018)	29,675
Information Technology	1998C	41,390	4.5-5.0	4,480	4,075 (2008)	23,265
Long-Range Bldg Program	1998D	14,855	4.4-5.0	100	1,720 (2015)	14,365
Energy Conservation Program (2)	1998E	1,250	4.25-4.6	120	150 (2008)	800
Renewable Res. Prgm Loans-Taxable	1999	1,035	6.0-6.5	50	105 (2015)	945
Long-Range Bldg Program	1999C	16,990	4.0-5.0	620	1,250 (2019)	15,045
Drinking Revolving Fund (10)	1998F	3,065	3.7-4.85	120	230 (2019)	2,840
Drinking Water Revolving Fund (10)	2000A	2,990	4.6-5.6	95	240 (2021)	2,900
Pollution Control Revolving Fund (10)	2000B	3,325	4.6-5.6	100	270 (2021)	3,225
Long-Range Bldg Program	2000C	17,195	5.0-5.55	510	1,320 (2020)	15,440
Information Technology	2000D	18,000	5.0	1,280	2,250 (2010)	14,830
Information Technology	2000E	800	5.6	270	270 (2003)	270
Long-Range Bldg Program	2001B	11,430	4.1-5.25	375	830 (2021)	10,640
Information Technology	2001C	1,600	3.85-4.2	135	185 (2011)	1,420
Energy Conservation Program (2)	2001D	1,250	3.85-4.2	105	145 (2011)	1,105
Renewable Resource Development (1)	2001E	1,040	5.2-6.8	45	105 (2017)	1,040
Drinking Revolving Fund (10)	2001G	3,190	4.0-4.75	95	235 (2022)	3,190
Pollution Control Revolving Fund (10)	2001H	2,690	4.0-4.75	80	200 (2022)	2,690
Total General Obligation Bonds		$318,590		$15,885		$214,135
Special Revenue Bonds						
Water Conservation (3)	-	$ 50	5.0	$ 2	$ 1 (2012)	$ 22
Department of Transportation	1993	72,375	5.0-5.05	13,095	3,705 (2004)	16,800
Renewable Resource Program (4)	1996A	14,985	4.45-5.2	1,060	110 (2017)	9,230
Renewable Resource Program (4)	1997A	1,205	6.65-7.3	40	110 (2017)	1,075
Renewable Resource Program (4)	1997B	2,660	4.5-5.375	95	210 (2017)	2,320
Developmental Center Project (6)	1994	13,100	5.5-6.4	390	1,015 (2019)	11,055
State Hospital Project (6)	1997	25,915	4.15-5.0	740	1,820 (2022)	23,870
Renewable Resource Program (4)	2001A	420	4.17-5.59	15	30 (2021)	405
Renewable Resource Program (4)	2001B	1,750	5.45-7.1	50	150 (2021)	1,705
Renewable Resource Program (4)	2001C	12,155	2.8-4.3	1,640	790 (2013)	10,620
Renewable Resource Program (4)	2001D	21,450	2.25-4.7	895	1,795 (2018)	21,450
Renewable Resource Program (4)	2001E	885	2.1-4.85	25	65 (2022)	885
Renewable Resource Program (4)	2001F	900	3.3-6.2	20	75 (2022)	900
Total Special Revenue Bonds		$167,850		$18,067		$100,337
Notes Payable						
Middle Creek Dam Project (5)		$ 3,272	8.125	$ 43	124 (2034)	$ 2,975
Tongue River Dam Project (9)		11,300	-	290	290 (2039)	10,431
Dept. of Justice INTERCAP Loan (8)		1,905	Variable	116	91 (2012)	1,655
Dept. of Environmental Quality INTERCAP Loan (8)		1,212	Variable	120	75 (2008)	736
Dept. of Corrections Resident Accounting System Loan (11)		320	5.73	64	71 (2005)	202
Office of the Commissioner of Higher Education INTERCAP Loan (8)		372	Variable	95	105 (2005)	301
Natural Resrce. Damage Lit. Pgm. (12)		1,827	Variable	-	-	1,827
Dept of Transportation (Motor Pool) INTERCAP Loan (8)		10,487	Variable	2,075	409 (2006)	4,916
Historical Society INTERCAP Loan (8)		100	Variable	32	35 (2005)	100
Dept of Natural Resources INTERCAP Loan (8)		92	Variable	5	10 (2009)	60
Total Notes Payable		$ 30,887		$ 2,840		$ 23,203
						337,675
Deferred Amount on Refunding						(987)
Unamortized Discount						(130)
Total Governmental Activities		$517,327		$36,792		$336,558

Governmental Activities	Series	Amount Issued	Interest Range (%)	Principal Payments FY 2003	Principal Payments In Year of Maturity (7)	Balance June 30, 2002
Business-Type Activities						
Bonds/Notes Payable						
State Lottery Note Payable		$5,025	5.12	$1,055	$1,110 (2004)	$2,165
Economic Development Bonds (13)						
Municipal Finance Consolidation Act Bonds (Irrigation Program) (14)	1998	4,976	6.60-7.75	515	130 (2014)	2,180
Municipal Finance Consolidation Act Bonds (School District Pooled Refunding Program) (15)	1991	6,234	4.75-6.5	285	294 (2005)	866
Conservation Reserve Enhancement Program (CRP Notes) (16)		8,703	6-8	1,240	43 (2011)	8,703
Subtotal Economic Dev. Bonds		19,913		2,040		11,749
Total Business-Type Activities		$24,938		$3,095		$13,914

(1) All Water Development Program Bonds and the Renewable Resource Development Bonds are secured additionally by a pledge of, and payable from, certain coal severance taxes. Series 1989B, 1991A, and 1993C bonds are also secured by a pledge of loan repayments from loans made from the bond proceeds.

(2) Bonds issued for financing the design, construction, and installation of energy conservation projects at various state buildings.

(3) Bonds sold to Farmers Home Administration.

(4) Issued by the Department of Natural Resources and Conservation (DNRC) and backed by a pledge of coal severance taxes and project revenues.

(5) U.S. Bureau of Reclamation loan to Montana Department of Natural Resources & Conservation. The outstanding balance includes $244,662 of interest owed.

(6) Facility Finance Authority loan to the Department of Public Health and Human Services for the Montana Developmental Center Project and the Montana State Hospital Project.

(7) Year of maturity refers to fiscal year.

