NEW JERSEY SCHOOLS CONSTRUCTION CORPORATION

(a component unit of the State of New Jersey)

FINANCIAL STATEMENTS

For the Year Ended December 31, 2006

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Financial Statements

For the Year Ended December 31, 2006

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New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Financial Statements

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INTRODUCTORY SECTION

PART I

New Jersey Schools Construction Corporation
Office of the Chief Executive Officer

SCOTT A. WEINER
Chief Executive Officer

TO THE OFFICE OF THE GOVERNOR AND MEMBERS OF THE NEW JERSEY STATE LEGISLATURE:

Pursuant to P.L.1974, c.80, s.4 (N.J.S.A. 34:1B-4j), I am pleased to present the New Jersey Schools Construction Corporation's ("SCC") financial statements for the year ended December 31, 2006. This financial report is presented in two sections. This transmittal letter serves as an introduction and summary. The financial section includes the basic financial statements and other required financial information.

2006 – A Year of Reform

The year 2006 was noteworthy for the SCC as it was challenged to restore confidence and accountability in the School Construction Program. As a result, the SCC focused on implementing a number of reforms to strengthen management of the organization, enhance project controls, and improve accountability and efficiency.

On February 7, 2006, Governor Jon S. Corzine signed Executive Order #3 ("E.O. #3") to facilitate review and reform at the SCC. In E.O. #3, I was named both Special Counsel on School Construction and Chairman of the newly created Interagency Working Group ("Working Group"). Other members named to the Working Group include Barry L. Zubrow - the Chairman of the SCC Board, the Commissioner and staff of the New Jersey Department of Education ("DOE"), the State Treasurer, the Commissioner and staff of the Department of Community Affairs ("DCA"), and a Citizens Panel. In 2006, the Working Group issued three reports that provide the framework for many reform efforts that were implemented during the year.

First Report of the Working Group

The Working Group's first report, issued in March, provided a historical overview of the SCC's practices and recommended major operational and programmatic reforms that were necessary to move the School Construction Program forward. In terms of looking to the past, the Working Group stated that the original funding allocation provided by the EFCFA was never sufficient to address all of the school facilities' needs throughout the State and that the enabling legislation did not provide enough flexibility to acquire sites for schools. It also noted that the start of the School Construction Program focused on the need for speed as a main driver affecting the construction of schools while management and accountability were secondary priorities.

Key recommendations from the first Working Group report include (1) transitioning the SCC's responsibilities to a new authority whose governance would be devoted exclusively to the mission of designing and constructing schools (2) developing a methodology to provide a systematic approach to prioritizing current and future projects (3) increasing collaboration with school districts, municipalities, the DOE, and the Legislature (4) sharing responsibility between the new authority for school construction and local school districts for site acquisition, and (5) perhaps allowing certain Abbott districts to oversee and manage their school facilities projects.

Second Report of the Working Group

In May, the Working Group released its second report. This report focused on developing sound ways to prioritize school construction projects and identifying specific statutory changes needed to make the School Construction Program more flexible and efficient.

In the area of legislative changes, the Working Group repeated its previous recommendation to craft legislation that would create a new authority for school construction. The governing board of this new organization would focus solely on school construction. To embark upon some of the challenges concerning site acquisition, the Working Group recommended legislation that would call for a moratorium on municipal approvals and variances for private development of proposed school sites and require greater collaboration between districts and municipalities in identifying school sites. The Working Group also recommended specific reforms to the Long Range Facility Plan (LRFP) process. This recommendation includes requiring districts to designate projects based on a five-year cycle, ensuring valid enrollment projections, and limiting the amendment opportunities. Finally, to address the lack of flexibility in how the SCC manages school facilities projects, it recommended legislation that would allow the SCC to consider a suite of project management options.

The Working Group's second report also made initial recommendations on the development of a prioritization methodology for school projects to proceed based on the educational priorities established by the New Jersey Supreme Court and in State statute. In order, those educational priorities include projects that address health and safety, early childhood education, and overcrowding. To assess these priorities and make a final recommendation on a prioritization methodology the Working Group convened a Project Prioritization Task Force ("Task Force"). The Working Group recommended that this methodology be the basis for the SCC and the DOE in developing statewide, strategic and capital plans.

Third Report of the Working Group

In September, the Working Group issued its third report. Based on the reform efforts that had been recently implemented at the SCC, the Working Group concluded that the SCC was now in a position to responsibly manage new projects. Furthermore, it recommended that the

Legislature provide $2.5 billion in additional funding for Abbott Districts and $750 million for Regular Operating Districts (non-Abbott schools). The additional Abbott funding would be used to both jumpstart some of the projects previously suspended due to the lack of funding and to cover an estimated $500 to $600 million shortfall for projects included in the capital plan but not yet in construction. The $3.25 billion would not be sufficient to finance all of the remaining school facility needs throughout the State. However, it would provide a manageable amount with which the SCC could proceed.

This report also included recommendations for a project prioritization methodology discussed in the Working Group's second report. Based on input received from various stakeholders, the Task Force recommended the use of a methodology based principally on the three core educational priorities (i.e., health and safety, early childhood education, and overcrowding in schools) previously identified in the EFCFA. However, the Task Force concluded that those three categories alone did not provide for sufficient differentiation among school facilities projects. Consequently, the Working Group's final recommendation for prioritization includes both educational criteria and logistical criteria, such as land status and estimated project schedule (i.e., construction notice to proceed date).

Additionally, the Working Group reported on a number of SCC reform efforts that addressed management capabilities (detailed below under Organizational Reforms), and recommended further legislative amendments that would ensure accountability and efficiency. Among those legislative changes, they highlighted the need for land acquisition reforms and suggested that the SCC plan a symposium to obtain stakeholder input.

Organizational Reforms

In 2006, the SCC identified or implemented numerous personnel and organizational changes to ensure that it had the right leadership to guide it for the future; an appropriate organizational structure to reflect its business processes; and a staff capable of supporting its mission. Barry Zubrow was appointed Chairman of the Board by Governor Corzine in February 2006. I was appointed Chief Executive Officer by the SCC Board in September 2006, after serving as Transitional Chief Executive Officer since March. Among the other senior leadership changes, Don Guarriello was named Acting Chief Financial Officer, John Clark became the SCC's first ever Chief Counsel, Beth Sztuk was named Sr. Director of the newly created Office of Management & Planning, Regina Bleck became Sr. Director, Project Management (formerly known as Design & Construction) and Scott Guibord was named Sr. Director and Secretary, Corporate Governance & Compliance. Mr. Clark, Ms. Sztuk and Ms. Bleck were all new hires in 2006. Gerald T. Murphy continued as the SCC's Chief Operating Officer.

Several other organizational and key personnel changes were implemented in 2006 to strengthen the overall management of the organization.

In the area of legal services, the new Office of Chief Counsel provides the SCC with in house professional legal support with vast experience in construction and contract management law. Among other things, this office will assist the SCC in matters of contract management, error and omission cost recoveries, environmental cost recoveries, and claims review and mitigation.

Regarding the newly created Office of Management & Planning, its Program Management function will oversee the SCC's strategic and capital planning efforts. The Project Controls unit will assemble and coordinate with teams of SCC staff and consultants who will thoroughly be involved in the management of school facilities projects from inception to project closeout. The SCC believes this team approach will ensure communication and coordination throughout the project life cycle, significantly improve accountability and ownership of projects, and ultimately lead to delivering first-rate schools to school districts on-time and on-budget. Also included in this office are the Procurement and Contract Services functions.

