APPENDIX A

THE

COMMONWEALTH

OF

MASSACHUSETTS

INFORMATION STATEMENT

Dated May 9, 2007

TABLE OF CONTENTS

THE COMMONWEALTH OF MASSACHUSETTS

CONSTITUTIONAL OFFICERS

Deval L. Patrick	**Governor**
Timothy P. Murray	**Lieutenant Governor**
William F. Galvin	**Secretary of the Commonwealth**
Martha Coakley	**Attorney General**
Timothy P. Cahill	**Treasurer and Receiver-General**
A. Joseph DeNucci	**Auditor**

LEGISLATIVE OFFICERS

Therese Murray	**President of the Senate**
Salvatore F. DiMasi	**Speaker of the House**

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THE COMMONWEALTH OF MASSACHUSETTS

INFORMATION STATEMENT

May 9, 2007

This Information Statement, together with its Exhibits (included by reference as described below), is furnished by The Commonwealth of Massachusetts (the Commonwealth). It contains certain fiscal, financial and economic information concerning the Commonwealth and its ability to meet its obligations. This Information Statement contains information only through its date and should be read in its entirety.

The ability of the Commonwealth to meet its obligations will be affected by future social, environmental and economic conditions, among other things, as well as by legislative policies and the financial condition of the Commonwealth. Many of these conditions are not within the control of the Commonwealth.

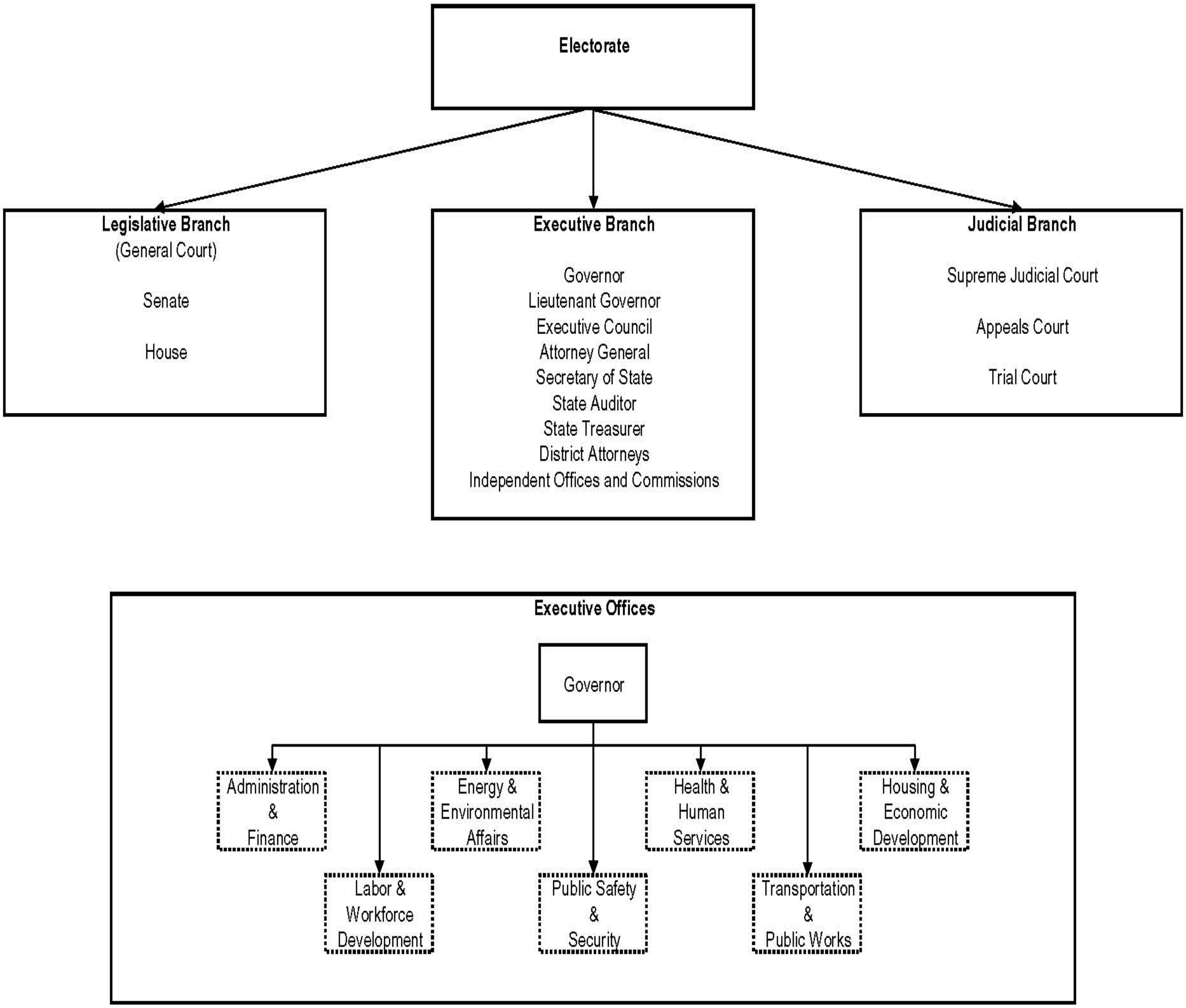
Exhibit A to this Information Statement is the Statement of Economic Information as of December 31, 2006. Exhibit A sets forth certain economic, demographic and statistical information concerning the Commonwealth.

Exhibits B and C, respectively, are the Commonwealth's Statutory Basis Financial Report for the year ended June 30, 2006 and the Commonwealth's Comprehensive Annual Financial Report, reported in accordance with generally accepted accounting principles (GAAP), for the year ended June 30, 2006. The Commonwealth's independent auditor has not been engaged to perform, and has not performed, since the respective dates of its reports included herein, any procedures on the financial statements addressed in such reports, nor has said independent auditor performed any procedures relating to the official statement of which this Information Statement is a part.

Specific reference is made to said Exhibits B and C, copies of which have been filed with each Nationally Recognized Municipal Securities Information Repository (NRMSIR) currently recognized by the Securities and Exchange Commission (SEC). The financial statements are also available at the home page of the Comptroller of the Commonwealth located at http://www.mass.gov/osc by clicking on "Financial Reports/Audits."

THE GOVERNMENT

The government of the Commonwealth is divided into three branches: the Executive, the bicameral Legislature and the Judiciary, as indicated by the chart below.



Executive Branch

Governor. The Governor is the chief executive officer of the Commonwealth. Other elected members of the executive branch are the Lieutenant Governor (elected with the Governor), the Treasurer and Receiver-General (State Treasurer), the Secretary of the Commonwealth (State Secretary), the Attorney General and the State Auditor. All are elected to four-year terms. The terms of the current office holders began in January, 2007.

The Executive Council, also referred to as the “Governor’s Council,” consists of eight members who are elected to two-year terms in even-numbered years. The Executive Council is responsible for the confirmation of certain gubernatorial appointments, particularly judges, and must approve all warrants (other than for debt service) prepared by the Comptroller for payment by the State Treasurer.

Also within the Executive Branch are certain independent offices, each of which performs a defined function, such as the Office of the Comptroller, the Board of Library Commissioners, the Office of the Inspector General, the State Ethics Commission and the Office of Campaign and Political Finance.

Governor’s Cabinet. The Governor’s Cabinet, which assists the Governor in administration and policy making, is comprised of the secretaries who head the seven Executive Offices, which are the Executive Office for Administration and Finance, the Executive Office of Health and Human Services, the Executive Office of Transportation and Public Works, the Executive Office of Public Safety and Security, the Executive Office of Housing and Economic Development, the Executive Office of Labor and Workforce Development and the Executive Office of Energy and Environmental Affairs. Finally, the Governor chairs an informal Development Cabinet to coordinate business development in the Commonwealth; it includes the Secretaries of Administration and Finance, Housing and Economic Development, Transportation and Public Works, Energy and Environmental Affairs, and Labor and Workforce Development. Cabinet secretaries and executive department chiefs serve at the pleasure of the Governor. Most other agencies are grouped under one of the seven Executive Offices for administrative purposes.

The Cabinet structure described above results from a constitutionally provided reorganization plan proposed by the Governor and approved unanimously by the legislature, which took effect on April 9, 2007.

The Governor’s chief fiscal officer is the Secretary of Administration and Finance. The activities of the Executive Office for Administration and Finance fall within five broad categories: (i) administrative and fiscal supervision, including supervision of the implementation of the Commonwealth’s budget and monitoring of all agency expenditures during the fiscal year; (ii) enforcement of the Commonwealth’s tax laws and collection of tax revenues through the Department of Revenue for remittance to the State Treasurer; (iii) human resource management, including administration of the state personnel system, civil service system and employee benefit programs and negotiation of collective bargaining agreements with certain of the Commonwealth’s public employee unions; (iv) capital facilities management, including coordinating and overseeing the construction, management and leasing of all state facilities; and (v) administration of general services, including information technology services.

State Treasurer. The State Treasurer has four primary statutory responsibilities: (i) the collection of all state revenues (other than small amounts of funds held by certain agencies); (ii) the management of both short-term and long-term investments of Commonwealth funds (other than the state employee and teacher pension funds), including all cash receipts; (iii) the disbursement of Commonwealth monies and oversight of reconciliation of the state’s accounts; and (iv) the issuance of almost all debt obligations of the Commonwealth, including notes, commercial paper and long-term bonds.

In addition to these responsibilities, the State Treasurer serves as Chairperson of the Massachusetts Lottery Commission, the State Board of Retirement, the Pension Reserves Investment Management Board, the Massachusetts Water Pollution Abatement Trust and the Massachusetts School Building Authority. The State Treasurer also serves as a member of numerous other state boards and commissions, including the Municipal Finance Oversight Board.

State Auditor. The State Auditor is charged with improving the efficiency of state government by auditing the administration and expenditure of public funds and reporting the findings to the public. The State Auditor reviews the activities and operations of approximately 750 state entities and contract compliance of private vendors doing business with the Commonwealth. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS."

Attorney General. The Attorney General represents the Commonwealth in all legal proceedings in both the state and federal courts, including defending the Commonwealth in actions in which a state law or executive action is challenged. The Attorney General also brings actions to enforce environmental and consumer protection statutes, among others, and represents the Commonwealth in public utility and automobile and health insurance rate setting procedures. The Attorney General works in conjunction with the general counsel of the various state agencies and executive departments to coordinate and monitor all pending litigation.

State Comptroller. Accounting policies and practices, publication of official financial reports and oversight of fiscal management functions are the responsibility of the Comptroller. The Comptroller also administers the Commonwealth's annual state single audit and manages the state accounting system. The Comptroller is appointed by the Governor for a term coterminous with the Governor's and may be removed by the Governor only for cause. The annual financial reports of the Commonwealth, single audit reports and any rules and regulations promulgated by the Comptroller must be reviewed by an advisory board. This board is chaired by the Secretary of Administration and Finance and includes the State Treasurer, the Attorney General, the State Auditor, the Chief Administrative Justice of the Trial Court and two persons with relevant experience appointed by the Governor for three-year terms. The Commonwealth's audited annual reports include audited financial statements on both the statutory basis of accounting (the Statutory Basis Financial Report, or SBFR) and the GAAP basis (the Comprehensive Annual Financial Report, or CAFR). The Commonwealth has hired the independent public accounting firm of KPMG LLP to audit the Commonwealth's financial statements and to conduct the state single audit for the year ending June 30, 2007. The Statutory Basis Financial Report for the year ended June 30, 2006, included herein by reference as Exhibit B, and the Comprehensive Annual Financial Report for the year ended June 30, 2006, included herein by reference as Exhibit C, were audited by Deloitte & Touche LLP, as stated in its reports appearing therein. Deloitte & Touche LLP has not been engaged to perform, and has not performed, since the respective dates of its reports included herein, any procedures on the financial statements addressed in such reports, nor has it performed any procedures relating to the official statement of which this Information Statement is a part. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS."

State Secretary. The Secretary of the Commonwealth is responsible for collection and storage of public records and archives, securities regulation, state elections, administration of state lobbying laws and custody of the seal of the Commonwealth.

Legislative Branch

The Legislature (formally called the General Court) is the bicameral legislative body of the Commonwealth, consisting of a Senate of 40 members and a House of Representatives of 160 members. Members of both the Senate and the House are elected to two-year terms in even-numbered years. The Legislature meets every year. The joint rules of the House and Senate require all formal business to be concluded by the end of July in even-numbered years and by the third Wednesday in November in odd-numbered years.

The House of Representatives must originate any bill that imposes a tax. Once a tax bill is originated by the House and forwarded to the Senate for consideration, the Senate may amend it. All bills are presented to the Governor for approval or veto. The Legislature may override the Governor's veto of any bill by a two-thirds vote of each house. The Governor also has the power to return a bill to the chamber of the Legislature in which it was originated with a recommendation that certain amendments be made; such a bill is then before the Legislature and is subject to amendment or re-enactment, at which point the Governor has no further right to return the bill a second time with a recommendation to amend but may still veto the bill.

Judicial Branch

The judicial branch of state government is composed of the Supreme Judicial Court, the Appeals Court and the Trial Court. The Supreme Judicial Court has original jurisdiction over certain cases and hears appeals from both the Appeals Court, which is an intermediate appellate court, and in some cases, directly from the Trial Court. The Supreme Judicial Court is authorized to render advisory opinions on certain questions of law to the Governor, the Legislature and the Governor's Council. Judges of the Supreme Judicial Court, the Appeals Court and the Trial Court are appointed by the Governor, with the advice and consent of the Governor's Council, to serve until the mandatory retirement age of 70 years.

Independent Authorities and Agencies

The Legislature has established a number of independent authorities and agencies within the Commonwealth, the budgets of which are not included in the Commonwealth's annual budget. The Governmental Accounting Standards Board (GASB) Statement 14 articulates standards for determining significant financial or operational relationships between the primary government and its independent entities. In fiscal 2006, the Commonwealth had significant operational or financial relationships, or both, as defined by GASB Statement 14 (as amended), with 34 of these authorities. A discussion of these entities and the relationship to the Commonwealth is included in footnote 1 to the fiscal 2006 general-purpose financial statements in the CAFR, included herein by reference as Exhibit C.

Local Government

All territory in the Commonwealth is in one of the 351 incorporated cities and towns that exercise the functions of local government, which include public safety, fire protection and public construction. Cities and towns or regional school districts established by them also provide elementary and secondary education. Cities are governed by several variations of the mayor-and-council or manager-and-council form. Most towns place executive power in a board of three or five selectmen elected to one- or three-year terms and retain legislative powers in the voters themselves, who assemble in periodic open or representative town meetings. Various local and regional districts exist for schools, water and wastewater administration and certain other governmental functions.

Municipal revenues consist of taxes on real and personal property, distributions from the Commonwealth under a variety of programs and formulas, local receipts (including motor vehicle excise taxes, local option taxes, fines, licenses and permits, charges for utility and other services and investment income) and appropriations from other available funds (including general and dedicated reserve funds). Because property tax levies are limited by Proposition 2½, an initiative petition approved by the voters in 1980, local governments have become increasingly reliant on distribution of revenues from the Commonwealth to support local programs and services, although the amount of aid received varies significantly among municipalities. See "COMMONWEALTH PROGRAMS AND SERVICES – Local Aid."

The cities and towns of the Commonwealth are also organized into 14 counties, but county government has been abolished in seven of those counties. The county governments that remain are responsible principally for the operation of correctional facilities, courthouses and registries of deeds. Where county government has been abolished, the functions, duties and responsibilities of the government have been transferred to the Commonwealth, including all employees, assets, valid liabilities and debts.

Initiative Petitions

Under the Massachusetts constitution, legislation may be enacted in the Commonwealth pursuant to a voter initiative process. Initiative petitions which have been certified by the Attorney General as to proper form and as to which the requisite number of voter signatures has been collected are submitted to the Legislature for consideration. If the Legislature fails to enact the measure into law as submitted, the petitioner may place the initiative on the ballot for the next statewide general election by collecting additional voter signatures. If approved by a majority of the voters at the general election, the petition becomes law 30 days after the date of the election. Initiative petitions so approved by the voters do not constitute constitutional amendments and may be subsequently amended or repealed by the Legislature. Initiative petitions may not make appropriations. In recent years, ballots at statewide general elections typically have presented a variety of initiative petitions, sometimes including petitions relating to tax and fiscal policy. A number of these have been approved and become law. See particularly "COMMONWEALTH REVENUES – Limitations on Tax Revenues" and "COMMONWEALTH PROGRAMS AND SERVICES – Local Aid."

Constitutional amendments also may be initiated by citizens, but they follow a longer adoption process, which includes gaining at least 25% of the votes of the House of Representatives and Senate jointly assembled in constitutional convention in two successive biennial legislative sessions before being decided by the voters.

COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS

Operating Fund Structure

The Commonwealth's operating fund structure satisfies the requirements of state finance law and is in accordance with generally accepted accounting principles (GAAP), as defined by the Government Accounting Standards Board (GASB). The General Fund and other funds that are appropriated in the annual state budget receive most of the non-bond and non-federal grant revenues of the Commonwealth. These funds are referred to in this Information Statement as the "budgeted operating funds" of the Commonwealth. Budgeted operating funds are created and repealed from time to time through the enactment of legislation, and existing funds may become inactive when no appropriations are made from them. Budgeted operating funds do not include the capital projects funds of the Commonwealth, into which the proceeds of Commonwealth bonds are deposited. See "Capital Investment Process and Controls" below.

Two of the budgeted operating funds account for most of the Commonwealth's appropriated spending: the General Fund and the Highway Fund, from which approximately 97.1% of the statutory basis budgeted operating fund expenditures in fiscal 2006 were made. The remaining approximately 2.9% of statutory operating fund expenditures occurred in other operating funds: the Commonwealth Stabilization Fund; the Workforce Training Fund; the Massachusetts Tourism Fund; the Children's and Seniors' Health Care Assistance Fund (which closed at the end of fiscal 2006); the Inland Fisheries and Game Fund; and three administrative control funds, including the Temporary Holding Fund, the Intragovernmental Service Fund, and the Transitional Escrow Fund. There were also three inactive funds which were authorized by law but had no activity: the Division of Energy Resources Credit Trust Fund; the Tax Reduction Fund; and the collective Bargaining Reserve Fund. The FMAP Escrow Fund, created in fiscal 2004 to hold and allow expenditure of one-time funds provided by the federal government to the states for one-time fiscal relief, expired as of the close of fiscal 2005. The Transitional Escrow Fund, created to account for undesignated fund balances in budgeted funds at the close of fiscal 2005 and carry them forward into fiscal 2006, expired on June 30, 2006.

At the end of a fiscal year, undesignated balances in the budgeted operating funds, unless excluded by law, are used to calculate consolidated net surplus. Under state finance law, balances in the Stabilization Fund and the Tax Reduction Fund, both of which may receive consolidated net surplus funds, and in the Inland Fisheries and Game Fund are excluded from the consolidated net surplus calculation. The balance in the Transitional Escrow Fund was not included in consolidated net surplus at the end of fiscal 2005, since it was established with surplus funds that remained after a number of mandated transfers to carry that money forward from fiscal 2005 to be available for expenditure in fiscal 2006. See "SELECTED FINANCIAL DATA — Stabilization Fund and Disposition of Year-End Surpluses."

Overview of Operating Budget Process

Generally, funds for the Commonwealth's programs and services must be appropriated by the Legislature. The process of preparing a budget begins with the executive branch early in the fiscal year preceding the fiscal year for which the budget will take effect. The legislative budgetary process begins in late January (or, in the case of a newly elected Governor, not later than early March) with the Governor's budget submission to the Legislature for the fiscal year commencing in the ensuing July. The Massachusetts constitution requires that the Governor recommend to the Legislature a budget which contains a statement of all proposed expenditures of the Commonwealth for the upcoming fiscal year, including those already authorized by law, and of all taxes, revenues, loans and other means by which such expenditures are to be defrayed. State finance law requires the Legislature and the Governor to approve a balanced budget for each fiscal year, and the Governor may approve no supplementary appropriation bills that would result in an unbalanced budget. However, this is a statutory requirement that may be superseded by an appropriation act.

The House Ways and Means Committee considers the Governor's budget recommendations and, with revisions, proposes a budget to the full House of Representatives. Once approved by the House, the budget is considered by the Senate Ways and Means Committee, which in turn proposes a budget to be considered by the full Senate. In recent years, the legislative budget review process has included joint hearings by the Ways and Means Committees of the Senate and the House. After Senate action, a legislative conference committee develops a joint budget recommendation for consideration by both houses of the Legislature, which upon adoption is sent to the Governor. Under the Massachusetts constitution, the Governor may veto the budget in whole or disapprove or reduce specific line items (line item veto). The Legislature may override the Governor's veto or specific line-item vetoes by a two-thirds vote of both the House and Senate. The annual budget legislation, as finally enacted, is known as the general appropriations act.

In years in which the general appropriations act is not approved by the Legislature and the Governor before the beginning of the applicable fiscal year, the Legislature and the Governor generally approve a temporary budget under which funds for the Commonwealth's programs and services are appropriated based upon the level of appropriations from the prior fiscal year budget.

State finance law requires the Commonwealth to monitor revenues and expenditures during a fiscal year. For example, the Secretary of Administration and Finance is required to provide quarterly revenue estimates to the Governor and the Legislature, and the Comptroller publishes a quarterly report of planned and actual revenues. See "COMMONWEALTH REVENUES – Tax Revenue Forecasting." Department heads are required to notify the Secretary of Administration and Finance and the House and Senate Committees on Ways and Means of any anticipated decrease in estimated revenues for their departments from the federal government or other sources or if it appears that any appropriation will be insufficient to meet all expenditures required in the fiscal year by any law, rule, regulation or order not subject to the administrative control. The Secretary of Administration and Finance must notify the Governor and the House and Senate Committees on Ways and Means whenever the Secretary determines that revenues will be insufficient to meet authorized expenditures. The Secretary of Administration and Finance is then required to compute projected deficiencies and, under Section 9C of Chapter 29 of the General Laws, the Governor is required to reduce allotments, to the extent lawfully permitted to do so, or submit proposals to the Legislature to raise additional revenues or to make appropriations from the Stabilization Fund to cover such deficiencies. The Supreme Judicial Court has ruled that the Governor's authority to reduce allotments of appropriated funds extends only to appropriations of funds to state agencies under the Governor's control.

Cash and Budgetary Controls

The Commonwealth has in place controls designed to ensure that sufficient cash is available to meet the Commonwealth's obligations, that state expenditures are consistent with periodic allotments of annual appropriations and that monies are expended consistently with statutory and public purposes. Two independently elected Executive Branch officials, the State Treasurer and the State Auditor, conduct the cash management and audit functions, respectively. The Comptroller conducts the expenditure control function. The Secretary of Administration and Finance is the Governor's chief fiscal officer and provides overall coordination of fiscal activities.

Capital Investment Process and Controls

Capital expenditures are primarily financed with debt proceeds, federal reimbursements, payments from third parties and transfers from other governmental funds. Authorization for capital investments requires approval by the Legislature, and the issuance of debt must be approved by a two-thirds vote of each house of the Legislature. Upon such approval to issue debt, the Governor submits a bill to the Legislature, as required by the state constitution, to set the terms and conditions of the borrowing for the authorized debt. The Governor, through the Secretary of Administration and Finance, controls the amount of capital expenditures through the allotment of funds in support of such authorizations, and therefore controls the amount of debt issued to finance such expenditures.

Based on outstanding authorizations, the Executive Office for Administration and Finance, at the direction of the Governor and in conjunction with the cabinet and other officials, establishes a capital investment plan. The plan is an administrative guideline and subject to amendment at any time. The plan assigns authority for secretariats and agencies to spend on capital projects and is reviewed each fiscal year. The primary policy objectives of the plan are to determine and prioritize the Commonwealth's investment needs, to determine the affordable level of debt that may be issued and the other funding sources available to address these investment needs, and to allocate these limited capital investment resources among the highest priority projects. See "COMMONWEALTH CAPITAL ASSET INVESTMENT PLAN."

The Comptroller has established various funds to account for financial activity related to the acquisition or construction of capital assets. In addition, accounting procedures and financial controls have been instituted to limit agency capital spending to the levels approved by the Governor. All agency capital spending is tracked against the capital investment plan on both a cash and encumbrance accounting basis on the state's accounting system, and federal reimbursements are budgeted and monitored against anticipated receipts.

Cash Management Practices of State Treasurer

The State Treasurer is responsible for ensuring that all Commonwealth financial obligations are met on a timely basis. The Massachusetts constitution requires that all payments by the Commonwealth (other than debt service) be made pursuant to a warrant approved by the Governor's Council. The Comptroller prepares certificates which, with the advice and consent of the Governor's Council and approval of the Governor, become the warrant to the State Treasurer. Once the warrant is approved, the State Treasurer's office disburses the money.

The Cash Management Division of the State Treasurer's office accounts on a daily basis for cash received into over 600 separate accounts of the Department of Revenue and other Commonwealth agencies and departments. The Division relies primarily upon electronic receipt and disbursement systems.

The State Treasurer is required to submit quarterly cash flow projections for the then current fiscal year to the House and Senate Committees on Ways and Means on or before each September 1, December 1, March 1 and June 1. The projections must include estimated sources and uses of cash, together with the assumptions from which such estimates were derived and identification of any cash flow gaps. See "FISCAL 2007 AND FISCAL 2008 – Cash Flow." The State Treasurer's office also oversees the Commonwealth's commercial paper program. See "LONG-TERM LIABILITIES – General Obligation Debt." The State Treasurer's office, in conjunction with the Executive Office for Administration and Finance, is also required to develop quarterly and annual cash management plans to address any gap identified by the cash flow projections and variance reports.

Fiscal Control, Accounting and Reporting Practices of Comptroller

The Comptroller is responsible for oversight of fiscal management functions, establishment of accounting policies and practices and publication of official financial reports. The Comptroller maintains the Massachusetts Management Accounting and Reporting System (MMARS), the centralized state accounting system that is used by all state agencies and departments but not independent state authorities. MMARS provides a ledger-based system of revenue and expenditure accounts enabling the Comptroller to control obligations and expenditures effectively and to ensure that appropriations are not exceeded during the course of the fiscal year. The Commonwealth's statewide accounting system also has various modules for receivables, payables, fixed assets and other processes management.

Expenditure Controls. The Comptroller requires that the amount of all obligations under purchase orders, contracts and other commitments for the expenditures of monies be recorded as encumbrances. Once encumbered, these amounts are not available to support additional spending commitments. As a result of these encumbrances, spending agencies can use MMARS to determine at any given time the amount of their appropriations available for future commitments.

The Comptroller is responsible for compiling expenditure requests into the certificates for approval by the Governor's Council. In preparing these certificates, which become the warrant, the Comptroller's office has systems in place to ensure that the necessary monies for payment have been both appropriated by the Legislature and allotted by the Governor in each account and sub-account. By law, certain obligations may be placed upon the warrant even if the supporting appropriation or allotment is insufficient. These obligations include debt service, which is specifically exempted by the state constitution from the warrant requirement, and Medicaid payments, which are mandated by federal law.

Although state finance law generally does not create priorities among types of payments to be made by the Commonwealth in the event of a cash shortfall, the Comptroller has developed procedures, in consultation with the State Treasurer and the Executive Office for Administration and Finance, for prioritizing payments based upon state finance law and sound fiscal management practices. Under those procedures, debt service on the Commonwealth's bonds and notes is given the highest priority among the Commonwealth's various payment obligations.

Internal Controls. The Comptroller establishes internal control policies and procedures in accordance with state finance law. Agencies are required to adhere to such policies and procedures. All unaccounted-for variances, losses, shortages or thefts of funds or property must be reported to the State Auditor, who is authorized to investigate and recommend corrective action.

Statutory Basis of Accounting. In accordance with state law, the Commonwealth adopts its budget and maintains financial information on a statutory basis of accounting. Under the statutory basis, tax and departmental revenues are accounted for on a modified cash basis by reconciling revenue to actual cash receipts confirmed by the State Treasurer. Certain limited revenue accruals are also recognized, including receivables from federal reimbursements with respect to paid expenditures. Expenditures are measured on a modified cash basis including actual cash disbursements and encumbrances for goods or services received prior to the end of a fiscal year.

For certain programs, such as Medicaid, expenditures are recognized under the statutory basis of accounting only to the extent of disbursements supported by current-year appropriations. Some prior year services billed after the start of a fiscal year have been paid from the new fiscal year's appropriation, in an amount determined by the specific timing of billings and the amount of prior year funds that remained after June 30 to pay the prior year's accrued billings, though this practice may vary from year to year.

GAAP Basis of Accounting. The Comptroller also prepares Commonwealth financial statements on a GAAP basis. The primary emphasis is to demonstrate inter-period equity through the use of modified accrual accounting and full accrual accounting for the recognition of revenues and expenditures or expenses. In addition to the primary government, certain independent authorities and agencies of the Commonwealth are included as component units within the Commonwealth's reporting entity, primarily as non-budgeted enterprise funds.

GAAP employs an economic resources management focus and a current financial resources management focus as two bases for accounting and reporting. Under the economic resources management focus (also called the "entity-wide perspective"), revenues and expenses (different from expenditures) are presented similarly to private-sector entities. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met. Capital assets, including infrastructure assets net of depreciation, and the long-term portion of all liabilities are reported on the statement of net assets.

Under the current financial resources management focus of GAAP (also called the "fund perspective"), revenues are reported in the period in which they become both measurable and available. Revenues are considered available when they are expected to be collected within the current period or soon enough thereafter to be used to pay liabilities of the current period.

Significant revenues susceptible to accrual include income, sales and use, corporation and other taxes, federal grants and reimbursements and reimbursements for the use of materials and services. Tax accruals, which include the estimated amounts due to the Commonwealth on previous filings, over- and under-withholdings, estimated payments on income earned and tax refunds and abatements payable, are all recorded as adjustments to statutory basis tax revenues.

Major expenditure accruals are recorded for the cost of Medicaid claims that have been incurred but not paid, claims and judgments and workers' compensation claims incurred but not reported. See Exhibit C (Comprehensive Annual Financial Report for the year ended June 30, 2006, Notes to the Basic Financial Statements).

Audit Practices of State Auditor

The State Auditor is mandated under state law to conduct an audit at least once every two years of all activities of the Commonwealth. The audit encompasses 750 entities, including the court system and the independent authorities, and includes an overall evaluation of management operations. The State Auditor also has the authority to audit federally aided programs and vendors under contract with the Commonwealth, as well as to conduct special audit projects. The State Auditor conducts both financial compliance and performance audits in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States. In addition, and in conjunction with an independent public accounting firm, the State Auditor performs a significant portion of the audit work relating to the state single audit.

Within the State Auditor's office is the Division of Local Mandates, which evaluates all proposed and actual legislation to determine the financial impact on the Commonwealth's cities and towns. In accordance with state law, the Commonwealth is required to reimburse cities and towns for any costs incurred through mandated programs established after the passage of Proposition 2½, the statewide tax limitation enacted by the voters in 1980, unless expressly exempted from those provisions, and the State Auditor's financial analysis is used to establish the amount of reimbursement due to the Commonwealth's cities and towns. See "COMMONWEALTH PROGRAMS AND SERVICES – Local Aid; *Property Tax Limits*."

Also within the State Auditor's office is the Bureau of Special Investigations, which is charged with the responsibility of investigating fraud within public assistance programs.

COMMONWEALTH REVENUES

In order to fund its programs and services, the Commonwealth collects a variety of taxes and receives revenues from other non-tax sources, including the federal government and various fees, fines, court revenues, assessments, reimbursements, interest earnings and transfers from its non-budgeted funds, which are deposited in the General Fund, the Highway Fund and other operating budgeted funds. For purposes of this Information Statement, these funds will be referred to as budgeted operating funds, and revenues deposited in such funds will be referred to as budgeted operating revenues. In fiscal 2006, on a statutory basis, approximately 62.5% of the Commonwealth's budgeted operating revenues and other financing sources were derived from state taxes. In addition, the federal government provided approximately 18.9% of such revenues, with the remaining 18.6% provided from departmental revenues and transfers from non-budgeted funds. The measurement of revenues for the budgeted operating funds on a statutory basis differs from governmental revenues on a GAAP basis. See "SELECTED FINANCIAL DATA – GAAP Basis; *Revenues – GAAP Basis*." The Commonwealth's executive and legislative branches establish the Commonwealth's budget using the statutory basis of accounting.

Statutory Basis Distribution of Budgetary Revenues

The following table sets forth the Commonwealth's revenues in its budgeted operating funds for fiscal 2002 through fiscal 2006 and projected revenues for fiscal 2007.