(8) Montana Board of Investments loans to Departments from the INTERCAP loan program.

(9) Northern Cheyenne Tribe loan to the Montana Dept. of Natural Resources & Conservation (DNRC). The loan will not accrue interest and will be repaid over 39 years. Loan repayment is secured by the issuance of a coal severance tax bond to the tribe.

(10) Provide matching funds to enable the State to obtain capitalization grants from the U.S Environmental Protection Agency for water system development loans to state political subdivisions.

(11) Norwest loan to provide funds for the development of a Y2K-compliant resident accounting system.

(12) Board of Investments loan to the Department of Justice for the Natural Resource Damage Litigation Program. Loan repayment is secured by a pledge of amounts to be recovered in the ongoing litigation with Atlantic Richfield Company.

(13) Economic Development & Municipal Finance Consolidation Act Bonds (EDB) – This program is directed by the nine-member Board of Investments, which is attached to the Department of Commerce for administrative purposes. This program assists Montana's small businesses and local governments in obtaining long-term, fixed rate financing through private Montana lending institutions.

(14) These bonds were issued to obtain funds for the Board of Investments, State of Montana, to purchase the refunding bonds of participating Irrigation Districts for the purpose of prepaying the U.S. Department of Interior, Bureau of Reclamation Projects Loans. The Irrigation Bonds, and the interest thereon, are payable solely from the collection of a special tax or assessment, which is a lien against real property in the Irrigation District. The Irrigation Bonds are not obligations of the State of Montana. However, the Irrigation Bonds are limited obligations of the Board of Investments, due to an irrevocable pledge to lend money for deposit by the trustee of the Irrigation District Pooled Loan Reserve Account E in an amount to any deficiencies therein, on any payment date. The indenture does not permit the issuance of additional bonds.

(15) These bonds were issued for the purpose of providing funds for the Board of Investments, State of Montana, to purchase the general obligation refunding bonds of participating Montana school districts. The School District Refunding Bonds, and the interest thereon, are payable from real property taxes levied within the school district. These bonds are limited obligations of the Board of Investments and are not a debt or liability of the State of Montana, and neither the faith and credit nor the taxing power of the State is pledged to the payment of principal of or interest on the bonds.

(16) These bonds and notes were issued for the purpose of providing funds for the Board of Investments, State of Montana, to make loans to participating farmers and ranchers under its Conservation Reserve Enhancement Program. The Series 1991 Bonds are not in any way a debt or liability of the State of Montana, and neither the full faith and credit nor the taxing power of the State of Montana is pledged to the payment of the principal of or interest on the Series 1991 Bonds. However, the 1991 bonds are limited obligations of the Board of Investments. The Bond Anticipation Notes (BAN), which matured on November 15, 1992, were reissued to correspond with maturities per the underlying loans. On November 15, 1994, eleven BANs were reissued to comply with statutory requirements limiting the maturity of notes to five years from issuance date. The outstanding BANs as of November 15, 1996, were reissued as bonds to comply with statutory requirements. The board now issues CRP bonds for the duration of the CRP contract purchased.

D. Debt Service Requirements

Primary government debt service requirements at June 30, 2002, were as follows (in thousands):

Governmental Activities

Year Ended June 30	General Obligation Bonds		Special Revenue Bonds		Notes Payable	
	Principal	Interest	Principal	Interest	Principal	Interest
2003	$ 15,885	$10,244	$ 18,067	$ 4,356	$ 2,840	$ 281
2004	15,470	9,462	8,982	3,747	2,451	209
2005	15,595	8,678	5,522	3,449	1,715	142
2006	15,990	7,889	5,282	3,232	1,090	100
2007	16,185	7,094	4,733	3,021	695	77
2008-2012	64,175	25,003	22,041	12,083	4,402	377
2013-2017	53,610	10,745	22,060	6,780	1,808	170
2018-2022	17,225	1,350	13,650	1,707	1,909	140
2023-2027	-	-	-	-	2,016	102
2028-2032	-	-	-	-	2,155	55
2033-2037	-	-	-	-	1,832	6
2038	-	-	-	-	290	-
Total	$214,135	$80,465	$100,337	$38,375	$23,203	$1,659

Governmental activities notes payable includes INTERCAP loans with an interest rate that varies based on the underlying bond rate of the Montana Board of Investments Municipal Finance Consolidation Act Bonds (INTERCAP Revolving Program) and is adjusted annually.

Business-Type Activities

Year Ended June 30	State Lottery		Economic Development Bonds	
	Principal	Interest	Principal	Interest
2003	$1,055	$ 91	$ 1,997	$767
2004	1,110	36	2,106	651
2005	-	-	1,927	529
2006	-	-	1,476	413
2007	-	-	1,444	306
2008-2012	-	-	2,549	407
2013-2014	-	-	250	20
Total	$2,165	$127	$11,749	$3,093

Debt service requirements of discretely presented component units at June 30, 2002, were as follows (in thousands):

Year Ended June 30	Montana State University		University of Montana		Housing Authority	
	Principal	Interest	Principal	Interest	Principal	Interest
2003	$ 5,079	$ 4,361	$ 3,540	$ 6,212	$ 37,973	$ 37,819
2004	5,028	4,121	3,829	6,064	12,401	37,418
2005	5,182	3,881	3,789	5,898	12,772	36,940
2006	5,217	3,628	3,682	5,722	13,164	36,347
2007	4,007	3,392	3,836	5,554	14,362	35,781
2008-2012	20,368	15,553	21,361	24,871	79,372	165,810
2013-2017	22,925	11,861	26,579	19,250	95,928	144,529
2018-2022	29,045	5,160	34,300	11,328	114,205	111,528
2023-2027	3,950	459	18,110	1,750	145,575	73,715
2028-2032	-	-	-	-	140,205	28,862
2033-2037	-	-	-	-	22,120	3,801
2038-2040	-	-	-	-	2,865	323
Total	$100,801	$52,416	$119,026	$86,649	$690,942	$712,873

Montana State University and the University of Montana bonds/notes payable includes INTERCAP loans with an interest rate that varies based on the underlying bond rate of the Montana Board of Investments Municipal Finance Consolidation Act Bonds (INTERCAP Revolving Program) and is adjusted annually.