Project Management

The task of project management was significantly enhanced in 2006 with the establishment of project teams. These project teams ensure communication and coordination throughout the life of a project. Project teams consist of an SCC representative from each of the several disciplines involved in planning, developing, managing, constructing, furnishing, and ultimately delivering completed school facilities projects to school districts. In addition, project teams may include representatives from DOE, DCA, DEP, the school district, and the city or town. The SCC also improved its project forecasting capabilities in 2006 and developed comprehensive project budgets for the first time. By the end of 2006, project budgets included all financial aspects of a project and were being updated and tracked monthly.

In addition, another key project management initiative is the continuing development of a project management software application, Primavera Expedition. Once implemented in 2007, this fully integrated project tracking system will consolidate all of the individual stand-alone databases that currently exist throughout the SCC and be used to track and manage project budgets and schedules.

Collaboration

Increased collaboration with our partners in State government, school districts, communities, and the construction and business industry is critical to ensuring the success of the School Construction Program.

Throughout 2006, the SCC worked hard to improve its partnership with the DOE and the DCA. First, the SCC began to meet regularly with the DOE to review and identify emergent health and safety projects and participated in the LRFP review process. It also met regularly with DCA management to discuss ways to streamline the process for construction inspections and approvals. Additionally, the SCC improved its working relationship with the DEP on environmental issues.

The SCC made efforts to increase direct communications with key stakeholders in the Abbott Districts. It began holding meetings with each Abbott District to discuss the status of their projects. These meetings helped to ensure that all parties involved understood the issues related to their projects.

In addition, the SCC wanted to engage its stakeholders in the decision-making process. This had not been done in the past. To this end, the SCC held a series of symposia to discuss key policy issues with districts, municipalities and advocates.

Transparency and Ethics

A key initiative for Chairman Zubrow in 2006 was to make the actions of the Board of Directors more open and transparent to the public. To that end, he requested that the minutes, agendas, management memoranda requesting Board action, and informational reports be posted to the SCC website in advance of the Board meetings.

Pursuant to a Memorandum of Understanding between the SCC and Office of the Inspector General, two Assistant Inspector Generals have been assigned to the SCC's main office. The function of the SCC Assistant Inspector Generals is to provide the SCC with assurances as to the efficiency and effectiveness of its operations, reliability of its programs and processes, and compliance with applicable laws and regulations. The SCC Assistant Inspector Generals report to and are supervised by the Inspector General.

Ethics and business conduct continued to be a top priority for the SCC throughout 2006. During the year, all employees received an "Ethics Package" which included the SCC Code of Conduct, an Acknowledgement Form, a Conflict of Interest Form and an SCC Ethics Brochure. This information, as well as other ethics forms, was centrally placed on the SCC Intranet site to ensure easy access by all employees. The SCC has also developed a New Employee Orientation program so that new employees are conscious of the SCC's ethical guidelines. It also created a Post-Employment Departure Letter to ensure that former employees are mindful of their post-employment restrictions. Furthermore, the SCC Ethics Liaison held live Ethics Briefings for all SCC employees to review the ethics requirements of the State Ethics Commission.

Independent Audit

The SCC's 2006 financial statements are presented in accordance with the rules promulgated by the Governmental Accounting Standards Board and have been audited by an independent accounting firm. I am pleased to inform you that Ernst & Young LLP has issued an unqualified opinion on the SCC's 2006 financial statements. The auditors' report is included in the financial section of this report.

Acknowledgements

I want to thank my colleagues, the approximately 240 SCC employees who have worked so diligently this past year, and our Board of Directors, through whose efforts we accomplished a great deal. I am confident we will continue to make progress in 2007.

Additionally, I want to thank Governor Jon Corzine and the members of the State Legislature for their continued support of the School Construction Program. I look forward to working with you in the future.

As always, please do not hesitate to contact me with any questions or concerns.

Sincerely,

Scott A Weiner

Scott A. Weiner

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Financial Statements

For the Year Ended December 31, 2006

FINANCIAL SECTION

PART II

ERNST & YOUNG

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Report of Independent Auditors

Members of the Corporation
New Jersey Schools Construction Corporation

We have audited the accompanying basic financial statements of the New Jersey Schools Construction Corporation (the Corporation), a component unit of the State of New Jersey, as of December 31, 2006 and for the year then ended as listed in the table of contents. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Corporation's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the New Jersey Schools Construction Corporation as of December 31, 2006, and the changes in its financial position for the year then ended in conformity with U.S. generally accepted accounting principles.

Management's discussion and analysis is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this required supplementary information. However, we did not audit the information and express no opinion on it.

Ernst + Young LLP

February 9, 2007

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Management's Discussion and Analysis

For the Year ended December 31, 2006

This section of the New Jersey Schools Construction Corporation's (the "Corporation" or "SCC") annual financial report presents our discussion and analysis of the Corporation's financial performance during the fiscal year ended December 31, 2006. This management discussion and analysis should be read in conjunction with the Corporation's financial statements and accompanying notes.

Background

The New Jersey Schools Construction Corporation was created as a subsidiary organization of the New Jersey Economic Development Authority ("NJEDA"). The Corporation was formed as a separate activity apart from the NJEDA's mandated economic development mission for the purpose of establishing a more concentrated focus and streamlined approach to the timely and efficient construction of quality schools in New Jersey ("State").

The New Jersey Educational Facilities Construction and Financing Act ("EFCFA") was enacted on July 18, 2000 by the Legislature in response to the New Jersey Supreme Court's decision in Raymond Abbott et al. v. Fred G. Burke, 153 N.J. 480 (1998). As a result of the EFCFA, the State is required to provide certain educational infrastructure improvements in the poor, urban school districts ("Abbott School Districts") so that students in these school districts can receive a thorough and efficient education, an explicit requirement of the New Jersey Constitution. The Corporation is responsible under the EFCFA for funding (full or partial), designing and constructing all school facilities projects in the Abbott School Districts, in districts eligible to receive 55% or more in State funding for education, and in districts that are designated as level II State monitoring by the New Jersey Department of Education ("DOE"). School facilities projects constructed in any of the 31 designated Abbott School Districts are eligible for full funding by the State. Additionally, the Corporation is responsible for providing grants to fund the State share of school facilities projects approved by the DOE in districts with a district aid percentage of less than 55%. Those districts, which receive less than 55% funding, may elect to have the Corporation undertake the construction of their school facilities projects.

The School Construction Program is the largest public construction program undertaken by the State of New Jersey and represents one of the largest school construction programs ever undertaken in the nation. The EFCFA provides for an aggregate $8.6 billion principal amount of bond proceeds ("EFCFA funding") to be issued by the NJEDA and transferred to the Corporation. Of this amount, $6 billion is slated for the Abbott School Districts, $2.5 billion is for non-Abbott districts, and $100 million is for vocational schools. Through December 31, 2006, the Corporation received $6.121 billion of the allotted $8.6 billion principal amount of bond proceeds authorized for the School Construction Program. In addition, as of that date, the Corporation has disbursed 62.1% of the current total funding, as follows:

	EFCFA Funding	Total Funding[1]	Disbursements	% Paid
Abbott Schools	$6,000,000,000	$6,075,016,849	$3,803,718,234	62.6%
Non-Abbott Schools	2,500,000,000	2,530,490,766	1,521,355,798	60.1%
Vocational Schools	100,000,000	101,218,098	81,048,476	80.1%
Totals	$8,600,000,000	$8,706,725,713	$5,406,122,508	62.1%

[1] Includes EFCFA funding as well as other income and miscellaneous revenue of $106.7 million earned through December 31, 2006, consisting primarily of interest income on invested funds and State appropriations received prior to 2003.