Commonwealth Revenues - Budgeted Operating Funds

(in millions)(1)

	Fiscal 2002	Fiscal 2003	Fiscal 2004(5)	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007(6)
Tax Revenues:						
Alcoholic beverages	$65.4	$66.3	$67.9	$68.6	$68.9	$70.3
Banks	137.0	344.5	238.7	198.9	349.9	251.3
Cigarettes	275.0	451.0	425.4	423.6	435.3	437.1
Corporations	586.7(4)	799.4(4)	997.6	1,062.7	1,390.7	1,497.6
Deeds	134.3	147.8	187.0	220.3	210.1	177.0
Income	7,912.9	8,026.1	8,830.3	9,690.3	10,483.4	11,121.9
Inheritance and estate	200.5	181.3	194.7	255.1	196.3	246.1
Insurance	382.9	387.8	420.2	423.4	448.5	449.2
Motor fuel	666.8	676.4	684.2	685.5	671.8	671.9
Public utilities	88.5	40.6	64.7	71.1	118.5	170.5
Racing	2.7	-	-	-	-	-
Room occupancy	123.3	120.0	88.9	97.8	105.8	112.9
Sales:						
Regular	2,601.4	2,583.6	2,591.6	2,746.6	2,864.7	2,944.5
Meals	500.9	512.0	531.7	555.6	584.1	608.9
Motor vehicles	593.6	612.5	625.8	584.2	555.5	537.0
Sub-Total–Sales	3,695.9	3,708.1	3,749.2	3,886.4	4,004.3	4,090.4
Miscellaneous	15.1	14.3	4.2	4.2	4.0	3.7
Total Tax Revenues	14,287.1	14,963.8(5)	15,953.2	17,087.9	18,487.5	19,300.0
MBTA transfer	(664.3)	(684.3)	(684.3)	(704.8)	(712.6)	(734.0)
MSBA transfer (2)	-	-	-	(395.7)	(488.7)	(557.4)
Total Budgeted Operating Tax Revenues	13,622.8	14,279.5	15,268.9	15,987.4	17,286.2	18,008.6
Non-Tax Revenues:						
Federal reimbursements	4,334.9	4,523.6	5,098.5	4,697.0	5,210.1	6,061.8
Departmental assessments and other revenues(7)	1,485.2	1,494.8	1,847.7	1,948.9	2,094.3	2,051.8
Inter-fund transfers from non-budgeted funds and other sources (3)	1,732.0	1,689.2	1,773.1	1,740.2	1,714.9	863.7
Budgeted Non-Tax Revenues and Other Sources	7,552.2	7,707.6	8,719.3	8,386.1	9,019.3	8,977.3
Budgeted Revenues and Revenues from Other Sources	$21,174.8	$21,987.2	$23,988.3	$24,373.5	$26,305.5	$26,985.9

SOURCE: Fiscal 2002-2006, Office of the Comptroller; fiscal 2007, Executive Office for Administration and Finance.

(1) Totals may not add due to rounding. Table does not reflect inter-fund transfers among budgeted funds and other sources that have no effect on ending balances. Excludes certain miscellaneous taxes expended outside the budget process.

(2) Beginning in fiscal 2005, sales tax transfers to the MSBA replaced budgetary appropriations for school building assistance. Actual expenditures for school building assistance in fiscal 2002 through 2004 were $365.4 million, $383.2 million and $551.4 million, respectively. See "SELECTED FINANCIAL DATA – Recent Financial Restructurings; *School Building Assistance Program.*"

(3) Inter-fund transfers from non-budgeted funds and other sources include profits from the State Lottery, tobacco settlement funds, abandoned property proceeds, transfers to the Commonwealth Care Trust Fund and Medical Assistance Trust Fund (successors to the Uncompensated Care Pool), as well as other inter-fund transfers.

(4) The Department of Revenue estimates that as a result of the timing of federal tax legislation relating to the depreciation deduction for corporations and the Commonwealth's legislation in response, tax revenue collections in fiscal 2002 were reduced by approximately $30 million and tax revenue collections in fiscal 2003 were increased by the same approximate amount.

(5) Beginning on July 1, 2003, certain minor budgeted funds were reclassified as non-budgeted funds. Prior years have not been restated.

(6) Based on fiscal 2007 consensus revenue estimate of $19.3 billion.

(7) Excludes intergovernmental revenues.

State Taxes

The major components of state taxes are the income tax, which is projected to account for approximately 57.6% of total tax revenues in fiscal 2007, the sales and use tax, which is projected to account for approximately 21.22%, and the corporations and other business and excise taxes (including taxes on insurance, financial institutions and public utility corporations), which are projected to account for approximately 12.2%. Other tax and excise sources are projected to account for the remaining 8.99% of total fiscal 2007 tax revenues.

Effects of Tax Law Changes. During fiscal 2002 and fiscal 2003, legislation was implemented that had the net effect of reducing revenues by decreasing income tax rates or increasing or establishing various deductions and credits. In addition, several administrative changes were implemented that reduced revenues. During fiscal 2003, legislation was implemented that reversed or delayed some of the previous tax reductions, and implemented increases in other taxes. The incremental net effect of these tax law and administrative changes (relative to the immediately preceding fiscal year) is estimated by the Department of Revenue to have been a reduction of approximately $700 million of fiscal 2002 revenues. In fiscal 2003, tax law changes (including the so-called loophole closing measures described below) are estimated to have increased revenue collections by a net amount of approximately $1.005 billion. The Department of Revenue estimates that in fiscal 2004, the impact of tax law and administrative changes (including the non-recurrence of some fiscal 2003 revenues from certain loophole closings and that year's tax amnesty program) was to reduce tax collections by approximately $110 million compared to fiscal 2003. The Department of Revenue estimates that tax law changes increased tax collections by approximately $31 million in fiscal 2005 compared to fiscal 2004, reduced tax collections by approximately $154 million in fiscal 2006 compared to fiscal 2005, will reduce tax collections by approximately $113 million in fiscal 2007 compared to fiscal 2006 and will reduce tax collections by approximately $48 million in fiscal 2008 compared to fiscal 2007. See "Fiscal 2006 and Fiscal 2007 Tax Revenues" below.

Income Tax. The Commonwealth assesses personal income taxes at flat rates, according to classes of income, after specified deductions and exemptions. A rate of 5.3% has been applied to most types of income since January 1, 2002. The tax rate on gains from the sale of capital assets held for one year or less and from the sale of collectibles is 12%, and the tax rate on gains from the sale of capital assets owned more than one year is 5.3%. Interest on obligations of the United States and of the Commonwealth and its political subdivisions is exempt from taxation.

Prior to January 1, 1999, a different rate was applied to "Part A" income (generally, interest and dividends) and "Part B" income (generally, "earned" income from employment, professions, trades, businesses, rents and royalties). The rate on Part A income was 12% prior to January 1, 1999; it was reduced to 5.95% as of January 1, 1999 and as of January 1, 2000 is the same as the rate on Part B income. The rate on Part B income was 5.95% prior to January 1, 2000, when it was reduced to 5.85%. The rate on Part B income was reduced to 5.6% on January 1, 2001 and to 5.3% on January 1, 2002 by an initiative petition approved by Massachusetts voters on November 7, 2000. This initiative petition also mandated a reduction in the Part B rate to 5.0% on January 1, 2003.

Legislation enacted in July, 2002 made several changes to the state income tax. These included a delay of the scheduled Part B tax rate reduction from 5.3% to 5.0% for at least four years, suspension of the deduction for charitable contributions and a 25% reduction in personal exemptions. This legislation also changed the tax structure for long-term capital gains (*i.e.*, capital gains on assets held for more than one year). Prior to the legislation, long-term capital gains were taxed at rates ranging from 0% to 5%, depending on how long the asset had been held before sale. Effective January 1, 2003, long-term capital gains are taxed at the Part B income tax income rate, which is currently 5.3%.

The 2002 legislation also included a mechanism by which the tax year 2001 personal exemptions and charitable deductions could be gradually restored, and the tax rate on Part B income could be gradually reduced to 5.0%, contingent upon "baseline" state tax revenue growth (*i.e.*, revenue growth after factoring out the impact of tax law and administrative processing changes) growing by 2% more than the rate of inflation for state and government purchases. Specifically, the personal exemption would be restored in four equal annual increases, contingent upon sufficient tax revenue growth in the immediately preceding fiscal year. Commencing in the year following the final personal exemption increase, the personal income tax rate would be reduced from 5.3% to 5.0% in six equal annual reductions of 0.05%, again contingent on sufficient revenue growth in each preceding fiscal year. In the tax year following that in which the personal income tax rate was reduced to 5.0%, the charitable deduction would be restored. In fiscal 2002 and 2003, tax revenue growth was such that personal exemptions remained at 2002 levels for tax years 2003 and 2004, respectively. In fiscal 2004, fiscal 2005 and fiscal 2006, baseline tax revenue growth was sufficient to trigger an increase in the personal exemptions for tax years 2005, 2006 and 2007, respectively. Based on the January 30, 2007 fiscal 2007 revenue estimate, fiscal 2007 tax revenue growth is not expected to be sufficient to trigger an increase in the personal exemption in tax year 2008. The next increase in the personal exemption will be the last before the personal income tax rate deductions are triggered, contingent on sufficient revenue growth.

The Department of Revenue estimates the following effects from the changes made in the July, 2002 legislation:

- Taxing capital gains at the Part B income rate increased fiscal 2003 revenues by approximately $250 million to $300 million, fiscal 2004 revenues by approximately $350 million to $400 million, fiscal 2005 revenues by approximately $720 million to $770 million and fiscal 2006 revenues by approximately $950 million to $1 billion and is expected to increase fiscal 2007 revenues by approximately $1.1 billion to $1.2 billion.

- The delay in the Part B rate reduction resulted in approximately $200 million more in revenue during fiscal 2003 than would have been the case had the rate been reduced to 5.0% in calendar 2003, resulted in additional revenue of approximately $506 million in fiscal 2004, $556 million in fiscal 2005 and $595 million in fiscal 2006, and is projected to result in additional revenue of approximately $625 million in fiscal 2007.

- The suspension of the deduction for charitable contributions increased revenues by approximately $170 million in fiscal 2003, $179 million in fiscal 2004, $185 million in fiscal 2005 and $190 million in fiscal 2006 and is projected to increase revenues by approximately $201 million in fiscal 2007.

- The decrease in the personal exemption amounts resulted in approximately $325 million in additional tax collections in fiscal 2003. The 25% cut in personal exemptions was retroactive to January 1, 2002, with the retroactive portion of the tax increase being paid primarily when taxpayers filed their tax year 2002 income tax returns in the spring of 2003. The retroactive nature of the fiscal 2003 revenue impact caused the fiscal 2004 revenue gain to be smaller than it was in fiscal 2003. The Department of Revenue estimates that the fiscal 2004 impact of the personal exemption reductions was approximately $225 million. The partial restoration of the personal exemptions in tax years 2005 and 2006 reduced the amount raised by the initial personal exemption decreases. The Department of Revenue estimates that the additional revenue generated by the personal exemption increases fell to approximately $200 million in fiscal 2005, $140 million in fiscal 2006 and a projected $80 million in fiscal 2007.

Sales and Use Tax. The Commonwealth imposes a 5% sales tax on retail sales of certain tangible property (including retail sales of meals) transacted in the Commonwealth and a corresponding 5% use tax on the storage, use or other consumption of like tangible properties brought into the Commonwealth. However, food, clothing, prescribed medicine, materials and produce used in food production, machinery, materials, tools and fuel used in certain industries and property subject to other excises (except for cigarettes) are exempt from sales taxation. The sales and use tax is also applied to sales of electricity, gas and steam for certain nonresidential use and to nonresidential and a portion of residential use of telecommunications services.

Sales tax receipts from establishments that first opened on or after July 1, 1997 and that are located near the site of the Boston Convention and Exhibition Center, sales tax receipts from retail vendors in hotels in Boston and Cambridge that first opened on or after July 1, 1997 and sales tax receipts from retail vendors located in the Springfield Civic and Convention Center or in hotels near the Springfield Civic and Convention Center that first opened on or after July 1, 2000 are required to be credited to the Convention Center Fund. As of enactment of the fiscal 2004 general appropriations act, this fund is no longer included in the calculation of revenues for budgeted operating funds. See "LONG-TERM LIABILITIES—Special Obligation Debt; *Convention Center Fund*."

A portion of the Commonwealth's receipts from the sales tax (other than the tax on meals) is dedicated through trust funds to the Massachusetts Bay Transportation Authority (MBTA) and the Massachusetts School

Building Authority (MSBA). The amount dedicated to the MBTA is the amount raised by a 1% sales tax (not including meals), with an inflation-adjusted floor. A comparable amount, though without the floor, will be dedicated to the MSBA beginning in fiscal 2010, with lesser amounts dedicated to the MSBA from fiscal 2005 through fiscal 2009. See “SELECTED FINANCIAL DATA - Recent Financial Restructurings.”

Legislation enacted in March, 2003, July, 2004 and November, 2005 closed several so-called tax loopholes related to the sales tax. These included changes to the taxation of promotional advertising materials, goods delivered through “drop shipments,” items that are fabricated outside of Massachusetts but sold in the state and the taxation of downloaded software that is pre-written or “canned.” The Department of Revenue estimates that these changes resulted in additional tax collections of $20-23 million in fiscal 2005, $34-48 million in fiscal 2006 and $71-81 million on an annualized basis thereafter.

The federal Internet Tax Nondiscrimination Act, passed by the U. S. Congress in late 2004, expanded the definition of “internet access” and thus had the effect of exempting from Massachusetts sales tax telecommunications services purchased, used or sold by a provider of internet access for use in providing internet access to its customers. Such telecommunications services had been taxed for Massachusetts sales and use tax purposes when purchased by a provider of internet access. The Department of Revenue estimates that the impact of this legislation was to reduce revenues by approximately $13 million in fiscal 2006 and $20-25 million annually thereafter.

Business Corporations Tax. Business corporations doing business in the Commonwealth, other than banks, trust companies, insurance companies, railroads, public utilities and safe deposit companies, are subject to an excise that has a property measure and an income measure. The value of Massachusetts tangible property (not taxed locally) or net worth allocated to the Commonwealth is taxed at $2.60 per $1,000 of value. The net income allocated to Massachusetts, which is based on net income for federal taxes, is taxed at 9.5%. The minimum tax is $456. Both rates and the minimum tax are inclusive of a 14% surtax.

In general, corporations apportion their income to Massachusetts based on the proportion of payroll, property and sales within the Commonwealth, with sales being double-weighted. However, beginning January 1, 1996, legislation was phased in over five years establishing a “single sales factor” apportionment formula for the business corporations tax. The formula calculates a firm’s taxable income as its net income times the percentage of its total sales that are in Massachusetts, as opposed to the prior formula that took other factors, such as payroll and property into account. Beginning January 1, 1997, legislation was phased in which sourced sales of mutual fund shares to the state of domicile of the purchaser instead of sourcing the sales to the state where the mutual fund provider bore the cost of performing services.

Legislation enacted in March, 2003, July, 2004 and November, 2005 closed several so-called loopholes in the corporate and financial institutions tax structure. Among these were provisions dealing with real estate investment trusts, qualified subchapter S subsidiaries and payments to related parties for intangible expenses. See also “*Financial Institutions Tax*.” Excluding provisions related to financial institutions, the Department of Revenue estimates that these changes increased revenues by approximately $25 million in fiscal 2003, $129 million in fiscal 2004, $150 million in fiscal 2005 and $173 million in fiscal 2006, and that revenues will be increased by $178 million annually thereafter. The fiscal 2008 budget recommendations filed by the Governor in February, 2007 call for additional changes in the corporate tax structure which are now being considered by the Legislature. See “FISCAL 2007 AND FISCAL 2008 - Fiscal 2008 Budget Proposals.”

Financial Institutions Tax. Financial institutions (which include commercial and savings banks) are subject to an excise tax of 10.5%.

Legislation enacted in March, 2003 clarified the treatment of real estate investment trust (REIT) distributions with respect to the dividends-received deduction, namely, that such distributions received by businesses subject to the corporate excise tax are not to be treated as dividends and that they have never been exempt or partially exempt from taxation. REIT distributions are subject to taxation at the recipient level. The Department of Revenue estimates that this change resulted in additional tax revenues of approximately $160-180 million for fiscal 2003, most of which was the result of liabilities for prior tax years. The Department of Revenue estimates that the REIT legislation has resulted in revenue increases of $40-60 million in each of the ensuing fiscal years and will continue to yield approximately the same amount in future fiscal years.

Insurance Taxes. Life insurance companies are subject to a 2% tax on gross premiums. Domestic companies also pay a 14% tax on net investment income. Property and casualty insurance companies are subject to a 2% tax on gross premiums plus a 14% surcharge, for an effective tax rate of 2.28%. Domestic companies also pay a 1% tax on gross investment income.

Other Taxes. Other tax revenues are derived by the Commonwealth from excise taxes on motor fuels, cigarettes, alcoholic beverages and deeds, among other tax sources. The excise tax on motor fuels is $0.21 per gallon. The tax on cigarettes was raised in fiscal 2003 from $0.76 per pack to $1.51 per pack; the same legislation also raised the tax rate on other types of tobacco products. The Department of Revenue estimates that this change resulted in additional revenue of approximately $185 million in fiscal 2003, $155-160 million in fiscal 2004 and $155 million in fiscal 2005 and thereafter. Legislation was enacted in March, 2003 that allowed the Commissioner of Revenue to provide incentives for inheritance trusts to settle future obligations during fiscal 2003. Through this program, approximately $34 million was raised in fiscal 2004, but inheritance tax collections in subsequent years were reduced.

In 2001, the United States Congress made numerous changes to Internal Revenue Code provisions relating to the estate and gift tax. For the estates of decedents dying on or after January 1, 2002, federal law raised the exemption amount and phased out the amount of the allowable credit for state death taxes by 25% a year until the credit was eliminated in 2005. Because the Massachusetts estate tax, prior to such Congressional action, equaled the amount of the allowable federal credit for state death taxes, this federal change meant that the Massachusetts estate tax (known as a "sponge tax") would have been phased out and eliminated. In October, 2002, the Massachusetts estate tax was retained by "decoupling" the Massachusetts estate tax from the federal estate tax for decedents dying on or after January 1, 2003. The Massachusetts sponge tax is now tied to the Internal Revenue Code as in effect on December 31, 2000. These federal changes are estimated to have reduced fiscal 2003 collections by approximately $30-40 million, and the decoupling is estimated to have increased fiscal 2004 tax revenues by $40 million and fiscal 2005 tax revenues by $13 million in the first three months of fiscal 2005, when the effect of the phase-in was complete.

Tax Revenue Forecasting

Under state law, on or before October 15 and March 15 of each year, the Secretary of Administration and Finance is required to submit to the Governor and to the House and Senate Committees on Ways and Means estimates of revenues available to meet appropriations and other needs in the following fiscal year. On or before October 15, January 15 and April 15, the Secretary is required to submit revised estimates for the current fiscal year unless, in her opinion, no significant changes have occurred since the last estimate of total available revenues. On or before January 15 of each year, the Secretary is required to develop jointly with the House and Senate Committees on Ways and Means a consensus tax revenue forecast for the following fiscal year. Beginning in fiscal 2005, state finance law has required that the consensus tax revenue forecasts be net of the amount necessary to fully fund the pension system according to the applicable funding schedule, which amount is to be transferred without further appropriation from the General Fund to the Commonwealth's Pension Liability Fund. See "COMMONWEALTH PROGRAMS AND SERVICES — Pension and Other Post-Retirement Benefit Obligations."

Fiscal 2002. There was no consensus tax revenue forecast in advance of the fiscal 2002 general appropriations act, which was not enacted until December, 2001. At that time, the Legislature assumed that fiscal 2002 tax revenues would be $15.6 billion (including sales tax receipts dedicated to the MBTA). In January, 2002, the Secretary of Administration and Finance estimated fiscal 2002 tax revenues at $15.405 billion, in April the Governor and legislative leaders agreed on a revised estimate of $14.750 billion, and in May, 2002, the Secretary of Administration and Finance reduced the estimate to $14.280 billion. Fiscal 2002 budgeted tax collections totaled approximately $14.287 billion, before transfers to the MBTA.

Fiscal 2003. In April, 2002, the Governor and legislative leaders agreed to a consensus tax revenue estimate for fiscal 2003 of $14.716 billion (including sales tax receipts dedicated to the MBTA). By June, 2002, the Secretary of Administration and Finance reduced that estimate to $14.175 billion, and further to $14.116 billion in July, 2002. The fiscal 2003 general appropriations act was enacted in July, 2002, based on a consensus tax revenue forecast of $14.116 billion, plus $1.241 billion in estimated tax increases, for a total of $15.356 billion. Forecasted revenues were reduced by the Secretary of Administration and Finance in October, 2002 (to $15.145 billion) and in February, 2003 (to $14.648 billion), before being raised in April, 2003 to $14.748 billion to account for increased revenue estimated to result from the closing of certain so-called tax loopholes. Fiscal 2003 budgeted tax collections totaled approximately $14.964 billion, before transfers to the MBTA.

Fiscal 2004. In February, 2003 the Secretary of Administration and Finance and legislative leaders announced a consensus estimate of Commonwealth tax revenues for fiscal 2004 of $14.678 billion, including sales tax receipts dedicated to the MBTA. The fiscal 2004 general appropriations act was enacted on June 30, 2003 based on a tax revenue estimate of $14.808 billion, composed of the consensus tax revenue estimate of $14.678 billion, plus $174 million in additional revenues attributable to legislation closing various so-called tax loopholes. In January, 2004 the Secretary of Administration and Finance raised the estimate to $15.230 billion. Fiscal 2004 budgeted tax collections totaled approximately $15.953 billion, before transfers to the MBTA.

Fiscal 2005. In January, 2004 the Secretary of Administration and Finance and legislative leaders announced a consensus fiscal 2005 Commonwealth tax estimate of $15.801 billion (including sales tax receipts dedicated to the MBTA and MSBA and amounts to be transferred to the pension system). The fiscal 2005 general appropriations act was enacted in June, 2004 based upon a tax estimate of $15.968 billion, including $167.2 million in revenue enhancements. In October, 2004 the Secretary of Administration and Finance raised the estimate to $16.231 billion. Fiscal 2005 budgeted tax collections totaled $17.088 billion, before transfers to the MBTA and MSBA and the pension system.

Fiscal 2006. There was no consensus tax revenue forecast in advance of the fiscal 2006 budget. In January, 2005, the Secretary of Administration and Finance estimated that fiscal 2006 tax revenues would be $17.336 billion, and legislative leaders announced agreement on an estimate of $17.100 billion, before transfers to the MBTA, the MSBA and the pension system. At the time the fiscal 2006 general appropriations act was enacted, the estimate of the Secretary of Administration and Finance was $17.448 billion, and the Legislature's estimate was $17.283 billion. In October, 2005 the Secretary of Administration and Finance increased the tax revenue estimate for fiscal 2006 to $17.957 billion. In January, 2006 the Secretary of Administration and Finance increased the estimate to $18.158 billion. Fiscal 2006 budgeted tax collections totaled approximately $18.487 billion, before transfers to the MBTA, the MSBA and the pension system.

Fiscal 2007. In January, 2006 the Secretary of Administration and Finance and legislative leaders announced a consensus fiscal 2007 Commonwealth tax estimate of $18.975 billion, before transfers to the MBTA, the MSBA and the pension system. In October, 2006 the Secretary of Administration and Finance raised the estimate to $19.132 billion. On January 30, 2007 the new Secretary of Administration and Finance raised the estimate to $19.3 billion.

Fiscal 2008. In January, 2007 the Secretary of Administration and Finance and legislative leaders announced a consensus fiscal 2008 Commonwealth tax estimate of $19.879 billion (including sales tax receipts dedicated to the MBTA and MSBA and amounts to be transferred to the pension system). The fiscal 2008 tax revenue estimate represents growth of 3% over the most recent (January, 2007) estimate for fiscal 2007. Excluding changes in the tax code, this represents "baseline" growth of 3.1%.

Fiscal 2006 and Fiscal 2007 Tax Revenues

Fiscal 2006. Tax revenue collections for fiscal 2006 totaled $18.487 billion, an increase of $1.4 billion or 8.2% over fiscal 2005. The following table shows monthly tax collections for fiscal 2006 and the change from tax collections in the same month in the prior year, both in dollars and as a percentage. The table also notes the amount of tax collections in fiscal 2006 that are dedicated to the MBTA and to the MSBA.

Fiscal 2006 Tax Collections (in millions) (1)

Month	Tax Collections	Change From Prior Year	Percentage Change	MBTA Portion (2)	MSBA Portion	Collections, Net of MBTA and MSBA
July	$ 1,188.8	$ 61.6	5.5%	$ 63.7	$ 44.6	$ 1,080.5
August	1,204.9	12.8	1.1	60.0	42.0	1,102.8
September	1,941.2	243.4	14.3	54.7	38.3	1,848.2
October	1,216.0	117.3	10.7	56.2	39.4	1,120.4
November	1,119.0	0.0	0.0	54.7	38.3	1,026.1
December	1,791.0	204.0	12.9	67.3	44.6	1,679.2
January	1,921.1	235.8	14.0	67.6	47.3	1,806.2
February	853.7	4.5	0.5	50.4	35.3	767.9
March	1,626.7	69.8	4.5	60.1	35.3	1,531.3
April	2,213.0	196.1	9.7	57.5	40.3	2,115.3
May	1,375.5	48.5	3.7	55.6	39.0	1,280.9
June	2,036.5	205.8	11.2	64.7	50.8	1,921.1
Total	$18,487.4	$1,399.5	8.2%	$712.6	$488.7	$17,286.2

SOURCE: Executive Office for Administration and Finance.

(1) Sum of details may not equal total because of rounding.

(2) Includes adjustment of $12.5 million on account of the second quarter, $9.7 million on account of the third quarter and $6.3 million on account of the fourth quarter, related to the inflation-adjusted floor applicable to tax receipts dedicated to the MBTA.

The tax revenue increase of $1.4 billion over fiscal 2005 is attributable in large part to an increase of approximately $448.4 million, or 5.8%, in withholding collections, an increase of approximately $252.6 million, or 15%, in income tax estimated payments, an increase of approximately $249.6 million, or 17.3%, in income tax payments with returns and bills, an increase of approximately $117.9 million, or 3%, in sales and use tax collections, and an increase of approximately $550.2 million or 32.3% in corporate and business collections, which are partially offset by changes in other revenues (net of refunds).

Fiscal 2007. Tax revenue collections for the first ten months of fiscal 2007 totaled $15.906 billion, an increase of $831 billion or 5.5% over the comparable period in fiscal 2006. The following table shows monthly tax collections for fiscal 2007 and the change from tax collections in the same months in the prior year, both in dollars and as a percentage. The table also notes the amount of tax collections in fiscal 2007 that are dedicated to the MBTA and to the MSBA.

Fiscal 2007 Tax Collections (in millions) (1)

Month	Tax Collections	Change From Prior Year	Percentage Change	MBTA Portion (3)	MSBA Portion	Collections, Net of MBTA and MSBA
July	$ 1,246.7	$ 57.9	4.9%	$ 61.5	$ 48.0	$ 1,137.2
August	1,188.2	(16.7)	(1.4)	58.2	45.4	1,084.5
September	2,068.9	127.7	6.6	63.8	43.2	1,961.9
October	1,244.8	28.8	2.4	60.7	47.4	1,136.7
November	1,229.8	110.7	9.9	54.5	42.5	1,125.2
December	1,784.4	(6.6)	(0.4)	68.3	43.2	1,672.9
January	2,052.9	131.7	6.9	69.9	54.5	1,928.5
February	987.2	133.6	15.6	54.3	42.3	890.7
March	1,768.0	141.3	8.7	59.4	38.6	1,670.0
April(2)	2,336.2	123.2	5.3	55.6	43.4	2,237.2
Total (2)	$15,905.9	$830.6	5.5%	$606.1	$448.5	$14,851.3

SOURCE: Executive Office for Administration and Finance.
(1) Details may not add to Total because of rounding.
(2) Figures are preliminary.
(3) Includes adjustment of $8.4 million on the account of the first quarter , $12.9 million on account of the second quarter and $9.9 million on account of the third quarter, related to the inflation-adjusted floor applicable to tax receipts dedicated to the MBTA.

The year-to-date tax revenue increase of $830.6 billion over fiscal 2006 is attributable in large part to an increase of approximately $422.8 million, or 6.2%, in withholding collections, an increase of approximately $84.7 million, or 5.6%, in income tax estimated payments, an increase of approximately $46.7 million, or 1.4%, in sales and use tax collections, an increase of approximately $171.2 million, or 9.9%, in corporate and business collections and an increase of $43.7 million, or 3.1%, in miscellaneous tax collections. Through April, 2007, fiscal 2007 year-to-date tax collections have exceeded the year-to-date benchmark by approximately $54 million. That benchmark was based on the January 30, 2007 fiscal 2007 tax revenue estimate of the Secretary of Administration and Finance of $19.300 billion. April, 2007 collections were $115 million below the benchmark for that month.

Federal and Other Non-Tax Revenues

Federal revenues are collected through reimbursements for the federal share of entitlement programs such as Medicaid and through block grants for programs such as Transitional Assistance to Needy Families (TANF). The amount of federal reimbursements to be received is determined by state expenditures for these programs. The Commonwealth receives reimbursement for approximately 50% of its spending for Medicaid programs. Block grant funding for TANF is received quarterly and is contingent upon a maintenance-of-effort spending level determined annually by the federal government. In fiscal 2006, federal reimbursements for budgeted operating activity amounted to $5.210 billion. Federal reimbursements for fiscal year 2007 are projected to be $6.062 billion. See "COMMONWEALTH PROGRAMS AND SERVICES."

Departmental and other non-tax revenues are derived from licenses, tuition, fees and reimbursements and assessments for services. For fiscal year 2006, budgeted departmental revenues were $1.6 billion, assessments were $146.1 million and other miscellaneous revenues, including investment income, were $308.3 million. The largest budgeted departmental revenues, assessments and miscellaneous revenues in fiscal 2006 included $410.6 million for Registry of Motor Vehicles fees, fines, assessments, $171.2 million in Executive Office of Health and Human Services pharmacy rebates, third party recoveries and other reimbursements, $212.0 million from filing, registration and other fees paid to the Secretary of State's Office, $137.2 million in housing authority and municipal payments on behalf of retired teachers to the Commonwealth for group health insurance, $74 million in tuition remitted to schools of higher education, $162.9 million from underground storage cleanup, deeds excise and other non-tax fees and remittances received by the Department of Revenue and $104.4 million in fees, fines and assessments charged by the court systems. For fiscal 2007, departmental and other non-tax revenues are estimated to be $2.052 billion.

Lottery Revenues. For the budgeted operating funds, inter-fund transfers include transfers of profits from the State Lottery Fund and the Arts Lottery Fund and reimbursements for the budgeted costs of the State Lottery Commission, which accounted for net transfers from the Lottery of $972.9 million, $957.5 million, $985.2 million, $1.018 billion and $1.035 billion in fiscal 2002 through 2006, respectively, and are estimated by the State Lottery Commission at $1.038 billion in fiscal 2007. Under state law, the net balance in the State Lottery Fund, as determined by the Comptroller on each September 30, December 31, March 31 and June 30, is to be used to provide local aid. The general appropriations act for fiscal 2007 stipulates that the aggregate distribution to cities and towns from the State Lottery Fund in fiscal 2007 shall be $920 million. The fiscal 2007 budget assumes total net transfers from the Lottery of $1.105 billion, including the $920 million aggregate distribution to cities and towns. The State Lottery Commission has never projected transfers of $1.105 billion. There is no provision in current law for dealing with the anticipated $67 million shortfall in net lottery revenues in fiscal 2007, but it would mean that the State Lottery Fund, a non-budgeted fund, would end fiscal 2007 in a deficit position.

Tobacco Settlement. In November, 1998, the Commonwealth joined with other states in a master settlement agreement that resolved the Commonwealth's and other states' litigation against the cigarette industry. Under the agreement, cigarette companies have agreed to make both annual payments (in perpetuity) and five initial payments (for the calendar years 1999 to 2003, inclusive) to the settling states. Each payment amount is subject to applicable adjustments, reductions and offsets, including upward adjustments for inflation and downward adjustments for decreased domestic cigarette sales volume.

The Commonwealth's allocable share of the base amounts payable under the master settlement agreement is approximately 4.04%. The Commonwealth's allocable share of the base amounts under the agreement through 2025 is more than $8.3 billion, subject to adjustments, reductions and offsets. However, in pending litigation tobacco manufacturers are claiming that because of certain developments they are entitled to reduce future payments under the master settlement agreement, and certain manufacturers withheld payments to the states due in April, 2006 and April, 2007. The Commonwealth believes it is due the full amount and is pursuing its claim to unreduced payments. See "LEGAL MATTERS - Taxes and Revenues." The Commonwealth was also awarded $414.3 million from a separate Strategic Contribution Fund established under the master settlement agreement to reward certain states' particular contributions to the national tobacco litigation effort. This additional amount, also subject to a number of adjustments, reductions and offsets, is payable in equal annual installments during the years 2008 through 2017.

