NEW ISSUE - BOOK-ENTRY ONLY

Ratings: Moody's: Aa2
Standard & Poor's: AA
Fitch: AA

In the opinion of Bond Counsel, assuming compliance by the Commonwealth with the Covenant and Tax Certificate (defined herein), under existing statutes and court decisions, interest on the Bonds is excluded from gross income of the owners thereof for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"). In the further opinion of Bond Counsel, interest on the Bonds is not treated as a preference item for purposes of the alternative minimum tax imposed under the Code with respect to individuals and corporations, although such interest is included in "adjusted current earnings" in computing alternative minimum taxable income for purposes of the alternative minimum tax imposed by the Code on certain corporations. In the further opinion of Bond Counsel, under the laws of the Commonwealth as presently enacted and construed, the Bonds are exempt from personal property taxes in the Commonwealth and interest on the Bonds is exempt from the Commonwealth's personal income tax and the Commonwealth's corporate net income tax. See "TAX MATTERS" herein.

$200,000,000
Commonwealth of Pennsylvania
General Obligation Bonds
First Series of 2005

Dated: Date of Issuance and Delivery **Due: July 1, as shown below**

The Bonds will be issued only in book-entry form initially registered in the name of Cede & Co., as nominee for The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository for the Bonds. Interest on the Bonds will be payable semi-annually on January 1 and July 1, commencing January 1, 2006. U.S. Bank National Association, Pittsburgh, Pennsylvania, is the Loan and Transfer Agent for the Bonds. Principal of and interest and redemption premium, if any, on the Bonds are payable to Cede & Co. See "THE BONDS – Book-Entry Only System."

The Bonds are subject to redemption as set forth herein. See "THE BONDS – Optional Redemption."

The Bonds are direct and general obligations of the Commonwealth and the full faith and credit of the Commonwealth are pledged for the payment of principal of and interest on the Bonds.

This cover page contains certain information for quick reference only. It is not a summary of the issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision regarding the Bonds.

FSA®

The scheduled payment of principal of and interest on the Bonds maturing on July 1, 2022 through 2025, inclusive (indicated by an * below, the "Insured Bonds"), when due, will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Insured Bonds by FINANCIAL SECURITY ASSURANCE INC.

MATURITY SCHEDULE

(Base CUSIP Number: 709141)

Due July 1	Principal Amount	Interest Rate	Yield	CUSIP Number	Due July 1	Principal Amount	Interest Rate	Yield	CUSIP Number
2006	$ 6,120,000	5.00%	2.80%	Y90	2016	$ 9,820,000	5.00%	3.66%	2B0
2007	6,370,000	5.00	2.75	Z24	2017	10,325,000	5.00	3.70	2C8
2008	6,650,000	5.00	2.92	Z32	2018	10,855,000	5.00	3.79	2D6
2009	6,955,000	5.00	3.00	Z40	2019	11,410,000	5.00	3.84	2E4
2010	7,285,000	5.00	3.05	Z57	2020	11,995,000	5.00	3.88	2F1
2011	7,650,000	5.00	3.18	Z65	2021	12,610,000	5.00	3.92	2G9
2012	8,040,000	5.00	3.29	Z73	2022	13,255,000*	4.15	4.13	2H7
2013	8,450,000	5.00	3.40	Z81	2023	13,935,000*	4.20	4.17	2J3
2014	8,885,000	5.00	3.49	Z99	2024	14,650,000*	4.20	4.18	2K0
2015	9,340,000	5.00	3.59	2A2	2025	15,400,000*	4.25	4.23	2L8

The interest rates shown above are the interest rates per annum payable by the Commonwealth on the Bonds of each maturity date as indicated. The yields shown above for each maturity were furnished to the Commonwealth by the group of banks and investment banking firms who purchased the Bonds from the Commonwealth on May 24, 2005, and may not reflect the current market prices of the Bonds. All information concerning the re-offering of the Bonds should be obtained from the underwriters and not from the Commonwealth.

The Bonds are offered when, as and if issued, and are subject to the receipt of the legal opinions of the Attorney General of the Commonwealth of Pennsylvania and of Obermayer Rebmann Maxwell & Hippel LLP, of Philadelphia, Pennsylvania, Bond Counsel. The Commonwealth expects that the Bonds will be available in definitive form for delivery in New York, New York, on or about June 9, 2005.

Dated: May 24, 2005

THE ISSUING OFFICIALS

Governor .... *EDWARD G. RENDELL*
State Treasurer .... *ROBERT P. CASEY, JR..*
Auditor General .... *JACK WAGNER*

OFFICE OF THE BUDGET

Secretary .... *MICHAEL J. MASCH*

Attorney General of the Commonwealth of Pennsylvania:

Tom Corbett

Bond Counsel:

Obermayer Rebmann Maxwell & Hippel LLP
Philadelphia, Pennsylvania

Special Disclosure Counsel:

Hunton & Williams LLP
Richmond, Virginia

No dealer, broker, salesperson or other person has been authorized to give any information or to make any representations, other than as contained in this Official Statement, in connection with the offering contained herein, and, if given or made, such other information or representations must not be relied upon as having been authorized by the Commonwealth of Pennsylvania. This Official Statement does not constitute an offer to sell, or a solicitation of an offer to buy, nor shall there be any sale of the Bonds by any person in any jurisdiction where such sale would be unlawful.

Except as otherwise noted, the information herein speaks as of its date and is as of the date of this Official Statement and is subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, in any circumstances, create any implication that there has been no change in the affairs of the Commonwealth of Pennsylvania since the date hereof.

The order and placement of the information in this Official Statement, including the Appendices hereto and the information incorporated herein by reference, are not to be deemed to be a determination of relevance, materiality or importance, and this Official Statement, including the Appendices, and the information incorporated herein by reference, must be considered in its entirety.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained in Appendix I specimen "Municipal Bond Insurance Policy" herein, none of the information in this Official Statement has been supplied or verified by Financial Security, and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the Bonds; or (iii) the tax exempt status of the interest on the Bonds.

TABLE OF CONTENTS

SUMMARY INFORMATION

THIS SUMMARY STATEMENT IS SUBJECT IN ALL RESPECTS TO THE MORE COMPLETE INFORMATION CONTAINED IN THIS OFFICIAL STATEMENT. OFFERING OF THE BONDS TO THE POTENTIAL PURCHASERS IS MADE ONLY BY MEANS OF THIS ENTIRE OFFICIAL STATEMENT, INCLUDING THE COVER AND APPENDICES HERETO AND THE INFORMATION INCORPORATED BY REFERENCE.

Issuer .... Commonwealth of Pennsylvania

Offering .... $200,000,000 Commonwealth of Pennsylvania, General Obligation Bonds, First Series of 2005 (the "Bonds")

Dated Date .... Date of Issuance and Delivery

Security .... General obligations of the Commonwealth of Pennsylvania; full faith and credit pledged

Use of Proceeds .... The Commonwealth of Pennsylvania is issuing the Bonds for the following purpose:

Purpose	Principal Amount
Capital Facilities Projects	$200,000,000

Redemption .... The Bonds maturing on or after July 1, 2016 are subject to optional redemption in whole or in part (and if in part, in part within one or more maturities) at any time on and after July 1, 2015 at a redemption price equal to the principal amount thereof, plus accrued interest to the date fixed for redemption

Authorized Denominations .... $5,000 or integral multiples thereof.

Form of Bonds .... Bonds are issued in fully registered form through a book-entry only system.

Loan & Transfer Agent .... U.S. Bank National Association, Pittsburgh, Pennsylvania.

Legal Opinions .... Obermayer Rebmann Maxwell & Hippel LLP, Bond Counsel.
Tom Corbett, Attorney General of the Commonwealth of Pennsylvania.

Bond Ratings
Moody's Investors Service Aa2
Standard & Poor's Rating Services, a division of the McGraw-Hill Companies....................AA
Fitch Ratings..AA

Official Statement
$200,000,000
Commonwealth of Pennsylvania
General Obligation Bonds
First Series of 2005

INTRODUCTION

This Official Statement of the Commonwealth of Pennsylvania (the "Commonwealth"), including the cover page and appendices, presents certain information in connection with the issuance of $200,000,000 aggregate principal amount of the Commonwealth's General Obligation Bonds, First Series of 2005 (the "Bonds"). The Bonds are being issued to finance various capital budget projects. See "USE OF PROCEEDS."

The Bonds are general obligations of the Commonwealth to which the full faith and credit of the Commonwealth are pledged. See "SECURITY AND SOURCE OF PAYMENT FOR BONDS." Principal of and interest payments on the Bonds will be paid from the General Fund. See "COMMONWEALTH FINANCIAL PERFORMANCE" and "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES."

When issued, the Bonds will be registered in the name of Cede & Co., as nominee for The Depository Trust Company, securities depository for the Bonds under a book-entry only registration system. See "THE BONDS — Book-Entry Only System" and Appendix D.

The Bonds are authorized investments for fiduciaries and personal representatives, as defined in the Probate, Estates and Fiduciaries Code within the Commonwealth; are legal investments for Pennsylvania banks, trust companies, bank and trust companies, savings banks, and insurance companies; and are acceptable as security for deposits of the funds of the Commonwealth. See "LEGALITY FOR INVESTMENT."

Except where otherwise expressly noted, the financial and other information provided in this Official Statement is generally derived from the records of the Commonwealth. All financial information should be considered as unaudited unless otherwise specifically identified. All estimates and assumptions are based on the best information available but do not constitute factual information. All estimates of future performance or events constituting "forward looking statements" may or may not be realized because of a wide variety of economic and other circumstances. Included in such forward-looking statements are numbers and other information from budgets for current and future fiscal years. The references to, and summaries of, Constitutional and statutory provisions of the Commonwealth and to bond resolutions and other documents are qualified in their entirety by reference to the complete provisions of such documents and to any judicial interpretations thereof.

THE BONDS

Description of the Bonds

The Bonds will be dated the date of issuance and delivery, will bear interest initially from such date, at the rate per annum for each maturity as specified on the cover page hereof, will be payable semi-annually on each January 1 and July 1, commencing January 1, 2006, calculated on the basis of a 360-day year of twelve 30-day months, and will mature in the amounts and on the dates as set forth on the cover page hereof.

The Resolutions (as hereinafter defined) and all provisions thereof are incorporated by reference in the text of the Bonds, including, without limitation, those provisions setting forth the conditions under which the Resolutions may be modified. The Bonds provide that each registered owner, Beneficial Owner, DTC Participant or Indirect Participant (as hereinafter defined) in DTC, by acceptance of a Bond (including receipt of a book-entry credit evidencing an interest therein), assents to all of such provisions as an explicit and material portion of the consideration running to the Commonwealth to induce it to adopt the Resolutions and to issue such Bond. Copies of the Resolutions, including the full text of the form of the Bonds, are on file at the designated office of U.S. Bank National Association, as Loan and Transfer Agent ("Loan and Transfer Agent").

Interest on the Bonds will be payable by check or draft mailed or other transfer made to the persons in whose names the Bonds shall be registered at the close of business on the fifteenth day (whether or not a business day) of the calendar month next preceding such interest payment date (the "Record Date"). Any interest on any Bond not timely paid or duly provided for shall cease to be payable to the person who is the registered owner as of the regular Record Date, and shall be payable to the person who is the registered owner at the close of business on a special record date for the payment of such defaulted interest. A special record date shall be a date not more than fifteen nor less than ten days prior to the date of the proposed payment and shall be fixed whenever moneys become available for payment of the defaulted interest. Notice of a special record date shall be given to registered owners of the Bonds not less than fifteen days prior thereto.

Whenever the due date for payment of interest on or principal of the Bonds or the date fixed for redemption of any Bond shall be a Saturday, a Sunday, a legal holiday or a day on which banks in the Commonwealth are required or authorized by law (including by executive order) to close, then payment of such interest, principal or redemption price need not be made on such date, but may be made on the next succeeding day which is not a Saturday, a Sunday, a legal holiday or a day upon which banks in the Commonwealth are required or authorized by law (including by executive order) to close, with the same force and effect as if made on the due date for payment of principal, interest or redemption price, and no interest shall accrue thereon for any period after such due date.

Book-Entry Only System

The Depository Trust Company, New York, New York ("DTC") will act as securities depository for the Bonds pursuant to a book-entry only system. Information regarding DTC and its book-entry system, provided by DTC, appears as Appendix D. Such information has been provided by DTC, and the Commonwealth does not assume any responsibility for the accuracy or completeness of such information. The Commonwealth may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

For so long as the Bonds are registered in the name of DTC, or its nominee Cede & Co., the Commonwealth and the Loan and Transfer Agent will treat Cede & Co. as the registered owner of the Bonds for all purposes, including payments, notices and voting.

Neither the Commonwealth nor the Loan and Transfer Agent shall have any responsibility or obligation to any Direct or Indirect Participant or Beneficial Owner (as defined in Appendix D) with respect to (i) the accuracy of any records maintained by DTC or any Direct or Indirect Participant with respect to any beneficial ownership interest in any Bonds; (ii) the payment by any Direct or Indirect Participant of any amount due to any Beneficial Owner in respect of the principal of, premium, if any, and interest on the Bonds; (iii) the delivery or timeliness of delivery by any Direct or Indirect Participant of any notice to any Beneficial Owner with respect to the Bonds, including, without limitation, any notice of redemption; or (iv) other action taken by DTC or Cede & Co., including the effectiveness of any action taken pursuant to an Omnibus Proxy.

Payments made by or on behalf of the Commonwealth to DTC or its nominee shall satisfy the Commonwealth's payment obligations with respect to the Bonds to the extent of such payments.

Optional Redemption

The Bonds maturing in the years 2006 to 2015, inclusive, are not subject to redemption. The Bonds, or portions thereof in integral multiples of $5,000, maturing on and after July 1, 2016, are subject to redemption at the option of the Commonwealth prior to scheduled maturity on or after July 1, 2015, as a whole or in part at any time and from time to time, in any order of maturity determined by the Commonwealth and by lot within a maturity in such manner as the Commonwealth in its discretion may determine, on at least 30 days' (but not more than 60 days') notice, at a redemption price equal to par (100% of stated principal amount) plus accrued interest to the date fixed for redemption.

As long as the Bonds are registered pursuant to a book-entry only system, notice of redemption will be given, as required by DTC's (or any successor depository's) procedures, to DTC, its nominee, or successor securities depository as registered owner of the Bonds. So long as Cede & Co. is the registered owner of the Bonds, the Commonwealth will not be responsible for mailing notices of redemption to anyone other than DTC or its nominee.

Notice of redemption shall be given by the Loan and Transfer Agent via first-class mail not less than 30 days, nor more than 60 days, prior to the date fixed for redemption to the persons in whose names the Bonds to be redeemed are registered at the close of business on the fifth (5^{th}) business day prior to such mailings; provided, however, that any defect in the notice or in the mailing thereof with respect to any registered owner shall not affect the validity of the proceedings for such redemption as to any other registered owner. Deposit of any such notice in the United States mail shall constitute constructive receipt of such notice by the registered owner to whom such notice is sent. Notice having been given as aforesaid and provision having been made for redemption from funds on deposit with the Loan and Transfer Agent, no interest on Bonds, or portions thereof, called for redemption shall accrue after the date fixed for redemption, and the registered holders of the Bonds, or portions thereof, called for redemption shall thereafter have no further right except to receive payment of the redemption price plus accrued interest to the redemption date.

In addition to the notice of redemption to the registered owners of the Bonds, the Loan and Transfer Agent shall cause copies of the original redemption notice to be sent by facsimile transmission, overnight delivery or certified mail with return receipt requested (or other similar means that can provide evidence of receipt) to all registered securities depositories then in the business of holding obligations similar to the Bonds, and to two or more national information services that disseminate redemption information; provided however, that failure to send such copies of the original redemption notice or any defect therein shall not affect the validity of the redemption proceedings.

SECURITY AND SOURCE OF PAYMENT FOR BONDS

The Bonds are direct and general obligations of the Commonwealth to which the full faith and credit of the Commonwealth have been pledged for the payment of the interest thereon as it becomes due and the payment of the principal thereof at maturity or prior redemption. The various acts authorizing the incurrence of debt by the Commonwealth require the General Assembly to appropriate annually the moneys necessary to pay such interest and principal for which other provisions are not made. See the statutes described in the subsection "Authorization" below. Principal of and interest payments on the Bonds will be made from the General Fund.

The Constitution of the Commonwealth of Pennsylvania (the "Constitution") places a claim on revenues of the Commonwealth as security for the payment of principal of and interest on all debt of the Commonwealth. Article VIII, Section 7(d) of the Constitution provides that if sufficient funds are not appropriated for the timely payment of the interest on and principal of all Commonwealth debt, the State Treasurer shall set apart from the first revenues thereafter received applicable to the appropriate fund, a sum sufficient to pay such interest and principal, and shall so apply the money so set apart.

The State Treasurer may be required to set aside and apply such revenues at the suit of any holder of Commonwealth obligations.

For a description of the constitutional provisions relating to the Bonds, see Appendix E. The proposed form of the opinion of the Attorney General is in Appendix F and the proposed form of the opinion of Bond Counsel is in Appendix G.

Authorization

The Bonds are authorized and issued pursuant to and in full compliance with the provisions, restrictions and limitations of Section 7 of Article VIII of the Constitution; the laws of the Commonwealth, including the Capital Facilities Debt Enabling Act, Act No. 1999-1, approved February 9, 1999, as amended, annual capital budget bills and various bond authorization bills enacted by the General Assembly. The Bonds are also authorized and issued pursuant to resolutions adopted by the Governor, the State Treasurer, and the Auditor General (the "Issuing Officials") on May 13, 2005, and May 24, 2005 (collectively, the "Resolutions").

Debt Limits

The Constitution (Article VIII, Section 7(a)) permits debt to be incurred (i) for purposes itemized in law and approved by voter referendum, (ii) without approval of the electorate for the rehabilitation of areas affected by man-made or natural disasters, and (iii) for capital facilities projects specifically itemized in a capital budget if such debt does not cause the amount of all net debt outstanding (as defined for purposes of that Section) to exceed one and three quarters times (1.75x) the average of the annual tax revenues of the Commonwealth deposited in all funds in the previous five fiscal years, as certified by the Auditor General (the "Constitutional Debt Limit"). The most recent semi-annual computation of the Constitutional Debt Limit and the amount of net debt outstanding subject to such limit is shown in Table 1:

Table 1
Constitutional Debt Limit[a]
February 28, 2005
(In Millions)

Average Annual Tax Revenues Fiscal 2000-2004	$ 25,091.0
Times 1.75	43,909.3
Less: Net Debt Outstanding[b]	6,255.0
Debt Issuable Within Limit	$ 37,654.3

[a] As certified by the Auditor General on March 1, 2005 (Appendix A).
[b] After credit for refunded debt.

The capital debt authorizations for the various categories of capital facilities projects is shown in Table 2.

Table 2
Aggregate Capital Debt Authorization
(In Millions)

Capital Facilities Projects Category	Debt Authorized	Issued[a]	Authorized But Unissued	Pro Forma Remaining After Issuance Of the Bonds
Buildings and Structures	$ 18,240.8	$ 6,476.5	$ 11,764.3	$ 11,664.3
Furniture and Equipment	737.8	381.5	356.2	356.2
Transportation Assistance	7,279.6	2,197.8	5,028.2	4,978.2
Redevelopment Assistance	15,829.5	1,484.0	14,245.5	14,195.5
Community Colleges	35.8	28.0	7.8	7.8
Highway and Highway Bridge	15,791.0	2,630.5	14,302.2	14,302.2
Advance Construction Interstate	450.0	450.0	0	0
Flood Control	322.1	42.8	278.3	278.3
Site Development	150.0	150.0	0	0
Total	$ 58,836.60	$ 13,841.1	$ 45,982.5	$ 45,782.5

[a] Not all are outstanding.

The amount of debt that may be issued during the fiscal year for capital projects authorized in current or previous capital budgets is enacted annually by the General Assembly and approved by the Governor. The fiscal year 2005 capital budget provided that such budget will be in effect until the fiscal year 2006 capital budget is enacted. The maximum amount of debt currently authorized by the fiscal year 2005 capital budget is as shown in Table 3 on the following page.

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Table 3

Fiscal Year 2005 Capital Budget Debt Limits[a]

(In Millions)

Capital Facilities Projects Category	Limits	Issued to Date	Remaining Issuable Within Limit	Pro Forma Remaining After Issuance Of the Bonds
Buildings and Structures	$ 335.0	$ 0.0	$ 335.0	$ 235.0.0
Transportation Assistance	150.0	100.0	50.0	0.0
Redevelopment Assistance	270.0	100.0	170.0	120.0
Flood Control	1.0	1.0	0.0	0.0
Total	$ 756.0	$ 201.0	$ 555.0	$ 355.0

[a] The fiscal year 2005 capital budget debt limits became effective November 30, 2004, and will remain in force until the fiscal 2006 capital budget debt limit becomes effective.

For a discussion of the Commonwealth's outstanding debt and projected future issuance of general obligation debt, see "OUTSTANDING INDEBTEDNESS OF THE COMMONWEALTH."

USE OF PROCEEDS

The Commonwealth is issuing the Bonds to provide for the construction, acquisition and major rehabilitation of capital facilities projects as described below under "Capital Facilities."

The proceeds received from the sale of the Bonds (including bond premium), after paying the costs of issuance, will be applied by the Commonwealth to pay the costs of the purposes described below. Any accrued interest payable upon original delivery of the Bonds will be credited ratably to the funds from which debt service on the Bonds is paid and will be used for debt service on the Bonds.

Capital Facilities

The proceeds of the Bonds will be deposited into the Capital Facilities Fund and applied to defray the costs of issuance of the Bonds and the financial costs of various capital facilities projects of the Commonwealth. Of the $200,000,000 aggregate principal amount of the Bonds issued for capital facilities projects, (i) $100,000,000 aggregate principal amount of the Bonds is to be allocated to the Department of General Services and used to pay for the construction and major rehabilitation of public buildings for the Commonwealth and its institutions; (ii) $50,000,000 aggregate principal amount of the Bonds is to be allocated to the Department of Transportation to fund transportation assistance projects; and (iii) $50,000,000 aggregate principal amount of the Bonds is to be allocated to the Department of Community and Economic Development to fund redevelopment assistance projects. Pending application to the above purposes, the proceeds of the Bonds allocated to these purposes will be held by the State Treasurer in the Capital Facilities Fund and invested in accordance with applicable state and federal laws.

Earnings from the investment of moneys deposited in the Capital Facilities Fund will be retained in that fund and used for the purposes of the fund.

COMMONWEALTH GOVERNMENT

The Commonwealth is organized into three separate branches of government — executive, legislative and judicial — as defined in the Constitution. Five officials of the Commonwealth's executive branch are elected in statewide elections for four-year terms expiring on the dates shown below.

Name	Office	Term Expires
Edward G. Rendell	Governor	January 16, 2007
Catherine Baker Knoll	Lieutenant Governor	January 16, 2007
Tom Corbett	Attorney General	January 20, 2009
Robert P. Casey, Jr.	State Treasurer	January 20, 2009
Jack Wagner	Auditor General	January 20, 2009

A more detailed description of the Commonwealth's government and fiscal administration is included in Appendix C.

Commonwealth Employees

Employees are permitted to organize and bargain collectively. As of July 2003, 82.9 percent of the full-time salaried employees under the Governor's jurisdiction were covered by collective bargaining agreements or memoranda of understanding. Approximately 46.4 percent of state employees are represented by the American Federation of State, County and Municipal Employees ("AFSCME").

Approximately 64 percent of state employees, represented by the AFSCME, Pennsylvania Social Services Union and other unions, are covered by contracts effective July 1, 2003 and expiring on June 30, 2007. These contracts provide 6.5 percent salary increases over the four-year life of the contracts. Contracts extending through June 30, 2007 also have been negotiated in the past year with two other unions whose contracts expired in June 2004. One union received a 6.5 percent salary increase over the three-year period ending June 30, 2007; the second received and interest arbitration award providing for a 14 percent salary increase over the four-year period ending June 30, 2008. Employees represented by three other unions whose contracts expired in June 2004 continue to work while negotiations with the unions continue. Table 4 presents the number of approved and filled positions under the Governor's jurisdiction for the period 1999 through 2003.

Table 4
Filled Salaried Positions and Employees
Under the Governor's Jurisdiction[a]
1999-2003

As of July 1	Total Full and Part Time Filled Salaried Positions	Total Full Time Salaried Employees	Civil Service Salaried Positions	Civil Service As a % of Total Filled Salaried Positions
1999	78,690	78,131	55,331	70.3
2000	79,207	78,712	55,453	70.0
2001	80,240	79,695	56,448	70.3
2002	80,146	79,665	56,296	70.2
2003	78,691	78,691	54,817	69.7

[a] Excludes employees of the legislative and judicial branches, the Department of the Auditor General, the Treasury Department, the State System of Higher Education and independent agencies, boards and commissions.
Source: Office of Administration, *Governor's Annual Work Force Reports*.

COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES

The Constitution and the laws of the Commonwealth require all payments from the State Treasury, with the exception of refunds of taxes, licenses, fees and other charges, to be made only by duly enacted appropriations. Amounts appropriated from a fund may not exceed its actual and estimated revenues for the fiscal year plus any unappropriated surplus available. Appropriations from the principal operating funds of the Commonwealth (the General Fund, the Motor License Fund and the State Lottery Fund) are generally made for one fiscal year and are returned to the unappropriated surplus of the fund (a lapse) if not spent or encumbered by the end of the fiscal year. The Commonwealth's fiscal year begins July 1 and ends June 30. (Fiscal year 2005 refers to the fiscal year ending June 30, 2005.) See Appendix C for a further description of the fiscal administration of the Commonwealth.

Description of Funds

The Commonwealth utilizes the fund method of accounting. For purposes of governmental accounting, a "fund" is defined as an independent fiscal and accounting entity with a self-balancing set of accounts. Each fund records the cash and/or other resources together with all related liabilities and equities that are segregated for the purpose of the fund. In the Commonwealth, funds are established by legislative enactment or in certain limited cases by administrative action. Over 150 funds have been established and currently exist for the purpose of recording the receipt and disbursement of moneys received by the Commonwealth. Annual budgets are adopted each fiscal year for the principal operating funds of the Commonwealth and several other special revenue funds. Expenditures and encumbrances against these funds may be made only pursuant to appropriation measures enacted by the General Assembly and approved by the Governor.

The General Fund, the Commonwealth's largest operating fund, receives all tax revenues, non-tax revenues and federal grants and entitlements that are not specified by law to be deposited elsewhere. The majority of the Commonwealth's operating and administrative expenses are payable from the General Fund. Debt service on all bond indebtedness of the Commonwealth, except that issued for highway purposes or for the benefit of other special revenue funds, is payable from the General Fund.

The Motor License Fund receives all tax and fee revenues relating to motor fuels and vehicles except the revenues from one-half cent per gallon of the liquid fuels tax that are deposited in the Liquid Fuels Tax Fund for distribution to local municipalities. All revenues relating to motor fuels and vehicles are required by the Constitution to be used only for highway purposes. Most federal aid revenues designated for transportation programs and tax revenues relating to aviation fuels are also deposited in the Motor License Fund. Operating and administrative costs for the Department of Transportation and other Commonwealth departments conducting transportation related programs, including the highway patrol activities of the Pennsylvania State Police, are also paid from the Motor License Fund. Debt service on bonds issued by the Commonwealth for highway purposes is payable from the Motor License Fund.

Other special revenue funds have been established by law to receive specified revenues that are appropriated to departments, boards and/or commissions for payment of their operating and administrative costs. Such funds include the Game, Fish, Boat, Banking Department, Milk Marketing, State Farm Products Show, Environmental Stewardship, State Racing, and Tobacco Settlement Funds. Some of these special revenue funds are required to transfer excess revenues to the General Fund, and some receive funding, in addition to their specified revenues, through appropriations from the General Fund.

The Tobacco Settlement Fund is a special revenue fund established to receive tobacco litigation settlement payments paid to the Commonwealth. The Commonwealth is one of forty-six states that settled certain smoking-related litigation in a November 1998 master settlement agreement with participating tobacco product manufacturers (the "Tobacco MSA"). Under the Tobacco MSA the Commonwealth is entitled to receive a portion of payments made pursuant to the Tobacco MSA by tobacco product manufacturers participating in the Tobacco MSA. Most revenues to the Tobacco Settlement Fund are subject to annual appropriation by the General Assembly and approval by the Governor.

The Tax Stabilization Reserve Fund and the Budget Stabilization Reserve Fund that replaced the Tax Stabilization Reserve Fund following its abolishment in 2002 are special revenue funds designated to receive a statutorily determined portion of the budgetary basis fiscal year-end surplus of the General Fund. The Budget Stabilization Reserve Fund was established in July 2002 after the Tax Stabilization Reserve Fund was abolished and its balance transferred to the General Fund for the 2002 fiscal year budget. The Budget Stabilization Reserve Fund is to be used for emergencies threatening the health, safety or welfare of citizens or during downturns in the economy that result in significant unanticipated revenue shortfalls not able to be addressed through the normal budget process. Assets of the fund may be used upon recommendation by the Governor and an approving vote by two-thirds of the members of each house of the General Assembly. For GAAP reporting purposes, the Budget Stabilization Reserve Fund (previously the Tax Stabilization Reserve Fund) has been reported as a fund balance reservation in the General Fund (governmental fund category) since fiscal year 1999. Prior to that fiscal year, the Tax Stabilization Reserve Fund was reported, on a GAAP basis, as a designation of the General Fund unreserved fund balance. See "Budget Stabilization Reserve Fund and Tax Stabilization Reserve Fund" below.

The Commonwealth maintains trust and agency funds that are used to administer funds received pursuant to a specific bequest or as an agent for other governmental units or individuals.

Enterprise funds are maintained for departments or programs operated like private enterprises. Two of the largest of such funds are the State Stores Fund and the State Lottery Fund. The State Stores Fund is used for the receipts and disbursements of the Commonwealth's liquor store system. Sale and distribution of all liquor within Pennsylvania is a government enterprise. The State Lottery Fund is also an Enterprise fund for the receipt of lottery ticket sales and lottery licenses and fees. Its revenues, after payment of prizes, are dedicated to paying the costs of programs benefiting the elderly and handicapped in Pennsylvania.

In addition, the Commonwealth maintains funds classified as working capital, bond, and sinking funds for specified purposes.

Accounting Practices

Financial information for the principal operating funds of the Commonwealth is maintained on a budgetary basis of accounting. The Commonwealth also prepares annual financial statements in accordance with generally accepted accounting principles ("GAAP"). Annual financial statements prepared in accordance with GAAP are audited jointly by the Auditor General of the Commonwealth and an independent public accounting firm.

Budgetary Basis

A budgetary basis of accounting is used for insuring compliance with the enacted operating budget and is governed by applicable statutes of the Commonwealth and by administrative procedures. The Constitution provides that operating budget appropriations shall not exceed the actual and estimated revenues and unappropriated surplus available in the fiscal year for which funds are appropriated. Annual budgets are enacted for the General Fund and certain special revenue funds that together represent the majority of expenditures of the Commonwealth. The annual budget classifies fund revenues as Commonwealth revenues, augmentations, federal revenues, or restricted receipts and revenues. Commonwealth revenues are revenues from taxes and from non-tax sources such as licenses and fee charges, penalties, interest, investment income and other miscellaneous sources. Augmentations consist of departmental and institutional billings that supplement an appropriation of Commonwealth revenues, thereby increasing authorized spending. For example, patient billings for services at Commonwealth-owned institutions are augmentations that supplement Commonwealth revenues appropriated to each institution for operating costs. Federal revenues are those federal aid receipts that pay for or reimburse the Commonwealth for funds disbursed for federally assisted programs. Restricted receipts and revenues are funds that are restricted to a specific use or uses by state law, administrative decision, or the provider of the funds. Only Commonwealth revenues and expenditures from these revenues are included in the computation made to determine whether an enacted budget is constitutionally balanced. Augmenting revenues and federal revenues are considered to be self-balancing with expenditures from their respective revenue sources.

The Commonwealth's budgetary basis financial reports for its governmental funds are based on a modified cash basis of accounting as opposed to a modified accrual basis prescribed by GAAP. Under the Commonwealth's budgetary basis of accounting, tax receipts, non-tax revenues, augmentations and all other receipts are recorded at the time cash is received. An adjustment is made at fiscal year-end to include accrued revenue unrealized; that is, revenues earned but not collected. Revenues accrued include estimated receipts from (i) sales and use, personal income, realty transfer, inheritance, cigarette, liquor, liquid fuel, fuels, and oil company franchise taxes, and interest earnings, and (ii) federal government commitments to the Commonwealth. Expenditures are recorded at the time payment requisitions and invoices are submitted to the Treasury Department for payment. Appropriated amounts are reserved for payment of contracts for the delivery of goods or services to the Commonwealth through an encumbrance process. Unencumbered appropriated funds are automatically lapsed at fiscal year-end and are available for re-appropriation. Estimated encumbrances are established at fiscal year-end to pay certain direct expenditures for salaries, wages, travel, and utility costs payable against current year appropriations but disbursed in the subsequent fiscal year. Recording of the applicable expenditure liquidates the encumbered amount. Over-estimates of fiscal year-end encumbrances are lapsed in the subsequent fiscal year and under-estimates are charged to a subsequent fiscal year appropriation. Appropriation encumbrances are shown on the Commonwealth's balance sheet as a reservation of fund balance.

Other reservations of fund balance include (i) the unexpended balance of continuing appropriations (that is, appropriations that do not lapse at fiscal year-end), and (ii) requested appropriation supplements and deficiency appropriations. Revenues dedicated for specific purposes and remaining unexpended at the fiscal year-end are likewise reserved.

GAAP Financial Reporting

At fiscal year-end, budgetary basis fund financial information, both revenues and expenditures, is adjusted to reflect appropriate accruals for financial reporting in conformity with GAAP. The Commonwealth is not required to prepare GAAP financial statements and does not prepare them on an interim basis. GAAP fund financial reporting requires a modified accrual basis of accounting for governmental funds, while proprietary and fiduciary funds are reported on the accrual basis of accounting.

Fund financial statements of the Commonwealth prepared under GAAP differ from those traditionally prepared on a budgetary basis for several reasons. Among other differences, the GAAP fund financial statements (i) generally recognize revenues when they become measurable and available rather than when cash is received, (ii) report expenditures when goods and services are received and a liability incurred rather than when cash is disbursed, (iii) include a combined balance sheet for the Commonwealth presented by GAAP fund type rather than by Commonwealth fund, and (iv) include activities of all funds in the reporting entity, including agencies and authorities usually considered as independent of the Commonwealth for budgetary purposes. Adjustments to budgetary basis revenues and expenditures required to conform to GAAP accounting generally require including (i) corporation, sales, and personal income tax accruals, (ii) tax refunds payable and tax credits, and (iii) expenditures incurred but not yet posted as expenditures or not covered by appropriations.