The 31 Abbott School Districts are located in 14 Counties throughout the State, as follows:

County	School District	County	School District
Atlantic	Pleasantville	Hudson	Union City
Bergen	Garfield	Hudson	West New York
Burlington	Burlington City	Mercer	Trenton
Burlington	Pemberton Township	Middlesex	New Brunswick
Camden	Camden	Middlesex	Perth Amboy
Camden	Gloucester City	Monmouth	Asbury Park
Cumberland	Bridgeton	Monmouth	Keansburg
Cumberland	Millville	Monmouth	Long Branch
Cumberland	Vineland	Monmouth	Neptune Township
Essex	East Orange	Passaic	Passaic City
Essex	Irvington	Passaic	Paterson
Essex	Newark	Salem	Salem City
Essex	Orange	Union	Elizabeth
Hudson	Harrison	Union	Plainfield
Hudson	Hoboken	Warren	Phillipsburg
Hudson	Jersey City		

Business Accomplishments and Developments

The following un-audited information provides insight into the activities of the School Construction Program during the last five years and is not intended to be presented in accordance with generally accepted accounting principles.

	$ In thousands				
	2006	**2005**	**2004**	**2003**	**2002**
EFCFA funding and appropriations received from State	$600,000	$2,075,000	$1,700,000	$607,929	$585,900
Investment earnings	39,702	17,473	8,098	5,488	9,991
Project costs	1,061,962	1,466,536	1,374,637	1,096,481	460,971
Administrative expenses and program costs	31,717	29,127	27,950	22,135	10,116
Capital expenditures	349	194	844	7,610	1,440
Employee count at end of year	241	240	250	204	96

In 2006, the SCC remained committed to carrying out its mission of building state-of-the-art schools throughout New Jersey. The SCC moved forward on several projects through the award of 11 design contracts worth $8.8 million for projects having an aggregate construction cost estimate of $87.1 million; and with the award of 50 construction contracts worth $361 million. Of these 61 design and construction contracts, 40 were awarded to small business enterprises and 58 went to New Jersey firms. A summary of the Corporation's major construction activities is presented below.

Abbott School Districts

In 2006, the SCC completed construction of 10 new schools, 4 major renovation or addition projects, as well as 11 rehabilitation projects. The SCC's investment funding in these 25 school facilities projects is over $610 million. Included among the SCC's 2006 accomplishments was the opening of Newark's Science Park High School which is the first new high school built in Newark in 40 years. The new facility incorporates a quality science high school curriculum for up to 1,200 students. In Trenton, the SCC completed both the Joyce Kilmer and Columbus Elementary school projects. These two facilities are the first new, free-standing schools to be built in Trenton in more than 40 years. Both schools are helping to ease overcrowding and are providing critical early childhood education to pre-kindergarten children. The SCC also opened two new schools in Vineland in 2006: Thomas W. Wallace Jr. Middle School and the Pauline J. Petway Elementary School. These schools were the first new educational facilities built in this Cumberland County community since 1976.

From its inception through 2006, the SCC has commenced work on over 600 Abbott school facilities projects consisting of new schools, additions, renovations, and rehabilitations. Included among the completed school facilities projects are 30 new schools, 26 major renovations or additions, and 354 health and safety projects. An additional 25 projects have been completed that are primarily building system upgrades. The SCC's investment funding in these 435 school facilities projects is over $2.2 billion. In addition, the SCC provides funding to Abbott School Districts through Section 13A Grant Agreements for projects with construction costs valued at less than $500,000. To date, the SCC has provided over 200 grants to the Abbott School Districts worth in excess of $42 million in State funding.

As of December 31, 2006, the Corporation had 32 school facilities projects under construction which, in the aggregate, have an estimated cost at completion of more than $1.2 billion.

During 2006, the SCC continued development of six Demonstration Projects designated for the Abbott Districts. The projects are located in Camden, East Orange, New Brunswick, Trenton, Union City, and Vineland, and are currently forecasted to cost upwards of $640 million to construct. Demonstration Projects, as provided for under the EFCFA, are designed as community development initiatives with schools serving as a community anchor to provide children with safe, modern classrooms while maximizing urban renewal efforts. Community design features such as athletic venues, auditoriums, and media centers accessible to students and residents alike are key components of the program. The

Demonstration Projects serve as a catalyst for private investment to revitalize urban communities with new housing and retail opportunities. By the end of 2006, construction had begun on all but the New Brunswick Demonstration Project.

Regular Operating Districts

The EFCFA provides $2.5 billion to Regular Operating Districts to construct, repair, or renovate their school facilities. Unlike Abbott projects, which the SCC is required to manage for the districts, the SCC only manages a small number of the construction projects in the Regular Operating Districts (principally those districts eligible to receive 55% or more in State funding). Instead, it provides Section 15 grants directly to the school districts which manage their own construction projects. Usually, these grants cover a minimum of 40 percent of the eligible cost of the project as determined by the DOE. Each project is subject to voter approval and the district is responsible for funding the remaining balance of the cost.

Since its inception, the SCC has completed construction of seven school facilities projects that it managed for the Regular Operating Districts. These projects consist of two new schools - one of which was completed in 2006 - and five major renovations or additions. The SCC's investment funding in these seven school facilities projects is approximately $53 million.

In 2006, the SCC executed 148 Section 15 Grant Agreements providing State funding of $43.6 million to Regular Operating Districts throughout New Jersey. Since program inception, the Corporation has executed 2,555 Section 15 Grant Agreements totaling $2.2 billion of State funding to Regular Operating Districts. These grants have helped to fund school facilities projects at nearly 1,430 schools in 472 Regular Operating Districts throughout the 21 counties of New Jersey. Furthermore, these grants support an additional investment of $7.1 billion in construction funded by the Regular Operating Districts.

School Construction Program Funding

The Corporation does not have an economic interest in any school facility project. With the exception of interest income on invested funds, the Corporation does not generate substantial operating revenues, yet it incurs significant operating expenses to administer the School Construction Program. Costs related to school facilities projects are reported as project costs in the statement of activities. Administrative expenses and program costs, considered to be eligible project costs under the EFCFA, but not identifiable to a specific project, are also paid from EFCFA funding.

As of December 31, 2006, essentially all of the funds authorized under the statutory bonding cap have either been committed or set aside in the capital plan approved by the SCC Board in July 2005. As a result, until such time that the bonding cap is increased, the School Construction Program will neither undertake any additional school facilities projects nor provide any new funding grants to the Regular Operating Districts. As discussed above, the Working Group has recommended that the State Legislature provide $2.5 billion in additional funding for the Abbott School Districts, and $750 million for Regular Operating

Districts. There can be no assurance that the Corporation will receive additional funding above the $8.6 billion presently authorized by the State under the EFCFA.

