

(See "MUNICIPAL BOND INSURANCE POLICY" and "OTHER INFORMATION—Ratings.")

In the opinion of Best Best & Krieger LLP, Riverside, California, Bond Counsel, based on existing statutes, regulations, rulings and court decisions and assuming, among other matters, compliance with certain covenants, interest on the Series A Bonds is excluded from gross income for federal income tax purposes and interest on the Series B Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that it is included in adjusted current earnings in calculating corporate alternative minimum taxable income. Interest on the Series B Bonds is not excluded from gross income for federal income tax purposes. In the further opinion of Bond Counsel, interest on the Series A Bonds and Series B Bonds is exempt from State of California personal income taxation. Bond Counsel expresses no opinion regarding other federal or State tax consequences relating to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See "OTHER INFORMATION—Tax Matters."

\$31,065,000

**REDEVELOPMENT AGENCY OF THE CITY OF RIVERSIDE
LEASE REVENUE REFUNDING BONDS**

(STATE OF CALIFORNIA DEPARTMENT OF GENERAL SERVICES PROJECT)

\$26,255,000

**2003 SERIES A
(Tax-Exempt)**

\$4,810,000

**2003 SERIES B
(Taxable)**

Dated: Date of Delivery

Due: October 1, as shown below

Authority for Issuance. The bonds captioned above (the "Bonds") are being issued by the Redevelopment Agency of the City of Riverside (the "Agency") under a Trust Agreement dated as of July 1, 2003, by and between the Agency and U.S. Bank National Association, as trustee (the "Trustee"), and a resolution of the Agency adopted on June 17, 2003.

Use of Proceeds. The Bonds are being issued to (i) provide funds to defease and refund on an advance basis the outstanding bonds of the Agency captioned "Redevelopment Agency of the City of Riverside Lease Revenue Bonds (State of California Department of General Services Project) 1994 Series A (Tax-Exempt) and 1994 Series B (Taxable) (collectively, the "1994 Bonds"), (ii) fund a reserve fund for the Bonds, and (iii) pay certain costs incurred in connection with issuing the Bonds.

Security for the Bonds. The Bonds are payable from and secured by the Agency's pledge of revenues under the Trust Agreement, consisting primarily of "Base Rental" payments received by or on behalf of the Agency under a lease entitled "Riverside/State Building Lease" dated as of April 26, 1994, as amended (the "Lease"), under which the Agency has leased to the Department of General Services of the State of California (the "Department of General Services") an office tower located in Riverside, California (the "Property"). The Bonds are also secured by all moneys on deposit in the funds and accounts established under the Trust Agreement (other than the Rebate Fund). See "SECURITY FOR THE BONDS."

"Base Rental" payments are semiannual rental payments made by the Department of General Services under the Lease for the right to use and occupy the Property. The Base Rental amounts are designed to be sufficient in both time and amount to pay, when due, the principal of and interest on the Bonds. See "SECURITY FOR THE BONDS—The Lease." Base Rental payments are subject to abatement under certain circumstances. See "SECURITY FOR THE BONDS—Abatement" and "RISK FACTORS."

Bond Terms; Book-Entry Only. The Bonds will bear interest at the rates shown below, payable semiannually on April 1 and October 1 of each year, commencing October 1, 2003, and will be issued in fully registered form in the denomination of \$5,000 or any integral multiple of \$5,000. The Bonds will be issued in book-entry only form, initially registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"). Purchasers of the Bonds will not receive certificates representing their interests in the Bonds.

Redemption. Prior to their maturity, the Bonds are subject to extraordinary redemption from insurance and condemnation proceeds, optional redemption and mandatory sinking fund redemption, as described in this Official Statement. See "THE BONDS—Redemption."

Bond Insurance. Payment of the principal of and interest on the Bonds when due will be insured by a financial guaranty insurance policy to be issued by Ambac Assurance Corporation simultaneously with the delivery of the Bonds.



THE BONDS ARE LIMITED OBLIGATIONS OF THE AGENCY AND ARE PAYABLE SOLELY FROM REVENUES DERIVED UNDER THE TRUST AGREEMENT, AS DESCRIBED HEREIN. NEITHER THE BONDS NOR THE OBLIGATION TO PAY PRINCIPAL OF OR INTEREST ON THE BONDS CONSTITUTES A DEBT OR A LIABILITY OF THE AGENCY, THE CITY OF RIVERSIDE, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL LIMITATION ON INDEBTEDNESS. IN NO EVENT WILL THE BONDS BE PAYABLE OUT OF ANY FUNDS OR PROPERTIES OTHER THAN THOSE OF THE AGENCY AS DESCRIBED IN THIS OFFICIAL STATEMENT.

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

**Maturity Schedule
[See Inside Cover]**

The Bonds are offered when, as and if issued and accepted by the Underwriter, subject to the approval as to their legality by Best Best & Krieger LLP, Riverside, California, Bond Counsel. Certain legal matters will be passed upon for the Agency by Agency Counsel and for the Underwriter by Jones Hall, A Professional Law Corporation, San Francisco, California. It is anticipated that the Bonds will be delivered in definitive form through DTC on or about July 8, 2003.

Stone & Youngberg LLC

MATURITY SCHEDULE

Series A Bonds (Tax-Exempt) \$26,255,000 Serial Bonds

<u>Maturity Date (October 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>Maturity Date (October 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>
2003	\$ 745,000	2.000%	1.000%	2014	\$1,120,000	3.750%	3.800%
2004	545,000	2.000	1.100	2015	1,195,000	3.850	3.950
2005	590,000	3.000	1.400	2016	1,275,000	4.000	4.050
2006	635,000	3.000	1.700	2017	1,365,000	5.000	4.100
2007	680,000	3.000	2.100	2018	1,470,000	5.000	4.250
2008	730,000	3.000	2.400	2019	1,580,000	5.000	4.320
2009	785,000	3.000	2.750	2020	1,700,000	5.000	4.380
2010	835,000	4.000	3.100	2021	1,820,000	5.000	4.400
2011	905,000	4.000	3.350	2022	1,950,000	5.000	4.450
2012	970,000	4.000	3.500	2023	2,085,000	5.000	4.500
2013	1,045,000	4.000	3.600	2024	2,230,000	5.000	4.550

Series B Bonds (Taxable)

\$310,000 Serial Bonds

<u>Maturity Date (October 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Price</u>
2003	\$165,000	1.200%	100.00%
2004	145,000	1.420%	100.00%

\$620,000 3.090% Term Bond due October 1, 2008, Price: 100%
\$1,110,000 4.340% Term Bond due October 1, 2014, Price: 100%
\$2,770,000 5.480% Term Bond due October 1, 2024, Price: 100%

REDEVELOPMENT AGENCY OF THE CITY OF RIVERSIDE

Ronald O. Loveridge, *Mayor*
Joy Defenbaugh, *Chairperson*
Chuck Beaty, *Member*
Ameal Moore, *Member*
Frank Schiavone, *Member*
Ed Adkison, *Member*
Nancy Hart, *Member*
Laura Pearson, *Member*

AGENCY STAFF

George A. Carvalho, *Executive Director*
Paul C. Sundeen, *Treasurer*
Colleen J. Nicol, *Secretary*
Michael J. Beck, *Deputy City Manager*
Brent A. Mason, *Assistant Treasurer*
Carol A. Britton, *Development Fiscal Manager*
Conrad Guzkowski, *Redevelopment Program Manager*
Gregory P. Priamos, Esq., *Agency Counsel*

BOND COUNSEL

Best Best & Krieger LLP
Riverside, California

VERIFICATION AGENT

McGladrey & Pullen LLP
Minneapolis, Minnesota

TRUSTEE and ESCROW BANK

U.S. Bank National Association
Los Angeles, California

Limit of Offering. No dealer, broker, salesperson or any other person has been authorized to give any information or make any representation with respect to the Bonds, other than as contained in this Official Statement, and, if given or made, any such information or representation must not be relied upon as having been authorized by the Agency. This Official Statement does not constitute an offer of any securities other than those described on the cover page or an offer to sell or a solicitation of an offer to buy, nor may there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful to make such offer, solicitation or sale. This Official Statement is not to be construed as a contract with the purchasers of the Bonds.

Information Subject to Change and Not Guaranteed. The information set forth in this Official Statement has been furnished by the Agency and other sources which are believed to be reliable, but it is not guaranteed as to accuracy or completeness. The information and expressions of opinion in this Official Statement are subject to change without notice and neither the delivery of this Official Statement nor any sale of the Bonds will, under any circumstances, create any implication that there has been no change in the affairs of the Agency since the date of this Official Statement.

Involvement of the Underwriter. The Underwriter has submitted the following statement for inclusion in this Official Statement: The Underwriter has reviewed the information in this Official Statement in accordance with, and as a part of, its responsibilities to investors under the Federal Securities Laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

Summaries. Summaries and references to statutes and documents in this Official Statement do not purport to be comprehensive or definitive and are qualified in their entirety by reference to each such statute or document.

Use of Official Statement. This Official Statement is submitted in connection with the sale of the Bonds and may not be reproduced or be used, as a whole or in part, for any other purpose.

Offering Prices. In connection with the offering of the Bonds, the Underwriter may over allot or effect transactions which stabilize or maintain the market price of the Bonds at a level above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time. The Underwriter may offer and sell the Bonds to certain dealers and dealer banks and banks acting as agent and others at prices lower than the public offering prices stated on the cover page of this Official Statement, and those public offering prices may be changed from time to time by the Underwriter.