Tobacco settlement payments were initially deposited in a permanent trust fund (the Health Care Security Trust), with only a portion of the monies made available for appropriation. Beginning in fiscal 2003, however, the Commonwealth has appropriated the full amount of tobacco settlement receipts in each year's budget. The balance accumulated in the Health Care Security Trust amounted to $471.7 million at the end of fiscal 2006. The Governor's fiscal 2008 budget recommendation proposes to use approximately 85% of the balance in the Health Care Security Trust to fund a new State Retiree Benefit Trust Fund, designed to begin the funding of the Commonwealth's unfunded liability associated with retiree healthcare costs. See "FISCAL 2007 AND FISCAL 2008 - Fiscal 2008 Budget Proposals."

The following table sets forth the amounts received by the Commonwealth to date. The table does not include approximately $30 million in withheld payments in fiscal 2006 and approximately $27 million in withheld payments in fiscal 2007 that the Commonwealth continues to pursue. See "LEGAL MATTERS - Taxes and Revenues."

Payments Received Pursuant to the Tobacco Master Settlement Agreement (in millions)(1)

Fiscal Year	Initial Payments	Annual Payments	Total Payments
2000	$186.6(2)	$139.6	$326.2(2)
2001	78.2	164.2	242.5
2002	82.8	221.7	304.5
2003	86.4	213.6	300.0
2004	-	253.6	253.6
2005	-	257.4	257.4
2006	-	236.3	236.3
2007	-	245.4	245.4
Total	$434.0	$1,731.8	$2,165.8

SOURCES: Fiscal 2000-2006, Office of the Comptroller; fiscal 2007, Executive Office for Administration and Finance.
(1) Amounts are approximate. Totals may not add due to rounding.
(2) Payments received for both 1999 and 2000.

Limitations on Tax Revenues

Chapter 62F of the General Laws, which was enacted by the voters in November, 1986, establishes a state tax revenue growth limit for each fiscal year equal to the average positive rate of growth in total wages and salaries in the Commonwealth, as reported by the federal government, during the three calendar years immediately preceding the end of such fiscal year. The growth limit is used to calculate "allowable state tax revenue" for each fiscal year. Chapter 62F also requires that allowable state tax revenues be reduced by the aggregate amount received by local governmental units from any newly authorized or increased local option taxes or excises. Any excess in state tax revenue collections for a given fiscal year over the prescribed limit, as determined by the State Auditor, is to be applied as a credit against the then-current personal income tax liability of all taxpayers in the Commonwealth in proportion to the personal income tax liability of all taxpayers in the Commonwealth for the immediately preceding tax year. The law does not exclude principal and interest payments on Commonwealth debt obligations from the scope of its tax limit. However, the preamble contained in Chapter 62F provides that "although not specifically required by anything contained in this chapter, it is assumed that from allowable state tax revenues as defined herein the Commonwealth will give priority attention to the funding of state financial assistance to local governmental units, obligations under the state governmental pension systems and payment of principal and interest on debt and other obligations of the Commonwealth."

Tax revenues in fiscal 2002 through 2006 were lower than the "allowable state tax revenue" limit set by Chapter 62F and are expected to be lower than the allowable limit in fiscal 2007.

Chapter 62F was amended by the fiscal 2003 and fiscal 2004 general appropriations acts to establish an additional tax revenue limitation. The fiscal 2003 general appropriations act created a quarterly cumulative "permissible tax revenue" limit equal to the cumulative year-to-date actual state tax revenue collected during the same fiscal period in the prior fiscal year, increased by the sum of the most recently available year-over-year inflation rate plus two percentage points. Effective July 1, 2003, at the end of each quarter the Commissioner of Revenue must calculate cumulative permissible tax revenue. The Comptroller must then divert tax revenue in excess of permissible tax revenue from the General Fund to a Temporary Holding Fund to make such excess revenue unavailable for expenditure. If actual tax revenue collections fall short of the permissible limit, the difference flows back into the General Fund. At the end of each fiscal year, tax revenue in excess of permissible state tax revenue for the year is to be held in the Temporary Holding Fund pending disposition by the Comptroller. The Comptroller is required to first use any funds in the Temporary Holding Fund to reimburse the Commonwealth Stabilization Fund for any amounts expended from the Stabilization Fund during the fiscal year. The general law amendments in the fiscal 2004 general appropriations act require that at the end of each fiscal year, the state comptroller must transfer remaining excess revenue from the Temporary Holding Fund back to the General Fund for inclusion in consolidated net surplus.

In fiscal 2006, cumulative net state tax revenues used to calculate the Commonwealth's state tax revenue growth limit, as established in Chapter 62F, were $18.592 billion, exceeding the "permissible tax revenue" limit of $18.540 billion by $52.2 million. The excess amount was transferred to the Commonwealth's Temporary Holding Fund and subsequently transferred to the Stabilization Fund pursuant to Chapter 62F.

As of March 31, 2007, actual state tax revenue has not exceeded the permissible state tax revenue limit set by Chapter 62F.

COMMONWEALTH PROGRAMS AND SERVICES

The following table identifies certain major spending categories of the Commonwealth and sets forth the budgeted expenditures for each fiscal year within each category. In addition, budgeted expenditures and other uses are adjusted to reflect the school building assistance program payments from fiscal 2002 through fiscal 2004, had they been non-budgeted in those years as they are beginning in fiscal 2005 with the creation of the Massachusetts School Building Authority.

Commonwealth Expenditures—Budgeted Operating Funds (in millions)(1)

Expenditure Category	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007
Direct local aid	$4,823.7	$4,686.2	$4,382.6	$4,476.7	$4,618.8	$5,038.2
Medicaid(2)	5,259.3	5,485.1	5,742.4	5,977.2	6,852.5	7,581.8
Public assistance	1,029.6	1,019.0	1,019.1	1,095.9	1,129.0	1,259.7
Other health/human services	3,282.5	3,179.4	3,497.2	3,503.1	3,708.7	3,878.1
Debt service/contract assistance	1,415.4	1,480.9	1,569.2	1,738.8	1,826.7	2,092.1
Higher education	1,029.5	969.0	831.3	915.0	987.8	1,160.1
Group insurance	716.9	739.1	787.6	846.4	963.7	1,041.5
Public safety(3)	1,008.4	1,022.1	1,077.8	1,160.5	1,241.9	1,372.2
Other program expenditures	3,152.1	2,814.4	2,698.9	2,354.2	2,589.6	3,105.9
Budgeted pension transfers	795.8	813.5	701.9(4)	1,216.9	1,274.7	1,335.2
Inter-fund transfers to non-budgeted funds — other(5)	287.1	229.6	540.3	494.4	391.2	--
Budgeted Expenditures and Other Uses	$22,800.3	$22,439.1	$22,848.3	$23,779.1	$25,584.6	$27,865.0
Adjustment for items moved off-budget(6)	(365.4)	(383.2)	(551.4)(7)	--	--	--
Adjusted Budgeted Expenditures and Other Uses	$22,434.9	$22,055.9	$22,296.6	$23,779.1	$25,584.6	$27,865.0

SOURCES: Fiscal 2002-2006 Office of the State Comptroller; fiscal 2007 and off-budget adjustments, Executive Office for Administration and Finance.

(1) Totals may not add due to rounding. Table does not reflect inter-fund transfers among budgeted funds and other sources that have no effect on ending balances. Excludes certain miscellaneous taxes expended outside the budget process.

(2) Excludes off-budget Medicaid spending in fiscal 2003, 2004, 2005, 2006 and 2007 estimated at $201.4 million, $329.2 million, $422.2 million, $332.5 million and $359.4 million, respectively. Fiscal 2002 through 2004 also exclude budgeted expenditures for the administration of the Medicaid program. Fiscal 2005 through 2007 include program administration.

(3) Public Safety comprises expenditures for the Executive Office of Public Safety plus the Commonwealth's expenditures for sheriffs. Prior fiscal years have been restated to identify public safety spending.

(4) The fiscal 2004 general appropriations act funded the Commonwealth's scheduled pension obligation using $687.3 million in cash and a transfer of assets to the pension fund valued at $145 million. The asset transfer has not occurred and is not expected to occur. The amount in the table also includes non-contributory pensions paid from the General Fund.

(5) During the fiscal year, the Executive Office for Administration and Finance reflects certain off-budget uses of funds as offsets to non-tax revenues rather than inter-fund transfers to non-budgeted funds. At fiscal year end, the Office of the State Comptroller reflects these off-budget uses of funds as inter-fund transfers to non-budgeted funds, which in this table are reflected as additions to budgeted program expenditures.

(6) Includes expenditures for school building assistance in fiscal years preceding off-budget restructuring of these expenditures. The amounts are subtracted from the years in which they were incurred to facilitate trend analysis.

(7) Includes $150 million transferred from surplus for initial funding of grants by the MSBA.

Local Aid

Commonwealth Financial Support for Local Governments. The Commonwealth makes substantial payments to its cities, towns and regional school districts (local aid) to mitigate the impact of local property tax limits on local programs and services. Local aid payments to cities, towns and regional school districts take the form of both direct and indirect assistance. Direct local aid consists of general revenue sharing funds and specific program funds sent directly to local governments and regional school districts as reported on the so-called “cherry sheet” prepared by the Department of Revenue, excluding certain pension funds and non-appropriated funds. In fiscal 2007, approximately 18.8% of the Commonwealth’s projected budget is allocated to direct local aid.

As a result of comprehensive education reform legislation enacted in June, 1993, a large portion of general revenue sharing funds is earmarked for public education and is distributed through a formula specified in Chapter 70 of the General Laws designed to provide more aid to the Commonwealth’s poorer communities. The legislation requires the Commonwealth to distribute aid to ensure that each district reaches at least a minimum level of spending per public education pupil. Since fiscal 1994, the Commonwealth has fully funded the requirements imposed by this legislation in each of its annual budgets. For fiscal 2007, the Commonwealth will provide a total of $3.505 billion of state aid through the Chapter 70 program.

Several specific programs are also funded through direct local aid, such as public libraries, police education incentives and property tax abatement for certain elderly or disabled residents. Until creation of the MSBA in fiscal 2005, the state’s share of school building construction costs was also included in direct local aid. The State Lottery and Additional Assistance programs, which comprise the other major components of direct local aid, provide unrestricted funds for municipal use.

In addition to direct local aid, the Commonwealth has provided substantial indirect aid to local governments, including, for example, pensions for teachers, funding for road construction, funding for local water and sewer projects financed through the Massachusetts Water Pollution Abatement Trust, the costs of courts and district attorneys that formerly had been paid by counties and state tax receipts dedicated to the MBTA and MSBA.

Property Tax Limits. In November, 1980, voters in the Commonwealth approved a statewide tax limitation initiative petition, commonly known as Proposition 2½, to constrain levels of property taxation and to limit the charges and fees imposed on cities and towns by certain governmental entities, including county governments. Proposition 2½ is not a provision of the state constitution and accordingly is subject to amendment or repeal by the Legislature. Proposition 2½, as amended to date, limits the property taxes that may be levied by any city or town in any fiscal year to the lesser of (i) 2.5% of the full and fair cash valuation of the real estate and personal property therein or (ii) 2.5% over the previous year’s levy limit plus any growth in the tax base from certain new construction and parcel subdivisions. The law contains certain voter override provisions and, in addition, permits debt service on specific bonds and notes and expenditures for identified capital projects to be excluded from the limits by a majority vote at a general or special election. Between fiscal 1981 and fiscal 2006, the aggregate property tax levy grew from $3.347 billion to $9.983 billion, a compound annual growth rate of 4.47%.

Medicaid

The Commonwealth’s Medicaid program, also called MassHealth, provides health care to low-income children and families, certain low-income adults, disabled individuals and low-income elders. The program, which is administered by the Executive Office of Health and Human Services (EOHHS), receives 50% in federal reimbursement on most expenditures. Beginning in fiscal 1999, payments for some children’s benefits became 65% federally reimbursable under the State Children’s Health Insurance Program.

Over a quarter of the Commonwealth’s budget is devoted to Medicaid. It is the largest and has been one of the fastest growing budget items in the Commonwealth’s budget. Medicaid spending from fiscal 2002 to fiscal 2006 grew by 8.9% on a compound annual basis. During the same period, Medicaid enrollment increased 1.9% on a compounded annual basis. The Executive Office for Administration and Finance projects total fiscal 2007 expenditures for Medicaid to be $7.941 billion, an increase of 10.5% over fiscal 2006. As described below, health care reform legislation enacted in 2006 also restored and expanded eligibility, benefits and rates, beginning in fiscal 2007, by $308.3 million, $70.9 million of which will be expended from the off-budget Commonwealth Care Trust Fund. Adjusted for the new health care reform expansions in fiscal 2007, growth in Medicaid spending from fiscal

2006 to fiscal 2007 is projected to be 5.2%. MassHealth's projected spending for fiscal 2007 is in line with current projections.

Medicaid Program Growth in Expenditures and Enrollment

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007
Budgeted Medicaid program expenses (in millions) (1)	$5,259.30	$5,485.10	$5,742.40	$5,855.50	$6,725.80	$7,443.5
Budgeted Medicaid administrative expenses (in millions)	$46.3	$110.1	$105.1	$121.7	$126.2	$138.3
Off-budget Medicaid expenses (in millions)	--	$ 201.4	$ 329.2	$ 422.2	$ 332.5	$ 359.4
Total expenditures (in millions)	$5,305.6	$5,796.6	$6,176.7	$6,399.4	$7,184.5	$7,941.2
Annual percentage growth in total expenditures	13%	9%	7%	4%	12%	10.5%
Enrollment	1,004,679	986,601	951,960	986,386	1,040,640	1,085,800
Annual percentage growth in enrollment	6%	-2%	-4%	4%	6%	4%
Per-enrollee expenditures	$5,281	$5,875	$6,488	$6,488	$6,904	$7,314
Annual percentage growth in per-enrollee expenditures	7%	11%	10%	0%	6%	6%

SOURCE: Executive Office for Administration and Finance.

(1) Years prior to fiscal 2006 include accounts payable spending ($142 million in fiscal 2003, $251.9 million in fiscal 2004 and $110.3 million in fiscal 2005). Fiscal years 2006 and 2007 reflect spending through June 30, 2006 and June 30, 2007 respectively.

Medicaid spending varies by type of Medicaid member. Medicaid spending on disabled individuals and elders together accounts for 66% of total spending and 33% of total caseload. Low-income children and families account for only 30% of total Medicaid spending but 62% of total caseload. In fiscal 2006, close to 40% of total Medicaid expenditures were for nursing home care and prescription drugs.

In recent years, many Medicaid savings initiatives were directed at controlling the rate of growth for these services. Savings initiatives target service utilization, provider rates, benefits and, to a limited degree, member eligibility. Pharmacy utilization control measures include the implementation of the MassHealth drug list to steer pharmacy utilization toward the use of lower cost brand name and generic drugs and monitoring of prescription utilization. On January 1, 2006, the federal Centers for Medicare and Medicaid Services (CMS) implemented the Medicare drug benefit, or "Medicare Part D." The program offers prescription drug coverage to Medicare beneficiaries and shifts the coverage for dual-eligible Medicare/Medicaid beneficiaries from Medicaid to Medicare Part D plans. This change results in a $138 million and $296.2 million net savings to the Commonwealth's Medicaid program in fiscal 2006 and fiscal 2007, respectively. However, the Commonwealth is required to make a maintenance-of-effort, or "clawback," payment to CMS. The clawback payment was $90 million in fiscal 2006 and is projected at $224.2 million in fiscal 2007. The clawback is designed to capture a portion of states' Medicaid savings to help finance the new Medicare benefit. The Commonwealth does not receive federal reimbursement on the clawback payment.

In fiscal 2007, in accordance with health care reform legislation passed in April, 2006, certain benefits considered optional under federal law were restored and new benefits were added for MassHealth clients (see "Health Care Reform" below for additional details). As part of the renewed waiver agreement with CMS, MassHealth also raised the enrollment cap for its "Essential" population from 43,000 to 60,000 members. (The "Essential" population includes long-term unemployed adults, with incomes up to 100% of the federal poverty level, who are not disabled, between ages 19 and 65.) To date, approximately 10,100 Essential members previously waitlisted and receiving interim services from the Commonwealth's Uncompensated Care Pool (described below) are now enrolled in MassHealth and have access to preventive and emergency health care services.

In October, 2004, EOHHS implemented two policy initiatives intended to improve access to the Commonwealth's Medicaid program and more efficiently deliver services to patients. These initiatives have intentionally contributed to the increase in MassHealth caseload in fiscal 2005, 2006 and 2007. First, EOHHS integrated the application process for Medicaid and for the Uncompensated Care Pool, which has helped EOHHS identify Medicaid-eligible individuals when they seek services at hospitals and community health centers. Second, EOHHS implemented the "Virtual Gateway," an information system through which hospitals, community health centers and other outreach workers electronically file applications to EOHHS to determine whether an individual is eligible for Medicaid or the Pool. This combined electronic application also now supports a component of the state's 2006 health care reform legislation, the Commonwealth Care program which was implemented in October, 2006. Both of these initiatives have contributed to higher Medicaid enrollment and, importantly, to a proportionate decrease in free-care utilization and costs, which is consistent with the Commonwealth's intention to direct Uncompensated Care Pool users into MassHealth and Commonwealth Care, in order to provide better management of care and reduce higher cost emergency utilization.

Three-year Renewal of 1115 Demonstration Project. On January 26, 2005 CMS approved a three-year extension of the Commonwealth's 1115 Demonstration Project ("waiver") under which the Commonwealth has operated its Medicaid program. The extension period runs from July 1, 2005 through June 30, 2008.

A major component of the renewal negotiations dealt with the state's funding mechanism for hospital and managed cared organization (MCO) supplemental payments. Supplemental payments are in addition to ordinary Medicaid rate payments for providing care to Medicaid members. The Commonwealth had used funding provided by other government entities (primarily local governments and the state-owned medical school) as the non-federal share of these supplemental Medicaid payments. The transfer of the non-federal share to the Medicaid agency to fund supplemental payments is called an inter-governmental transfer (IGT).

As a part of the 1115 waiver renewal negotiations, the Commonwealth and CMS agreed to sunset IGT's as a mechanism for financing the non-federal share of hospital supplemental payments effective June 30, 2005 and of supplemental payments to Medicaid MCO's effective June 30, 2006. In and of itself, sunsetting the IGT funding mechanism and, as a result, ending the associated supplemental payments would have had no net effect on the Commonwealth's financial condition because both spending and revenue would have been reduced by an equal amount. However, since the termination of supplemental payments would be disruptive to the Commonwealth's safety net hospital system, the Commonwealth has worked to identify alternative non-federal funding mechanisms to use in place of IGT's in order to resume supplemental payments to certain hospitals. The 1115 Demonstration Project waiver renewal also allowed for a mechanism by which the Commonwealth could continue to receive federal funding available prior to the IGT changes. CMS agreed to provide federal reimbursement on certain fully state-funded health care programs already operated by the Commonwealth (known as "Designated State Health Programs"). In fiscal 2007, the Commonwealth expects to receive $191.1 million in federal reimbursement on these Designated State Health Programs.

The waiver renewal directs certain funding within the Demonstration Project for the establishment of a fund, called the Safety Net Care Pool, dedicated to reducing the rate at which Massachusetts residents are uninsured. The availability of these funds is subject to the conditions generally described herein. Expenditures from this fund may only be used for the provision of health care services to uninsured individuals and for unreimbursed Medicaid costs. The funds can be used through any type of provider or through insurance products. The Commonwealth is planning to use the Safety Net Care Pool to fund part of the Uncompensated Care Pool (described below), the Commonwealth Care Health Insurance Program (described below), certain supplemental hospital payments and the Designated State Health Programs.

The total allotment for the Safety Net Care Pool is $1.34 billion per year in spending and about one-half that amount in federal reimbursements in each year of the extension period. The actual amount of dollars in the fund was set by the amount of state fiscal 2006 supplemental payments made to the Medicaid MCOs, $770 million, and the state's federal fiscal year 2005 disproportionate share hospital allotment of $574.5 million.

The Safety Net Care Pool is a capped pool of expenditures, but part of the larger federal budget neutrality calculation. As part of all 1115 Demonstration Waivers, CMS requires states to demonstrate that the waiver program is budget neutral to the federal government, meaning that costs to the federal government under the waiver program will be no more than what they would have been in the absence of the waiver program. The Commonwealth currently projects waiver spending through the period ending June 30, 2008 to be $70 million below to $270 million above the federal budget neutrality ceiling. This calculation is based on various assumptions of MassHealth spending, enrollment and utilization. During fiscal years 2007 and 2008, the Commonwealth will continue to track assumptions and actual expenditures to ensure that waiver spending complies with federal requirements.

Uncompensated Care Pool. The Uncompensated Care Pool reimburses acute care hospitals and community health centers in Massachusetts for eligible services provided to low-income uninsured and underinsured people. In Pool fiscal year 2006 (October 1, 2005 through September 30, 2006), the Pool paid for approximately 34,000 inpatient and 1.2 million outpatient visits for nearly 450,000 individuals. Pool fiscal year 2007 is projecting to serve 406,000 individuals. Community health centers continue to be paid on a fee-for-service basis, up to an annual cap. Revenues into the Pool include state funds, hospital assessments and surcharge payer assessments.

The Governor's fiscal 2008 budget recommends $353.9 million for payments made during Pool fiscal year 2008 for free care provided at acute care hospitals and community health centers. The fiscal 2008 budget approved by the House of Representatives on April 27, 2007 is consistent with this recommendation. This recommendation reflects several changes that will occur as a result of the 2006 health care reform legislation, including:

- the Uncompensated Care Pool will transition to the Health Safety Net Trust Fund (described below),
- the payment methodology will transition to a claims-based (or retrospective) system and
- users will be transitioned from the Health Safety Net Trust Fund into health insurance programs, including the Commonwealth Care Health Insurance Plan.

Health Care Reform Legislation. In April, 2006, legislation was enacted to reform health care by mandating that individuals 18 years and older purchase insurance, while offering subsidized coverage to uninsured residents whose income falls below 300% of the federal poverty level and providing new, affordable products for uninsured residents whose income exceeds this threshold. The reform asks employers to play a role by requiring that businesses with 11 or more full-time employees either contribute to coverage or pay an assessment. These businesses must also establish a mechanism wherein employees can pay for health insurance coverage on a pre-tax basis. Businesses that are subject to this requirement but do not comply may potentially face a surcharge. The legislation also created the Commonwealth Health Insurance Connector Authority (Connector), charged with linking uninsured residents to affordable, and in some cases subsidized, coverage.

The Commonwealth began implementing health care reform shortly after its enactment. The legislation included many new concepts and initiatives, including the restoration and expansion of several MassHealth programs. As of May 1, 2007, over 69,000 residents have been enrolled in the subsidized Commonwealth Care Health Insurance Program, and MassHealth has enrolled 57,135 people, including over 25,000 children, since enactment of the legislation. On May 1, 2007, the Connector also launched the Commonwealth Choice program to offer individuals a range of unsubsidized affordable health insurance plans. The Connector board continues to examine and make policy decisions and to monitor conversions from the Uncompensated Care Pool into the Commonwealth Care Health Insurance Program, as well as new enrollees who did not previously access care through the Pool.

The Commonwealth continues to monitor closely the current and projected costs of health care reform. The following table shows the projected incremental cost from fiscal 2006 through fiscal 2008 (as included in the Governor's fiscal 2008 budget recommendations) only in the components of the Massachusetts health care financing system changed by the health care reform legislation. Fiscal 2007 costs and revenues include the changes directly driven by the legislation and in some cases also include inflation that would have occurred in the absence of the health care reform legislation. Other costs attributable to the existing MassHealth program but not directly affected by the legislation are not included in the table.

Health Care Reform Spending and Revenue (in millions)

	Fiscal 2006	Fiscal 2007	Fiscal 2008
Revenue Categories			
MassHealth restoration and expansion	$	$ 154.2	$ 257.2
Acute care hospitals and community health centers	580.6	914.4	785.8
Commonwealth Care Health Insurance Program	-	77.0	232.0
Health program investments	808.5	6.1	1.5
Other revenue	$ 70.0	221.1	185.0
Total Revenue	$1,459.1	$1,372.7	$1,461.6
Spending Categories			
MassHealth restoration and expansion	$	$ 308.3	$ 514.4
Acute care hospitals and community health centers	567.0	1,140.8	873.7
Commonwealth Care Health Insurance Program	-	152.8	471.9
Health program investments	770.0	71.4	14.7
Total Spending	$1,337.0	$1,673.3	$1,874.6
Net Impact on General Fund	**$ 122.1**	**$(300.6)**	**$ (413.1)**

SOURCE: Executive Office for Administration and Finance.

The spending projections in the table above include the following elements: Spending for MassHealth restoration and expansion includes $142.2 million in fiscal 2007 and $224.2 million in fiscal 2008 for restored and expanded eligibility and member benefits, $95.3 million in fiscal 2007 and $149.3 million in fiscal 2008 for Medicaid managed care organization rate increases and $70.9 million in fiscal 2007 and $140.9 million in fiscal 2008 for hospital and physician rate increases. Spending for acute care hospitals and community health centers includes $577.3 million in fiscal 2007 and $414.6 million in fiscal 2008 for uncompensated care, $526 million in fiscal 2007 and $431 million in fiscal 2008 for acute hospital supplemental payments and $38 million in fiscal 2007 and $28 million in fiscal 2008 for essential community provider trust fund grants. Spending for the Commonwealth Care Health Insurance Program includes $127.8 million in fiscal 2007 and $472 million in fiscal 2008 for premium assistance payments, as well as $25 million in fiscal 2007 for start-up administrative costs at the Commonwealth Health Insurance Connector Authority. Spending for health program investments includes $25 million in fiscal 2007 and $14.7 million in fiscal 2008 for spending within state agencies, $13 million in fiscal 2007 for a health care reform implementation reserve account and $33.4 million in fiscal 2007 for planned surplus transfers to the Commonwealth Care Trust Fund.

The Commonwealth generally expects to receive federal financial participation in an amount equal to 50% of these expenditures, excluding essential community provider grants. As noted above, the Commonwealth expects to benefit from $191.1 million of federal reimbursements for costs that have previously not qualified for federal funds. After fiscal 2007, premium assistance payments are expected to be funded in part by redeployment of existing funds previously used to reimburse hospitals for free care. The Governor's fiscal 2008 budget recommendations project that nearly 100,000 current users of the Uncompensated Care Pool whose income falls below 300% of the federal poverty level will become members of the Commonwealth Care Health Insurance Program.

The health care reform legislation is also expected to result in a reduction in tax revenues starting in fiscal 2008, due to increased pre-tax spending on health insurance premiums by employees and businesses in the Commonwealth. The January 30,2007 consensus revenue estimate includes a downward adjustment of $20 million to account for any potential impact of the legislation.

Review of Targeted Case Management Services Rendered by Department of Social Services. The federal Department of Health and Human Services, Office of the Inspector General (OIG), has issued a final audit report and recommendation concerning whether services provided by the Department of Social Services were properly claimed as Medicaid reimbursable Targeted Case Management services. With regard to such services, the OIG's final report recommends that CMS disallow $86.0 million in federal financial participation (FFP) claimed in federal fiscal years 2002 and 2003. The OIG expressed no opinion about an additional $13.0 million in FFP claimed over the same period. If CMS accepts the OIG's recommendation, the Commonwealth expects to challenge such disallowance and believes there is a strong legal basis to support such a challenge. Given the OIG's audit report findings, Targeted Case Management services claims for subsequent periods (which may equal or exceed the annual amounts at issue in the audit report) potentially could be at issue in the future.

CMS asserted in June, 2000 that the portion of the Medicaid program funded by the Commonwealth's Uncompensated Care Pool might violate federal regulations regarding impermissible taxes on health care providers. Since 1993, the Commonwealth has been seeking a federal waiver for the Commonwealth's assessment on acute care hospitals to fund the Uncompensated Care Pool. EOHHS believes that the assessment complies with the federal law pertaining to provider taxes. Under federal regulations, if the Commonwealth were ultimately determined to have imposed an impermissible provider tax, the federal government could seek retroactive repayment of federal Medicaid reimbursements, although EOHHS believes any remedy imposed would likely be prospective and not retroactive. From 1993, when the first waiver request was submitted, through fiscal 2000, the Commonwealth received an estimated $1.068 billion in federal Medicaid reimbursements related to expenditures associated with the Uncompensated Care Pool. The Commonwealth has continued to collect approximately $40 million per fiscal quarter for each quarter since fiscal 2000. Many other states have provider taxes similar to the one funding the uncompensated care pool, and CMS' interpretation of this area of federal law continues to evolve. As a result, resolution of this issue could take several years. In the fall of 2004 and again in the fall of 2005 CMS posed questions regarding the funding mechanism for the uncompensated care pool, but CMS has not taken any further action in regard to this matter.

Prescription Advantage Program. The Prescription Advantage Program (formerly known as the Senior Pharmacy Program) began in April, 2001 and is currently administered by the Executive Office of Elder Affairs. In fiscal 2006 spending for the program was $91.0 million. Fiscal 2007 spending is projected at approximately $63.5 million.

The Prescription Advantage Program has been affected by federal implementation of Medicare Part D, which began January 1, 2006. Prescription Advantage has shifted from providing primary drug coverage to becoming a secondary payer for members eligible for Medicare Part D. The Program also provides gap coverage for members who spend between $2,250 and $5,100 per year, expenditures that are not covered by Medicare Part D. Fiscal 2007 Prescription Advantage Program spending is expected to decrease by $27.5 million from spending in fiscal 2006, reflecting the first full year of Medicare Part D implementation.

Public Assistance

The Commonwealth administers four major programs of income assistance for its poorest residents: Transitional Aid to Families with Dependent Children (TAFDC), Emergency Assistance, Emergency Aid to the Elderly, Disabled and Children (EAEDC) and the state supplement to federal Supplemental Security Income (SSI). The following table illustrates the recent expenditures within these categories.

Public Assistance Program Expenditures (in millions)

Category of Public Assistance	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007
TAFDC(1)	$417.9	$404.9	$404.5	$467.9(2)	$467.2	$475.0
Child care	338.4	332.8	338.7	348.8	373.5	494.0(3)
EAEDC	64.0	67.6	66.8	66.8	72.0	73.6
SSI	209.3	209.7	209.1	212.4	216.2	217.1
Total	$1,029.6	$1,019.0	$1,019.1	$1,095.9	$1,128.9	$1,259.7

SOURCES: Fiscal 2002-2006, Office of the Comptroller; fiscal 2007, Executive Office for Administration and Finance.
(1) Includes expenditures for TAFDC, ESP and Emergency Assistance.
(2) Includes program administrations cost of $64.3 million which had not been included in prior years.
(3) Includes program administration and related or support costs of $79.2 million which had not been included in prior years.

TAFDC expenditures in fiscal 2007 are estimated to be $475 million, approximately $7.8 million, or 1.0%, more than in fiscal 2006. The Emergency Assistance program provides disaster relief and shelter to homeless families. The cost of this program is included in the TAFDC expenditure category above.

The Commonwealth is federally required to provide child care to TAFDC recipients and those transitioning off TAFDC for up to one year. In addition, the Commonwealth provides child care assistance to income eligible families. Total child care expenditures for fiscal 2007 are projected to be $494.0 million, including $79.2 million for program administration which was not included in prior years. Fiscal 2006 expenditures were $373.5 million.

The Commonwealth provided approximately 22,360 childcare slots for TAFDC recipients and 24,213 child care slots for income-eligible families in 2006. The Commonwealth projects that it will provide approximately 25,984 child care slots to TAFDC recipients and 24,871 childcare slots for income-eligible families in fiscal 2007. The Commonwealth has met federal requirements for child care in the past three fiscal years.

Fiscal 2007 expenditures for EAEDC are projected to be $73.6 million, up $1.6 million, or 2.2%, from fiscal 2006. Caseload is projected to increase 2.7%.

SSI is a federally administered and funded cash assistance program for individuals who are elderly, disabled or blind. SSI payments are funded entirely by the federal government up to $530 per individual recipient per month and entirely by the state above that amount. The additional state supplement ranges from $39 to $454 per month per recipient. Fiscal 2007 expenditures for SSI are estimated to be $217.1 million. Fiscal 2006 expenditures were $216.2 million.