E. Summary of Changes in Long-Term Liabilities Payable

Primary government long-term liability activity for the year ended June 30, 2002, was as follows (in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Governmental Activities					
Bonds/Notes Payable					
General Obligation Bonds	$ 232,220	$ -	$ 18,085	$ 214,135	$ 15,885
Special Revenue Bonds	115,378	35,390	50,431	100,337	18,067
Notes Payable	22,598	4,175	3,570	23,203	2,840
	370,196	39,565	72,086	337,675	36,792
Deferred Amount on Refunding	-	(1,080)	(93)	(987)	-
Unamortized Discount	-	(139)	(9)	(130)	-
Total Bonds/Notes Payable	370,196	38,346	71,984	336,558	36,792
Other Liabilities					
Compensated Absences Payable	63,199	37,569	34,312	66,456	34,292
Early Retirement Benefits Payable	356	136	156	336	91
Arbitrage Rebate Tax Payable	1,425	259	233	1,451	1,036
Estimated Claims	32,415	80,466	73,869	39,012	15,085
Total Other Liabilities	97,395	118,430	108,570	107,255	50,504
Total-Governmental Activities Long-Term Liabilities	$ 467,591	$156,776	$180,554	$ 443,813	$ 87,296
Business-Type Activities					
Bonds/Notes Payable					
State Lottery	$3,167	$ -	$1,002	$2,165	$1,055
Economic Development Bonds	13,999	1,044	3,294	11,749	2,040
Total Bonds/Notes Payable	17,166	1,044	4,296	13,914	3,095
Other Liabilities					
Compensated Absences Payable	901	572	495	978	491
Arbitrage Rebate Tax Payable	373	74	275	172	72
Estimated Claims	5,617	34,897	35,389	5,125	3,348
Lottery Prizes Payable	3,433	30,842	31,231	3,044	1,337
Total Other Liabilities	10,324	66,385	67,390	9,319	5,248
Total-Business-Type Activities Long-Term Liabilities	$ 27,490	$ 67,429	$ 71,686	$ 23,233	$ 8,343

Long-term liability activity of discretely presented component units for the year ended June 30, 2002, was as follows (in thousands):

Discretely Presented Component Units					
Bonds/Notes Payable					
Montana State University	$ 100,715	$ 1,188	$ 5,311	$ 96,592	$ 5,079
University of Montana	119,536	648	3,196	116,988	3,540
Housing Authority	714,021	89,593	113,691	689,923	37,973
Total Bonds/Notes Payable	934,272	91,429	122,198	903,503	46,592
Other Liabilities					
Compensated Absences Payable	36,757	18,505	15,934	39,328	16,728
Arbitrage Rebate Tax Payable	942	660	99	1,503	570
Estimated Claims	430,600	89,731	83,030	437,301	83,642
Total Other Liabilities	468,299	108,896	99,063	478,132	100,940
Total-Discretely Presented Component Units Long-Term Liabilities	$1,402,571	$200,325	$221,261	$1,381,635	$147,532

The compensated absences liability attributable to the governmental activities will be liquidated by several of the governmental and internal service funds. The early retirement benefits payable will be liquidated by the general, state special revenue, and federal special revenue funds. The arbitrage rebate tax payable will be liquidated by the state special revenue and debt service funds. The Employee Group Benefits and Administration Insurance internal service funds will liquidate the estimated claims liability.

F. Refunded and Early Retired Bonds

Primary Government

Pre-payments and Early Retirements

During fiscal year 2002, the Department of Natural Resources and Conservation (DNRC) used current available resources to pre-pay $175,000 of Series 1989B Water Development Program Bonds and $620,000 of Series 2001C Renewable Resource Program Revenue Bonds. DNRC used current available resources to redeem Series 1991B Wastewater Treatment Works Bonds in the amount of $1,965,000.

Advance Refundings

On August 9, 2001, the Montana Department of Natural Resources and Conservation (DNRC) issued $12,155,000 of 2001 Refunding Series C, Coal Severance Tax, Renewable Resource Program Bonds to advance refund $5,100,000 of 1992 Refunding Series A and $6,840,000 of 1992B Coal Severance Tax, Renewable Resource Program Bonds. The net proceeds of $11,963,248 (after payment of $191,752 in underwriting fees and other issuance costs) plus an additional $315,625 of certain other available funds were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust, with an escrow agent, to provide for future debt service payments. As a result, the 1992 Refunding Series A and the 1992B Series bonds are considered to be defeased, and the liability for those bonds has been removed from the financial statements. The defeasance resulted in a reduction of debt service to maturity of $675,000 and an economic gain of $626,000.

On October 31, 2001, the Montana Department of Natural Resources and Conservation (DNRC) issued $21,450,000 of 2001 Refunding Series D, Coal Severance Tax, Renewable Resource Program Bonds to advance refund $21,735,000 of 1991 Refunding Series A Coal Severance Tax, Renewable Resource Program Bonds. The net proceeds of $21,036,557 (reduced for the original issue discount of $139,042 and after payment of $ $274,400 in underwriting fees and other issuance costs) plus an additional $1,439,629 of certain other available funds were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust, with an escrow agent, to provide for future debt service payments. As a result, the 1991 Refunding Series A bonds are considered to be defeased, and the liability for those bonds has been removed from the financial statements. The defeasance resulted in a reduction of debt service to maturity of $5,912,000 and an economic gain of $4,095,000.

Deferred loss on primary government refundings at June 30, 2002, was $987,000.

Prior-year Defeasance of Debt

In prior years, the State of Montana has defeased certain general obligation and revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the financial statements. At June 30, 2002, $41.5 million of bonds outstanding are considered defeased.

Discretely Presented Component Units

Current Refundings

Housing Authority – On May 31, 2001, Series 2001A bonds were issued in the amount of $71,000,000, the proceeds of which were used to refund Series 1991A and 1991B bonds on July 1, 2001. In addition, on March 19, 2002, Series 2002A bonds were issued in the amount of $39,000,000, the proceeds of which were used to refund the 1992A Series bonds on April 1, 2002.

Deferred loss on Housing Authority refundings at June 30, 2002, was $972,000.

Prior-year Defeasance of Debt

In prior years, Montana State University and the University of Montana defeased certain bond issues by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the financial statements. At June 30, 2002, $7.4 and $55.4 million of bonds outstanding are considered defeased for Montana State University and the University of Montana, respectively.

G. No-Commitment Debt

Information is presented below for financing authorities participating in debt issues. The State has no obligation for this debt. Accordingly, these bonds and notes are not reflected in the accompanying financial statements.