No Registration. The Bonds have not been registered under the Securities Act of 1933, as amended, in reliance upon an exemption contained in that act. The Bonds have not been registered or qualified under the securities laws of any state.

Estimates and Forecasts. Certain statements included or incorporated by reference in this Official Statement constitute "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995, Section 21E of the United States Securities Exchange Act of 1934, as amended, and Section 27A of the United States Securities Act of 1933, as amended. Such statements are generally identifiable by the terminology used such as "plan," "expect," "estimate," "project," "budget" or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The Agency does not plan to issue any updates or revisions to the forward-looking statements set forth in this Official Statement.

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OFFICIAL STATEMENT

\$31,065,000
REDEVELOPMENT AGENCY OF THE CITY OF RIVERSIDE
LEASE REVENUE REFUNDING BONDS
(State of California Department of General Services Project)

\$26,255,000 **\$4,810,000**
2003 Series A (Tax-Exempt) **2003 Series B (Taxable)**

INTRODUCTION

This Official Statement, which includes the cover page and attached appendices, provides certain information concerning the sale and delivery of the bonds captioned above (the "Series A Bonds" and the "Series B Bonds" and, collectively, the "Bonds") being issued by the Redevelopment Agency of the City of Riverside (the "Agency"). Capitalized terms used but not defined herein have the meanings set forth in the Trust Agreement. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Authority for Issuance

The Bonds are being issued pursuant to (i) the laws of the State of California (the "State"), including Article 10 and Article 11 of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code (commencing with Section 53570), as amended (the "Act") (ii) a Trust Agreement dated as of July 1, 2003 (the "Trust Agreement"), by and between the Agency and U.S. Bank National Association, Los Angeles, California, as trustee (the "Trustee"), and (iii) and a resolution adopted by the Agency on June 17, 2003.

Financing Purpose

The proceeds of the sale of the Bonds will be used to (i) provide funds to defease and refund on an advance basis the outstanding bonds of the Agency captioned "Redevelopment Agency of the City of Riverside Lease Revenue Bonds (State of California Department of General Services Project) 1994 Series A (Tax-Exempt) and 1994 Series B (Taxable) (collectively, the "1994 Bonds"), (ii) fund a reserve fund for the Bonds, and (iii) pay certain costs incurred in connection with issuing the Bonds. See "FINANCING PLAN."

The 1994 Bonds were issued to finance the acquisition and improvement of an office tower located in Riverside, California, known as the California Tower (the "Property"). See "THE PROPERTY."

Security for the Bonds

The Series A Bonds and the Series B Bonds are payable on a parity basis from and secured by the Agency's pledge of revenues under the Trust Agreement, consisting primarily of "Base Rental" payments received by or on behalf of the Agency under a lease entitled "Riverside/State Building Lease" dated as of April 26, 1994, as amended (the "Lease"), under which the Agency has leased the Property to the Department of General Services of the State of California (the "Department of General Services"). The Bonds are also secured by all moneys on deposit in the funds and accounts established under the Trust Agreement (other than the Rebate Fund). See "SECURITY FOR THE BONDS."

THE OBLIGATION OF THE DEPARTMENT TO PAY BASE RENTAL PAYMENTS DOES NOT CONSTITUTE AN OBLIGATION OF THE STATE FOR WHICH THE STATE IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE STATE HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. THE OBLIGATION OF THE DEPARTMENT OF GENERAL SERVICES TO PAY BASE RENTAL PAYMENTS DOES NOT CONSTITUTE AN INDEBTEDNESS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTIONS.

Lease Payments

"Base Rental" payments are semiannual rental payments made by the Department of General Services under the Lease for the right to use and occupy the Property. The Base Rental amounts are designed to be sufficient in both time and amount to pay, when due, the principal of and interest on the Bonds. Under the Lease the Department of General Services has covenanted to take such action within its power as may be necessary to include all Base Rental payments in annual State budgets and to make the necessary annual allocation for all such Base Rental payments, subject to abatement (as described below). See "SECURITY FOR THE BONDS - The Lease."

Abatement

The Base Rental payments are subject to complete or partial abatement during any period in which, by reason of any material damage or destruction or condemnation of all or a portion of the Property, there is substantial interference with the use and right of possession of all or a portion of the Property by the Department of General Services. If the Base Rental payments are abated under the Lease, and are not paid from alternative sources as described in this Official Statement, the Bond Owners would receive less than the full amount of principal of and interest on the Bonds. To the extent proceeds of rental interruption insurance are available or there are moneys in the Reserve Fund for the Bonds, Base Rental payments may be made from those sources during periods of abatement. See "SECURITY FOR THE BONDS - Abatement" and "RISK FACTORS."

Municipal Bond Insurance.

Payment of the principal of and interest on the Bonds when due will be insured by a financial guaranty insurance policy to be issued by Ambac Assurance Corporation (the "Insurer") simultaneously with the delivery of the Bonds. See "FINANCIAL GUARANTY INSURANCE POLICY" and "APPENDIX E - Specimen Financial Guaranty Insurance Policy."

The Official Statement

This Official Statement contains brief descriptions of, among other things, the Agency, the Lease, the Department of General Services, the Bonds and the Trust Agreement. Such descriptions do not purport to be comprehensive or definitive. All references in this Official Statement to documents are qualified in their entirety by reference to such documents, and references to the Bonds are qualified in their entirety by reference to the form of Bond included in the Trust Agreement.

FINANCING PLAN

Use of Proceeds of the Bonds

The proceeds of the sale of the Bonds will be used to (i) provide funds to defease and refund on an advance basis the 1994 Bonds, (ii) fund a reserve fund for the Bonds, and (iii) pay certain costs incurred in connection with issuing the Bonds.

The Property

The Property is an office building known as "The California Tower," located at 3737 Main Street in the City's downtown central business district, with retail frontage on the Main Street Mall, Seventh Street and University Avenue. It is one block southwest of the Mission Inn and is approximately midway between the Convention Center to the north and the County Courthouse to the south.

The Property is an eleven-story building consisting of approximately 160,000 square feet with approximately 142,543 useable square feet. The building was constructed in the early 1970s of steel frame with a glass curtain wall. Parking for the Property is available in an adjacent public garage owned by the Parking Authority of the City.

The Department of General Services occupies approximately 122,679 usable square feet of the Property, in which it houses approximately 450 State employees. The Department of General Services subleases approximately 19,864 usable square feet on the ground floor to the Agency; the Agency has subleased this property to retail tenants.

1994 Bonds

The 1994 Bonds were issued on October 6, 1994 in the aggregate original principal amount of \$29,115,000 pursuant to an Indenture of Trust dated as of September 15, 1994 (the "1994 Indenture"), by and between the Agency and First Trust of California, National Association, as trustee. The 1994 Bonds are payable from lease payments made under the Riverside/State Building Lease dated as of April 26, 1994, as amended by an Amendment to Riverside/State Building Lease and Leaseback Agreement dated as of September 15, 1994 (collectively, the "1994 Lease").

Proceeds of the 1994 Bonds were used to reimburse the Agency for the cost of acquiring the Property and to repay the City for advances made to the Agency for related design, engineering and architectural costs for the renovation of the Property.

Refunding Plan

The Agency plans to apply a portion of the proceeds of the Bonds to prepay, defease and refund on an advance basis the outstanding 1994 Bonds.

The Trustee will deposit a portion of the proceeds from the sale of the Series A Bonds in the Series A Bonds Escrow Account established under an Escrow Deposit and Trust Agreement dated as of July 1, 2003 (the "Escrow Agreement"), by and between the Agency and U.S. Bank National Association, as escrow bank (the "Escrow Bank"), and will deposit a portion of the proceeds from the sale of the Series B Bonds in the Series B Bonds Escrow Account established under the Escrow Agreement. A portion of the funds deposited in the Escrow Fund will be invested in "Federal Securities," which are generally defined in the Escrow Agreement and the

1994 Indenture as direct obligations of (including obligations issued or held in book-entry form on the books of) the Department of the Treasury of the United States of America. The remaining funds will be held by the Escrow Bank uninvested and in cash.

The Escrow Bank will cause the funds and investments deposited in the Escrow Fund, including interest on the invested funds, to be applied for the sole purpose of paying the scheduled principal of and interest on the 1994 Bonds to and including October 1, 2004 and redeeming the 1994 Bonds in full on October 1, 2004, at a redemption price of 102%.

Sufficiency of the deposits and investment earnings for those purposes will be verified by McGladrey & Pullen LLP, Minneapolis, Minnesota. See "VERIFICATION OF MATHEMATICAL ACCURACY" below. Assuming the accuracy of McGladrey & Pullen's computations, as a result of the deposit and application of funds as provided in the Escrow Agreement, the 1994 Bonds will be defeased pursuant to the provisions of the 1994 Indenture as of the date of issuance of the Bonds.

The Federal Securities and other moneys held by the Escrow Bank in the Escrow Fund are pledged solely to the payment of the 1994 Bonds. Neither the funds deposited in the Escrow Fund nor the interest on the invested funds will be available for the payment of the Bonds.