2006 Financial Highlights

- The Corporation's total net assets are $613.7 million
- Cash and investments are $896.7 million
- Total revenues are $640.1 million, $600 million of which is EFCFA funding received from the State (or 93.7%)
- Total expenses are $1.095 billion, $1.062 billion of which are Project Costs (or 97%)
- Excess of general fund expenditures over general fund revenues is $455.4 million

Overview of the Financial Statements

The financial section of this annual report consists of two parts: Management's Discussion and Analysis (this section) and the basic financial statements. The Corporation's basic financial statements consist of three components: 1) government-wide financial statements, 2) governmental fund financial statements (these are also referred to as the "general fund" financial statements) and 3) notes to financial statements. Because the Corporation operates a single governmental program, its government-wide and governmental fund financial statements have been combined using a columnar format that reconciles individual line items of general fund financial data to government-wide data in a separate column on the face of the financial statement.

Government-wide financial statements are designed to provide readers with a broad overview of the Corporation's finances, in a manner similar to a private sector business. The statement of net assets presents information on all of the Corporation's assets and liabilities, with the difference between the two reported as net assets. Over time, an increase or decrease in net assets may serve as a useful indicator of whether the financial position of the Corporation is improving or deteriorating.

The statement of activities presents information showing how the Corporation's net assets changed during the most recent period. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenue and expenses are reported in this statement for some items that will only result in cash flows in the future fiscal period.

Governmental fund financial statements are designed to provide the reader information about an entity's various funds. A fund is a grouping of related accounts that is used to maintain control over the resources that have been segregated for specific activities or objectives. The Corporation uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The Corporation operates a single governmental fund for financial reporting purposes and this fund is considered a general fund.

The focus of governmental fund financial statements is on near-term inflows and outflows of spendable resources as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Corporation's near-term financing requirements.

Because the focus of the governmental fund is narrower than that of the government-wide financial statements, it is useful to compare the information presented for the governmental fund with similar information presented in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Corporation's near-term financing decisions. Both the fund balance sheet and the financial statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison.

Financial Analysis of the Corporation

Net Assets - The Corporation's net assets decreased to $613.7 million at year-end, primarily due to 2006 expenditures for school facilities projects ($1.062 billion) exceeding 2006 State funding under the EFCFA ($600 million). The following table summarizes the Corporation's financial position at December 31, 2006 and 2005.

	$ In thousands			
	2006	**2005**	**$ Increase/ (Decrease)**	**% Increase/ (Decrease)**
Current assets	$897,398	$1,367,038	$(469,640)	(34.4)%
Capital assets-net	6,690	7,855	(1,165)	(14.8)%
Total assets	904,088	1,374,893	(470,805)	(34.2)%
Current liabilities	268,411	282,618	(14,207)	(5.0)%
Non-current liabilities	22,009	23,563	(1,554)	(6.6)%
Total liabilities	290,420	306,181	(15,761)	(5.1)%
Net assets:				
Invested in capital assets	6,690	7,855	(1,165)	(14.8)%
Restricted for Qualified Zone Academies	2,689	3,539	(850)	(24.0)%
Restricted for Schools Construction Special Revenue Fund	604,289	1,057,318	(453,029)	(42.8)%
Total net assets	$613,668	$1,068,712	$(455,044)	(42.6)%

Operating Activities - During the bidding process, the Corporation charges a minimal fee ranging from $50 up to $500 for copies of design plans and specifications as specified in the construction project advertisements.

The Corporation earns interest on invested funds primarily through its participation in the State Cash Management Fund, a fund managed by the Division of Investment under the Department of Treasury. The fund consists of U.S. Treasury obligations, government agencies obligations, certificates of deposit and commercial paper.

The following table summarizes the change in net assets for the years ended December 31, 2006 and 2005.

	$ In thousands			
	2006	2005	$ Increase/ (Decrease)	% Increase/ (Decrease)
Revenues				
EFCFA funding received from State	$600,000	$2,075,000	$(1,475,000)	(71.1)%
Bidding fees-plans and specs	31	78	(47)	(60.9)%
Investment earnings	39,702	17,473	22,229	127.2 %
Rental property income	386	553	(167)	(30.1)%
Other revenue	30	7	23	309.1 %
Total revenues	640,149	2,093,111	(1,452,962)	(69.4)%
Expenses				
Administrative expenses	29,627	27,637	1,990	7.2 %
Program costs	2,090	1,490	600	40.3 %
Depreciation	1,514	2,127	(613)	(28.8)%
Project costs	1,061,962	1,466,536	(404,574)	(27.6)%
Total expenses	1,095,193	1,497,790	(402,597)	(26.9)%
Change in net assets	(455,044)	595,321	(1,050,365)	(176.4)%
Net assets, beginning of year	1,068,712	473,391	595,321	125.8 %
Net assets, end of year	$613,668	$1,068,712	$(455,044)	(42.6)%

Contacting the Corporation's Financial Management

This financial report is designed to provide New Jersey citizens and taxpayers, and the Corporation's customers, clients and creditors, with a general overview of the Corporation's finances and to demonstrate the Corporation's accountability for the funds it receives from the State. If you have questions about this report or need additional financial information, contact the Office of the Chief Financial Officer, NJSCC, P.O. Box 991, Trenton, NJ 08625-0991, or visit our web site at: **www.njscc.com**.

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Financial Statements

For the Year Ended December 31, 2006

BASIC FINANCIAL STATEMENTS

PART II-A

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Statement of Net Assets and General Fund Balance Sheet

December 31, 2006

	General Fund Total	Adjustments (Note 8)	Statement of Net Assets
Assets			
Cash and cash equivalents	$896,731,246		$896,731,246
Receivables	482,450		482,450
Prepaid expenses	184,073		184,073
Capital assets-net of accumulated depreciation of $5,483,776		$6,690,508	6,690,508
Total assets	897,397,769	6,690,508	904,088,277
Liabilities			
Accrued project expenditures	190,074,958	21,371,085	211,446,043
Other accrued liabilities	3,110,784	638,355	3,749,139
Deposits	75,224,889		75,224,889
Total liabilities	268,410,631	22,009,440	290,420,071
Fund Balances and Net Assets			
Fund balances:			
Reserved for prepaids	184,073	(184,073)	
Reserved for qualified zone academies	2,689,268	(2,689,268)	
Unreserved-designated for schools construction special revenue fund	626,113,797	(626,113,797)	
Total fund balances	628,987,138	(628,987,138)	
Total liabilities and fund balances	$897,397,769		
Net Assets			
Invested in capital assets		6,690,508	6,690,508
Restricted for qualified zone academies		2,689,268	2,689,268
Restricted for schools construction special revenue fund		604,288,430	604,288,430
Total net assets		$613,668,206	$613,668,206

See accompanying notes.