An independent public accounting firm and the Auditor General jointly audit the Commonwealth's annual GAAP basis financial statements. The audited Basic Financial Statements are a component of the Commonwealth's Comprehensive Annual Financial Report ("CAFR"). The CAFRs for recent fiscal years, including the fiscal year ended June 30, 2004, have been filed with each Nationally Recognized Municipal Information Repository (a "NRMSIR") currently recognized by the Securities and Exchange Commission and are available from any NRMSIR and at the Budget & Financial Reports section of the Office of the Budget's web site - www.budget.state.pa.us - and such CAFRs are incorporated herein by reference. In February 2004, the Commonwealth restated its GAAP basis financial statements for the fiscal year ended June 30, 2002, for reasons discussed in "COMMONWEALTH FINANCIAL PERFORMANCE – Restatement of Financial Statements." The Commonwealth has filed both the restated financials and restated CAFR with each NRMSIR and has posted them at the Office of the Budget's web site. **Beginning with the CAFR for the fiscal year ended June 30, 2002 and continuing in subsequent CAFR's, the Commonwealth has incorporated several new accounting and reporting standards that affect the comparability of financial information for those fiscal years to GAAP basis financial information reported for fiscal years prior to the adoption of the new standards. See "New Governmental Accounting and Reporting Standards" below.**

New Governmental Accounting and Reporting Standards

Beginning with its GAAP basis financial statements for the fiscal year ended June 30, 2002, the Commonwealth adopted several new accounting and reporting standards established by the Governmental Accounting Standards Board in its Statements 33, 34, 35, 36, 37 and 38 (collectively, the "New Standards"). Among other things, these New Standards require presentation of government-wide and fund financial statements that constitute basic financial statements and replace general-purpose financial statements reported under former standards. Government-wide financial statements are intended to portray the government "as a whole" while fund financial statements provide fund-specific information. Government-wide financial statements are intended to describe the total cost of providing governmental services and disclose whether the Commonwealth's financial condition improved or weakened during the fiscal year. Other features of the new government-wide financial statements are the reporting of infrastructure assets and related depreciation. Previously, the Commonwealth did not report infrastructure values or accumulated depreciation related to general fixed assets. As part of implementing the New Standards, effective July 1, 2001, the Commonwealth reclassified and/or restated numerous fund balance amounts previously reported at June 30, 2001 and reported governmental activities net assets at June 30, 2001. Note B to the financial statements in the June 30, 2002 CAFR provides a detailed explanation of the nature and amount of such restatements. The New Standards also require providing supplementary information, including a Management's Discussion and Analysis of the financial statements.

Beginning with fiscal year 2002 the Commonwealth also changed how functional expenditure categories are defined. All of these changes may hamper the comparability of GAAP basis financial information for fiscal years ended June 30, 2002 and later to financial reports for years prior to the implementation of the New Standards.

Investment of Funds

The Treasury Department is responsible for the deposit and investment of most funds belonging to the Commonwealth, including the proceeds of the Bonds and the funds held for the periodic payment of interest on and maturing principal of the Bonds. The Commonwealth's Fiscal Code contains statutory limitations on the investment of funds by the Treasury Department. The Board of Finance and Revenue, a six-person board of state officials chaired by the State Treasurer, is authorized to establish the aggregate amount of funds that may be invested in some of the various categories of permitted investments. The State Treasurer ultimately determines the asset allocation and selects the investments within the parameters of the law.

The Commonwealth's Fiscal Code permits investments in the following types of securities: (i) United States Treasury securities and United States Agency securities maturing within two years of issue; (ii) commercial paper issued by industrial, common carrier or finance companies rated "Prime One" or its equivalent; (iii) certificates of deposit of Pennsylvania-based commercial banks, savings banks or savings and loans; (iv) repurchase obligations secured with obligations described under (i); (v) banker's acceptances written by domestic commercial banks with a rating of "Aa" or better, or its equivalent; and (vi) other non-equity investments subject to a "prudent investor" test not to exceed ten percent of assets. The Treasury Department maintains additional investment restrictions contained in its Investment Policy Guidelines. A summary of the Investment Policy Guidelines and a report on investment activity and performance of funds invested by the Treasury Department are contained in a report periodically prepared and publicly distributed by the Treasury Department.

Additionally, in June 1999, legislation authorized the State Treasurer to invest Commonwealth moneys in equity securities under a prudent person standard. The common investment pool operated by the State Treasurer for the investment of operating funds of the Commonwealth maintains a portion of its investments in equity securities. The legislative authorization to invest in equity securities has been extended until December 2006.

Budget Stabilization Reserve Fund and Tax Stabilization Reserve Fund

Legislation enacted with the adoption of the fiscal year 2003 budget abolished the Tax Stabilization Reserve Fund and transferred its balance of $1.038 billion to the General Fund. That legislation also established a new reserve fund named the Budget Stabilization Reserve Fund and initially directed $300 million of funding from the General Fund for deposit to the fund during fiscal year 2003. Subsequently, the General Assembly repealed the $300 million transfer allowing that amount to remain in the General Fund to help offset anticipated revenue shortfalls to the fiscal year 2003 budget.

Balances in the Budget Stabilization Reserve Fund, the successor to the Tax Stabilization Reserve Fund, may be used to alleviate emergencies threatening the health, safety or welfare of the Commonwealth's citizens or to offset unanticipated revenue shortfalls due to economic downturns. Income to the fund is provided by the transfer of a legislatively determined portion of the General Fund budgetary basis unappropriated surplus at the close of a fiscal year, by investment income to the fund, and by specific appropriation from other available funds by the General Assembly. The Budget Stabilization Reserve Fund is intended to accumulate a balance equal to 6 percent of General Fund revenues. Beginning with fiscal year 2003, 25 percent of any fiscal year-end surplus is to be deposited into the Budget Stabilization Reserve Fund. When the Budget Stabilization Reserve Fund balance reaches or exceeds a level equal to 6 percent of General Fund revenues, the proportion of the General Fund's fiscal year-end balance to be transferred to the Budget Stabilization Reserve Fund is to be lowered from 25 percent to 10 percent. The General Assembly may appropriate additional amounts to this fund at any time. During fiscal year 2003, the General Assembly repealed a fiscal year 2003 $300 million transfer from the General Fund to the Budget Stabilization Reserve Fund to retain that amount in the General Fund. This action, in addition to other budget actions taken during fiscal year 2003 (See "Fiscal Year 2003 Financial Results"), contributed to the achievement of a General Fund unappropriated surplus balance of $279.1 million on June 30, 2003. As required by law, 25 percent of that amount, or $69.8 million was transferred to the Budget Stabilization Reserve Fund. Following completion of the fiscal year 2004 budget, a General Fund unappropriated surplus balance of $266.9 million was achieved with 25 percent or $66.7 million transferred to the Budget Stabilization Reserve Fund. In addition, the Commonwealth made an additional transfer to the Budget Stabilization Reserve Fund of $123.3 million, which resulted in a total fiscal year 2004 contribution of $190 million. At present, the Commonwealth maintains a balance of approximately $263.4 million in the Budget Stabilization Reserve Fund. Additionally, at present the Commonwealth maintains balances in various funds and accounts, including the Budget Stabilization Reserve Fund, totaling approximately 6 percent of the Commonwealth's annual operating costs. These additional funds may become available through either executive or legislative action to address unforeseen budgetary stresses that could occur. The proposed fiscal year 2006 budget anticipates a partial draw down of a portion of these reserves, primarily a majority of the remaining balance in the Commonwealth's intergovernmental transfer reserve account. See data contained in Table 8 for additional information.

Balances in the Budget Stabilization Reserve Fund are to be used only when emergencies involving the health, safety or welfare of the residents of the Commonwealth or downturns in the economy resulting in significant unanticipated revenue shortfalls cannot be dealt with through the normal budget process. Funds in the Budget Stabilization Reserve Fund may be appropriated only upon the recommendation of the Governor and the approval of a separate appropriation bill by a vote of two-thirds of the members of both houses of the General Assembly. Any funds appropriated from the Budget Stabilization Reserve Fund that are unspent are returned to the Budget Stabilization Reserve Fund.

COMMONWEALTH FINANCIAL PERFORMANCE

Recent Developments

The continuation of modest economic growth in the nation continues to positively impact the revenue estimates incorporated in the enacted budget for fiscal year 2005. In February 2005, the Governor's proposed budget for fiscal year 2006 included a revision to the fiscal year 2005 revenue estimate for General Fund revenues to reflect expectations that revenues may exceed the estimate by approximately $290 million. Subsequently, actual revenues through April 2005 are nearly $374 million or 1.9 percent above the estimate enacted in July 2004 as part of the fiscal year 2005 budget. The enacted fiscal year 2005 budget provides for an increase of appropriations of 4.5 percent over fiscal year 2004 appropriations. Based on projections of revenues, as incorporated in the Governor's proposed fiscal year 2006 budget released in February, the General Fund is currently projected to have a preliminary ending balance of $268.0 million. See "Fiscal Year 2005 Budget."

On February 9, 2005, the Governor submitted to the General Assembly his proposed fiscal year 2006 budget. See "Fiscal Year 2006 Proposed Budget."

The CAFR for the fiscal year ended June 30, 2004 was issued on March 31, 2005. The CAFR, beginning with the one issued for the fiscal year ended June 30, 2002, incorporates several new accounting and reporting standards that affect the comparability of financial information for that fiscal year and subsequent fiscal years to GAAP basis financial information reported for fiscal years prior to the adoption of the new standards. Also beginning with the fiscal year ended June 30, 2002, the CAFR provides a new presentation of government-wide financial statements that are intended to provide an all-encompassing view of a government's financial condition and activities. See the discussion in "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES – New Governmental Accounting and Reporting Standards" and below in "Government-Wide Financial Data (GAAP Basis)."

Introduction

The most recent audited financial statements for a fiscal year are available in the CAFR issued by the Commonwealth for the fiscal period ended June 30, 2004 ("fiscal year 2004"), which was filed with each NRMSIR during April 2005. Beginning with the CAFR for fiscal year 2002, the Commonwealth incorporates New Standards that affect the comparability of financial information for that fiscal year to GAAP basis financial information reported for fiscal years prior to the adoption of the New Standards. See "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES - New Governmental Accounting And Reporting Standards." Information contained in the fund financial statements for fiscal year 2002, 2003 and 2004 continue to report what was formerly reported for governmental funds in the General Purpose Financial Statements in CAFRs for prior fiscal years although fund reclassifications and changed definitions for categories of expenditures for fiscal year 2002 and beyond will hamper comparability to data for prior fiscal years.

Copies of CAFRs recently issued by the Commonwealth are available from (i) any NRMSIR listed in the section "CONTINUING DISCLOSURE", (ii) the Secretary of the Budget, Mr. Michael Masch, Attn: Mr. Mike Higgins, 6th Floor, Strawberry Square Bell Tower, Harrisburg, Pennsylvania 17101 (Telephone (717) 787-5312), and (iii) the Budget & Financial Reports section of the Office of the Budget's web site at www.budget.state.pa.us, which CAFRs are incorporated herein by reference. The basic financial statements for fiscal year 2004 are incorporated herein by the above reference as to their availability by other than in this Official Statement. This means that (i) the incorporated information is considered part of this Official Statement and (ii) such information should be reviewed by prospective purchasers of the Bonds as a part of their review of this entire Official Statement.

Government Wide Financial Data (GAAP Basis)

Government-wide financial statements report financial position and results of activity for the Commonwealth as a whole. Government-wide statements do not report information fund-by-fund; rather, they reveal information for all governmental activities and all business-type activities in separate columns. In government-wide statements, for both governmental and business-type activities, the economic resources measurement focus and accrual basis of accounting are used, with revenues and expenses recognized when they occur, rather than when cash is received or paid. This results in assets including an estimate of the total amount of receivables due at fiscal year-end that are expected to be collected in the future. Capital assets are reported with acquisition or construction costs being reported when the assets are placed in service less accumulated depreciation. Reported liabilities include all liabilities, regardless of when payment is due, including bond principal, employee disability claims liability, and employee compensated absence liabilities.

Table 5 on the following page presents condensed financial statement information derived from the Commonwealth's government-wide June 30, 2004 Statement of Net Assets and includes amounts for the "primary government" only.

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Table 5
Condensed Statement of Net Assets
Primary Government
Fiscal Year Ended June 30, 2004
(In Billions)

	Governmental Activities	Business-Type Activities	Total
Assets:			
Cash and investments	$ 10.5	$ 4.8	$ 15.3
Capital assets (net)	20.8	-	20.8
All other assets	5.7	1.1	6.8
Total Assets	$ 37.0	$ 5.9	$ 42.9
Liabilities:			
Accounts payable	$ 4.0	$ 0.4	$ 4.4
All other current liabilities	4.3	1.3	5.6
Total Current Liabilities	8.3	1.7	10.0
Bonds payable	6.7	-	6.7
All other long-term liabilities	2.3	2.1	4.4
Total Long-Term Liabilities	9.0	2.1	11.1
Total Liabilities	$ 17.3	$ 3.8	$ 21.1
Net assets:			
Invested in capital assets, net of related debt	16.9	-	16.9
Restricted	3.0	2.1	5.1
Unrestricted	(0.2)	-	(0.2)
Total Net Assets	$ 19.7	$ 2.1	$ 21.8

Source: Comprehensive Annual Financial Report, fiscal year ended June 30, 2004.

During fiscal year 2004, the overall financial position (net assets) of the Commonwealth, including both governmental and business-type activities, increased by $1.1 billion or 5.3 percent of total beginning (as restated at July 1, 2003) net assets of $20.7 billion. For governmental activities, the net increase in net assets was $1.5 billion or 8.2 percent of beginning net assets of $18.2 billion. Total investments, not counting the State Employees' Retirement Fund and other fiduciary funds, were over $14.2 billion and total cash balances were over $1.1 billion. These amounts represent considerable liquidity for the current and future fiscal years. The increase in net assets for governmental activities compares favorably relative to the prior year change, where revenues, transfers and special items exceeded expenses by $0.3 billion. These increases represent a year-over-year improvement in the Commonwealth's overall financial position during each of the fiscal years ended June 30, 2004 and 2003. On the other hand, the $0.4 billion decrease in total net assets for business-type activities follows a $1.0 billion decrease during the prior fiscal year. Both decreases can be attributed to unemployment compensation benefit payments that exceeded employer/employee assessments during each of the fiscal years ended June 30, 2004 and 2003. During these fiscal years, unemployment compensation activities net assets decreased by $0.4 and $0.9 billion, respectively. Statutory contribution increases occurred during each of the fiscal years ended June 30, 2004 and 2003. Such increases are intended to eliminate net asset decreases in the unemployment compensation program. During the fiscal year ended June 30, 2004, net assets for all other business-type activities did not change significantly. During the prior fiscal year, those net assets decreased by approximately $80 million for the fiscal year ended June 30, 2004. Business-type activities revenues were equal to expenses; total expenses exceeded total revenues by $0.4 billion in the prior fiscal year. Including net transfers to other funds of $0.4 billion ($0.6 billion in the prior year), business-type activities net assets decreased by over $0.4 billion ($1.0 billion in the prior year). The primary reason for this decrease was that Unemployment Compensation Fund expenses exceeded revenues by $0.4 billion ($0.9 billion in the prior year). Fiscal year 2004 Unemployment

Compensation Fund revenues decreased by over $0.3 billion and expenses decreased by $0.9 billion compared to the fiscal year ended June 30, 2003.

Financial Data for Governmental Fund Types (GAAP Basis)

Governmental fund financial statements provide fund-specific information about the General Fund, the Motor License Fund, and the Tobacco Settlement Fund (initially reported for fiscal year 2002) and for other Commonwealth funds categorized as governmental funds and reported as such in the General Purpose Financial Statements of prior fiscal years. Where government-wide financial statements cover the entirety of the Commonwealth, fund financial statements provide a more detailed view of the major individual funds established by the Commonwealth. Fund financial statements differ from government-wide statements in the use by the latter of the current financial resources measurement focus and the modified accrual basis of accounting

The governmental funds balance sheet reports total fund balances for all governmental funds. Assets of the Commonwealth's governmental funds (the General Fund, the Motor License Fund and the Tobacco Settlement Fund are major governmental funds) as of June 30, 2004 were $16,201.14 million. Liabilities for the same date totaled $9,407.26 million, leaving a fund balance of $6,793.88 million, an increase of $1,158.5 million from the restated fund balance at June 30, 2003. On a fund specific basis, the fund balance for the General Fund increased by $648.8 million, the fund balance for the Motor License Fund increased by $187 million, the fund balance for the Tobacco Settlement Fund increased by $74 million and the fund balance for aggregated non-major funds increased by $248 million. See "General Fund – Fiscal Year 2004 Financial Results."

To help understand the relationship between the Commonwealth's GAAP fund balance (fund perspective) for governmental funds and the Commonwealth's governmental net assets (government-wide perspective) under the new presentation of financial information the following reconciliation is presented:

Table 6
Reconciliation of the Balance Sheet
Governmental Funds (Fund Perspective) to
the Statement of Net Assets - Governmental Activities
June 30, 2004
(In Thousands)

Fund Balances - Governmental Funds		
General Fund	$	3,006.5
Motor License Fund		1,079.6
Tobacco Settlement Fund		893.0
Nonmajor Funds		1,814.7
Total Fund Balance - Governmental Funds	$	6,793.8
Plus: Capital Assets, including infrastructure		30,616.4
Less: Accumulated depreciation		(9,911.1)
Plus: Deferred revenue		1,665.1
Plus: Additional accrued receivables		97.3
Plus: Net assets of internal service funds		70.1
Plus: Inventories		80.6
Less: Long-term liabilities		(9,726.6)
Total Net Assets - Governmental Activities	$	19,685.6

More detailed information with respect to the General Fund and the Motor License Fund, major operating funds that are categorized as governmental funds, is presented in Table 7 (General Fund) and in Table 9 (Motor License Fund).

The financial tables that follow containing GAAP basis financial data are unaudited but are derived from the Commonwealth's audited financial statements. The discussion of financial performance on a budgetary basis for prior fiscal years is based on an analysis of budget numbers and not on numbers prepared in accordance with GAAP. Likewise, the discussion of the financial estimates for fiscal year 2005 and the proposed budget for fiscal year 2006 reflects a budgetary basis analysis rather than a GAAP basis analysis.

General Fund

Financial Results for Recent Fiscal Years (GAAP Basis)

During the five-year period from fiscal year 2000 through fiscal year 2004, total revenues and other sources increased by an average of 4.6 percent annually. Tax revenues during this same period increased by an annual average of 2.7 percent. During the past several fiscal years slow economic growth and the resulting slow growth for tax revenues have caused fees and license income and other financing sources such as transfers from other funds to become a larger portion of income to the General Fund. Expenditures and other uses during the fiscal years 2000 through 2004 rose at an average annual rate of 5.4 percent. Comparison of expenditures by individual category in fiscal years 2002 through 2004 to prior fiscal years is not reliable due to a change to the definitions for these expenditure categories in fiscal year 2002.

The fund balance at June 30, 2004 totaled $3,006.5 million, an increase of $648.8 million from the balance at June 30, 2003. The fiscal year 2004 year-end unreserved-undesignated portion of the fund balance was $1,633.3 million, $318.8 million above the amount recorded for fiscal year 2003 at years end.

Table 7 on the next page presents a summary of revenues and expenditures (GAAP basis for the General Fund, including the Budget Stabilization Reserve Fund that replaced the Tax Stabilization Reserve Fund) for the fiscal years 2000 through 2004.

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Table 7
Results of Operations–General Fund
GAAP Basis–Unaudited
(In Thousands)

	Fiscal Year Ended June 30				
	2000	2001	2002(a)	2003	2004
Fund Balance — Beginning of Period	$ 2,863,420	$ 4,263,641	$ 4,484,995	$ 3,022,842	$ 2,357,713
Restatements	-	-	159,919	-	-
Fund Balance — Beginning of Period, as Restated	$ 2,863,420	$ 4,263,641	$ 4,644,914	$ 3,022,842	$ 2,357,713
Revenues:					
Taxes	$ 19,046,032	$ 19,297,659	$ 18,649,928	$ 19,553,998	$ 21,190,494
Licenses and fees	197,012	202,591	201,388	250,264	275,898
Intergovernmental	10,062,420	10,588,526	11,652,199	12,943,624	14,790,701
Other revenues	3,069,378	2,779,739	2,539,271	2,313,183	2,423,649
Other Financing Sources:					
Operating transfers in	78,723	75,491	213,419	425,875	133,670
Transfer from component unit	-	-	256,206	-	-
Other additions	594	2,789	4,428	3,851	1,535
TOTAL REVENUES AND OTHER SOURCES	$ 32,454,159	$ 32,946,795	$ 33,516,839	$ 35,490,795	$ 38,815,947
Expenditures: (b)					
Direction and supportive services	$ 1,333,114	$ 1,613,383	$ 910,399	$ 854,434	$ 1,412,250
Protection of persons and property	2,912,289	3,026,625	3,104,079	2,941,339	2,958,160
Health and human services	15,645,577	16,645,180	18,221,987	19,549,141	20,816,721
Public education	8,281,804	8,667,618	8,813,198	10,174,386	10,520,428
Recreation and cultural enrichment	-	-	326,361	324,186	225,367
Conservation of natural resources	134,511	155,468	-	-	-
Economic development	471,716	522,073	824,830	984,334	963,926
Transportation	399,412	401,621	315,591	407,328	351,911
Capital outlay	44,998	117,354	50,818	17,698	142,651
Other Uses:					
Operating transfers out	1,707,038	1,460,431	1,528,451	903,078	775,732
Transfers to component units	-	-	1,043,197	-	-
TOTAL EXPENDITURES AND OTHER USES	$ 30,930,459	$ 32,609,753	$ 35,138,911	$ 36,155,924	$ 38,167,146
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURE AND OTHER USES	1,523,700	337,042	(1,622,072)	(665,129)	648,801
Residual Equity Transfer In (Out)	(123,479)	(115,688)	-	-	-
Fund Balance — End of Period	$ 4,263,641	$ 4,484,995	$ 3,022,842	$ 2,357,713	$ 3,006,514
Components of Fund Balance					
Reserved for encumbrances	$ 397,827	$ 426,956	$ 479,314	$ 341,881	$ 259,178
Reserved for advances and other	1,487,789	1,454,146	315,822	431,552	622,292
Unreserved — designated	677,897	1,079,047	623,884	269,775	491,718
Unreserved — undesignated	1,700,128	1,524,846	1,603,822	1,314,505	1,633,326
TOTAL FUND BALANCE	$ 4,263,641	$ 4,484,995	$ 3,022,842	$ 2,357,713	$ 3,006,514

(a) Restated. For the fiscal year ended June 30, 2002 and subsequent fiscal years, the Commonwealth has adopted several new accounting and reporting standards described earlier in "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES – New Governmental Accounting and Reporting Standards." The new standards require numerous changes to how fund financial statements are presented. Certain funds have been reclassified and fund balances restated. See Note B to the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2002 for a more detailed explanation. These changes may limit the comparability of that year's data and subsequent data to data for prior fiscal years.

(b) Beginning with the fiscal year ended June 30, 2002, the number and the definition of the functional categories of expenditures have been revised. These changes limit the comparability of fiscal years' 2002, 2003 and 2004 data to data shown for prior fiscal years.

Source: Compiled from Office of the Budget, Comprehensive Annual Financial Report for fiscal years ended June 30, 2004, 2003, 2002, 2001, and 2000.

Fiscal Year 2003 Financial Results

GAAP Basis. At June 30, 2003, the General Fund reported a fund balance of $2,357.7 million, a decrease of $665 million from the reported $3,022.8 million fund balance at June 30, 2002. On a net basis, total assets increased by $388 million to $8,525 million. Liabilities increased by $1,053 million to $6,167 million largely because of a $383 million increase in accounts payable. A large part of the $665 million net decrease in General Fund fund balance was because the General Fund transferred $903 million to other Funds and provided $1,037 million to component units. Without these items, the General Fund would have increased by $1,275 million. Total General Fund expenditures increased by 8.2 percent during the fiscal year ended June 30, 2003, on a reported basis, largely because of a sharp increase in expenditures for medical and other assistance (reported as part of health and human services) and a change in classification for component unit subsidies. Year-over-year expenditures for that function increased by 7.3 percent; otherwise, all other expenditures increased by 2 percent, largely as a result of executive spending controls during the fiscal year, before the change in component unit subsidy treatment. General Fund tax revenues increased by 4.9 percent due to economic growth and, to a large degree, by increases in cigarette tax rates. Intergovernmental revenues increased by 11.1 percent due to increases in federally-funded programs, particularly medical and other assistance. Total General Fund revenues increased by 6.1 percent during the fiscal year. The overall decrease in fund balance ($665 million) during the fiscal year was an improvement of $957 million over the prior year fiscal year decrease in fund balance ($1,622 million). On an overall basis, during periods of declining or slow economic growth, it is common for the fund balance of the General Fund to decline.

Budgetary Basis. The following financial information is based on the Commonwealth's unaudited budgetary basis financial statements for fiscal year 2003. Continued slow growth in the national economy since the recession of 2001 impacted the Commonwealth tax and revenue collections in fiscal year 2003. Actual fiscal year Commonwealth revenues were below estimate by 2.3 percent or $497.6 million. Total fiscal year 2003 Commonwealth revenues net of reserves for tax refunds and including intergovernmental transfers and additional resources were $21,808.5 million. Actual expenditures from fiscal year 2003 appropriations were 1.4 percent or $295.7 million below the original enacted amounts for fiscal year 2003. Total expenditures net of appropriation lapses and including intergovernmental transfers and expenditures from additional resources totaled $21,671.9 million. As result of financial operations during fiscal year 2003, efforts to reduce expenditures and the General Assembly's repeal of the transfer of $300 million from the General Fund to the Budget Stabilization Reserve Fund, the unappropriated surplus balance increased by $136.6 million prior to the statutorily required 25 percent transfer to the Budget Stabilization Reserve Fund. As result, the fiscal year 2003 final unappropriated surplus balance was $209.3 million as of June 30, 2003.

Revenues available to the Commonwealth, including intergovernmental transfers and additional resources, and prior to reserves for refunds increased 11.0 percent from fiscal year 2002 levels. Fiscal year 2003 revenues totaled $21,808.5 million, an increase of $2.2 billion over fiscal year 2002 revenues. Commonwealth taxes and revenues, prior to reserves for refunds, increased by $1.3 billion to $21,314.5 million in fiscal year 2003, a 6.3 percent increase. This increase in tax revenues was primarily due to increases for certain Commonwealth taxes enacted with the fiscal 2003 budget. While Commonwealth revenues increased year over year, revenues were below the estimate enacted with the fiscal 2003 budget. Commonwealth taxes and revenues (prior to reserves for tax refunds) totaled $21,314.5 million, $497.6 million (2.3 percent) below the estimate made at the time the fiscal year 2003 budget was enacted. Most major Commonwealth tax categories performed below the estimated amount for fiscal year 2003. Corporate tax receipts were below estimate by $173.3 million or 4.4 percent, including corporate net income tax receipts which were $201.2 million, or 12.6 percent below estimate. The Commonwealth's capital stock and franchise tax was also below estimate by $60.3 million, or 6.3 percent for fiscal year 2003. Other selective corporate taxes exceeded their estimate for fiscal year 2003 by $87.4 million or 6.4 percent. Sales tax collections, the Commonwealth's largest tax source, were below the fiscal year 2003 estimate by $12.1 million or 0.2 percent. Receipts from taxes on the sale or lease of motor vehicles were above estimate $75.7 million (6.5 percent) while sales tax collections from non-motor vehicle sales were below estimate by $87.8 million or 1.4 percent. Personal income tax receipts were below estimate by $289.9 million or 3.9 percent. Within the personal income tax category, receipts from withholding collections were $129.4 million or 2.2 percent below estimate. Non-withholding personal income tax receipts were also below estimate by $160.5 million or 10.2 percent. Non-tax revenues, particularly earnings on investments and escheats, exceeded the estimate by $15.7

million or 2.0 percent. Reserves for tax refunds in fiscal year 2003 were $929.6 million, a decrease of $37.6 million or 3.9 percent from fiscal year 2002 levels.

Commonwealth expenditures of appropriations, including supplemental appropriations, intergovernmental transfers and additional resources, and net of appropriation lapses, totaled $21,671.9 million, representing an increase of $797.5 million or 3.8 percent from fiscal year 2002 levels. A total of $466.9 million in appropriations were lapsed in fiscal year 2003 as part of a comprehensive effort by the executive branch to limit expenditures in response to revenue collections below the estimate enacted with the 2003 budget. The fiscal year 2003 budget relied on intergovernmental transfers for a larger portion of medical assistance costs than in fiscal 2002. Intergovernmental transfers replaced $844.6 million of General Fund medical assistance costs in fiscal year 2003 compared to $549.6 million in fiscal year 2002. Expenditures normally funded from Commonwealth revenues, but which were funded from additional resources in fiscal year 2003 totaled $578.9 million. These expenditures included $380.4 million in General Fund debt service that was paid from other available funds, including the proceeds of a May 2002 refunding bond issued by the Pennsylvania Industrial Development Authority as well as $198.5 million in long term care costs that were paid from Tobacco Settlement Fund revenues. In addition, $300 million had been appropriated from the General Fund in fiscal year 2003 for transfer to the Budget Stabilization Reserve Fund. This transfer, however, was repealed by the General Assembly during fiscal year 2003 as part of the enactment of the fiscal year 2004 budget. A more detailed description of fiscal year 2003 expenditures among major program areas is provided in the section titled "COMMONWEALTH REVENUES AND EXPENDITURES."

Fiscal Year 2004 Financial Results

GAAP Basis. At June 30, 2004, the General Fund reported a fund balance of $3,006.5 million, an increase of $648.8 million from the reported $2,357.7 million fund balance at June 30, 2003. On a net basis, total assets increased by $1,939 million to $10,464 million. Liabilities increased by $1,290 million to $7,457 million largely because of a $764 million increase in accounts payable.

General Fund tax revenues increased by 8.4 percent due to economic growth and specific statutory increases in certain tax bases and rates enacted in December 2003. Intergovernmental revenues increased by 14.3 percent, due primarily to increases in Federally-funded programs, particularly medical and other assistance, where expenditures increased over the prior year. Total General Fund revenues increased by 10.3 percent during the fiscal year. The overall increase in the fund balance, $648.8 million, during the fiscal year was an improvement of $1,314 million over the prior fiscal year decrease in fund balance of $665 million. On an overall basis, during periods of declining or slow economic growth, it is common for the fund balance of the General Fund to decline and, conversely, to increase during periods of economic growth. During periods of economic growth, General Fund revenues increase while certain significant expenditures, such as medical assistance, also increase, but at a slower rate. Total General Fund expenditures increased by 6.0 percent during the fiscal year ended June 30, 2004, on a GAAP-reported basis, largely because of the increase in expenditures for medical and other assistance (reported as part of health and human services). Expenditures for direction and supportive services increased due to significantly higher employer costs for both active and retired employee healthcare benefits. Year-over-year expenditures for the health and human services function increased by 6.5 percent; all other expenditures, on a combined basis, increased by 5.5 percent, largely as a result of higher amounts appropriated throughout most of the General Fund.

Budgetary Basis. A rebounding national economy that exceeded preliminary estimates for growth resulted in actual fiscal year 2004 Commonwealth General Fund revenues exceeding the budget estimate by 2.9 percent, or $636.7 million. Total fiscal year 2004 revenues net of reserves for tax refunds and including intergovernmental transfers and additional resources totaled $23,159.7 million. Total expenditures net of appropriation lapses and including intergovernmental transfers and expenditures from additional resources was $23,089.2 million. As result of Commonwealth financial operations during the fiscal year the preliminary unappropriated surplus balance, prior to the statutorily required 25 percent transfer to the Budget Stabilization Reserve Fund, was scheduled to increase $57.5 million to $266.8 million from the fiscal year 2003 ending balance. Following the statutorily required 25 percent transfer to the Budget Stabilization Reserve Fund ($66.7 million), a supplemental transfer of $123.3 million was also made to the Budget Stabilization Reserve Fund. As result, the fiscal year 2004 final unappropriated surplus balance was $76.7 million as of June 30, 2004.

Revenues available to the Commonwealth, including intergovernmental transfers and additional resources, increased 6.2 percent from fiscal year 2003 levels. Fiscal year 2004 revenues totaled $23,159.7 million, an increase of $1,351.2 million over fiscal year 2003 revenues. Commonwealth taxes and revenues, prior to reserves for refunds, increased by $1,513.6 million to $22,828.1 million in fiscal year 2004, a 7.1 percent increase from fiscal year 2003 actual receipts. This increase in tax revenues was primarily due to increases for certain Commonwealth taxes enacted with the fiscal year 2004 budget. Tax revenues to the Commonwealth for fiscal year 2004 exceeded the budget estimate, as re-certified in December 2003, by $636.7 million or 2.9 percent. Nearly all Commonwealth major tax and revenue categories experienced revenue collections above the budget estimate. The personal income tax was $117.8 million or 1.5 percent over the estimate for fiscal year 2004; the non-withholding portion of the personal income tax was 8.4 percent or $124.5 million over the estimate. Corporate net income tax collections were $201.6 million (13.7 percent) over estimate and the Capital Stock and Franchise tax collections were $50 million (5.4 percent) more than projected. Sales and use tax receipts exceeded the budgeted amount by $28 million or 0.4 percent. The insurance premiums tax and the inheritance tax each exceed their estimates by $58.9 million (17.7 percent) and $43.3 million (6.2 percent) respectively. Non-tax revenue collections were $158.9 million (25.5 percent) greater than projected, principally due to increased earnings on investments and the enhancement of the Commonwealth's escheat program. The rate of growth in earnings on investments was, in large part, the result of actions by the Commonwealth Treasurer to terminate a formerly separate pool of available General Fund cash balances that have been invested in equity securities. By combining all General Fund cash balances into one common investment pool, the General Fund achieved approximately $50 million in previously unrealized capital gains during fiscal year 2004. Further, revisions to the escheat program resulted in approximately $190 million in additional revenues. As part of the fiscal year 2004 budget certain tax, fee and other revenue enhancement items totaling $794 million were enacted. Major components of the $794 million increase were: (i) an increase in the personal income tax rate from 2.8 percent to 3.07 percent, which is estimated to have provided $301.7 million in fiscal year 2004; (ii) an extension of the gross receipts tax to cellular and interstate telecommunications, which is estimated to have provided $222.4 million; (iii) revisions to the law regarding the escheating of property to the Commonwealth, which is estimated to have provided $190 million; (iv) a continued partial deferral of the scheduled reduction in the capital stock and franchise tax, which is estimated have provided $60.7 million; (v) an increase of 10 cents per pack to the cigarette tax, which is estimated to have provided $25.4 million; and (vi) various other minor revisions, including some tax cuts, which combined to total a net increase in Commonwealth revenues of $794 million in fiscal year 2004.