(1) Montana Board of Investments (BOI) – The BOI is authorized to issue industrial revenue bonds to finance projects for qualifying borrowers. Assets and revenues of the borrower are pledged to repay the bonds. The industrial revenue bonds issued by BOI do not constitute a debt, liability, obligation, or pledge of faith and credit of the State of Montana. At June 30, 2002, industrial revenue bonds outstanding aggregated $210.7 million.

(2) Facility Finance Authority (FFA) - Component Unit – The FFA is authorized to issue bonds and notes to finance projects for qualifying health care and other community-based service providers. The revenue bonds are payable solely from loan repayments to be made by eligible facilities pursuant to loan agreements, and further, from

the funds created by the indentures and investment earnings thereon. The notes are payable solely from loan repayments to be made by health institutions pursuant to loan agreements. The revenue bonds and notes payable issued by the FFA do not constitute a debt, liability, obligation, or pledge of faith and credit of the State of Montana. At June 30, 2002, revenue bonds outstanding aggregated $552.6 million, and notes payable outstanding aggregated $10.9 million.

The Board of Investments (BOI) and the FFA have entered into a capital reserve account agreement for certain bond issues. In accordance with the agreement, the BOI irrevocably committed to lend the FFA funds sufficient to insure timely payments of principal and interest on the bonds. If necessary, the loans will be made by the BOI from the Coal Severance Tax Permanent Trust Fund, a Trust Fund Bond Pool participant, or any other legally available funds administered by the BOI.

NOTE 12 — INTERFUND TRANSACTIONS

During the course of normal operations, the State has numerous transactions between funds to finance operations, provide services, construct assets, service debt, etc. Montana statutes include a provision for interfund loans when the expenditure of an appropriation is necessary and the cash balance in the account from which the appropriation was made is insufficient to pay the expenditure. To the extent that certain transactions between funds are not paid or received as of June 30, 2002, interfund receivables/payables (Due From/To Other Funds) are recorded. The schedule below presents all interfund balances outstanding at June 30, 2002, (in thousands) and interfund activity for the fiscal year then ended:

Within Primary Government	Interfund Loans/Advances		Due From Other Funds	Due To Other Funds	Operating Transfers	
	Receivable	Payable			In	Out
General	$ 81,067	$ -	$19,878	$ 3,304	$73,739	$33,651
Special Revenue						
State	54,681	88,396	12,638	6,362	122,004	89,367
Federal	541	76,159	1,349	4,113	8,054	53,210
Debt Service						
Coal Tax Bonds	1,698	1,771	-	3	14,505	441
Long-Range Building Program	-	-	-	11	14,419	-
Water Development	-	8,996	-	-	7,108	5,627
Highway Revenue Bonds	-	-	-	-	13,749	-
Health Care Debt Service	-	-	-	-	2,888	-
Information Technology Bonds	-	-	-	-	7,677	-
Energy Bonds	-	-	-	-	-	63
Capital Projects						
Long-Range Building Program	-	10	1,000	79	9,260	3,838
Information Technology Project	-	1,674	243	49	65	33
Fed./Private Construction Grants	-	-	-	-	285	-
Capital Land Grant	-	-	9	-	934	1,431
Permanent Funds						
Coal Severance Tax	46,368	-	3	5,907	219	43,120
Land Grant	-	-	6,835	15,198	46,451	54,387
Resource Indemnity Tax	-	-	-	1,230	-	7,321
Parks Trust	-	-	-	369	-	1,101
Cultural Trust	-	-	-	129	-	305
Real Property Trust	-	-	-	254	-	627
Noxious Weed Management	-	970	-	172	-	1,184
Thomas Teakle Trust	-	-	-	-	-	3
Tobacco Settlement Interest	-	-	-	122	5	1,020
Enterprise						
Unemployment Insurance	-	-	18	152	-	-
Economic Development Bonds	-	-	-	4	-	-
Liquor Warehouse	75	-	1	8,407	-	19,332
Hail Insurance	-	-	-	18	-	42
State Lottery	-	-	3	1,600	-	7,467
Prison Ranch	411	-	79	30	-	-
Prison Industries	-	111	129	24	2	-
Womens Prison Industries	-	-	-	-	-	2
MUS Group Insurance	-	-	-	1	-	-
Subsequent Injury	-	-	-	-	-	33

Within Primary Government	Interfund Loans/Advances		Due From Other Funds	Due To Other Funds	Operating Transfers	
	Receivable	Payable			In	Out
Montana Career Info. Systems	-	-	26	21	-	-
Sec. of State Business Services	190	-	4	47	-	-
Historical Soc. Publications	-	-	-	25	54	-
Surplus Property	-	275	23	19	-	-
West Yellowstone Airport	-	-	-	-	25	-
Judiciary Law Library	6	-	2	11	-	-
Local Govt. Audits	-	-	-	1	-	-
Advanced Drivers Education	-	-	11	14	24	-
FWP Visitor Services	-	-	4	-	15	-
Internal Service						
FWP Equipment	-	300	168	3	240	-
FWP Warehouse Inventory	-	-	4	-	-	-
FWP Office Supply	-	-	6	-	-	-
Highway Equipment	-	-	761	-	612	-
Employee Group Benefits	-	-	8	9	-	-
Information Services Division	40	-	2,254	117	-	-
Administration Insurance	-	4,700	-	123	1,150	436
Motor Pool	-	1,400	421	-	-	-
Administration Supply	275	-	155	4	-	-
Publications & Graphics	-	-	385	9	-	-
Buildings & Grounds	-	-	128	426	933	418
Labor Central Services	-	-	97	65	-	-
Commerce Central Services	-	-	122	20	-	18
OPI Central Services	-	-	217	81	-	-
DEQ Indirect Cost Pool	-	-	677	38	-	-
Mail & Messenger	-	-	308	1	-	-
Payroll Processing	-	-	1	4	-	-
Warrant Processing	-	-	45	44	-	-
Investment Division	-	-	28	54	-	-
Aircraft Operation	-	-	31	1	389	-
Justice Legal Services	-	100	183	4	10	10
Personnel Training	-	-	31	4	-	-
Records Management	-	190	28	7	-	-
Debt Collection/CSC	-	-	-	29	-	104
Statewide Fueling Network	-	-	-	1	-	-
Administration Central Services	-	-	-	3	18	-
MSP Food Factory	-	300	179	4	48	-
Pension (and Other Employee Benefit) Trust Funds						
Voluntary Emp Benefit Assoc.	-	-	-	1	-	-
Private Purpose Trust Funds						
Rural Development	-	-	-	1	-	-
Escheated Property	-	-	311	74	-	395
Total	$185,352	$185,352	$48,803	$48,803	$324,882	$324,986

In the fund financial statements, total transfers in of $324,882 are less than total transfers out of $324,986 because of the treatment of transfers of capital assets from the Debt Collection/CSC internal service fund. During the year, existing capital assets related to the internal service fund, with a book value of $104,000 were transferred to the General Fund. No amounts were reported in the governmental fund, as the transaction did not involve the transfer of financial resources. However, the internal service fund did report a transfer out for the capital resources provided.