The following table illustrates the trend in caseload for public assistance programs:

Public Assistance Average Caseload

Category of Public Assistance	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007
TAFDC(1)	45,432	47,821	48,541	49,069	47,340	44,970
EAEDC	14,967	15,999	17,058	17,188	16,668	17,120
SSI(2)	163,566	163,713	164,729	166,112	167,481	171,195
Total	223,965	226,536	230,328	231,369	231,489	233,285

SOURCE: Department of Transitional Assistance.
(1) TAFDC caseload estimates do not include the Emergency Assistance caseload.
(2) SSI caseload does not include blind recipients whose benefits are administered by the Massachusetts Commission for the Blind.

Federal Welfare Reform. The federal welfare reform legislation that was enacted on August 22, 1996 eliminated the federal entitlement program of Aid to Families with Dependent Children and replaced it with block grant funding for Transitional Assistance to Needy Families (TANF). The TANF program replaced Title IV-A of the Social Security Act and allows states greater flexibility in designing programs that promote work and self-sufficiency. The block grant for the Commonwealth was established at $459.4 million annually for federal fiscal years 1997 through 2006. The Commonwealth must meet federal maintenance-of-effort requirements in order to be eligible for the full TANF grant award. The Commonwealth successfully met the requirements in each of the federal fiscal years 1997 through 2006. The Commonwealth also received approximately $101 million in child care block grant funds in fiscal 2006 to support child care programs. The federal waiver that has allowed the Commonwealth to calculate work participation rates using a more lenient method of assessment expired in fiscal 2006, with no major fiscal implications for fiscal 2006 or fiscal 2007. In February, 2006, federal legislation reauthorized the TANF block grant providing $459.4 million annually to the Commonwealth for the next five years, provided that the Commonwealth meets federal work requirements outlined below.

TANF Work Requirements. Federal legislation has been enacted that alters significantly the requirements on states administering the TANF program. The changes concerning federal work participation rates require that Massachusetts increase its current work participation rate from 15% to 50% for all TANF families and 90% for two-parent families beginning in federal fiscal year 2007. The federal work participation rate is calculated by dividing the number of individuals participating in countable work activities for the required number of hours by the total number of work-eligible individuals in the program. If either rate is not achieved, the federal government will require that the Commonwealth increase its maintenance-of-effort funding by 5% of the 1994 base year, or $24 million. In addition, the federal government would reduce its TANF grant by up to 5%. Massachusetts would be required to increase its maintenance-of-effort spending to offset the federal penalty. The penalties and increased maintenance-of-effort requirement would continue each year that compliance is not realized, with the federal penalties increasing two percentage points each year to a maximum of 21% of the TANF block grant. It is anticipated that the Commonwealth will meet the work participation rate in federal fiscal year 2007 through the identification of countable state spending that offsets the participation rate. As excess existing maintenance-of-effort spending has been identified, there is no anticipated revenue loss in either fiscal 2007 or fiscal 2008.

The Department of Transitional Assistance has been working on initiatives to move toward compliance with the federal work participation standards within the provisions of existing state law. These include efforts designed to engage more individuals in qualifying activities and to align program and funding structures, in compliance with federal regulations, to both minimize the number of individuals in the calculation that are not participating and maximize the number that are meeting the federal requirement.

Other Controls and Reforms. The Department of Transitional Assistance in recent years has instituted tighter procedures and management controls. Stricter standards have been established to determine eligibility for TAFDC, Emergency Assistance and EAEDC benefits. The Department of Transitional Assistance also has instituted automated systems to re-determine eligibility for benefits and has taken steps to reduce welfare fraud. In addition, the Department of Revenue has improved its collection of child support payments.

Other Health and Human Services

In fiscal 2006, other health and human services spending included expenditures for the Department of Mental Retardation ($1.130 billion), Department of Mental Health ($603.3 million), Department of Social Services ($722.3 million), Department of Public Health ($454.6 million) and other human services programs ($690.6 million).

In fiscal 2007, other health and human services spending includes expenditures for the Department of Mental Retardation (projected to be $1,192.4 billion), Department of Mental Health (projected to be $658.7 million), Department of Social Services (projected to be $782.2 million), Department of Public Health (projected to be $520.6 million) and other human services programs (projected to be $798.5 million).

Debt Service

Debt service expenditures relate to general obligation bonds, special obligation bonds and federal grant anticipation notes issued by the Commonwealth. See "LONG-TERM LIABILITIES."

Pension and Other Post-Retirement Benefit Obligations

Almost all non-federal public employees in Massachusetts participate in defined-benefit pension plans administered pursuant to state law by 106 public retirement systems. The Commonwealth is responsible for the payment of pension benefits for Commonwealth employees (members of the state employees' retirement system) and for teachers of the cities, towns and regional school districts throughout the state (including members of the teachers' retirement system and teachers in the Boston public schools, who are members of the State-Boston retirement system but whose pensions are also the responsibility of the Commonwealth). Employees of certain independent authorities and agencies, such as the Massachusetts Water Resources Authority and of counties, cities and towns (other than teachers) are covered by 104 separate retirement systems. Pension benefits for state employees are administered by the State Board of Retirement, and pension benefits for teachers are administered by the Teachers' Retirement Board. Investment of the assets of the state employees' and teachers' retirement systems is managed by the Pension Reserves Investment Management Board. In the case of all other retirement systems, the retirement board for the system administers pension benefits and manages investment of assets. Many such retirement boards invest their assets with the Pension Reserves Investment Management Board, and the Governor has proposed legislation mandating that certain underperforming boards do so. With a very small number of exceptions, the members of these state and local retirement systems do not participate in the federal Social Security System.

Legislation approved in 1997 provided, subject to legislative approval, for annual increases in cost-of-living allowances equal to the lesser of 3% or the previous year's percentage increase in the United States Consumer Price Index on the first $12,000 of benefits for members of the state employees' and teachers' retirement systems. The Commonwealth pension funding schedule (discussed below) assumes that annual increases of 3% will be approved for its retirees. The fiscal 2006 general appropriations act authorized a 3% cost of living increase. Local retirement systems that have established pension funding schedules may opt in to the requirement as well, with the costs and actuarial liabilities attributable to the cost-of-living allowances required to be reflected in such systems' funding schedules. Legislation approved in 1999 allows local retirement systems to increase the cost-of-living allowance up to 3% during years that the previous year's percentage increase in the United States Consumer Price Index is less than 3%.

Employee Contributions. The state employees' and teachers' retirement systems are partially funded by employee contributions of regular compensation – 5% for those hired before January 1, 1975, 7% for those hired from January 1, 1975 through December 31, 1983, 8% for those hired from January 1, 1984 through June 30, 1996 and 9% for those hired on or after July 1, 1996, plus an additional 2% of compensation above $30,000 per year for all those members hired on or after January 1, 1979. Employee contributions are 12% of compensation for members of the state police hired after July 1, 1996. Legislation enacted in fiscal 2000 establishing an alternative superannuation retirement benefit program for members of the teachers' retirement system and teachers of the State-Boston retirement system mandates that active members who opt for the alternative program and all teachers hired on or after July 1, 2001 contribute 11% of regular compensation. Members who elect to participate are required to make a minimum of five years of retirement contributions at the 11% rate. Approximately 45,000 active teachers joined the enhanced benefit program and will retire under the terms of the program over the next 30 years.

Early Retirement Incentive Program. As a means of reducing payroll costs in fiscal 2002 and 2003, the Commonwealth adopted two early retirement incentive programs, each of which offered an enhanced pension benefit to retirement-eligible employees. The Public Employee Retirement Administration Commission (PERAC) has reported that the 2002 program resulted in an increased actuarial liability of $312.2 million and that the 2003 program resulted in an increased actuarial liability of $224.8 million.

Unfunded Actuarial Accrued Liability. The retirement systems were originally established as "pay-as-you-go" systems, meaning that amounts were appropriated each year to pay current benefits, and no provision was made to fund currently the future liabilities already incurred. In fiscal 1978 the Commonwealth began to address the unfunded liabilities of the two state systems by making appropriations to pension reserves. Prior to the establishment of the pension funding program described below, the Commonwealth appropriated approximately $680 million to the pension reserves during the mid-1980's, in addition to the pay-as-you-go pension costs during those years. Comprehensive pension funding legislation was approved in January, 1988 to require the Commonwealth to fund future pension liabilities currently and to amortize the Commonwealth's accumulated unfunded liability. Under current law such unfunded liability is required to be amortized to zero by June 30, 2023.

The Secretary of Administration and Finance is required by law to prepare a funding schedule providing for both the normal cost of Commonwealth benefits (normal cost being that portion of the actuarial present value of pension benefits which is allocated to a valuation year by an actuarial cost method) and the amortization by June 30, 2023, of the unfunded actuarial liability of the Commonwealth for its pension obligations. The funding schedule is required to be updated periodically on the basis of new actuarial valuation reports prepared under the direction the Secretary of Administration and Finance. Funding schedules are to be filed with the Legislature triennially by January 15 and are subject to legislative approval. If a schedule is not approved by the Legislature, payments are to be made in accordance with the most recently approved schedule at a level at least equal to the prior year's payments.

The current funding schedule, approved for fiscal 2005, is based upon a January 1, 2004 actuarial valuation. The assumptions underlying the new funding schedule retain the 2023 date for fully amortizing the unfunded liability and utilize an amortization growth rate of 4.5% per year. The schedule is as follows:

Funding Schedule for Pension Obligations (in thousands)

Fiscal Year	Payments	Fiscal Year	Payments
2005	$1,216,936	2015	$1,936,059
2006	1,274,675	2016	2,028,266
2007	1,335,176	2017	2,124,903
2008	1,398,573	2018	2,226,183
2009	1,465,004	2019	2,332,332
2010	1,534,617	2020	2,443,587
2011	1,607,565	2021	2,560,194
2012	1,684,010	2022	2,682,414
2013	1,764,121	2023	2,810,519
2014	1,848,075		

SOURCE: Executive Office for Administration and Finance.

It is expected that the next funding schedule will be submitted in January, 2008 for use in connection with the fiscal 2009 budget.

Valuation of Pension Obligation. On September 26, 2006, PERAC released its actuarial valuation of the total pension obligation as of January 1, 2006. The unfunded actuarial accrued liability as of that date for the total obligation was approximately $14.488 billion, including approximately $3.769 billion for the State Employees' Retirement System, $9.104 billion for the Massachusetts Teachers' Retirement System, $1.182 billion for Boston Teachers and $433.0 million for cost-of-living increases. The valuation study estimated the total actuarial accrued liability as of January 1, 2006 to be approximately $50.865 billion (comprised of $20.407 billion for state employees, $27.788 billion for state teachers, $2.237 billion for Boston Teachers and $433.0 million for cost-of-living increases). Total assets were valued at approximately $36.376 billion based on a five-year average valuation method, which equaled 93.2% of the January 1, 2006 total asset market value.

The following table shows the valuation of accrued liabilities and assets from 2002 through 2006:

Pension Fund Valuation and Unfunded Accrued Liabilities (in millions)

			Unfunded Accrued Liabilities		
Valuation Date	Total Actuarial Accrued Liability	Actuarial Value of Assets(1)	Unfunded Actuarial Liability(2)	Market Value of Unfunded Liability	Valuation Date
January 1, 2002	$39,067	$31,699	$7,369	$10,359	January 1, 2002
January 1, 2003	43,030	29,629	13,401	17,266	January 1, 2003
January 1, 2004	46,059	34,045	12,014	14,350	January 1, 2004
January 1, 2005	48,358	34,939	13,419	12,861	January 1, 2005
January 1, 2006	50,865	36,377	14,488	11,844	January 1, 2006

SOURCE: Public Employee Retirement Administration Commission.

(1) Based on five-year average smoothing methodology.
(2) Based on actuarial valuation.

The existing funding schedule is based on the January 1, 2003 actuarial liability brought forward on an estimated basis to January 1, 2004 and on asset values on January 1, 2004.

On March 15, 2007, the Public Employee Retirement Administration Commission (PERAC) released an actuarial valuation dated January 1, 2007 of the State Employee's Retirement System's portion of the total pension obligation. The valuations of the Massachusetts Teachers' Retirement System and Boston Teachers' portions, as well as local cost-of-living adjustments, which together represent more than half of the total valuation, are expected to be released in September, 2007. The unfunded actuarial accrued liability as of January 1, 2007 for the State Employees' Retirement System was $3.2 billion; the total actuarial accrued liability for this system as of January 1, 2007 was $21.7 billion. The valuation method was the same as the method used in the 2006 valuation, except that the actuarial value of assets was determined so as not to be less than 90% or greater than 110% of market value. In prior valuations, the asset corridor was 85% to 115% of the market value. This change resulted in a decrease in unfunded liability of $295 million.

Other Post Employment Benefits (OPEB). New accounting standards will require the Commonwealth to begin disclosing its liability for other post-employment benefits (commonly referred to as "OPEB") in its fiscal 2008 financial reports. An initial valuation report by an independent actuarial firm of the Commonwealth's liability for these health care and life insurance benefits was released in June, 2006. The report presented two separate calculations of the Commonwealth's OPEB liability, depending on whether the liability would be pre-funded in a manner meeting the requirements of GASB Statement No. 45.

According to the June, 2006 report, assuming no pre-funding, the actuarial accrued liability of the Commonwealth for OPEB obligations earned through January 1, 2006 is $13.287 billion. If pre-funding is assumed, the actuarial accrued liability is reduced to $7.562 billion. This difference is solely attributable to the standards requirement that a lower discount rate must be used without pre-funding. Under pre-funding, the annual required contribution was calculated in June, 2006 to commence at $702.9 million for fiscal 2006 and projected to increase to $1.205 billion for fiscal 2016. The independent actuarial firm updated these projections on January 24, 2007 for the purpose of providing estimates for the Governor's fiscal 2008 budget recommendations. If pre-funding is assumed, the annual required contribution was calculated to be $763.1 million in fiscal 2008, increasing to $1.223 billion in fiscal 2016.

Should the Commonwealth not fully fund the amortization of the actuarial liability, a liability for the difference between the amount funded and the actuarially required contribution will be reflected on the Commonwealth's statement of net assets, as presented on a GAAP basis. The liability will increase or decrease each year depending on the amount funded, investment return and changes in amortization and assumptions. This change in liability will be reflected either as a revenue or expense item in the Commonwealth's statement of activities as presented on a GAAP basis, dependent on these factors. The January 24, 2007 update reported that if no pre-funding is assumed, the Commonwealth will be required to record a projected $1.203 billion expense in fiscal 2008, increasing to $2.818 billion in fiscal 2016.

In making these calculations, the independent actuarial firm utilized employment and other data provided by the Commonwealth and assumed annual claims growth initially at 10.5% and declining to 5% after ten years and continuation of current benefit levels and current retiree contribution requirements.

The independent actuarial report covered only the Commonwealth's OPEB obligations for Commonwealth employees and their survivors. Municipalities and authorities of the Commonwealth, even if their health care coverage is administered by the Group Insurance Commission, will perform their own valuations, as the Commonwealth acts only as an agent for these entities with respect to OPEB and does not assume the risk or financial burden of their health care costs.

The difference between the value of pre-funded and non-pre-funded OPEB liabilities is due to the discount rate used in the calculation. In the absence of pre-funding, the discount rate must approximate the Commonwealth's rate of return on non-pension (liquid) investments over the long term, estimated at 4.5% for the purpose of this study. In the event of pre-funding, the discount rate would increase to a standard return on long-term investments, estimated at 8.25% for the purpose of this study. In order to qualify its OPEB liabilities as pre-funded, the Commonwealth would have to enact legislation providing for the escrowing of annual contributions in a qualifying trust in accordance with the requirements of GASB Statement No. 45 (and similar to the program for funding the Commonwealth's unfunded actuarial liability for pensions).

GASB Statement No. 45 requires that OPEB obligations be recalculated at two-year intervals. Such calculations may be affected by many factors, including changing experience and assumptions regarding future health care claims, by whether or not the Commonwealth enacts legislation that qualifies its OPEB obligations to be calculated on a pre-funded basis, by changes in the Commonwealth's employee profile and possibly by changes in OPEB coverage levels and retiree contribution requirements. Accordingly, it should be anticipated that the actuarial accrued liability of the Commonwealth for OPEB liabilities may fluctuate.

A copy of the June, 2006 valuation report discussed above may be viewed at the website of the Comptroller of the Commonwealth at http://www.mass.gov/osc. Click on "Financial Reports/Audits."

In his fiscal 2008 budget recommendations, the Governor has proposed beginning to pre-fund the Commonwealth's OPEB liability and escrowing these pre-funding contributions in a qualifying trust in a manner meeting the requirements of GASB Statement No. 45. The House budget for fiscal 2008 also provides for the establishment of a qualifying trust but does not provide for pre-funding of the unfunded liability. See "FISCAL 2007 AND FISCAL 2008 - Fiscal 2008 Budget Proposals."

Group Insurance

The Group Insurance Commission (GIC) provides health insurance benefits to approximately 286,000 active and retired state employees and their dependents. Currently the GIC has a tiered structure for employee contributions to health coverage. All employees hired on or before June 30, 2003 contribute 15% of total premium costs. All employees hired after June 30, 2003 pay 20% of premium costs.

For fiscal 2006, the Commission spent $890 million to provide health coverage to these groups. For fiscal 2007, the Commission projects to spend $1.042 billion, an increase of 17% over fiscal year 2006. Beginning in January, 2007, the employees of the city of Springfield began accessing health coverage through the GIC, with the costs of coverage of the city's employees fully covered by the city and employee contributions. The city is expected to realize cost savings on account of the GIC's expansive purchasing pool, and the Legislature is considering proposals to permit other cities and towns to access coverage through the Commission.

Public Safety

The Commonwealth of Massachusetts expended a total of $1.242 billion in fiscal 2006 for the Executive Office of Public Safety and sheriffs and expects to spend $1.372 billion in fiscal 2007. Twelve state agencies fall under the umbrella of the Executive Office of Public Safety. The largest is the Department of Correction, which operates 18 correctional facilities and centers across the Commonwealth, expending $444.5 million in fiscal 2006 and a projected $460.9 million in fiscal 2007. Other public safety agencies include the State Police, which expended $260 million in fiscal 2006 and is projected to spend $286.3 million in fiscal 2007, the Parole Board, the Department of Fire Services, the Military Division, the Office of the Chief Medical Examiner and six other public safety related agencies. In addition to expenditures for these twelve state public safety agencies, the Commonwealth provides funding for the operation of 16 regional jails and correctional facilities that are managed by independently elected sheriffs, for which the Commonwealth expended $235.2 million in fiscal 2006 and projects spending of $251.2 million in fiscal 2007. Expenditures for all other public safety agencies totaled $302.2 million for fiscal 2006 and are projected at $373.6 million for fiscal 2007.

Higher Education

Fiscal 2006 spending on higher education was $987.8 million. Fiscal 2007 spending is projected to be $1.160 billion. The Commonwealth's system of higher education includes the five-campus University of Massachusetts, nine state colleges and 15 community colleges. The system is coordinated by the Board of Higher Education, and each institution is governed by a separate board of trustees. The Board of Higher Education appoints a chancellor of the system of public higher education, who is responsible for carrying out the policies established by the board.

The operating revenues of each institution consist primarily of state appropriations and of student and other fees that may be imposed by the board of trustees of each institution. Tuition levels are set by the Board of Higher Education. Tuition revenue is required to be remitted to the State Treasurer by each institution; however, the Massachusetts College of Art and the Massachusetts Maritime Academy have the authority to retain tuition through fiscal 2008. The University of Massachusetts-Amherst and the Massachusetts College of Liberal Arts is authorized to retain out-of-state tuition through fiscal 2007. The board of trustees of each institution submits annually audited financial statements to the Comptroller and the Board of Higher Education. The Board of Higher Education prepares annual operating budget requests on behalf of all institutions, which are submitted to the Executive Office for Administration and Finance and to the House and Senate Committees on Ways and Means. The Legislature appropriates funds for the higher education system in the Commonwealth's annual operating budget in various line items for each institution.

Other Program Expenditures

The remaining expenditures on other programs and services for state government amounted to $2.590 billion in fiscal 2006 and are projected to be $3.104 billion in fiscal 2007, including the judiciary ($658.6 million in fiscal 2006 and $800 million in fiscal 2007), district attorneys ($85.7 million in fiscal 2006 and $93 million in fiscal 2007), the Attorney General ($37.1 million in fiscal 2006 and $38.1 million in fiscal 2007), the Executive Office for Administration and Finance ($485.6 million in fiscal 2006 and $460.8 million in fiscal 2007), the Executive Office of Energy and Environmental Affairs ($199.8 million in fiscal 2006 and $269.8 million in fiscal 2007), the Executive Office of Transportation and Public Works ($213 million in fiscal 2006 and $300.6 million in fiscal 2007), the Department of Housing and Community Development ($117.2 million in fiscal 2006 and $184.6 million in fiscal 2007) and various other programs ($792.6 million in fiscal 2006 and $957.5 million in fiscal 2007).

Unemployment Trust Fund

As of March 31, 2007, the overall balance in the Unemployment Trust Fund was $721.5 million. Under current economic conditions, the Division of Unemployment Assistance projects that the fund will not experience a cash deficit in fiscal 2007 or fiscal 2008 and will not need to borrow from the federal government during these periods.

SELECTED FINANCIAL DATA

Statutory Basis

The revenues and expenditures of the budgeted operating funds presented in the following table are derived from the Commonwealth's audited statutory basis financial statements for fiscal 2002 through 2006. Projections for fiscal 2007 have been prepared by the Executive Office for Administration and Finance. The financial information presented includes all budgeted operating funds of the Commonwealth. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS — Operating Fund Structure" for additional detail.

During a fiscal year there are numerous transactions among these budgeted funds, which from a fund accounting perspective create offsetting inflows and outflows. In conducting the budget process, the Executive Office for Administration and Finance excludes those inter-fund transactions that by their nature have no impact on the combined fund balance of the budgeted funds. The following table isolates this inter-fund activity from the budgeted sources and uses to align more clearly forecasts prepared during the budget process to the detailed fund accounting of the Commonwealth's annual financial statements..

Budgeted Operating Funds -- Statutory Basis

(in millions)(1)

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	Projected Fiscal 2007
Beginning Fund Balances						
Reserved or Designated	$895.3	$195.2	$76.8	$664.6	$355.6	$947.2
Tax Reduction Fund	33.6	-	-	-	-	-
Transitional Escrow Fund					304.8	-
Stabilization Fund	1,715.0	881.8	641.3	1,137.3	1,728.4	2,154.7
Undesignated	369.5	311.0	34.7	90.9	98.4	106.2
Total	3,013.3	1,388.0	752.8(5)	1,892.8	2,487.2	3,208.1
Revenues and Other Sources						
Tax revenues	13,622.8	14,279.5	15,269.0	15,987.4	17,286.2	18,008.6
Federal reimbursements	4,334.9	4,523.6	5,098.5	4,697.0	5,210.1	6,061.8
Departmental and other revenues	1,485.2	1,494.8	1,847.7	1,948.9	2,094.3	2,051.8
Inter-fund transfers from non-budgeted funds and other sources (2)	1,732.0	1,689.2	1,773.1	1,740.2	1,714.9	863.7
Budgeted Revenues and Other Sources	21,174.8	21,987.1	23,988.3	24,373.4	26,305.5	26,985.9
Inter-fund Transfers	1,874.4	3,310.5(4)	2,058.7	2,231.3	1,358.1	283.3
Total Budgeted Revenues and Other Sources	23,049.2	25,297.7	26,047.0	26,604.7	27,663.3	27,269.2
Expenditures and Uses						
Programs and services (3)	22,513.2	22,209.5	21,456.1	22,067.7	23,918.7	26,529.8
Inter-fund transfers to non-budgeted funds and other uses	287.1	229.6	1,392.2	1,711.3	1,665.9	1,335.2
Budgeted Expenditures and Other Uses	22,800.3	22,439.1	22,848.3	23,779.1	25,584.6	27,865.0
Inter-fund Transfers	1,874.4	3,310.5(5)	2,058.7	2,231.2	1,358.1	283.3
Total Budgeted Expenditures and Other Uses	24,674.7	25,749.6	24,907.0	26,010.3	26,942.7	28,148.3
Excess (Deficiency) of Revenues and Other Sources Over Expenditures and Other Uses	(1,625.4)	(451.9)	1,140.0	594.4	720.9	(879.1)
Ending Fund Balances						
Reserved or Designated (6)	195.2	76.8	664.6	355.6	947.2	65.4
Tax Reduction Fund	--	--	--	--	--	--
Transitional Escrow Fund	--	--	--	304.8	--	--
Stabilization Fund	881.8	641.3	1,137.3	1,728.4	2,154.7	2,224.7
Undesignated	311.0	218.0	90.9	98.4	106.2	39.0
Total	$1,388.0	$936.1(6)	$1,892.8	$2,487.2	$3,208.1	$2,329.1

SOURCE: Fiscal 2002-2006, Office of the Comptroller; fiscal 2007, Executive Office for Administration and Finance.

(1) Totals may not add due to rounding.

(2) Inter-fund Transfers from Non-budgeted Funds and Other Sources include profits from the State Lottery, transfer of tobacco settlement funds to allow their expenditure, abandoned property proceeds and transfers to the Uncompensated Care Pool, as well as other inter-fund transfers.

(3) Certain Medicaid expenditures have been accounted for off-budget since fiscal 2003 and have continued through 2007. The Governor has proposed consolidating this spending onto budgeted spending beginning in fiscal 2008.

(4) Inter-fund transfers increased substantially in fiscal 2003 due to the elimination of a number of Budgeted Operating Funds pursuant to the fiscal 2004 general appropriations act, effective June 30, 2003.

(5) The variance between fiscal 2003 ending fund balances and fiscal 2004 beginning fund balances reflects a decrease of $181.3 million in the undesignated fund balance due to closure of minor budgeted funds and the transfer of various funds off budget.

(6) Reserved or Designated largely consists of appropriations from previous years, authorized to be expended in current years.

Recent Financial Restructurings

In recent years certain major spending programs formerly included in the budgeted operating funds have been moved off-budget. In certain cases the items moved off-budget are being funded by dedicated sales tax revenue, as described below. The total amount of such off-budget funding in fiscal 2007 is projected to be $1.651 billion (including $734 million for the MBTA, $557.4 million for the MSBA and $359.4 million for Medicaid).

Massachusetts Bay Transportation Authority. Beginning in fiscal 2001, the finances of the MBTA were restructured, and its financial relationship to the Commonwealth changed materially. The MBTA finances and operates mass transit facilities in eastern Massachusetts. The Commonwealth is obligated to provide the MBTA with a portion of the revenues raised by the Commonwealth's sales tax, generally the amount raised by a 1% sales tax (not including meals) with an inflation-adjusted floor. (For fiscal 2007 the floor is $734 million.) This amount is dedicated to the MBTA under a trust fund. The dedicated revenue stream is disbursed to the MBTA without state appropriation to be used to meet the Commonwealth's debt service contract assistance obligations relating to the MBTA's prior debt, as described below, and to meet the MBTA's other operating and debt service needs. The MBTA is authorized to assess a portion of its costs on 175 cities and towns in eastern Massachusetts; after a five-year phase-in of reduced assessments (from approximately $144.6 million in fiscal 2001 to approximately $136.0 million in fiscal 2006), the cities and towns are required by law to pay assessments equal to at least $136 million in the aggregate, as adjusted in each year after fiscal 2006 for inflation (with no annual increase to exceed 2.5% per year).

Prior to July 1, 2000, the Commonwealth provided financial support of the MBTA through guaranties of the debt service on its bonds and notes, contract assistance generally equal to 90% of the debt service on outstanding MBTA bonds and payment of its net cost of service (current expenses, including debt service and lease obligations not otherwise provided for, minus current income). In order to draw down dedicated sales tax receipts or municipal assessments from the state treasury, the MBTA must first certify that it has made provision in its annual budget for sufficient amounts to be available to meet debt service payments or other payments due under pre-July 1, 2000 financing obligations for which the Commonwealth has pledged its credit or contract assistance or is otherwise liable or as to which the MBTA has covenanted to maintain net cost of service or contract assistance support. To the extent the dedicated sales tax receipts and municipal assessments are insufficient in any year to meet the MBTA's debt service payments with respect to such obligations, the Commonwealth remains liable for the payment of such pre-July 1, 2000 obligations or the provision of net cost of service or contract assistance support as to such obligations. The amount of any support provided to the MBTA beyond the dedicated sales tax receipts and municipal assessments is to be in the form of a no-interest loan repayable within five years from the MBTA's system revenues and the dedicated sales tax receipts and municipal assessments.

School Building Assistance Program. The Commonwealth has operated a school building assistance program since 1948 to provide financial assistance to municipalities for building schools. Prior to fiscal 2005, financial assistance was provided in the form of annual contract assistance payments to subsidize a portion of local debt issues for such purposes. Assistance was appropriated annually through the Commonwealth's operating budget, reaching $401.4 million in fiscal 2004. In July, 2004, legislation was enacted to reform the program by moving it off-budget, dedicating sales tax receipts to support it and establishing an independent authority, the MSBA, to administer and manage it. The MSBA is required by the legislation to continue the contract assistance payments for previously approved and funded projects, to fund all projects on the waiting list at previously agreed-upon subsidy levels and to develop a program for funding new school projects beginning in fiscal 2008, at somewhat reduced subsidy levels. Funding for the program is provided by the dedication of a portion of the revenues raised by the Commonwealth's sales tax, generally the amount raised by a 1% sales tax (not including meals), phased in through fiscal 2011. The legislation guaranteed the MSBA $395.7 million in fiscal 2005, 70% of the dedicated sales tax amount (but not less than $488.7 million) in fiscal 2006, 78% of the dedicated sales tax amount (but not less than $557.4 million) in fiscal 2007, 85% of the dedicated sales tax amount (but not less than $634.7 million) in fiscal 2008, 90% of the dedicated sales tax (but not less than $702.3 million) in fiscal 2009 and 95% of the dedicated sales tax amount in fiscal 2010. In addition to dedicated sales tax revenues, the legislation authorized the Commonwealth to issue $1 billion of general obligation bonds to help the MSBA fund its liabilities. The Commonwealth issued these bonds during fiscal 2005 and 2006. The legislation also transferred $150 million from the fiscal 2004 surplus to the MSBA as start-up funding. The MSBA is expected to finance a substantial portion of its liabilities through the issuance of revenue bonds, and the legislation authorizes up to $10 billion of such issuance, of which $4 billion have been issued.

Medicaid. Beginning in fiscal 2003, certain expenditures included in the Commonwealth's Medicaid program have been funded off-budget. These included providing supplemental payments to nursing facilities and, commencing in fiscal 2004, the MassHealth Essential program. The sources of funds included transfers from the Uncompensated Care Pool and assessments on nursing facilities, together with related federal reimbursements. See "COMMONWEALTH PROGRAMS AND SERVICES - Medicaid."