Estimated Sources and Uses of Funds

The table below sets forth the estimated sources and uses of Bond proceeds:

	<u>Series A Bonds</u>	<u>Series B Bonds</u>	<u>Total</u>
<u>Sources of Funds</u>			
Par Amount of Bonds	\$ 26,255,000.00	\$4,810,000.00	\$31,065,000.00
Plus Net Original Issue Premium	960,102.35	-0-	960,102.35
Plus Funds Relating to the 1994 Bonds	2,417,922.43	430,500.00	2,848,422.43
Less Underwriter's Discount	<u>(129,962.25)</u>	<u>(23,809.50)</u>	<u>(153,771.75)</u>
<i>Total Sources</i>	\$29,503,062.53	\$5,216,690.50	\$ 34,719,753.03
<u>Uses of Funds</u>			
Deposit to Escrow Fund [1]	\$26,162,281.49	\$4,661,022.87	\$30,823,304.36
Deposit to Reserve Account	2,341,500.00	370,832.00	2,712,332.00
Costs of Issuance [2]	<u>999,281.04</u>	<u>184,835.63</u>	<u>1,184,116.67</u>
<i>Total Uses</i>	\$29,503,062.53	\$5,216,690.50	\$ 34,719,753.03

[1] Represents amounts to be used to refund the 1994 Bonds. See "FINANCING PLAN - Refunding Plan" above.

[2] Includes, among other costs, all printing and document preparation expenses in connection with the Bonds, fees of the rating agencies rating the Bonds, CUSIP Service Bureau charges, insurance premiums and fees incurred in connection with the Financial Guaranty Insurance Policy, legal fees and expenses of counsel with respect to the financing, and the initial fees and expenses of the Trustee and its counsel.

THE BONDS

Authority for Issuance

The Bonds are being issued pursuant to (i) the laws of the State, including the Act, (ii) the Trust Agreement, and (iii) and a resolution adopted by the Agency on June 17, 2003.

Bond Terms

Dated Date; Maturities; Denominations. The Bonds will be dated their date of delivery. Subject to the redemption provisions outlined below, the Bonds will mature on the dates and in the amounts set forth on the cover page of this Official Statement.

The Bonds will be issued in denominations of \$5,000 or any integral multiple of \$5,000.

Interest and Principal. Each Bond will bear interest at the rates set forth on the cover page of this Official Statement, payable semiannually on April 1 and October 1 of each year, beginning on October 1, 2003 (each, an "Interest Payment Date").

Each Bond will bear interest from its date until the principal of such Bond is paid. Payment of interest on the Bonds due on or before the maturity or prior redemption will be made to the person whose name appears in the Bonds registration books kept by the Trustee as of the close of business on the 15th day of the calendar month (whether or not a Business Day) next preceding each Interest Payment Date, such interest to be paid in lawful money of the United States of America.

Book-Entry Only System. The Bonds will be issued as fully registered bonds, registered in the name of Cede & Co. as nominee of The Depository Trust Company, New York, New York ("DTC") and will be available to ultimate purchasers under the book-entry system maintained by DTC. While the Bonds are subject to the book-entry system, the principal, interest and any prepayment premium with respect to a Bond will be paid by the Trustee to DTC, which in turn is obligated to remit such payment to its DTC Participants for subsequent disbursement to Beneficial Owners of the Bonds as described in this Official Statement. See "APPENDIX D – BOOK-ENTRY ONLY SYSTEM."

Redemption

Extraordinary Redemption From Insurance or Condemnation Proceeds. The Bonds are subject to redemption prior to their respective maturity dates, upon notice as provided in the Trust Agreement, at the option of the Agency, on any date, in whole or in part, from proceeds of insurance or proceeds of eminent domain proceedings, upon the terms and conditions of, and as provided in, the Trust Agreement, at a redemption price equal to the principal amount thereof together with accrued interest to the date fixed for redemption, without premium.

Optional Redemption. On and after October 1, 2013 the Bonds maturing on and after October 1, 2014 will be subject to redemption prior to their respective maturity dates, at the option of the Agency, from any available funds, including amounts deposited with the Trustee by the Agency upon the exercise by the Department of General Services of its option to purchase the Agency's right title and interest in and to any portion of the Property in accordance with the Lease, either in whole on any date or in part on any date, at a redemption

price equal to the principal amount of the bonds called for redemption, plus accrued interest to the date fixed for redemption, without premium.

Series B Bonds Mandatory Sinking Fund Redemption. Subject to the terms and conditions set forth in the Trust Agreement, the Series B Bonds maturing on October 1, 2008, October 1, 2014 and October 1, 2024 (the "2003 Series B Term Bonds") are subject to redemption prior to their respective maturity dates, in part, by lot at the principal amount thereof plus accrued interest to the date fixed for redemption, without premium, from mandatory sinking account payments on the schedule set forth below.

<u>2008 Term Series B Bonds</u>	
Sinking Fund Redemption	
<u>Date (October 1)</u>	<u>Sinking Payments</u>
2005	\$150,000
2006	150,000
2007	160,000
2008(maturity)	160,000

<u>2014 Term Series B Bonds</u>	
Sinking Fund Redemption	
<u>Date (October 1)</u>	<u>Sinking Payments</u>
2009	\$165,000
2010	175,000
2011	180,000
2012	190,000
2013	195,000
2014(maturity)	205,000

<u>2024 Term Series B Bonds</u>	
Sinking Fund Redemption	
<u>Date (October 1)</u>	<u>Sinking Payments</u>
2015	\$215,000
2016	225,000
2017	240,000
2018	250,000
2019	270,000
2020	280,000
2021	295,000
2022	315,000
2023	330,000
2024 (maturity)	350,000

Selection of Bonds for Redemption. If less than all Outstanding Bonds are to be redeemed at any one time from the proceeds of insurance or eminent domain proceedings, the Trustee will select Bonds to be redeemed from each series and from each maturity within a series on a proportionate basis; provided that within each maturity in a series, such Bonds will be selected by lot.

If less than all Outstanding Bonds are to be redeemed at any one time, other than from the proceeds of insurance or eminent domain proceedings or sinking account redemption, the Trustee will select such Bonds to be redeemed from each series and from each maturity within a series, on a proportionate basis; provided that within each maturity such Bonds will be selected by lot.

Purchase In Lieu of Redemption. In lieu of redemption of any Term Bond of a series, at any time prior to giving notice of redemption, the Trustee, upon written direction of the Agency, may apply moneys in the respective subaccount of the Principal Account being held for sinking fund redemption of such Bonds to the purchase of Term Bonds of such series and maturity at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Account) as are determined by the Agency, except that the purchase price (excluding accrued interest) may not exceed the redemption price that would be payable for such Bonds upon redemption by application of such mandatory sinking account payment. If, during the twelve-month period immediately preceding the mandatory sinking account payment date, the Trustee has purchased Term Bonds of such series and maturity with moneys in such Sinking Account, then such Bonds so purchased will be applied, to the extent of the full principal amount thereof, to reduce the next succeeding mandatory sinking account payment.

Notice of Redemption. Notice of redemption will be mailed by the Trustee, not less than 30 nor more than 60 days prior to the date fixed for redemption to (i) the respective Holders of the Bonds designated for redemption at their addresses appearing on the registration books of the Trustee, (ii) the Securities Depositories and (iii) one or more Information Services; provided, however, that so long as a book-entry system is used for the Bonds, the Trustee will send notice of redemption only to the Securities Depositories and the Information Services. Notice of redemption to the Securities Depositories and the Information Services will be given by registered mail, other electronically secure means or any other method agreed upon.

Failure by the Trustee to give notice pursuant to the Trust Agreement to any one or more of the Information Services or Securities Depositories, or the insufficiency of any such notice, will not affect the sufficiency of the proceedings for redemption. Failure by the Trustee to mail notice of redemption pursuant to the Trust Agreement to any one or more of the respective Holders of any Bonds designated for redemption will not affect the sufficiency of the proceedings for redemption with respect to the Holders to whom such notice was mailed.

Effect of Redemption. If notice of redemption has been duly given as required by the Trust Agreement, and money for the payment of the redemption price of the Bonds called for redemption is held by the Trustee, then, on the redemption date designated in such notice, such Bonds will become due and payable, and from and after the date so designated, interest on such Bonds called for redemption will cease to accrue, and the Holders of such Bonds will have no rights in respect thereof except to receive payment of the redemption price thereof.

Debt Service Schedule

The following table sets forth the annual debt service on the Bonds (assuming no Optional Redemption or Special Mandatory Redemption of the Bonds).