NOTE 13 — FUND DEFICITS

The following funds have a deficit fund balance/net assets found on the operating statements for June 30, 2002, (in thousands):

	Deficit
Primary Government	
Governmental Activities	
Internal Service Funds	
Records Management	(94)
Administration Insurance	(33,303)
Justice - Legal	(2)
Business-Type Activities	
Enterprise Funds	
Subsequent Injury	(17)
Judiciary Law Library	(3)
Total Fund Deficits – Primary Government	$(33,419)
Fiduciary Funds	
Public Employee Defined Contribution Plan	$ (1,027)
Voluntary Employee Benefit Association	(28)
Total Fund Deficits – Fiduciary Funds	$ (1,055)

The net assets deficit in the Administration Insurance and Subsequent Injury funds are due to recording the expense for estimated claims including claims incurred, but not reported. Refer to Note 8 for further discussion of these funds. The deficit fund balance in the Public Employee Defined Contribution Plan is based on start-up costs. Member contributions will not be made until July 1, 2003.

NOTE 14 — RESERVED FUND BALANCES

Federal Special Revenue Fund – The reserve for Montana's Federal Family Education Loan Program is comprised of the following: $5,290,229 reserve for recalled funds under the Federal Balanced Budget Act of 1997, P.L. 105-33; and $6,772,062 reserve related to Federal Student Loan Reserve Fund activities.

Coal Tax Trust Permanent Fund – The reserve for trust principal is comprised of the following: Permanent Coal Tax Trust $528,092,626; Treasure State Endowment Fund $105,754,250; and the School Bond Contingency Loan Fund $2,177,964.

NOTE 15 — RELATED PARTY TRANSACTIONS

The Montana Board of Regents, an agency within the State, is the guarantor of the loans owned by the Montana Higher Education Student Assistance Corporation (MHESAC), a private non-profit corporation. The Board of Regents and MHESAC have four common board members. Approximately 54.02% of the Regents' outstanding loan volume, or $410,468,710, is held by MHESAC. During fiscal year 2000, MHESAC undertook a reorganization under which its operating staff and assets were transferred to the Student Assistance Foundation of Montana (SAF), and MHESAC entered into agreements with SAF to provide management and loan servicing to MHESAC. The Board of Regents and SAF have four common board members. Lewis & Clark County owns the building that houses the staff of the Board of Regents and the Office of the Commissioner of Higher Education (OCHE). Upon satisfaction of the financing obligations, SAF has the option to purchase the building. OCHE paid SAF during fiscal year 2002 for its share of various costs, such as personnel costs for employees of SAF who performed services that were of direct benefit to the State; equipment leases, computer maintenance costs, utilities, and other shared operating expenses. The total amount of these expenses for fiscal year 2002 amounted to $471,006. SAF employees are allowed to participate in the university system group insurance plan, and SAF also pays OCHE reimbursement for services such as telephones, postage, and computer services. During fiscal year 2002, SAF paid OCHE a total of $598,558.

There is a foundation affiliated with each university and college unit that solicits contributions and manages those funds for the benefit of that unit. Although each foundation is a separate legal entity, each unit exercises significant

influence over its affiliated foundation. The units generally provide the foundations with office space, some staff and related office expenses, and an annually contracted fee. The units paid their foundations approximately $1,882,004 in fiscal year 2002. In return the universities received from their foundations approximately $15,358,889 during fiscal year 2002 for scholarships and academic/institutional support. In addition to support from their affiliated foundations, the University of Montana-Missoula, University of Montana-Western, Montana State University-Billings, and Montana State University-Bozeman received a total of $4,037,749 from their related athletic associations/booster organizations and affiliated museums and public broadcasting radio stations.

The FWP Foundation is affiliated with the Department of Fish, Wildlife & Parks. Its purpose is to provide private support for the efforts of the department and to take a leading role in insuring the protection of Montana's natural, cultural, and recreational resources for future generations. In fiscal year 2002, the department provided $69,960 in support of the Foundation, and the Foundation provided $15,500 to the department.

The Department of Administration, Personnel Division, has a staff member that serves as Director of the Montana Association of Health Care Purchasers for no remuneration. The Department pays this Association $1,000 per year to maintain its membership

NOTE 16 — CONTINGENCIES

A. Litigation

The State is party to legal proceedings, which normally occur in government operations. The legal proceedings are not, in the opinion of the State's legal counsel and the Department of Administration, likely to have a material adverse impact on the State's financial position, except where listed below.

The State of Montana is involved in a lawsuit with the potential for substantial recovery of monetary relief against private parties. State of Montana v. Atlantic Richfield Co., No CV-83-317-H-PHG(D.Mont.), is a case where natural resource damage claims have been asserted under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, with respect to environmental injury to Clark Fork River Basin. The State and Atlantic Richfield settled a portion of the case for $215 million, but unresolved is a claim by the State for $180 million. Atlantic Richfield filed a counterclaim against the State, the amount of which is unspecified and therefore could reduce or exceed the State's remaining claim. The State believes it has meritorious defenses to the counterclaim. Any recovery in this litigation must be used under federal and state law to further reclamation and recovery efforts or to offset attorney fees and assessment costs incurred by the State.

In United States ex rel. Matthew J. Sisler vs. State of Montana et al., filed in the United States District Court, State of Montana, Missoula Division, Cause No. CV 99-125-M-DWM, plaintiffs allege that Department of Public Health and Human Services and its agent Healthy Mothers, Healthy Babies, a nonprofit corporation, fraudulently submitted monies to the federal government which were claimed as donations and as such eligible for federal matching funds. The complaint alleges that approximately $1 million was paid to the State of Montana during the time period at issue. It is further alleged that the federal government is entitled to treble damages plus civil penalties of $5,000 to $10,000 for each violation. The State believes the amount of loss in monetary terms may be closer to $300,000 rather than the higher claim asserted in the complaint.