Stabilization Fund

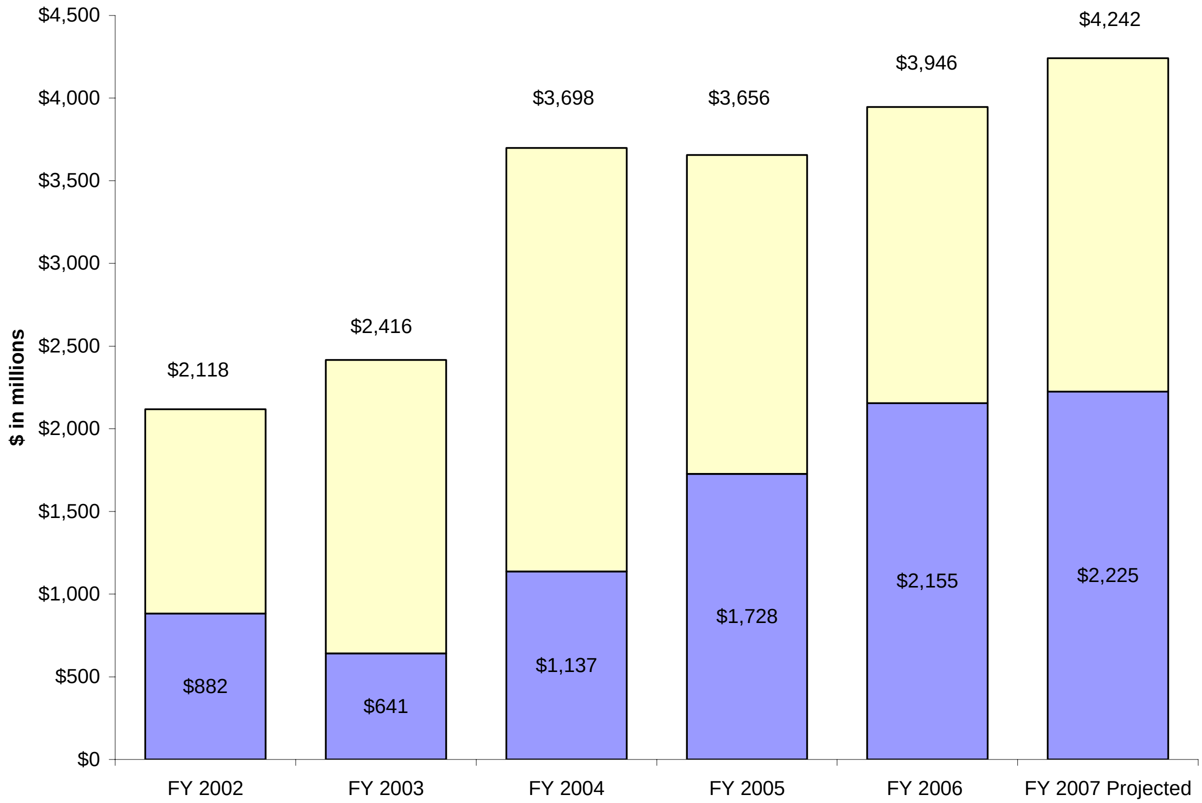
State finance law requires that any consolidated net surplus at the close of the fiscal year be deposited in the Commonwealth's Stabilization Fund. Over the last several fiscal years, a number of changes have been implemented to increase the flow of money into the Stabilization Fund and to increase its statutory capacity, including:

- Beginning June 30, 2003, all budgeted operating fund balances, except the Stabilization Fund, the Tax Reduction Fund and the Inland Fish and Game Fund are included in the calculation of the consolidated net surplus. These funds currently include the General Fund, the Highway Fund, the Intragovernmental Service Fund, the Workforce Training Fund, the Massachusetts Tourism Fund and the Division of Energy Resources Credit Trust Fund. The Governor's fiscal 2008 budget recommendations propose to include the Inland Fish and Game Fund in the calculation of consolidated net surplus.

- Beginning July 1, 2004, 0.5% of current-year net tax revenues must be deposited into the Stabilization Fund, and 0.5% of current-year net tax revenues must be made available for the next fiscal year before the year-end surplus is calculated. (The Governor's fiscal 2008 budget recommendations would provide for this Stabilization Fund transfer for fiscal year 2007 and fiscal 2008 to be suspended. The fiscal 2007 year-end projection reflects this proposal. The fiscal 2008 budget approved by the House of Representatives on April 27, 2007 follows this recommendation. See "FISCAL 2007 AND FISCAL 2008 - Fiscal 2008 Budget Proposals.")

- The fiscal 2004 general appropriations act increased the ceiling on the balance of the Stabilization Fund from 10% to 15% of total current year revenues. Once this limit has been reached, surplus dollars are deposited into the Tax Reduction Fund.

The following graph sets forth ending balances in the Stabilization Fund for fiscal 2002 through fiscal 2006 and the projection for fiscal 2007. For each year, the whole column area equals the allowable Stabilization Fund balance under the statutory formula, and the shaded area shows the amount of the actual ending balance.



SOURCES: Fiscal 2002-2006 Office of the Comptroller; fiscal 2007, Executive Office for Administration and Finance.

The following table shows the sources and uses of the Stabilization Fund during fiscal 2002 through 2006:

Stabilization Fund Sources and Uses (in thousands)

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006
Beginning fund balances	$ 1,714,990	$ 881,771	$ 641,325	$1,137,320	$1,728,355
Revenues and Other Sources					
Consolidated net surplus	-	75,673	663,457	776,959	353,990
Lottery transfer taxes	-	-	-	3,996	4,204
CA/T project cost recoveries	-	-	695	90	-
Investment income	39,566	6,456	5,259	17,270	68,115
Transfers due to fund consolidation	-	227,425	-	-	-
Excess permissible tax revenue	-	-	357,465	135,991	20,000
Transfer from Transitional Escrow Fund	157,215	-	-	-	-
Total Revenues and Other Sources	196,781	309,554	1,026,876	934,306	446,309
Total Expenditures and Other Uses	1,030,000	550,000	530,881	343,271	20,000
Excess (Deficiency) of Revenues and Other Sources Over Expenditures and Other Uses	(833,219)	(240,446)	495,995	591,035	426,309
Ending fund balances	$ 881,771	$ 641,325	$1,137,320	$1,728,355	$2,154,664
Allowable Stabilization Fund Balance	$ 2,117,492	$ 2,415,827	$3,697,771	$3,656,015	$3,945,820

SOURCE: Office of the Comptroller.

GAAP Basis

The Commonwealth's GAAP financial statements for the year ended June 30, 2006, incorporated herein by reference as Exhibit C, are prepared in accordance with reporting standards first established by GASB Statements 34 and 35, as amended. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS - Fiscal Control, Accounting and Reporting Practices of Comptroller." The GAAP financial statements present a government-wide perspective, including debt, fixed assets and accrual activity on a comprehensive statement of net assets. All fixed assets, including road and bridge infrastructure and all long-term liabilities, including outstanding debt and commitments of long-term assistance to municipalities and authorities, are part of the statements. The Commonwealth's statement of revenues, expenditures and changes in fund balances are presented as a statement of activities.

The table below presents the transition from the Commonwealth's statutory basis budgetary fund balance to the "fund perspective" balance, as depicted in the fund financial statements to the Commonwealth's "entity wide" governmental financial position. Differences between statutory and GAAP basis can be summarized in five major adjustments. Those adjustments are for Medicaid (as well as the somewhat related liability for uncompensated care), taxes, projected amounts due to the Commonwealth in the next fiscal year under the master tobacco settlement agreement, claims and judgments and amounts due to authorities. As evidenced in the trend line of fund balance (deficit) over time, however, these adjustments connect between the GAAP basis measurement when viewed using a fund perspective under GAAP and the statutory basis measurement. While the difference in fund balances may vary in a given fiscal year, both balances generally trend in the same direction. To convert to a full accrual basis, major adjustments are made for the net book value of the Commonwealth's assets, inclusive of infrastructure, the realizable value of long-term deferred revenues (largely from tax payment plans) and the amount of the Commonwealth's outstanding long-term debt and other liabilities.

Governmental Funds – Statutory to GAAP – Fund Perspective and to Governmental Net Assets (in millions)

Governmental Funds – Statutory Basis, June 30, 2006:	
Budgeted Fund Balance	$3,208.1
Non-Budgeted Special Revenue Fund Balance	1,852.9
Capital Project Fund Balance	(208.8)
Governmental Fund Balance – Statutory Basis, June 30, 2006	**4,852.2**
Plus:	
Expendable Trust and Similar Statutory Balances that are considered Governmental Funds for GAAP Reporting Purposes	343.9
Owner Controlled Insurance Program Net Assets	114.4
Adjusted Statutory Governmental Fund Balance – June 30, 2006	**5,310.5**
Accruals, net of allowances and deferrals for increases / (decreases):	
Taxes	1,428.9
Medicaid	(261.7)
Master Settlement Agreement receivables	124.7
Compensated absences	(5.2)
Contract Assistance Due to Component Units	(233.7)
Uncompensated Care liability	(155.9)
Claims, judgments and other risks	(50.8)
Workers' compensation and group insurance	(110.4)
Other accruals	(90.8)
Net Increase to governmental fund balances	645.1
Massachusetts School Building Authority fund balance	1,307.6
Total changes to governmental funds	1,952.7
Governmental Fund Balance (fund perspective)	**7,263.2**
Plus: Fixed assets including infrastructure, net of accumulated depreciation	22,497.2
Plus: Deferred revenue	581.5
Less: School construction grants payable	(8,699.0)
Less: CA/T Project assets to be transferred to Turnpike Authority	(11,691.5)
Less: Bonds payable, current and long term	(18,461.4)
Less: Other current and long term liabilities	(1,787.4)
Total Governmental Net Assets (entity-wide perspective)	**$(10,297.4)**

SOURCE: Office of the Comptroller

The largest portion of the Commonwealth'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 Commonwealth uses these capital assets to provide services to citizens. Although the Commonwealth'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. Additional restrictions are put on net assets. These restrictions represent resources that are subject to external restrictions on how they must be used. The remaining balance of unrestricted net assets may be used to meet the Commonwealth's ongoing obligations to citizens and creditors. However, due to the factors discussed previously, the negative unrestricted net assets presented are not indicative of the Commonwealth's fiscal well being, as they represent accounting adjustments and funding decisions.

Revenues – GAAP Basis. The measurement of revenues for the budgeted operating funds from a statutory basis differs from governmental revenues on a GAAP basis in that certain funds that are not governmental for statutory purposes are included on a GAAP basis, including revenue accruals for Medicaid and taxes, which are included on a GAAP basis but not on a statutory basis. In addition, internal transfers are eliminated under GAAP from an entity-wide perspective. The following table shows the distribution of major sources of revenue in fiscal 2006:

Comparison of Fiscal 2006 Governmental Revenues (in millions)

		GAAP Basis – Governmental	
	Statutory Basis	Fund Perspective	Entity-wide Perspective
Taxes	$18,593.4	$18,754.5	$18,668.3
Federal Revenue	8,352.8	8,828.5	8,829.6
Departmental and Miscellaneous Revenue	8,782.1	9,219.4	9,129.3
Total	$35,728.3	$36,802.4	$36,627.2

SOURCE: Office of the Comptroller

Financial Results—GAAP Basis. The following table provides financial results on a GAAP basis for fiscal 2002 through fiscal 2006 for all governmental operating funds of the Commonwealth.

Governmental Fund Operations – GAAP Basis – Fund Perspective (in millions)

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006
Beginning fund balances	$4,255.4	$2,467.9	$2,021.0	$4,424.4	$5,048.6
Restatement due to the implementation of GASB 34	551.2	-	-	-	-
Revenues and Financing Sources	36,476.6	42,798.0	44,371.7	43,532.6	47,189.9
Expenditures and Financing Uses	38,815.3	43,244.9	41,968.3	42,908.4	44,975.3
Excess (deficit)	(1,787.5)	(446.9)	2,403.4	624.2	2,214.6
Ending fund balances—GAAP fund perspective	$2,467.9	$2,021.0	$4,424.4	$5,048.6	$7,263.2

SOURCE: Office of the Comptroller

Financial Reports. The Commonwealth issues annual audited annual report included audited financial statements on both the statutory basis of accounting and the GAAP basis. These financial statements are issued as two separate reports, the SBFR and the CAFR. The SBFR is published by the Comptroller by October 31 and the CAFR is published by the Comptroller by the second Wednesday in January. The SBFR for the year ended June 30, 2006 and the CAFR for the year ended June 30, 2006 are included herein by reference as Exhibits B and C, respectively. For fiscal 1991 through 2006 the independent auditor's opinions were unqualified. Copies of these financial reports are available at the address provided under "CONTINUING DISCLOSURE." The SBFR for fiscal 1997 through fiscal 2006 and the CAFR for fiscal 1994 through fiscal 2006 are also available on the web site of the Comptroller of the Commonwealth located at http://www.mass.gov/osc by clicking on "Financial Reports/Audits."

The Comptroller retains an independent certified public accounting firm to audit the Commonwealth's financial statements and issue certain other reports required by the single audit. As part of the single audit, the independent auditors render a report on all programs involving federal funding for compliance with federal and state laws and regulations and assess the adequacy of internal control systems.

For each year beginning in fiscal 1991, the Commonwealth CAFRs, from which certain information contained in this Information Statement has been derived, have been awarded the Certificate of Achievement for Excellence in Financial Reporting by the Government Finance Officers Association of the United States and Canada (GFOA). The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting. Fiscal 2005 marked the fifteenth consecutive year that the Commonwealth has received this award. The CAFR for fiscal 2006 has been submitted to the GFOA for the award.

Discussion of Financial Condition

As the annual operating budget of the Commonwealth is adopted in accordance with the statutory basis of accounting, public and governmental discourse on the financial affairs of the Commonwealth has traditionally followed the statutory basis. Consequently, the financial information set forth in this document follows the statutory basis, except where otherwise noted. Since fiscal 1990, the Commonwealth has prepared separate audited financial reports on the statutory basis and on a GAAP basis. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS – Fiscal Control, Accounting and Reporting Practices of Comptroller; *Financial Reports*." The SBFR for the year ended June 30, 2006 is included herein by reference as Exhibit B. The CAFR for the year ended June 30, 2006 is included herein by reference as Exhibit C. Without limiting the generality of the references to the SBFR and CAFR for the year ended June 30, 2006, attention is called in particular to the portion of the CAFR under the heading "Management's Discussion and Analysis."

Auditor's Report on Fiscal 2006 CAFR

The basic financial statements included in the CAFR of the Commonwealth for the year ended June 30, 2006 were audited by Deloitte & Touche LLP (Deloitte & Touche). The Deloitte & Touche audit report dated December 22, 2006 on the general purpose financial statements included in the CAFR for the year ended June 30, 2006 contained an unqualified opinion. A copy of the audit report of Deloitte & Touche dated December 22, 2006 has been filed with each NRMSIR currently recognized by the SEC and is incorporated by reference in Exhibit C to this Information Statement and in each statement in this Information Statement referred to the Commonwealth CAFR for the year ended June 30, 2006. Deloitte & Touche has not been engaged to perform, and has not performed, since the respective dates of its reports included herein, any procedures on the financial statements addressed in such reports, nor has said independent auditor performed any procedures relating to the official statement of which this Information Statement is a part.

FISCAL 2007 AND FISCAL 2008

Fiscal 2006 Ending Balance

As of June 30, 2006, the Commonwealth ended fiscal 2006 with a surplus of $261.0 million. State law also required that 0.5% of current-year tax revenues, or $93.0 million, be transferred to the Stabilization Fund. The total transfer to the Stabilization Fund at the end of fiscal 2006 was $354 million.

For fiscal 2006, the Commonwealth's audited financial statements report a year-end balance in the Stabilization Fund of $2.155 billion. This balance reflects inflows of $354 million outlined above and $72.3 million in interest income. The year closed with additional reserved fund balances of $947.2 million and undesignated fund balances of $106.2 million. The total fund balance in the budgeted operating funds was $3.208 billion.

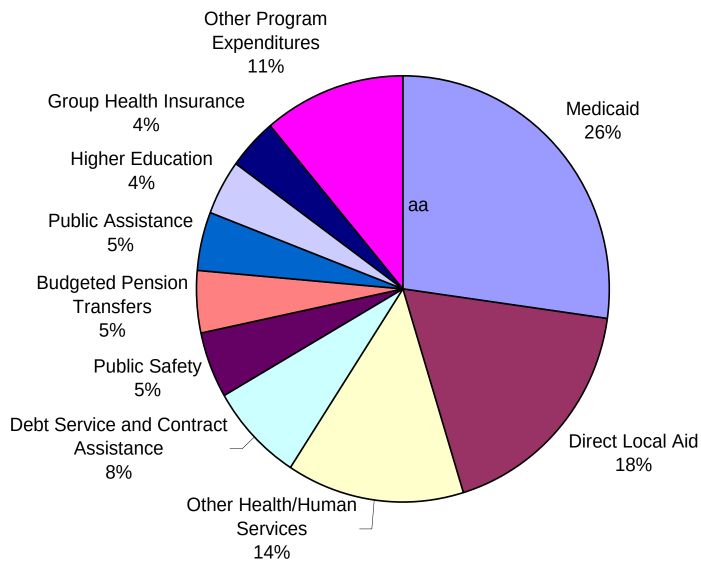
Fiscal 2007

To date, appropriations for fiscal 2007 total $25.705 billion. The fiscal 2007 general appropriations act provided for $25.676 billion in budgetary spending. Appropriations totaling $935 million in fiscal 2006 were authorized as prior appropriations continued (PACs), allowing these funds to be spent in fiscal 2007.

In addition to this spending in the budgeted operating funds, the Commonwealth has significant "off-budget" expenditures in fiscal 2007 in the amounts of dedicated sales taxes transferred to the MBTA and MSBA, projected to be in the amounts of $734 million and $557.4 million, respectively, and $359.4 million of off-budget expenditures in the Medicaid program. See "SELECTED FINANCIAL DATA – Recent Financial Restructurings."

The following is a graph depicting the breakdown of major categories of projected budgeted operating spending for fiscal 2007.

Fiscal 2007 Projected Operating Spending



General Appropriations Act. On July 8, 2006, former Governor Romney signed the general appropriations act for fiscal 2007. The budget as signed included $25.249 billion in spending, reflecting $458.6 million in line item reductions and $118 million in reductions to transfers from the General Fund. The Legislature subsequently overrode $427 million of the former Governor's line item vetoes, bringing the total value of the general appropriations act to $25.676 billion. The Legislature also overrode all of the vetoes of transfers from the General Fund.

The general appropriations act restored the distribution of the state's lottery revenues to the cities and towns. The fiscal 2007 distribution of $920 million reflects an increase of $158.6 million over the fiscal 2006 level. The budget also included significant increases to the Chapter 70 education aid program. The fiscal 2007 Chapter 70 distribution of $3.506 billion reflects an increase of $216.6 million over the fiscal 2006 level.

The fiscal 2007 general appropriations act directed the transfer of $550 million from the Commonwealth Stabilization Fund to the General Fund to support the appropriated spending. Former Governor Romney vetoed $576.6 million in appropriations and transfers. He also vetoed the transfer from the Stabilization Fund, being unnecessary at the reduced spending level. The Legislature overrode many of the line item and transfer vetoes as discussed above. The Stabilization Fund transfer veto was not overridden. On October 5, 2006 the former Governor vetoed provisions of a supplemental appropriations bill that would have transferred $450 million from the Stabilization Fund to the General Fund.

Section 9C Spending Reductions and Restoration. On November 10, 2006, former Governor Romney, pursuant to Section 9C of Chapter 29 of Massachusetts General Laws, decreased fiscal 2007 spending authorizations (called allotments) by $425 million. These reductions included many items previously vetoed by the former Governor, as well as broad-based decrease of 1% of most appropriations in executive branch agencies under the control of the Governor. Section 9C requires that if the Secretary of Administration and Finance determines that available revenues will be insufficient to meet all of the expenditures authorized to be made from any fund, the Governor shall reduce allotments accordingly, propose to the Legislature the raising of sufficient additional revenue or recommend an appropriation from the Stabilization Fund. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS – Overview of Operating Budget Process."

On December 1, 2006, former Governor Romney, pursuant to Section 9C of Chapter 29 of Massachusetts General Laws, revised the original Section 9C reductions discussed above, restoring $41.4 million of the reductions, as actual tax revenue receipts for November, 2006 exceeded the monthly benchmark by $84 million. On January 5, 2007, Governor Patrick restored the remaining $383.6 million in original section 9C reductions. The Executive Office for Administration and Finance anticipates that current tax revenues will be sufficient to support the additional spending levels.

Supplemental Appropriations. A number of supplemental appropriations bills have been filed and approved during fiscal 2007. The statutory basis financial tables in this document include all spending appropriated and any additional amounts for which the Governor has filed for supplemental appropriations. These bills include:

On July 13, 2006, Governor Romney approved a $20 million supplemental appropriation to fund a review of tunnel portions of the Central Artery/Tunnel Project. The appropriation was made in connection with other parts of the act that granted the Governor authority over safety inspections and reopening of Central Artery/Tunnel components that were closed subsequent to the July 2006 ceiling panel collapse in the Ted Williams connector tunnel. See "COMMONWEALTH CAPITAL ASSET INVESTMENT PLAN — Central Artery/Tunnel Project."

On July 11, 2006, legislation became law without Governor Romney's signature directing the transfer of $30 million to the Brownfields Redevelopment Fund. This transfer had originally been part of an economic stimulus bill passed in June, 2006. Governor Romney had returned this section for amendment, proposing a lesser transfer amount of $15 million. This transfer in the lesser amount had previously been included in the Commonwealth financial statements for fiscal 2006.

On February 6, 2007, Governor Patrick filed $19.0 million in supplemental appropriations to fund $5.7 million in collective bargaining increases, $4.1 million for higher caseloads and $2.7 million for existing family shelter capacity, both at the Emergency Assistance for the Elderly, Disabled, and Children program at the Department of Transitional Assistance. The bill also included $6.5 million in other programs and services. The spending in the bill is fully offset by $22.4 million in other spending reductions in accounts with surplus funding, and new revenues. The balance, $3.4 million, will be returned to the General Fund.

Tax Revenue Estimate Update. On October 24, 2006, as a result of a periodic review required by state law, the Executive Office for Administration and Finance increased the tax revenue estimate for fiscal 2007 by $202 million to $19.132 billion. The update also included the initial projection for fiscal 2008 revenues of $19.705 billion.

On January 30, 2007, as part of the consensus revenue estimate, the Executive Office for Administration and Finance increased the tax revenue estimate for fiscal 2007 by $168 million to 19.3 billion and announced, with legislative leaders, a consensus tax revenue estimate for fiscal 2008 of $19.879 billion.

Tobacco Master Settlement Agreement Revenue. In April, 2007, the Commonwealth received $243.3 million in tobacco settlement proceeds. The statutory financial tables in this document reflect the receipt of this revenue. This payment reflects a withholding of approximately $20 million due to the Non-Participating Manufacturer's (NPM) adjustment. See "LEGAL MATTERS." The Commonwealth is actively pursuing litigation to secure its right to receive the full amount of the April payment.

Settlement with the Conservation Law Foundation. The Commonwealth recently reached a settlement agreement with the Conservation Law Foundation with regard to a lawsuit asserting that the Commonwealth failed to complete several public transit projects that were proposed to offset the supposed environmental impacts of the Central Artery/Tunnel Project. The settlement agreement states that the Commonwealth will extend the MBTA's Green Line beyond Lechmere Station in Cambridge to Medford Hillside in Medford and to Union Square in Somerville; add four stops to the existing Fairmount commuter rail line; prepare a final design of the Red Line-Blue Line connector that would link the Blue Line at Government Center with the Red Line's Charles Street/MGH station; seek improvements to existing public transit service in the Arborway corridor in Jamaica Plain; complete the Greenbush commuter rail line by December 31, 2007; finish the ongoing modernization and platform lengthening of the Blue Line; and build 1,000 new parking spaces for public transit commuters. The agreement includes deadlines and provides a mechanism for the orderly substitution of projects if the described projects cannot be completed. The four main components of the agreement – the Green Line to Medford and Somerville, improvements to Fairmont, 1,000 new parking spaces, and the design of the Red/Blue connection are preliminarily estimated to cost $743.5 million. On March 23, 2007, the Governor approved legislation authorizing the issuance of $100 million of bonds to begin the first phase of these projects.

Fiscal 2008 Budget Proposals

On February 28, 2007, Governor Patrick filed his fiscal 2008 budget recommendations, providing for $26.714 billion in spending and based upon the fiscal 2008 consensus tax revenue figure of $19.879 billion.

Approximately $935 million in fiscal 2006 appropriations were authorized for expenditure in fiscal 2007 through the mechanism of "prior appropriation continued" (PAC) provisions, creating a large structural deficit in fiscal 2007. The Executive Office for Administration and Finance estimates that approximately $250 million of this authorized spending is recurring in nature and, accordingly, creates a gap in the fiscal 2008 budget.

Initial estimates of fiscal 2008 revenues and expenditures reflected a budget gap of approximately $1.3 billion, including the $250 million in recurring PAC spending. In addition to $295 million in additional revenues anticipated from proposed tax law changes and $174 million in additional fiscal 2008 tax revenues included in the consensus tax revenue forecast, the Governor's fiscal 2008 budget recommendations propose to close the budget gap through $180 million in net decreases in projected MassHealth (Medicaid) spending, $175 million from suspended deposits to the state's Stabilization Fund, $86 million in spending reductions associated with the elimination of "earmarked" projects, $50 million in transfers from reserve funds and $340 million in other spending reductions and revenue increases.

The Governor's fiscal 2008 budget recommendations propose to create an irrevocable trust, the State Retiree Benefit Trust, to begin funding the unfunded OPEB (Other Post-Employment Benefits) liability. See "COMMONWEALTH PROGRAMS AND SERVICES - Pension and Other Post-Retirement Benefit Obligations." To fund the trust, the Governor has proposed that an estimated $423 million of funds from the proposed repeal of the Health Care Security Trust fund be deposited in the new fund and that a portion of future master settlement agreement payments from tobacco companies be dedicated to the fund. Under the Governor's plan, 10% of all future tobacco settlement payments would be set aside first to support smoking cessation programs. Beginning in fiscal 2009, one-quarter of the remaining 90% received would be deposited in the new trust fund. By fiscal 2012, and in all subsequent years, 90% of the annual tobacco payments would be deposited in the fund. See "COMMONWEALTH REVENUES - Federal and Other Non-Tax Revenues."

On April 27, 2007, the House of Representatives approved its fiscal 2008 budget proposal which includes proposed appropriations of $26.9 billion. The House budget is also based on the consensus tax revenue estimate of $19.879 billion. The House budget does not assume approval of the Governor's proposed changes in corporate taxation. The House budget includes estimated use of reserves to support budgeted spending, including proposed transfers from the Stabilization Fund and the Health Care Security Trust Fund of $320 million and $150 million, respectively. The House budget includes an additional $20 million in local aid distributions through the chapter 70 program. The House budget creates a State Retiree Benefit Trust but does not include funding to begin to pre-fund the Commonwealth's unfunded OPEB liability.

The Senate Ways and Means Committee is expected to release its budget by May 16, 2007.

Related Legislation. On February 15, 2007, Governor Patrick proposed to the Legislature a Municipal Partnership Act. This bill would increase the local property tax base by repealing a 1915 exemption of certain telecommunication property. The bill also proposes to allow cities and towns to adopt a local meals tax of up to 2% and to expand an existing local-option tax on hotel and motel rentals from 4% to 5%. Finally, the bill contains other provisions intended to reduce costs to cities and towns. The proposed legislation is currently under consideration by the Legislature.

On the same day he filed his proposed fiscal 2008 budget, February 28, 2007, the Governor also filed legislation that would make changes in various tax laws. The Governor's budget proposal assumed that the total revenue increase from this bill would be approximately $295 million in fiscal 2008 – necessary to balance the Governor's proposed budget – and $479 million per fiscal year thereafter. The proposed legislation is currently under consideration by the Legislature. On April 30, 2007, the Governor, the Senate President and the Speaker of the House announced the formation of a 15-member study commission on corporate taxation to review and offer recommendations for streamlining the current corporate tax code. An interim report on legislative recommendations providing revenue for fiscal 2008 will be due by June 15, 2007. A final report on long-term changes to corporate tax laws is expected to be completed by January 1, 2008.

Along with his proposed changes to the corporate tax code, the Governor also announced a plan to create a "homeowner circuit breaker." Homeowners of all ages, with incomes up to certain defined levels, would be eligible for a tax credit to offset their local property tax assessments. The cost of the tax credit would be offset by revenues raised by the changes in corporate taxation.

Cash Flow

On February 28, 2007, the State Treasurer and the Secretary of Administration and Finance released a revised projected cash flow forecast for fiscal 2007. Fiscal 2006 ended with a non-segregated cash balance of $1.619 billion and a segregated bond balance of $222.2 million. The cash flow projection for fiscal 2007 is based on the general appropriations act signed into law on July 8, 2006 and includes the value of all vetoes and subsequent overrides as well as all prior appropriations continued into fiscal 2007 from the prior fiscal year. The cash flow projection also reflects all supplemental appropriations bills either filed or enacted that would affect the Commonwealth's cash flow in fiscal 2007. It reflects authorized transfers between budgeted funds and certain reserve funds as provided for in the general appropriations act and in subsequent legislation. The fiscal 2007 projection is based on actual spending and revenue through October, 2006 and estimates for the remainder of fiscal 2007. The fiscal 2007 projection is based on the Executive Office for Administration and Finance's fiscal 2007 tax estimate of $19.3 billion. The gross tax figure includes $1.335 billion dedicated to the Commonwealth's fiscal 2007 pension obligation, $733 million in sales tax revenues dedicated to the MBTA and $557.3 million in sales tax revenues dedicated to the MSBA. This forecast also includes an inflow of $217.1 million on April 15, 2007 pursuant to the tobacco master settlement agreement. The tobacco revenue estimate for fiscal year 2007 has been lowered by $42.9 million based upon the expected nonparticipating manufacturer adjustment to the April, 2007 payment. This reduction is similar in nature to that applied to the April, 2006 payment. The Commonwealth continues to actively pursue litigation to secure the right to receive the full amount of these payments. See "LEGAL MATTERS."

Fiscal 2007 opened with a starting balance of $2.072 billion of cash and is projected to have a June 30, 2007 ending balance of $509.3 million. These figures are somewhat higher than the reported figures for the close of fiscal 2006 because of system improvements in the State Treasurer's ability to calculate a more discrete figure. These figures do not include balances in the Stabilization Fund or certain other off-budget reserve funds, but do include monies sequestered to pay for projected capital projects totaling $222.2 million with respect to the starting balance and $63.1 million with respect to the ending balance. Excluding these sequestered capital funds, the Commonwealth's operating cash balance opened the year at $1.850 billion and is projected to end the fiscal year at $446.2 million, a $1.404 billion decrease. A portion of the overall decline in the operating cash balance is due to approximately $935 million in supplemental spending authorized in fiscal 2006 which has been carried forward into fiscal 2007. The decline also reflects the November, 2006 transfer of $353.9 million of fiscal 2006 surplus dollars, plus $6.9 million in accrued interest, to the Stabilization Fund and the January, 2007 restoration of $383.6 million of prior spending reductions made in November, 2006 under Section 9C of Chapter 29 of Massachusetts General Laws. See "FISCAL 2007 AND FISCAL 2008."

The Commonwealth's cash flow management incorporates the periodic use of commercial paper borrowing to meet cash flow needs for both capital and operating expenditures. In particular, the Commonwealth makes local aid payments of approximately $1 billion to its cities and towns at the end of each calendar quarter, which in recent years has often resulted in short-term cash flow borrowings. The Commonwealth began fiscal 2007 with $25.1 million of commercial paper outstanding in the form of bond anticipation notes (BANs). This commercial paper is currently outstanding. The Commonwealth's cash position reflects a typical cycle of tightening in the second and third quarter of the fiscal year. The Commonwealth borrowed $300 million in November, 2006 and an additional $600 million in December, 2006 to make the second-quarter local aid payment. In January, 2007, $200 million of revenue anticipation notes (RANs) were repaid, leaving $700 million of commercial paper RANs and $25.1 million of commercial paper BANs outstanding. The total amount of $725.1 million of commercial paper currently outstanding is expected to be paid down by June 30, 2007.

In March, 2007, $400 million of bond anticipation notes were issued as 90-day notes (outside the commercial paper program). These notes will mature in May, 2007 and are expected to be retired with bond proceeds at that time.

The February, 2007 cash flow projection includes an estimated $1.370 billion in proceeds of long-term borrowing for capital projects in fiscal 2007. This includes $500.1 million of proceeds from general obligation bonds issued in August, 2006 and $372.6 million of proceeds from general obligation bonds issued in November, 2006. In addition, a general obligation bond issue of $500 million in April, 2007 is forecast. That bond issue is now expected to occur in May, 2007.

The Commonwealth's next cash flow projection is expected to be released on or before June 1, 2007.

COMMONWEALTH CAPITAL ASSET INVESTMENT PLAN

Capital Spending Plan

The Executive Office for Administration and Finance develops and manages a multi-year capital investment plan. This plan coordinates capital expenditures by state agencies and authorities that are funded by Commonwealth debt, certain operating revenues, third-party payments and federal grants.

The Executive Office for Administration and Finance sets an annual administrative limit on the amount of bond-funded capital expenditures. The purpose of the administrative limit, known as the "bond cap," is to keep Commonwealth debt within affordable levels. The stated annual bond cap for fiscal 2004 through 2007 has been $1.25 billion, plus unexpended amounts carried forward from prior years. It should be noted, however, that debt for the Central Artery/Ted Williams Tunnel (CA/T) project, the Boston and Springfield convention center projects and the Massachusetts School Building Authority's school building assistance program has been issued in excess of the bond cap during the last several fiscal years. Under Governor Patrick, the Executive Office for Administration and Finance is in the process of developing a rational and transparent methodology for establishing the bond cap for fiscal 2008 and future fiscal years based on a standard measure of debt affordability.

In addition to approximately $1.373 billion of bond-funded capital expenditures subject to the bond cap, the Commonwealth's fiscal 2007 capital budget provides for the investment of the following amounts from other funding sources in the following projects in fiscal 2007: $362 million of federal grants for road and bridge projects, $238 million of federal grants, operating revenues and third-party contributions for the CA/T project, $41 million of federal grants for various information technology projects and $2.1million of special obligation bond proceeds for the Boston convention center project.