Debt Service Schedule

	Series A	Series A	Series A	Series B	Series B	Series B	Total
<u>Oct. 1</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt</u>	<u>Debt</u>
			<u>Service</u>			<u>Service</u>	<u>Service</u>
2003	\$745,000	\$259,976.17	\$1,004,976.17	\$165,000	\$51,452.39	\$216,452.39	\$1,221,428.57
2004	545,000	1,112,707.50	1,657,707.50	145,000	221,187.00	366,187.00	2,023,894.50
2005	590,000	1,101,807.50	1,691,807.50	150,000	219,128.00	369,128.00	2,060,935.50
2006	635,000	1,084,107.50	1,719,107.50	150,000	214,493.00	364,493.00	2,083,600.50
2007	680,000	1,065,057.50	1,745,057.50	160,000	209,858.00	369,858.00	2,114,915.50
2008	730,000	1,044,657.50	1,774,657.50	160,000	204,914.00	364,914.00	2,139,571.50
2009	785,000	1,022,757.50	1,807,757.50	165,000	199,970.00	364,970.00	2,172,727.50
2010	835,000	999,207.50	1,834,207.50	175,000	192,809.00	367,809.00	2,202,016.50
2011	905,000	965,807.50	1,870,807.50	180,000	185,214.00	365,214.00	2,236,021.50
2012	970,000	929,607.50	1,899,607.50	190,000	177,402.00	367,402.00	2,267,009.50
2013	1,045,000	890,807.50	1,935,807.50	195,000	169,156.00	364,156.00	2,299,963.50
2014	1,120,000	849,007.50	1,969,007.50	205,000	160,693.00	365,693.00	2,334,700.50
2015	1,195,000	807,007.50	2,002,007.50	215,000	151,796.00	366,796.00	2,368,803.50
2016	1,275,000	761,000.00	2,036,000.00	225,000	140,014.00	365,014.00	2,401,014.00
2017	1,365,000	710,000.00	2,075,000.00	240,000	127,684.00	367,684.00	2,442,684.00
2018	1,470,000	641,750.00	2,111,750.00	250,000	114,532.00	364,532.00	2,476,282.00
2019	1,580,000	568,250.00	2,148,250.00	270,000	100,832.00	370,832.00	2,519,082.00
2020	1,700,000	489,250.00	2,189,250.00	280,000	86,036.00	366,036.00	2,555,286.00
2021	1,820,000	404,250.00	2,224,250.00	295,000	70,692.00	365,692.00	2,589,942.00
2022	1,950,000	313,250.00	2,263,250.00	315,000	54,526.00	369,526.00	2,632,776.00
2023	2,085,000	215,750.00	2,300,750.00	330,000	37,264.00	367,264.00	2,668,014.00
2024	2,230,000	111,500.00	2,341,500.00	350,000	19,180.00	369,180.00	2,710,680.00
TOTAL	\$26,255,000	\$16,347,516.17	\$42,602,516.17	\$4,810,000	\$3,108,832.39	\$7,918,832.39	\$50,521,348.57

SECURITY FOR THE BONDS

Revenues; Pledge of Revenues

Pledge of Revenues and Funds. All Revenues and amounts on deposit in the funds and accounts established under the Trust Agreement (other than amounts on deposit in the Rebate Fund) are irrevocably pledged to the payment of the principal of, redemption premium, if any, and interest on the Series A Bonds and the Series B Bonds, on a parity basis, as provided in the Trust Agreement, and the Revenues may not be used for any other purpose while any of the Bonds remain Outstanding; provided, however, that out of the Revenues there may be allocated such sums for such purposes as are expressly permitted by the Trust Agreement. This pledge will constitute a first pledge of and charge and lien upon the Revenues (other than Revenues on deposit in the Rebate Fund) for the payment of the principal of, redemption premium, if any, and interest on the Bonds.

Revenues. The Trust Agreement defines "Revenues" as all Base Rental payments received by or on behalf of the Agency under the Lease, and all other benefits, charges, income, proceeds, profits, receipts, rents, proceeds of insurance and revenues derived by the Agency from the ownership, operation or use of the Project and the Site, including interest or profits from the investment of money in any account or fund (other than the Rebate Fund) established under the Trust Agreement. (However, once money in the Surplus Fund is released and transferred to the Agency, it will be released from the pledge and lien created under the Trust Agreement.)

Limited Obligation of the Department of General Services. THE OBLIGATION OF THE DEPARTMENT OF GENERAL SERVICES TO PAY BASE RENTAL PAYMENTS DOES NOT CONSTITUTE AN OBLIGATION OF THE STATE FOR WHICH THE STATE IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE STATE HAS LEVIED OR PLEDGED ANY FORM OF TAXATION. THE OBLIGATION OF THE DEPARTMENT OF GENERAL SERVICES TO PAY BASE RENTAL PAYMENTS DOES NOT CONSTITUTE AN INDEBTEDNESS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTIONS.

Assignment to Trustee. In the Trust Agreement the Agency will irrevocably assign and transfer to the Trustee, for the benefit of the Owners of the Bonds, all of its rights and interest in the Lease including, without limitation, its rights to receive and collect Base Rental payments from the Department of General Services under the Lease and the right to exercise such rights and remedies as are conferred on the Agency by the Lease as may be necessary to enforce payment of the Base Rental payments when due or otherwise to protect its interests upon the occurrence of an event of a default by the Department under the Lease (except the Agency's rights to indemnification under the Lease and its rights to payment of its costs and expenses under the Lease).

Application of Revenues

Under the Trust Agreement the Agency and the Trustee are required to deposit all Revenues when and as received in the Revenue Fund to be held by the Trustee. Within the Revenue Fund, the Trustee will establish separate accounts for the Series A Bonds and the Series B Bonds, and will allocate all payments of Base Rental it receives under the Lease to these accounts, as appropriate, based upon the schedules contained in the Lease.

Subject to the provisions of the Trust Agreement requiring deposits into the Rebate Fund, the Trustee will set aside all money in the Revenue Fund in the following accounts and subaccounts within the Revenue Fund in the following order of priority:

- (1) the Interest Account (including subaccounts for the Series A Bonds and the Series B Bonds);
- (2) the Principal Account (including subaccounts for the Series A Bonds and the Series B Bonds);
- (3) the Reserve Account (including subaccounts for the Series A Bonds and the Series B Bonds);
- (4) the Surplus Account.

The Trustee will hold all money in each of these accounts in trust and will apply, use and withdraw these funds only for the purposes authorized in the Trust Agreement, as described below. If the Revenues received by the Trustee and deposited in any of these accounts at any time are insufficient to make required deposits in full into the subaccounts within any such account, the Trustee will deposit such moneys transferred to such account on a pro rata basis into the various subaccounts within such account.

Interest Account. On or before the last Business Day of March and September each year, beginning on the last Business Day of September 2003, the Trustee will set aside from the respective account of the Revenue Fund and deposit in the respective subaccount of the Interest Account an amount of money which, together with any money contained therein, is equal to the aggregate amount of interest becoming due and payable on all Outstanding Series A Bonds and Series B Bonds, respectively, on the next succeeding Interest Payment Date.

All money in the Interest Account will be used and withdrawn by the Trustee solely for the purpose of paying the interest on the applicable series of Bonds as it becomes due and payable (including accrued interest on any Bonds purchased or redeemed prior to maturity).

Principal Account. On or before the last Business Day of September each year, beginning on the last Business Day of September 2004, the Trustee will set aside from the applicable account in the Revenue Fund and deposit into the applicable subaccount in the Principal Account an amount of money equal to the aggregate principal amount of all Outstanding Serial Bonds of the applicable series maturing on the next succeeding October 1. On or before the last Business Day of September each year, beginning on the last Business Day of September, 2003, the Trustee will set aside from the Revenue Fund and deposit into the applicable subaccount of the Principal Account an amount of money equal to the aggregate principal amount of all sinking payments required to be made on the next succeeding October 1 into the respective sinking accounts for all Outstanding Term Bonds of the applicable series.

No deposit need be made in the applicable subaccount of the Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal of all Outstanding Serial Bonds of the applicable series maturing by their terms on such October 1 plus the aggregate amount of all sinking account payments required to be made during the year ending on such October 1 for all Outstanding Term Bonds of the applicable series.

All money in the applicable subaccounts of the Principal Account will be used and withdrawn by the Trustee solely for the purpose of paying the principal of the applicable series of the Bonds as they become due and payable, except that any money in any sinking account payment will be used and withdrawn by the Trustee only to purchase or to redeem or to pay Term Bonds for which such sinking account payment was created.

Reserve Account. On or before the last Business Day of March and September each year, beginning on the last Business Day of September 2004, the Trustee will set aside from the applicable account of the Revenue Fund and deposit in the applicable subaccount of the Reserve Account that amount of money which is required to maintain the applicable subaccount of the Reserve Account in the full amount of the Reserve Account Requirement for the applicable series of Bonds or such larger amount as is required to be maintained in the applicable subaccount of the Reserve Account by any Supplemental Trust Agreement. No deposit need be made in a subaccount of the Reserve Account so long as there is on deposit therein a sum equal to at least the amount required by the Trust Agreement to be on deposit therein.

All money in the Reserve Account and the subaccounts therein will be used and withdrawn by the Trustee solely for the purpose of replenishing the applicable subaccount of the Interest Account or the Principal Account in that order, in the event of any deficiency at any time in either of such accounts or subaccounts therein for the purpose of paying the principal of, redemption premium, if any, or interest on the applicable series of Bonds or for the retirement of all the Bonds then Outstanding. So long as the Agency is not in default under the Trust Agreement, any amount in the applicable subaccount of the Reserve Account in excess of the amount required by the Trust Agreement to be on deposit therein may be withdrawn from the applicable subaccount of the Reserve Account and deposited in the Revenue Fund. The subaccounts of the Reserve Account are not cross-collateralized, and amounts in a subaccount of the Reserve Account relating the one series of Bonds are not available to secure Revenue Fund deficiencies attributable to the other series of Bonds.