Reserves for tax refunds in fiscal year 2004 were $1,014.7 million, an increase of 9.2 percent over fiscal year 2003 reserves. Recent tax rate and tax base changes have contributed to the growth rate in refunds in fiscal year 2004. Actual tax refunds have stabilized after several recent years of increases. At the end of fiscal year 2004, approximately $91.7 million of reserves were available for making tax refunds in the following fiscal year.

Expenditures for the fiscal year, including supplemental appropriations, intergovernmental transfers and additional resources, and net of appropriation lapses, totaled $23,089.2 million, representing an increase of $1,417.3 million or 6.5 percent from the fiscal year 2003 level. A total of $182.9 million in appropriations were lapsed in fiscal year 2004. The fiscal year 2004 budget continued to utilize an enhanced level of intergovernmental transfers for a portion of medical assistance costs, albeit at a reduced rate from fiscal year 2003. Intergovernmental transfers replaced $738.7 million of General Fund medical assistance costs in fiscal year 2004, compared to $844.6 million in fiscal year 2003. Expenditures normally funded from Commonwealth revenues that were instead funded from additional resources in fiscal year 2004 totaled $607.6 million. These expenditures included $457.6 million in available federal fiscal relief funds, which were used to offset certain medical assistance and other health care costs as well as $150 million in available capital debt fund reserves, which were used to offset General Fund debt service costs in fiscal year 2004.

As part of his fiscal year 2004 budget proposal, the Governor proposed two major program expansions that were enacted by the General Assembly. In education, the Governor proposed to shift a substantial portion of local public school costs from local property taxes levied by school districts to an increased subsidy payment to school districts by the Commonwealth. The program as enacted would increase, over time, the Commonwealth's subsidy of local public school costs to 50 percent of total costs in the aggregate. Funds for education at the local level totaling nearly $1.0 billion are expected to be funded from taxes realized from the legalization of slot machines at racetracks in the state. The increased level of education funding from the Commonwealth would be used to reduce local property taxes by an equal amount. The Governor also proposed an economic stimulus plan for the Commonwealth to provide additional funding to be combined with private investments to invest in economic development projects within the state. Investments are to be directed to blighted rural, urban and suburban sites to be re-developed to spur the location of new job-creating businesses. The funding for the economic stimulus program is to come from $2,025 million of debt issued over more than four fiscal years. The proposed debt is composed of (i) $890 million of capital budget debt in addition to that anticipated to support the current capital budget program, and (ii) $1,135 million of debt of the newly created Commonwealth Financing Authority (the "Authority") to be repaid from annual budget appropriations.

Major portions of the Governor's economic stimulus proposal were enacted with the passage of Acts 10, 12, 22, 23 and 67 of 2004. Act 22 created the Authority, an independent authority with the power to issue debt of the Authority for the purposes of funding certain activities of the economic stimulus program. Legislation enacted to date has established, through the Authority, several new grant and loan programs as well as new loan guarantee programs to be funded with debt of the Authority. The Business in Our Sites program is expected to be capitalized with $300 million in debt of the Authority so that it may offer flexible loans and grants to local municipalities for acquisition and site preparation for economic development opportunities. The Building Pennsylvania program is expected to receive $150 million in Authority bond proceeds to provide funding for the development of real estate assets for purposes of economic stimulation. These funds will be loaned to private sector real estate funds on a matching basis to encourage economic development through real estate development. A new Pennsylvania Venture Guarantee Program is being created to be funded with up to $250 million in Authority bond proceeds in order to provide guarantees to venture capital firms investing in Pennsylvania. The Pennsylvania Capital Investment Program will provide up to $60 million in capital, derived from Authority bond proceeds, to Pennsylvania venture capital firms for investment in underserved areas of the Commonwealth. The First Industries Fund is expected to be capitalized with $150 million from Authority debt, to provide financial incentives and assistance to tourism-related and agricultural projects. A Second Stage Loan program is expected to be capitalized with $50 million in bond proceeds to provide guarantees for bank loans to second stage manufacturers and technology companies for working capital needs. The Core Industries Program will provide $75 million in revolving loan funds, funded by bonds of the Authority, for enhanced machinery and equipment financing. The Tax Increment Financing Guarantee Program, which will be funded through debt of the Authority, will provide $100 million in loan guarantee assistance for small and mid-sized Commonwealth communities to encourage this method of financing economic development projects.

It is anticipated that General Fund appropriations will be required to support the Authority's annual debt service cost on its debt. Provisions of Act 22 of 2004 place limitations on the incurring of debt to fund portions of the economic stimulus program. Such limitations include provisions that no more than $250 million in debt may be issued within a fiscal year to support certain activities within the economic stimulus program. Further, Act 22 of 2004 requires the Secretary of the Budget to certify that sufficient excess General Fund revenues exist or will likely exist to support the annual issuance of up to $250 million in economic stimulus debt. The General Assembly also approved Act 67 of 2004 which enacted the remaining component of the Governor's economic stimulus proposal, an increase of $640 million in certain capital budget debt authorization for local economic redevelopment projects.

In February 2004, the General Assembly approved Act 10 of 2004, which authorized a ballot referendum pertaining to the Governor's proposed water and sewer infrastructure program. On April 27, 2004, the voters of the Commonwealth approved the referendum proposal authorizing the Commonwealth to incur an additional $250 million in general obligation debt for the funding of certain local water and sewer capital infrastructure projects directly related to economic development projects funded via the Governor's economic stimulus program. The General Assembly has approved legislation to authorize the issuance of debt approved by the referendum.

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Table 8
Sources, Uses and Changes in Unappropriated Balance
General Fund and Other Funding Sources — Unaudited Budgetary Basis
Commonwealth Revenues Only
(In Millions)

	Actual Fiscal Year 2004	Estimate Fiscal Year 2005	Proposed Fiscal Year 2006
Sources:			
Cash revenues	$ 22,828.1	$ 24,157.4	$ 24,734.1
Tax refunds	(1,014.7)	(1,060.5)	(1,085.0)
Additional resources available	607.6	399.2	44.1
Intergovernmental transfer transactions[(a)]	738.7	692.5	907.6
TOTAL SOURCES	$ 23,159.7	$ 24,188.6	$ 24,600.8
Uses:			
General fund appropriations	$ 21,925.8	$ 23,030.8	$ 23,845.6
Expenditures from additional resources	607.6	399.2	44.1
Lapses and other reductions[(b)]	(182.9)	(125.0)	......
Intergovernmental transfer transactions[(a)]	738.7	692.5	907.6
TOTAL USES	$ 23,089.2	$ 23,997.5	$ 24,797.3
OPERATING BALANCE	$ 70.5	$ 191.1	$ (196.5)
BEGINNING UNAPPROPRIATED BALANCE	209.3	76.7	201.5
ADJUSTMENT TO UNAPPROPRIATED BALANCE[(c)]	(13.1)	0.8	......
TRANSFER (TO)/FROM BUDGET STABILIZATION RESERVE FUND[(d)]	(190.0)	(67.1)	(1.2)
ENDING UNAPPROPRIATED BALANCE	$ 76.7	$ 201.5	$ 3.8

Totals may not add due to rounding.
(a) Only includes funds replacing Commonwealth funds. Fiscal year 2005 includes $267.3 million and Fiscal year 2006 includes $145 million from a nursing home tax used to augment appropriated funds for long-term care.
(b) Includes prior year appropriation lapses from fiscal year 2003 of $142.5 million in fiscal year 2004 and $75 million from fiscal year 2004 in fiscal year 2005.
(c) The fiscal year 2004 adjustments generally reflect the appropriation of prior year funds.
(d) The Tax Stabilization Reserve Fund was abolished in fiscal year 2002 and replaced by the Budget Stabilization Reserve Fund in fiscal year 2003.

Fiscal Year 2005 Budget

The following financial information is based on the Commonwealth's budgetary basis financial data.

Budgetary Basis. The adopted budget for fiscal year 2005, enacted on July 4, 2004, was based initially on an estimated 4.5 percent increase for Commonwealth General Fund revenues prior to accounting for any changes in tax and revenue provisions enacted in the second half of fiscal year 2004. After adjustments for various tax rate and tax base changes enacted for the fiscal year 2004 budget, total Commonwealth General Fund revenues were projected to increase 3.8 percent over fiscal year 2004 actual receipts and total $23,866.5 million prior to reserves for tax refunds. The tax revenue component of Commonwealth receipts, including the effects of the tax rate and tax base changes enacted in fiscal year 2004, was expected to rise $1,342.1 million or 6.1 percent over fiscal year 2004 actual receipts. Approximately two-thirds of the increase in tax revenues is associated with the various tax rate and tax base changes. Major components of the tax revisions are: (i) an increase in the personal income tax from 2.8 percent to 3.07 percent, which was expected to produce $729 million in fiscal year 2005; (ii) a restructuring of taxation of telecommunications to include the imposition of the gross receipts tax on cellular and interstate telecommunication as well as certain sales and use tax exemptions for particular telecommunications activities which was estimated to generate $292.1 million in fiscal year 2005; (iii) an increase to the cigarette tax from $1.00 per pack to $1.35 per pack, which was expected to produce $247.5 million in fiscal year 2005; $191.9 million of this $247.5 million, however, is expected to be transferred to the new Health Care Provider Retention Account to be used to provide financial assistance for malpractice premiums for certain physicians practicing in particular high-risk medical specializations under the medical malpractice abatement program. This program was enacted for calendar years 2003 and 2004, and the General Assembly has recently approved an extension for an additional year; (iv) a modification of the scheduled phase-out of the capital stock and franchise tax for tax years 2003 and 2004, which was projected to produce $116.8 million in fiscal year 2005; and (v) various other tax rate and tax base revisions, including some tax cuts. Receipts of Commonwealth non-tax revenues were expected to return to historic levels of approximately $478.4 million in fiscal year 2005, a reduction of $303.6 million from fiscal year 2004 actual receipts. Various revisions to the Commonwealth's escheat program were enacted as part of the fiscal year 2003 and 2004 budgets. These revisions to the escheat program have produced substantial non-recurring revenues during each of the two most recent fiscal years. Additionally, significant non-recurring capital gains earnings on the investment of available General Fund cash balances (See "General Fund Fiscal Year 2004 Financial Results") and increased contributions from the Commonwealth's liquor store profits contributed to enhanced non-tax revenues during the prior two fiscal years. Projected growth in fiscal year 2005 non-tax revenues was estimated to be 6.6 percent above the average non-tax revenues collected in fiscal years 1999-2002, which were prior to the aforementioned enhancements to the escheat program.

The fiscal year 2005 estimate for Commonwealth revenues, as estimated in June 2004, was based upon an economic forecast for national real gross domestic product to grow at a 4.1 percent rate from the second quarter 2004 to the second quarter 2005. The forecast anticipated that economic growth would continue to recover from a period of softness in the second quarter of 2004 and that employment levels would continue to improve moderately. Trends in the Pennsylvania economy are expected to maintain their close association with national economic trends. Personal income growth in Pennsylvania is projected to remain slightly below that of the U.S., while the Pennsylvania unemployment rate is anticipated to be close to the national rate.

Through the second half of calendar 2004 and early 2005, while economic growth in the nation and the state has been slightly below that which was forecasted in June 2004, Commonwealth revenues have nonetheless exceeded the estimates used to certify fiscal year 2005 General Fund revenues. Estimates for fiscal year 2005 General Fund revenues were revised in February 2005 as part of the Governor's proposed fiscal year 2006 budget. Based on prevailing economic conditions and trends in actual receipts through January, the fiscal year 2005 General Fund revenue estimate was increased by $290.9 million. Total General Fund revenues for fiscal year 2005 are projected to be $24,157.4 million. Actual Commonwealth revenues for the fiscal year-to-date through April 2005 are $374 million above the estimate for that period, a surplus of 1.9 percent. Corporate taxes are $28.3 million over estimate, a 0.7 percent surplus to the year-to-date estimate. Personal income taxes are $211.8 million over estimate, a surplus of nearly 3 percent versus the year-to-date estimate. Sales and Use taxes are $41 million, 0.6 percent, over estimate and Realty Transfer taxes are $65 million or 20 percent over estimate. Non-tax revenues exceed the year-to-date estimate by $111.7 million or 28 percent. Non-tax revenues continue to be positively affected by remaining benefits of changes to the Commonwealth's escheat program enacted as part of the 2003 and 2004 budgets. Additional revenues from the previous changes to the escheats program were not forecast as part of the fiscal year 2005 revenue estimate. Additionally, earnings on investments of available Commonwealth cash deposits are exceeding the estimate.

The enacted fiscal year 2005 budget provides $22,876.1 million of appropriations from Commonwealth revenues, an increase of 4.5 percent from fiscal year 2004 appropriations, and represents a planned draw down of $71.8 million of the unappropriated surplus balance available at the end of fiscal year 2004. In addition, approximately $377.6 million of remaining federal fiscal relief is appropriated in fiscal year 2005 to fund expenditures normally funded from Commonwealth revenues. The enacted budget also includes $673.8 million in funding for medical assistance expenditures through intergovernmental transfer proceeds. This amount is a decrease of 8.8 percent from the $738.7 million in intergovernmental transfer proceeds utilized during fiscal year 2004. Under these intergovernmental transfer transactions certain county governments contribute funds to the Commonwealth to help pay Medicaid expenses. The Commonwealth receives the contributions as augmentations to appropriations of Commonwealth revenues for the medical assistance program. These augmentations have the effect of supplementing the amount of Commonwealth revenues available for the medical assistance program and are available to match federal Medicaid funds. Federal authority for Pennsylvania to use the county contributions to pool transactions to match additional federal funds is currently scheduled to expire in 2010. The fiscal year ending unappropriated balance is currently estimated to be $201.5 million for fiscal year 2005. Included in the Governor's proposed fiscal year 2006 budget is a request for supplemental appropriations for fiscal year 2005 totaling $154 million. Additional funding via the requested supplemental appropriation includes emergency response funding relative to Tropical Storm Ivan as well as additional funding for the Department of Public Welfare to address an increase in medical assistance caseloads and rising health care costs beyond those forecast in the fiscal year 2005 budget.

The achievement of the budgeted results may be adversely affected by a number of trends or events, including developments in the national and state economy.

Fiscal Year 2006 Proposed Budget

A proposed fiscal year 2006 budget was submitted by the Governor to the General Assembly on February 9, 2005. The proposed budget recommends appropriations totaling $23.8 million of Commonwealth funds against estimated revenues, net of tax refunds and proposed tax reductions of $23.6 billion. The $0.2 billion difference between estimated revenues and recommended appropriations is to be funded by a draw down of the anticipated $201 million beginning balance. Additionally, the proposed fiscal year 2006 budget allocates additional state funds to replace significant amounts of formerly available federal fiscal relief. The Governor has again proposed a major environmental initiative in the fiscal year 2006 proposed budget. The proposal, known as "Growing Greener II," included a proposed $800 million voter referendum bond issue to fund certain environmental programs. Additionally, the Governor has proposed $91 million in new fees to be imposed on the deposit of certain waste in Pennsylvania landfills of which a portion would be utilized to support debt service on the proposed Growing Greener II referendum debt. Following negotiations between the Governor and the General Assembly regarding the amount of the proposed referendum debt, the General Assembly enacted and the Governor signed into law Act 1 of 2005. This act authorizes the placement on the May 17, 2005 ballot of a question as to whether the voters of the Commonwealth will approve the issuance of up to $625 million in debt of the Commonwealth to support programs commonly referred to as "Growing Greener II." Prior to the issuance of such debt, voters of the Commonwealth must approve the referendum and the General Assembly must enact legislation authorizing the expenditure of any voter-approved referendum debt.

In April 2005, the Pennsylvania House of Representatives began deliberations and the amendment process for the fiscal year 2005 General Appropriation Bill, that could become the 2006 fiscal year enacted budget if approved by both houses of the General Assembly and the Governor. Further legislative debate on these various bills, including the General Appropriations Bill, is anticipated before they are adopted by both legislative houses.

The General Assembly may change, eliminate or add amounts and items to the proposed budget submitted by the Governor and there can be no assurance that the budget, as proposed by the Governor, will be enacted into law by June 30. In the event that the General Assembly fails to pass or the Governor fails to sign an appropriation act prior to July 1 of any fiscal year for that fiscal year, the Pennsylvania Constitution, the laws of Pennsylvania and certain state and federal court decisions provide that the Commonwealth may continue during such periods of an un-budgeted fiscal year to make debt service payments, payments for mandated federal programs such as cash assistance and payments related to the health and safety of the citizens of the Commonwealth such as police and correctional services. Failure, however, of the Governor and the General Assembly to reach agreement on the budget could potentially have adverse effects on the Commonwealth including, among others, the collection of revenue and completion of the annual audit. See Appendix C for additional information on the budget enactment process.

Motor License Fund

The Constitution requires all proceeds of motor fuels taxes, vehicle registration fees, license taxes, operators' license fees and other excise taxes imposed on products used in motor transportation to be used exclusively for construction, reconstruction, maintenance and repair of and safety on highways and bridges and for debt service on obligations incurred for these purposes. The Motor License Fund is the fund through which most such revenues are accounted for and expended. Portions of certain taxes whose receipts are deposited into the Motor License Fund are legislatively restricted to specific transportation programs. These receipts are accounted for in restricted accounts in the Motor License Fund and are not included in the budgetary basis presentations or discussions on the Motor License Fund. The Motor License Fund budgetary basis includes only unrestricted revenue available for annual appropriation for highway and bridge purposes. The GAAP basis presentations include restricted account revenues and expenditures.

Financial Results for Recent Fiscal Periods (GAAP Basis)

The fund balance at June 30, 2004, was $1,079.6 million, a $186 million increase from the June 30, 2003 fund balance, which represents a nearly 21 percent increase. Over the five fiscal years of 2000 through 2004, revenues and other sources have averaged an annual 4.5 percent increase. Expenditures and other uses during the period from fiscal years 2000 through 2004 have averaged a 3.3 percent annual increase. Revenues grew 1.4 percent from fiscal 2003 to fiscal 2004. During fiscal year 2004, the fund reported total tax revenues of $1,742 million and license and fee revenue of $867 million, which represented growth of 2.2 percent and 2.9 percent respectively from fiscal year 2003 to fiscal year 2004. Reported federal revenues, received principally from the Federal Highway Administration totaled $1,323 million, a decrease of 4.1 percent. Other revenues to the fund, principally earnings on investments, totaled $177 million, an increase of 41.7 percent from the prior fiscal year. Expenditures from the fund were $3,922 million during fiscal year 2004, an increase of 1.3 percent over fiscal year 2003 expenditure levels. The increase in capital outlay during the 2004 fiscal year was caused by a change in reporting classification for highway/bridge construction costs, offset by a corresponding decrease in reported transportation expenditures. In combination, the year-over-year increase for both classifications was $65 million or 2 percent. Table 9 sets forth a condensed summary of revenues and expenditures (presented on a GAAP basis) for the Motor License Fund for the fiscal years 2000 through 2004.

Table 9
Results of Operations–Motor License Fund
GAAP Basis–Unaudited
(In Thousands)

	2000	2001	2002[a]	2003	2004
Fund Balance — Beginning of Period	$ 711,558	$ 684,681	$ 751,961	$ 712,427	$ 893,133
Revenues:					
Taxes	$ 1,632,698	$ 1,647,122	$ 1,694,421	$ 1,705,082	$ 1,742,332
Licenses and fees	806,256	806,726	838,525	842,466	866,552
Intergovernmental	840,092	1,305,345	1,402,468	1,379,786	1,323,005
Other revenues	159,639	123,480	94,273	124,866	176,910
Other Financing Sources:					
Operating transfers in	-	-	3,937	-	-
Other additions	13,962	3,818	1,339	805	-
TOTAL REVENUES AND OTHER SOURCES	$ 3,452,647	$ 3,886,491	$ 4,034,963	$ 4,053,005	$ 4,108,799
Expenditures: (b)					
Direction and supportive services	$ 383,151	$ 399,531	$ 48,579	$ 48,400	$ 49,693
Protection of persons and property	-	-	492,504	514,100	496,105
Public education	-	-	1,075	1,068	1,023
Recreation and cultural enrichment	-	-	1,927	3,504	4,199
Transportation	2,884,897	3,234,879	3,369,240	3,205,830	1,641,755
Capital outlay	53,494	46,712	46,416	39,154	1,668,261
Other Uses:					
Operating transfers out	129,982	110,089	86,756	60,243	61,279
Transfers to component units	-	-	28,000	-	-
TOTAL EXPENDITURES AND OTHER USES	$ 3,451,524	$ 3,791,211	$ 4,074,497	$ 3,872,299	$ 3,922,315
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURE AND OTHER USES	1,123	95,280	(39,534)	180,706	186,484
Residual Equity Transfers In (Out)	(28,000)	(28,000)	-	-	-
Fund Balance — End of Period	$ 684,681	$ 751,961	$ 712,427	$ 893,133	$ 1,079,617
Components of Fund Balance					
Reserved for encumbrances	$ 250,948	$ 382,462	$ 389,942	$ 456,015	$ 591,598
Reserved for advances and other	-	-	-	-	220,662
Unreserved - designated - highways	250,743	182,670	175,249	215,946	209,647
Unreserved - undesignated	182,990	186,829	147,236	221,172	57,710
TOTAL FUND BALANCE	$ 684,681	$ 751,961	$ 712,427	$ 893,133	$ 1,079,617

(a) For the fiscal year ended June 30, 2002 and subsequent fiscal years, the Commonwealth has adopted several new accounting and reporting standards described earlier in "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES – New Governmental Accounting and Reporting Standards." The new standards require numerous changes to how fund financial statements are presented. Certain funds have been reclassified and fund balances restated. See Note B to the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2002 for a more detailed explanation. These changes limit the comparability of that year's data and subsequent data to data for prior fiscal years.

(b) Beginning with the fiscal year ended June 30, 2002, the functional categories of expenditures have been revised. Additionally, beginning with the fiscal year ended June 30, 2004 a portion of the functional categories within expenditures (transportation and capital outlay) have been further revised. These changes limit the comparability of fiscal years' 2002, 2003 and 2004 data to data for prior fiscal years.

Source: Compiled from Office of the Budget, Comprehensive Annual Financial Report for fiscal years ended June 30, 2004, 2003, 2002, 2001 and 2000.

The following budgetary basis information is derived from the Commonwealth's unaudited budgetary basis financial statements.

Fiscal Year 2003 Financial Results

Budgetary Basis. The Motor License Fund ended the fiscal year with an unappropriated surplus of $30.4 million, a net decrease of $26.0 million during the fiscal year. Actual revenue collection was below estimate by $30.5 million, or 1.5 percent. Motor License Fund revenues collected during fiscal year 2003 totaled $1,998.8 million, an increase of 2.2 percent from the prior fiscal year. The slow-growing national economy impacted the rate of growth of the Motor License Fund as the liquid fuels tax, the largest revenue category of the Fund and license and fees revenue grew by 1.4 percent and 1.8 percent respectively from the prior year level. Other revenues to the Motor License Fund, principally earnings on investments, grew 28.5 percent from fiscal year 2002 totals. Expenditures, net of lapses, totaled $2,048.1 million, an increase of 0.3 percent over fiscal year 2002 expenditures.

Fiscal Year 2004 Financial Results

Budgetary Basis. Commonwealth revenues to the Motor License Fund totaled $2,085.7 million, an increase of 4.3 percent over actual fiscal year 2003 revenues. Liquid fuels taxes grew by less than 1 percent, while license and fee revenues grew by 1.7 percent. Other revenue receipts, namely earnings on investments, grew by $64.9 million or 101 percent from prior year receipts. The rate of growth in earning on investments was, in large part, the result of actions by the Commonwealth Treasurer to terminate a formerly separate pool of available Motor License Fund cash balances that have been invested in equity securities. By combing all Motor License Fund cash balances into one common investment pool, the Motor License Fund achieved approximately $20 million in previously unrealized capital gains. Expenditures, net of current year lapses, totaled $2,022.6 million. This amount represents a decrease of 1.2 percent from expenditures in fiscal year 2003. Revenues, including prior year lapses, in excess of expenditures for fiscal year 2004 contributed to the Motor License Fund ending the fiscal year with an unappropriated surplus of $113.6 million, an increase of $83.2 million or 274 percent from fiscal year 2003.

Fiscal Year 2005 Budget

Estimates of Commonwealth revenues to the Motor License Fund for fiscal year 2005 have been revised upwards by $11.2 million to $2,113 million, an increase of 1.3 percent over actual fiscal year 2004 revenues. Motor License Fund tax receipts are estimated to grow approximately 4.0 percent, while other revenue receipts, namely earnings on investments, are estimated to decline 28 percent. Contributing to the estimated decline in other revenue receipts is the large amount of one-time capital gains on investments of available Motor License Fund cash balances. See Motor License Fund "Fiscal Year 2004 Financial Results." Appropriations of Commonwealth Motor License Fund revenues total $2,082 million for fiscal year 2005, an increase of 2.9 percent from actual fiscal year 2004 expenditures net of lapses. The adopted fiscal year 2005 budget projects an increase of the unappropriated fiscal year ending balance of $31 million, bringing the cumulative unappropriated surplus to a projected $144.6 million following conclusion of the fiscal year 2005 budget.

Through April 2005, Commonwealth revenues in the Motor License Fund have totaled $84.5 million or 4.8 percent above the estimate for that period.

The achievement of the budgeted results may be adversely affected by a number of trends or events, including developments in the national and state economy or adverse developments in the price and availability of motor vehicle fuels.

Fiscal Year 2006 Proposed Budget

A budget proposing $2,249 million of appropriations from Commonwealth funds for fiscal year 2006 has been submitted to the General Assembly. The requested amount of appropriations represents an increase of 8 percent above the budget appropriated for fiscal year 2005. The proposed budget projects a draw down of approximately $55 million from the estimated fiscal year beginning balance.

The General Assembly is considering the Governor's budget proposal through debate on various bills, including the General Appropriation Bill, required to enact the proposed budget. The General Assembly may change, eliminate or add amounts and items to the proposed budget submitted by the Governor and there can be no assurance that the budget, as proposed by the Governor, will be enacted into law on June 30. See Appendix C for additional information on the budget enactment process.

State Lottery Fund

The Commonwealth operates a statewide lottery program that consists of various lottery games using computer sales terminals located throughout the state, and instant games using preprinted tickets. The net proceeds of all lottery game sales, less sales commissions and directly paid prizes, are deposited into the State Lottery Fund.

State Lottery Fund receipts support programs to financially assist elderly and handicapped individuals, primarily through property tax and rent rebate assistance and a pharmaceutical assistance program to recipients who meet specified income limits, and the provision of free mass transit rides during off-peak hours. Certain administrative costs and the payment to the General Fund of the personal income tax due on lottery prizes, which taxes and costs were previously paid from the State Lottery Fund, are now being paid by the General Fund, beginning in fiscal year 2000.

Financial Results for Recent Fiscal Periods (GAAP Basis)

State Lottery Fund cash and investments increased during the fiscal year ended June 30, 2004, due to an increase in gross ticket sales and an expansion in the Treasury Department securities lending program during the 2004 fiscal year. Revenue increased 11.6 percent, primarily due to an increase in instant ticket sales during the fiscal year. Expenditures and other uses from the State Lottery Fund increased 9 percent during the fiscal year, partly due to increased field paid prizes from instant ticket sales. The fiscal year 2004 statutory transfer from the State Lottery Fund for the payment of benefits to the elderly that the fund subsidizes amounted to $370 million, a decrease of $25 million over fiscal year 2003. Table 10 on the following page sets forth a condensed summary of revenues and expenditures (presented on a GAAP basis) for the State Lottery Fund for fiscal years 2000 through 2004.

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Table 10
Results of Operations–State Lottery Fund
GAAP Basis–Unaudited
(In Thousands)

	Fiscal Year Ended June 30				
	2000	**2001**	**2002(a)**	**2003**	**2004**
Fund Balance/Net Assets -					
Beginning of Period	$ 213,409	$ 242,987	$ 201,215	$ 180,921	$ 142,372
Restatements	-	-	173	-	-
Fund Balance/Net Assets -					
Beginning of Period, as Restated	$ 213,409	$ 242,987	$ 201,388	$ 180,921	$ 142,372
Revenues:					
Lottery revenues	1,695,371	1,788,333	1,932,692	2,100,096	2,350,892
Intergovernmental	57,057	67,758	-	-	-
Investment income	22,065	21,645	23,042	15,139	13,127
Other revenues	(128)	7,478	65,474	68,522	73,681
TOTAL REVENUES AND OTHER SOURCES	$ 1,774,365	$ 1,885,214	$ 2,021,208	$ 2,183,757	$ 2,437,700
Expenditures:					
Operating expenses (b)	$ 1,484,787	$ 1,636,986	$ 1,682,675	$ 1,827,306	$ 2,051,646
Other Uses:					
Operating transfers out	260,000	290,000	359,000	395,000	370,000
TOTAL EXPENDITURES AND OTHER USES	$ 1,744,787	$ 1,926,986	$ 2,041,675	$ 2,222,306	$ 2,421,646
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURE AND OTHER USES	29,578	(41,772)	(20,467)	(38,549)	16,054
Fund Balance/Net Assets - End of Period	$ 242,987	$ 201,215	$ 180,921	$ 142,372	$ 158,426
Components of Fund Balance/Net Assets					
Reserved for encumbrances	$ 1,290	$ 5	-	-	-
Reserved for long-term investments	-	-	-	-	-
Reserved for other	-	13	-	-	-
Unreserved - designated - other	264	264	-	-	-
Unreserved - undesignated (deficit)	241,433	200,933	$ 180,921	$ 142,372	$ 158,426
TOTAL FUND BALANCE/NET ASSETS	$ 242,987	$ 201,215	$ 180,921	$ 142,372	$ 158,426

(a) For the fiscal year ended June 30, 2002 and subsequent fiscal years, the Commonwealth has adopted several new accounting and reporting standards described earlier in "COMMONWEALTH FINANCIAL STRUCTURE AND PROCEDURES – New Governmental Accounting and Reporting Standards." The new standards require numerous changes to how fund financial statements are presented. The State Lottery Fund has been reclassified from the governmental fund category to the proprietary fund category. The change in fund category also produced a change in basis of accounting and required a restatement of beginning fund balance/net assets for the fund at June 30, 2001. See Note B to the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2002 for a more detailed explanation. These changes limit comparability of fiscal year 2002, 2003 and 2004 data to data reported for prior fiscal years.

(b) The reclassification of the State Lottery Fund to the proprietary fund category caused a change in reporting of all expenditures as operating expenses.

Source: Compiled from Office of the Budget, Comprehensive Annual Financial Report for fiscal years ended June 30, 2004, 2003, 2002, 2001and 2000.

The following budgetary basis information is derived from the Commonwealth's unaudited budgetary basis financial statements.

Fiscal Year 2003 Financial Results

Budgetary Basis. During fiscal year 2003, ticket sales less field prizes and commissions were $1,066.8 million, an increase of 6.4 percent over actual receipts in fiscal year 2002. Expenditures net of current year lapses totaled $1,140 million, an increase of 10.7 percent. Increased costs for the provision of pharmaceutical aid to eligible Pennsylvania seniors continued to be significant components of the increased level of expenditures. The excess of expenditures over fiscal year revenues was funded by a partial draw down of $63.4 million from the unappropriated surplus of the fund.

Fiscal Year 2004 Financial Results

Budgetary Basis. Lottery ticket sales rose 9.7 percent from fiscal year 2003 and provided net revenues of $1,170.5 million. Revenues from various lottery sources, including the state's participation in the multi-state Powerball game, were 1.6 percent below the budget estimate. Expenditures net of current year lapses totaled $1,139 million. Revenues, including prior year lapses, in excess of expenditures for fiscal year 2004 contributed to an unappropriated fund balance and reserve of $299.8 million (including $100 million of reserves), an increase of 20 percent from fiscal year 2003.

Fiscal Year 2005 Budget

The enacted fiscal year 2005 budget anticipates a 6.3 percent increase in revenues from lottery sources, including the state's participation in the multi-state Powerball game. Budgeted expenditures totaling $1,218 million are 6.9 percent above fiscal year 2004 expenditures. A continuation of revenues in excess of budgeted expenditures is projected to contribute to a fiscal year-end balance and reserve totaling $357.5 million (including $100 million of reserves), a projected increase of nearly 29 percent from fiscal year 2004.

The achievement of the budgeted results may be adversely affected by a number of factors, including failure of the marketing and game strategies to achieve the projected rise in revenues and increased competition from other forms of gaming that may be available to Pennsylvania lottery players.

Fiscal Year 2006 Proposed Budget

The Governor's proposed fiscal year 2006 budget anticipates a 5.9 percent increase in revenues from lottery sources, including instant ticket sales and the state's participation in the multi-state Powerball game. Appropriations totaling $1,294 million are recommended. The proposed fiscal year-end balance and reserve is projected to total $381.9 million, an increase of 9.5 percent.

Trend projections for fiscal years beyond fiscal year 2005 show estimated program and administrative costs above estimated net revenues. The estimated expenditures in excess of estimated revenues will be funded from a further draw-down of available reserves and balances in the State Lottery Fund. Based upon current projections, higher revenues and/or lower expenditures will be required for the State Lottery Fund to balance operations within a fiscal year.

The General Assembly is considering the Governor's budget proposal through debate on various bills, including the General Appropriation Bill, required to enact the proposed budget. The General Assembly may change, eliminate or add amounts and items to the proposed budget submitted by the Governor and there can be no assurance that the budget, as proposed by the Governor, will be enacted into law on June 30. See Appendix C for additional information on the budget enactment process.

COMMONWEALTH REVENUES AND EXPENDITURES

Recent Receipts and Forecasts

Table 11 on the following page presents the Commonwealth revenue receipts, including net revenues accrued but not deposited, on a budgetary basis, for the major operating funds of the Commonwealth as actually received for fiscal years 1999 through 2004 and as re-estimated for the fiscal year 2005 budget.