New Jersey Schools Construction Corporation
(a component unit of the State of New Jersey)

Statement of Activities and General Fund Revenues, Expenditures and Changes in Fund Balances

For the Year ended December 31, 2006

	General Fund Total	Adjustments (Note 8)	Statement of Activities
Revenues			
School Construction Program:			
EFCFA funding received from State	$600,000,000		$600,000,000
Bidding fees-plans and specs	30,750		30,750
General:			
Investment earnings	39,701,591		39,701,591
Rental property income	386,292		386,292
Other revenue	29,952		29,952
Total revenues	640,148,585		640,148,585
Expenditures/Expenses			
Personnel and benefits	22,179,737	$75,934	22,255,671
General and administrative	7,371,165		7,371,165
Program costs	2,090,313		2,090,313
Capital expenditures	349,158	(349,158)	-
Capital depreciation		1,513,787	1,513,787
Project costs	1,063,590,663	(1,628,915)	1,061,961,748
Total expenditures/expenses	1,095,581,036	(388,352)	1,095,192,684
Excess of expenditures (over)/under revenues	(455,432,451)	388,352	
Change in net assets			(455,044,099)
Fund Balance/Net Assets			
Beginning of year, January 1, 2006	1,084,419,589	(15,707,284)	1,068,712,305
End of year, December 31, 2006	$628,987,138	$(15,318,932)	$613,668,206

See accompanying notes.

1. Nature of the Corporation

The New Jersey Schools Construction Corporation (the "Corporation") is a subsidiary organization of the New Jersey Economic Development Authority ("NJEDA") and a component unit of the State of New Jersey ("State"). The Corporation was created on October 1, 2002, pursuant to N.J.S.A. 34:1B-159 and Executive Order #24 as a subsidiary of the NJEDA. With the exception of the power to incur indebtedness, the Corporation assumed all the responsibilities and obligations conferred upon the NJEDA pursuant to the Educational Facilities Construction and Financing Act, P.L.2000, c.72 ("EFCFA"). The Corporation is governed by its own Board of Directors and is fiscally dependent upon the State for funding.

The EFCFA has been adopted by the Legislature in response to the New Jersey Supreme Court's decision in Raymond Abbott et al. v. Fred G. Burke, 153 N.J. 480 (1998). This decision requires the State to provide certain educational infrastructure improvements in the poor, urban school districts ("Abbott School Districts"). The EFCFA provides for an aggregate $8.6 billion principal amount of bond proceeds ("EFCFA funding") to be issued by the NJEDA and transferred to the Corporation. Of this amount, the EFCFA has allocated $6 billion for the Abbott School Districts, $2.5 billion for non-Abbott districts, and $100 million for vocational schools. Pursuant to the EFCFA, the Corporation is responsible for the design and construction of school facilities in the Abbott School Districts. It has the same responsibility for districts that receive 55% or more State funding for education and those that are designated as level II State monitoring by the New Jersey Department of Education ("DOE"). School facilities projects constructed in any of the 31 designated Abbott School Districts are eligible for full funding by the State. Additionally, the Corporation is responsible for providing grants to fund the State share of school facilities projects approved by DOE in districts with an aid percentage of less than 55%. Those districts that receive less than 55% funding may elect to have the Corporation undertake the construction of their school facilities projects.

The Corporation has reviewed its current operating cost obligations and outstanding commitments. It has concluded that sufficient resources are available to satisfy these anticipated expenditures through at least January 1, 2008. Assuming the realization of assets and payment of liabilities in the ordinary course of business, the accompanying financial statements have been prepared on the basis that the Corporation will continue to operate as a going concern.

As discussed above, the Corporation has assessed the status of its ongoing operations, outstanding construction projects, and ability to meet its contractual commitments. As of December 31, 2006, the Corporation has 32 school facilities projects under construction throughout the Abbott School Districts. The Corporation expects that all of these projects will be completed with the remaining authorized funding provided under the EFCFA. Furthermore, the Corporation foresees the majority of these projects in construction being completed during the next two years. The Corporation has 42 additional Abbott School District projects in various stages of design that were approved for construction in 2005 as part of the Corporation's capital plan. The DOE, in conjunction with the Corporation, is currently in the process of reviewing and prioritizing these projects to determine which can be constructed with the remaining authorized funds. The DOE and the Corporation are also reviewing numerous other projects in various stages of design and pre-development that are suspended due to the lack of available funding. Once this review and prioritization is completed, the Corporation will neither undertake any additional school facilities projects nor provide any new funding grants to school districts unless additional funding is provided by the State. As discussed below, the Interagency Working Group on School Construction ("Working Group") has recommended that the State Legislature provide $2.5 billion in additional funding for the Abbott School Districts and $750 million for Regular Operating Districts. There can be no assurance that the Corporation will receive additional funding above the $8.6 billion authorized by the State under the EFCFA.

Recent Developments

(a) Legislative Developments

On February 7, 2006, Governor Jon S. Corzine signed Executive Order #3 ("E.O. #3") to facilitate review and reform at the Corporation. Among other things, E.O. #3 mandates the following:

- Establishes the position of Special Counsel to the Governor for School Construction ("Special Counsel") to serve as the Governor's representative in all matters pertaining to the management and operations of the Corporation and to serve on the Corporation's Board of Directors. In E.O. #3, Governor Corzine named Scott A. Weiner as Special Counsel; however, since that time Mr. Weiner was named Transitional Chief Executive Officer ("CEO") of the SCC in March 2006 and permanent CEO in September 2006.

- Creates the Working Group comprised of the Special Counsel serving as its Chairman, the Corporation's Board Chairman, the Commissioner and staff of the Department of Education, the State Treasurer; and the Commissioner and staff of the Department of Community Affairs. The Working Group is authorized and directed to:

  - Review the entire School Construction Program and the laws, regulations, and policies governing educational facilities. It will also develop recommendations, including statutory and regulatory initiatives, for reforms to be presented to the Governor.

  - Consider and develop specific recommendations for reorganization of the Corporation.

  - Develop, for consideration by the Corporation and the Commissioner of Education, recommendations that provide immediate improvements in the operation and management of the School Construction Program. Such recommendations would establish an effective program to design and build schools in collaboration with local school boards and communities.

- Creates a Citizens Advisory Panel to assist the Working Group in fulfilling its mission. The panel shall consist of five public members appointed by the Governor. Two of the five members shall be appointed by the Governor upon the separate recommendations of the President of the Senate and the Speaker of the Assembly.

- Directs the Attorney General to provide such assistance to the Corporation as may be necessary to immediately review the adequacy of contracts entered into by the Corporation. It also directs the commencement of legal proceedings to recover monies disbursed due to either design errors, overcharges for completed work, or other causes for which the Corporation has a right to seek recovery.

- Directs the Commissioner of Education to institute such organizational changes as are required to ensure coordination of school construction activities with other Abbott initiatives and to enhance the (i) management and active participation of the DOE in the School Construction Program for all matters regarding educational policy (ii) development and application of educational facilities standards, and (iii) priority-setting by and among local school districts.

During 2006, the Working Group made several recommendations for reform at the SCC. They are contained in the three Working Group reports issued to the Governor. The most noteworthy recommendations include (1) transitioning the SCC's responsibilities to a new authority whose governance would be devoted exclusively to the mission of designing and constructing schools (2) developing a prioritization methodology to provide a systematic approach to prioritizing current and future projects (3) increasing collaboration with school districts, municipalities, the DOE, and the Legislature (4) sharing responsibility for site acquisition with local school districts (5) identifying specific statutory changes needed to make the School Construction Program more flexible and efficient (6) reforming the Long Range Facility Plan process, and (7) requesting that the Legislature provide additional funding of $2.5 billion for Abbott School Districts and $750 million for Regular Operating Districts.