Surplus Account. On or before October 2 of each year, beginning October 2, 2003, the Trustee will deposit in the Surplus Account all money remaining in the Revenue Fund after any deposit required to be made into the Rebate Fund and the deposits required to be made into the Interest Account, Principal Account and Reserve Account have been made. Thereafter, on October 15 each year, commencing October 15, 2003, provided the Trustee has not received any notice that the Agency is in default under the Trust Agreement or that the Department is in default under the Lease, all moneys on deposit in the Surplus Account will be released by the Trustee and transferred to the Agency for use by the Agency for any lawful purpose under the Law, and will be released from the pledge and lien created under the Trust Agreement.

The Lease

Lease Term. The term of the lease commenced on or about October 1, 1994, and will end on the earlier of October 1, 2024, or the date on which the Bonds are fully paid and retired or if the Department of General Services has purchased the Agency's right, title and interest in and to the Property (as permitted by the Lease).

Base Rental Payments. "Base Rental" payments are semiannual rental payments made by the Department of General Services under the Lease for the right to use and occupy the Property. The Base Rental amounts are designed to be sufficient in both time and amount to pay, when due, the principal of and interest on the Bonds.

Covenant to Budget and Appropriate Base Rental. Base Rental payments are payable from lawfully available funds of the State, including without limitation moneys appropriated by the State legislature. Under the Lease the Department of General Services has covenanted to take such action within its power as may be necessary to include all Base Rental payments in its annual budgets and to make the necessary annual allocation for all such Base Rental payments, subject to abatement (as described below). See "APPENDIX A – STATE OF CALIFORNIA" for a description of the State budgeting process and current status of the State budget crisis.

Additional Rental. Under the Lease the Department of General Services also agrees to pay "Additional Rental" to the Agency, generally consisting of reasonable amounts required by the Agency each year to pay its administrative costs in connection with the Property.

Abatement

Abatement During Substantial Interference with Use of Property. Base Rental payments are to be paid by the Department of General Services for and in consideration of the right to use and occupy the Property during each rental period. Except to the extent of certain amounts on hand or deposited with the Trustee, as described below, Base Rental payments will be abated during any period in which, by reason of any material damage or destruction or condemnation of the Property or any portion thereof, there is substantial interference with the use and right of possession of the Property or any portion thereof by the Department of General Services. The amount of such abatement will be such that the resulting Base Rental payments do not exceed the fair rental value of the portions of the Property as to which the damage, destruction or condemnation does not substantially interfere with the use and right of possession of the Department of General Services.

Abatement Period. Any abatement of Base Rental payments will continue for the period commencing with the date of interference resulting from the damage, destruction or condemnation and ending when such use and possession are restored and as a result the Property is again in a fully tenantable condition.

In the event of any abatement, the Lease will continue in full force and effect and the Department of General Services will be unable to terminate the Lease.

Exceptions. Notwithstanding the foregoing, there will be no abatement of Base Rental payments under the Lease to the extent of (i) amounts held by the Trustee in the Bond Fund (which are not attributable to Base Rental that has been abated) and in the Reserve Fund, (ii) amounts received in respect of rental interruption insurance, if any, and (iii) amounts, if any, otherwise legally available to the Department of General Services or the Agency and deposited with the Trustee for the purpose of making payments in respect of the Bonds.

See "RISK FACTORS – Abatement" and "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Additional Parity Bonds

Test For Issuing Additional Bonds. The Agency may at any time issue Additional Bonds payable from the Revenues on a parity with the Bonds provided the conditions set forth in the Trust Agreement are met, including (among others) the condition that the Base Rental payable by the Department of General Services under the Lease must be an amount at least sufficient to pay the interest on and principal of such Additional Bonds as the same become due, accompanied by a Certificate of the Agency or the Department to the effect that such Base

Rental is consistent with the fair rental value for the Property. See "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Additional Bonds Issued as Refunding Bonds. Nothing contained in the Trust Agreement limits the issuance of any lease revenue bonds of the Agency payable from the Revenues and secured by a pledge of and charge and lien upon the Revenues if after the issuance and delivery of such lease revenue bonds none of the Bonds theretofore issued under the Trust Agreement will be Outstanding.

Reserve Account

General. Under the Trust Agreement, a Reserve Account will be established for the Bonds (the "Reserve Account"), and will be held in trust by the Trustee.

The Trustee will deposit a portion of the proceeds of the Bonds in the amount of the Reserve Requirement for each series of Bonds into the applicable subaccount of the Reserve Account concurrently with issuance of the Bonds. The "Reserve Requirement" means, as of the date of calculation, the following:

Series A Bonds: an amount equal to the least of:

- (i) \$2,341,500,
- (ii) 10% of the aggregate principal amount of the Series A Bonds then Outstanding,
- (iii) the maximum annual debt service on the Series A Bonds in the then current Lease Year or any future Lease Year, or
- (iv) 125% of average annual debt service on the Series A Bonds payable in each Lease Year between the date of calculation and the last maturity of the Series A Bonds.

Series B Bonds: an amount equal to \$370,832.

Additional Bonds: the amount specified in the Supplemental Trust Agreement providing for the issuance of the Additional Bonds.

The subaccounts of the Reserve Account are not cross-collateralized, and amounts in a subaccount of the Reserve Account relating the one series of Bonds are not available to secure Revenue Fund deficiencies attributable to the other series of Bonds.

Substitution of Letter of Credit, Insurance Policy or Surety. In lieu of making the deposits to a subaccount of the Reserve Account under the Trust Agreement, or in replacement of moneys then on deposit in the applicable subaccount of the Reserve Account (which will be transferred by the Trustee to the Revenue Fund), the Agency may deliver to the Trustee either of the following:

- (a) The Agency may deliver, at its sole cost and expense, an irrevocable letter of credit issued by a financial institution having unsecured debt obligations rated in one of the two highest rating categories by a nationally recognized rating agency, in an amount (together with an insurance policy or surety bond (as described below) securing an amount, plus moneys and Permitted Investments, on deposit in the applicable

subaccount of the Reserve Account) equal to the applicable Reserve Account Requirement. Such letter of credit shall have a term no less than three years. At least one year prior to the stated expiration of such letter of credit, the Agency will deliver to the Trustee either

- (i) a replacement letter of credit, with substantially the terms as the previous letter of credit and issued by a financial institution having unsecured debt obligations rated in one of the two highest rating categories by a nationally recognized rating agency,
- (ii) an extension of the letter of credit for at least an additional year, or
- (iii) an insurance policy or surety bond satisfying the requirements described below.

Upon delivery of such replacement letter of credit, extended letter of credit, insurance policy, or surety bond, the Trustee will deliver the expiring letter of credit, insurance policy or surety bond to or upon the order of the Agency. If the Agency fails to deposit a replacement letter of credit, extended letter of credit, insurance policy or surety bond with the Trustee, the Agency will obtain lawfully available funds in order to make quarterly deposits with the Trustee so that an amount equal to the Reserve Account Requirement is on deposit in the applicable subaccount of the Reserve Account no later than the stated expiration date of the letter of credit.

If a drawing is made on the letter of credit, the Agency, will make such payments as may be required by the terms of the letter of credit or any obligations related thereto (but no less than quarterly pro rata payments) so that the letter of credit will, absent the delivery to the Trustee of an insurance policy or surety bond satisfying the requirements described below or the deposit in the applicable subaccount of the Reserve Account of an amount sufficient to increase the balance in the applicable subaccount of the Reserve Account to the applicable Reserve Account Requirement, be reinstated in the amount of such drawing within one year of the date of such drawing.

(b) The Agency may also deliver to the Trustee an insurance policy or surety bond securing an amount, together with moneys, Permitted Investments or letters of credit on deposit in the applicable subaccount of the Reserve Account, no less than the Reserve Account Requirement, issued by an insurance company whose unsecured debt obligations (or for which obligations secured by such insurance company's insurance policies) are rated in one of the two highest rating categories by a nationally recognized rating agency. If such insurance policy or surety bond for any reason lapses or expires, the Agency, shall immediately implement the provisions described in subsections (a)(i) or (a)(iii) above or make the required deposits to the Reserve Account.

The Agency will provide written notice to any nationally recognized rating agency then rating the Bonds if a letter of credit, insurance policy or surety bond is delivered to the Trustee. If the Agency exercises its option to substitute an insurance policy or surety bond as described above for the moneys held by the Trustee in the applicable subaccount of the Reserve Account, the moneys then on deposit in the applicable Subaccount of the Reserve Account will be available to be withdrawn by the Agency and used by the Agency for any purpose permitted by the Law, or for other capital expenditures of the Agency, as applicable, whether or not related to the Property, so long as such use will not adversely affect the exclusion of interest on the Series A Bonds from gross income for federal income tax purposes.

Insurance; Condemnation Awards

Insurance. Under the Trust Agreement the Agency is required to maintain or cause to be maintained fire, lightning and extended coverage insurance, public liability insurance and rental interruption insurance with respect to the Property, all of which the Department of General Services is required to maintain under the Lease. See "APPENDIX B - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

If the Property or any portion thereof is damaged or destroyed, the Agency will make an election either to redeem Bonds or to repair or replace the Property or affected portion thereof in accordance with the Lease. The proceeds of any insurance (other than any rental interruption insurance), including the proceeds of any self-insurance, received on account of any damage or destruction of the Property or a portion thereof will as soon as possible be deposited with the Trustee and be held by the Trustee in a special account and made available for and, to the extent necessary, will be applied to redeem Bonds or applied to the cost of repair or replacement of the Property or the affected portion thereof. Pending such application, such proceeds may be invested by the Trustee as directed by the Agency in Permitted Investments that mature not later than such times that such moneys are expected to be needed.