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Table 11
Commonwealth Revenues [a]
General Fund, Motor License Fund and State Lottery Fund - Unaudited
Fiscal Year 1999 – Fiscal Year 2004 and Fiscal Year 2005 Estimate
(In Millions)

	Fiscal Year Ended June 30						
	1999	2000	2001	2002	2003	2004	Estimate 2005
General Fund							
Tax Revenues:							
Sales and use	$ 6,605.8	$ 7,018.3	$ 7,203.8	$ 7,292.5	$ 7,519.6	$ 7,728.5	$ 8,001.3
Personal income	6,683.6	7,066.0	7,491.5	7,138.7	7,105.9	7,733.8	8,595.2
Corporate (b)	2,825.3	2,943.7	2,666.4	2,331.9	2,292.9	2,661.7	2,908.4
Public utility (c)	794.8	762.1	705.8	739.4	897.6	1,062.7	1,241.6
Inheritance	760.7	819.1	799.8	779.6	693.8	747.6	719.3
Financial and insurance (d)	455.2	475.9	481.3	516.9	545.0	608.3	623.9
Cigarette	275.8	272.4	269.3	266.8	826.7	856.4	804.0
Realty transfer	258.0	271.9	268.8	290.5	362.6	400.6	440.9
Alcoholic beverages (e)	170.5	179.6	187.6	197.4	219.9	221.4	232.1
Other	4.8	1.9	16.6	19.9	33.2	25.0	9.8
TOTAL TAX REVENUES	$ 18,834.5	$ 19,810.9	$ 20,090.9	$ 19,573.6	$ 20,497.2	$ 22,046.0	$ 23,576.5
Non-Tax Revenues:							
Liquor store profits	$ 50.0	$ 50.0	$ 50.0	$ 120.0	$ 155.0	$ 50.0	$ 54.9
Licenses, fees and miscellaneous	314.4	368.7	387.7	333.4	627.4	696.9	493.1
Fines, penalties and interest	27.9	27.1	33.1	32.6	34.9	35.1	32.9
TOTAL NON-TAX REVENUES	$ 392.3	$ 445.8	$ 470.8	$ 486.0	$ 817.3	$ 782.0	$ 580.9
TOTAL GENERAL FUND	$ 19,226.8	$ 20,256.7	$ 20,561.7	$ 20,059.6	$ 21,314.5	$ 22,828.0	$ 24,157.4
Motor License Fund							
Tax Revenues:							
Liquid fuels	$ 538.5	$ 556.9	$ 567.8	$ 578.5	$ 579.4	$ 587.1	$ 587.1
Fuels use	146.8	151.6	146.2	148.4	148.8	155.0	158.5
Oil company franchise	324.5	327.7	324.5	337.3	343.1	342.4	387.7
Motorbus & alt fuels	18.0	17.8	31.7	26.4	34.2	28.6	26.6
TOTAL TAX REVENUES	$ 1,027.8	$ 1,054.0	$ 1,070.2	$ 1,090.6	$ 1,105.5	$ 1,113.1	$ 1,159.9
Non-Tax Revenues:							
Licenses and fees	$ 755.4	$ 807.9	$ 795.4	$ 814.4	$ 828.8	$ 843.2	$ 852.3
Other and miscellaneous	94.7	97.5	86.3	50.2	64.5	129.4	100.9
TOTAL NON-TAX REVENUES	$ 850.1	$ 905.4	$ 881.7	$ 864.6	$ 893.3	$ 972.6	$ 953.2
TOTAL MOTOR LICENSE FUND	$ 1,877.9	$ 1,959.4	$ 1,951.9	$ 1,955.2	$ 1,998.8	$ 2,085.7	$ 2,113.1
State Lottery Fund							
Non-Tax Revenues:							
Lottery revenues	$ 899.7	$ 908.8	$ 916.1	$ 989.6	$ 1,057.0	$ 1,152.2	$ 1,219.7
Other and miscellaneous	26.4	20.5	11.7	12.9	9.8	18.3	24.9
TOTAL NON-TAX REVENUES	$ 926.1	$ 929.3	$ 927.8	$ 1,002.5	$ 1,066.8	$ 1,170.5	$ 1,244.6
TOTAL STATE LOTTERY FUND	$ 926.1	$ 929.3	$ 927.8	$ 1,002.5	$ 1,066.8	$ 1,170.5	$ 1,244.6

Source: Office of the Budget. Totals may not add due to rounding
(a) Budgetary basis including taxes and interest accrued but not deposited by the Commonwealth by June 30 of each fiscal year.
(b) Includes the corporate net income and the capital stock and franchise taxes.
(c) Includes the utility gross receipts and utility property taxes.
(d) Includes the financial institution and insurance premium taxes.
(e) Includes the liquor and malt beverage taxes.

Table 12 on the following page presents a comparison of the actual revenues on a budgetary basis to the official revenue estimate used for budget enactment for the General Fund and the Motor License Fund for fiscal years 2000 through 2004.

Table 12
Commonwealth Revenues — Official Estimate vs. Actual[(a)]
General Fund and Motor License Fund – Unaudited
Fiscal Year 2000 — Fiscal Year 2004
(In Millions)

	General Fund			Motor License Fund		
Fiscal Year Ended June 30	Official Estimate[(b)]	Actual	Variance	Official Estimate [(b)]	Actual	Variance
2000	$19,374.9	$20,256.7	$881.8	$1,884.0	$1,959.4	$75.4
2001	20,480.5	20,561.7	81.2	1,970.4	1,951.9	-18.5
2002	21,328.3	20,059.6	-1,268.7	1,955.8	1,955.2	-0.6
2003	21,812.1	21,314.5	-497.6	2,029.3	1,998.8	-30.5
2004	22,191.3	22,828.0	636.7	2,026.3	2,085.7	59.3

Source: Office of the Budget.

(a) Budgetary basis including taxes and interest accrued but not deposited by the Commonwealth by June 30 of each fiscal year.

(b) As certified for budget enactment.

Tax Revenues

Tax revenues constitute approximately 97 percent of Commonwealth revenues in the General Fund. The major tax sources for the General Fund of the Commonwealth are the sales tax, the personal income tax, the corporate net income tax, and the capital stock and franchise tax. Together these four taxes produce over 79 percent of General Fund tax revenues.

The major tax sources for the Motor License Fund are the liquid fuels taxes and the oil company franchise tax. Together these taxes produce over 53 percent of Motor License Fund revenues. Portions of certain taxes whose receipts are deposited into the Motor License Fund are legislatively restricted to specific transportation programs. These receipts are accounted for in restricted accounts in the Motor License Fund and are not included in the discussions of the tax revenues of the Motor License Fund.

The major tax sources for the General Fund and the Motor License Fund are described briefly below. The tax receipt amounts in the descriptions are on a budgetary basis.

Sales Tax. This tax accounted for $7,728.5 million or 33.9 percent of fiscal year 2004 General Fund Commonwealth revenues. The tax is levied at a rate of 6 percent on the sale, use, storage, rental or consumption of tangible personal property, cigarettes, and certain services, and upon the occupancy of hotel rooms. Substantial exemptions from the tax include clothing, food purchased in grocery stores or supermarkets, medical supplies, drugs, residential use of certain utilities, motor fuels, and machinery, equipment and items used in manufacturing, processing, farming or dairying, and utility service. The tax base was expanded in fiscal year 1992 to include a number of services not previously taxed. Beginning in fiscal year 1998, 1.22 percent of collections, up to an annual limit of $75 million, are transferred to a special fund for mass transit assistance. Beginning in fiscal year 2004, an additional 0.417 percent of receipts are transferred for transit assistance purposes.

Vendors collecting $600 or more in the previous year's third quarter are required to remit collections monthly within 20 days of the last day of the collection month.

Personal Income Tax. This tax accounted for $7,733.8 million or 33.9 percent of fiscal year 2004 General Fund Commonwealth revenues. The tax is levied at a flat rate on the taxable income of all residents and resident trusts and estates and taxable income attributable to Pennsylvania non-resident estates and trusts. The current tax rate of 3.07 percent became effective on January 1, 2004, having been raised from the prior rate of 2.8 percent, which was in effect since July 1, 1992. Credit against the tax is allowed for gross or net income taxes paid to other states by Pennsylvania residents.

Withholding is required by employers from all persons liable for the tax with the size of collections determining the frequency for remittance to the Commonwealth. A declaration and partial payment of the estimated tax is required for those individuals with taxable incomes over $8,000 per year, other than wages subject to withholding.

Individuals and families meeting qualifying income limits do not pay personal income tax on all or a portion of their taxable income with the exemptions depending on their total income. A qualifying family of four owes no personal income tax on taxable income up to $32,000 annually.

Corporate Net Income Tax. The Commonwealth received $1,677.9 million, or 7.4 percent of fiscal year 2004 General Fund Commonwealth revenues, from this tax. The tax is paid by all domestic and foreign corporations for the privilege of doing business, carrying on activities, or employing capital or property in Pennsylvania and is levied on federal net taxable income with Pennsylvania modifications. Building and loan associations, banks, savings institutions, trust companies, insurance and surety companies, Pennsylvania S corporations and non-profit corporations are exempt from the tax. When less than the entire business of any corporation is transacted within the Commonwealth, the taxable income in Pennsylvania is determined by an apportionment formula.

The current tax rate of 9.99 percent became effective for fiscal years beginning on or after January 1, 1995. The previous tax rate of 11.99 percent had been in effect since January 1, 1994.

The corporate net income tax is to be paid in four equal installments throughout the corporation's tax year based on estimated taxes due for the entire tax year. Any remaining portion of taxes due is to be paid with the corporation's annual report due three and one-half months following the end of the corporation's tax year.

Utility Gross Receipts Tax. This tax accounted for $1,012.4 million, or 4.4 percent of fiscal year 2004 General Fund Commonwealth revenues. The tax is levied on the gross receipts from business transacted within Pennsylvania by specified public utilities owned, operated or leased by corporations, associations or individuals. Public utilities owned or operated by a municipality or a municipal authority furnishing public utility services within the limits of the municipality are exempt from paying tax on the receipts arising from business done within the municipality. Beginning January 1, 2004, interstate and cellular telecommunications services are subject to the gross receipts tax. The tax rate is 50 mills, which became effective in July 1991, having been raised from its prior tax rate of 44 mills for all utilities except electric utilities, which are taxed at the rate of 44 mills. The tax rate for electric utilities is adjusted annually under provisions of a formula enacted with the deregulation of electric generation in Pennsylvania. Beginning with fiscal year 1999, 0.18 percent of receipts are transferred to a special fund for mass transit purposes. Revenue from 0.2 mills of the tax is deposited in the Alternative Fuels Incentive Grant Fund.

All firms, except public utilities owned or operated by a municipality or a municipal authority and motor transportation companies, are required to file estimated revenue reports annually, together with the tentative payment of the current year's tax calculated by applying the current tax rate to 90 percent of the tax base for the preceding year. Effective for tax years effective after January 1, 2000, natural gas companies became exempt from the tax. The tax report and tentative payment are required to be made by March 15. The remaining tax is due and payable by the succeeding March 15.

Capital Stock and Franchise Taxes. These taxes generated $984.3 million for the Commonwealth in fiscal year 2004, or 4.3 percent of General Fund Commonwealth revenues. They are levied on the capital stock value of domestic and foreign corporations doing business or having property or capital employed in Pennsylvania on that portion of capital stock value apportionable to Pennsylvania under a statutory formula.

Capital stock and franchise tax tentative payments are payable quarterly based on 90 percent of the tax liability of the year preceding the immediate prior year. Under current law, the General Fund tax rate for tax years that began in 2004 is 6.99 mills, having been reduced from 7.24 mills effective January 1, 2004. This tax is scheduled to be phased out by annual rate reductions through 2010 under legislation enacted in 2002 and amended in 2003.

Collection of certain prior fiscal year revenues under the capital stock and franchise taxes is the subject of litigation. See "LITIGATION - *PPG Industries, Inc. v. Commonwealth of Pennsylvania.*"

Cigarette Tax. Collections of this tax totaled $856.4 million in fiscal year 2004, or 3.8 percent of General Fund Commonwealth revenues. The tax is imposed and assessed on the sale or possession of cigarettes within the Commonwealth. It is levied on the consumer but is collected by the sale of stamps and meter units to dealers who affix them to each package. The current rate is $1.35 per package of 20 cigarettes, which was increased by 31 cents in 2002 and further increased by 35 cents effective in 2004. The 6 percent sales tax is also imposed on the retail sale of cigarettes. A portion of the collections from the tax are transferred to a special fund for children and to a special fund for preserving farmland. Additionally, an amount approximately equal to 25 cents per pack is transferred to the Healthcare Provider Retention Account.

Inheritance and Estate Taxes. Collections of these taxes were $747.6 million in fiscal year 2004, or 3.3 percent of General Fund Commonwealth revenues. The inheritance tax is levied on the value of property transferred to heirs of a deceased person. Prior to July 1, 2000, the tax rate was 6 percent of the value, if passing to lineal heirs, and 15 percent if passing to collateral heirs. Effective July 1, 2000, the tax rate on transfers to parents, grandparents and lineal descendents was lowered to 4.5 percent and a new tax rate of 12 percent on transfers to siblings was established. The estate tax is a "pick-up" tax in the amount of the maximum federal tax credit less State death taxes paid. Counties collect the inheritance and estate tax, which is due within nine months following the death of the person whose property is being transferred.

Insurance Premiums Tax. This tax is levied at the rate of 2 percent of the gross premiums (subject to retaliatory provisions) on all business of domestic and foreign insurance companies transacted within the Commonwealth during each calendar year. Revenues from the two percent tax on foreign fire and casualty companies accrues to special revenue funds while the remaining taxes accrue to the General Fund. The tax on foreign companies is based on the amount of business transacted in Pennsylvania. Marine insurance companies, both domestic and foreign, pay a 5 percent tax on underwriting profits attributable to Pennsylvania in lieu of the gross premium tax.

A 90 percent tentative payment is required for insurance companies, except foreign fire and casualty companies, calculated on the tax base of the preceding tax year. As an alternative, the taxpayer may elect to make a tentative payment in an amount not less than 90 percent of the tax as finally reported. Payments must be submitted by March 15 of each year while the remaining amount due must be paid by April 15 of the following year.

Realty Transfer Tax. This tax is levied at the rate of 1 percent of the value of the real property transferred, as represented by deed, instrument or other writing. The tax is collected by the recorders of deeds in the counties and transmitted to the Commonwealth when collected. From July 1994 through December 2001 fifteen percent of the revenues from this tax was transferred to the Keystone Recreation, Park and Conservation Fund, and the remaining portion was deposited in the General Fund. For the period from January 2002 through June 2002 the transfer amount was reduced to 10 percent and from July 2002 to June 2003 the transfer was reduced to seven and one-half percent. Effective July 2003 the transfer is fifteen percent.

Liquor Tax. This tax is levied at the rate of 18 percent of the net purchase price on all liquor sold by the Pennsylvania Liquor Control Board. Revenues from this tax accrue to the General Fund. The 6 percent sales tax is also imposed on all liquor sold by the Pennsylvania Liquor Control Board and is included in the sales tax receipts.

Financial Institution Taxes. The bank shares tax is levied at the rate of 1.25 percent of the value of shares of state and national banks and title insurance companies. Each institution computes the tax base by averaging the share value, adjusted to exclude the value of United States obligations, for each quarter of the previous calendar year. A payment of the tax for the current tax year is due by March 15 of that year. Revenues of this tax are deposited into the General Fund.

The mutual thrift institutions tax is levied on the taxable net income of such institutions at the rate of 11.5 percent. Revenues of this tax accrue to the General Fund. Annually, the mutual thrift institutions are required to transmit tentative reports together with a tentative payment of the current year's tax computed by applying the current tax rate to 90 percent of the tax base for the second preceding tax year. The taxpayer may elect to make a tentative payment at an amount not less than 90 percent of the tax as finally reported. Tentative reports and prepayments are due by March 15 of the current calendar year, with the remaining amount payable by April 15 of the next year.

Public Utility Realty Tax. The tax is levied on the state taxable value of utility real property belonging to a firm or other entity (i) furnishing utility service and (ii) regulated by the Pennsylvania Public Utility Commission or similar regulatory body. State taxable value is the current market value derived from assessed values for county real estate tax purposes. Certain items are specifically exempt from the tax. The tax rate for the General Fund portion of the tax is set annually by the Secretary of Revenue. The tax rate is to be set at a rate intended to produce revenues sufficient to reimburse local taxing authorities for foregone property tax. Revenues from an additional 7.6 mill tax are deposited into a special revenue fund.

The tax is subject to a tentative payment of the then current year's tax liability. The tentative reports and tax payments are due in May. The remaining tax payments must be paid in September.

Malt Beverage Tax. This tax is levied on all malt or brewed beverages sold in Pennsylvania. The tax rate is $^2/_3$ cent per half-pint, 1 cent per pint and $2.48 per barrel. The various manufacturers pay the tax monthly to the Department of Revenue. Revenues from this tax are deposited into the General Fund.

Liquid Fuels Tax. This tax accounted for $587.1 million, or 28.2 percent of Motor License Fund Commonwealth revenues in fiscal year 2004. It is an excise tax imposed upon all liquid fuels used or sold within the Commonwealth. The tax is imposed upon and collected by the fuel distributor. After discounts, all monies collected are deposited in the Motor License Fund, except that an amount equal to one-half cent per gallon is deposited in the Liquid Fuels Tax Fund. Fuels sold and delivered to the U.S. government, the Commonwealth and any of its political subdivisions, public authorities, non-profit schools, volunteer fire companies, ambulance services, rescue squads, and fuels sold and delivered in interstate commerce, are exempt from payment of the tax. In addition to these exemptions, reimbursement is made for fuels used for certain agricultural purposes. The present rate of the liquid fuels tax is 12 cents per gallon.

Oil Company Franchise Tax. This tax accounted for $342.4 million, or 16.4 percent of fiscal year 2004 Motor License Fund Commonwealth revenues. The tax is levied on the privilege of selling petroleum products subject to liquid fuels taxes for transportation purposes at the rate of 153.5 mills upon each dollar of such revenues. The tax rate was increased by 38.5 mills in May 1997 to its current rate. By law, portions of the tax are dedicated to certain highway purposes, including transfers to local governments for roads and highways. Exemptions from the tax are the same as those provided from the liquid fuels tax.

Fuels Tax. This tax accounted for $154.9 million, or 7.4 percent of fiscal year 2004 Motor License Fund Commonwealth revenues. It is an excise tax imposed on fuels (primarily diesel fuel) used or sold within the Commonwealth. The tax is imposed upon and collected by the distributor. After discounts, all monies collected are deposited in the Motor License Fund, except an amount equal to one-half cent per gallon placed in the Liquid Fuels Tax Fund for distribution to local governments. The present tax rate is 12 cents per gallon for fuel used in the Commonwealth.

Fuels exempt from this tax are those delivered in interstate commerce, those used by and sold to the Commonwealth and any of its political subdivisions, those sold and delivered to the U.S. government, those (less than 50 gallons) brought into the Commonwealth in the fuel tanks of motor vehicles, those used by public authorities, volunteer fire companies, ambulance services, rescue squads and non-profit schools, and those used for certain agricultural purposes.

Motor Carriers Road Tax. This tax is levied on motor carrier vehicles having a gross weight in excess of 26,000 pounds. All monies collected are deposited in the Motor License Fund. The current rate is 12 cents per gallon, plus an additional factor based on the oil company franchise tax for fuel used within the Commonwealth. In May 1997 the tax rate was reduced by 6 cents to its current level. The revenue lost from the tax reduction is being covered by an additional 55 mills tax rate for the oil company franchise tax. Both the repealed and the new tax portions are dedicated to bridge improvement.

Non-Tax Revenues

Licenses and Fees. License and fee receipts in the General Fund for fiscal year 2004 totaled $105.2 million representing 0.5 percent of Commonwealth revenues to the General Fund. A general increase in various General Fund fees was enacted in December 2003 and effective beginning in January 2004. Revenues from motor vehicle licenses and fees in fiscal 2004 were $843.2 million, representing 40.4 percent of total fiscal year 2004 Motor License Fund Commonwealth revenues. A general increase in various fees and licenses was enacted in April 1997 and effective beginning with the 1998 fiscal year.

Miscellaneous Revenue. Revenues from non-tax sources not categorized elsewhere are credited to miscellaneous revenues. Interest earnings on securities and deposits are included in this source.

State Stores Fund Transfers. This is an amount determined by the Liquor Control Board to be available for transfer to the General Fund. The amount transferred for fiscal year 2004 was $50.0 million. In Pennsylvania, the distribution and sale of liquor is a state enterprise.

Fines, Penalties and Interest. This revenue source includes all fines, penalties and interest collected in the enforcement of tax regulations. The amount deposited to the General Fund for fiscal year 2004 was $35.1 million. The largest portion is from corporation tax penalties.

Tobacco Settlement Payments. The Commonwealth's portion of payments made by cigarette manufacturers participating in the Tobacco MSA are deposited in the Tobacco Settlement Fund to be used for certain health-related programs. See "COMMONWEALTH FINANCAL STRUCTURE AND PROCEDURES – Description of Funds."

Federal Revenues

Receipts by the Commonwealth in its General Fund, Motor License Fund and State Lottery Fund from the federal government during fiscal year 2005 totaled $17.6 billion. Approximately $11.7 billion, or 66 percent of total federal revenue to the Commonwealth for fiscal year 2005, is attributable to public health and welfare programs, the largest of which are for the medical assistance and temporary assistance to needy families programs.

For fiscal year 2006, funds expected to be received from the federal government in the General Fund, the Motor License Fund and the State Lottery Fund are estimated to be $16.8 billion.

Major Commonwealth Expenditures

The Commonwealth's major operating funds—the General Fund, the Motor License Fund and the State Lottery Fund—provide financial resources to operate programs and fund grants. Trends in expenditures from those funds for various program areas are discussed below based on budgetary basis financial statements for fiscal year 2004, the enacted fiscal year 2005 budget, and the proposed budget for fiscal year 2006.

Education

In fiscal year 2004, expenditures from Commonwealth revenues for education purposes were just over $9.1 billion. The enacted budget for fiscal year 2005 includes over $9.8 billion in education funding, an increase of over 7 percent over fiscal year 2004. The proposed budget for fiscal year 2006 includes over $10.06 billion in education funding.

Elementary and Secondary Education. The financing of public elementary and secondary education in Pennsylvania is shared by the Commonwealth and local school districts. There are 501 local school districts in the state. With certain exceptions, each is governed by a locally elected school board responsible for the administration of the public schools in the school district with the authority to levy taxes within the limits prescribed by the Public School Code of 1949, as amended. Funds supplied by the Commonwealth supplement the funds raised locally. Local school districts receive various subsidy payments for basic instruction, vocational education, debt service, pupil transportation, employee retirement programs including social security, and various special education programs from the Commonwealth. The largest such subsidy is the Basic Education Funding subsidy. The enacted budget for fiscal year 2005 increases Basic Education Funding by over $150 million, or 3.5 percent, to over $4.36 billion. The increase includes a base supplement based on school district enrollment and relative wealth, a small district assistance component, an enrollment growth supplement and a supplement based upon school district personal income and relative wealth and a supplement based upon enrollment and relative local taxing effort. For fiscal year 2005, every school district is guaranteed a 2 percent increase over its fiscal year 2004 total allocation. The recommended budget for fiscal year 2006 includes $4,470 billion, or a $109.03 million or 2.5 percent, increase over fiscal year 2005.

Certain specialized education programs are operated and administered in Pennsylvania by 29 intermediate units established by the component local school districts. These intermediate units are funded from annual General Fund appropriations and contributions from member school districts. Programs operated by intermediate units generally are special education programs for the gifted, for individuals with mental and physical disabilities, and for support of nonpublic schools through the provision of auxiliary services and the lending of instructional materials such as textbooks to children attending nonpublic schools in Pennsylvania.

Total Commonwealth expenditures for basic education programs in fiscal year 2004 were over $7.25 billion, representing 79.1 percent of all Commonwealth expenditures for education in fiscal year 2004. The enacted budget for fiscal year 2005 includes over $7.8 billion for basic education programs. The recommended budget for fiscal year 2006 includes just over $8.05 billion for basic education programs.

Table 13
Fall Enrollment in Pennsylvania Public and Non-Public Elementary Schools and Secondary Schools School Years 2000-2004
(In Thousands)

	School Year Ended June				
	2000	**2001**	**2002**	**2003**	**2004**
Elementary Schools					
Public	977	967	960	942	933
Nonpublic	245	242	236	229	220
Secondary Schools					
Public	840	847	862	874	888
Nonpublic	85	85	85	84	83
Total					
Public	1,817	1,814	1,822	1,816	1,821
Nonpublic	330	327	321	313	303
Total	2,147	2,141	2,143	2,129	2,124

Source: Pennsylvania Department of Education.

Philadelphia School District. The Secretary of Education of the Commonwealth, under the provisions of the Commonwealth's Public School Code (the "School Code"), declared the Philadelphia School District as distressed effective December 22, 2001. During the period of distress covered by that declaration all powers and duties of the Philadelphia School District Board of Education granted under the School Code or any other law are suspended and all such powers and duties are vested in a school reform commission. Currently, the school reform commission statutorily consists of five members, four appointed by the Governor and one appointed by the Mayor of the City of Philadelphia. The school reform commission's objectives are to improve the levels of academic achievement and achieve financial stability within the school district. Termination of the declaration of distress by the Secretary of Education of the Commonwealth may be made only upon the recommendation of a majority of the members of the school reform commission. Upon termination of the declaration of distress the Philadelphia School District Board of Education will resume the exercise of its powers.

The fiscal year 2005 enacted budget included an additional $25 million of appropriations for the Philadelphia School District. The fiscal year 2006 recommended budget also includes a $25 million appropriation for the Philadelphia School District.

Higher Education. Higher education in Pennsylvania is provided through 267 degree-granting institutions, which include the fourteen universities of the State System of Higher Education ("SSHE"), four State-related universities, community colleges, independent colleges/universities and specialized degree-granting institutions. SSHE, created in 1982 from the fourteen state-owned colleges, is administered by a Board of Governors whose members are appointed by the Governor and confirmed by the Senate. Over $1.81 billion was expended by the Commonwealth in the 2004 fiscal year for these institutions and for student financial assistance. The enacted budget for fiscal year 2005 includes over $1.88 billion. The Governor's proposed budget for fiscal year 2006 includes over $1.91 billion for higher education.

Table 14
Full-Time Equivalent Enrollment at State-Supported Institutions of Higher Education
School Years 2001-2005
(In Thousands)

	School Year Ended June				
	2001	**2002**	**2003**	**2004**	**2005**
State System of Higher Education.	90	94	96	95	96
State-Related Universities	133	137	140	141	142
Community Colleges	67	75	81	87	92
State-Aided Institutions	38	39	40	42	43
Total	328	345	357	365	373

Source: Governor's Executive Budget, various years.

Public Health and Human Services

The Commonwealth provides temporary support for its residents who are seeking to achieve and sustain independence. It also provides care, treatment and rehabilitation to persons with mental and physical disabilities and supports programs to prevent or reduce social, mental and physical disease and disabilities. In addition, it plans for and coordinates all the health resources within Pennsylvania. Services are provided directly through administration of programs and services, and indirectly through programs of standard setting, regulation, supervision, licensing, grants, subsidies and purchases of services.

Fiscal year 2004 public health and human services expenditures were $21.3 billion and are projected to be $23.6 billion for fiscal year 2005. For fiscal year 2006, $23.7 billion is proposed for these purposes. Of the fiscal year 2005 expenditures, $8.2 billion will be funded from the General Fund, while $8.7 billion is estimated to be provided from the General Fund for fiscal year 2006. Federal funds are expected to decrease by $357.9 million, and augmentations are expected to decrease by $73 million for fiscal year 2006. The fiscal year 2006 budget also includes $367.4 million of receipts from the Tobacco Settlement Fund that will be expended for health care. Federal funds matching the additional state Tobacco MSA funds are included in the decrease noted above. Public health and human service programs are the largest single component of combined state and federal spending in the Commonwealth's operating budget. The overall budget increase reflects caseload increases as well as higher costs to provide support for former welfare clients obtaining work, federal mandates, litigation and continued support of county operated programs for child welfare, mental health and mental retardation.

Programs providing temporary financial assistance and medical assistance comprise the largest portion of public health and human services expenditures. General Fund expenditures for these assistance programs by the Commonwealth amounted to $4.7 billion in fiscal year 2004, while $4.7 billion is budgeted from the General Fund for fiscal year 2005 and $5.0 billion is proposed for fiscal year 2006. The fiscal year 2005 budget provides for use of approximately $24 million in additional intergovernmental transfer funds to offset General Fund requirements and $300 million is proposed for the fiscal year 2006 budget for expected program cost increases. A nursing home assessment fee is expected to provide a General Fund offset of $267.3 million in fiscal year 2005 and $145.0 million in fiscal year 2006. In addition, a managed care organization assessment is anticipated to provide a General Fund offset of $174.9 million in fiscal year 2005 and $214.2 million in fiscal year 2006. Approximately 37 percent of the total cost of assistance to the economically needy is supported by Commonwealth funds appropriated from the General Fund. The balance is provided from reimbursements by the federal government and through various program collection activities conducted by the Commonwealth.

Medical assistance continues to be a rapidly growing component of public health and human services expenditures. Despite implementation of Commonwealth initiatives to restrain costs, the program continues to grow due to an expanding caseload, technology improvements and general medical inflation. Expenditures for medical assistance increased during the period from fiscal years 1994 through 2004 by an average annual rate of 8.6 percent. Fiscal year 2005 expenditures from Commonwealth funds are projected to be $4.2 billion and the proposed budget for fiscal year 2006 is $4.5 billion for medical assistance, an increase of 7.3 percent over the previous fiscal year. The increase reflects normal inflationary increases and is deflated by proposed cost containment initiatives anticipated to reduce General Fund expenditures by $383.4 million in fiscal year 2006. The Commonwealth has experienced the rise in medical and pharmaceutical costs that has been occurring nationwide. This increase is particularly evident in the rates requested by managed care providers and in services for children. Income maintenance cash assistance payments to families in transition to independence are projected to be $985.3 million for fiscal year 2005, of which $381.7 million is from the General Fund. The proposed budget for fiscal year 2006 includes a total of $958.5 million, with $377.3 million provided from the General Fund. The $26.7 million decrease results primarily from a $25.1 million reduction in one-time Federal storm disaster funding. Cash assistance is time-limited and requires participation in work activities to maintain eligibility. To support a client's finding and retaining employment, small grants are available to clients to overcome employment obstacles such as child care, transportation, vision and hearing difficulties, and other such barriers. In fiscal year 2005 and the future, increased costs are expected to be incurred in training and support for the most hard to place clients. These increased costs will include some state-only payments for clients who are working the required amount but still require assistance to complete training.

Transportation

The Commonwealth is responsible for the construction, restoration and maintenance of the highways and bridges in the 40,000 mile state highway system, including certain city streets that are a part of the state highway system. Assistance for the maintenance and construction of local roads and bridges is provided to municipalities through grants of financial aid. Highway maintenance costs, construction costs and assistance grants are paid from the Motor License Fund. The General Fund, the State Lottery Fund and other special funds, including the Public Transportation Assistance Fund, the Liquid Fuels Tax Fund, the Highway Beautification Fund and the Motor Vehicle Transaction Recovery Fund provide the remainder of funding for transportation programs.

In addition to its unrestricted state funds, the Motor License Fund includes five restricted revenue accounts funded by specific state revenues legislatively dedicated to specific purposes. Some of the restricted purposes funded from these accounts also receive funding by annual appropriations of unrestricted Motor License Fund revenues. Programs receiving funds from a restricted account include highway bridges, highway construction and maintenance, grants to municipalities for highways and bridges, and airport development.

In addition to its support of the highway system, the Commonwealth provides subsidies for mass transit systems including passenger rail and bus service. The Commonwealth assists local mass transit systems through grants and payment for free rides by senior citizens during non-peak hours. In addition, transit operators receive payments for providing senior citizen transportation service on a shared-ride basis generally in areas where fixed route service is not available. A total of $485.1 million in Commonwealth revenues was expended from the General Fund and the State Lottery Fund for such purposes in fiscal year 2004, and $500.5 million is available for fiscal year 2005. A total of $497.9 million is the proposed budget for fiscal year 2006. Beginning with fiscal year 1998, 1.22 percent of sales and use tax collections in the General Fund, up to an annual limit of $75 million, is transferred to a separate account and used to pay mass transportation operating grants to local mass transit systems.

In 1991, the Public Transportation Assistance Fund was created with dedicated sources of funding for mass transit systems. Funds totaling $174.7 million were expended from this fund in fiscal year 2004, and $193.0 million is budgeted for fiscal year 2005. A total of $174.4 million is the proposed budget for fiscal year 2006.

Liquid fuels tax and license and fee increases enacted in 1997 are providing resources for a substantial expansion of expenditures for highway construction and maintenance. Major portions of the revenues generated by these recent increases were restricted to certain transportation purposes. Motor License Fund restricted revenues budgeted for highway construction purposes totaled $528.7 million in fiscal year 2004, and $581.2 million is available for fiscal year 2005. A total of $594.2 million is the proposed budget for fiscal year 2006. Combined Motor License

Fund and restricted revenues expended for highway maintenance in fiscal year 2004 was $1,114.6 million, and $1,192.7 million is budgeted for fiscal year 2005. A total of $1,318.2 million is the proposed budget for fiscal year 2006. Support of highway and bridge expenditures by local governments through grants paid from Motor License Fund and restricted revenues were $276.2 million in fiscal year 2004, and $303.8 million is available for fiscal year 2005. A total of $313.5 million is the proposed budget for fiscal year 2006.

The Commonwealth's current aviation program funds the development of public airport facilities through a grant program providing for airport development, runway rehabilitation, and real estate tax rebates for public use airports. Taxes levied on aviation and jet fuel provide revenues for a restricted account for aviation programs in the Motor License Fund. In fiscal year 2004, $17.2 million was expended from the aviation restricted account for such purposes and $8.3 million is available for fiscal year 2005. A total of $7.3 million is the proposed budget for fiscal year 2006.

The Commonwealth is not responsible for the toll roads and bridges in Pennsylvania. These are under the jurisdiction of various authorities and commissions. See "GOVERNMENT AUTHORITIES AND OTHER ORGANIZATIONS."

OUTSTANDING INDEBTEDNESS OF THE COMMONWEALTH

General

The Constitution permits the Commonwealth to incur the following types of debt: (i) debt to suppress insurrection or rehabilitate areas affected by disaster, (ii) electorate approved debt, (iii) debt for capital projects subject to an aggregate debt limit of 1.75 times the annual average tax revenues of the preceding five fiscal years, and (iv) tax anticipation notes payable in the fiscal year of issuance. All debt except tax anticipation notes must be amortized in substantial and regular amounts. See Appendix E for the text of selected constitutional provisions relating to the finances of the Commonwealth.