(b) Potential Reorganization of the Corporation

As mentioned above, the Working Group recommended that the responsibilities now vested in the Corporation be transitioned to a new, independent authority ("New Authority for Schools") that is located in, but not of, the Department of the Treasury. The New Authority for Schools would have both a governance and oversight board. Members of these boards would be selected based on their specific backgrounds and knowledge of the activities of the authority.

Any change in the organizational structure of the Corporation would require an act of the New Jersey State Legislature.

As of the date of this report, management has no knowledge of either the eventual organizational structure of the Corporation or the likelihood that the current organizational structure will continue to exist for the remainder of 2007.

2. Summary of Significant Accounting Policies

(a) Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all the activities of the Corporation.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific program. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment, and (2) EFCFA funding received from the State which monies are restricted to meeting either the operational or capital requirements of the School Construction Program.

Separate financial statements are provided for the Corporation's governmental fund (these are also referred to as the "general fund" financial statements). Because the Corporation operates a single governmental program, its government-wide and governmental fund financial statements have been combined using a columnar format that reconciles individual line items of general fund financial data to government-wide data in a separate column on the face of the financial statement.

(b) Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows.

The Corporation's governmental fund is classified as a general fund and its financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Corporation considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting; however, expenditures related to compensated absences and accruals associated with remediation of the Dr. Martin Luther King, Jr. Middle School in Trenton (see Note 9) are recorded only when payment is due.

(c) Revenue Recognition

The Corporation charges a minimal fee during the bidding process for copies of the design plans and specifications as specified in the construction project advertisements. Rental revenue is received under a month-to-month lease occupancy agreement. Acquisitions of various properties for the construction of school facilities projects generate rental revenue prior to the relocation of the occupants. Fees and rental revenues are recognized when received.

(d) Cash Equivalents

Cash equivalents consist of highly liquid debt instruments with original maturities of three months or less, and participation in the State's Cash Management Fund ("NJCMF"), a fund managed by the Division of Investment under the Department of Treasury. It consists of U.S. Treasury obligations, government agencies obligations, certificates of deposit and commercial paper. Cash equivalents are stated at fair value.

(e) Prepaid Expenses

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

(f) Capital Assets

Capital assets are reported in the governmental activity column in the government-wide financial statements and are recorded at historical cost or estimated historical cost if purchased and constructed. The Corporation's current capitalization threshold is $10,000 for individual items meeting all other capitalization criterion. As of December 31, 2006, the Corporation's capital assets consist of leasehold improvements, equipment, computer software and furniture and fixtures. Depreciation is provided by the straight-line method over the shorter of the life of the lease or the useful life of the related asset.

(g) Taxes

The Corporation is exempt from all federal and state income taxes and real estate taxes.

(h) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

(i) Recently Issued GASB Standard

In June 2004, the Government Accounting Standards Board ("GASB") issued Statement No. 45, *"Accounting and Financial Reporting by Employers for Postretirement Benefits Other Than Pensions,"* which establishes standards of accounting and financial reporting for other postretirement benefits ("OPEB") expense and related OPEB liabilities or assets, financial statement disclosures and required supplementary information. The Corporation is required to implement Statement No. 45 during the fiscal year ending December 31, 2007. As of December 31, 2006, the Corporation has not determined the future impact of Statement No. 45 on its financial statements.

3. Cash, Cash Equivalents and Investments

(a) Cash Flows

Overall cash and cash equivalents decreased during the year by approximately $470 million to $897 million as follows:

Cash and cash equivalents, beginning of year	$1,366,305,039
Changes in cash:	
EFCFA funding received from State	600,000,000
Investment and interest income	39,701,591
Project costs	(1,069,330,378)
SCC administrative and program costs	(30,483,062)
Local share deposits, net	(9,564,640)
Other, net	102,696
Cash and cash equivalents, end of year	$896,731,246

(b) Cash and Cash Equivalents

Operating cash, in the form of Negotiable Order of Withdrawal ("NOW") accounts, is held in the Corporation's name by a commercial banking institution. At December 31, 2006, the carrying amount of operating cash is $3,181,492 and the bank balance is $3,180,906. Regarding the amount held by a commercial banking institution, $100,000 is insured with Federal Deposit Insurance.

Pursuant to GASB Statement No. 40, "Deposit and Investment Risk Disclosures" ("GASB 40"), NOW accounts are profiled in order to determine exposure, if any, to custodial credit risk (risk that in the event of failure of the counterparty the account owner would not be able to recover the value of its deposits or investment). Deposits are considered to be exposed to custodial credit risk if they are: uncollateralized (securities not pledged to the depositor), collateralized with securities held by the pledging financial institution, or collateralized with securities held by the financial institution's trust department or agent but not in the government's name. At December 31, 2006, all of the Corporation's deposits were collateralized by securities held in its name and, accordingly, not exposed to custodial credit risk. The Corporation does not have a policy for custodial credit risk.

As of December 31, 2006, cash and cash equivalents include $75.1 million for local share deposits (see Note 5).

(c) Investments

In order to maximize liquidity, the Corporation utilizes the NJCMF as its sole investment. The NJCMF invests pooled monies from various State and non-State agencies in primarily short-term investments. These investments include: U.S. Treasuries, short-term Commercial Paper, U.S. Agency Bonds, Corporate Bonds, and Certificates of Deposit. Agencies that participate in the NJCMF typically earn returns that mirror short-term investment rates. Monies can be freely added or withdrawn from the NJCMF on a daily basis without penalty. At December 31, 2006, the Corporation's investments in the NJCMF total $893,549,754.

Custodial Credit Risk: Pursuant to GASB 40, the NJCMF, which is a pooled investment, is exempt from custodial credit risk disclosure. The Corporation does not have a policy for custodial credit risk.

Credit Risk: The Corporation does not have an investment policy regarding the management of credit risk. GASB 40 requires that disclosure be made as to the credit rating of all debt security investments except for obligations of the U.S. government or investments guaranteed by the U.S. government. The NJCMF is not rated by a rating agency.

Interest Rate Risk: The Corporation does not have a policy to limit interest rate risk. The average maturity of the Corporation's sole investment, the NJCMF, is less than one year.

4. Prepaid Expenses

As of December 31, 2006, the Corporation's prepaid expenses are as follows:

Office rents	$173,554
Other	10,519
Total prepaid expenses	$184,073

5. Deposits

The Corporation has received funds from several local school districts as required by Local Share Agreements for the funding of the local share portion of non-Abbott school facility projects, or to cover certain ineligible costs pertaining to projects in the Abbott School Districts. These deposits, including investment earnings, are reflected as liabilities in the accompanying financial statements.

As of December 31, 2006, deposits held in bank accounts are as follows:

Barnegat Township	$21,810,771
Egg Harbor Township	20,980,762
Buena Borough	9,822,702
Clark Township	8,445,065
Cumberland Township	6,798,757
Neptune Township	2,400,358
Harrison Township	1,413,151
City of Newark	1,314,476
Manchester Township	660,045
Fairfield Township	507,888
Burlington City	507,712
Other local share deposits	434,423
Total local share deposits	75,096,110
Other deposits	128,779
Total deposits	$75,224,889

6. Rental of Office Space

The Corporation rents commercial office space that is utilized by its staff at its Trenton Headquarters, Jersey City, Newark, and West Paterson Regional Offices. The remaining terms of these leases range from 8 months to over 7 years. Total rental expense for the year ended December 31, 2006 amounted to $2,002,753.