In Travis D., et al. v. Eastmont Human Services Center, et al., filed in the United States District Court, District of Montana, Helena Division, Civil Action No. CV 96-63-H-CCL, plaintiffs allege that the State of Montana, in its operation of the Eastmont Human Services Center and the Montana Development Center, is not placing residents in the "least restrictive environment." In addition, plaintiffs' second amended complaint, dated November 2, 2001, expanded their claims to demand services for those Medicaid eligible recipients who are "at risk" of being institutionalized or on a "waiting list" for services but cannot be served due to limited funding provided by the Montana legislature for the "home and community services program" for the developmentally disabled. Their claims are based upon alleged violations of the Americans with Disabilities Act, Title XIX of the Social Security Act (Medicaid), and a constitutional equal protection and due process. The court has denied a motion for summary judgment filed by the defendants, who plan an appeal. The trial date of May 26, 2003, has been vacated. The State estimates the annual loss in monetary terms (based upon the amended complaint) at $25 million, of which $12.775 million would be federal funds and $12.225 million would be general fund.

B. Federal Contingencies

Federal Financial Assistance – The State receives federal financial assistance for specified purposes, which is subject to review and audit in accordance with the Single Audit Act Amendments of 1996. Any disallowances resulting from these audits would become the liability of the State. There are no disallowances reported as of June 30, 2002.

USDA Commodities – In fiscal year 2002, the State distributed $7,040,644 in commodities. The value of the commodities stored in the State's warehouses was $2,341,362 at June 30, 2002, for which the State is liable in the event of loss.

C. Miscellaneous Contingencies

Commitment Fees – The Board of Investments (BOI) and the Facility Finance Authority (FFA) have entered into a capital reserve account agreement for certain bond issues. In accordance with the agreement, the BOI irrevocably committed to lend the FFA funds sufficient to insure timely payments of principal and interest on the bonds. If necessary, the loans will be made by the BOI from the Coal Severance Tax Permanent Trust Fund. The total amount of these bonds outstanding as of June 30, 2002, was $36,883,151.

The BOI has issued INTERCAP bonds backed by commitments from the Coal Severance Tax Permanent Trust Fund. The total amount of these bonds outstanding as of June 30, 2002, was $60,335,799.

Gain Contingencies – Certain natural resource and corporation tax assessments are not reported on the State's financial statements because they are being protested administratively. As of June 30, 2002, the following assessments (by fund type) were outstanding (in thousands):

Taxes	General	State Special Revenue	Permanent Trust
Coal Severance	$ 4,235	$ -	$ -
Metal Mines	10	7	-
Oil & Gas	1,256	75	-
Resource Indemnity	-	63	63
Total	$5,501	$145	$63

Collectibility of these contingencies is dependent upon the decisions of the court, other authorities, or agreed upon settlements. Interest related to Corporation Tax Assessments is distributed to the General Fund.

Loss Contingencies – Certain corporations have requested refunds that are not reported on the State's financial statements as of June 30, 2002. After review, the State has denied these refund requests. The corporations have appealed the decision. As of June 30, 2002, these include $14,330,603 of General Fund corporation tax refunds.

NOTE 17 — SUBSEQUENT EVENTS

Bond Issues

In July 2002, the Montana Board of Housing issued $52.19 million of single-family mortgage bonds, 2002 Series B.

In July 2002, the Department of Environmental Quality issued $2.5 million of General Obligation State Hard Rock Mining Reclamation Bonds, Series 2002C.

In July 2002, the Department of Administration issued $10.475 million of General Obligation Long Range Building Program Bonds, Series 2002B.

In July 2002, the Board of Regents of the Montana University System authorized the issuance of Series G 2002 Revenue Bonds. The bonds were subsequently issued on October 7, 2002. The bond proceeds of approximately $18.5 million will be used for the purpose of constructing a student housing complex on the University of Montana – Missoula campus.

On October 16, 2002, the State of Montana issued $15.805 million of General Obligation Refunding Bonds, Series 2002D.

On October 17, 2002, the State of Montana issued $92.8 million in Tax and Revenue Anticipation Notes.

Board of Investments

Retirement Funds Bond Pool

The RFBP holds a $7 million par, 6.40% Enron bond maturing July 15, 2006, and a $7 million par, 6.95% Enron bond maturing July 15, 2028. The combined book value of these securities was $13,582,030 as of November 30, 2001. On

December 12, 2001, the Enron Corp. filed for Chapter 11 bankruptcy protection. Accordingly, the Board of Investments (BOI) reduced the book value for the two issues to $5.6 million as of June 30, 2002. In October 2002, the book value was reduced to $2.8 million for both issuers. BOI, currently, anticipates receiving up to $2.8 million from bankruptcy claims.

Deutsche Bank Securities, Inc. Complaint
The board received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $5 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002, sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $538,632 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs, and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. BOI tendered the Pennzoil Quaker State holdings on October 8, 2002, at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, BOI received $5,683,075 in principal and interest plus $150,000 as a consent fee.

The RFBP portfolio includes a $6,000,000 par, 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was $5,477,400 on June 30, 2002. On July 21, 2002, WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value is $2,400,000. At this time, BOI expects bankruptcy recovery up to $2,400,000. On November 7, 2002, the Attorney General for the State of Montana filed a lawsuit against certain WorldCom executives, directors, and financial institutions associated with WorldCom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the Montana Board of Investments.

Trust Funds Bond Pool
The TFBP holds a $2 million par, 6.75% Enron bond maturing August 1, 2009; a $3 million par, 6.40% Enron bond maturing July 15, 2006; and a $3 million par Enron bond maturing July 15, 2028. The combined book value of these securities was $7,560,870 as of November 30, 2001. On December 12, 2001, the Enron Corp. filed for Chapter 11 bankruptcy protection. Accordingly, we reduced the book value for the three issues to $3.2 million as of June 30, 2002. In October 2002, the book value was reduced to $1.6 million for the three issues. BOI, currently, anticipates receiving up to $1.6 million from bankruptcy claims.

Deutsche Bank Securities, Inc. Complaint
BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $8 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002, sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $861,811 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs, and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. BOI tendered the Pennzoil Quaker State holdings on October 8, 2002, at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, BOI received $9,092,920 in principal and interest plus $240,000 as a consent fee.