Debt service on Commonwealth general obligation debt is paid from appropriations out of the General Fund except for debt issued for highway purposes, which is paid from Motor License Fund appropriations.

Table 15
General Obligation Debt Outstanding[a]
Fiscal Years 1995-2004
(In Millions)

June 30	General Obligation Debt Outstanding
1995	$5,045.4
1996	5,056.1
1997	4,795.1
1998	4,724.5
1999	4,921.5
2000	5,014.9
2001	5,416.2
2002	6,059.3
2003	6,767.2
2004	6,892.6

[a] Net of sinking fund balances for all debt.

Net outstanding general obligation debt totaled $6,892.6 million at June 30, 2004, a net increase of $125.4 million from June 30, 2003. Over the 10-year period ended June 30, 2004, total net outstanding general obligation debt increased at an annual rate of 3.1 percent. Within the most recent 5-year period, outstanding general obligation debt has increased at an annual rate of 7.0 percent.

General obligation debt for non-highway purposes of $6,704.6 million was outstanding on June 30, 2004. Outstanding debt for these purposes increased by a net $169.3 million since June 30, 2003. For the period ended June 30, 2004, the 10-year and 5-year average annual compound growth rate for total outstanding debt for non-highway purposes has been 5.3 percent and 8.8 percent respectively. In its current debt financing plan, Commonwealth infrastructure investment projects include improvement and rehabilitation of existing capital facilities and construction of new facilities, such as public buildings, prisons and parks, transit facilities, economic development and community facilities, and other local public buildings.

Outstanding general obligation debt for highway purposes was $188.0 million on June 30, 2004, a decrease of $43.9 million from June 30, 2003. Highway outstanding debt has declined over the most recent 10-year and 5-year periods ended June 30, 2004, by the annual average rates of 16.0 percent and 18.8 percent respectively. The decline in outstanding highway debt is due to the policy begun in 1980 of funding highway capital projects with current revenues except for very limited exceptions. No debt issuance for highway capital projects is currently planned.

Table 16 on the following page shows selected debt ratios for the Commonwealth for fiscal year 1994 and for fiscal years 2000 through 2004. Table 16 contains corrections to certain prior fiscal year data as well as a revision in the methodology to account for debt service payments to include funding from all sources rather than debt service as paid from appropriations (resulting in some information in Table 16 being different from that appearing in previous official statements of the Commonwealth).

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Table 16
Selected Debt Ratios
Fiscal Years 1994 and 2000 to 2004

		1994		2000		2001		2002		2003		2004
				Fiscal Year Ended June 30								
Net Outstanding Debt (Millions)												
General Obligation Debt(a)	$	5,076	$	5,015	$	5,416	$	6,059	$	6,767	$	6,893
Lease Payment Obligations(b)		977		684		651		687		648		114
Total	$	6,053	$	5,699	$	6,067	$	6,746	$	7,415	$	7,007
% Increase (Decrease) over prior year		1.8%		0.9%		6.5%		11.2%		9.9%		-5.5%
Population (Thousands)		12,042		12,285		12,298		12,328		12,365		12,365
Per Capita Debt	$	503	$	464	$	493	$	547	$	600	$	567
Personal Income (Millions)	$	275,336	$	365,626	$	378,350	$	391,354	$	395,669	$	395,669
Debt as a % of Personal Income		2.2%		1.6%		1.6%		1.7%		1.9%		1.8%
Debt Service (Millions)[c]												
Highway Bonds(d)	$	214	$	128	$	121	$	84	$	62	$	28
All Other Bonds(e)		503		613		636		676		701		769
Lease Payments		60		80		74		70		73		12
Total	$	777	$	821	$	831	$	830	$	836	$	809
Increase (Decrease) Over Prior Year		3.8%		4.7%		1.2%		(0.1%)		0.7%		(3.2%)
Cash Revenues (Million)[f]												
Motor License Fund	$	1,503	$	1,959	$	1,952	$	1,955	$	1,999	$	2,086
General Fund		15,211		20,257		20,562		20,059		21,315		22,828
Total	$	16,714	$	22,216	$	22,514	$	22,014	$	23,314	$	24,914
% Increase (Decrease) over prior year		3.4%		5.2%		1.3%		(2.2%)		5.9%		6.9%
Highway Bond Debt Service as a % of Motor License Fund Revenues		14.2%		6.5%		6.2%		4.3%		3.1%		1.3%
All Other Bond Debt Service and Lease Payments as a % of General Fund Revenues		3.7%		3.4%		3.5%		3.7%		3.6%		3.4%
Total Debt Service and Lease Payments as a % of Motor License and General Fund Revenues		4.7%		3.7%		3.7%		3.8%		3.6%		3.3%

(a) Net of all sinking fund balances. Includes bond anticipation notes.
(b) Includes unduplicated data of issues contained in Table 18.
(c) As paid from appropriations, available funds and/or sinking fund balances.
(d) Highway Bonds, interest portion of Advance Construction Bonds, Highway Public Improvement Bonds, State Highway and Bridge Authority Bonds, General Authority Rentals, and Highway Bridge Improvement Bonds.
(e) Fiscal year 2000 excludes additional amounts appropriated but not used to pay debt service in those years. Fiscal year 2002 decline due to use of available balance in lieu of appropriations.
(f) Commonwealth revenues only.

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General Obligation Debt Outstanding

As of June 30, 2004, the Commonwealth had the following amount of general obligation debt outstanding:

Table 17
General Obligation Debt Outstanding as of June 30, 2004[a]
(In Thousands)

	Debt Outstanding[b]	Less: Refunding Escrow[c]	Less: Sinking Fund[d]	Net Debt Outstanding
Capital Projects Debt:				
Capital Facilities Bonds	$ 5,158,035	$ (361,090)	$ (60,852)	$ 4,736,093
Highway Bonds	-	-	-	-
Refunding Bonds	1,518,885	-	-	1,518,885
Total Capital Projects Debt Outstanding	$ 6,676,920	$ (361,090)	$ (60,852)	$ 6,254,978
Electorate Approved Debt:				
PA Economic Revitalization Bonds	$ 4,710	$ (500)	$ (3)	$ 4,207
Land & Water Development Bonds	1,755	-	(36)	1,719
Nursing Home Loan Development Bonds	-	-	-	-
Volunteer Companies' Loan Bonds	7,790	(1,130)	-	6,660
Vietnam Veterans Compensation Bonds	-	-	-	-
Water Facilities Restoration-1981 Referendum	30,200	(10,185)	-	20,015
Pennvest—1988 Referendum Bonds	42,920	(10,350)	-	32,570
Pennvest—1992 Referendum Bonds	38,555	(17,085)	....	21,470
Agricultural Conservation Easement Bonds	20,070	(405)	-	19,665
Local Criminal Justice Bonds	28,725	(12,245)	-	16,480
Keystone Recreation, Parks & Conservation Bonds	30,295	(16,205)	-	14,090
Total Electorate Approved Debt Outstanding	$ 205,020	$ (68,105)	$ (39)	$ 136,876
Other Bonded Debt:				
Disaster Relief Bonds	$ 20,115	(8,095)	-	$ 12,020
Refunding Bonds	488,679	....	-	488,679
Total Other Bonded Debt Outstanding	$ 508,794	$ (8,095)	-	$ 500,699
Total General Obligation Debt Outstanding	$ 7,390,734	$ (437,290)	$ (60,891)	$ 6,892,553

(a) Subsequent to June 30, 2004, the Commonwealth has issued $201 million of new bonds and $1,469.255 million of advance refunding bonds.
(b) Accreted value of capital appreciation bonds included.
(c) Principal amount of bonds refunded to be paid from State Treasurer escrow account.
(d) Balance in sinking fund.

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Debt service payable during each fiscal year on outstanding general obligation debt, net of refunding escrow amounts, as of June 30, 2004, for the years shown is as follows:

Table 18
Bond Debt Service
(In Thousands)

Fiscal Year Ending June 30	Principal	Interest	Total
2005	$ 478,112	$ 338,877	$ 816,989
2006	505,635	326,779	832,413
2007	503,423	295,994	799,417
2008	498,132	270,420	768,552
2009	497,210	245,031	742,241
2010	490,925	215,426	706,351
2011	495,365	189,482	684,847
2012	489,970	163,961	653,931
2013	462,505	139,537	602,042
2014	408,980	116,168	525,148
2015	344,615	95,753	440,368
2016	302,480	79,287	381,767
2017	267,500	66,187	333,687
2018	254,300	53,350	307,650
2019	237,230	41,596	278,826
2020	199,555	31,355	230,910
2021	176,480	22,341	198,821
2022	154,920	14,014	168,934
2023	93,590	6,871	100,461
2024	61,225	2,521	63,746
Grand Total	$ 6,922,151	$ 2,714,951	$ 9,637,102

Totals may not add due to rounding.

Nature of Commonwealth Debt

Capital Projects Debt. The Commonwealth may incur debt to fund capital projects for community colleges, highways, public improvements, transportation assistance, flood control, and redevelopment assistance. Before a project may be funded, it must be itemized in a capital budget bill adopted by the General Assembly. An annual capital budget bill states the maximum amount of debt for capital projects that may be incurred during the current fiscal year for projects authorized in the current or previous years' capital budget bills. Capital projects debt is subject to a constitutional limit on debt.

Once capital projects debt has been authorized by the necessary legislation, issuance authority rests with two of the Issuing Officials (the Governor, the State Treasurer and the Auditor General), one of whom must be the Governor.

Electorate Approved Debt. The issuance of electorate approved debt is subject to the enactment of legislation that places on the ballot the question of whether debt shall be incurred. The legislation authorizing the referendum must state the purposes for which the debt is to be authorized and, as a matter of practice, includes a maximum amount of funds to be borrowed. Upon electorate approval and enactment of legislation implementing the proposed debt-funded program, bonds may be issued. All such authorizing legislation to date has given issuance authority to two of the Issuing Officials, one of whom must be the Governor.

Other Bonded Debt. Debt issued to rehabilitate areas affected by disasters is authorized by specific legislation. Authorizing legislation has given issuance authority to two of the Issuing Officials, one of whom must be the Governor.

Tax Anticipation Notes. Due to the timing of major tax payment dates, the Commonwealth's General Fund cash receipts are generally concentrated in the last four months of the fiscal year, from March through June. Disbursements are distributed more evenly throughout the fiscal year. As a result, operating cash shortages can occur during certain months of the fiscal year. When necessary, the Commonwealth engages in short-term borrowing to fund expenses within the fiscal year through the sale of tax anticipation notes. The authority to issue such notes rests with the Issuing Officials.

The Commonwealth may issue tax anticipation notes only for the account of the General Fund or the Motor License Fund or both such funds. The principal amount issued, when added to that outstanding, may not exceed in the aggregate 20 percent of the revenues estimated to accrue to the appropriate fund or both funds in the fiscal year.

Tax anticipation notes must mature within the fiscal year in which they were issued. The Commonwealth is not permitted to fund deficits between fiscal years with any form of debt. Any year-end deficit balances must be funded within the succeeding fiscal year's budget.

Currently, the Commonwealth has no tax anticipation notes outstanding. The fiscal year 2005 budget does not anticipate issuing tax anticipation notes.

In the last six fiscal years the Commonwealth has not issued any tax anticipation notes.

Bond Anticipation Notes. Pending the issuance of bonds, the Commonwealth may issue bond anticipation notes subject to the applicable statutory and constitutional limitations generally imposed on bonds. The term of such borrowings may not exceed three years. Issuing authority rests with the Issuing Officials. No bond anticipation notes are outstanding.

Projected Issuance of Long-Term Debt

Table 19 shows projected future issuance of new-money long-term bonds or bond anticipation notes through fiscal year 2009 as currently estimated based on current authorizations. Included in Table 19 are bonds expected to be issued under two bond referendums, proposed by the Governor and enacted by the General Assembly in 2004 and 2005 (See "Fiscal Year 2004 Financial Results" and "Fiscal Year 2005 Budget"). Not included however, are bonds authorized under the new economic stimulus program of the Commonwealth Financing Authority. Actual issuance of bonds will be affected by a number of economic and other factors and may vary significantly from this projection.

Table 19
Projected Bond Issuance and Principal Retirements
Fiscal Years 2005-2009[a]
(In Millions)

	Fiscal Year Ending June 30				
	2005	2006	2007	2008	2009
Capital Facilities[b]					
Buildings and Structures	$ 75	$ 355	$ 365	$ 285	$ 285
Furniture and Equipment	0	0	15	12	3
Transportation Assistance	125	150	150	150	150
Redevelopment Assistance	155	165	250	305	265
Flood Control	1	11	7	10	8
Special Purpose:					
Pennvest — 1988 & 1992 Referenda	0	50	1	2	2
Local Criminal Justice	0	0	0	0	0
Disaster Relief	0	0	0	0	0
Water Facilities Loan—1981 Referendum	0	0	1	1	1
Water and Wastewater Referendum[a]	0	25	40	40	145
Growing Greener II Referendum[a]	0	200	200	200	200
Total Projected Issuance	$ 356	$ 956	$ 1,029	$ 1,005	$ 1,059
Principal Retirement[c]	$ 478.1	$ 497.4	$ 534.7	$ 574.5	$ 608.2

Totals may not add due to rounding.
[a] As proposed in fiscal year 2006 budget.
[b] Includes issuance for new projects and for projects previously authorized.
[c] On bonded debt outstanding and pro forma for projected.

OTHER STATE-RELATED OBLIGATIONS

Moral Obligations

Moral obligation financing is a financing arrangement in which designated officials of the Commonwealth, its departments or agencies agree, when necessary, to request the General Assembly to appropriate funds as may be required to make up any deficiency in a debt service reserve fund established to assure payment of obligations issued under such an arrangement. The General Assembly is not required to approve such appropriation requests.

Pennsylvania Housing Finance Agency ("PHFA"). The PHFA is a state-created agency that provides financing for housing for lower and moderate income families in the Commonwealth. The bonds, but not the notes, of the PHFA are partially secured by a capital reserve fund required to be maintained by the PHFA in an amount equal to the maximum annual debt service on its outstanding bonds in any succeeding calendar year. If there is a potential deficiency in the capital reserve fund or if funds are necessary to avoid default on interest, principal or sinking fund payments on bonds or notes of PHFA, the statute creating PHFA provides a mechanism for obtaining additional funds. That mechanism directs the Governor, upon notification from PHFA, to place in the budget of the Commonwealth for the next succeeding year an amount sufficient to make up any such deficiency or to avoid any such default. The budget as finally adopted by the General Assembly may or may not include the amount so placed therein by the Governor. PHFA is not permitted to borrow additional funds so long as any deficiency exists in the capital reserve fund. No deficiency exists currently.

According to PHFA, as of December 31, 2004, PHFA had $3,115.5 million of revenue bonds outstanding.

The Hospitals and Higher Education Facilities Authority of Philadelphia (the "Hospitals Authority"). The Hospitals Authority is a municipal authority organized by the City of Philadelphia (the "City") to, *inter alia,* acquire and prepare various sites for use as intermediate care facilities for the mentally retarded. In August 1986, the Hospitals Authority issued $20.4 million of bonds, which were refunded in 1993, by a $21.1 million bond issue of the Hospitals Authority for such facilities for the City. In July 2003, the Hospitals Authority issued its $13.32 million Series 2003 Bonds (the "Hospitals Authority Bonds") to refund the 1993 bonds. The Hospitals Authority Bonds are secured by leases with the City payable only from project revenues and a debt service reserve fund. The Commonwealth's Department of Public Welfare ("DPW") has agreed with the Hospitals Authority to request in DPW's annual budget submission to the Governor an amount of funds sufficient to alleviate any deficiency that may arise in the debt service reserve fund for the Hospitals Authority Bonds. The budget as finally adopted may or may not include the amount requested. If funds are paid to the Hospitals Authority, DPW will obtain certain rights in the property financed with the Hospitals Authority Bonds in return for such payment.

In response to a delay in the availability of billable beds and the revenues from these beds to pay debt service on the Hospitals Authority Bonds, PHFA agreed in June 1989, to provide a $2.2 million low-interest loan to the Hospitals Authority. The loan enabled the Hospitals Authority to make all debt service payments on the Hospitals Authority Bonds during 1990. Enough beds were completed in 1991 to provide sufficient revenues to the Hospitals Authority to meet its debt service payments and to begin repaying the loan from PHFA. According to the Hospitals Authority, as of December 31, 2004, $0.08 million of the loan principal was outstanding. DPW has agreed that the additional costs of the project arising from the PHFA loan will be reimbursed to the City by DPW through payments under provider agreements between the City and DPW, as reasonable costs of the project.

Lease Financing

The Commonwealth, through several of its departments and agencies, leases various real property and equipment. Some leases and their respective lease payments are, with the Commonwealth's approval, pledged as security for debt obligations issued by certain public authorities or other entities within the state. All lease payments payable by Commonwealth departments and agencies are subject to and dependent upon an annual spending authorization approved through the Commonwealth's annual budget process. The Commonwealth is not required by law to appropriate or otherwise provide moneys from which the lease payments are to be paid. The obligations to be paid from such lease payments are not bonded debt of the Commonwealth.

Table 20 contains summary information on obligations of significant amount secured by lease payments from leases with Commonwealth departments and agencies payable from the General Fund or other budgeted special funds.

Table 20
Obligations Secured By Commonwealth Lease Payments
(In Thousands)

Lessor	Purpose	Maximum Annual Lease Payment	Principal Amount Outstanding as of 6/30/2004	Final Maturity
Harristown Development Corporation	Office Space	$ 6,306	$ 62,675	May 1, 2016
Philadelphia Regional Port Authority	Port Facilities	5,101	50,700 [(a)]	Sept. 1, 2020

[(a)] The outstanding balance of the Authority's Series 1993 Bonds was refunded by the issuance of its $53.9 million principal amount of Series 2003 Bonds in August 2003.

The Harristown Development Corporation leases office space to the Commonwealth in the city of Harrisburg. Certificates of participation in the principal amount of $71,135,000 were issued in October 2001, representing undivided rights in the lease payments by the Commonwealth to the Harristown Development Corporation for nearly one million square feet of office space occupied by Commonwealth departments and agencies since 1978.

The Commonwealth has also leased port facilities of the Philadelphia Regional Port Authority ("PRPA") to encourage trade through the Port of Philadelphia. Lease revenue bonds of PRPA in the amount of $53.,9 million were issued by that authority in August 2003 to refund all outstanding PRPA Series 1993 Bonds. These bonds are payable from lease payments made by the Commonwealth from an annual appropriation authorizing payments to PRPA.

These lease obligations and agreements to lease various other facilities and equipment entered into by the Commonwealth are included in Note K to the Fund Financial Statements for the fiscal year ended June 30, 2004.

Commonwealth Financing Authority

The Commonwealth Financing Authority (the "CFA"), a major component of the Governor's Economic Stimulus Proposals for the Commonwealth, was established in April 2004 with the enactment of legislation establishing the CFA as an independent authority and an instrumentality of the Commonwealth. The CFA is authorized to issue its limited obligation revenue bonds and other types of limited obligation revenue financing for the purposes of promoting the health, safety, employment, business opportunities, economic activity and general welfare of the Commonwealth and its citizens through loans, grants, guarantees, leases, lines and letters of credit and other financing arrangements to benefit both for-profit and non-profit entities. The CFA's bonds and financings are to be secured by revenues and accounts of the CFA, including funds appropriated to CFA from general revenues of the Commonwealth for repayment of CFA obligations. The obligations of the CFA will not be a debt or liability of the Commonwealth but it is expected that the CFA may issue debt that may be payable from appropriations of the Commonwealth.

The CFA has not, to date, issued bonds or other obligations for its purposes and no appropriations have been made from Commonwealth general revenues to the CFA for repayments of any such bonds or other obligations. However, the CFA expects to begin issuing its bonds or other obligations during fiscal year 2005 that may require appropriation of Commonwealth general revenues for fiscal year 2006 and for subsequent fiscal years to the CFA for payment of all or a portion of CFA debt service during each fiscal year. Any appropriation of general revenues will require the passage of legislation by the General Assembly and approval by the Governor for a designated fiscal period.

Pensions and Retirement Systems

The Commonwealth maintains contributory benefit pension plans covering all state employees, public school employees and employees of certain state-related organizations. State employees and employees of certain state-related organizations are members of the State Employees' Retirement System ("SERS"). Public school employees are members of the Public School Employees' Retirement System ("PSERS"). With certain exceptions, membership in the applicable retirement system is mandatory for covered employees.

SERS and PSERS are established by state law as independent administrative boards of the Commonwealth, each directed by a governing board, which exercises control and management of its system, including the investment of its assets. The board of the SERS consists of eleven members, six appointed by the Governor, two members each from the Senate and House of Representatives and the State Treasurer. The PSERS board has fifteen members including the Commonwealth's Secretary of Education, the State Treasurer, the executive secretary of the Pennsylvania School Boards Association, two members appointed by the Governor, six elected members (five from among PSERS members and one from among school board members in Pennsylvania) and two members each from the Senate and the House of Representatives.

The retirement plans of SERS and PSERS are contributory defined benefit plans for which the benefit payments to members and contribution rates by employees are specified in state law. Changes in benefit and contribution provisions for each retirement plan must be made by legislation. Under statutory provisions established in 1981, all legislative bills and amendments proposing to change a public employee pension or retirement plan are to be accompanied with an actuarial note prepared by an enrolled pension actuary providing an estimate of the cost and actuarial effect of the proposed change.

The Commonwealth's retirement programs are jointly contributory between the employer and employee. The contribution rate for PSERS new members who enroll in the pension plan on or after January 1, 2002 is 7.5 percent of compensation. The contribution rates for current PSERS members range from 5 percent to 7.5 percent of compensation depending upon their date of employment and elections made by the member. SERS' contribution rate for most employees is 6.25%. Interest on each employee's accumulated contributions is credited annually at a 4 percent rate mandated by state statute. Accumulated contributions plus interest credited is refundable to covered employees upon termination of their employment.

Act 40 of 2003 amended the PSERS' actuarial cost method. Under Act 40, the outstanding balance of the unfunded accrued liability as of June 30, 2001 and the decrease in the unfunded accrued liability due to the actuarial asset method change provided by Act 38 continue to be amortized over a 10-year period, with level dollar funding, beginning July 1, 2002. The increases in the unfunded accrued liability due to the July 1, 2002 and July 1, 2003 cost-of-living adjustments provided by Act 38 continue to be amortized over a 10-year period, with level dollar funding, starting on July 1, 2003 and July 1, 2004, respectively. All other changes in the unfunded accrued liability at June 30, 2001, June 30, 2002, and June 30, 2003, are amortized over a 30-year period, with level dollar funding, starting on July 1, 2002, July 1, 2003, and July 1, 2004, respectively. Future benefit improvements for active members and retirees will be amortized over a 10-year period with level dollar funding. Future gains and losses will be amortized over a 30-year period with level dollar funding. Act 40 also provides a 4.00% floor on the employer pension rate for PSERS.

With respect to SERS, Act 40 of 2003 set the amortization period for the accrued liabilities at 10 and 30 year schedules with level payments. Additionally, Act 40 revised minimum contributions for SERS to 2%, 3%, and 4% effective July 1, 2004, 2005, and 2006, respectively. Supplemental annuity contributions are funded over 10 years with level dollar payments. SERS employer rates vary by class/category of service. For fiscal year 2003, the SERS employer rate for most employees is 0.5 percent and for fiscal year 2004 is 1.43 percent.

For PSERS, the employer's contribution is shared by the Commonwealth and the school districts. For school entities, the Commonwealth remits its employer contribution portion to those school entities, which then remit the entire employer contributions (both school entity and Commonwealth portions) to PSERS. The Commonwealth's contribution is appropriated annually from the General Fund to the Department of Education. The PSERS employer rate for fiscal year 2005 is 4.23 percent and for fiscal year 2006 is 4.69 percent.

Contributions to the pension plans by the employer (including normal costs and payments to amortize prior service costs and medical premium assistance payments), employee contributions, interest earnings on the plans and benefit payments are shown in the following tables, which have been prepared by the staffs of SERS and PSERS.

Table 21
Public School Employees' Retirement Fund
(In Millions)

Year Ended June 30	Employer Contributions	Employee Contributions	Net Investment Income	Total Deductions From Plan Net Assets[a]	Net Assets[b]
2000	$413	$680	$5,765	$2,411	$53,422
2001	186	722	(3,844)	2,332	48,153
2002	109	806	(2,523)	2,948	43,597
2003	116	897	1,022	3,144	42,488
2004	407	944	8,245	3,547	48,537

(a) Includes the PSERS administrative expenses.

(b) PSERS adopted GASB Statement No.'s 25 and 26 retroactively to fiscal 1994. GASB Statement No. 25 requires the presentation of Plan Net Assets, which combines the cumulative residual effects of all System assets and current liabilities. System long-term actuarial liabilities are not presented on the System's basic financial statements, but instead are presented upon a supplementary schedule of funding progress. The presentations above include the effects of financial activity related to the administration of the PSERS healthcare insurance premium assistance program and Health Options Program. As required with the adoption of GASB Statement No. 26, separate financial presentation for these programs are made on PSERS financial statements. PSERS also adopted GASB Statement No. 34 for the fiscal year beginning July 1, 2001 that requires the presentation of Management's Discussion and Analysis as required supplementary information preceding the financial statement.

Table 22
State Employees' Retirement Fund
(In Millions)

Year Ended December 31	Employer Contributions	Employee Contributions	Net Investment Income[a]	Total Deductions From Plan Net Assets[b]	Plan Net Assets[c]
1999	$ 225	$ 271	$ 4,723	$ 1,248	$ 28,093
2000	168	232	586	1,198	27,880
2001	77	241	(2,226)	1,266	24,706
2002	51	304	(2,731)	1,450	20,880
2003	69	308	4,936	1,656	24,536

(a) Includes net appreciation (depreciation) in fair value of investments.

(b) Includes SERS administrative costs.

(c) Market value of investment assets. SERS adopted GASB Statement No. 25 retroactively as of January 1, 1995. GASB Statement No. 25 requires that investments be reported at their fair value. The 1995 net asset value has been restated in accordance with GASB Statement No. 25. Also includes securities lending collateral pool pursuant to GASB Statement No. 28. In 2002, SERS adopted GASB Statement No. 34 that requires the presentation of Management Discussion and Analysis as required supplementary information preceding the financial statements.

Annual actuarial valuations are required by state law to determine the employer contribution rates necessary to accumulate sufficient assets and provide for payment of future benefits. The actuary's recommendations for employer contribution rates represent a funding plan for meeting current and future retirement obligations and are included in the enacted budget for the current fiscal year. The employer's contribution rate is computed to fully amortize the unfunded actuarial accrued liability of the respective plan as determined by its actuary. The unfunded accrued liability is a measure of the present value of benefits estimated to be due in the future for current employees given assumptions as to mortality, pay levels, retirement experience and employee turnover, less the present value of assets available to pay those benefits given assumptions of normal cost, supplemental annuity amortization, employer contribution levels and member contributions. The unfunded actuarial accrued liability for the most recent years with completed valuations based on the projected benefit method utilizing level percentage entry age and normal cost is shown in Table 23 on the next page. Both SERS and PSERS currently use an investment rate of return assumption of 8.5 percent.

Table 23
Unfunded Actuarial Accrued Liability
2000-2004
(In Millions)

Valuation Year Ended	SERS[a]	PSERS[b]
2000	$ (6,392)	$ (9,470)
2001	(3,846)	(6,913)
2002	(1,848)	(2,500)
2003	(1,286)	(1,543)
2004	NA	5,028

[a] The fiscal year for SERS ends on December 31 of each year.
[b] The fiscal year for PSERS ends on June 30 of each year. The net decrease in the unfunded actuarial accrued liability between 1999 and 2000 is due primarily to investment returns exceeding the actuarially assumed rate. The net increase in the unfunded actuarial accrued liability from 2001 to 2004 is attributable to pension plan modification under Act 9 of 2001 and Act 38 of 2002 and actuarial investment returns below the actuarially assumed rate.

For financial reporting purposes, both SERS and PSERS have adopted the Governmental Accounting Standards Board's Statement No. 25. This Statement requires a specific method of accounting and financial reporting for defined benefit pension plans. Among other things, the Statement requires a comparison of employer contributions to "annual required contributions" (ARC). Independently audited financial statements for both SERS and PSERS, as of December 31, 2003 and June 30, 2004, respectively, provide this comparison for each of the five fiscal years then ended. For all years shown, for both SERS and PSERS, employer contributions were at least 100 percent of ARC.

GOVERNMENT AUTHORITIES AND OTHER ORGANIZATIONS

Certain state-created organizations have statutory authorization to issue debt for which state appropriations to pay debt service thereon are not required. The debt of these organizations is funded by assets of, or revenues derived from, the various projects financed and is not a statutory or moral obligation of the Commonwealth. However, some of these organizations are indirectly dependent upon Commonwealth operating appropriations. In addition, the Commonwealth may choose to take action to financially assist these organizations. These organizations, their purposes and their outstanding debt, as computed by each organization, are as follows:

Delaware River Joint Toll Bridge Commission ("DRJTBC"). The DRJTBC, a public corporation of the Commonwealth and New Jersey, owns and operates bridges across the Delaware River. Debt service on bonds is paid from tolls and other revenues of the Commission. The DRJTBC had $151.2 million in bonds outstanding as of December 31, 2004.

Delaware River Port Authority ("DRPA"). The DRPA, a public corporation of the Commonwealth and New Jersey, operates several toll bridges over the Delaware River, and promotes the use of the Philadelphia-Camden port and promotes economic development in the port district. Debt service on bonds is paid from toll revenues and other revenues pledged by DRPA to repayment of bonds. The DRPA had $1,273.1 million in revenue bond debt outstanding as of December 31, 2004.

Pennsylvania Economic Development Financing Authority ("PEDFA"). The PEDFA was created in 1987 to offer pooled bond and other bond issues for both taxable and tax-exempt bonds on behalf of local industrial and commercial development authorities for economic development projects. Bonds may be secured by loan repayments and all other revenues of the PEDFA. The PEDFA had $1,702.0 million of debt outstanding as of December 31, 2004.

Pennsylvania Energy Development Authority ("PEDA"). The PEDA was created in 1982 to finance energy research projects, demonstration projects promoting the production or conservation of energy and the promotion, utilization and transportation of Pennsylvania energy resources. The authority's funding is from appropriations and project revenues. Debt service on bonds is paid from project revenues and other revenues pledged by PEDA to repayment of bonds. The PEDA had $28.1 million in bonds outstanding as of December 31, 2004.

Pennsylvania Higher Education Assistance Agency ("PHEAA"). The PHEAA makes or guarantees student loans to students or parents, or to lending institutions or post-secondary institutions. Debt service on the bonds is paid by loan interest and repayments and other agency revenues. The PHEAA had $4,724.8 million in bonds outstanding as of December 31, 2004.

Pennsylvania Higher Educational Facilities Authority ("PHEFA"). The PHEFA is a public corporation of the Commonwealth established to finance college facilities. As of December 31, 2004, the PHEFA had $4,644.4 million in revenue bonds and notes outstanding payable from the lease rentals or loan repayments of the projects financed. Some of the lessees or borrowers, although private institutions, receive grants and subsidies from the Commonwealth.

Pennsylvania Industrial Development Authority ("PIDA"). The PIDA is a public corporation of the Commonwealth established for the purpose of financing economic development. The PIDA had $488.3 million in revenue bond debt outstanding on December 31, 2004, to which all of its revenues are pledged.

Pennsylvania Infrastructure Investment Authority ("Pennvest"). Pennvest was created in 1988 to provide low interest rate loans and grants for the purpose of constructing new and improving existing water supply and sewage disposal systems to protect the health and safety of the citizens of the Commonwealth and to promote economic development within the Commonwealth. Loans and grants are available to local governments and, in certain circumstances, to private companies. The Pennvest bonds are secured by principal repayments and interest payments on Pennvest loans. Pennvest had $96.8 million of revenue bonds outstanding as of December 31, 2004.

Pennsylvania Turnpike Commission ("PTC"). The PTC operates the Pennsylvania Turnpike System ("System"). Its outstanding indebtedness, $2,452.0 million as of December 31, 2004, is payable from the net revenues of the System, primarily toll revenues and rentals from leases and concessions or from certain taxes dedicated to the System.

State Public School Building Authority ("SPSBA"). The SPSBA finances public school projects and community colleges. Bonds issued by the SPSBA are supported by the lease rental payments or loan repayments made to the SPSBA by local school districts and the community colleges. A portion of the funds appropriated annually by the Commonwealth as aid to local school districts and community colleges may be used by them to pay a portion of such lease rental payments or loan repayments. The SPSBA had $1,442.9 million of revenue bonds outstanding as of December 31, 2004.

CITY OF PHILADELPHIA - PICA

The Pennsylvania Intergovernmental Cooperation Authority ("PICA") was created by Commonwealth legislation in 1991 to assist the City of Philadelphia, the Commonwealth's largest city, in remedying its fiscal emergencies. PICA is authorized to provide assistance through the issuance of funding debt and to make factual findings and recommendations to Philadelphia concerning its budgetary and fiscal affairs. This financial assistance has included grants used by the City for defeasance of certain City general obligation bonds, funding of capital projects and the liquidation of the cumulative general fund balance deficit of the City of Philadelphia as of June 30, 1992, of $224.9 million. At this time, Philadelphia is operating under a five-year fiscal plan approved by PICA on December 21, 2004.

No further bonds may be issued by PICA for the purpose of either financing capital projects or a deficit as the authority for such bond issuance expired December 31, 1994. PICA's authority to issue debt for the purpose of financing a cash flow deficit expired on December 31, 1995. Its ability to refund existing outstanding debt is unrestricted. PICA had $770.7 million in special tax revenue bonds outstanding as of June 30, 2004. Neither the taxing power nor the credit of the Commonwealth is pledged to pay debt service on PICA's bonds.

LITIGATION

The Commonwealth's Office of Attorney General and Office of General Counsel have reviewed the status of pending litigation against the Commonwealth, its officers and employees, and have provided the following brief descriptions of certain cases affecting the Commonwealth.

In 1978, the General Assembly approved a limited waiver of sovereign immunity. Damages for any loss are limited to $250,000 for each person and $1,000,000 for each accident. The Supreme Court of Pennsylvania has held that this limitation is constitutional. Approximately 3,500 suits against the Commonwealth remain open. Tort claim payments for the departments and agencies, other than the Department of Transportation, are paid from departmental and agency operating and program appropriations. Tort claim payments for the Department of Transportation are paid from an appropriation from the Motor License Fund. The Motor License Fund tort claim appropriation for fiscal year 2005 is $20.0 million.