Future rent commitments under operating leases are as follows:

2007	$1,925,007
2008	1,688,720
2009	1,573,602
2010	1,508,531
2011	1,183,176
2012-2014	2,464,987
Total future rent expense	$10,344,023

7. Capital Assets

Capital asset activity for the year ended December 31, 2006 is as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Leasehold improvements	$7,727,448	$123,251	$ -	$7,850,699
Furniture and fixtures	3,037,818	-	-	3,037,818
Equipment	1,059,860	-	-	1,059,860
Construction in progress	-	225,907	-	225,907
Capital assets-gross	11,825,126	349,158	-	12,174,284
Less: accumulated depreciation	3,969,989	1,513,787	-	5,483,776
Capital assets-net	$7,855,137	$(1,164,629)	$ -	$6,690,508

Construction in progress consists of computer software under development.

8. Reconciliation of Government-Wide and Fund Financial Statements

(a) Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets

"Total fund balances" for the Corporation's general fund ($628,987,138) differs from the "net assets" reported on the statement of net assets ($613,668,206). This difference results from the long-term economic focus of the statement of net assets versus the current financial resources focus of the fund balance sheet. When capital assets (leasehold improvements, equipment, and furniture and fixtures) that are to be used in the Corporation's activities are constructed or acquired, the costs of those assets are reported as expenditures in the fund financial statements. However, the statement of net assets includes those capital assets among the assets of the Corporation as a whole. In addition, expenses associated with depreciation and noncurrent compensated absences are not recorded in the fund financial statements.

Fund balances	$628,987,138
Capital assets, net of related depreciation of $5,483,776	6,690,508
Accrued project expenditures	(21,371,085)
Compensated absences	(638,355)
Net assets	$613,668,206

(b) Explanation of certain differences between the governmental fund statement of revenues, expenditures, and changes in fund balances and the government-wide statement of activities

The governmental fund statement of revenues, expenditures, and changes in fund balances includes a reconciliation between excess of expenditures over revenues and changes in net assets as reported in the government-wide statement of activities. Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. Also, some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.

Excess of expenditures over revenues	$(455,432,451)
Capital asset acquisitions	349,158
Depreciation expense	(1,513,787)
Project costs	1,628,915
Compensated absences	(75,934)
Changes in net assets	$(455,044,099)

9. Commitments and Contingencies

(a) Contractual Commitments

At December 31, 2006, the Corporation has approximately $1.957 billion of unaccrued contractual commitments relating to future expenditures associated with school facilities projects.

(b) Contractor Claims

Numerous contractor claims not involving lawsuits have been filed with the Corporation by design consultants, general contractors and project management firms relating to disputes concerning school construction matters (e.g., delays, labor and material price increases). The Corporation resolves contractor claims by following the administrative process noted in the relevant contract. As of December 31, 2006, the Corporation's potential loss from these claims has been reasonably estimated to be approximately $20.3 million, which represents an increase of $8.3 million from the prior year end accrual. Accordingly, as of December 31, 2006, an accrued liability of $20.3 million is reflected in the statement of net assets & general fund balance sheet and, for the year then ended, $8.3 million is charged to project costs on the statement of activities & general fund revenues, expenditures and changes in fund balances.

(c) Litigation and Insurance

During construction of the Dr. Martin Luther King, Jr. Middle School ("MLK") in Trenton, New Jersey, Turner Construction Company ("Turner"), the firm contracted by the Corporation to construct the new school facility, is alleged to have brought contaminated fill onto the site consisting of recycled concrete aggregate and other materials. Testing of samples of the fill material collected on the site has revealed the presence of several hazardous substances. The MLK site is owned by the Trenton Board of Education ("TBOE") which filed a lawsuit against the Corporation, Turner and others demanding, among other things, remediation of the site as well as costs and damages. Construction of the new school facility ceased in May 2005 with the structure being only partially completed.

TBOE has demanded that the contaminated fill be removed from the site and replaced with clean fill, which will also require that the partially-constructed school be torn down and rebuilt ("TBOE's demand"). The New Jersey Department of Environmental Protection ("NJDEP") has issued a Directive and Notice to Insurers dated September 21, 2005, and a Supplemental Directive and Notice to Insurers dated October 24, 2005, ("NJDEP Directives") which, among other things, require the Corporation to comply with TBOE's demand. The Superior Court Judge presiding over this matter has placed all litigation on hold, permitting the parties to resolve TBOE's demand in accordance with the NJDEP Directives.

The Corporation has indicated its intention to fully comply with the NJDEP Directives, including TBOE's demand. As of December 31, 2006, the partially constructed school has been torn down. Additionally, remediation work to remove the contaminated fill from the site and replace it with clean fill has begun.

As of December 31, 2006, the Corporation estimates the cost to comply with TBOE's demand to be approximately $21.4 million, which is net of $1.6 million spent to date. This cost includes removal of all contaminated fill brought onto the site and replacement with clean fill, environmental monitoring, reconstruction of the school facility to its prior state and general inflation. Accordingly, as of December 31, 2006, an accrued liability of $21.4 million is reflected on the statement of net assets. For the year ended December 31, 2006, $1.6 million is charged to project costs on the statement of general fund revenues, expenditures and changes in fund balances for the portion of work that was completed in 2006. However, the $1.6 million charge is not included on the statement of activities for the year then ended. This charge was previously included on the statement of activities in 2005 after the Corporation accrued the estimated cost of TBOE's demand. Therefore, a $1.6 million credit is shown in project costs under the adjustments column.

The Corporation will vigorously oppose unrelated allegations made by the TBOE, and intends to seek recovery from Turner and other third parties for any cost or liability incurred by the Corporation related to the contamination, or any associated effects including, but not limited to, fugitive dust that allegedly may have migrated to a nearby school facility. However, there can be no assurance as to either the outcome of this matter or the extent to which the Corporation will be successful in recovering any such cost from third parties.

The Corporation has also either received Notices of Claims or is a named defendant in several lawsuits relating to its land acquisition activities including, among other things, disputes over relocation benefits, and various claims for damages. As of December 31, 2006, management believes its exposure related to these matters is reasonably estimated to be $3.7 million, which amount represents a $1.6 million decrease from the prior year end accrual. Accordingly, as of December 31, 2006, an accrued liability of $3.7 million is reflected on the statement of net assets & general fund balance sheet and, for the year then ended, $1.6 million is credited to project costs on the statement of activities & general fund revenues, expenditures and changes in fund balances.

The Corporation maintains commercial insurance coverage for, among other things, workers' compensation, tort liability (including public liability and automobile) and property damage. As of December 31, 2006, management is not aware of any insurable claim that is expected to exceed its commercial insurance coverage. In addition, the Corporation is involved in several lawsuits not covered under its commercial insurance; however, in the opinion of management, none of these claims is expected to have a material effect on the Corporation's financial statements.