The proceeds of any insurance, including the proceeds of any self-insurance, remaining after the property which was damaged or destroyed is restored to and made available to the Department of General Services in substantially the same condition as that which existed prior to the damage or destruction or the redemption, or provision for the redemption, of Bonds, in each case as evidenced by a Written Certificate of the Agency to such effect, will be deposited into the Accounts of the Reserve Fund to the extent that the amount therein is less than the Reserve Requirement.

Any amounts not required to be so deposited into the Reserve Fund will be paid to the Agency to be used for any lawful purpose under the Law if there is first delivered to the Trustee a Certificate of the Agency to the effect that the annual fair rental value of the Property after such damage or destruction, and after any repairs or replacements made as a result of such damage or destruction, is at least equal to the maximum amount of Base Rental payments becoming due under the Lease in the then current Lease Year or any subsequent Lease Year. If the Agency cannot deliver the certificate described in the preceding sentence, then any excess amounts will be transferred to the Revenue Fund and used to redeem Bonds.

Condemnation Awards. Under the Lease, if the Property or any portion thereof is taken by eminent domain proceedings (or sold to a government threatening to exercise the power of eminent domain) then under the Lease the eminent domain proceeds will be deposited with the Trustee in a special fund in trust and will be applied and disbursed as follows:

(a) If less than the entire Property is taken and the remainder is usable as a State office building, the Lease will continue in full force and effect as to the remainder, and if the portion taken is replaced by a facility of equal or greater utility within or adjacent to the remainder, the Trustee will disburse the proceeds to the party that incurred the expense of making such replacement, but failing the making of such replacement, the Trustee will apply the eminent domain proceeds as described in subsection (b) below.

(b) If less than the entire Property is taken and the remainder is not usable as a State office building, or if the entire Property is taken, then the term of the Lease will cease as of the day that possession is taken. The Trustee will apply the eminent domain proceeds, together with any other money then available to it for this purpose, for the payment of the entire amount of principal then due or to become due upon all Outstanding Bonds, together with the interest thereon and the redemption premiums, if

any, so as to enable the Agency to retire all of the Bonds then Outstanding by redemption or by payment at maturity; except that if the eminent domain proceeds, together with any other available moneys, are insufficient to provide for this purpose, then the eminent domain proceeds will be applied to the construction of replacement office space, and upon completion, Base Rental payments will continue under the Lease until all Outstanding bonds, together with accrued interest and redemption premiums, if any, are paid in full.

Notwithstanding the provisions of the Lease described above, the Agency will, within 90 days of the conclusion of the eminent domain proceeding, notify the Trustee and the Department in writing of whether or not the Property will be replaced or the Bonds redeemed. The proceeds of any condemnation award will as soon as possible be deposited with the Trustee and be held by the Trustee in a special account and made available for and, to the extent necessary, will be applied to redeem Bonds or applied to the cost of replacement of the Property. Pending such application, such proceeds may be invested by the Trustee as directed by the Agency in Permitted Investments that mature not later than such times that such moneys are expected to be needed.

The proceeds of any condemnation award remaining after the Property has been replaced by property available to the Department of General Services under the Lease in substantially the same condition and fair rental value as that which existed prior to the eminent domain proceedings or the redemption, or provision for the redemption, of Bonds, will be deposited into the Accounts of the Reserve Fund to the extent that the amount therein less than the Reserve Requirement.

Any amounts not required to be so deposited into the Reserve Fund will be paid to the Agency to be used for any lawful purpose under the Law, if there is first delivered to the Trustee a Certificate of the Agency to the effect that the annual fair rental value of the replacement Demised Premises is at least equal to the maximum amount of Base Rental payments becoming due under the Lease in the then current Lease Year or any subsequent Lease Year. If the Agency cannot deliver the certificate described in the preceding sentence, then any excess amounts will be transferred to the Revenue Fund and used to redeem Bonds.

FINANCIAL GUARANTY INSURANCE POLICY

The following information has been furnished by the Insurer for use in this Official Statement. A specimen Financial Guaranty Insurance Policy is attached as "APPENDIX E – SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY." Capitalized terms used but not defined in this section have the meanings given in the Financial Guaranty Insurance Policy.

Payment Pursuant to Financial Guaranty Insurance Policy

Ambac Assurance has made a commitment to issue a financial guaranty insurance policy (the "Financial Guaranty Insurance Policy") relating to the Bonds effective as of the date of issuance of the Bonds. Under the terms of the Financial Guaranty Insurance Policy, Ambac Assurance will pay to The Bank of New York, in New York, New York or any successor thereto (the "Insurance Trustee") that portion of the principal of and interest on the Bonds which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Financial Guaranty Insurance Policy). Ambac Assurance will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Trustee. The insurance will extend for the term of the Bonds and, once issued, cannot be canceled by Ambac Assurance.

The Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Bonds become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Bonds, Ambac Assurance will remain obligated to pay principal of and interest on outstanding Bonds on the originally scheduled interest and principal payment dates including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Bonds, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration.

In the event the Trustee has notice that any payment of principal of or interest on a Bond which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Financial Guaranty Insurance Policy does not insure any risk other than Nonpayment, as defined in the Policy. Specifically, the Financial Guaranty Insurance Policy does not cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity.
2. payment of any redemption, prepayment or acceleration premium.
3. nonpayment of principal or interest caused by the insolvency or negligence of any Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Financial Guaranty Insurance Policy, payment of principal requires surrender of Bonds to the Insurance Trustee together with an appropriate

instrument of assignment so as to permit ownership of such Bonds to be registered in the name of Ambac Assurance to the extent of the payment under the Financial Guaranty Insurance Policy. Payment of interest pursuant to the Financial Guaranty Insurance Policy requires proof of Holder entitlement to interest payments and an appropriate assignment of the Holder's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Bond, appurtenant coupon, if any, or right to payment of principal or interest on such Bond and will be fully subrogated to the surrendering Holder's rights to payment.

In the event that Ambac Assurance were to become insolvent, any claims arising under the Policy would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Ambac Assurance Corporation

Ambac Assurance Corporation ("Ambac Assurance") is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately \$6,362,000,000 (unaudited) and statutory capital of approximately \$3,945,000,000 (unaudited) as of March 31, 2003. Statutory capital consists of Ambac Assurance's policyholders' surplus and statutory contingency reserve. Standard & Poor's Credit Markets Services, a Division of The McGraw-Hill Companies, Moody's Investors Service and Fitch, Inc. have each assigned a triple-A financial strength rating to Ambac Assurance.

Ambac Assurance has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by Ambac Assurance will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by Ambac Assurance under policy provisions substantially identical to those contained in its financial guaranty insurance policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Obligor of the Obligations.

No representation is made by Ambac Assurance regarding the federal income tax treatment of payments that are made by Ambac Assurance under the terms of the Policy due to nonappropriation of funds by the Department of General Services.

Ambac Assurance makes no representation regarding the Bonds or the advisability of investing in the Bonds and makes no representation regarding, nor has it participated in the preparation of, the Official Statement other than the information supplied by Ambac Assurance and presented under this heading "FINANCIAL GUARANTY INSURANCE POLICY."

Available Information

The parent company of Ambac Assurance, Ambac Financial Group, Inc. (the "Company"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at <http://www.sec.gov> that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC, including the Company. These reports, proxy statements and other information can also be read at the

offices of the New York Stock Exchange, Inc. (the "NYSE"), 20 Broad Street, New York, New York 10005.

Copies of Ambac Assurance's financial statements prepared in accordance with statutory accounting standards are available from Ambac Assurance. The address of Ambac Assurance's administrative offices and its telephone number are One State Street Plaza, 19th Floor, New York, New York 10004 and (212) 668-0340.

Incorporation of Certain Documents by Reference

The following documents filed by the Company with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

1. The Company's Current Report on Form 8-K dated January 23, 2003 and filed on January 24, 2003;
2. The Company's Current Report on Form 8-K dated February 25, 2003 and filed on February 28, 2003;
3. The Company's Current Report on Form 8-K dated February 25, 2003 and filed on March 4, 2003;
4. The Company's Current Report on Form 8-K dated March 18, 2003 and filed on March 20, 2003;
5. The Company's Current Report on Form 8-K dated March 19, 2003 and filed on March 26, 2003;
6. The Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002 and filed on March 28, 2003;
7. The Company's Current Report on Form 8-K dated March 25, 2003 and filed on March 31, 2003;
8. The Company's Current Report on Form 8-K dated April 17, 2003 and filed on April 21, 2003; and
9. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2003 and filed on May 15, 2003.

All documents subsequently filed by the Company pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in "Available Information".

THE STATE OF CALIFORNIA AND THE AGENCY

State of California Finances

The Bonds are payable primarily from Base Rental payments made by the Department of General Services under the Lease for the right to use and occupy the Property. Base Rental payments are payable from lawfully available funds of the State, including without limitation moneys appropriated by the State legislature. See "APPENDIX A - THE STATE OF CALIFORNIA" for a detailed description of the State finances, historical financial results, State indebtedness and the status of the State budget negotiations.

State of California Department of General Services

The Department of General Services was created to provide for operating efficiency and economy in State government by providing central administration of business management activities. With respect to other State agencies, the Department of General Services performs both service and control functions.