Powell v. Ridge

Over recent years, there have been three suits directed at school funding, *Marrero v. Commonwealth; Pennsylvania Association of Rural and Small Schools v. Ridge*; and *Powell v. Ridge*. The first two have been resolved in the Commonwealth's favor. The third, *Powell v. Ridge*, remains pending but does not appear to present a viable claim in its current form.

In 1998, a suit was filed in the United States District Court for the Eastern District of Pennsylvania on behalf of a variety of plaintiffs, including the School District of Philadelphia, the parents of several Philadelphia school children, local community organizations, and the City and Mayor of Philadelphia. The suit alleges that the Commonwealth's formula for distributing school funding provides less money to districts with a majority non-white population than it does to similarly situated districts that have a majority of white students. The suit claims that the funding disparities ultimately injure non-white students by limiting their educational opportunities. The plaintiffs seek a declaration that the Commonwealth's funding practices and policies discriminate against minority students in violation of Federal law; and they seek an injunction prohibiting the Commonwealth prospectively from using a discriminatory school funding scheme.

Since June 23, 2000, the case has been in civil suspense for a variety of reasons. Most recently, the court continued the stay of proceedings until the U.S. Court of Appeals for the Third Circuit and the U.S. Supreme Court decided other cases that likely would directly affect the plaintiffs' claims. Those decisions have now been issued and make clear that the plaintiffs' claims, as currently pled, are not viable.

In *Alexander v. Sandoval*, 532 U.S. 275 (2001), the U.S. Supreme Court held that no party other than the federal government may bring suit to enforce regulations promulgated by a federal agency under Title VI of the Civil Rights Act of 1964 prohibiting federally-funded programs from having racially discriminatory effects. Then, in *South Camden Citizens In Action v. New Jersey Dep't of Env. Prot.*, 274 F.3d 771 (3d Cir. 2001), *cert. denied*, 122 S.Ct. 2621 (2002), the U.S. Court of Appeals for the Third Circuit ruled that a plaintiff also could not seek to enforce Title VI regulations prohibiting discriminatory effects in federally-funded programs under 42 U.S.C. § 1983. The principles applied by the Court of Appeals in *South Camden Citizens In Action* were endorsed by the U.S. Supreme Court in *Gonzaga Univ. v. Doe*, 122 S. Ct. 2268 (2002). Based on these cases, it seems clear that the claims now presented by the plaintiffs in *Powell v. Ridge* cannot proceed as they are pled.

Though *South Camden Citizens In Action* was decided finally in June 2003, no party has taken action to lift the stay in *Powell*. Based on statements to the district court made by some of the *Powell* plaintiffs in 2001, the defendants – the Governor, the Secretary of Education, the State Treasurer, and the chair of the State Board of Education – anticipate that one or more of the plaintiffs may seek to amend the complaint in an effort to state a claim for intentional discrimination under Title VI of the Civil Rights Act. However, the U.S. Court of Appeals has made clear:

> To prove intentional discrimination by a facially neutral policy [actionable under Title VI of the Civil Rights Act,], a plaintiff must show that the relevant decision-maker (e.g., a state legislature) adopted the policy at issue "'because of,' not merely 'in spite of,' its adverse effects upon an identifiable group." A mere awareness of the consequences of an otherwise neutral policy will not suffice.

A new judge was assigned to this case on August 26, 2004. On September 28, 2004, it was ordered that the stay could continue through April of 2005.

County of Allegheny v. Commonwealth of Pennsylvania

In December 1987, the Supreme Court of Pennsylvania held in *County of Allegheny v. Commonwealth of Pennsylvania* that the statutory scheme for county funding of the judicial system is in conflict with the Pennsylvania Constitution. However, the Supreme Court of Pennsylvania stayed its judgment to afford the General Assembly an opportunity to enact appropriate funding legislation consistent with its opinion and ordered that the prior system of county funding shall remain in place until this is done.

The Court appointed retired Justice Frank J. Montemuro, Jr. as special master to devise and submit a plan for implementation. The *Interim Report of the Master* recommended a four phase transition to state funding of a unified judicial system, during each of which specified court employees would transfer into the state payroll system. Phase I recommended that the General Assembly provide for an administrative structure of local court administrators to be employed by the Administrative Office of Pennsylvania Courts, a state agency. Numbering approximately 165 people statewide, local court administrators are employees of the counties in which they work. On June 22, 1999, the Governor approved Act No. 1999-12 under which approximately 165 county-level court administrators became employees of the Commonwealth. Act 12 also triggered the release of appropriations that had been made for this purpose in 1998 and 1999.

The remainder of Justice Montemuro's recommendation for later phases remains pending before the Supreme Court of Pennsylvania.

PPG Industries, Inc. v. Commonwealth of Pennsylvania

By decision dated November 30, 2001, the Pennsylvania Supreme Court held that the manufacturing exemption to Pennsylvania's capital stock/franchise tax discriminates against interstate commerce in violation of the Commerce Clause of the United States Constitution. Accordingly, the Court ordered the manufacturing exemption severed from the capital stock/franchise tax. Further, the Court directed that the Commonwealth must forthwith provide a retrospective remedy to taxpayers along the lines of those provided by the U.S. Supreme Court in *McKesson v. Division of Alcoholic Beverages and Tobacco, Dept. of Business Regulation of Florida*, 496 U.S. 18 (1990), i.e., (1) refunds for those taxpayers who were discriminated against by the unlawful exemption, (2) additional assessments against those who benefited by the unlawful exemption, or (3) some combination of the two so long as any remedy does not discriminate against interstate commerce. During the course of this litigation, the General Assembly enacted amendments to the Tax Reform Code of 1971, which presumptively cure the constitutional problem with the tax after January 1, 1999, but do not impact on the tax during the years involved in this litigation.

PPG filed with the court a petition for reconsideration of its November 30, 2001, Opinion and Order which the Court denied by per curium order dated February 1, 2002. The retrospective remedy announced by the Commonwealth on April 29, 2002, appears to be revenue neutral and satisfactory for in-state manufacturers. However, out-of-state manufacturers have appealed, involving an undetermined but significant dollar amount and those appeals remain pending.

Most of the appeals of out-of-state manufacturers have been resolved through settlement. Some significant cases remain open, but overall, it is probable that these matters will be successfully resolved through settlement without significant fiscal input.

Unisys Corporation v. Commonwealth

Unisys challenged the statutory three-factor apportionment formula used for the apportionment of capital stock value in the franchise tax on constitutional and statutory (fairness) grounds. Unisys's argument is that because the valuation formula requires the use of consolidated net worth, instead of separate company net worth, and the inclusion of dividends paid by subsidiary corporations, the apportionment factors should also include the property, payroll and sales of the subsidiary corporations, not just those of the taxpayer.

The case was argued before the Commonwealth Court en banc, which issued its decision on March 8, 1999. The court sustained the statute from the constitutional challenge in favor of the Commonwealth. However, it ruled in favor of the taxpayer's fairness argument, which was based on 72 P.S. §7401(3) 2. (a)(18). There were two dissents.

The Commonwealth appealed this decision to the Pennsylvania Supreme Court and Unisys cross-appealed. The Court held oral argument in December 2000. On October 25, 2002, the Court issued a decision reversing the holding of the Commonwealth Court and upholding the Commonwealth's statutory apportionment formula. Unisys filed an application for re-argument, which was denied. Unisys filed a petition for certiorari to the U.S. Supreme Court, which was denied. The decision in this matter denied relief to the taxpayer because it failed to carry its burden of proof and did not resolve the underlying issue. Thus, the decision has very limited applicability to the numerous cases pending which raise the identical issue and which collectively involve undetermined but significant dollars.

Northbrook Life Insurance Co., No. 1120 F&R 1996

This case is the lead case in potential litigation with the entire insurance industry that does business in Pennsylvania. Currently, the Commonwealth Court has docketed in excess of 40 cases representing 20 or more insurance companies. Dozens of additional cases are being held pending this litigation at the administrative boards.

The cases challenge the Department of Revenue's application of portions of the Life and Health Guarantee Association Act of 1982 (the "Act"). The Act establishes a funding mechanism to fulfill defaulted obligations of insurance companies under life and health insurance policies and annuities contracts to insured Pennsylvania residents. In accordance with this funding mechanism, other insurance companies are assessed to provide the funds due to Pennsylvania residents insured by insurance companies which have become insolvent or are otherwise in default to their insureds.

Because the assessed insurance companies are paying the insurance obligations of other companies, a provision was placed in the Act which allows assessed insurance companies to claim a credit against their gross premiums tax liability based on such assessments.

The assessments on each company are broken into various categories including life insurance assessments, health insurance assessments, and annuity assessments, based on the type and amount of business each company transacts in Pennsylvania.

Life and health insurance premiums have always been subject to the premiums tax and there is no dispute that companies may claim credit for life and health assessments. Annuity considerations, however, were taxed for approximately a three-year period, 1992-1995. Some annuity considerations were subject to tax, others were not. After several changes of direction, the Department of Revenue decided to allow credits for assessments paid on taxable annuity considerations. Credits were not allowed for assessments paid on non-taxable annuities.

There is no provision in the insurance law that restricts the credit to only the assessments paid on taxable annuities. Taxpayers want the credit for assessments paid on all annuities, both during the period that annuities were taxed and going forward.

The matter is being prepared for litigation. Settlement negotiations continue although the possibility of settlement appears to be unlikely. Estimates of refund potential vary widely, ranging from $50 million to $300 million.

Duquesne Light Co. v. Commonwealth

There are several appeals involving various years and taxes. These matters challenge the capital stock tax, corporate net income tax and gross receipts tax as applied to this taxpayer. There is over $100 million in total disputed taxes, and issues raised include entitlement to the manufacturing exemption for capital stock tax purposes for the generation of electricity, non-business income treatment on gains realized from the sale of several power plants in Ohio, and where sales receipts should be sourced for corporate net income tax and gross receipts tax reporting purposes. These matters are being reported to be on the conservative side, as it is highly doubtful that the exposure would ever be anywhere near the disputed amount. At present, these matters are the subject of discussions between the parties as to how they might be resolved.

RATINGS

Moody's Investors Service ("Moody's") has assigned its municipal bond rating of "Aa2" to the Bonds, Standard and Poor's Ratings Services, a division of the McGraw-Hill Companies ("S&P") has assigned its municipal bond rating of "AA" to the Bonds, and Fitch Ratings ("Fitch") has assigned its municipal bond rating of "AA" to the Bonds. The ratings reflect only the views of the rating agencies.

The ratings are based upon current information furnished by the Commonwealth or obtained from other sources considered reliable by the rating agencies, which do not perform any audit in connection with any rating and may, on occasion, rely on unaudited financial information. Reference is made to the rating agencies' manuals for complete descriptions of their respective rating procedures and other rating categories, and to S&P's, Moody's and Fitch's discussions of the Commonwealth expected to be released in connection with their ratings.

A security rating is not a recommendation to buy, sell or hold securities. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely if, in the opinion of the rating agencies, circumstances warrant such revision or withdrawal. Any such downward revision or withdrawal could have an adverse effect on the marketability or market price of the Bonds. The Commonwealth has not undertaken any responsibility after issuance of the Bonds to assure the maintenance of the ratings, to oppose any revision or withdrawal of the ratings by S&P, Moody's or Fitch or to inform the holders of the Bonds of any such revision or withdrawal, except as set forth under "CONTINUING DISCLOSURE."

TAX MATTERS

In the opinion of Bond Counsel, under existing law, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. It should be noted, however, that with respect to corporations (as corporations are defined for federal income tax purposes), such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax imposed on corporations by the Internal Revenue Code of 1986, as amended (the "Code").

Bond Counsel is also of the opinion that, under existing law, interest on the Bonds is exempt from Pennsylvania personal income tax and from Pennsylvania corporate net income tax, and the Bonds are exempt from personal property taxes in Pennsylvania.

Except as expressly stated above, Bond Counsel will not express any opinion as to any other federal or state tax consequences of acquiring, carrying, owning or disposing of the Bonds, and prospective purchasers of the Bonds should consult with their own tax advisors as to the applicability of these and any other collateral tax consequences of ownership of the Bonds.

The opinion of Bond Counsel on federal tax matters will be based upon and will assume the accuracy of certain representations and certifications, and compliance with certain covenants, of the Commonwealth to be contained in the transcript of proceedings and that are intended to evidence and assure that the Bonds are and will remain obligations the interest on which is excluded from gross income for federal income tax purposes. Bond Counsel will not independently verify the accuracy of those certifications and representations.

The Code prescribes a number of qualifications and conditions for the interest on state and local obligations to be and to remain excluded from gross income for federal income tax purposes, some of which require future or continued compliance after issuance of the obligations in order for the interest to be and to continue to be so excluded from the date of issuance. Noncompliance with these requirements by the Commonwealth may cause the interest on the Bonds to be included in gross income for federal income tax purposes and thus to be subject to federal income tax retroactively to their date of issuance. The Commonwealth has covenanted to take the actions required of it for the interest on the Bonds to be and to remain excluded from gross income for federal income tax purposes, and not to take any actions that would adversely affect that exclusion.

Ownership of the Bonds may result in collateral federal income tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, individual recipients of Social Security or Railroad Retirement benefits, S corporations with "excess net passive income" and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry the Bonds. Bond Counsel expresses no opinion as to such collateral federal income tax consequences.

Certain of the Bonds were sold with original issue premium (the "Premium Bonds"). The difference between the first price at which a substantial amount of the Premium Bonds is sold to the public and the stated redemption price at maturity constitutes to an initial purchaser amortizable bond premium which is not deductible from gross income for regular federal income tax purposes. The amount of amortizable bond premium for the taxable year is determined actuarially on a constant interest rate basis over the term of a Premium Bond. For purposes of determining gain or loss on the sale or other disposition of a Premium Bond, an initial purchaser who acquires such obligation in the initial offering to the public at the initial offering price is required to decrease such person's adjusted basis in such Premium Bond by the amount of amortizable bond premium for the taxable year. Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

* * * * * *

THE FOREGOING IS NOT INTENDED AS AN EXHAUSTIVE DISCUSSION OF THE PROVISIONS OF FEDERAL OR STATE TAX LAW WHICH MAY HAVE AN EFFECT ON INDIVIDUALS AND CORPORATIONS HOLDING THE BONDS OR RECEIVING INTEREST THEREON. PROSPECTIVE PURCHASERS OF THE BONDS SHOULD CONSULT WITH THEIR TAX ADVISORS REGARDING THE EFFECT ON THEIR AFFAIRS OF HOLDING THE BONDS OR RECEIVING INTEREST THEREON, INCLUDING, BUT NOT LIMITED TO, THE EFFECT OF STATE AND LOCAL TAX LAWS.

UNDERWRITING

After competitive bidding on May 24, 2005, the Bonds were awarded to Morgan Stanley & Co., Incorporated (the "Underwriters") for a purchase price of $213,117,757.95. The Underwriters have supplied the public offering yields of the Bonds shown on the front cover hereof. If all of the Bonds are resold to the public at such yields, the underwriters' discount (including payment for insurance of certain maturities of the Bonds as described on the cover page of this Official Statement) will approximate 0.171625percent of the aggregate principal amount of the Bonds. The Underwriters may change the public offering yields from time to time.

LEGALITY FOR INVESTMENT

Under the Pennsylvania Probate, Estates and Fiduciaries Code, the Bonds are authorized investments for fiduciaries, as defined in that code, within the Commonwealth of Pennsylvania. The Bonds are legal investments for Pennsylvania savings banks, banks, bank and trust companies, and insurance companies and are acceptable as security for deposits of funds of the Commonwealth. The Bonds are eligible for purchase, dealing in, underwriting and unlimited holding by national banking associations pursuant to regulations promulgated by the Comptroller of the Currency set forth in the Code of Federal Regulations, Title 12—Banks and Banking, Sections 1.3(c) and 1.4.

FINANCIAL ADVISOR

Public Financial Management, Philadelphia, Pennsylvania, is serving as independent Financial Advisor to the Commonwealth with respect to the Bonds (the "Financial Advisor"). The Financial Advisor's fees in connection with the issuance of the Bonds are expected to be paid from Bond proceeds.

LEGAL MATTERS

All legal matters incident to the authorization and issuance of the Bonds are subject to the approval of the Attorney General of the Commonwealth of Pennsylvania, The Honorable Tom Corbett, and of Obermayer Rebmann Maxwell & Hippel LLP, Philadelphia, Pennsylvania, Bond Counsel. A copy of the opinion of Bond Counsel will accompany the Bonds delivered to DTC. Copies of the opinion of the Attorney General, together with additional copies of the opinion of Bond Counsel, will be available at the time of delivery of the Bonds. Proposed forms of these opinions are included as Appendices F and G respectively.

Hunton & Williams LLP, Richmond, Virginia, serves as a special disclosure counsel to the Commonwealth in connection with its general obligation bonds.

ADDITIONAL INFORMATION

Periodic public reports relating to the financial condition of the Commonwealth are prepared by the Office of the Budget. These reports and additional information may be obtained upon request from the office of the Secretary of the Budget, Mr. Michael Masch, Attn.: Mr. Richard Dreher, 7th Floor, Bell Tower, 303 Walnut Street, Harrisburg, Pennsylvania 17101-1808 (Telephone (717) 783-3086). The annual Comprehensive Annual Financial Report ("CAFR"), and a summary of the enacted fiscal year 2005 budget, the proposed fiscal year 2006 budget and certain other information are available in the Budget and Financial Reports section of the Office of the Budget's web site on the World Wide Web, http://www.budget.state.pa.us.

CONTINUING DISCLOSURE

The Commonwealth will execute a written agreement (the "Continuing Disclosure Agreement") for the benefit of the beneficial owners of the Bonds in order to assist the Underwriters in meeting the requirements of Rule 15c2-12 (the "Rule") promulgated by the Securities and Exchange Commission. The Continuing Disclosure Agreement will require the Commonwealth to:

(i) File not later than 240 days following the end of each of the Commonwealth's fiscal years, Annual Financial Statements and Annual Operating Data, as defined below, with each then-existing NRMSIR, or to DisclosureUSA or a similar central repository approved by the Securities and Exchange Commission (a "Central Repository"), and if one is established and then in operation, with any State Information Depository ("SID") for the Commonwealth of Pennsylvania;

(ii) File in a timely manner to each NRMSIR or a Central Repository (and any SID then existing) notice of certain specified events listed below; and

(iii) File with either each NRMSIR, a Central Repository, or the Municipal Securities Rulemaking Board (and with any SID then existing) notice of any failure of the Commonwealth to file the information required by (i) above.

Annual Financial Information. It is expected that the financial statements to be filed annually as provided by (i) above will be audited financial statements. The Continuing Disclosure Agreement, however, permits the filing of unaudited financial statements if audited financial statements are not available by the 240-day deadline, with audited financial statements to be filed as soon as they are available. The Annual Operating Data will be operating data of the type contained in this Official Statement in the following tables:

(i) Tables 5 through 12 under the heading "COMMONWEALTH FINANCIAL PERFORMANCE";

(ii) Tables 15 and 17 through 18 under the heading "OUTSTANDING INDEBTEDNESS OF THE COMMONWEALTH"; and

(iii) Tables 20 through 23 under the heading "OTHER STATE-RELATED OBLIGATIONS."

If any of the tables listed above reflect information that is no longer calculated and available or relevant because of changes in operations, the Commonwealth will provide notice of such change in the first annual filing of Annual Operating Data after such changes are undertaken. The format of the tables also may be altered.

Event Disclosure. The Continuing Disclosure Agreement requires the Commonwealth to provide timely notice to each NRMSIR or a Central Repository (and any SID then existing) of the following events if such events are material with respect to the Bonds:

* principal and interest payment delinquencies;
* nonpayment related defaults;
* unscheduled draws on debt service reserves reflecting financial difficulties;
* unscheduled draws on credit enhancements reflecting financial difficulties;
* substitution of credit or liquidity providers, or their failure to perform;
* adverse tax opinions or events affecting the tax-exempt status of the Bonds;
* modifications to the rights of holders of the Bonds;
* Bond calls;
* defeasances;

* release, substitution, or sale of property securing repayment of the Bonds; and
* rating changes.

The eleven events listed above are specified by the Rule but some of them may not be relevant to the Bonds.

Limitations, Remedy and Amendments. The Continuing Disclosure Agreement requires the Commonwealth to provide only limited information at limited times, and such information may not include all information necessary to determine the value of the Bonds at any time. The Commonwealth may also make other information available on a voluntary basis, but it is not contractually obligated to do so. See "ADDITIONAL INFORMATION" herein for the availability of other information from the Commonwealth's Office of the Budget.

The sole and exclusive remedy for any breach by the Commonwealth of its obligations under the Continuing Disclosure Agreement is an action to compel specific performance by the Commonwealth of its obligations. No assurance can be provided as to the outcome of any such proceeding. A breach by the Commonwealth of its obligations under the Continuing Disclosure Agreement does not constitute a default under the Bonds.

The Commonwealth reserves the right to amend the Continuing Disclosure Agreement consistent with the provisions of the Rule as then in effect.

The Commonwealth has never failed to comply in all material respects with any previous continuing disclosure undertaking.

NRMSIRs. As of the date of this Official Statement, the Securities and Exchange Commission has recognized the following NRMSIRs:

Bloomberg Municipal Repository
100 Business Park Drive
Skillman, NJ 08558
Phone: (609) 279-3225
Fax: (609) 279-5962
E-mail: munis@bloomberg.com

Standard & Poor's Securities Evaluations, Inc.
55 Water Street
45th Floor
New York, NY 10041
Phone: (212) 438-4595
Fax: (212) 438-3975
E-mail: nrmsir_repository@sandp.com

DPC Data Inc
One Executive Drive
Fort Lee, NJ 07024
Phone: (201) 346-0701
Fax: (201) 947-0107
E-mail: nrmsir@dpcdata.com

FT Interactive Data
Attn: NRMSIR
100 William Street
New York, NY 10038
Phone (212) 771-6999
Fax: (212) 771-7390
E-mail: nrmsir@ftid.com

A current list of all NRMSIRs can be obtained at any time from the Securities and Exchange Commission. The Commonwealth makes no representation as to the scope of services provided to the secondary market by any NRMSIR or as to the costs of any such services.

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The execution of this Official Statement has been authorized in the Resolutions.

Edward G Rendell

EDWARD G. RENDELL, Governor

Robert P. Casey, Jr.

ROBERT P. CASEY, JR., State Treasurer

Jack Wagner

JACK WAGNER, Auditor General

CERTIFICATE OF THE AUDITOR GENERAL
Pursuant to
ARTICLE VIII, SECTION 7(a)(4) and (c)
of the
CONSTITUTION OF PENNSYLVANIA
and
Section 304 of the Capital Facilities Debt Enabling Act

To the Governor and the General Assembly:

I, Jack Wagner, Auditor General of the Commonwealth of Pennsylvania, pursuant to the Pennsylvania Constitution Article VIII, (Section 7(a)(4) and Section 304 of Capital Facilities Debt Enabling Act (Act 1 of 1999) certify as follows:

The average annual tax revenues deposited in all funds in the five fiscal years ended preceding the date of February 28, 2005	$ 25,091,013,830
(i) The amount of outstanding net debt as of the end of the preceding fiscal year	$ 6,254,978,088
(ii) The amount of such net debt as of February 28, 2005	$ 6,133,685,057
(iii) The difference between the limitation upon all net debt outstanding as provided in Article VIII, Section 7 (a) (4) of the Constitution of Pennsylvania and the amount of such net debt as of the date of February 28, 2005	$ 37,775,589,146
(iv) The amount of such debt scheduled to be repaid during the remainder of the current fiscal year	$ 74,990,000
(v) The amount of debt authorized by law to be issued, but not yet incurred	$ 45,982,483,468
(vi) The amount of outstanding obligations excluded from outstanding debt as self sustaining pursuant to Article VIII, Section 7(c)(1), (2) and (3) of the Constitution of Pennsylvania	$ 4,355,713,310

IN TESTIMONY WHEREOF, I have set my hand and affixed the seal of the Auditor General, this 1st day of March 2005.

/s/Jack Wagner
JACK WAGNER
Auditor General
Commonwealth of Pennsylvania

(Seal)

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SELECTED DATA ON THE COMMONWEALTH OF PENNSYLVANIA

General

The Commonwealth of Pennsylvania is one of the most populous states, ranking sixth behind California, Texas, New York, Florida, and Illinois. Pennsylvania is an established state with a diversified economy. Pennsylvania had been historically identified as a heavy industrial state. That reputation has changed over the last thirty years as the coal, steel and railroad industries declined. The Commonwealth's business environment readjusted with a more diversified economic base. This economic readjustment was a direct result of a long-term shift in jobs, investment, and workers away from the northeast part of the nation. Currently, the major sources of growth in Pennsylvania are in the service sector, including trade, medical, health services, education and financial institutions.

Pennsylvania's agricultural industries remain an important component of the Commonwealth's economic structure, accounting for more than $5.5 billion in crop and livestock products annually. In 2004, agribusiness and food related industries reached record export sales surpassing $1.5 billion in economic activity. Over 59,000 farms form the backbone of the State's agricultural economy. Farmland in Pennsylvania includes over four million acres of harvested cropland and three million acres of pasture and farm woodlands - nearly one-third of the Commonwealth's total land area. Agricultural diversity in the Commonwealth is demonstrated by the fact that Pennsylvania ranks among the top ten states in the production of a variety of agricultural products. Agriculture exports have grown by more than 6% since 2002.

Pennsylvania's extensive public and private forests provide a vast source of material for the lumber, furniture, and paper products industries. The forestry and related industries accounts for 1.5% of employment with economic activity of nearly $4.5 billion in domestic and international trade. Additionally, the Commonwealth derives a good water supply from underground sources, abundant rainfall, and a large number of rivers, streams, and lakes. Other natural resources include major deposits of coal, petroleum, and natural gas. Annually, about 80 million tons of anthracite and bituminous coal, 180 billion cubic feet of natural gas, and about 1.8 million barrels of oil are extracted from Pennsylvania.

Pennsylvania is a Mid-Atlantic state within easy reach of the populous eastern seaboard and, as such, is the keystone to the Midwest. A comprehensive transportation grid enhances the Commonwealth's strategic geographic position. The Commonwealth's water systems afford the unique feature of triple port coverage, a deep-water port at Philadelphia, a Great Lakes port at Erie and an inland water port at Pittsburgh. Between air, rail, water, and road, Pennsylvania is easily accessible for both inter and intra state trade and commerce.

Population

The Commonwealth is highly urbanized. Of the Commonwealth's 2004 mid-year population estimate, 79 percent resided in the 15 Metropolitan Statistical Areas ("MSAs") of the Commonwealth. The largest MSAs in the Commonwealth are those that include the cities of Philadelphia and Pittsburgh, which together contain almost 44 percent of the State's total population. The population of Pennsylvania, 12.4 million people in 2004, according to the U.S. Bureau of the Census, represents a population growing slower than the nation with a higher portion than the nation or the region comprised of persons 45 or over. The following tables present the population trend from 1994 to 2004 and the age distribution of the population for 2004.

Population Trends
Pennsylvania, Middle Atlantic Region and the United States
1994-2004

	Total Population In Thousands			Total Population as a % of 1994 base		
As of July 1	PA	Middle Atlantic Region[a]	U.S.	PA	Middle Atlantic Region[a]	U.S.
1994	12,042	38,117	260,327	100%	100%	100%
1995	12,044	38,161	262,803	100	100	101
1996	12,038	38,191	265,228	100	100	102
1997	12,015	38,213	267,783	100	100	103
1998	12,002	38,257	270,248	99	100	104
1999	11,994	38,334	272,690	99	100	105
2000	12,286	38,715	282,178	102	101	108
2001	12,298	39,877	285,094	102	104	109
2002	12,328	40,038	287,974	102	105	110
2003	12,370	40,194	290,810	102	105	112
2004	12,406	40,332	293,655	103	105	113

[a] Middle Atlantic Region: Pennsylvania, New York, New Jersey
Source: U.S. Department of Commerce, Bureau of the Census

Population By Age Group — 2004
Pennsylvania, Middle Atlantic Region and the United States

Age	Pennsylvania	Middle Atlantic Region[a]	United States
Under 5 years	5.7%	6.3%	6.8%
5-24 years	26.6	26.7	28.0
25-44 years	26.7	28.4	28.8
45-64 years	25.7	24.9	24.1
65 years and over	15.3	13.7	12.3

[a] Middle Atlantic Region: Pennsylvania, New York, New Jersey.
Source: U.S. Department of Commerce, Bureau of the Census

Employment

Non-agricultural employment in Pennsylvania over the ten years ending in 2004 increased at an average annual rate of 0.8 percent compared with a 0.5 percent rate for the Middle Atlantic region and 1.3 percent rate for the U.S. The following table shows employment trends from 1995 through 2004.

Non-Agricultural Establishment Employment Trends
Pennsylvania, Middle Atlantic Region and the United States
1995-2004

	Total Establishment Employment In Thousands			Total Establishment Employment as a % of 1995 base		
Calendar Year	PA	Middle Atlantic Region[a]	U.S.	PA	Middle Atlantic Region[a]	U.S.
1995	5,253	17,268	117,298	100 %	100 %	100 %
1996	5,306	17,541	119,708	101	101	105
1997	5,406	17,919	122,776	103	104	107
1998	5,495	18,005	125,930	104	104	110
1999	5,586	18,148	128,993	106	105	113
2000	5,691	18,737	131,785	108	108	115
2001	5,682	18,733	131,826	108	108	115
2002	5,640	18,836	130,341	107	109	111
2003	5,611	19,155	129,999	106	111	110
2004	5,639	18,088	131,480	107	105	112

[a] Middle Atlantic Region: Pennsylvania, New York, New Jersey.
Source: U.S. Department of Labor, Bureau of Labor Statistics.

Non-manufacturing employment in Pennsylvania has increased in recent years and reached 87.8 percent of total employment by 2004. Consequently, manufacturing employment constitutes a diminished share of total employment within the Commonwealth. Manufacturing, contributing 12.2 percent of 2004 non-agricultural employment, has fallen behind both the services sector and the trade sector as the largest single source of employment within the Commonwealth. In 2004, the services sector accounted for 42.9 percent of all non-agricultural employment while the trade sector accounted for 16.6 percent. The following table shows trends in employment by sector for Pennsylvania from 2000 through 2004.

Non-Agricultural Establishment Employment by Sector
Pennsylvania
2000-2004
(In Thousands)

	CALENDAR YEAR									
	2000		2001		2002		2003		2004	
	Employees	%	Employees	%	Employees	%	Employees	%	Employees	%
Manufacturing:										
Durable..................	537.4	9.4	514.6	9.0	478.7	8.5	422.1	7.4	404.8	7.2
Non-Durable............	388.6	6.8	377.9	6.6	363.4	6.4	294.7	5.2	284.5	5.0
Total Manufacturing[d]......	926.0	16.3	892.5	15.7	842.1	14.9	716.8	12.6	689.3	12.2
Non-Manufacturing:										
Trade[a].................	1,275.2	22.4	1,272.0	22.3	1,266.0	22.4	900.9	15.8	937.2	16.6
Finance[b]...............	326.3	5.7	328.6	5.8	327.8	5.8	338.8	5.9	338.8	6.0
Services.................	1,872.4	32.9	1,907.6	33.5	1,921.7	34.0	2,476.9	43.5	2,420.3	42.9
Government............	726.9	12.8	729.8	12.8	740.4	13.1	771.4	13.5	759.5	13.5
Utilities[c]................	301.1	5.3	303.3	5.3	288.3	5.1	220.6	3.9	228.7	4.1
Construction............	251.1	4.4	248.4	4.4	248.7	4.4	254.5	4.5	248.2	4.4
Mining...................	19.4	0.3	19.0	0.3	17.0	0.3	18.0	0.3	17.5	0.3
Total Non-Manufacturing[d]	4,772.4	83.7	4,808.7	84.1	4,809.9	85.1	4,981.1	87.4	4,950.2	87.8
Total Employees[d][e]	5,698.4	100.0	5,701.2	99.8	5,652.0	100.0	5,697.9	100.0	5,639.5	100.0

[a] Wholesale and retail trade.
[b] Finance, insurance and real estate.
[c] Includes transportation, communications, electric, gas and sanitary services.
[d] Discrepancies occur due to rounding.
[e] Does not include workers involved in labor-management disputes.
Source: US Bureau of Labor Statistics

The following table presents the percentages of non-agricultural employment in various sectors in Pennsylvania and the United States in 2004.

Non-Agricultural Establishment Employment by Sector
Pennsylvania and the United States

	2004 Calendar Year	
	Pennsylvania	United States
Manufacturing..	12.2%	11.9%
Trade[a]...	16.6	16.1
Finance[b]	6.0	6.8
Services..	42.9	39.8
Government..	13.5	16.2
Utilities[c]	4.1	3.6
Construction..	4.4	5.2
Mining..	0.3	0.4
Total[d]	100.0%	100.0%

[a] Wholesale and retail trade.
[b] Finance, insurance and real estate.
[c] Includes transportation, communications, electric, gas and sanitary services.
[d] Discrepancies occur due to rounding.
Source: U.S. Department of Labor, Bureau of Labor Statistics.

Within the manufacturing sector of Pennsylvania's economy, which now accounts for less than one-eighth of total non-agricultural employment in Pennsylvania, the fabricated metals industries employed the largest number of workers. Employment in fabricated metals industries was 12.5 percent of Pennsylvania manufacturing employment but only 0.2 percent of total Pennsylvania non-agricultural employment in 2004. The following table shows trends in manufacturing employment by industry for Pennsylvania from 2000 through 2004.