10. Employee Benefits

(a) Public Employees Retirement System of New Jersey

All active, full-time employees of the Corporation are required as a condition of employment to participate in the Public Employees Retirement System of New Jersey ("PERS" or "Plan"), a cost-sharing, multiple-employer defined benefit plan administered by the State. Employees currently contribute 5% of their annual compensation to the Plan. The Corporation's total payroll for the years ended December 31, 2006, 2005 and 2004, which approximates its covered payroll, was $17,385,246, $17,100,699 and $15,025,891, respectively.

The primary funding objective of the PERS is to accumulate sufficient plan assets during its members' active careers so as to have their pension benefits fully funded at the time of retirement. Local employers are essentially responsible by State statute to cover any shortfall in the amount of funds required to meet the retirement system's obligations and those funds available from employee contributions and investment earnings on plan assets. Thus, employers may also be required to make annual normal and accrued liability contributions to the PERS. Pursuant to State statute, annual employer contributions to the PERS are determined using the projected unit credit actuarial cost method. This method utilizes a set of actuarial assumptions to forecast a pension system's liabilities and annual funding requirements. These assumptions include such things as mortality among active and retired members, former service, expected salary increases, investment performance, and rates of disability, retirement and withdrawal. An employer's annual normal cost represents the present value of benefits that have accrued on behalf of its own members during the valuation year. An accrued liability contribution represents an employer's respective share of the pension system's unfunded actuarial liability amortized over a 30 to 40 year period. The unfunded actuarial liability of a retirement system at any time is the excess of the system's actuarial liability over the value of its assets.

The State and local employers, including independent authorities such as the Corporation, were not required to make normal contributions to the PERS between 1997 and 2004 based on Pension Security legislation passed in 1997. Beginning in 2005, mandatory normal and accrued liability contributions to the PERS were resumed since the actuarial value of the Plan's assets was insufficient to support the projected value of accrued liabilities. However, in order to minimize the immediate fiscal impact of the annual pension obligation, Chapter 108, P.L. 2003 was enacted, which calls for a phase-in of the employer's funding requirement. This State statute provides that the Treasurer shall reduce an employer's normal and accrued liability contributions to a percentage of the amount certified annually by the PERS as follows: 20% of the actuarially calculated liability is payable in 2005; not more than 40% of the actuarially calculated liability is payable in 2006; not more than 60% of the actuarially calculated liability is payable in 2007; not more than 80% of the actuarially calculated liability is payable in 2008; and 100% of the actuarially calculated liability is payable in 2009. Accordingly, in 2006 and 2005 the Corporation contributed $309,156 and $48,633, respectively, to the PERS, which was charged to personnel and benefits expense, and no amounts were contributed to the PERS in 2004. The Corporation's 2007 contribution is projected to be $618,649.

The general formula for annual retirement benefits is the final average salary divided by 55, times the employee's years of service. Pension benefits fully vest upon reaching 10 years of credited service. Members are eligible for retirement at age 60 with no minimum years of service required. Members who have 25 years or more of credited service may elect early retirement without penalty at or after age 55 and receive full retirement benefits. The PERS also provides death and disability benefits. All benefits are established by State statute. The State of New Jersey, Department of the Treasury, Division of Pension and Benefits, issues publicly available financial reports that include the financial statements and required supplementary information for the PERS. The financial reports may be obtained by writing to the State of New Jersey, Department of the Treasury, Division of Pension and Benefits, P.O. Box 295, Trenton, New Jersey, 08625-0295.

(b) Deferred Compensation

The Corporation has established an Employees Deferred Compensation Plan under section 457 of the Internal Revenue Code. All active, full-time employees are eligible to participate in the plan, which permits participants to defer a portion of their pay in accordance with the contribution limits established in section 457(b) of the Internal Revenue Code. The Corporation does not make any contributions to the plan.

(c) Post-Retirement Health Care and Insurance Benefits

The Corporation provides health benefit and prescription drug coverage through the State Health Benefits Bureau to its retirees having 25 years or more of service in the PERS or who are approved for disability retirement. Benefits are provided at no cost to the retiree. For a retiree who reaches or is 65 years of age, Medicare must become the primary coverage, with State Health Benefits providing supplemental coverage. Life insurance is provided at no cost to the retiree in an amount equal to 3/16 of their average salary during the final 12 months of active employment. Post-retirement benefits are paid on a pay-as-you-go basis. At December 31, 2006, one active employee was eligible for post-retirement benefits. Total post-retirement benefits expense for two retirees for the year ended December 31, 2006 amounted to $69,353.

11. Compensated Absences

In accordance with GASB Statement No. 16, "Accounting for Compensated Absences", the Corporation recorded a liability in the amount $638,355 as of December 31, 2006. The liability is the value of employee accrued vacation time as of the balance sheet date and vested sick leave benefits that are probable of payment to employees upon retirement. The vested sick leave benefit to retirees for unused accumulated sick leave is calculated at the lesser of ½ the value of earned time or $15,000. The payment of sick leave benefits, prior to retirement, is dependent on the occurrence of sickness as defined by the Corporation's policy; therefore, such unvested benefits are not accrued.

12. Long-Term Liabilities

During 2006, the following changes in long-term liabilities are reflected in the statement of net assets:

	Beginning Balance	Additions	Deductions	Ending Balance
Accrued project expenditures	$23,000,000	-	$1,628,915	$21,371,085
Compensated absences	562,421	$75,934	-	638,355
Total long-term liabilities	$23,562,421	$75,934	$1,628,915	$22,009,440

The general fund is normally used to liquidate long-term liabilities. As of December 31, 2006, the Corporation estimates that a majority of the $21.4 million of long-term accrued project expenditures will be liquidated in 2007.

For further information, see Notes 9 and 11.

13. Net Assets

The Corporation's net assets are categorized as: invested in capital assets; restricted for qualified zone academies; and restricted for schools construction special revenue fund.

Invested in capital assets includes leasehold improvements, furniture and fixtures, equipment and computer software used in the Corporation's operations, net of accumulated depreciation. Qualified zone restricted assets includes net assets that have been restricted in use for construction projects that qualify under Section 1397E(e)(2) of the Internal Revenue Code as qualified zone academies. Schools construction restricted assets include all net assets not included in the other two categories. When both restricted and unrestricted resources are available for use, it is the Corporation's policy to first use restricted resources then unrestricted resources as needed.

The changes during 2005 and 2006 in net assets are as follows:

	Invested in Capital Assets	Restricted for Qualified Zone Academies	Restricted for Schools Construction Special Revenue Fund	Totals
Net assets, December 31, 2004	$9,787,884	$38,885,429	$424,717,262	$473,390,575
Loss before receipt of EFCFA funding and transfers	(2,127,141)		(11,015,819)	(13,142,960)
Capital assets acquired	194,394		(194,394)	-
EFCFA funding received from State			2,075,000,000	2,075,000,000
Project expenditures		(35,345,972)	(1,431,189,338)	(1,466,535,310)
Net assets, December 31, 2005	$7,855,137	$3,539,457	$1,057,317,711	$1,068,712,305
(Loss)/Excess before receipt of EFCFA funding and transfers	(1,513,787)		8,431,436	6,917,649
Capital assets acquired	349,158		(349,158)	-
EFCFA funding received from State			600,000,000	600,000,000
Project expenditures		(850,189)	(1,061,111,559)	(1,061,961,748)
Net assets, December 31, 2006	$6,690,508	$2,689,268	$604,288,430	$613,668,206