The Department of General Services was created October 1, 1963 by Chapter 1768, Statutes of 1963. Legislation in 1965 further defined the authority and responsibilities of the Department and placed the Department in what is now the State and Consumer Services Agency.

Departmental responsibilities are specified primarily in Sections 14600 to 14973 of the Government Code. These responsibilities include: supervision over all matters concerning the financial and business policies of the State; providing centralized services including planning, acquisition, construction, maintenance and police protection of State buildings and property; purchasing; printing; architectural services; administrative hearings; and accounting services. The Department has the specific authority to execute and deliver the Lease under the provisions of Senate Bill 772 (Chapter 430, Statutes of 1993), approved by the Governor on September 21, 1993.

The Agency

General. The Agency was established under the Redevelopment Law on November 14, 1967. The City Council declared itself to be the Agency and since that time members of the City Council have served as both Council members and Agency members. Currently, the Agency is comprised of the following members who serve four-year terms:

<u>Name and Office</u>	<u>Expiration of Term</u>
Ronald O. Loveridge, Mayor	November 2005
Joy Defenbaugh, Chairperson	November 2003
Chuck Beaty, Member	November 2003
Ameal Moore, Member	November 2005
Frank Schiavone, Member	November 2005
Ed Adkison, Member	November 2003
Nancy Hart, Member	November 2005
Laura Pearson, Member	November 2003

Powers. The Agency is charged with the responsibility of eliminating blight within its redevelopment project areas throughout the process of redevelopment. Generally, this process culminates when the Agency disposes of land for development by the private sector. Before this can be accomplished, the Agency must complete the process of acquiring and assembling

the necessary sites, relocating residents and businesses, demolishing the deteriorated improvements, grading and preparing the sites for purchase by developers and providing for ancillary off-site improvements.

All powers of the Agency are vested in its seven members. The Agency exercises all of the governmental functions authorized under the Redevelopment Law in carrying out a project and has sufficient broad authority to acquire, develop, administer and sell or lease property, including the right of eminent domain and the right to issue bonds, notes and other evidences of indebtedness and expend their proceeds.

RISK FACTORS

The following discussion of risks is not meant to be an exhaustive list of the risks associated with the purchase of the Bonds and does not necessarily reflect the relative importance of the various risks.

Limited Obligations of the Agency and the State

Payment of principal of and interest on the Bonds depends upon the Agency's receipt of Base Rental payments from the Department of General Services. The Bonds are limited obligations of the Agency and are not secured by a legal or equitable pledge or charge or lien upon any property of the Agency or any of its income or receipts, except the Base Rental Payments and other amounts consisting of Revenues under the Trust Agreement. The obligation of the Agency to pay debt service on the Bonds does not constitute an obligation of the Agency to levy or pledge any form of taxation or for which the Agency has levied or pledged any form of taxation.

The obligation of the Department of General Services to pay Base Rental does not constitute an obligation of the State for which the State is obligated to levy or pledge any form of taxation or excises, or for which the Department of General Services has levied or pledged any form of taxation or excises. The obligation of the Department of General Services to the pay Base Rental does not constitute a debt or indebtedness of the State or any of its political subdivisions within the meaning of any constitutional or statutory debt limitation or restriction.

Although the Lease does not create a pledge, lien or encumbrance upon the funds of the State, the Department of General Services is obligated under the Lease to make Base Rental payments from any source of legally available funds (subject to abatement) and the Department of General Services has covenanted in the Lease that, for so long as the Property is available for its use, it will take such action within its powers as may be necessary to include all Base Rental in its annual budgets and make the necessary annual allocations therefore. The Department of General Services is currently liable on other obligations payable from general revenues of the State.

See "APPENDIX A – STATE OF CALIFORNIA" for a description of the State and State finances, including the current State budget crisis.

Abatement of Base Rental

Base Rental due under the Lease will be subject to abatement during any period in which, by reason of damage, destruction or condemnation of the Property or any portion thereof, there is substantial interference with the use and right of possession by the Department of General Services of the Property or any portion thereof. The Lease provides that the amount of rental abatement will be such that the resulting rental payments represent fair consideration for the use and possession of the portions of the Property not damaged, destroyed, interfered with or taken. Such abatement will continue for the period commencing with the date of such interference and ending when use and possession of the Property are restored and the Property is in fully tenantable condition.

During any period of substantial interference with the use and occupancy of the Property, the payments required to be made on the Bonds from Revenues derived under the Lease are payable only from (i) amounts on deposit in the Bond Fund (which are not attributable to Base Rental which has been abated) and in the Reserve Fund, (ii) amounts received in respect of rental interruption insurance required under the Lease or liquidated

damages, if any, and (iii) amounts which are otherwise legally available to the Department of General Services or the Agency and deposited with the Trustee for the purpose of making payments in respect of the Bonds.

If the resulting Base Rental after an abatement, together with the other moneys available to the Trustee as described above, are insufficient to pay the principal of and interest on the Bonds during the period that the abatement remains in effect, neither the Agency nor the Department of General Services will have any obligation to pay to the Trustee the amount necessary to cover such deficiency. The failure to make such payment of principal and interest under such circumstances would not constitute a default by the Department of General Services under the Lease. Under such circumstances, no remedy for non-payment is available to the Trustee or the Owners of the Bonds against the Department of General Services under the Lease.

State Budget Crisis

The State of California faces severe budget issues for fiscal year 2003-04 and possibly beyond. Governor Davis introduced the proposed 2003-04 State Budget on January 10, 2003, and on May 14, 2003, issued his revised budget for fiscal year 2003-04. The proposed 2003-04 State Budget addresses a deficit estimated by the Governor to be \$34.6 billion by the end of 2003-04 absent any corrective action by the Legislature.

The proposed 2003-04 State Budget is subject to revision by the Legislature and the Governor prior to approval, which is scheduled to occur in June 2003. (The 2003-04 State Budget has not been approved as of the date of this Official Statement.) The Agency cannot predict what impact any budget proposals will have on the financial condition of the Department of General Services or its ability to pay Base Rental under the Lease.

See "APPENDIX A – STATE OF CALIFORNIA" for a description of State finances, including the current State budget crisis.

Limitations on Remedies and Limited Recourse on Default

Limited Remedies Under the Lease. The Bonds are subject to acceleration under the Trust Agreement upon the occurrence of an event of default and with the consent of the Insurer. However, should a corresponding event of default occur under the Lease, there is no remedy of acceleration of the total Base Rental over the term of the Lease. Rather, the Trustee, as assignee of the Agency's rights under the Lease, may proceed with certain specified remedies and also take whatever action at law or in equity may appear necessary or desirable to enforce the rights of the Owners of the Bonds. All amounts received from such proceedings after subtracting therefrom all costs of collection will be credited against Base Rental due from the Department of General Services.

The Department of General Services is only liable for Base Rental on an annual basis. If the Department of General Services fails to pay Base Rental in accordance with the terms of the Lease, the Trustee would be required to seek a separate judgment each year for that year's defaulted payments of Base Rental. Any such suit for money damages would be subject to the limitations on legal remedies against public entities in the State, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest.

Possession and Re-letting by the Trustee. The Lease provides that the Trustee, acting on behalf of the Agency, may take possession of the Property. Upon doing so, the Trustee may re-let the Property to another lessee (at such rent, upon such conditions and for such terms as the Agency deems necessary or advisable) for the account of the Department of General

Services, in which event the obligation of the Department of General Services will continue to accrue from year to year in accordance with the Lease, and the Department of General Services will continue to receive the value of the use of the Property from year to year.

If the Trustee elects to attempt to re-let the Property, the rent received from such re-letting must first be applied to the expenses of re-letting and collection, including expenses necessary for repair and restoration of the Property. There is no assurance that the Trustee could re-let the Property at rental rates that would be sufficient to pay the principal and interest on the Bonds when due.

The Agency has subleased a portion of the Property to retail tenants through commercial subleases, under which these tenants have required nondisturbance protection in the event that either the Department of General Services fails to make timely payments of Base Rental or the Agency fails to make its rental payments to the Department of General Services. Should the Trustee take possession of the Property on behalf of the Agency, the Trustee has agreed not to evict a commercial tenant having a nondisturbance agreement unless that commercial tenant has not complied with the terms of its lease. However, the leases to retail tenants are subordinate to the Lease, the leaseback to the Agency and the Trust Agreement.

Judicial Limitations on Remedies. The remedies available to the owners of the Bonds upon the occurrence of an event of default under the Trust Agreement or the Lease are in many respects dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time consuming to obtain.

In addition to the limitations on remedies contained in the Trust Agreement and the Lease (see "APPENDIX B – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS"), the enforceability of the rights and remedies of the Owners and the Trustee, and the obligations incurred by the Agency and the Department of General Services, may be subject to the following: the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting the enforcement of creditors' rights generally, now or hereafter in effect; usual equity principles which may limit the specific enforcement of certain remedies; the exercise by the United States of America of the powers delegated to it by the federal Constitution; and the reasonable and necessary exercise, in certain exceptional situations, of the police power inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose. Bankruptcy proceedings, or the exercise of powers by the federal or State government, if initiated, could subject the Owners to judicial discretion and interpretation of their rights in bankruptcy or otherwise, and consequently may entail risks of delay, limitation or modification of their rights.