Manufacturing Establishment Employment by Industry
Pennsylvania
2000-2004
(In Thousands)

	CALENDAR YEAR									
	2000		2001		2002		2003		2004	
	Employees	%	Employees	%	Employees	%	Employees	%	Employees	%
Durable Goods:										
Primary Metals................	67.8	8.0	62.9	7.8	57.9	7.8	44.0	6.1	40.8	5.9
Fabricated Metals............	89.6	9.1	86.8	9.2	81.5	9.2	90.5	12.6	86.2	12.5
Machinery (excluding electrical)....	99.4	11.3	92.9	11.4	83.4	11.4	56.5	7.9	54.3	7.9
Electrical Equipment..........	80.9	8.1	78.3	8.1	65.9	8.1	24.4	3.4	25.2	3.7
Transportation Equipment....	49.4	5.4	46.8	5.5	43.3	5.5	41.4	5.8	39.7	5.8
Stone, Clay and Glass.........	38.8	4.1	37.9	4.1	36.6	4.1	32.1	4.5	29.7	4.3
Other Durable Goods.........	111.5	11.3	109.0	11.5	108.1	11.5	133.2	18.6	128.9	18.7
Total Durable Goods[a]......	537.4	57.3	514.6	57.7	476.7	57.7	422.1	58.9	404.8	58.7
Non-Durable Goods:										
Apparel & Related Goods...	38.2	4.6	32.6	4.3	28.9	3.1	15.8	2.2	11.2	1.6
Food Products..................	84.3	9.1	85.0	9.0	85.3	9.1	73.6	10.3	75.8	11.0
Chemical Products............	70.2	7.2	72.3	7.3	72.8	7.8	60.6	8.5	58.9	8.5
Printing and Publishing......	82.3	8.8	80.5	8.7	78.0	8.3	40.1	5.6	38.8	5.6
Textile Products...............	21.5	2.4	18.6	2.3	16.8	1.8	16.8	2.3	16.8	2.4
Paper Products................	36.0	3.9	35.3	3.9	34.7	3.7	29.8	4.2	26.9	3.9
Other Non-Durable Goods...	63.5	6.7	64.3	6.8	61.4	6.6	58.0	8.1	56.1	8.1
Total Non-Durable Goods[a]	396.8	42.7	397.6	42.5	377.9	40.4	294.7	41.1	284.5	41.3
Total Manufacturing Employees[a]...............	940.7	100.0	929.6	100.0	936.4	100.0	716.8	100.0	689.3	100.0

[a] Discrepancies occur due to rounding
Source: U.S. Department of Labor, Bureau of Labor Statistics.

Unemployment

Pennsylvania's annual average unemployment rate was equivalent to the national average throughout the 1990's. Slower economic growth caused the unemployment rate in the Commonwealth to rise to 5.9 percent in 1995. The resumption of faster economic growth resulted in a decrease in the Commonwealth's annual unemployment rate to 4.2 percent in 2000. Since that time, the combination of a recession and slow economic growth has pushed the Commonwealth's annual unemployment rate to 5.5 percent through 2004. From 1995 through 2004, Pennsylvania's annual average unemployment rate was at or below the Middle Atlantic Region's average. Since 2001 Pennsylvania's annual average has been at or below both the Middle Atlantic and the United States. As of March 2005, the most recent month for which figures are available, Pennsylvania had a seasonally adjusted annual unemployment rate of 5.4 percent. The following table represents the annual non-adjusted unemployment rate in Pennsylvania, the Middle Atlantic Region, and the United States from 1995 through 2004.

Annual Average Unemployment Rate
Pennsylvania, Middle Atlantic Region and the United States
1995-2004

Calendar Year	Pennsylvania	Middle Atlantic Region[a]	United States
1995	5.9 %	6.2 %	5.6 %
1996	5.4	6.0	5.4
1997	5.1	5.8	4.9
1998	4.6	5.1	4.5
1999	4.4	4.8	4.2
2000	4.2	4.2	4.0
2001	4.7	4.7	4.7
2002	5.6	5.9	5.8
2003	5.7	6.1	6.0
2004	5.5	5.5	5.5

[a] Middle Atlantic Region: Pennsylvania, New York, New Jersey.
Source: U.S. Department of Labor, Bureau of Labor Statistics.

The following table presents the thirty largest non-governmental employers in Pennsylvania:

Commonwealth of Pennsylvania
Thirty Largest
Non-Governmental Employers
June 2004

Company	Rank	Company	Rank
Wal-Mart Associates	1	Heartland Employment	16
University of Pennsylvania	2	Pennsylvania Blue Shield	17
Pennsylvania State University	3	Lowe's Home Centers Inc	18
Giant Food Stores	4	Vanguard Group Inc.	19
University of Pittsburgh	5	Acme Markets Inc	20
United Parcel Service	6	Wachovia Bank	21
US Airways Inc	7	Verizon Co Inc.	22
UPMC Presbyterian	8	Temple University	23
Weis Markets Inc	9	May Department Stores	24
Merck & Co Inc	10	GMR Restaurants of Pennsylvania	25
The Home Depot USA Inc	11	Hershey Foods Corporation	26
KMART of Pennsylvania LP	12	Eckerd Corporation	27
PNC Bank, NA	13	Tenet Health System Inc Philadelphia	28
Sears Roebuck & Co	14	Mellon Bank, NA	29
Giant Eagle Inc	15	Rite Aid of Pennsylvania Inc	30

Source: Pennsylvania Department of Labor, Office of Employment Security.

Personal Income

Personal income in the Commonwealth for 2004 is $413.71 billion, an increase of 5.5 percent over the previous year. During the same period, national personal income increased at a rate of 5.7 percent. Based on the 2004 personal income estimates, per capita income for 2004 is at $33,348 in the Commonwealth compared to per capita income in the United States of $32,937. The following tables represent annual personal income data and per capita income from 1995 through 2004

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Personal Income
Pennsylvania, Mideast Region and the United States
1995-2004

	Total Personal Income Dollars in Millions			Total Personal Income As a % of 1995 base		
Year	PA	Mideast Region[a]	U.S.[b]	PA	Mideast Region[a]	U.S.
1995	$ 285,923	$1,193,865	$ 6,192,235	100 %	100 %	100 %
1996	299,001	1,255,345	6,538,103	104	105	105
1997	313,457	1,315,810	6,928,545	110	110	111
1998	330,733	1,400,562	7,418,497	116	117	118
1999	342,357	1,458,307	7,779,511	120	122	126
2000	364,837	1,580,733	8,422,074	128	132	132
2001	371,897	1,625,768	8,718,165	130	136	143
2002	380,161	1,649,048	8,868,261	133	138	148
2003	392,057	1,694,202	9,148,680	137	142	152
2004	413,730	1,784,887	9,672,205	145	150	156

[a] Mideast Region: Pennsylvania, New York, New Jersey, Maryland, District of Columbia, and Delaware.
[b] Sum of States.
Source: U.S. Department of Commerce, Bureau of Economic Analysis

Per Capita Income
Pennsylvania, Mideast Region and the United States
1995-2004

	Per Capita Income			As a % of U.S.	
Calendar Year	PA	Mideast Region[a]	U.S.	PA	Mideast Region[a]
1995	$ 23,439	$ 26,421	$ 23,255	101 %	114 %
1996	24,467	27,661	24,270	101	114
1997	25,635	28,868	25,412	101	114
1998	27,008	30,565	26,893	100	114
1999	27,916	31,630	27,880	100	113
2000	29,759	34,013	29,760	100	114
2001	30,752	34,952	30,413	101	115
2002	31,727	36,403	30,941	103	118
2003	31,998	36,243	31,632	101	115
2004	33,348	37,756	32,937	101	115

[a] Mideast Region: Pennsylvania, New York, New Jersey, Maryland, District of Columbia, and Delaware.
Source: U.S. Department of Commerce, Bureau of Economic Analysis

The following table presents growth rates in personal income and selected components of personal income for Pennsylvania, the Mideast Region and the United States from 2000 through 2004.

Annual Growth Rates
Personal Income and Selected Components of Personal Income
Pennsylvania, Mideast Region and the United States

Calendar Year	Pennsylvania	Mideast Region[a]	United States
Total Personal Income			
2000	6.5%	8.0 %	7.9%
2001	3.4	3.3	7.9
2002	3.2	1.7	1.7
2003	1.1	2.2	3.1
2004	4.8	5.5	5.7
Manufacturing			
2000	3.0%	6.3%	7.6%
2001	-1.5	-1.5	-3.2
2002	-18.2	-23.9	-14.1
2003	-14.8	0.7	1.0
2004	2.2	2.3	2.5
Trade[b]			
2000	5.8%	6.9%	7.0%
2001	1.6	1.0	1.0
2002	-14.7	-14.8	-17.4
2003	4.4	4.4	3.1
2004	3.6	5.1	4.6
Finance[c]			
2000	6.4%	10.8%	8.4%
2001	5.8	4.8	6.5
2002	3.2	-2.1	0.1
2003	6.5	2.3	6.3
2004	8.6	9.6	10.2
Services			
2000	7.4%	8.5%	9.7%
2001	6.4	6.3	5.7
2002	19.3	12.1	6.6
2003	10.5	7.8	8.0
2004	10.1	7.9	7.7
Utilities[d]			
2000	4.4%	5.9%	6.8%
2001	3.6	3.9	4.0
2002	-29.5	-19.2	-11.0
2003	2.8	2.4	1.7
2004	1.5	1.8	3.7
Construction			
2000	7.3%	9.2%	8.4%
2001	5.7	7.5	5.1
2002	12.2	9.6	7.4
2003	2.9	2.4	2.9
2004	4.3	5.4	7.6
Mining			
2000	0.1%	2.5%	10.4%
2001	4.7	5.0	9.5
2002	-11.0	-12.7	1.2
2003	8.7	8.9	12.6
2004	11.8	11.3	11.8

[a] Mideast Region: Delaware, District of Columbia, Maryland, Pennsylvania, New York, and New Jersey.
[b] Wholesale and retail trade.
[c] Finance, insurance and real estate.
[d] Includes transportation, communications, electric, gas and sanitary services.
Source: U.S. Department of Commerce, Bureau of Economic Analysis

The Commonwealth's average hourly wage rate of $16.95 for manufacturing and production workers compares to the national average of $17.75 for 2004. The following table presents the average hourly wage rates for 2000 through 2004.

Average Hourly Wages
Production Workers on Manufacturing Payrolls
Pennsylvania and the United States
2000-2004

Calendar Year	PA	U.S.
2000	$ 14.60	$ 13.76
2001	14.85	14.31
2002	15.99	15.20
2003	16.70	15.50
2004	16.95	17.75

Source: U.S. Department of Labor, Bureau of Labor Statistics

Market and Assessed Valuation of Real Property

Annually, the State Tax Equalization Board (the "STEB") determines an aggregate market value of all taxable real property in the Commonwealth. The STEB determines the market value by applying assessment to sales ratio studies to assessment valuations supplied by local assessing officials. The market values certified by the STEB do not include property that is tax exempt but do include an adjustment correcting the data for preferential assessments granted to certain farm and forestlands.

The table below shows the assessed valuation as determined and certified by the counties and the market value and the assessed to market value ratio determined by the STEB for real property over the last ten years. Increases in valuations shown below result from reassessment valuations by the counties, changes in property tax rolls and increases in the real value of existing property. In computing the market values for uneven-numbered years, the STEB is statutorily restricted to certifying only those changes in market value that result from properties added to or removed from the assessment rolls. The STEB is permitted to adjust the market valuation to reflect any change in real estate values or other economic change in value only in even-numbered years. This restriction accounts for the two-year pattern of market value changes apparent in the data below.

Valuations of Taxable Real Property
1994-2003

Year	Market Value[(a)]	Assessed Valuation	Ratio of Assessed Valuation to Market Value[(a)]
1994	$ 333,872,670,300	$ 98,004,141,038	29.4%
1995	338,550,074,600	101,088,995,085	29.9
1996	359,993,651,000	102,107,687,304	28.4
1997	366,096,581,900	123,734,109,457	37.2
1998	388,146,465,800	204,581,152,222	52.7
1999	390,136,860,900	208,896,190,899	53.5
2000	420,041,123,600	241,060,798,812	57.4
2001	430,102,389,400	310,111,943,560	72.1
2002	467,311,009,700	325,451,064,697	69.6
2003	478,362,689,800	348,726,965,926	72.9

(a) Value adjusted for difference between regular assessment and preferential assessment permitted on certain farm and forestlands.
Source: Annual Certifications by the State Tax Equalization Board July 2004.

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COMMONWEALTH GOVERNMENT AND FISCAL ADMINISTRATION

The government of the Commonwealth is composed of three separate branches. A general organization chart of the Commonwealth's government is shown on the following page.

Legislative Branch

The legislative branch consists of the General Assembly and its staff. The General Assembly is bicameral, composed of the Senate and the House of Representatives. The 50 members of the Senate serve staggered four-year terms and the 203 Representatives serve identical two-year terms. The General Assembly meets in regular session biannually beginning on the first Tuesday of January following elections. Special sessions may be called by the Governor on petition of a majority of the members of each house or whenever the Governor determines that public interest so requires. Legislative leadership includes majority and minority leaders in each house, a President Pro Tempore of the Senate and a Speaker of the House of Representatives.

Executive Branch

The Executive Branch is headed by five elected officials and encompasses 19 departments and approximately 37 independent commissions, boards, authorities and agencies.

The five elected officials are the Governor, the Lieutenant Governor, the Attorney General, the State Treasurer and the Auditor General. The Governor and the Lieutenant Governor are elected on the same ballot and serve a four-year term. The Governor is eligible to succeed himself for one term. The Auditor General, the Attorney General and the State Treasurer are elected for four-year terms in an even-year election held between gubernatorial elections.

The Governor is the chief executive officer of the Commonwealth. All departments except those of the State Treasurer, the Attorney General and the Auditor General are under the direct jurisdiction of the Governor. The head of each of the remaining departments is a Secretary who is appointed by the Governor and confirmed by a majority vote of the Senate. Each Secretary serves at the Governor's pleasure and is a member of the Governor's Cabinet.

The Lieutenant Governor presides over the Senate and serves as Acting Governor during the disability of the Governor and becomes Governor in the case of the death, conviction or impeachment, failure to qualify or resignation of the Governor.

The Attorney General is the chief law enforcement officer of the Commonwealth and is responsible for upholding and defending the constitutionality of all statutes. He is also responsible for reviewing the form and legality of all proposed rules and regulations, deeds, leases and contracts to be executed by Commonwealth agencies. The Office of Attorney General is under the Attorney General's direct jurisdiction.

The State Treasurer is charged with receiving, depositing and investing all Commonwealth funds and is responsible for the pre-audit approval of all requisitions for the disbursements of monies in the State Treasury. The Treasury Department is under the State Treasurer's direct jurisdiction.

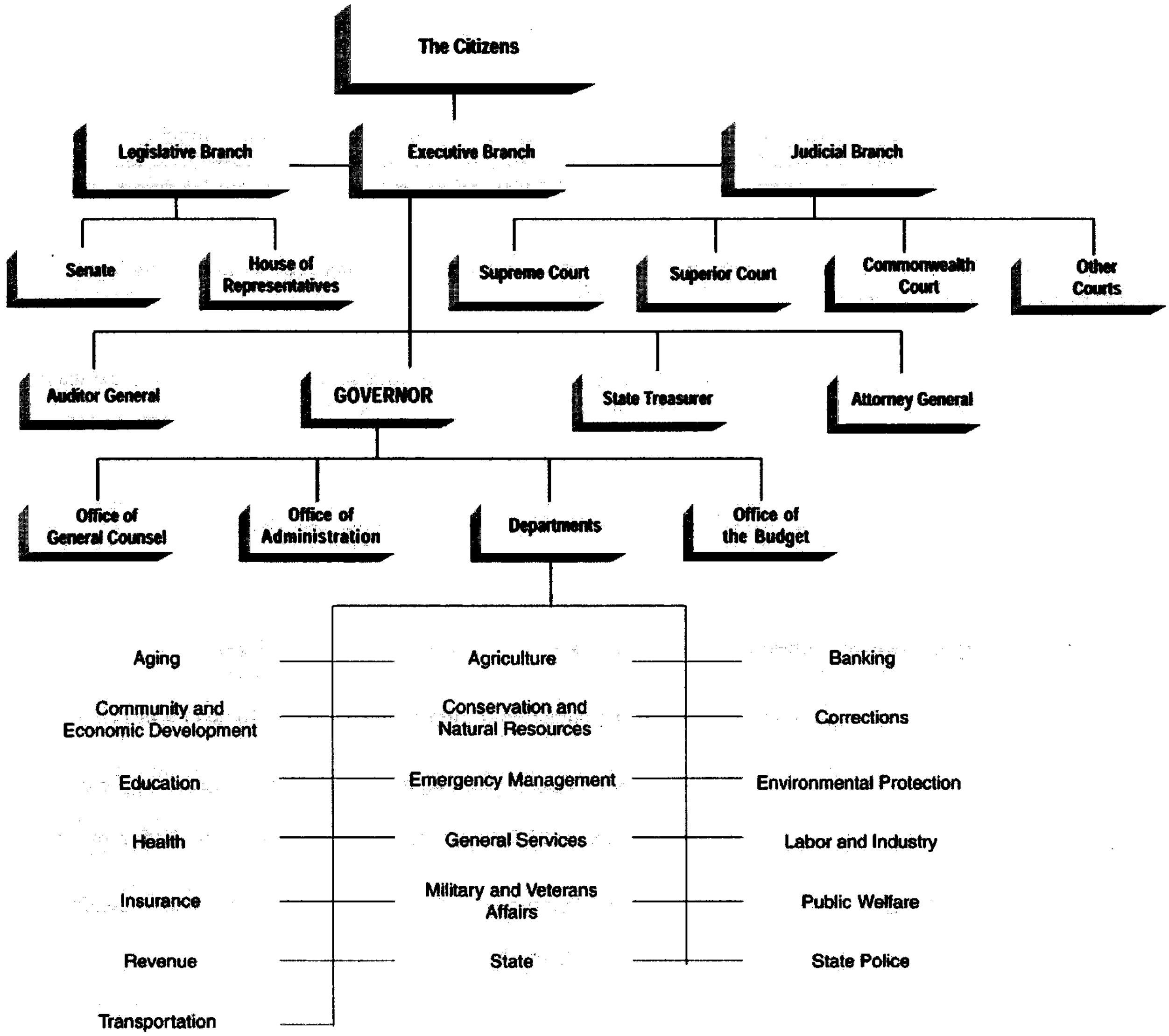
The Auditor General is charged with making audits of completed financial transactions. The Department of the Auditor General is under the Auditor General's direct jurisdiction.

Activities of state government are also conducted by various independent commissions, boards, authorities and agencies created by statute and not under the direct jurisdiction of the executive and legislative branches.

Judicial Branch

The judicial power of the Commonwealth is vested in a unified judicial system consisting of a Supreme Court and various other courts of original and appellate jurisdiction which are under the supervision and authority of the Supreme Court. All justices, judges and district justices are elected to office.

Commonwealth of Pennsylvania
Organization Chart



AGENCIES

Higher Education Assistance
Housing Finance
Interstate Agencies

AUTHORITIES

Commonwealth Financing
Energy Development
Higher Education Facilities
Industrial Development
Infrastructure Investment
Minority Business Development
Public School Building

BOARDS

Claims
Environmental Hearing
Gaming Control
Finance and Revenue
Liquor Control
Milk Marketing
Municipal Retirement
Pardons
Probation and Parole
Public School Employees' Retirement
State Employees' Retirement
Tax Equalization

COMMISSIONS

Civil Service
Crime and Delinquency
Ethics
Fish and Boat
Game
Harness Racing
Historical and Museum
Horse Racing
Human Relations
Juvenile Court Judges
Public Employee Retirement
Public Television Network
Public Utility
Securities
Turnpike

Fiscal Organization

Each branch of the Commonwealth's government is responsible for its respective fiscal operations subject to restrictions embodied in the Constitution, the Administrative Code, and the Fiscal Code. Such restrictions are enforced and other central administrative functions are provided by four departments: the Offices of Budget and Administration ("OBA"), the Treasury Department, the Department of Revenue and the Department of the Auditor General. OBA is an administrative office within the Governor's offices. The Secretary of the Budget and Administration is appointed by the Governor and is responsible for the operations of the office. The Department of Revenue is led by the Secretary of Revenue, who is appointed by the Governor subject to the advice of the Senate. The Treasury Department and the Department of the Auditor General are headed by the respective elected officials.

OBA monitors the operation of the Commonwealth's departments, operates a central accounting system, compiles and publishes the Commonwealth's financial reports, assists in the preparation and publication of the budget, coordinates capital improvements and is responsible for the issuance of the Commonwealth's debt and for personnel policy and programs, management policy and organizational structure, data processing service, and electronic data processing policy and planning. The Treasury Department receives, invests and disburses all funds and maintains central cash records. The Department of Revenue administers the collection of most taxes. The Department of the Auditor General oversees the examination of the majority of financial transactions.

Commissions, authorities and agencies that are both independent by statute and financially self-supporting, operate autonomously although their capital projects and financing are reviewed by OB and included in the capital budget.

The Budgetary Process

The Commonwealth operates on a fiscal year beginning July 1 and ending June 30. For example, "fiscal year 2005" refers to the fiscal year ending on June 30, 2005.

The budget process commences in September, nine months prior to the beginning of the fiscal year, as departments formulate their initial budgets in response to Program Policy Guidelines issued by the Governor and hold preliminary hearings with OBA and other members of the Governor's staff. By November 1, formal budget requests are submitted to OBA by all government departments and other institutions requesting appropriations. OBA, under the direction of the Secretary of Budget and Administration, reviews the requests through November and December and may hold formal hearings.

The Department of Revenue, in conjunction with OBA, prepares revenue estimates. In the preparation of such estimates, internal analysis, information from selected departments and econometric analysis are utilized. The Commonwealth subscribes to economic forecasts prepared by Global Insight for national and Pennsylvania economic data that are used to estimate economically sensitive Commonwealth revenues. Other econometric forecasts are also consulted.

The Constitution requires that the Governor submit annually to the General Assembly a budget consisting of three parts:

(a) a balanced operating budget for the ensuing fiscal year setting forth proposed expenditures and estimated revenues from all sources and, if estimated revenues and available surplus are less than proposed expenditures, recommending specific additional sources of revenue sufficient to pay the deficiency;

(b) a capital budget for the ensuing fiscal year setting forth in detail proposed expenditures to be financed from the proceeds of obligations of the Commonwealth or of its agencies or authorities or from operating funds; and

(c) a financial plan for not less than the succeeding five fiscal years, which includes for each year (i) projected operating expenditures classified by department or agency and by program, and estimated revenues by major categories from existing and additional sources, and (ii) projected expenditures for capital projects specifically itemized by purpose and their proposed sources of financing.

All funds received by the Commonwealth are subject by statute to appropriation in specific amounts by the General Assembly or by executive authorizations by the Governor. The Governor's budget encompasses both annual appropriations and executive authorizations.

The Governor is required to submit the proposed budget as soon as possible after the organization of the General Assembly but not later than the first full week in February except in his first year of office. The Governor's submission begins with the Budget Message delivered in joint session. The budget in the form of a proposed bill is delivered to the appropriations committee of one of the houses. Hearings are held on the bills constituting the budget. In an iterative process, bills are reported from committee to floor and considered in and between houses.

The operating budget is considered in the form of the General Appropriations Bill and its supplements. The Bill is limited to appropriations for debt service, public schools and the executive, legislative and judicial branches. Its supplements cover appropriations from special revenue funds not included in the General Appropriations Bill and for such subjects as capital projects funded from current revenues. The operating budget also includes single subject bills covering appropriations made to any charitable or educational institutions not under the absolute control of the Commonwealth other than certain State-owned schools ("non-preferred appropriations").

The Constitution mandates that total operating budget appropriations made by the General Assembly may not exceed the sum of (a) the actual and estimated revenues in a given year, and (b) the surplus of the preceding year. The Constitution further specifies that a surplus of operating funds at the end of the fiscal year shall be appropriated. That is, if funds remain from the end of a fiscal year they must be appropriated for the ensuing year. Also, if a deficit occurs at year-end, funds must be provided for such a deficit.

Pursuant to the Administrative Code, the executive branch establishes the revenue estimates used in the budget. In practice, the revenue estimates used to balance the operating budget consist of the appropriate fund's available surplus and its estimated cash receipts for the fiscal year as well as net accruals. Appropriation lapses estimated to occur during the year or at year-end are not included; lapses are not available for re-appropriation until they occur.

Under this budgetary process a deficit can occur if revenues are less than those estimated in the budget and the shortfall is not offset by any unappropriated surplus or by appropriation lapses during or at the end of the year or by legislative action to increase revenues or reduce appropriation.

The Administrative Code was amended in 1978 to provide for stronger executive control of expenditures. All departments under the Governor's jurisdiction may be required to submit estimates of expenditures during the ensuing month, quarter or any other such period as requested by the Governor. These estimates are subject to the approval of the Secretary of Budget and Administration. The Governor is empowered to request the State Treasurer to withhold funds from any such department not spending within such estimates. The Secretary of Budget and Administration is empowered to set personnel levels for departments. Departments are required to provide personnel data monthly so that the Commonwealth's computerized data file on personnel levels can be maintained and used to monitor the Commonwealth's largest operating expense.

The proposed capital budget is considered in the form of the Capital Budget Bill and its supplements. The capital budget determines limits for the amount of debt that can be issued in that fiscal year for categories of capital projects, itemizes for funding all capital projects not previously itemized, authorizes the issuance of debt to finance these projects and appropriates the proceeds from the issuance of debt.

All appropriations require the majority vote of all members in each house except for non-preferred appropriations and appropriations from the Tax Stabilization Reserve Fund and from the Health Endowment Account portion of the Tobacco Settlement Fund which require passage by a two-thirds vote. During the legislative process, the General Assembly may add, change or delete any items in the budget proposed by the Governor. Once the bills constituting the budget have passed both houses and are returned to the Governor, he may either veto bills or item veto appropriations within bills. A gubernatorial veto can be overridden only by a two-thirds majority of all members of each house.

In the event that the General Assembly fails to pass or the Governor fails to sign an appropriations act prior to July 1 of any fiscal year for that fiscal year, the Pennsylvania Constitution, the laws of Pennsylvania and certain state and federal court decisions provide that the Commonwealth may continue during such un-budgeted fiscal year to make debt service payments, payments for mandated federal programs such as cash assistance and payments related to the health and safety of the citizens of the Commonwealth such as police and correctional services.

Accounting and Budgetary Controls

Every department of the executive branch that receives appropriations from the Commonwealth, with the exception of the Treasury Department and the Departments of the Auditor General and the Attorney General, has a comptroller appointed by and under the direct jurisdiction of the Governor. These agencies share a centralized encumbrance-based accounting system supervised by OBA. Executive departments operating separate additional accounting systems include the Department of Transportation for the Motor License Fund, the Liquor Control Board for the State Stores Fund and the Department of Labor and Industry for the payment of unemployment compensation benefits. Officials within the Treasury Department, the Departments of the Auditor General and the Attorney General and the judicial and legislative branches administer individual operations under the jurisdiction of their respective areas.

Expenditure control occurs at two levels. The first is by appropriations and is enforced by the State Treasurer and individual comptrollers. The second is by allocations and allotments and is enforced by OBA for all departments receiving appropriations, except for the legislative branch.

Departments receive authorization to spend and commit funds in the form of appropriations for a specific amount, purpose and time period. Funds appropriated to a single department may be in one or more appropriations as the General Assembly determines. When multiple appropriations to a department are enacted, separate appropriations are made for general operating expenses, special outlays and for specific programs or groupings thereof. The degree to which a department's total appropriations are itemized may vary, but control is exercised over both total and individual appropriations.

The Constitution requires that with the exceptions named, monies may be paid from the Treasury only if appropriated by law. Accordingly, when a voucher is submitted to the State Treasurer, a check will not be issued unless the amount is within the balance of the agency's total appropriation.

Departments are prevented by their comptrollers from incurring obligations in excess of their unexpended individual appropriations by an encumbrance system. Encumbrance control prevents spending beyond remaining individual appropriation balances. When a commitment or obligation is incurred, for example, when a contract or purchase order is signed, the required portion of the corresponding appropriation is reserved. This reserving of funds is called the encumbrance procedure. All obligations anticipating future disbursement of cash in the fiscal year require an encumbrance, with the exception of debt service payments. Since a debt service appropriation is used for no purpose other than debt service, an encumbrance is not necessary.

All individual appropriations are allocated by OBA to departments by major object groups. For example, a department's appropriation for operating expenses may be broken down into such major object groups as personnel service, operating expenses and supplies, etc. Additionally, major object groups are subdivided into minor object groups. For example, personnel service would be broken down into salaries, benefits, overtime, etc. Department expenditures are monitored to insure that expenditures within an allocation do not exceed the designated totals. The departments, however, are free to adjust their expenditures between minor object groups as long as they do not exceed the major object group allocation. OBA can monitor department expenditures against their allocations on a continuing basis as the records of departments under the Governor's jurisdiction can be accessed from the central system while those of most other departments and branches are provided monthly.

In addition to the preceding controls, another check is provided by the financial reporting process. All department records are reconciled by OBA on a monthly basis with the Treasury Department's records of cash transactions and with the Department of Revenue's records of cash collections.

Audits

The Constitution requires that the financial affairs of any entity receiving appropriations and all department boards, commissions, agencies, instrumentalities, authorities and institutions of the Commonwealth be subject to audits made in accordance with generally accepted auditing standards. Any Commonwealth officer whose approval is necessary for any transaction may not be charged with the function of auditing that transaction after its occurrence.

The Department of the Auditor General has the responsibility for auditing all state-related financial transactions except its own, those of the legislative and judicial branches, and boards and commissions on which the Auditor General serves and those of certain funds. At least one audit must be made annually of the fiscal affairs of the executive branch. Audits of the Commonwealth General Purpose Financial Statements since fiscal 1985 have been performed jointly by the Department of the Auditor General and an independent public accounting firm.

The Treasury Department is required to pre-audit all requests for expenditures to insure that they are in accordance with law. In addition, OBA conducts, as a matter of administrative policy, periodic audits of comptrollers under the Governor's jurisdiction and performance audits of state and federal programs.

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APPENDIX D

INFORMATION REGARDING THE DEPOSITORY TRUST COMPANY AND ITS BOOK-ENTRY SYSTEM

The information that follows concerning The Depository Trust Company, New York, New York ("DTC") and the book-entry only system described below is based solely on information furnished by DTC and is not, and should not be construed as, a representation by the Commonwealth as to its accuracy, completeness or otherwise.

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants ("Direct Participants") deposit with DTC. DTC also facilitates the settlement among Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Direct Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc., and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks, and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). The rules applicable to DTC and its Direct Participants are on file with the Securities and Exchange Commission.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. or such other name as requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Beneficial Owners of the Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. Beneficial Owners of Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners, or in the alternative, Beneficial Owners may wish to provide their names and addresses to the Loan and Transfer Agent and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor such other DTC nominee) will consent or vote with respect to the Bonds. Under its usual procedures, DTC will mail an Omnibus Proxy to the Commonwealth as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Bonds will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Commonwealth or its agent, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Direct and Indirect Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Direct and Indirect Participants and not of DTC (nor its nominee), the Loan and Transfer Agent, or the Commonwealth, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Commonwealth or the Loan and Transfer Agent, disbursement of such payments to Direct Participants is the responsibility of DTC, and disbursement of such payments to the Beneficial Owners is the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the Commonwealth or the Loan and Transfer Agent. Under such circumstances, in the event that a successor securities depository is not obtained, Bond certificates are required to be printed and delivered.

The foregoing information concerning DTC and DTC's book-entry system has been obtained from information furnished by DTC. No representation or warranty is made by the Commonwealth as to the accuracy or completeness of such information.

The Commonwealth may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

For so long as the Bonds are registered in the name of DTC, or its nominee Cede & Co., the Commonwealth and the Loan and Transfer Agent will treat Cede & Co. as the registered owner of the Bonds for all purposes, including payments, notices and voting.

Neither the Commonwealth nor the Loan and Transfer Agent shall have any responsibility or obligation to any Direct or Indirect Participant or Beneficial Owner with respect to (a) the accuracy of any records maintained by DTC or any Direct or Indirect Participant with respect to any beneficial ownership interest in any Bonds; (b) the payment by any Direct or Indirect Participant of any amount due to any Beneficial Owner in respect of the principal of, premium, if any, and interest on the Bonds; (c) the delivery or timeliness of delivery by any Direct or Indirect Participant of any notice to any Beneficial Owner of any notice with respect to the Bond, including, without limitation any notice of redemption; or (d) other action taken by DTC or Cede & Co., including the effectiveness of any action taken pursuant to an Omnibus Proxy.

SELECTED CONSTITUTIONAL PROVISIONS RELATING TO THE FINANCES OF THE COMMONWEALTH

Article VIII — TAXATION AND FINANCE

Commonwealth Indebtedness

Section 7. (a) No debt shall be incurred by or on behalf of the Commonwealth except by law and in accordance with the provisions of this section.

(1) Debt may be incurred without limit to suppress insurrection, rehabilitate areas affected by man-made or natural disaster, or to implement unissued authority approved by the electors prior to the adoption of this article.

(2) The Governor, State Treasurer and Auditor General, acting jointly, may (i) issue tax anticipation notes having a maturity within the fiscal year of issue and payable exclusively from revenues received in the same fiscal year, and (ii) incur debt for the purpose of refunding other debt, if such refunding debt matures within the term of the original debt.

(3) Debt may be incurred without limit for purposes specifically itemized in the law authorizing such debt, if the question whether the debt shall be incurred has been submitted to the electors and approved by a majority of those voting on the question.

(4) Debt may be incurred without the approval of the electors for capital projects specifically itemized in a capital budget if such debt will not cause the amount of all net debt outstanding to exceed one and three-quarters times the average of the annual tax revenues deposited in the previous five fiscal years as certified by the Auditor General. For the purposes of this subsection, debt outstanding shall not include debt incurred under clauses (1) and (2) (i), or debt incurred under clause (2) (ii) if the original debt would not be so considered, or debt incurred under subsection (3) unless the General Assembly shall so provide in the law authorizing such debt.

(b) All debt incurred for capital projects shall mature within a period not to exceed the estimated useful life of the projects as stated in the authorizing law, and when so stated shall be conclusive. All debt, except indebtedness permitted by clause (2) (i), shall be amortized in substantial and regular amounts, the first of which shall be due prior to the expiration of a period equal to one-tenth the term of the debt.

(c) As used in this section, debt shall mean the issued and outstanding obligations of the Commonwealth and shall include obligations of its agencies or authorities to the extent they are to be repaid from lease rentals or other charges payable directly or indirectly from revenues of the Commonwealth. Debt shall not include either (1) that portion of obligations to be repaid from charges made to the public for the use of the capital projects financed, as determined by the Auditor General, or (2) obligations to be repaid from lease rentals or other charges payable by a school district or other local taxing authority, or (3) obligations to be repaid by agencies or authorities created for the joint benefit of the Commonwealth and one or more other State governments.

(d) If sufficient funds are not appropriated for the timely payment of the interest upon and installments of principal of all debt, the State Treasurer shall set apart from the first revenues thereafter received applicable to the appropriate fund a sum sufficient to pay such interest and installments of principal, and shall so apply the money so set apart. The State Treasurer may be required to set aside and apply such revenues at the suit of any holder of Commonwealth obligations.

Commonwealth Credit Not to be Pledged

Section 8. The credit of the Commonwealth shall not be pledged or loaned to any individual, company, corporation or association nor shall the Commonwealth become a joint owner or stockholder in any company, corporation or association.