The TFBP portfolio includes a $9,000,000 par, 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was $8,216.100 on June 30, 2002. On July 21, 2002, WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value was $3,600,000. At this time, BOI expects bankruptcy recovery up to $3,600,000. On November 7, 2002, the Attorney General for the State of Montana files a lawsuit against certain WorldCom executives, directors, and financial institutions associated with WorldCom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the BOI.

Montana Stock Pool
Owens-Corning Complaint
BOI received a summons and complaint, dated October 11, 2002, regarding the bankruptcy of Owens-Corning. The company seeks a determination that the dividend payments paid from October 1996 through July 2000 represent "fraudulent transfers" under Chapter 11 Bankruptcy provisions and applicable state law and are, therefore, voidable. The complaint states that BOI was the "recipient of dividends in the amount of $357,099 for the relevant period".

All Other Funds
Deutsche Bank Securities, Inc. Complaint
BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $2 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002, sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $215,453,453 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs, and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State Debt. BOI tendered the Pennzoil Quaker State holdings on October 8, 2002, at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, BOI received $2,273,230 in principal and interest plus $60,000 as a consent fee.

STATE OF MONTANA
REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE
GENERAL AND MAJOR SPECIAL REVENUE FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(expressed in thousands)

	GENERAL FUND			
	ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET
REVENUES				
Licenses/permits	$ 109,265	$ 109,265	$ 115,808	$ 6,543
Taxes:				
Natural resource	26,186	26,186	24,700	(1,486)
Individual income	574,962	574,962	516,532	(58,430)
Corporate income	80,301	80,301	68,379	(11,922)
Property	173,754	173,754	166,786	(6,968)
Fuel	-	-	-	-
Other	190,873	190,873	151,781	(39,092)
Charges for services/fines/forfeits/settlements	43,461	43,461	50,556	7,095
Investment earnings	17,690	17,690	13,125	(4,565)
Sale of documents/merchandise/property	262	262	291	29
Rentals/leases/royalties	91	91	46	(45)
Contributions/premiums	-	-	12	12
Grants/contracts/donations	2,305	2,305	1,333	(972)
Federal	24,816	24,816	22,866	(1,950)
Federal indirect cost recoveries	100	100	87	(13)
Other revenues	354	354	195	(159)
Total revenues	1,244,420	1,244,420	1,132,497	(111,923)
EXPENDITURES				
Current:				
General government	159,645	160,070	155,599	4,471
Public safety/corrections	131,054	131,924	129,045	2,879
Transportation	177	182	172	10
Health/social services	270,653	276,043	275,280	763
Education/cultural	601,167	636,225	538,576	97,649
Resource development/recreation	26,844	30,298	29,962	336
Economic development/assistance	21,075	21,071	20,794	277
Debt service:				
Principal retirement	339	339	546	(207)
Interest/fiscal charges	59	59	59	-
Capital outlay	1,463	1,308	1,708	(400)
Total expenditures	1,212,476	1,257,519	1,151,741	105,778
Excess of revenue over (under) expenditures	31,944	(13,099)	(19,244)	(6,145)
OTHER FINANCING SOURCES (USES)				
Loan proceeds	-	-	-	-
Bond proceeds	303	303	-	(303)
Proceeds of refunding bonds	-	-	-	-
Discount on bonds/notes issued	-	-	-	-
Payment to refunded bond escrow agent	-	-	-	-
General fixed asset sale proceeds	41	41	82	41
Operating transfers in	64,939	64,939	72,499	7,560
Operating transfers out	(25,434)	(24,958)	(23,212)	1,746
Transfers to component units	(123,089)	(123,089)	(123,295)	(206)
Total other financing sources (uses)	(83,240)	(82,764)	(73,926)	8,838
Excess of revenues/other sources over (under) expenditures/other uses (Budgetary basis)	(51,296)	(95,863)	(93,170)	2,693
RECONCILIATION OF BUDGETARY/GAAP REPORTING				
1. Adjust expenditures for encumbrances	-	-	2,695	2,695
2. Adjustments for nonbudgeted activity	-	-	(9,350)	(9,350)
3. Intrafund elimination - revenues/transfers in	-	-	-	-
4. Intrafund elimination - expenditures/transfers out	-	-	-	-
5. Securities lending income	-	-	608	608
6. Securities lending costs	-	-	(531)	(531)
Excess of revenues/other sources over (under) expenditures/other uses (GAAP basis)	(51,296)	(95,863)	(99,748)	(3,885)
Unreserved fund balances - July 1	172,897	172,897	172,897	
Prior period adjustments	-	-	7,445	7,445
Decrease (increase):				
Encumbrances reserve	-	-	849	849
Advances to other funds reserve	-	-	(60)	(60)
Long-term loans reserve	-	-	(67)	(67)
Trusts/endowments/fed loans reserve	-	-	-	-
Unreserved fund balances - June 30	$ 121,601	$ 77,034	$ 81,316	$ 4,282

The notes to the required supplementary information are an integral part of this schedule.