In addition, there are certain capital expenditures in fiscal 2007 funded from operating revenues that were provided for in the operating budget. Pursuant to legislation approved March 23, 2007, $229.1 million of such operating revenues that were unexpended as of May 1, 2007 will be applied to defease outstanding bonds of the Commonwealth, and bonds will be issued to fund the remaining capital expenditures that were to be funded from such operating revenues. These capital investments are not reflected in the Commonwealth's capital budget described below.

The Commonwealth has aggregated its capital budget expenditures into the following seven major categories:

- *Economic Development.* The Commonwealth expends funds in this category to support and develop its economy. Types of investments include construction of convention centers and parking facilities and grants for local economic development. Various state agencies are responsible for coordinating the Commonwealth's economic development investments. Fiscal 2007 spending in this category is currently budgeted to be $47 million.

- *Environment.* The Commonwealth expends funds in this category to provide a safe environment to its citizens. Types of investments include environmental remediation projects, open space acquisitions and water supply protection. The Executive Office of Energy and Environmental Affairs is responsible for coordinating the Commonwealth's environmental investments. Fiscal 2007 spending in this category is currently budgeted to be $152 million.

- *Housing*. The Commonwealth expends funds in this category to finance affordable housing. Types of investments include rehabilitation of public housing units and financial support of developers for the construction of affordable housing units. The Department of Housing and Community Development is responsible for coordinating the Commonwealth's housing investments. Fiscal 2007 spending in this category is currently budgeted to be $143 million.

- *Information Technology*. The Commonwealth expends funds in this category to improve productivity and program outcomes through the use of technology. Types of investments include the purchase of enterprise infrastructure systems and applications, telecommunications equipment, program and web-based applications and other computing hardware and software. The Information Technology Division within the Executive Office for Administration and Finance coordinates the Commonwealth's technology investments. Fiscal 2007 spending in this category is currently budgeted to be $86 million.

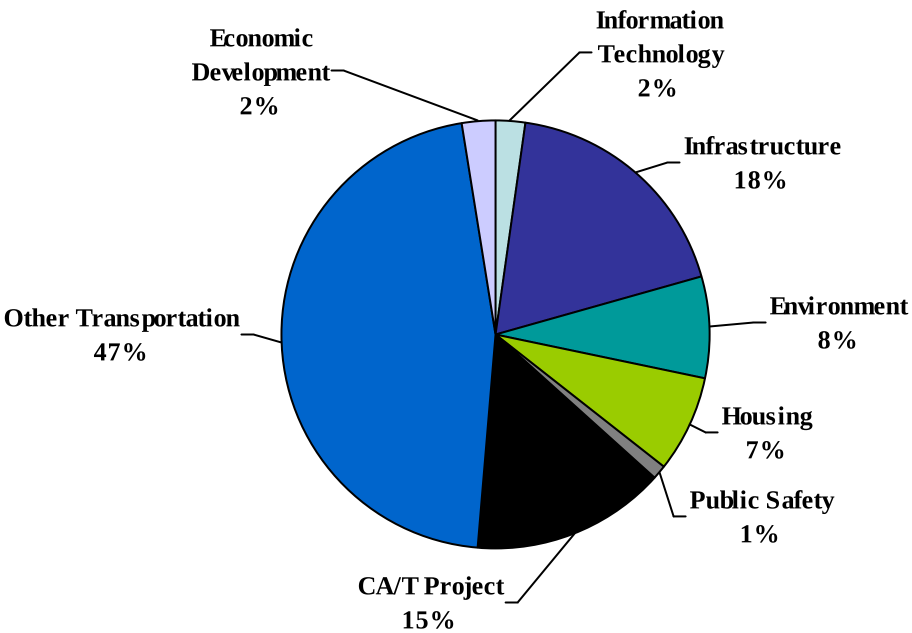
- *Infrastructure and Facilities*. The Commonwealth expends funds in this category to build and maintain its facilities, which enable the delivery of state services to its citizens. Investments in this category include construction of courthouses and prisons, rehabilitation of state office buildings and improvements to higher education facilities. The Division of Capital Asset Management and Maintenance within the Executive Office for Administration and Finance is responsible for coordinating the Commonwealth's investments in this category. Fiscal 2007 spending in this category is currently budgeted to be $362 million.

- *Public Safety*. The Commonwealth expends funds in this category to ensure the safety of its citizens. Types of investments include public safety vehicles, communications equipment and facility rehabilitation and maintenance. The Executive Office of Public Safety is responsible for coordinating the Commonwealth's public safety investments. Fiscal 2007 spending in this category is currently budgeted to be $24 million.

- *Transportation*. The Commonwealth expends funds in this category to provide a transportation network to support its economy. Types of investments include rehabilitation of bridges, construction and repair of roadways and financing of mass transportation. The Executive Office of Transportation and Public Works is responsible for coordinating the Commonwealth's transportation investments. Fiscal 2007 spending in this category is currently budgeted to be $1.210 billion, including $297 million for the CA/T project and $913 million for the balance of state transportation projects. See "Central Artery/Tunnel Project" below.

The following is a graph depicting the breakdown of major categories of budgeted capital expenditures for fiscal 2007:

Fiscal 2007 Budgeted Capital Expenditures



The following table sets forth the Commonwealth's capital spending and sources of funding in fiscal 2002 through 2006 and budgeted capital spending and sources of funding in fiscal 2007. Any budgeted capital spending for fiscal 2007 that is not completed in fiscal 2007 will be carried forward to fiscal 2008.

Commonwealth Historical Capital Spending (in millions)(1)

USES:	**Fiscal 2002**	**Fiscal 2003**	**Fiscal 2004**	**Fiscal 2005**	**Fiscal 2006**	**Fiscal 2007 (2)**
Information technology	$86	$76	$75	$61	$88	$86
Infrastructure	235	274	251	262	283	362
Environment	156	134	113	122	142	152
Housing	106	112	121	122	129	143
Public safety	8	37	20	18	19	24
Transportation						
CA/T project	1,296	1,015	691	509	318	297
Non-CA/T projects	612	682	767	791	871	913
Economic development						
Convention centers	134	225	113	54	12	2
Other	99	86	64	39	30	47
School building assistance	-	-	-	565	435	-
Total Uses:	$2,732	$2,641	$2,215	$2,543	$2,327	$2, 116
SOURCES:						
Funds from general obligation debt	$1,847	$1,472	$1,285	$1,850	$1,647	$1,373
Funds from special obligation debt	139	230	119	64	9	2
Funds from grant anticipation notes	9	24	-	-	-	-
Operating revenues	195	354	133	194	44	27
Third-party payments	52	52	63	99	274	84
Federal reimbursements	490	509	615	336	353	593(3)
Total Sources:	$2,732	$2,641	$2,215	$2,543	$2,327	$2,116

SOURCE: Fiscal 2002-2006, Office of the State Comptroller.

(1) Totals may not add due to rounding.
(2) Budgeted Capital Spending. The Executive Office for Administration and Finance periodically reviews capital expenditures and alters budgeted capital spending as circumstances may dictate.
(3) Includes $125 million of federal reimbursements for the CA/T project which are still being withheld from the project by the federal government pending approval of the Turnpike Authority's finance plan for the project. If not expended on the CA/T project during the federal fiscal year ending September 30, 2007, these federal reimbursements will be applied to reimburse costs of other road and bridge projects. Until the CA/T finance plan is approved and $125 million of federal grants funds are permitted to be applied to the project, the Commonwealth has been temporarily financing the related costs of the project. See "Central Artery/Tunnel Project."

On March 23, 2007, Governor Patrick approved legislation authorizing $1.58 billion of general obligation bonds to fund a number of urgent projects, including critical repair projects, projects that needed to proceed to secure significant federal grant funding, projects that had been stopped or unable to proceed on schedule, legally mandated projects and others. This "immediate needs" bond bill was limited in scope to projects that needed to commence during calendar 2007 for the reasons described above. Such legislation also authorizes the Commonwealth to issue refunding bonds to refinance certain of the Commonwealth's outstanding contract assistance and capital lease payment liabilities to achieve annual savings. In addition, the legislation provides for the use of over $200 million of cash previously appropriated to fund certain capital projects to defease outstanding bonds of the Commonwealth and for the funding of those capital projects with bonds instead.

The Executive Office of Administration and Finance is in the process of engaging in a comprehensive assessment of the Commonwealth's capital investment needs in order to develop a five-year capital spending plan for fiscal 2008 through fiscal 2012. The five-year plan is expected to be completed by June 30, 2007. It is anticipated that the Governor will file comprehensive bond bills in July, 2007 to obtain the borrowing authorization necessary to fund the capital spending plan.

The Governor recently announced two major capital investment initiatives. The South Coast Rail Project is a $1.435 billion project to extend commuter rail service from Boston to the southeastern region of Massachusetts. The initial planning phase of the project is expected to last through fiscal year 2010 and cost approximately $17 million, which is expected to be funded with proceeds of general obligation bonds of the Commonwealth. A finance plan for the design and construction phase of the project, expected to run from fiscal years 2011 through 2017, is anticipated to be completed by January 1, 2010. The finance plan is expected to rely in large part on new state tax revenues that will be generated from economic development along the new rail corridor.

The Governor's other major capital investment initiative is to support the life sciences industry in Massachusetts. The Governor has proposed borrowing $500 million over a 10-year period to fund a new stem cell bank at the University of Massachusetts, new life science innovation centers and other public facilities around the state to support research and development of new products in the life sciences industry. The Governor has also proposed spending $250 million of operating funds over the next ten years to support research and fellowships and granting $250 million in tax credits over the next ten years for companies that bring jobs to Massachusetts in the life sciences industry.

Legislation enacted in 2004 established a special Transportation Finance Commission to develop a comprehensive, multi-modal, long-range transportation finance plan for the Commonwealth. The Commission was charged with analyzing the state's long-term capital and operating needs for the transportation system and the funds expected to be available for such needs, as well as recommending how to close any perceived funding gap through potential cost savings, efficiencies and additional revenues. On March 28, 2007, the Commission issued a report containing its analysis of the Commonwealth's ability to fund needed surface transportation improvements over the next 20 years. For state-controlled roads and bridges and environmental transit commitments related to the Central Artery/Ted Williams Tunnel project, the report identifies funding needs of $25.670 billion and expected available state and federal funding of $16.820 billion, leaving a funding gap of $8.849 billion. The report also identifies substantial needs and funding gaps related to the Massachusetts Turnpike system, local roads and bridges and MBTA operations and capital needs. The Commission has not yet filed recommendations for closing these perceived funding gaps.

Central Artery/Ted Williams Tunnel Project

The largest single component of the Commonwealth's capital program in recent years has been the Central Artery/Ted Williams Tunnel (CA/T) project, a major construction project that is part of the completion of the federal interstate highway system. The CA/T project has involved the replacement of the elevated portion of Interstate 93 in downtown Boston (the Central Artery) with an underground expressway, and the construction of a new tunnel under Boston harbor (the Ted Williams Tunnel) linking the Boston terminus of the Massachusetts Turnpike (Interstate 90) to Logan International Airport and points north. The CA/T project is administered by the Massachusetts Turnpike Authority (Turnpike Authority).

Project Status. The CA/T project was substantially completed in January, 2006, with all major ramps, roadway and streets open for public use and most major contracts in the closeout phase. The major components of the work remaining for final completion of the CA/T project include reconstruction of the downtown surface street system, completion of the traffic management system and construction of certain parks. The completion of the surface roadways is expected to occur by June, 2007. Other remaining work is expected to be completed by October, 2007, except for one park and certain other project elements, which are expected to be completed in 2010.

Project Budget and Oversight and Delay of Federal Funding. Periodically, the Turnpike Authority has produced a cost/schedule update for the project, of which the most recent version, Revision 11 (CSU 11), was prepared in July, 2004 and included a $14.625 billion CA/T project budget. In addition, and in accordance with federal and state law, the CA/T project develops finance plans which must receive certain federal and state approvals.

In October, 2000, following an announcement by CA/T project officials of substantially increased cost estimates, a federal law was enacted that requires the U. S. Secretary of Transportation to withhold federal funds and all project approvals for the CA/T project in each federal fiscal year unless the Secretary has approved an annual update of the project's finance plan for such year and has determined that the Commonwealth is maintaining a balanced statewide transportation program and is in full compliance with a project partnership agreement among the Federal Highway Administration, the Executive Office of Transportation and Public Works, the Turnpike Authority and the Massachusetts Highway Department. In addition, the law limits total federal funding for the CA/T project to $8.549 billion (including $1.5 billion to pay the principal of federal grant anticipation notes), consistent with the project partnership agreement. Finally, the law ties future federal funding for the project to an annual finding by the Inspector General of the U. S. Department of Transportation that the annual update of the project's finance plan is consistent with Federal Highway Administration financial plan guidance. Should any federal assistance be withheld from the CA/T project pursuant to such law, such funding is nonetheless available to the Commonwealth for projects other than the CA/T project. Moreover, the law provides that federal funds will not be withheld if the Secretary of Administration and Finance certifies that such funds are required to pay all or any portion of the principal of federal grant anticipation notes issued for the CA/T project.

The CA/T project finance plans submitted through October, 2003 have received the requisite approvals. The most recent finance plan, based on CSU 11, was submitted in July, 2004, but has not yet received federal approval. Since 2004, the Turnpike Authority has revised certain elements of the budget in CSU 11 as a result of updated completion and cost estimates. In addition, at the request of the Federal Highway Administration, the Turnpike Authority is currently in the process of preparing a finance plan update to reflect recent developments, including the impact of the July, 2006 incident described below and other factors on costs and schedule, and expects to file such update this month following approval by the Massachusetts Highway Department, the Executive Office of Transportation and Public Works and the Executive Office for Administration and Finance.

According to federal and Commonwealth records, the total amount of federal funds withheld pending federal approval of the finance plan submitted in July, 2004 is approximately $125 million. Federal review of the finance plan submitted in July, 2004 is ongoing. The delay in receiving federal approval is due primarily to the failure to realize and resolve certain budgeted project financing sources and to the desire of the Federal Highway Administration to review a finance plan with updated cost estimates and funding sources.

Certain funding issues related to the July, 2004 finance plan remain unresolved. One is the need to replace $94 million that such finance plan projected would be realized from the disposition of the CA/T project headquarters and contiguous parcels located on Kneeland Street in Boston. Based on a December, 2004 request for bids for such property, the Turnpike Authority is no longer relying on this source of funding. The Turnpike Authority has identified $27 million in added interest earnings on the sale proceeds of certain land in Allston as a partial source of funding this amount. The Turnpike Authority has been seeking to secure the remaining $67 million from the state's Statewide Road and Bridge and Central Artery/Tunnel Infrastructure Fund (TIF). In addition, the Commonwealth has identified a $21 million shortfall attributable to expected interest earnings on amounts previously contributed by the Turnpike Authority to finance project costs that are in fact not available. Final agreement has not been reached regarding the use of additional funds from the TIF and other authorized sources for these purposes.

In connection with the preparation of the finance plan update, the Turnpike Authority has reviewed all of the major cost centers and has preliminarily revised the CA/T project budget and cash flows. The Executive Office of Transportation and Public Works just completed its own assessment of the Turnpike Authority's updated budget. Based on such reviews, the Commonwealth and the Turnpike Authority now estimate that the total cost of the project will be $14.798 billion, exclusive of certain cost recoveries, insurance payments and credits received or to be received in the future. However, due to the uncertain timing and amounts of CA/T cost recoveries, the cash needs to complete the project must be provided by the Commonwealth or the Turnpike Authority, at least until such cost recoveries are realized. Such cash needs are projected to be approximately $210 million.

The Commonwealth has proposed to the Turnpike Authority that the $210 million funding shortfall be covered from the following two sources: (a) at least $140 million projected to be available in the TIF through June 30, 2009; and (b) up to $70 million of Commonwealth bond proceeds. This commitment by the Commonwealth to cover the funding shortfall is subject to the following conditions: (i) the Turnpike Authority must cover any future shortfalls in Turnpike Authority funding to complete the project and any costs in excess of $14.798 billion; (ii) all cost recoveries, insurance proceeds and, until the amounts advanced to the project by the

Commonwealth described in (a) and (b) above are recovered, proceeds of the sale of certain real property of the Turnpike Authority related to the project that are received by the Turnpike Authority or the Commonwealth shall, subject to legislative authorization, be deposited into the TIF to pay project costs in lieu of the additional amounts committed by the Commonwealth or to reimburse the Commonwealth for project costs already paid; (iii) to the extent that, by June 30, 2010, the amounts described in clause (ii) above received by or paid to the Commonwealth have aggregated less than the portion of the $210 million funding shortfall paid from Commonwealth bonds, the Turnpike Authority will pay the difference to the Commonwealth by not later than January 1, 2011; and (iv) to the extent legally and practically feasible, the Turnpike Authority must comply with new reporting and accounting requirements to improve the transparency of project financing matters to the Commonwealth. The Turnpike Authority is expected to approve this proposal at its board meeting on May 15, 2007.

The revised project cost estimates are based on assumptions concerning the resolution of claims, liquidated damages and back charges to the Turnpike Authority that the Turnpike Authority believes to be reasonable. The actual resolution of such amounts could vary from those assumptions, and the Federal Highway Administration, in its review of the finance plan update, could arrive at different conclusions as to whether these assumptions are sound. The order of magnitude of the additional exposure related to such claims, liquidated damages and back charges is $160 million.

When the 2004 finance plan failed to receive approval prior to the end of the federal fiscal years ended September 30, 2005 and September 30, 2006, the Commonwealth applied the federal funds to other eligible transportation projects within the Commonwealth and to the payment of principal of federal grant anticipation notes. Although the Turnpike Authority is working to provide the Federal Highway Administration with the requested finance plan update by the middle of May, 2007 in order to receive approval to apply the $125 million of federal funds to the project before the end of the federal fiscal year ending September 30, 2007, if such approval is not received by then, the Commonwealth will apply the federal funds to other eligible transportation projects and to pay the principal of federal grant anticipation notes this year as well. Until such federal funds are received, the related costs of the project are being temporarily financed by the Commonwealth.

CA/T Project Cash Flow. Through fiscal 2006, $14.206 billion has been expended on CA/T project costs. Current estimates identify to-go cash flow needs of $297 million in fiscal 2007, $260 million in fiscal 2008 and $35 million thereafter. This includes project cost increases as a result of changes in scope and delay in completion of the project, including delays and increased costs attributable to redeployment of CA/T project staff and contractors to address the remediation of the July, 2006 incident described below. The updated finance plan being developed is expected to identify the sources of funding for such cash flow needs. Since federal funds have not been received on the schedule previously anticipated, the Commonwealth has made funds available to the CA/T project to bridge the ultimate receipt of federal funds. The Commonwealth expects to continue this practice, to the extent necessary, until the federal funds are received.

July, 2006 Incident and Other Quality Concerns. On July 10, 2006, panels fell from the ceiling of the eastbound Interstate 90 connector tunnel that leads to the Ted Williams Tunnel, causing the death of an automobile passenger. The incident caused substantial property damage and resulted in other significant costs. There are ongoing federal and state investigations. Following the incident and pursuant to a new state law, the Executive Office of Transportation and Public Works assumed oversight and responsibility for the inspection and remediation of the Interstate 90 connector tunnel. In addition, the Commonwealth instituted a comprehensive safety audit of all tunnels that are part of the Metropolitan Highway System, including the tunnels that are part of the CA/T project, and the Legislature appropriated $20 million to fund the audit, which is ongoing. Repairs and other work related to the July, 2006 incident are expected to cost $54 million. These costs are currently being borne by the Commonwealth. There are additional costs being incurred by the Commonwealth and the Turnpike Authority related to the July, 2006 incident. While the Commonwealth and the Turnpike Authority anticipate that all such costs are subject to recovery, the amount of such recovery is unknown at this time.

In addition, the Massachusetts Port Authority (Massport), which has agreed to acquire certain portions of the CA/T project consisting of roadways, viaducts and other structures located at Logan International Airport in East Boston, has advised the Commonwealth that it is not satisfied with the condition of certain of these facilities. The Turnpike Authority has budgeted what it believes to be the cost of addressing needed repairs to the property being transferred to Massport in order to address Massport issues that the Turnpike Authority accepts, and some of this work is already scheduled to be done. At present, the Turnpike Authority and Massport are negotiating a schedule for completing the work and transferring the property. The $50 million portion of the purchase price for the property that Massport has not already paid is expected to be paid in progress payments as the work is done, with the first payment of at least $25 million by June 30, 2007. It should be noted that this will not directly affect the CA/T project's cash flow, since the Commonwealth advanced the $50 million to the project several years ago in anticipation of reimbursement by Massport.

Additional quality issues may emerge as the safety audit and other investigations proceed. Formulating estimates of needed contingencies is an inexact process.

SEC Inquiry. In late August and early September, 2006, the Securities and Exchange Commission (SEC) sent certain departments and instrumentalities of the Commonwealth letters requesting voluntary provision of documents and information regarding safety reviews of the CA/T project during the period January 1, 2004 to the present and related disclosures. The Commonwealth and the Turnpike Authority are cooperating with the SEC.

LONG-TERM LIABILITIES

The following table shows long-term debt of the Commonwealth as issued and retired from fiscal 2002 through fiscal 2007:

Long-Term Debt Issuance and Repayment Analysis (in thousands) (1)

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	As of April 2, 2007 (4)
Fiscal Year Beginning Balance (as of July 1)	$13,999,454	$14,955,135	$15,962,506	$17,382,172	$17,856,799	$18,461,406
General and special obligation debt issued	1,470,272	1,845,458(2)	1,925,990(3)	1,267,281	1,770,346	836,258
Subtotal	15,469,726	16,800,593	17,888,496	18,649,453	19,627,145	19,297,664
Debt retired or defeased, exclusive of refunded debt	(692,341)	(737,832)	(758,444)	(882,266)	(1,024,542)	(990,293)
Refunding debt issued, net of refunded debt	177,750	(100,255)	252,120	89,612	(141, 215)	(25,224)
Fiscal Year Ending Balance (June 30)	$14,955,135	$15,962,506	$17,382,172	$17,856,799	$18,461,406	$18,282,147

SOURCE: Office of the Comptroller.

(1) Including premium, discount and accretion of capital appreciation bonds. Capital appreciation bonds are reported at original net proceeds for the purposes of calculating debt limit compliance.

(2) Includes $30.1 million of bonds, which, although not legally defeased, will be paid in fiscal 2008 from funds held in escrow by a third-party trustee. Also includes a series of $209.5 million of bonds, which, although not legally defeased, will be paid in fiscal 2008 and 2012 from funds held in escrow by a third-party trustee.

(3) Includes $408.0 million of grant anticipation notes, which, although not legally defeased, will be paid in fiscal 2009 and 2011 from funds held in escrow by a third-party trustee.

(4) Amounts are preliminary.

General Authority to Borrow

Under its constitution, the Commonwealth may borrow money (a) for defense or in anticipation of receipts from taxes or other sources, any such loan to be paid out of the revenue of the year in which the loan is made, or (b) by a two-thirds vote of the members of each house of the Legislature present and voting thereon. The constitution further provides that borrowed money shall not be expended for any other purpose than that for which it was borrowed or for the reduction or discharge of the principal of the loan. In addition, the Commonwealth may give, loan or pledge its credit by a two-thirds vote of the members of each house of the Legislature present and voting thereon, but such credit may not in any manner be given or loaned to or in aid of any individual, or of any private association, or of any corporation which is privately owned or managed.

The Commonwealth has waived its sovereign immunity and consented to be sued on contractual obligations, which term includes bonds and notes issued by it and all claims with respect thereto. However, the property of the Commonwealth is not subject to attachment or levy to pay a judgment, and the satisfaction of any judgment generally requires legislative appropriation. Enforcement of a claim for payment of principal of or interest on bonds and notes of the Commonwealth may also be subject to the provisions of federal or Commonwealth statutes, if any, hereafter enacted extending the time for payment or imposing other constraints upon enforcement, insofar as the same may be constitutionally applied. The United States Bankruptcy Code is not applicable to states.

Statutory Limit on Direct Debt. Legislation enacted in December 1989 imposes a limit on the amount of outstanding "direct" bonds of the Commonwealth. The law, which is codified in Section 60A of Chapter 29 of the General Laws, set a fiscal 1991 limit of $6.8 billion and provided that the limit for each subsequent fiscal year was to be 105% of the previous fiscal year's limit. This limit is calculated under the statutory basis of accounting, which differs from GAAP in that the principal amount of outstanding bonds is measured net of underwriters' discount, costs of issuance and other financing costs. The law further provides that bonds to be refunded from the proceeds of Commonwealth refunding bonds are to be excluded from outstanding "direct" bonds upon the issuance of the refunding bonds. Pursuant to special legislation enacted over the years, certain outstanding Commonwealth debt obligations are not counted in computing the amount of bonds subject to the limit, including Commonwealth refunding/restructuring bonds issued in September and October, 1991, federal grant anticipation notes, bonds issued to pay operating notes issued by the MBTA or to reimburse the Commonwealth for advances to the MBTA, bonds payable from the Central Artery and Statewide Road and Bridge Infrastructure Fund and bonds issued to finance the MSBA. The statutory limit on "direct" bonds during fiscal 2007 is approximately $14.8 billion.

The outstanding Commonwealth debt, the amounts of debt excluded from the statutory debt limit, the net amounts of Commonwealth debt subject to the statutory debt limit and the statutory debt limit as of the end of each of the last five fiscal years are shown in the following table:

Calculation of the Debt Limit (in thousands)

	2002	2003	2004	2005	2006
Balance as of June 30	$14,995,135	$15,962,506	$17,382,172	$17,856,799	$18,461,406
Less amounts excluded:					
(Discount)/premium and issuance costs	(181,910)	(68,718)	1,120	70,937	112,673
1991 refunding/restructuring	(22,043)	(10,600)	-	-	-
Special obligation debt (1)	(772,812)	(748,124)	(1,347,822)	(1,485,548)	(1,291,266)
Federal grant anticipation notes (1)	(1,500,000)	(1,500,000)	(1,908,015)	(1,908,015)	(1,789,876)
Assumed county debt	(1,115)	(855)	(675)	(600)	(525)
MBTA forward funding	(625,000)	(680,869)	(601,027)	(511,546)	(416,830)
Transportation Infrastructure Fund	(838,193)	(1,386,869)	(1,066,638)	(1,336,741)	(1,476,287)
MSBA	-	-	-	(500,000)	(1,000,002)
Outstanding Direct Debt(2)	$11,054,062	$11,566,472	$12,459,055	$12,185,286	$12,599,293
Statutory Debt Limit	$11,630,307	$12,211,823	$12,822,414	$13,463,535	$14,136,712

SOURCE: Office of the Comptroller.

(1) Includes three series of outstanding crossover refunding bonds, two of which are special obligation bonds and one of which consists of federal grant anticipation notes. The refunding escrows funded by these bonds and related premiums are used to pay interest on the refunding bonds until the refunded bonds are callable and then to redeem the refunded bonds. Interest on the refunded bonds prior to redemption continues to be paid from pledged revenues as before.

(2) Capital appreciation bonds reported at original net proceeds for the purposes of calculating debt limit, not at maturity value.

Limit on Debt Service Appropriations. In January, 1990, legislation was enacted to impose a limit on debt service appropriations in Commonwealth budgets beginning in fiscal 1991. The law, which is codified as Section 60B of Chapter 29 of the General Laws, provides that no more than 10% of the total appropriations in any fiscal year may be expended for payment of interest and principal on general obligation debt of the Commonwealth. Debt service relating to bonds that are excluded from the debt limit on direct debt is not included in the limit on debt service appropriations. See "*Statutory Limit on Direct Debt.*" Section 60B is subject to amendment or repeal by the Legislature at any time and may be superseded in the annual appropriations act for any year. The following table shows the percentage of total appropriations expended or estimated to be expended from the budgeted operating funds for debt service on general obligation debt (excluding debt service on bonds excluded from the debt limit) in the fiscal years indicated:

Debt Service Expenditures (in millions)(1)

Fiscal Year	Budgeted Debt Service	Total Budgeted Expenditures and Other Uses	Percentage
2002	1,219.0	22,800.3	5.4
2003	1,203.5	22,439.1	5.4
2004	1,227.0	22,848.3	5.4
2005	1,398.7	23,779.1	5.9
2006	1,422.8	25,584.6	5.6

SOURCE: Office of the Comptroller.

(1) Reflects budgeted debt service subject to the provisions of Section 60B of Chapter 29 of the Massachusetts General Laws.

Commonwealth Debt. The Commonwealth is authorized to issue three types of debt directly – general obligation debt, special obligation debt and federal grant anticipation notes. General obligation debt is secured by a pledge of the full faith and credit of the Commonwealth. Special obligation debt may be secured either with a pledge of receipts credited to the Highway Fund or with a pledge of receipts credited to the Convention Center Fund. See "Special Obligation Debt." Federal grant anticipation notes are secured by a pledge of federal highway construction reimbursements. See "Federal Grant Anticipation Notes."

Other Long-Term Liabilities. The Commonwealth is also authorized to pledge its credit in aid of and provide contractual support for certain independent authorities and political subdivisions within the Commonwealth. These Commonwealth liabilities are classified as (a) general obligation contract assistance liabilities, (b) budgetary contractual assistance liabilities or (c) contingent liabilities.

General obligation contract assistance liabilities arise from statutory requirements for payments by the Commonwealth to the Massachusetts Convention Center Authority and the Foxborough Industrial Development Financing Authority of 100% of the debt service of certain bonds issued by those authorities, as well as payments to the Massachusetts Water Pollution Abatement Trust and the Massachusetts Turnpike Authority that are not directly tied to debt service. Such liabilities constitute a pledge of the Commonwealth's credit for which a two-thirds vote of the Legislature is required.

Budgetary contract assistance liabilities arise from statutory requirements for payments by the Commonwealth under capital leases, including leases supporting certain bonds issued by the Chelsea Industrial Development Financing Authority and the Route 3 North Transportation Improvements Association and other contractual agreements, including a contract supporting certain certificates of participation issued for Plymouth County. Such liabilities do not constitute a pledge of the Commonwealth's credit.

Contingent liabilities relate to debt obligations of independent authorities and agencies of the Commonwealth that are expected to be paid without Commonwealth assistance, but for which the Commonwealth has some kind of liability if expected payment sources do not materialize. These liabilities consist of guaranties and similar obligations with respect to which the Commonwealth's credit has been pledged, as in the case of certain debt obligations of the MBTA, the Woods Hole, Martha's Vineyard and Nantucket Steamship Authority and the higher education building authorities; and of statutorily contemplated payments with respect to which the Commonwealth's credit has not been pledged, as in the case of the Commonwealth's obligation to replenish the capital reserve funds securing certain debt obligations of the Massachusetts Housing Finance Agency and the Commonwealth's obligation to fund debt service, solely from monies otherwise appropriated for the affected institution, owed by certain community colleges and state colleges on bonds issued by the Massachusetts Health and Educational Facilities Authority and the Massachusetts State College Building Authority.

The following table sets forth the amounts of Commonwealth long-term general obligation debt, special obligation debt and federal grant anticipation notes outstanding as of the end of the last five fiscal years and as of April 2, 2007.

Long Term Commonwealth Debt (in thousands) (1)

	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005	Fiscal 2006	As of April 2, 2007(3)
General Obligation Debt	$12,682,323	$13,714,382	$14,126,275	$14,463,236	$15,383,366	$15,265,247
Special Obligation Debt (2)	772,812	748,124	1,347,882	1,485,548	1,288,595	1,288,595
Federal Grant Anticipation Notes (2)	1,500,000	1,500,000	1,908,015	1,908,015	1,789,445	1,728,305
TOTAL	$14,955,135	$15,962,506	$17,382,172	$17,856,799	$18,461,406	$18,282,147

SOURCE: Office of the Comptroller.
(1) The amount of debt is calculated based on net proceeds.
(2) Includes three series of outstanding crossover refunding bonds, two of which are special obligation bonds and one of which consists of federal grant anticipation notes. Amounts attributable to such bonds are shown in this table beginning in fiscal 2004. The refunding escrows funded by these bonds and related premiums are used to pay interest on the refunding bonds until the refunded bonds are callable and then to redeem the refunded bonds. Interest on the refunded bonds prior to redemption continues to be paid from pledged revenues as before.
(3) Amounts are preliminary.

In addition, for fiscal 2002, 2003, 2004, 2005 and 2006, and as of April 2, 2007, there was outstanding the following amounts of debt the entire principal of and interest on which is supported by Commonwealth general obligation contract assistance payments: $167.6 million, $147.7 million, $127.5 million, $118.9 million, $87 million and $78 million, respectively. Such debt includes debt of the Massachusetts Convention Center Authority, the Massachusetts Development Finance Agency and the Foxborough Industrial Development Financing Authority. The Massachusetts Water Pollution Abatement Trust also has debt outstanding the principal of and interest on which is supported, in part, by Commonwealth contract assistance payments. For the total amount of the Commonwealth's general obligation contract assistance payment requirements, see "General Obligation Contract Assistance Requirements" below.