Municipal Debt Not to be Assumed by Commonwealth

Section 9. The Commonwealth shall not assume the debt, or any part thereof, of any county, city, borough, incorporated town, township or any similar general purpose unit of government unless such debt shall have been incurred to enable the Commonwealth to suppress insurrection or to assist the Commonwealth in the discharge of any portion of its present indebtedness.

Audit

Section 10. The financial affairs of any entity funded or financially aided by the Commonwealth, and all departments, boards, commissions, agencies, instrumentalities, authorities and institutions of the Commonwealth, shall be subject to audits made in accordance with generally accepted auditing standards.

Any Commonwealth officer whose approval is necessary for any transaction relative to the financial affairs of the Commonwealth shall not be charged with the function of auditing that transaction after its occurrence.

Gasoline Taxes and Motor License Fees Restricted

Section 11. (a) All proceeds from gasoline and other motor fuel excise taxes, motor vehicle registration fees and license taxes, operators' license fees and other excise taxes imposed on products used in motor transportation after providing there from for (a) cost of administration and collection, (b) payment of obligations incurred in the construction and reconstruction of public highways and bridges shall be appropriated by the General Assembly to agencies of the State or political subdivisions thereof; and used solely for construction, reconstruction, maintenance and repair of and safety on public highways and bridges and costs and expenses incident thereto, and for the payment of obligations incurred for such purposes, and shall not be diverted by transfer or otherwise to any other purpose, except that loans may be made by the State from the proceeds of such taxes and fees for a single period not exceeding eight months, but no such loan shall be made within the period of one year from any preceding loan, and every loan made in any fiscal year shall be repayable within one month after the beginning of the next fiscal year.

(b) All proceeds from aviation fuel excise taxes, after providing therefrom for the cost of administration and collection, shall be appropriated by the General Assembly to agencies of the State or political subdivisions thereof and used solely for: the purchase, construction, reconstruction, operation, and maintenance of airports and other air navigation facilities; aircraft accident investigation; the operation, maintenance and other costs of aircraft owned or leased by the Commonwealth; any other purpose reasonably related to air navigation including but not limited to the reimbursement of airport property owners for property tax expenditures; and costs and expenses incident thereto and for the payment of obligations incurred for such purposes, and shall not be diverted by transfer or otherwise to any other purpose.

Governor's Budgets and Financial Plan

Section 12. Annually, at the times set by law, the Governor shall submit to the General Assembly:

(a) A balanced operating budget for the ensuing fiscal year setting forth in detail (i) proposed expenditures classified by department or agency and by program and (ii) estimated revenues from all sources. If estimated revenues and available surplus are less than proposed expenditures, the Governor shall recommend specific additional sources of revenue sufficient to pay the deficiency and the estimated revenue to be derived from each source;

(b) A capital budget for the ensuing fiscal year setting forth in detail proposed expenditures to be financed from the proceeds of obligations of the Commonwealth or of its agencies or authorities or from operating funds; and

(c) A financial plan for not less than the next succeeding five fiscal years, which plan shall include for each such fiscal year:

(i) Projected operating expenditures classified by department or agency and by program, in reasonable detail, and estimated revenues, by major categories, from existing and additional sources; and

(ii) Projected expenditures for capital projects specifically itemized by purpose, and the proposed sources of financing each.

Appropriations

Section 13. (a) Operating budget appropriations made by the General Assembly shall not exceed the actual and estimated revenues and surplus available in the same fiscal year.

(b) The General Assembly shall adopt a capital budget for the ensuing fiscal year.

Surplus

Section 14. All surplus of operating funds at the end of the fiscal year shall be appropriated during the ensuing fiscal year by the General Assembly.

Project "70"

Section 15. In addition to the purposes stated in article eight, section seven of this Constitution, the Commonwealth may be authorized by law to create debt and to issue bonds to the amount of seventy million dollars ($70,000,000) for the acquisition of land for State parks, reservoirs and other conservation and recreation and historical preservation purposes and for participation by the Commonwealth with political subdivisions in the acquisition of land for parks, reservoirs and other conservation and recreation and historical preservation purposes, subject to such conditions and limitations as the General Assembly may prescribe.

Land and Water Conservation and Reclamation Fund

Section 16. In addition to the purposes stated in article eight, section seven of this Constitution, the Commonwealth may be authorized by law to create debt and issue bonds in the amount of five hundred million dollars ($500,000,000) for a Land and Water Conservation and Reclamation Fund to be used for the conservation and reclamation of land and water resources of the Commonwealth, including the elimination of acid mine drainage, sewage, and other pollution from the streams of the Commonwealth, the provision of State financial assistance to political subdivisions and municipal authorities of the Commonwealth of Pennsylvania for the construction of sewage treatment plants, the restoration of abandoned strip-mined areas, the control and extinguishment of surface and underground mine fires, the alleviation and prevention of subsidence resulting from mining operations, and the acquisition of additional lands and the reclamation and development of park and recreational lands acquired pursuant to the authority of Article VIII, section 15 of this Constitution, subject to such conditions and liabilities as the General Assembly may prescribe.

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APPENDIX F

PROPOSED FORM OF OPINION OF THE ATTORNEY GENERAL OF THE COMMONWEALTH OF PENNSYLVANIA

June 9, 2005

TO THE GOVERNOR, AUDITOR GENERAL
AND STATE TREASURER AS THE ISSUING
OFFICIALS OF THE COMMONWEALTH:

Re: Commonwealth of Pennsylvania General Obligation Bonds, First Series of 2005

This opinion is furnished to you in connection with the issuance and sale by the Commonwealth of Pennsylvania (the "Commonwealth") on the date hereof of $200,000,000 aggregate principal amount of Commonwealth of Pennsylvania General Obligation Bonds, First Series of 2005 (the "Bonds"). The Bonds are dated the date of issuance and delivery. The Bonds are issued as fully registered bonds without coupons in the denomination of $5,000 or any integral multiple thereof within a maturity and will bear interest from June 9, 2005, payable semi-annually on January 1 and July 1 of each year commencing January 1, 2006, until the obligation with respect to the payment of such principal shall have been discharged.

The Bonds are authorized and issued pursuant to and in full compliance with the provisions, restrictions and limitations of Section 7 of the Constitution; the laws of the Commonwealth, including the Capital Facilities Debt Enabling Act, Act No. 1999-1, approved February 9, 1999, as amended by Act No. 2002-130, approved October 28, 2002, Act No. 2003-49, approved December 23, 2003, and Act No. 2004-67, approved July 4, 2004, annual capital budget bills and various bond authorization bills enacted by the General Assembly. The Bonds are also authorized and issued pursuant to resolutions adopted by the Governor, the Auditor General, and the State Treasurer (the "Issuing Officials") on May 13, 2005, and May 24, 2005 (collectively, the "Resolutions").

The Resolutions, among other things, authorize the issuance and sale of the Bonds, and prescribe the forms thereof, the manner of bidding therefor and the forms of the bidding documents used in connection with the issuance and sale of the Bonds.

Under Section 7(a)(4) of Article VIII of the Constitution, the Commonwealth may incur debt without the approval of the electors to finance such projects, if such debt will not cause the amount of all debt outstanding (as defined for the purposes of that Section) to exceed one and three-quarters times the average of the annual tax revenues deposited in all funds in the previous five fiscal years, as certified by the Auditor General.

I have examined Article VIII, Section 7 of the Constitution and the statutes referred to above, specimens of the Bonds, the Resolutions, and the other certificates delivered today at the Closing and such other matters and documents as I deemed necessary or appropriate.

I am of the opinion that:

1. Section 7 of Article VIII of the Constitution has been duly approved and adopted and has become part of the Constitution of Pennsylvania, and the statutes referred to above have been duly and properly enacted.

2. Pursuant to full and adequate legal power conferred upon them by the Constitution and the statutes referred to above, the Governor, the Auditor General and the State Treasurer have duly adopted the Resolutions and have validly taken all other necessary and proper action to issue and sell the Bonds, and the Bonds have been validly authorized, issued and sold pursuant to proper and appropriate action of such officials.

3. The Bonds are lawful, valid, direct and general obligations of the Commonwealth, and the full faith and credit of the Commonwealth is pledged for the payment of interest thereon as the same shall become due and for the payment of the principal thereof at maturity.

4. Under the provisions of Section 2901 of the Tax Reform Code of 1971, as amended, the Bonds and the interest thereon are exempt from taxation for state and local purposes within the Commonwealth, but this exemption does not extend to (a) gift, estate, succession or inheritance taxes or (b) any other taxes not levied or assessed directly on the Bonds or the interest thereon.

5. The Commonwealth has the power to provide for the payment of the principal of and interest on the Bonds by levying unlimited ad valorem taxes upon all taxable property within the Commonwealth and excise taxes upon all taxable transactions within the Commonwealth, uniform on the same class of subjects, except gasoline and other motor fuel excise taxes, motor vehicle registration fees and license taxes, and operators' license fees and other excise taxes imposed on products used in motor transportation, and aviation fuel excise taxes, the proceeds of which are limited to certain special purposes by Section 11 of Article VIII of the Constitution.

6. If sufficient funds are not appropriated for timely payment of interest on and installments of principal of the Bonds, the Constitution requires the State Treasurer to set apart from the first revenues thereafter received applicable to the appropriate fund, a sum sufficient to pay such interest and installments of principal and to apply said sum to such purposes, and the State Treasurer may be required to set aside and apply such revenues at the suit of the holder of any of the Bonds.

Very truly yours,

Tom Corbett
Attorney General

Proposed Form of Opinion of Bond Counsel

[Date of Issuance of Bonds]

To: The Governor, the Auditor General and the State Treasurer, as the Issuing Officials of the Commonwealth of Pennsylvania

Re: Commonwealth of Pennsylvania General Obligation Bonds, First Series of 2005

We have acted as Bond Counsel to the Commonwealth of Pennsylvania (the "Commonwealth") in connection with the issuance and sale by the Commonwealth of $200,000,000 aggregate principal amount of its General Obligation Bonds, First Series of 2005 (the "Bonds"). The Bonds are authorized and issued pursuant to and in full compliance with the provisions, restrictions and limitations of the Constitution and laws of the Commonwealth, including Article VIII, Section 7 of the Constitution of the Commonwealth, the Capital Facilities Debt Enabling Act (Act No. 1999-1, approved February 9, 1999, as amended), the Capital Budget Act of 2004-2005 (Act No. 2004-182, approved November 30, 2004), and certain other capital budget acts, debt authorizing acts and legislation as described in the Resolutions (as hereinafter defined). The Bonds are also authorized and issued pursuant to certain resolutions adopted by the Governor, the Auditor General and the State Treasurer (collectively, the "Issuing Officials") on May 13, 2005 and May __, 2005, respectively (together, the "Resolutions"). The Resolutions, among other things, authorize the issuance and sale of the Bonds and prescribe the respective forms thereof, the manner of bidding therefor and the forms of the bidding documents used in connection with the issuance and sale of the Bonds.

In our capacity as Bond Counsel to the Commonwealth, we have examined the proceedings relating to the authorization and issuance of the Bonds, including, among other things, (a) the Resolutions; (b) a certificate of the Auditor General as to tax revenues and outstanding debt; (c) an opinion of The Honorable Tom Corbett, Attorney General of the Commonwealth; and (d) certificates of the Commonwealth as to certain material factual matters (including a certificate of the Commonwealth intended to satisfy certain provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and applicable Treasury Regulations, and certificates of the Commonwealth and U.S. Bank National Association, as Loan and Transfer Agent, with respect to the execution and authentication of the Bonds and certain other matters.

In rendering the opinions set forth below, we have assumed the genuineness, authenticity, truthfulness and completeness of all documents, records and other instruments we have examined and the genuineness of all signatures thereon. We have not undertaken to verify by independent investigation the factual matters set forth therein. Except as set forth in paragraphs 6 and 8 below, our opinions are given only with respect to the laws of the Commonwealth as enacted and construed on the date hereof.

On the basis of the foregoing and subject to the limitations and qualifications hereinafter stated, We are of the opinion that, under existing law:

1. The Bonds are valid, binding and enforceable direct obligations of the Commonwealth, and the full faith and credit of the Commonwealth are pledged for the payment of interest thereon as the same shall become due and the payment of the principal thereof at maturity.

2. The principal amount of the Bonds is within all applicable debt and other limitations fixed by the Constitution and the laws of the Commonwealth.

3. The Bonds have been validly authorized, issued and sold pursuant to all necessary action of the Issuing Officials.

4. The Commonwealth has the power to provide for the payment of principal of and interest on the Bonds by levying unlimited ad valorem taxes upon all taxable property within the Commonwealth and excise taxes upon all taxable transactions within the Commonwealth, uniform on the same class of subjects, except gasoline and other motor fuel excise taxes, motor vehicle registration fees and license taxes and operators' license fees and other excise taxes imposed on products used in motor transportation and aviation fuel excise taxes, the proceeds of which are limited to certain special purposes by Article VIII, Section 11 of the Constitution of the Commonwealth.

5. If sufficient funds are not appropriated for the timely payment of interest upon and installment of principal of the Bonds, the Constitution of the Commonwealth requires the State Treasurer to set apart from the first revenues thereafter received applicable to the appropriate fund a sum sufficient to pay such interest and installments of principal and to apply said sum to such purposes, and the State Treasurer may be required to set aside and apply such revenues at the suit of the holder of any of the Bonds.

6. Interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. It should be noted, however, that with respect to certain corporations (as defined for federal income tax purposes), such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax imposed on such corporations. The opinion set forth in this paragraph is subject to the condition that the Commonwealth comply with all requirements of the Code that must be satisfied subsequent to the issuance of the Bonds in order that interest thereon be (or continue to be) excluded from gross income for federal income tax purposes. Failure to comply with certain of such requirements could cause the interest on the Bonds to be included in gross income retroactive to the date of issuance of the Bonds. The Commonwealth has covenanted to comply with all such requirements.

7. Under the laws of the Commonwealth, the interest on the Bonds is exempt from Pennsylvania personal income tax and from Pennsylvania corporate net income tax and the Bonds are exempt from personal property taxes in the Commonwealth.

8. The Bonds are exempt from registration under the provisions of the Securities Act of 1933, as amended.

With respect to the foregoing, it is to be understood that the rights of the owners of the Bonds and the enforceability of the Bonds may be limited by bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights generally and by equitable principles, whether considered in a proceeding at law or in equity.

We express no opinion as to any matter not set forth herein, including federal and state tax consequences arising with respect to the Bonds other than as expressed in paragraphs 6 and 7 above, or as to the accuracy, adequacy or completeness of the Official Statement prepared with respect to the Bonds, and we make no representation that we have independently verified the contents of such Official Statement.

This opinion is given as of the date hereof, and we assume no obligation to update or supplement this opinion to reflect any facts or circumstances which may hereafter come to our attention or any changes in laws which may hereafter occur.

Very truly yours,

OBERMAYER REBMANN MAXWELL & HIPPEL LLP

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NOTICE OF SALE
$200,000,000
Commonwealth of Pennsylvania
General Obligation Bonds
First Series of 2005

Sealed and electronic bids (as explained below) will be received by the Commonwealth of Pennsylvania (the "Commonwealth"), in the case of sealed bids, at

Office of the Budget
7th Floor Bell Tower, 303 Walnut Street
Harrisburg, Pennsylvania 17101

and in the case of electronic bids via ***PARITY***® ("Parity") in the manner described below, up to 11:00 A.M., Eastern Daylight Time, on

Tuesday, May 24, 2005

or such other subsequent date ("Amended Bid Date") to be announced in an Amended Notice of Sale (as hereinafter defined) to be distributed not later than 4:00 P.M. on the last business day prior to the Amended Bid Date, for the purchase of all, but not less than all, of the aggregate principal amount of Commonwealth of Pennsylvania General Obligation Bonds, First Series of 2005 (the "Bonds").

Bids must be submitted in accordance with this Notice of Sale prior to the deadline of 11:00 A.M. Eastern Daylight Time. No bid will be accepted after the bid deadline. Bids may be submitted by any of the methods described below:

(a) in a sealed envelope to the Commonwealth at the address above; or
(b) electronically via Parity.

Right to Amend

The Commonwealth reserves the right, in its sole discretion, to change the date it will receive and open electronic and sealed bids to purchase the Bonds and to increase or decrease the principal amount of Bonds being offered. Changes to the Bonds being offered, if made, will be contained in an Amended Notice of Sale (the "Amended Notice") to be transmitted via the Bond Buyer Wire not later than 4:00 P.M. on the last business day prior to the Amended Bid Date. The Amended Notice shall (i) state the Amended Bid Date (a date not before May 24, 2005) and the time by which bids to purchase the Bonds must be received by the Commonwealth; (ii) state the revised principal amounts; (iii) state the proposed closing date; and (iv) supplement and update the information contained herein to the extent deemed necessary by the Commonwealth.

Security

The Bonds will be direct and general obligations of the Commonwealth, issued pursuant to and within the applicable debt limits prescribed by Section 7 of Article VIII of the Constitution of Pennsylvania and various implementing acts of the General Assembly.

Bond Details

The Bonds will be dated the date of issuance and delivery, and will bear such rate or rates of interest, payable semiannually on January 1 and July 1 in each year commencing January 1, 2006, as shall be fixed by the purchaser in its proposal for the purchase of the Bonds. The Bonds shall mature serially on July 1 in the respective years and in the respective amounts set forth in the following table:

Due July 1	Principal Amount	Due July 1	Principal Amount
2006	$6,120,000	2016	$9,820,000
2007	6,370,000	2017	10,325,000
2008	6,650,000	2018	10,855,000
2009	6,955,000	2019	11,410,000
2010	7,285,000	2020	11,995,000
2011	7,650,000	2021	12,610,000
2012	8,040,000	2022	13,255,000
2013	8,450,000	2023	13,935,000
2014	8,885,000	2024	14,650,000
2015	9,340,000	2025	15,400,000

Delivery of the Bonds is proposed to occur on June 9, 2005, unless another date is set forth in any Amended Notice (the "Closing Date").

The Bonds will be issued and sold by means of a book-entry only system with no distribution of Bond certificates made to the public. Bond certificates representing the aggregate principal amount of the Bonds maturing in each year will be issued and fully registered as to principal and interest in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), a depository registered with the Securities and Exchange Commission. Beneficial ownership of the Bonds will be in principal amounts of $5,000 or integral multiples thereof within a maturity pursuant to the rules and procedures established between DTC and its participants. Transfers of beneficial ownership will be effected through records maintained by DTC and its participants pursuant to rules and procedures established by DTC. The responsibility for maintaining, reviewing and supervising such records rests collectively with DTC and its participants. The winning bidder, as a condition to the delivery of the Bonds, shall be required to deposit the Bond certificates in its account at DTC, registered in the name of Cede & Co. Interest on the Bonds will be payable on each semi-annual interest payment date and principal of the Bonds will be paid annually as set forth in the foregoing maturity schedule, in same-day funds to DTC or its nominee as registered owner of the Bonds. Transfer of principal and interest payments to the beneficial owners by participants of DTC will be the responsibility of such DTC participants and other nominees of beneficial owners. The Commonwealth will not be responsible or liable for maintaining, supervising or reviewing the records maintained by DTC, its participants or persons acting through such participants.

Optional Redemption

The Bonds, or portions thereof in integral multiples of $5,000, maturing on and after July 1, 2016, are subject to redemption at the option of the Commonwealth prior to scheduled maturity, on or after July 1, 2015, as a whole or in part at any time and from time to time, in any order of maturity and by lot within a maturity in such a manner as the Commonwealth in its discretion may determine, on at least 30 days (but not more than 60 days) notice, at a redemption price equal to par (100%) plus accrued interest thereon to the date fixed for redemption.

Interest Rate and Bidding Details

Each bidder shall designate a rate of interest per annum to be paid on the Bonds of each maturity, subject to the following limitations:

(i) all Bonds of the same maturity date must bear the same rate of interest and no one Bond shall bear more than one rate of interest;

(ii) no interest rate shall be other than a whole multiple of one-twentieth (1/20) or one-eighth (1/8) of one percent (1%) and a zero rate of interest may not be named; and

(iii) the reoffering price for Bonds of any maturity must be greater than 98½% and less than 119% of that maturity's par value.

No bid for the Bonds at a price less than 98½% of their par value, exclusive of accrued interest, will be considered. Bids may specify any number of interest rates subject to (i) through (iii) above. No bid will be considered which does not offer to purchase all of the Bonds.

Electronic Bidding Procedure

Solely as an accommodation to bidders, the Commonwealth will receive bids delivered electronically through Parity. Further information about Parity, including any fee charged and applicable requirements, may be obtained from:

i-Deal LLC
40 West 23rd Street
5th Floor
New York, NY 10010
Phone: (212) 404-8102

All electronic bids must be delivered via Parity. If any provision of this Notice of Sale conflicts with information provided by Parity, this Notice of Sale shall control. Each bidder submitting an electronic bid agrees by doing so that it is solely responsible for all arrangements with (including any charges by) Parity, that the Commonwealth does not endorse or encourage the use of Parity, and that Parity is not acting as an agent of the Commonwealth. Instructions for submitting electronic bids must be obtained from Parity, and the Commonwealth does not assume any responsibility for ensuring or verifying bidder compliance with the procedures of Parity. The Commonwealth shall be entitled to assume that any bid received via Parity has been made by a duly authorized agent of the bidder. Acceptance of electronic bids shall be subject to the limitations set forth in **"Warnings Regarding Electronic Bids"** below.

Warnings Regarding Electronic Bids

The Commonwealth and Bond Counsel assume no responsibility for any error contained in any bid submitted electronically, or for failure of any bid to be transmitted or received at the official time for receipt of bids. The Commonwealth assumes no responsibility for informing any bidders prior to the deadline for receiving bids that its bid is incomplete or not received.

The Commonwealth will accept bids in electronic form only through Parity on the official bid form created for such purpose by Parity. Each bidder submitting an electronic bid understands and agrees by doing so that it is solely responsible for all arrangements with Parity, that the Commonwealth neither endorses nor explicitly encourages the use of Parity, and that Parity is not acting as agent of the Commonwealth. Instructions and forms for submitting electronic bids must be obtained from Parity, and the Commonwealth assumes no responsibility for ensuring or verifying bidder compliance with the procedures of Parity. The Commonwealth shall assume that any bid received though Parity has been made by a duly authorized agent of the bidder.

Reoffering and Sale of Bonds to Public

Within thirty minutes after notification of award of the Bonds the successful bidder (the "Underwriter") shall provide to the Commonwealth the initial offering price to the public (excluding bond houses and brokers or similar persons or organizations acting in the capacity as wholesalers or underwriters) for each maturity of the Bonds (the "Initial Reoffering Prices") and certain other information to enable the Commonwealth to compute the yield on the Bonds for federal tax law purposes. The successful bidder will be required to provide a certificate prior to settlement for the Bonds in form satisfactory to the Commonwealth and Bond Counsel stating the Initial Reoffering Prices at which a substantial amount (at least 10 percent) of each maturity of Bonds has been sold and stating the yield on the Bonds.

Each bidder, by the submission of a bid, agrees that if it is the successful bidder, it will make a *bona fide* public offering of the Bonds at prices not greater than the Initial Reoffering Prices, offer the Bonds only pursuant to the Official Statement and only in jurisdictions where the offer is legal, and deliver a copy of the Official Statement to each person or entity that purchases the Bonds from the Underwriter as required by Securities and Exchange Commission Rule 15c2-12. The Underwriter shall abide by all rules of the Municipal Securities Rulemaking Board ("MSRB") in connection with the issuance and sale of the Bonds, including the delivery to the MSRB of the Official Statement and any advance refunding documents.

Basis of Awards

Award of the Bonds will be made on or before 4:00 P.M. Eastern Daylight Time, on May 24, 2005 or, in the event of the announcement of an Amended Bid Date, the date specified in the Amended Notice. The Bonds will be sold to the bidder making a bid conforming to the terms of the offering which, on the basis of the lowest net effective interest rate for the Bonds, determined in the manner hereinafter stated, is the best bid, subject to the right of the undersigned in their sole discretion to reject any and all bids. The net effective interest rate for the Bonds shall be the interest rate determined on a true interest cost ("TIC") basis by doubling the semi-annual interest rate, compounded semi-annually, necessary to discount the debt service payments to the date of delivery of the Bonds, (June 9, 2005, unless otherwise announced in an Amended Notice) to the price bid, including interest accrued to the date of delivery, if any. In the event of more than one bid specifying such lowest rate, the Bonds will be awarded to the bidder whose bid is selected by lot from among all such lowest bids.

Official Bid Form

Sealed bids must be made upon the prescribed Official Bid Form, and all electronic bids shall be deemed to incorporate the provisions of the Official Bid Form. The Commonwealth reserves the right in its sole discretion to waive any minor errors or irregularities in form or content of any bid. All sealed bids should be enclosed in a sealed envelope, marked on the outside, "Bid for Commonwealth of Pennsylvania General Obligation Bonds," or such similar legend which identifies the contents, and delivered to the Honorable Edward G. Rendell, Governor, or his duly authorized representative in the Office of the Budget, 7th Floor Bell Tower, Strawberry Square, 303 Walnut Street, Harrisburg, Pennsylvania.

Good Faith Check or Surety Bond

A certified or bank cashier's or treasurer's check drawn on an incorporated bank or trust company, must be provided or a financial surety bond (the "Surety Bond") submitted, payable to the order of the Commonwealth of Pennsylvania in the amount of $1,000,000 (the "Deposit"). If a check is provided, it must accompany the bid. If a Surety Bond is submitted, it must be from an insurance company acceptable to the Commonwealth and licensed to issue such a bond in the Commonwealth of Pennsylvania, such Surety Bond must be submitted to the Commonwealth prior to the opening of bids and must be in form and substance acceptable to the Commonwealth. The Surety Bond must identify each bidder whose Deposit is guaranteed by such Surety Bond. Checks accompanying bids not accepted will be returned to the bidders within 24 hours from the time of opening the bids. If the Bonds are awarded to a bidder utilizing a Surety Bond, then that successful bidder is required to submit its Deposit in the form of a federal funds wire transfer as instructed by the Commonwealth by not later than 11:00 a.m. Eastern Daylight Time on the next business day following the award. If such deposit is not received by that time, the Surety Bond may be drawn upon by the Commonwealth to satisfy the Deposit requirement.

The Commonwealth reserves the right, in its sole discretion, to present the good faith check of the successful bidder for payment and to deposit the proceeds of such check or the draw on the Surety Bond and to invest the Deposit to the date of settlement on the Bonds. The Deposit, but not any earnings from any investment thereof, will be applied to the purchase price of the Bonds, or, if such bid is not performed, such proceeds will be retained by the Commonwealth as liquidated damages, unless the failure of performance shall be caused by an act or omission of the Commonwealth.

Official Statement and Continuing Disclosure - SEC Rule 15c2-12

The Preliminary Official Statement dated May 13, 2005, issued with respect to the Bonds (the "Preliminary Official Statement"), has been deemed final by the Commonwealth as of its date for purposes of SEC Rule 15c2-12 (the "Rule"), except for the omission of information as permitted by the Rule, but is subject to revision, amendment, and completion in the final Official Statement (hereinafter the "Official Statement") to be prepared with respect to the Bonds. A reasonable number of copies (not to exceed 1,000) of the Official Statement, to be dated as of a date prior to settlement, will be furnished to the purchaser within seven business days after the sale date. Copies of the Official Statement in excess of 1,000 will be furnished at the request of the successful bidder at its own expense. The successful bidder will be required to provide pricing information necessary for the Commonwealth to complete the Official Statement.

In order to assist bidders in complying with the Rule, the Commonwealth will execute a written Continuing Disclosure Agreement to provide or cause to be provided, in accordance with the Rule, certain annual financial information and timely notices of the occurrence of certain events, if material, with respect to the Bonds. A description of this Continuing Disclosure Agreement is set forth in the Preliminary Official Statement and will also be set forth in the Official Statement.

CUSIP Numbers

CUSIP numbers will be assigned at the purchaser's expense. The CUSIP numbers will be printed on the Bonds, provided, however, that incorrect numbers shall not constitute grounds for a purchaser of the Bonds to refuse delivery thereof.

Delivery of Bonds

Bond certificates will be delivered through the Loan and Transfer Agent to DTC using DTC's Fast Automated Security Transfer (FAST) System. Payment for the Bonds must be made by wire in immediately available funds for credit at U.S. Bank National Association, Loan and Transfer Agent, in Pittsburgh, Pennsylvania, at 10:00 A.M., Eastern Daylight Time, on the Closing Date, or at such other place and time as may be agreed upon with the successful bidder.

The successful bidder shall have the right, at its option, to cancel its obligation to purchase the Bonds if the Commonwealth shall fail to tender the Bonds for delivery within 60 days from the date herein fixed for the receipt of the bids, and in such event, the successful bidder shall only be entitled to the return of its Deposit, without interest, and shall have no right of action against the Commonwealth.

Legal Opinions

The Commonwealth will deliver to the purchaser without charge: (i) the opinion of the Attorney General of the Commonwealth and (ii) the opinion of Obermayer Rebmann Maxwell & Hippel LLP, Philadelphia, Pennsylvania, appointed by the Commonwealth as Bond Counsel, both substantially in the forms of their opinions set forth as appendices to the Preliminary Official Statement.

Closing Documents

The Bonds are offered subject to the delivery at settlement by the Commonwealth of (i) a certificate stating that there is no litigation pending affecting the validity of the Bonds or their issuance and sale to the purchaser; (ii) a certification by the Secretary of the Budget that the financial statements contained in the Official Statement accurately reflect the conditions and facts they purport to reflect, that the estimates contained therein, in light of the information available, are believed to be reliable and that there have been no material adverse changes in the financial position of the Commonwealth since the dates of such financial statements not disclosed in the Official Statement; (iii) a certification by the Governor, the Auditor General and the State Treasurer that the Official Statement, except as to the financial statements contained therein, contains no untrue statement of a material fact and does not omit to state a material fact necessary in order to make the statements made therein, in light of the circumstances under which they were made, not misleading; and (iv) a Continuing Disclosure Agreement to provide or cause to be provided certain annual financial information and timely notices of the occurrence of certain events, if material, with respect to the Bonds.

Prior to settlement the purchasers will be required to deliver the certificate referred to under the caption "Reoffering and Sale of Bonds to Public" above.

Copies of Documents

Additional information and copies of the Preliminary Official Statement, which includes the Official Bid Form as Appendix H issued in connection with the Bonds, may be obtained from the Loan and Transfer Agent, U.S. Bank National Association, Pittsburgh, Pennsylvania (Telephone 412-522-2140) or from the Office of the Budget, Seventh Floor, Bell Tower, Harrisburg, Pennsylvania 17101 (Telephone 717-783-3086). The

Preliminary Official Statement may also be downloaded from the Office of the Budget area on the Commonwealth's site on the world wide web, http://www.budget.state.pa.us.

EDWARD G. RENDELL
Governor

ROBERT P. CASEY, JR.
State Treasurer

JACK WAGNER
Auditor General

Dated: May 13, 2005

OFFICIAL BID FORM FOR SEALED BIDS

$200,000,000 Commonwealth of Pennsylvania General Obligation Bonds

First Series of 2005

Honorable Edward G. Rendell, Governor
Honorable Robert P. Casey, Jr., State Treasurer
Honorable Jack Wagner, Auditor General

May 24, 2005

Gentlemen:

The undersigned, on behalf of a group which we have formed consisting of the persons, firms and corporations named below, and in accordance with the terms and conditions of the Notice of Sale, dated May 13, 2005 (the "Notice"), which hereby is made a part hereof by reference thereto, for the purchase of $200,000,000 aggregate principal amount of Commonwealth of Pennsylvania General Obligation Bonds, First Series of 2005, (the "Bonds"), and subject to the conditions hereinafter stated, hereby agree to purchase all, but not less than all, of the Bonds and pay therefor the sum of:

$ ....

(Purchase price not to be less than $197,000,000)

together with accrued interest, if any, to the date of delivery.

The Bonds will be initially dated the date of issuance and delivery, and will mature serially on July 1 in the years and in the respective principal amounts, and will bear interest from the date of issuance and delivery, payable semiannually on January 1 and July 1 in each year commencing January 1, 2006, at the respective rates, all as set forth in the following table, and subject to redemption as set forth in the Notice:

Due July 1	Principal Amount	Interest Rate	Due July 1	Principal Amount	Interest Rate
2006	$6,120,000	..........%	2016	$9,820,000	..........%
2007	6,370,000	....	2017	10,325,000	....
2008	6,650,000	....	2018	10,855,000	....
2009	6,955,000	....	2019	11,410,000	....
2010	7,285,000	....	2020	11,995,000	....
2011	7,650,000	....	2021	12,610,000	....
2012	8,040,000	....	2022	13,255,000	....
2013	8,450,000	....	2023	13,935,000	....
2014	8,885,000	....	2024	14,650,000	....
2015	9,340,000	....	2025	15,400,000	....

In accordance with the terms of the Notice, there is enclosed herewith a certified or official bank check or a surety bond for $1,000,000 payable to the order of the Commonwealth of Pennsylvania.

Signature and Title:______________________________________ Contact Person:______________________
(Print or Type)

Firm:____ Telephone:________________________
(Attach additional sheet if necessary for sealed bids)

NOT A PART OF BID

Net effective interest rate per annum calculated in conformity with the Notice ....%.

Total amount of interest from date of the Bonds to final maturity $..

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FINANCIAL SECURITY ASSURANCE INC.
BOND INSURANCE

Bond Insurance Policy

Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. ("Financial Security") will issue its Municipal Bond Insurance Policy (the "Policy") for the Bonds maturing on July 1, of the years 2022 through 2025, inclusive (the "Insured Bonds"). The Policy guarantees the scheduled payment of principal of and interest on the Insured Bonds when due as set forth in the form of the Policy included as an exhibit to this Official Statement.

Financial Security Assurance Inc.

Financial Security is a New York domiciled financial guaranty insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation, and of Dexia Credit Local, a direct wholly-owned subsidiary of Dexia, S.A. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance, banking and asset management in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At March 31, 2005, Financial Security's total policyholders' surplus and contingency reserves were approximately $2,321,918,000 and its total unearned premium reserve was approximately $1,672,672,000 in accordance with statutory accounting practices. At March 31, 2005, Financial Security's total shareholders' equity was approximately $2,726,667,000 and its total net unearned premium reserve was approximately $1,356,678,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Bonds or the advisability of investing in the Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Issuer the information presented under this caption for inclusion in the Official Statement.

FINANCIAL SECURITY ASSURANCE®

MUNICIPAL BOND INSURANCE POLICY

ISSUER:

BONDS:

Policy No.: -N

Effective Date:

Premium:

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the

United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud), whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature] FINANCIAL SECURITY ASSURANCE INC.

By ______________________________ By ______________________________
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022 (212) 826-0100

Form 500NY (5/90)

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