STATE SPECIAL REVENUE FUND				FEDERAL SPECIAL REVENUE FUND			
ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET	ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET
$ 112,429	$ 112,429	$ 86,630	$ (25,799)	$ -	$ -	$ -	$ -
47,456	47,456	41,981	(5,475)	-	-	-	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
9,415	9,415	1,432	(7,983)	-	-	-	-
188,657	188,657	192,750	4,093	-	-	-	-
41,849	41,849	36,193	(5,656)	1	1	5	4
87,315	87,315	77,595	(9,720)	38,771	38,771	32,290	(6,481)
9,441	9,441	15,597	6,156	3,062	3,062	615	(2,447)
6,512	6,512	6,604	92	1	1	-	(1)
839	839	520	(319)	-	-	-	-
5,794	5,794	6,229	435	-	-	-	-
14,328	14,328	15,961	1,633	2,355	2,355	65	(2,290)
6,675	6,675	1,857	(4,818)	1,401,565	1,401,565	1,238,927	(162,638)
12	12	-	(12)	1,624	1,624	2,652	1,028
6,455	6,455	2,302	(4,153)	1,459	1,459	659	(800)
537,177	537,177	485,651	(51,526)	1,448,838	1,448,838	1,275,213	(173,625)
86,873	87,438	58,242	29,196	4,933	5,240	3,737	1,503
33,854	34,728	27,609	7,119	59,173	70,640	29,448	41,192
194,567	195,413	157,402	38,011	316,027	328,676	284,799	43,877
101,616	103,740	68,525	35,215	759,505	781,655	681,171	100,484
53,974	54,159	50,804	3,355	149,669	153,602	132,641	20,961
169,747	102,523	60,932	41,591	26,410	41,513	20,531	20,982
60,194	65,367	45,611	19,756	117,488	129,824	93,093	36,731
1,880	64,725	1,151	63,574	281	266	182	84
561	12,840	3,955	8,885	31	30	20	10
9,548	7,161	20,492	(13,331)	1,183	2,218	11,858	(9,640)
712,814	728,094	494,723	233,371	1,434,700	1,513,664	1,257,480	256,184
(175,637)	(190,917)	(9,072)	181,845	14,138	(64,826)	17,733	82,559
1,749	1,749	279	(1,470)	70	70	-	(70)
2,016	2,016	1,184	(832)	-	-	-	-
34,873	34,873	33,605	(1,268)	-	-	-	-
-	-	(139)	(139)	-	-	-	-
-	-	(21,037)	(21,037)	-	-	-	-
217	217	252	35	-	-	-	-
83,849	83,849	37,320	(46,529)	36,692	36,692	(27,753)	(64,445)
(15,377)	(15,693)	74,277	89,970	(69,761)	(66,726)	4,562	71,288
(13,920)	(13,920)	(13,920)	-	(500)	(500)	(500)	-
93,407	93,091	111,821	18,730	(33,499)	(30,464)	(23,691)	6,773
(82,230)	(97,826)	102,749	200,575	(19,361)	(95,290)	(5,958)	89,332
-	-	(5,731)	(5,731)	-	-	889	889
-	-	(68,841)	(68,841)	-	-	2,132	2,132
-	-	(481)	(481)	-	-	(1,075)	(1,075)
-	-	481	481	-	-	1,075	1,075
-	-	888	888	-	-	7	7
-	-	(778)	(778)	-	-	(6)	(6)
(82,230)	(97,826)	28,287	126,113	(19,361)	(95,290)	(2,936)	92,354
425,608	425,608	425,815	207	9,967	9,967	9,967	-
-	-	4,566	4,566	-	-	(6,408)	(6,408)
-	-	3,186	3,186	-	-	2,475	2,475
		(10,082)	(10,082)	-	-	-	-
-	-	(12,300)	(12,300)	-	-	128	128
-	-	-	-	-	-	(5,510)	(5,510)
$ 343,378	$ 327,782	$ 439,472	$ 111,690	$ (9,394)	$ (85,323)	$ (2,284)	$ 83,039

State of Montana
NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
For the Fiscal Year Ended June 30, 2002

NOTE RSI-1— BUDGETARY REPORTING

A. State Budget Process

The Montana Legislature meets in the odd-numbered years to prepare annual budgets for the next biennium. The constitution requires that legislative appropriations not exceed available revenues. The legislature utilizes revenue estimates in the budgetary process to establish appropriation levels. Expenditures may not legally exceed budgeted appropriations at the fund level. In addition, the State Constitution prohibits borrowing to cover deficits incurred because appropriations exceeded anticipated revenues. State law requires an appropriation for disbursements from the general, special revenue and capital projects funds, except for those special revenue funds from non-state and non-federal sources restricted by law or by the terms of an agreement. The level of budgetary control is established by fund type, except capital project funds, which are at project level. Budgets may be established in other funds for administrative purposes.

Agency budget requests are submitted to the Governor and the Legislative Fiscal Division. The Governor and budget director establish priorities and the proposed budget. The Governor's budget is submitted to the Legislative Fiscal Division which prepares recommendations. A comparison of those recommendations with the Governor's budget is submitted to the legislature. Joint appropriations subcommittee hearings are held and an omnibus appropriation bill is reported in the House and subsequently sent to the Senate. The legislature generally enacts one bill to establish the majority of appropriations for the next two fiscal years. The Office of Budget and Program Planning establishes appropriations for each program by accounting entity (fund) within an agency. The legislature enacts other appropriations, but only within the available revenue. Agencies must prepare and submit to the budget director operational plans showing the allocation of operating budgets by expenditure category (i.e., personal services, operating expenses, equipment, etc.). The budget director or other statutorily designated approving authority may authorize changes among expenditure categories and transfers between program appropriations.

Appropriations may not be increased by amendment in the General Fund. However, a department, institution, or agency of the executive branch desiring authorization to make expenditures from the General Fund during the first fiscal year of the biennium from appropriations for the second fiscal year of the biennium may apply for authorization from the Governor through the budget director. In the second year of the biennium, during the legislative session, the legislature may authorize supplemental appropriations. The Governor, or designee, may approve budget amendments for non-general fund monies not available for consideration by the legislature and for emergencies. In the accompanying financial schedule, original and final budget amounts are reported. There have been budget amendments authorized for fiscal year 2002 that were material to specific budgets; however, they did not materially affect the State's budget as a whole. There were no expenditures in excess of total authorized appropriations in the State's budgeted funds for the fiscal year.

Appropriations may be continued into the next fiscal year when authorized by the legislature or the Governor's office. After fiscal year-end, appropriations that are not continued are reverted. The reverted appropriations remain available for one fiscal year for expenditures that exceed the amount accrued/encumbered. Fund balances/net assets are not reserved for reverted appropriations. For fiscal year 2002, reverted appropriations were as follows: General Fund - $6.1 million, State Special Revenue Fund - $40.6 million, and Federal Special Revenue Fund - $107.6 million. Agencies are allowed to carry forward 30% of their reverted operating appropriations into the next two fiscal years. This amount can be used for new expenditures at the request of the agency and upon approval of the budget office.

Appropriations for capital projects funds are not made on an annual basis, but are adopted on a project-length basis. Because these non-operating budgets primarily serve a management control purpose, and related appropriations are continuing in nature, no comparison between budgeted and actual amounts for funds budgeted on this basis is provided.

B. Budget Basis

The legislature's legal authorization ("appropriations") to incur obligations is enacted on a basis inconsistent with GAAP. The budget basis differs from GAAP for encumbrances outstanding at fiscal year-end; compensated absences, fixed assets and inventories purchased in proprietary funds; certain loans from governmental funds; and other miscellaneous nonbudgeted activity (e.g., bad-debt write-offs, etc.).