General Obligation Debt

The Commonwealth issues general obligation bonds and notes pursuant to Chapter 29 of the General Laws. General obligation bonds and notes issued thereunder are deemed to be general obligations of the Commonwealth to which its full faith and credit is pledged for the payment of principal and interest when due, unless specifically provided otherwise on the face of such bond or note.

Notes. The Commonwealth is authorized to issue short-term general obligation debt as revenue anticipation notes or bond anticipation notes. Revenue anticipation notes may be issued by the State Treasurer in any fiscal year in anticipation of the receipts for that year. Revenue anticipation notes must be repaid no later than the close of the fiscal year in which they are issued. Bond anticipation notes may be issued by the State Treasurer in anticipation of the issuance of bonds, including special obligation convention center bonds. See "Special Obligation Debt." The Commonwealth currently has liquidity support for a $1 billion commercial paper program for general obligation notes, through five $200 million credit lines which expire in December, 2007, September, 2008, June, 2010, December, 2010 and November, 2015, respectively.

Synthetic Fixed Rate Bonds. In connection with the issuance of certain general obligation bonds that were issued as variable rate bonds, the Commonwealth has entered into interest rate exchange (or "swap") agreements with certain counterparties pursuant to which the counterparties are obligated to pay the Commonwealth an amount equal to the variable rate payment on the related bonds and the Commonwealth is obligated to pay the counterparties a stipulated fixed rate. Only the net difference in interest payments is actually exchanged with the counterparty, and the Commonwealth is responsible for making interest payments to the variable rate bondholders. The effect of the agreements is to fix the Commonwealth's interest payment obligations with respect to the variable rate bonds. The Commonwealth will be exposed to a variable rate if the counterparties default or if the swap agreements are terminated. Termination of a swap agreement may also result in the Commonwealth's making or receiving a termination payment. The variable rate bonds associated with such swaps are supported by stand-by bond purchase liquidity facilities with commercial banks, which require the applicable bank to purchase any bonds that are tendered and not successfully remarketed. Unless and until remarketed, the Commonwealth would be required to pay the bank interest on such bonds at a rate equal to the bank's prime rate. In addition, the Commonwealth would be required to amortize the principal of any such bonds according to an accelerated schedule. Such liquidity facilities expire well before the final maturity date of the related bonds and are expected to be renewed. As of April 2, 2007, the amount of such variable rate bonds outstanding with a synthetic fixed rate agreement was approximately $2.198 billion.

Variable Rate Demand Bonds, Auction Rate Securities and U.Plan Bonds. As of April 2, 2007, the Commonwealth had outstanding approximately $625.6 million of variable rate demand bonds (not converted to a synthetic fixed rate as described above) in a daily interest rate mode, with liquidity support provided by commercial banks under agreements terminating in January, 2009, March, 2011, March, 2013 and December, 2015. As of April 2, 2007, the Commonwealth had outstanding $401.5 million of auction rate securities in a seven-day interest rate mode. As of April 2, 2007, the Commonwealth had outstanding approximately $86.3 million of variable rate "U.Plan" bonds, sold in conjunction with a college savings program administered by the Massachusetts Educational Financing Authority, which bear deferred interest at a rate equal to the percentage change in the consumer price index plus 2%**,** together with current interest at the rate of 0.5%.

Special Obligation Debt

Highway Fund. Section 2*O* of Chapter 29 of the General Laws authorizes the Commonwealth to issue special obligation bonds secured by all or a portion of revenues accounted to the Highway Fund. Revenues, which are currently accounted to the Highway Fund, are primarily derived from taxes and fees relating to the operation or use of motor vehicles in the Commonwealth, including the motor fuels excise tax. Chapter 33 of the Acts of 1991 authorizes the Commonwealth to issue such special obligation bonds in an aggregate amount not to exceed $1.125 billion. As of April 2, 2007, the Commonwealth had outstanding $649.9 million of such special obligation bonds, including $640.4 million of such bonds secured by a pledge of 6.86¢ of the 21¢ motor fuels excise tax. These amounts are exclusive of crossover refunding bonds, which have been issued to refund a portion of the outstanding special obligation bonds described above in fiscal 2008 and 2012.

Convention Center Fund. Chapter 152 of the Acts of 1997, as amended, authorizes $694.4 million of special obligation bonds to be issued for the purposes of building a new convention center in Boston ($609.4 million), the Springfield Civic Center ($66 million) and the Worcester convention center ($19 million). The bonds are payable from monies credited to the Convention Center Fund created by such legislation, which include certain hotel tax receipts from hotels in Boston, Cambridge, Springfield and Worcester, a surcharge on car rentals in Boston, a parking surcharge at all three facilities, a surcharge on sightseeing tours and cruises in Boston and sales tax receipts from certain hotels and other retail establishments in Boston, Cambridge and Springfield. The legislation requires a capital reserve fund to be maintained at a level equal to maximum annual debt service and provides that if the fund falls below its required balance the 2.75% convention center financing fee in Boston is to be increased (though the overall hotel tax in Boston, including the fee, cannot exceed 14%). In June, 2004, the Commonwealth issued $686.7 million of special obligation bonds secured solely by the pledge of receipts of tax revenues within the special districts surrounding the centers and other special revenues connected to such facilities, $638.7 million of which remain outstanding as of April 2, 2007.

Federal Grant Anticipation Notes

The Commonwealth has issued federal grant anticipation notes yielding aggregate net proceeds of $1.5 billion, the full amount authorized, to finance the current cash flow needs of the CA/T project in anticipation of future federal reimbursements. The legislation authorizing such notes contains a statutory covenant that as long as any such grant anticipation notes remain outstanding, the Commonwealth will deposit all federal highway reimbursements into the Grant Anticipation Note Trust Fund, to be released to the Commonwealth once all the debt service and reserve funding obligations of the trust agreement securing the grant anticipation notes have been met. If the United States Congress reduces the aggregate amount appropriated nationwide for federal highway spending to less than $17.1 billion and debt service coverage with respect to the notes falls below 120%, then the legislation further pledges that 10¢ per gallon of existing motor fuel tax collections will be deposited into the trust fund, to be used for debt service on the notes, subject to legislative appropriation. Principal amortization of the notes began in fiscal 2006 and will continue through fiscal 2015. Under the trust agreement securing the notes, aggregate annual debt service on grant anticipation notes may not exceed $216 million. Such notes and the interest thereon are secured solely by the pledge of federal highway construction reimbursement payments and by a contingent pledge of certain motor fuels excises. In practice, the interest on such notes has been paid from state appropriations.

On July 16, 2003, the Commonwealth issued special obligation refunding notes for the purpose of refunding approximately $408 million of outstanding federal grant anticipation notes in 2008 and in 2010. Pursuant to the crossover refunding method employed, interest on the notes will be paid solely by an escrow account established with the proceeds of the notes. Upon the redemption of $408 million of outstanding federal grant anticipation notes on the crossover dates in 2008 and 2010, the refunding notes will become secured by the Grant Anticipation Note Trust Fund.

As of April 2, 2007, $1.728 billion of such notes, inclusive of the special obligation crossover refunding notes, remain outstanding.

Debt Service Requirements

The following table sets forth, as of April 2, 2007, the annual fiscal year debt service requirements on outstanding Commonwealth general obligation bonds, special obligation bonds and federal grant anticipation notes. For variable rate bonds with respect to which the Commonwealth is a fixed-rate payor under an associated interest rate exchange agreement, the debt service schedule assumes payment of the fixed rate due under such agreement. For other variable rate bonds and for auction rate securities, the schedule assumes a 5% interest rate.

Debt Service Requirements on Commonwealth Bonds as of April 2, 2007

(in thousands)(1)

	General Obligation Bonds				*Federal Grant Anticipation Notes(2)*			*Special Obligation Bonds(1)*			
Fiscal Year	Principal	Current Interest	Interest on CABS at Maturity	Sub Total	Principal	Interest	Sub Total	Principal	Interest	Sub Total	Total Debt Service Commonwealth Bonds
2007	$105,175	$134,021	$ -	$239,196	$62,685	$43,172	$105,857	$30,325	$16,808	$47,133	$392,186
2008	993,165	741,847	5,801	1,740,812	130,240	81,469	211,709	32,545	66,141	98,686	2,051,207
2009	1,019,991	691,638	6,900	1,718,529	137,230	74,478	211,708	33,960	64,631	98,591	2,028,828
2010	946,537	640,292	6,905	1,593,734	158,815	66,835	225,650	35,530	63,067	98,597	1,917,981
2011	960,072	589,342	7,763	1,557,177	214,620	57,206	271,826	37,240	61,359	98,599	1,927,602
2012	840,113	538,225	7,802	1,386,139	226,420	45,694	272,114	39,135	59,470	98,605	1,756,858
2013	909,713	492,651	8,611	1,410,975	208,410	35,110	243,520	41,150	57,438	98,588	1,753,083
2014	797,547	449,214	6,686	1,253,446	302,820	21,697	324,517	38,925	55,200	94,125	1,672,089
2015	796,706	408,962	6,201	1,211,869	287,065	7,185	294,250	87,430	53,210	140,640	1,646,758
2016	843,175	370,915	4,873	1,218,964	-	-	-	90,760	48,593	139,353	1,358,317
2017	809,064	331,087	3,302	1,143,453	-	-	-	108,385	43,803	152,188	1,295,641
2018	611,921	295,171	2,419	909,511	-	-	-	46,350	38,425	84,775	994,286
2019	601,219	264,437	20,002	885,658	-	-	-	48,775	36,121	84,896	970,553
2020	677,680	231,545	1,212	910,438	-	-	-	49,020	33,499	82,519	992,957
2021	871,371	193,525	1,044	1,065,940	-	-	-	51,515	31,064	82,579	1,148,519
2022	662,407	154,837	892	818,136	-	-	-	54,355	28,292	82,647	900,784
2023	569,691	123,511	670	693,872	-	-	-	36,960	25,428	62,388	756,260
2024	493,508	96,543	246	590,297	-	-	-	28,990	23,443	52,433	642,730
2025	426,015	73,587	69	499,671	-	-	-	30,625	21,848	52,473	552,145
2026	285,858	55,483	31	341,371	-	-	-	32,360	20,164	52,524	393,896
2027	295,591	41,575		337,166	-	-	-	34,190	18,384	52,574	389,740
2028	101,915	31,509		133,424	-	-	-	36,125	16,504	52,629	186,053
2029	178,335	24,368		202,703	-	-	-	38,170	14,517	52,687	255,390
2030	184,090	14,966		199,056	-	-	-	40,330	12,418	52,748	251,803
2031	192,960	5,067		198,027	-	-	-	42,610	10,199	52,809	250,837
2032	-	-	-	-				45,020	7,856	52,876	52,876
2033	-	-	-	-				47,565	5,380	52,945	52,945
2034	-	-	-	-				50,250	2,764	53,014	53,014
TOTAL	$15,173,819	$6,997,318	$91,428	$22,259,565	$1,728,305	$432,845	$2,161,150	$1,288,595	$936,027	2,224,622	$26,645,337

SOURCE: Office of the State Treasurer and Office of the Comptroller.

(1) Amounts are preliminary.

(2) Includes three series of outstanding crossover refunding bonds, two of which are special obligation bonds and one of which consists of federal grant anticipation notes. The refunding escrows funded by these bonds and related premiums are used to pay interest on the refunding bonds until the refunded bonds are callable and then to redeem the refunded bonds. Interest on the refunded bonds prior to redemption continues to be paid from pledged revenues as before. The amount of debt is calculated based on net proceeds as provided under state finance law relative to debt limits.

General Obligation Contract Assistance Liabilities

Massachusetts Convention Center Authority. The Massachusetts Convention Center Authority (MCCA) was created for the purpose of promoting the economic development of the Commonwealth through the operation of the Hynes Convention Center, the Boston Common Parking Garage and the Springfield Convention Center (now called the MassMutual Center). In addition, the MCCA has overseen the construction of and is now operating the Boston Convention and Exhibition Center. The MCCA has issued bonds which are fully secured by contract assistance payments by the Commonwealth, which payments are limited by statute to an amount equal to the annual debt service on $200 million of bonds outstanding at any one time. The assistance contract is a general obligation of the Commonwealth for which its full faith and credit is pledged. As of April 2, 2007, the MCCA had $14.7 million of such bonds outstanding. On May 9, 2007, pursuant to recently enacted legislation, the Commonwealth sold its own general obligation bonds to refund these MCCA bonds and thereby refinance its outstanding contract assistance liability. The Commonwealth bonds are expected to be delivered on May 30, 2007. The outstanding MCCA bonds do not include the bonds issued to finance construction of the Boston Convention and Exhibition Center and the renovation and expansion of the MassMutual Center; these projects were financed by the issuance of Commonwealth special obligation bonds.

Foxborough Industrial Development Financing Authority. Pursuant to legislation approved May 24, 1999, the Commonwealth entered into a contract for financial assistance with the Foxborough Industrial Development Financing Authority in June, 2000 obligating the Commonwealth to pay the full amount of the debt service on bonds issued to finance up to $70 million of capital expenditures for infrastructure improvements related to the construction of a new professional football stadium in the town of Foxborough. The obligation of the Commonwealth to make such payments is a general obligation for which the full faith and credit of the Commonwealth is pledged. Under the authorizing legislation the Commonwealth is to receive $400,000 per year in parking fees for stadium-related events, an administrative fee of $1 million per year from the stadium lessee and will be entitled to recover from the stadium lessee a portion of its contract assistance payments if professional football ceases being played at the stadium during the term of the bonds. As of April 2, 2007, the Foxborough Industrial Development Financing Authority had $60.4 million of such bonds outstanding. No more such bonds may be issued under current law. On May 9, 2007, pursuant to recently enacted legislation, the Commonwealth sold its own general obligation bonds to refund these Foxborough bonds and thereby refinance its outstanding contract assistance liability. The Commonwealth bonds are expected to be delivered on May 30, 2007.

Massachusetts Turnpike Authority. The Commonwealth is obligated to pay contract assistance to the Massachusetts Turnpike Authority pursuant to legislation enacted in 1998 and a contract for financial assistance dated as of February 19, 1999 between the Turnpike Authority and the Commonwealth. The payments are in recognition of the financial burden imposed on the Turnpike Authority by virtue of its assumption of the responsibility for operation and maintenance of certain roadways in the Metropolitan Highway System that were formerly maintained by the Commonwealth. The Commonwealth's obligation to make such payments is a general obligation for which the faith and credit of the Commonwealth is pledged for the benefit of the Turnpike Authority and its bondholders. The contract provides that no later than September 1 of each year the Turnpike Authority is to submit to the Secretary of Transportation a certificate setting forth the total amount of costs incurred by the Turnpike Authority during the prior fiscal year in connection with the operation and maintenance of the roadways covered by the contract. The contract further provides that as soon as practicable following receipt of such certificate, but no later than December 1 of such year, the Commonwealth is to pay the Turnpike Authority the amount set forth in such certificate, subject to Commonwealth review, provided that such annual payment may not be more than $25 million. Payments are required under the contract through fiscal year 2045.

Massachusetts Water Pollution Abatement Trust. The Massachusetts Water Pollution Abatement Trust was created to implement the Commonwealth's state revolving fund program under Title VI of the federal Clean Water Act and the federal Safe Drinking Water Act. The Trust is authorized to apply for and accept federal grants and associated Commonwealth matching grants to capitalize the revolving funds and to issue debt obligations to make loans to local governmental units to finance eligible water pollution abatement and water treatment projects. Under state law, each loan made by the Trust is required to provide for debt service subsidies or other financial assistance sufficient to result in most new loans being the financial equivalent of a two percent interest loan. To subsidize its loans, the Trust receives contract assistance payments from the Commonwealth. Under the Trust's enabling act, the annual contract assistance maximum for the Clean Water Act program is $71 million, and the contract assistance maximum for the Safe Drinking Water Act program is $17 million. The contract assistance agreements constitute general obligations of the Commonwealth for which its faith and credit are pledged, and the Trust's right to receive payments thereunder may be pledged by the Trust as security for repayment of the Trust's debt obligations. As of May 1, 2007, the Trust had approximately $3.012 billion of bonds outstanding. Approximately 17% of the aggregate debt service on such bonds is expected to be paid from Commonwealth contract assistance.

The following table sets forth the Commonwealth's general obligation contract assistance requirements pursuant to contracts with the Massachusetts Convention Center Authority, MassDevelopment, the Foxborough Industrial Development Financing Authority, the Massachusetts Turnpike Authority and the Massachusetts Water Pollution Abatement Trust. These figures are as of July 1, 2006, except that the Massachusetts Water Pollution Abatement Trust figures are as of May 1, 2007.

General Obligation Contract Assistance Requirements (in thousands)(1)

Fiscal Year	Massachusetts Convention Center Authority	Massachusetts Water Pollution Abatement Trust	Massachusetts Turnpike Authority(2)	Foxborough Industrial Development Financing Authority	Total
2007	$ 2,532	$ 63,700	$ 25,000	$ 5,337	$ 96,569
2008	2,533	67,498	25,000	5,336	100,367
2009	2,534	65,674	25,000	5,340	$98,548
2010	2,534	65,600	25,000	5,338	$98,472
2011	2,534	64,621	25,000	5,338	$97,493
2012	2,533	62,994	25,000	5,338	$95,865
2013	2,536	60,499	25,000	5,341	$93,376
2014	2,536	57,458	25,000	5,339	$90,333
2015	--	56,015	25,000	5,337	$86,352
2016	--	51,190	25,000	5,337	$81,527
2017	--	44,068	25,000	5,336	$74,404
2018	--	38,355	25,000	5,339	$68,694
2019	--	38,558	25,000	5,336	$68,894
2020	--	32,993	25,000	5,335	$63,328
2021	--	25,473	25,000	5,337	$55,810
2022	--	16,306	25,000	5,340	$46,646
2023	--	16,718	25,000	5,340	$47,058
2024	--	8,712	25,000	5,340	$39,052
2025	--	4,757	25,000	5,340	$35,097
2026 through 2045	--	4,273	500,000(3)	--	504,273
Total	$20,272	$845,462	$975,000	$101,424	$1,942,158

SOURCES: Massachusetts Water Pollution Abatement Trust and Massachusetts Convention Center Authority columns –Office of the State Treasurer; Foxborough Industrial Development Financing Authority and Massachusetts Turnpike Authority columns - Executive Office for Administration and Finance.

(1) Totals may not add due to rounding.

(2) Reimbursement funds operating and maintenance costs expended in the prior state fiscal year. These costs are projections and are subject to review pursuant to the contract for financial assistance. These projections do not include certain costs submitted by the Massachusetts Turnpike Authority for reimbursement, which the Executive Office for Administration and Finance has determined not to be reimbursable under the contract. The disputed costs remain subject to review and discussion.

(3) Signifies $25 million per year for fiscal 2026 to fiscal 2045, inclusive.

Budgetary Contract Assistance Liabilities

Plymouth County Certificates of Participation. In May, 1992, Plymouth County caused to be issued approximately $110.5 million of certificates of participation to finance the construction of a county correctional facility. In March 1999, Plymouth County caused to be issued approximately $140.1 million of certificates of participation to advance refund the 1992 certificates, construct an administration office building and auxiliary facilities near the county correctional facility and fund repairs and improvements to the facility. The Commonwealth, acting through the Executive Office of Public Safety and the Department of Correction, is obligated under a memorandum of agreement with Plymouth County to pay for the availability of 380 beds (out of 1,140) in the facility, regardless of whether 380 state prisoners are housed therein. The amounts payable by the Commonwealth will at least equal the debt service on the outstanding certificates of participation, but are subject to appropriation of such amounts by the Legislature in the annual budgetary line item for the Executive Office of Public Safety. The obligation of the Commonwealth under the memorandum of agreement does not constitute a general obligation or a pledge of the credit of the Commonwealth. As of April 2, 2007, such certificates were outstanding in the aggregate principal amount of $107.2 million.

City of Chelsea Commonwealth Lease Revenue Bonds. In November, 1993, the Chelsea Industrial Development Financing Authority issued approximately $95.8 million of lease revenue bonds. The proceeds of the bonds were loaned to the Massachusetts Industrial Finance Agency (now MassDevelopment) and applied to the cost of the Massachusetts Information Technology Center, a tax processing facility of the Department of Revenue and a data processing information system center for the Department and for certain other departments and agencies of the Commonwealth. The bonds bear interest at a variable rate, and under an interest rate swap agreement that was entered into at the time, MassDevelopment receives variable rate payments with respect to the full amount of the bonds and is obligated to make fixed rate payments in exchange therefor. Simultaneously with the issuance of the bonds, the Commonwealth entered into a 30-year lease, which provides for the payment of debt service on the bonds and certain other expenses associated with the project. The obligations of the Commonwealth do not constitute a general obligation or a pledge of the credit of the Commonwealth or of MassDevelopment and are subject to annual appropriation by the Legislature. As of April 2, 2007, such bonds were outstanding in the aggregate principal amount of $73.1 million.

Route 3 North Transportation Improvements Association Commonwealth Lease Revenue Bonds. In August, 2000, the Route 3 North Transportation Improvements Association issued approximately $394.3 million of lease revenue bonds to finance the reconstruction and widening of a portion of state Route 3 North. In May, 2002, the Route 3 North Transportation Improvements Association issued approximately $312.7 million of additional lease revenue bonds, $305.6 million of which were issued as refunding bonds. In connection with the financing, the Commonwealth leased the portion of the highway to be improved to the Association, and the Association leased the property back to the Commonwealth pursuant to a sublease. Under the sublease the Commonwealth is obligated to make payments equal to the debt service on the bonds and certain other expenses associated with the project. The obligations of the Commonwealth do not constitute a general obligation or a pledge of the credit of the Commonwealth and are subject to annual appropriation by the Legislature. As of April 2, 2007, the Route 3 North Transportation Improvements Association had $680.5 million of such lease revenue bonds outstanding. Pursuant to recently enacted legislation, the Commonwealth is authorized to refund these bonds by issuing its own general obligation bonds and thereby refinancing all or a portion of its outstanding lease liability. On May 9, 2007, the Commonwealth sold general obligation bonds to refund approximately $53.4 million of the lease revenue bonds. The Commonwealth bonds are expected to be delivered on May 30, 2007.

Saltonstall Building Redevelopment Corporation Project. In May, 2002, MassDevelopment issued $195.8 million of lease revenue bonds pursuant to an agreement to loan the proceeds of the bonds to the MassDevelopment/ Saltonstall Building Redevelopment Corporation. The loan was used to finance the redevelopment of the Saltonstall State Office Building. Under the provisions of the legislation relating to the building's redevelopment, the building was leased to MassDevelopment/Saltonstall Building Redevelopment Corporation for a term of up to 50 years, with extension terms permitted for an aggregate of 30 more years. MassDevelopment/Saltonstall Building Redevelopment Corporation is obligated to pay $2.45 million per year to the Commonwealth for the lease. Due to lower than anticipated cash flow and required priority funding of the project reserve, rent and interest payments to the Commonwealth have accrued in the amounts of $2.65 million and $81,335 respectively, as of March 31, 2007. Rent payments will commence once the project reserve fund is replenished to $5 million, which is anticipated for late fiscal year 2008. MassDevelopment/ Saltonstall Building Redevelopment Corporation has renovated the building and subleased half of it back to the Commonwealth for office space and related parking (for a comparable lease term), in respect of which sublease the Commonwealth makes sublease payments to MassDevelopment/Saltonstall Building Redevelopment Corporation. The remainder of the building has been redeveloped as private office space, as well as private housing units and retail establishments. The obligations of the Commonwealth under the office sublease do not constitute a general obligation or a pledge of the credit of the Commonwealth and are subject to annual appropriation by the Legislature. The Commonwealth's full year costs include $7.065 million per year of base rent and parking space rent for the first five years, after which the parking space rent may be adjusted for fair market value every five years. In addition, included in the table below are the Commonwealth's estimated pro-rata share of office operating expense reimbursements, escalating at 3% per year and also the Commonwealth's replacement reserve contribution calculated at $.21 per rental square foot per year. As of March 31, 2007, MassDevelopment/Saltonstall Building Redevelopment Corporation had $193.96 million of such lease revenue bonds outstanding for the Saltonstall Building redevelopment project.

Long-Term Operating Leases and Capital Leases. In addition to Commonwealth-owned buildings and facilities, the Commonwealth leases additional space from private parties. In certain circumstances, the Commonwealth has acquired certain types of capital assets under long-term capital leases; typically, these arrangements relate to computer and telecommunications equipment and to motor vehicles. Minimum future rental expenditure commitments of the Commonwealth under operating leases and long-term principal and interest obligations related to capital leases in effect at June 30, 2006 are set forth in the table below (except that the figures for the Saltonstall Building are as of March 31, 2007). These amounts represent expenditure commitments of both budgeted and non-budgeted funds.

Budgetary Contract Assistance Liabilities (in thousands)(1)

Fiscal Year	Plymouth County Certificates of Participation	City of Chelsea Commonwealth Lease Revenue Bonds	Route 3 North Transportation Improvements Association Commonwealth Lease Revenue Bonds	MassDevelopment/ Saltonstall Building Redevelopment Corporation Lease Revenue Bonds(3)	Other Leases	Total
2007	$10,246	$6,465	$26,756	$9,369	$182,868	$235,704
2008	10,243	6,465	26,757	9,437	142,984	195,886
2009	10,247	6,465	26,756	9,506	97,722	150,696
2010	10,244	6,465	26,755	9,578	77,337	130,379
2011	10,245	6,453	26,756	9,693	72,349	125,496
2012	10,240	6,453	26,754	9,770	32,034	85,251
2013	10,245	6,453	26,754	9,848	32,034	85,334
2014	10,244	6,453	26,756	9,929	32,034	85,416
2015	10,250	6,453	26,756	10,012	32,034	85,505
2016	10,245	6,435	26,754	10,155	32,034	85,623
2017	10,238	6,435	26,758	10,243	14,639	68,313
2018	10,244	6,435	26,756	10,334	14,639	68,408
2019	10,244	6,435	26,754	10,428	14,639	68,500
2020	10,246	6,435	26,757	10,524	14,639	68,601
2021	10,243	6,435	26,754	10,658	14,639	68,729
2022	10,252	6,395	26,752	10,760	11,542	65,701
2023	--	6,379	26,752	10,866	11,542	55,539
2024	--	--	26,754	10,974	11,542	49,270
2025 through 2034	--	--	240,827(2)	116,923	88,509	446,260
Total	$163,916	$109,509	$722,418	$299,008	$929,760	$2,224,611

SOURCES: Other Leases column –Office of the Comptroller; all other columns -- Executive Office for Administration and Finance.
(1) Totals may not add due to rounding.
(2) Approximately $27 million per year for fiscal 2025 through fiscal 2033, inclusive.
(3) Cash flows from the Commonwealth represent gross payments to MassDevelopment, including projections of the Commonwealth's share of operating costs and other items that are subject to change.

Contingent Liabilities

Massachusetts Bay Transportation Authority. The MBTA issues its own bonds and notes and is also responsible for the payment of obligations issued by the Boston Metropolitan District prior to the creation of the MBTA in 1964. Prior to July 1, 2000, the Commonwealth supported MBTA bonds and notes through guaranties of the debt service on its bonds and notes, contract assistance generally equal to 90% of the debt service on outstanding MBTA bonds and payment of the MBTA's net cost of service (current expenses, including debt service, minus current income). Beginning July 1, 2000, the Commonwealth's annual obligation to support the MBTA for operating costs and debt service is limited to a portion of the revenues raised by the Commonwealth's sales tax, but the Commonwealth remains contingently liable for the payment of MBTA bonds and notes issued prior to July 1, 2000. The Commonwealth's obligation to pay such prior bonds is a general obligation for which its full faith and credit have been pledged. As of April 2, 2007, the Massachusetts Bay Transportation Authority had approximately $1.4 billion of such prior bonds outstanding. Such bonds are currently scheduled to mature annually through fiscal

2030, with annual debt service in the range of approximately $198 million to $175 million through fiscal 2013 and declining thereafter. See "SELECTED FINANCIAL DATA – Recent Financial Restructurings; *Massachusetts Bay Transportation Authority*."

Woods Hole, Martha's Vineyard and Nantucket Steamship Authority. The Steamship Authority operates passenger ferries to Martha's Vineyard and Nantucket. The Steamship Authority issues its own bonds and notes. Commonwealth support of the bonds and notes of Steamship Authority includes a Commonwealth guaranty pursuant to statutory provisions requiring the Commonwealth to provide the Authority with funds sufficient to meet the principal of and interest on their bonds and notes as they mature to the extent that funds sufficient for this purpose are not otherwise available to such entity and the Commonwealth's payment, under applicable statutory provisions, of the net cost of service of the Steamship Authority (current expenses, including debt service, minus current income). The Steamship Authority is currently self-supporting, requiring no net cost of service or contract assistance payments. As of April 2, 2007, the Steamship Authority had approximately $60 million of bonds outstanding and no notes outstanding. The Commonwealth's obligations to the Steamship Authority are general obligations for which its full faith and credit have been pledged.

University of Massachusetts Building Authority and Massachusetts State College Building Authority. Two higher education building authorities, created to assist institutions of public higher education in the Commonwealth, may issue bonds which are guaranteed as to their principal and interest by the Commonwealth. The guaranty is a general obligation of the Commonwealth for which its full faith and credit is pledged. In addition to such guaranty, certain revenues of these authorities, including dormitory rental income and student union fees, are pledged to their respective debt service requirements. As of April 2, 2007, the University of Massachusetts Building Authority had approximately $29.8 million of Commonwealth-guaranteed debt outstanding, and the Massachusetts State College Building Authority had approximately $56.1 million of Commonwealth-guaranteed debt outstanding.

Massachusetts Housing Finance Agency (MassHousing). MassHousing is authorized to issue bonds to finance multi-family housing projects within the Commonwealth and to provide mortgage loan financing with respect to certain single-family residences within the Commonwealth. Such bonds are solely the obligations of MassHousing, payable directly or indirectly from, and secured by a pledge of, revenues derived from MassHousing's mortgage on or other interest in the financed housing. MassHousing's enabling legislation also permits the creation of a capital reserve fund in connection with the issuance of such bonds. No single-family housing bonds secured by capital reserve funds are outstanding, and no such bonds have been issued by MassHousing since 1985. As of June 30, 2006, MassHousing had outstanding approximately $419.8 million of multi-family housing bonds secured by capital reserve funds. Any such capital reserve fund must be in an amount at least equal to the maximum annual debt service in any succeeding calendar year on all outstanding bonds secured by such fund. All such capital reserve funds are maintained at their required levels. If amounts are withdrawn from a capital reserve fund to pay debt service on bonds secured by such fund, upon certification by the chairperson of MassHousing to the Governor of any amount necessary to restore the fund to the above-described requirement, the Legislature may, but is not legally bound to, make an appropriation in such amount. No such appropriation has been necessary to date.

Authorized But Unissued Debt

General obligation bonds of the Commonwealth are authorized to correspond with capital appropriations. See "COMMONWEALTH BUDGET AND FINANCIAL MANAGEMENT CONTROLS – Capital Investment Process and Controls." Over the last decade, the Commonwealth has typically had a large amount of authorized but unissued debt. However, the Commonwealth's actual expenditures for capital projects in a given year relate more to the capital needs which the Commonwealth determines it can afford to finance in such year than to the total amount of authorized but unissued debt. The table below presents authorized but unissued debt at year end:

Authorized but Unissued Debt (in thousands)

Fiscal Year	Authorized But Unissued Debt
2002	$8,483,658
2003	8,721,581
2004	6,827,993
2005	9,506,821
2006	7,668,331

SOURCE: Office of the Comptroller.

Authorized but unissued debt is measured in accordance with the statutory basis of accounting, which is different from GAAP. Only the net proceeds of bonds issued (exclusive of underwriters' discount, costs of issuance and other financing costs) are deducted from the amount of authorized but unissued debt. Therefore, the change in authorized but unissued debt at the end of any fiscal year is not intended to correlate to the change in the principal amount of debt outstanding as measured and reported in conformity with GAAP.

There is $38 million of authorized but unissued debt under Chapter 33 of the Acts of 1991 that can only be issued as special obligation bonds secured by receipts in the Commonwealth's Highway Fund. See "Special Obligation Debt." In addition, several of the statutes authorizing general obligation bonds for transportation purposes also authorize such bonds to be issued as special obligation highway bonds, at the discretion of the Governor and the State Treasurer.

STATE WORKFORCE

The following table sets forth information regarding the Commonwealth's workforce as of the end of fiscal years 2002 through 2006 and as of December 31, 2006. The table does not reflect the reorganization of executive departments that took effect on April 9, 2007.

Budget-Funded Workforce (1)

	June 2002	June 2003	June 2004	June 2005	June 2006	December 2006
Executive Office	80	94	73	71	66	57
Office of the Comptroller	107	102	102	124	122	121
Executive Departments						
Administration and Finance	2,974	2,921	2,791	2,913	2,990	3,006
Environmental Affairs	2,312	2,156	1,997	1,984	2,057	2,032
Housing and Community Development	109	98	92	94	91	90
Early Education and Care	-	-	-	-	164	194
Health and Human Services	21,803	21,440	20,682	21,066	21,022	21,039
Transportation	843	445	344	1,139(2)	1,078	1,064
Board of Library Commissioners	18	13	12	11	12	13
Economic Development	1,094	922	879	935	960	959
Department of Education	277	248	223	241	266	271
Board of Higher Education	14,038	14,117	11,844	13,198	12,932	14,388
Public Safety	9,567	9,148	8,765	8,109(2)	8,430	8,460
Elder Affairs	43	38	28	51	34	40
Subtotal under Governor's authority	53,265	51,742	47,832	49,934	50,223	51,735
Judiciary	7,379	7,233	7,175	7,435	7,630	7,896
Other (3)	7,319	7,256	7,220	7,352	7,594	7,799
Total	67,963	66,232	62,227	64,721	65,447	67,430

SOURCE: Executive Office for Administration and Finance.

(1) Excludes employees whose positions are established in accounts funded by capital projects funds, direct federal grants, expendable trusts and other non-appropriated funds, as well as seasonal help, members of boards and commissions and staff of independent authorities. Numbers represent full-time equivalent positions (FTEs), not individual employees. Total may not add due to rounding.

(2) Effective July, 2004, the Registry of Motor Vehicles was transferred from the Executive Office of Public Safety to the Executive Office of Transportation and Public Works. Approximately 814 FTEs were involved in the transfer.

(3) Other includes members of the Legislature and their staff, the offices of the State Treasurer, Secretary, Auditor and Attorney General, the eleven District Attorneys, the seven former county sheriffs that have become state agencies, and other agencies independent from the Governor.

Unions and Labor Negotiations

Under Chapter 150E of the General Laws, all employees of the Commonwealth, with the exception of managerial and confidential employees and employees of the legislature, have the right to bargain collectively with the Commonwealth through certified employee organizations recognized as exclusive bargaining representatives for appropriate bargaining units. Collective bargaining with employees of the Commonwealth's colleges and universities, its judicial branch and the Lottery Commission generally is conducted directly by those entities. The Human Resources Division of the Executive Office for Administration and Finance conducts the collective bargaining negotiations with all other employees of the Commonwealth. Such negotiations may cover wages, hours and other terms and conditions of employment, but may not include the levels of pension and group insurance benefits. All labor agreements negotiated by the Human Resources Division are subject to approval by the Secretary of Administration and Finance and, once approved, are forwarded to the Legislature for funding approval. Labor contracts are often funded by supplemental appropriations.

The Trial Court, the Lottery Commission, state sheriffs, the Registries of Deeds under the control of the Secretary of the Commonwealth and public higher education management negotiate directly with their respective employee representatives, but all wage increases and other economic provisions contained in agreements negotiated by the Lottery Commission, state sheriffs, Registries of Deeds and higher education management are subject to the review of the Governor and to funding approval by the Legislature. If the Governor does not recommend the requested appropriation to fund contractual increases, he may refer the contracts back to the parties for further negotiation.

Approximately 39,331 executive branch full-time-equivalent state employees are organized in 12 bargaining units, the employees of the Commonwealth's colleges and universities are organized in 28 bargaining units, and the employees of the judicial branch and the Lottery Commission are organized in seven bargaining units. Public employees of the Commonwealth do not have a legal right to strike or otherwise withhold services.

Negotiations are currently underway with the Massachusetts Correction Officers Federated Union, representing employees in Unit 4, to replace their contract which expired December 31, 2003; with the Coalition of Public Safety, representing employees in Unit 5, to replace their contract which expired June 30, 2004; and with the Service Employees International Union, representing employees in Units 8 and 10, to replace their contracts which expired December 31, 2006.

The Commonwealth has outstanding agreements with the following bargaining units (negotiations are underway with the units that have contracts due to expire in June, 2007):

(1) The International Brotherhood of Correctional Officers/National Association of Government Employees has a one-year contract from July, 2006 to June, 2007 that included a 3% increase in July, 2006. The total estimated cost of the contract is $281,356.

(2) The Massachusetts Organization of State Engineers and Scientists has a one-year contract from July, 2006 to June, 2007 that provided a 3% increase in July, 2006. The total estimated cost of the contract is $2.5 million.

(3) The National Association of Government Employees, representing Units 1, 3 and 6, has a one-year contract from July, 2006 to June, 2007 that provided a 3% increase in July, 2006. The total estimated cost of the contract is $14.6 million.

(4) The Alliance Unit 2 (American Federation of State, Country and Municipal Employees) has a one-year contract from July, 2006 to June, 2007 that provided a 3% increase in July, 2006. The total estimated cost of the contract is $18.6 million.

(5) The Massachusetts Nurses Association is under contract through December, 2007. A one-year contract from July, 2004 to June, 2005 did not provide for any salary increases. A two-and-a-half-year contract from July, 2005 to December, 2007 provided for a 3% increase in July, 2005, a directed job upgrade of approximately 4.4% for specific titles within the unit, including nurses, effective January, 2006, a 2% increase in January, 2006, a

3% increase in July, 2006 and a 1.5% increase in January, 2007 and provides for a 1.5% increase in July, 2007. The total estimated cost of the contract is $58.6 million.

(6) The State Police Association of Massachusetts is under contract until December, 2008. A two-year contract from January, 2007 to December, 2008 provided a 3.75% increase in January, 2007 and provides a 3.75% increase in January, 2008. The total estimated cost of the contracts is $108.7 million.

The following table sets forth information regarding the 12 bargaining units that are within the responsibility of the Human Resources Division.

Human Resources Division Bargaining Units(1)(2)

Contract Unit	Bargaining Union	Type of Employee	FTEs	Contract Expiration Dates
1	National Association of Government Employees	Clerical	2,893	6/30/07
2	Alliance/American Federation of State, County & Municipal Employees and Service Employees International Union	Institutional services	9,325	6/30/07
3	National Association of Government Employees	Skilled trades	547	6/30/07
4	Massachusetts Correction Officers Federated Union	Corrections	3,783	12/31/03
4A	Corrections Captains	Corrections	86	6/30/07
5	Coalition of Public Safety	Law enforcement	225	6/30/04
5A	State Police Association of Massachusetts	State Police	1,952	12/31/08
6	National Association of Government Employees	Administrative professionals	8,088	6/30/07
7	Massachusetts Nurses Association	Health professionals	1,723	12/31/07
8	Alliance/Service Employees International Union	Social workers	7,279	12/31/06
9	Massachusetts Organization of State Engineers and Scientists	Engineers/scientists	2,835	6/30/07
10	Alliance/Service Employees International Union	Secondary education	596	12/31/06
	Total		39,331	

SOURCE: Executive Office for Administration and Finance.
(1) Totals may not add due to rounding.
(2) Numbers represent full-time equivalent filled positions (FTEs) in the standard workforce as of March 17, 2007 whose positions are established in accounts funded by all sources (the annual operating budget, capital projects funds, direct federal grants and expendable trusts and other non-appropriated funds).

LEGAL MATTERS

There are pending in state and federal courts within the Commonwealth and in the Supreme Court of the United States various suits in which the Commonwealth is a party. In the opinion of the Attorney General, no litigation is pending or, to her knowledge, threatened which is likely to result, either individually or in the aggregate, in final judgments against the Commonwealth that would affect materially its financial condition.

Programs and Services

From time to time actions are brought against the Commonwealth by the recipients of governmental services, particularly recipients of human services benefits, seeking expanded levels of services and benefits and by the providers of such services challenging the Commonwealth's reimbursement rates and methodologies. To the extent that such actions result in judgments requiring the Commonwealth to provide expanded services or benefits or pay increased rates, additional operating and capital expenditures might be needed to implement such judgments.

Ricci v. Murphy. Challenges by residents of five state schools for the retarded (U.S. District Court C.A. No. 72-469-T) resulted in a consent decree in the 1970's, which required the Commonwealth to upgrade and rehabilitate the facilities in question and to provide services and community placements in western Massachusetts. The District Court issued orders in October, 1986, leading to termination of active judicial supervision. On May 25, 1993, the District Court entered a final order vacating and replacing all consent decrees and court orders. In their place, the final order requires lifelong provision of individualized services to class members and contains requirements regarding staffing, maintenance of effort (including funding) and other matters.

On July 14, 2004, a subset of plaintiffs filed a motion to reopen the case and enforce the final order of May 25, 1993, asserting various reasons why the Department of Mental Retardation is not in compliance with the 1993 final order, mostly relating to the Commonwealth's plan to close the Fernald Developmental Center. Another subgroup of plaintiffs (representing class members from the Dever and Wrentham Developmental Centers) have sought to re-open the case as well. The Department filed a responsive pleading on August 16, 2004, asserting that all of the requirements of the final order were met. On August 28, 2004, the Disability Law Center filed a motion to intervene, asserting an interest on behalf of persons with disabilities in the closing of the facility, which was allowed. On February 8, 2006, the judge ordered all transfers from Fernald halted indefinitely and appointed United States Attorney Michael Sullivan as court monitor over the closure of Fernald. On March 6, 2007, the United States Attorney issued his long-awaited report, in which he did not find any violations by the Department of federal or state law, but nonetheless recommended that the Fernald Developmental Center remain open to serve any residents who wish to remain there. Shortly thereafter, the Court declared that its 2006 order prohibiting transfers from the Fernald Center (absent a specific written order to the contrary) would remain in effect at least until June 2007.

Rolland v. Romney (U.S. District Court C.A. No. 98-32208 KPN) is a class action by mentally retarded nursing home patients seeking community placements and services. The court approved a settlement agreement entered into by the parties, which will provide certain benefits to nursing home residents with mental retardation and other developmental disabilities until 2007. The Department of Mental Retardation estimates that the agreement will cost approximately $5 million per fiscal year for seven years.

Health Care for All v. Romney et al. (United States District Court). A group of individual plaintiffs brought this action for injunctive and declaratory relief, challenging the Commonwealth's administration of the MassHealth dental program. Specifically, the plaintiffs asserted that the Commonwealth's administration of the dental program fails to comply with federal Medicaid law. On February 8, 2006, the United States District Court entered judgment against the state defendants on three counts of the plaintiffs' Third Amended Complaint with respect to MassHealth-eligible members under age 21. Pursuant to that judgment, the Commonwealth must develop and implement a remedial plan to improve access to Medicaid-covered dental services for MassHealth-eligible members under age 21. Crucial aspects of the plan, including certain regulatory changes and the retention of a third-party administrator for the MassHealth dental plan, have already been implemented, but it is anticipated that additional program costs necessary to comply with the judgment will be incurred over the next several fiscal years. It is not possible, at this time, to accurately estimate the amount of likely future program costs that will be required to comply with the judgment.

Rosie D. v. Governor. The plaintiffs, MassHealth-eligible children with behavioral-health issues, asserted claims under the Early and Periodic Screening, Diagnostic and Treatment provisions of the federal Medicaid law. Specifically, the plaintiffs asserted that the Commonwealth is required to but does not provide them with intensive home-based mental health services. The plaintiffs have not quantified the cost of the services they seek. Trial was held from April 25 through June 9, 2005. On January 26, 2006, the Court issued its decision finding in favor of the plaintiffs on two of three counts of the complaint and ordering the parties to meet and attempt to achieve an agreed-upon plan. The parties did not agree on a remedial plan, but submitted separate plans to the Court. On February 22, 2007, the Court issued an order adopting the defendants' proposed plan with provisos. This plan, scheduled to be implemented in stages through mid-2009, will significantly expand access to services for MassHealth-eligible children with behavioral-health issues.

Disability Law Center, Inc. v. Massachusetts Department of Correction et al (United States District Court). In this recently filed suit, prompted by recent prisoner suicides, the plaintiff alleges that the Department of Correction subjects inmates with mental illness to cruel and unusual punishment by placing them in segregated confinement. The complaint seeks, among other things, an injunction ordering the Department to construct "maximum security residential treatment units" as an alternative to segregation. Some or all of the changes requested in the complaint were already under consideration by the Department at the time the complaint was filed.

The Brain Injury Association of Massachusetts v. Deval Patrick et al. In this threatened litigation, the plaintiffs, who claim to represent a class of over 500 persons with serious brain injuries, allege that the Commonwealth's failure to provide long-term care in community settings has resulted in their unnecessary institutionalization. A demand letter has been sent and a draft complaint provided, but the complaint has not yet been filed.

Taxes

There are several tax cases pending that could result in significant refunds if taxpayers prevail. It is the policy of the Attorney General and the Commissioner of Revenue to defend such actions vigorously on behalf of the Commonwealth, and the descriptions that follow are not intended to imply that the Commissioner has conceded any liability whatsoever. As of May 9, 2007, approximately $102 million in contingent liabilities exist in the aggregate in tax cases pending before the Appellate Tax Board, Appeals Court or Supreme Judicial Court. These contingent liabilities include both taxes and interest. Several cases comprise a sizeable share of these liabilities.

TJX Companies v. Commissioner of Revenue (Appellate Tax Board). The taxpayer is challenging a tax liability of approximately $23 million arising from the Commissioner's disallowance of deductions for various royalty payments and interest taken in connection with transactions between several subsidiaries of the taxpayer. On August 8, 2006, the Appellate Tax Board issued its decision in favor of the Commissioner. The Board's findings of fact and report have been requested but not yet issued.

MBNA America Bank v. Commissioner of Revenue, Greenwood Trust Co. v. Commissioner of Revenue, Providian Nat'l Bank v. Commissioner of Revenue (Appellate Tax Board). These are financial excise "nexus" cases involving credit card businesses. The total potential refund is approximately $24.1 million. On October 13, 2006, the Appellate Tax Board issued a decision for the Commission in the similar case of *Capital One Bank and Capital One F.S.B.* The findings of fact and report in *Capital One* have been requested but not yet issued.

Other Revenues

Commonwealth of Massachusetts v. Philip Morris Inc., RJ Reynolds Tobacco Company, Lorillard Tobacco Company, et al. (Supreme Judicial Court). This matter arises under the Tobacco Master Settlement Agreement (MSA), entered into in 1998, that settled litigation and claims by Massachusetts and 45 other states, the District of Columbia, Puerto Rico, Guam, the Virgin Islands, American Samoa and the Northern Marianas (collectively the "States"), against the major tobacco manufacturers. Under the MSA, payments made by the Original Participating Manufacturers (OPMs) and subsequent Participating Manufacturers (collectively the "Participating Manufacturers" or "PMs") are potentially subject to a number of adjustments. One such adjustment is the Non-Participating Manufacturer (NPM) Adjustment, which can be triggered if, among other things, the PMs suffer a specified market share loss attributable in significant part to their compliance with the MSA. Because it has been determined that the PMs did experience such market-share loss in 2003 and 2004, the PMs claim that they are entitled to offset the annual settlement payments due in April, 2006 and April, 2007 by the amount of their alleged overpayments in 2003 and 2004. The total potential NPM Adjustment for all states is approximately $1.2 billion for 2003 and $1.1 billion for 2004, with Massachusetts' share approximately $45-$50 million for each year.

Under the MSA, a state is immune from the NPM adjustment if the state continuously had a "qualifying statute," as defined in the MSA, "in full force and effect during the entire calendar year immediately preceding the year in which the payment in question is due, and diligently enforced the provisions of such statute during such entire calendar year." Massachusetts had such a "qualifying statute" in effect for the relevant period. Nonetheless, the PMs have asserted that Massachusetts (and all other states) failed to diligently enforce its qualifying statute in 2003 and 2004 as required by the MSA and have withheld payment on that basis. In connection with annual payments due on April 17, 2006, the PMs withheld approximately $30 million from the Commonwealth's share of payments for the 2003 diligent enforcement dispute. In connection with annual payments due on April 26, 2007, the PMs withheld approximately $27 million for the 2004 diligent enforcement dispute.

On April 18, 2006, upon the PMs' withholding of the payment due April 17, 2006, the Commonwealth filed an emergency motion in Middlesex County Superior Court seeking immediate payment of the disputed amount and a judicial declaration that Massachusetts diligently enforced its qualifying statute during 2003. The PMs cross-moved to compel arbitration. On June 22, 2006, the Superior Court allowed the PMs' motion to compel arbitration of the diligent-enforcement dispute and dismissed the Commonwealth's complaint. The Commonwealth appealed the Superior Court's order, and the Supreme Judicial Court allowed its application for direct appellate review. On April 23, 2007, the Supreme Judicial Court affirmed the Superior Court's order dismissing the Commonwealth's motion and compelling arbitration of the diligent enforcement dispute. The Supreme Judicial Court did not resolve the merits of the diligent enforcement dispute, leaving that determination to a panel of arbitrators selected in accordance with the terms of the MSA. At the present time, no arbitration panel has been selected, and no arbitration proceeding has been scheduled.

Grand River Enterprises Six Nations, Ltd. v. William Pryor et al. (United States District Court, New York). This case challenges certain state statutes enacted following the execution of the MSA. The plaintiffs are a group of companies that manufacture, import or distribute cigarettes manufactured by tobacco companies that are not parties to the MSA ("Non-Participating Manufacturers" or "NPMs"). The plaintiffs challenge so-called "escrow" or "qualifying" statutes enacted by various states, including Massachusetts, which require, among other things, each NPM to establish and fund an escrow or reserve account in an amount determined by the manufacturer's sales volume in the state. The plaintiffs sued 31 attorneys general, including the Massachusetts Attorney General, alleging that the defendants have commenced or threatened enforcement actions against them for failure to establish or adequately fund their escrow accounts. The plaintiffs contend that these enforcement actions and the related statutes are unconstitutional, violate the Sherman Anti-Trust Act and are pre-empted by the Federal Cigarette Labeling Act. Following ultimately unsuccessful litigation on the defendants' motion to dismiss, a scheduling conference was held on March 21, 2007, and discovery has commenced. If the plaintiffs ultimately obtain a judgment declaring the states' escrow statutes invalid, that result could make it more likely that the so-called NPM Adjustment referred to in the preceding paragraphs might apply to reduce future payments to Massachusetts and other states under the MSA in amounts that could be significant but cannot be estimated at this time.

Environment

The Commonwealth is engaged in various lawsuits concerning environmental and related laws, including an action brought by the U.S. Environmental Protection Agency alleging violations of the Clean Water Act and seeking to reduce the pollution in Boston Harbor. *United States v. Metropolitan District Commission*. See also *Conservation Law Foundation v. Metropolitan District Commission* and *United States v. South Essex Sewerage District*. The Massachusetts Water Resources Authority (MWRA), successor in liability to the Metropolitan District Commission, has assumed primary responsibility for developing and implementing a court-approved plan and timetable for the construction of the treatment facilities necessary to achieve compliance with the federal requirements. The MWRA currently projects that the total cost of construction of the wastewater facilities required under the court's order, not including combined sewer overflow (CSO) costs, will be approximately $3.142 billion in current dollars, with approximately $131 million to be spent after June 30, 2001. With CSO costs, the MWRA anticipates spending approximately $633 million after that date. Under the Clean Water Act, the Commonwealth may be liable for any cost of complying with any judgment in these or any other Clean Water Act cases to the extent the MWRA or a municipality is prevented by state law from raising revenues necessary to comply with such a judgment.

Wellesley College v. Commonwealth (Suffolk Superior Court). Wellesley College is seeking contribution from the Commonwealth for costs related to the clean up of environmental contamination on the Wellesley College campus and adjacent areas, including Lake Waban. On September 5, 2001, the court entered judgment incorporating a partial settlement between the parties, under which the College will fund a clean up of hazardous materials at the campus and the northern shoreline of Lake Waban, which is expected to cost approximately $40 million. The judgment has since been amended by agreement of the parties and approval by the court. Pursuant to the terms of the partial settlement and Judgment, the Commonwealth has reimbursed the College about $1.1 million (about 2.5%) from an escrow account, after the Department of Environmental Protection determined that the clean up in the shoreline of Lake Waban was properly performed. No further reimbursement is due to the College under the judgment. The clean-up of the remainder of Lake Waban, downstream areas and groundwater is not addressed under the current settlement, because the Department of Environmental Protection has not yet selected a remedy for these areas. Once a remedy is determined and costs are known, negotiations may be reopened with the College. The Commonwealth and the College have reserved their rights against each other regarding liability for the future clean up costs for this part of the site, which could involve tens of millions of dollars.

In re Massachusetts Military Reservation (pre-litigation). The Commonwealth, through the Executive Office of Energy and Environmental Affairs, the Department of Environmental Protection and the Attorney General's Office, is engaged in preliminary discussions with federal Natural Resource Trustees, including the United States Army and Air Force, the Department of Interior and the National Oceanic and Atmospheric Administration regarding natural resource damages at the Massachusetts Military Reservation on Cape Cod. The Commonwealth's Executive Office of Energy and Environmental Affairs is the State Natural Resources Trustee. Federal Trustees claim that the Commonwealth and others are liable for natural resource damages due to widespread contamination primarily from past military activities at the Reservation. This asserted liability also may extend to response actions and related activities necessary to remediate the site. The assessment process for natural resource damages is set forth in federal regulations and is expected to take many months to complete. While no recent comprehensive estimate of natural resource damages and response actions is available, it is expected that the damages and response actions may cost at least tens of millions of dollars. Currently the Commonwealth is in settlement negotiations with one of the private contractors regarding contamination at a portion of the Massachusetts Military Reservation site.

Conservation Law Foundation v. Romney (U. S. District Court). An environmental group brought a citizens' Clean Air Act case to compel the Commonwealth to improve the state's mass transit system in connection with the approaching completion of the Central Artery/Ted Williams Tunnel project. The Commonwealth settled this action in November, 2006, by agreeing to proceed on certain public transit commitments to offset an alleged increase in pollution as a result of the Big Dig. The terms of the settlement require the Commonwealth to move forward on various transit projects (including developing a connector between the Red and Blue subway lines), provide interim deadlines for existing projects and increase public participation and oversight. The court action has been stayed indefinitely, pending implementation of the settlement.

The Arborway Committee v. Executive Office of Transportation and Public Works et al. (Suffolk Superior Court). The plaintiff, a volunteer group of residents and merchants in Jamaica Plain, filed a complaint in February, 2007, seeking to compel the Commonwealth to restore electric light rail service between Heath Street and the Forest Hills station in Boston. Green Line service along this route, known as the Arborway line, was discontinued in 1985. The plaintiff claims that the Commonwealth's failure to restore the Arborway Line is a breach of a memorandum of understanding entered into between the Commonwealth and the Conservation Law Foundation in 1990.

Other

Shwachman v. Commonwealth (Worcester Superior Court). The Commonwealth, through its Division of Capital Asset Management, took by eminent domain certain property in Worcester to build a new courthouse for Worcester County. Suit was filed in May, 2004 seeking additional compensation for the land taking; the plaintiff may seek an additional $30 million. Discovery is ongoing.

Perini Corp., Kiewit Construction. Corp., Jay Cashman, Inc., d/b/a Perini - Kiewit - Cashman Joint Venture v. Commonwealth (Superior Court). In six consolidated cases and related potential litigation, plaintiffs make claims for alleged increased costs arising from differing site conditions and other causes of delay on the Central Artery/Ted Williams Tunnel project. Plaintiffs have asserted claims of approximately $150 million, which are at various stages of resolution at the Superior Court and before the Central Artery Tunnel Project Dispute Review Board panels.

American Council of Engineering Cos. v. Mass Turnpike, Mass Highway Department and the Commonwealth (Suffolk Superior Court). The plaintiff, a trade association of consulting engineers, asserts that, due to the financial difficulties of two insurers who are part of the Central Artery/Ted Williams Tunnel project's owner-controlled insurance program, the CA/T project is contractually required to replace two insurance policies totaling $25 million. The Commonwealth's motion to dismiss has been denied and the case is at the discovery stage.

Central Artery/Ted Williams Tunnel Cost Recovery Program Litigation (Suffolk Superior Court). In 2004, the Commonwealth and the Massachusetts Turnpike Authority filed ten civil actions against section design consultants of the Central Artery/Ted Williams Tunnel project, claiming that the designers' errors and omissions caused the project to expend additional costs during construction. The actions were filed as part of the project's cost recovery program to recoup extra costs directly attributable to the designers' errors and omissions in design. The Commonwealth and the Turnpike Authority also filed a complaint in 2004 against the project's management consultant, Bechtel/Parsons Brinckerhoff (B/PB), a joint venture. The main claim in this case is B/PB's failure to disclose the true cost of the project. The cost recovery efforts were transferred to the Attorney General's office effective February 1, 2005. In addition, in November, 2006, the Commonwealth, on behalf of the Massachusetts Highway Department, along with the Turnpike Authority, brought an action against B/PB and other defendants alleging breach of contract, negligence and other claims arising out of the July, 2006, ceiling collapse in the I-90 Connector Tunnel of the CA/T project.

Nathaniel Lavallee et al. v. Justices of Hampden Superior Court et al., Michael Carabello et al. v. Justices of Hampden Superior Court et al., and Rosemary Cooper v. Region V Administrative Justice et al. (Supreme Judicial Court for Suffolk County). In these companion cases, the Supreme Judicial Court decided in July, 2004 that the constitutional rights of indigent criminal defendants in Hampden County had been violated by the inability of the Committee for Public Counsel Services (CPCS) to appoint attorneys for them because statutory rates of state-paid compensation were so low that many Hampden County bar advocates had become unwilling to accept appointments. The court ruled that indigent criminal defendants must be released from custody if they have been incarcerated pending trial for more than seven days without counsel and that charges must be dismissed without prejudice after 45 days without counsel. The court declined, at that time, to order an increase in rates of bar advocate compensation. The cases were remanded to a single justice of the Supreme Judicial Court for implementation of a mechanism for the appointment of counsel by Hampden County courts. One bar advocate, Rosemary Cooper, sought additional compensation in a separate case. On October 10, 2006, the Supreme Judicial Court denied her petition for relief. The remainder of this litigation is not currently active, but could be resumed if the shortage of available attorneys recurs. See the discussion of relevant legislative developments below.

Arianna S. et al. v. Commonwealth (Supreme Judicial Court for Suffolk County). This is a class action on behalf of all indigent persons who are constitutionally entitled to state-compensated counsel in civil and criminal proceedings. The petitioners claim to have been deprived of the effective assistance of counsel because of the low rates paid to bar advocates and to represent a statewide class consisting of all indigent persons similarly situated. As in the cases described in the preceding paragraph, the relief sought includes a court-ordered increase in bar advocate compensation. The proceedings have been stayed. In August, 2005, the Legislature substantially increased the hourly rates for bar advocates and has appropriated funds therefor for both fiscal 2006 and fiscal 2007. If additional future rate increases were to be ordered by the court, no reliable estimate has been made of the increased expenditures.

Goldberg v. Commonwealth (Suffolk Superior Court). This case involves billboards at the East Boston entrance to Logan Airport. One billboard was removed as part of parkland mitigation for the CA/T project. The plaintiff claims to be subject to a regulation that prohibits billboards within 300 feet of a park. Thus, the plaintiff expects to lose the rest of his billboards and values the loss of these property rights at approximately $20 million. The case is scheduled for trial in November, 2007.

Suffolk Construction Co. and NER Construction Management, Inc. d/b/a Suffolk/NER v. Commonwealth of Massachusetts Division of Capital Asset Management (Suffolk Superior Court). The general contractor for the historic renovation project for the Suffolk County court house sued the Division of Capital Asset Management claiming that it is owed additional amounts for extra costs and delays associated with the project. Total exposure is approximately $60 million ($16 million in claims of the general contractor and $44 million in pass-through claims from subcontractors). Discovery is continuing in this matter and a special discovery master has been appointed by the court.

MISCELLANEOUS

Any provisions of the constitution of the Commonwealth, of general and special laws and of other documents set forth or referred to in this Information Statement are only summarized, and such summaries do not purport to be complete statements of any of such provisions. Only the actual text of such provisions can be relied upon for completeness and accuracy.

This Information Statement contains certain forward-looking statements that are subject to a variety of risks and uncertainties that could cause actual results to differ from the projected results, including without limitation general economic and business conditions, conditions in the financial markets, the financial condition of the Commonwealth and various state agencies and authorities, receipt of federal grants, litigation, arbitration, force majeure events and various other factors that are beyond the control of the Commonwealth and its various agencies and authorities. Because of the inability to predict all factors that may affect future decisions, actions, events or financial circumstances, what actually happens may be different from what is set forth in such forward-looking statements. Forward-looking statements are indicated by use of such words as “may,” “will,” “should,” “intends,” “expects,” “believes,” “anticipates,” “estimates” and others.

All estimates and assumptions in this Information Statement have been made on the best information available and are believed to be reliable, but no representations whatsoever are made that such estimates and assumptions are correct. So far as any statements in this Information Statement involve any matters of opinion, whether or not expressly so stated, they are intended merely as such and not as representations of fact. The various tables may not add due to rounding of figures.

Neither the Commonwealth’s independent auditors, nor any other independent accountants, have compiled, examined, or performed any procedures with respect to the prospective financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information.

The information, estimates and assumptions and expressions of opinion in this Information Statement are subject to change without notice. Neither the delivery of this Information Statement nor any sale made pursuant to any official statement of which this Information Statement is a part shall, under any circumstances, create any implication that there has been no change in the affairs of the Commonwealth or its agencies, authorities or political subdivisions since the date of this Information Statement, except as expressly stated.

CONTINUING DISCLOSURE

The Commonwealth prepares its Statutory Basis Financial Report and its Comprehensive Annual Financial Report with respect to each fiscal year ending June 30. The Statutory Basis Financial Report becomes available by October 31 of the following fiscal year and the Comprehensive Annual Financial Report becomes available in January of the following fiscal year. Copies of such reports and other financial reports of the Comptroller referenced in this document may be obtained by requesting the same in writing from the Office of the Comptroller, One Ashburton Place, Room 909, Boston, Massachusetts 02108. The financial statements are also available at the Comptroller’s web site located at http://www.mass.gov/osc by clicking on “Financial Reports/Audits.”

On behalf of the Commonwealth, the State Treasurer will provide to each NRMSIR within the meaning of Rule 15c2-12 of the SEC, no later than 270 days after the end of each fiscal year of the Commonwealth, certain financial information and operating data relating to such fiscal year, as provided in said Rule 15c2-12, together with audited financial statements of the Commonwealth for such fiscal year. To date, the Commonwealth has complied with all of its continuing disclosure undertakings relating to the general obligation debt of the Commonwealth and has not failed in the last five years to comply with its continuing disclosure undertakings with respect to its special obligation debt and federal grant anticipation notes. However, the annual filings relating to the fiscal year ended June 30, 2001 for the Commonwealth’s special obligation debt and for the Commonwealth’s federal highway grant anticipation notes were filed two days late, on March 29, 2002. Proper notice of the late filings was provided on March 29, 2002 to the Nationally Recognized Municipal Securities Information Repositories and the Municipal Securities Rulemaking Board.

The Department of the State Auditor audits all agencies, departments and authorities of the Commonwealth at least every two years. Copies of audit reports may be obtained from the State Auditor, State House, Room 229, Boston, Massachusetts 02133.

AVAILABILITY OF OTHER FINANCIAL INFORMATION

Questions regarding this Information Statement or requests for additional information concerning the Commonwealth should be directed to Patrick F. Landers, III, Assistant Treasurer, Office of the Treasurer and Receiver-General, One Ashburton Place, 12th floor, Boston, Massachusetts 02108, telephone (617) 367-3900 (ext. 226), or to Jay Gonzalez, Assistant Secretary for Capital Finance and Intergovernmental Affairs, Executive Office for Administration and Finance, State House, Room 373, Boston, Massachusetts 02133, telephone (617) 727-2040. Questions regarding legal matters relating to this Information Statement should be directed to John R. Regier, Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C., One Financial Center, Boston, Massachusetts 02111, telephone (617) 348-1720.

THE COMMONWEALTH OF MASSACHUSETTS

By /s/ Timothy P. Cahill
Timothy P. Cahill
Treasurer and Receiver-General

By /s/ Leslie A. Kirwan
Leslie A. Kirwan
Secretary of Administration and Finance

May 9, 2007

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