Pursuant to the foregoing, any remedy under the Lease or the Trust Agreement which affects the right of the public to use the Property may not be enforceable due to the essential public purposes served by the Property.

Insurance; Loss due to Uninsured Cause

Sufficiency of Insurance. Under the Trust Agreement the Agency is required to maintain or cause to be maintained fire, lightning and extended coverage insurance, public liability insurance and rental interruption insurance with respect to the Property, all of which the Department of General Services is required to maintain under the Lease. The Department of General Services and the Agency make no representation as to the ability of any insurer to fulfill its obligations under any insurance policy or policies required under the Lease, and no assurance can be given as to the adequacy of any such insurance to fund necessary repair or replacement or to pay principal of and interest on the Bonds when due. See "SECURITY FOR THE BONDS – Insurance; Condemnation Awards."

Seismic Considerations; Absence of Earthquake Insurance. The City, like much of California, is subject to seismic activity that could result in damage to or destruction of the Property. Although no major active faults are known to exist in the City, there are several major active fault zones transecting Riverside County in the vicinity of the City that could cause strong ground motion. These faults include the San Andreas fault (located 11 miles from the City's downtown), the San Jacinto fault (located 7 miles from the City's downtown), and the Elsinore fault (located 13 miles from the City's downtown). No assurance can be given that a future seismic event will not materially adversely affect the Property.

The Lease requires the Department of General Services to maintain insurance on the Property against earthquakes only if the Department of General Services determines in good faith that the premiums, coverage and availability are reasonable. The Department of General Services does not currently plan to obtain insurance against earthquake, and there can be no assurance that such earthquake insurance will be acquired or maintained by the Department of General Services in the future.

Loss due to Uninsured Cause. The Property could be damaged or destroyed due to earthquake or other catastrophic events (such as civil disturbance or acts of terrorism or war) which are not covered under the hazard or rental interruption insurance currently required by the Lease. Under these circumstances, an abatement of Base Rental would likely occur and continue until the Property was repaired or replaced. There is currently no obligation on the part of the Agency or the Department of General Services to repair or replace the Property under the Lease. See "- Abatement of Base Rental" above and "APPENDIX B - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - The Trust Agreement."

Tax Exemption of the Series A Bonds

The Agency has covenanted in the Trust Agreement that it will take all actions necessary to assure the exclusion of interest on the Series A Bonds from the gross income of the Owners of the Series A Bonds to the same extent as such interest is permitted to be excluded from gross income under the Internal Revenue Code of 1986, as amended. If the Agency fails to comply with this tax covenant, the interest on the Series A Bonds may become includable in the gross income of the Owners thereof for federal tax purposes. See "OTHER INFORMATION - Tax Matters." *Interest on the Series B Bonds is not excluded from gross income under the Internal Revenue Code.*

OTHER INFORMATION

Certain Legal Matters

The validity of the Bonds and certain other legal matters are subject to the approving opinion of Best Best & Krieger LLP, Riverside, California, Bond Counsel. Certain matters will be passed upon for the Underwriter by Jones Hall, A Professional Law Corporation, San Francisco, California. Certain legal matters will be passed upon for the Agency by Agency counsel.

Payment of the fees and expenses of Bond Counsel and Underwriter's Counsel is contingent upon the issuance of the Bonds.

Bond Counsel has not undertaken any responsibility for the accuracy, completeness or fairness of this Official Statement or other offering materials relating to the Bonds and expresses no opinion relating thereto.

Continuing Disclosure

The State. The Department of General Services will covenant in a Continuing Disclosure Agreement, for the benefit of the holders and beneficial owners of the Bonds, to provide certain financial information and operating data relating to the Department of General Services and the State (the "Annual Report") by not later than April 1 of each year in which any Bonds are Outstanding, commencing on April 1, 2004 with the report for the 2002-03 Fiscal Year, and to provide notices of the occurrence of certain enumerated events, if material. The Department of General Services will file, or cause to be filed, the Annual Report with each Nationally Recognized Municipal Securities Information Repository, and with the appropriate State information depository, if any. The Department of General Services will file, or cause to be filed, the notices of material events with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any). The specific nature of the information to be contained in the Annual Report or the notices of material events is set forth below in "APPENDIX C – Form of Continuing Disclosure Agreements." These covenants have been made in order to assist the Underwriter in complying with SEC Rule 15c2-12(b)(5).

The State has never failed to comply in any material respect with previous undertakings made under Rule 15c2-12(b)(5) in the past five years.

The Agency. The Agency will covenant in a Continuing Disclosure Agreement, for the benefit of the holders and beneficial owners of the Bonds, to provide notices of the occurrence of certain enumerated events, if material. The Agency will file, or cause to be filed, the notices of material events with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any). The specific nature of the information to be contained in the Agency's notices of material events is set forth below in "APPENDIX C – Form of Continuing Disclosure Agreements." These covenants have been made in order to assist the Underwriter in complying with SEC Rule 15c2-12(b)(5).

The Agency has never failed to comply in any material respect with previous undertakings made under Rule 15c2-12(b)(5) in the past five years.

Tax Matters

Series A Bonds. In the opinion of Best Best & Krieger LLP, Riverside, California, Bond Counsel, based on existing statutes, regulations, rulings and court decisions, interest on the Series A Bonds is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes.

The Internal Revenue Code of 1986 (the "Code"), imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Series A Bonds. The Agency and the Department have covenanted to comply with certain restrictions designed to assure that interest on the Series A Bonds will not be included in federal gross income. Failure to comply with these covenants may result in interest on the Series A Bonds being included in federal gross income, possibly from the date of issuance of the Series A Bonds. The opinion of Bond Counsel assumes compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring) after the date of issuance of the Series A Bonds may affect the value of, or the tax status of interest on the Series A Bonds. Further, no assurance can be given that pending or future legislation or amendments to the Code, will not adversely affect the value of, or the tax status of interest on, the Series A Bonds. Prospective owners are urged to consult their own tax advisors with respect to proposed changes to federal income tax. Bond Counsel is further of the opinion that interest on the Series A Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes. Bond Counsel observes, however, that interest on the Series A Bonds is included in adjusted current earnings in calculating corporate alternative minimum taxable income.

Prospective purchasers of the Series A Bonds should be aware that (i) with respect to insurance companies subject to the tax imposed by Section 831 of the Code, Section 832(b)(5)(B)(i) reduces the deduction for loss reserves by 15 percent of the sum of certain items, including interest on the Series A Bonds, (ii) interest on the Series A Bonds earned by certain foreign corporations doing business in the United States could be subject to a branch profits tax imposed by Section 884 of the Code, (iii) passive investment income, including interest on the Series A Bonds, may be subject to federal income taxation under Section 1375 of the Code for subchapter S corporations having subchapter C earnings and profits at the close of the taxable year and gross receipts more than 25% of which constitute passive investment income, and (iv) Section 86 of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take into account, in determining gross income, receipts or accruals of interest on the Series A Bonds.

Bond Counsel is further of the opinion that the difference between the principal amount of the Series A Bonds (the "Discount Series A Bonds") and the initial offering price to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriter or wholesalers) at which price a substantial amount of such Discount Series A Bonds was sold (excluding amounts stated to be interest and payable at least annually over the term of such Discount Series A Bonds) constitutes original issue discount which is excluded from gross income for federal income tax purposes to the same extent as interest on the Series A Bonds. Further, such original issue discount accrues actuarially on a constant interest rate basis over the term of each Discount Series A Bond and the basis of such Discount Series A Bond acquired at such initial offering price by an initial purchaser of each Discount Series A Bond will be increased by the amount of such accrued discount.

The Code contains certain provisions relating to the accrual of original issue discount or premium in the case of purchasers of the Discount Series A Bonds who purchase such Discount Series A Bonds after the initial offering of a substantial amount thereof. Owners who do not

purchase such Discount Series A Bonds in the initial offering at the initial offering prices should consult their own tax advisors with respect to the tax consequences of ownership of such Discount Series A Bonds. All holders of the Discount Series A Bonds should consult their own tax advisors with respect to the allowance of a deduction for any loss on a sale or other disposition to the extent that calculation of such loss is based on accrued original issue discount.

Series B Bonds. In the opinion of Bond Counsel, interest on the Series B Bonds is exempt from State of California personal income taxes. Interest on the Series B Bonds is not excluded from gross income for federal income tax purposes.

General. Although Bond Counsel has rendered an opinion that interest on the Series A Bonds is excluded from federal gross income, and that interest on the Series A Bonds and Series B Bonds is exempt from State of California personal income taxes, the ownership or disposition of the Bonds, and the accrual or receipt of interest on the Bonds may otherwise affect an Owner's state or federal tax liability. The nature and extent of these other tax consequences will depend upon each Owner's particular tax status and the Owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences. A copy of the proposed opinion of Bond Counsel is set forth in APPENDIX F hereto.

Absence of Litigation

There is no action, suit or proceeding known to be pending or threatened, restraining or enjoining the issuance or sale of the Bonds or the execution of the Trust Agreement, or in any way contesting or affecting the validity of the foregoing or any proceedings of the Agency taken with respect to any of the foregoing.

The Trustee

The Agency has appointed U.S. Bank National Association, a national banking association organized under the laws of the United States, to serve as Trustee. The Trustee is to carry out those duties assignable to it under the Trust Agreement. Except for the contents of this section, the Trustee has not reviewed or participated in the preparation of this Official Statement and assumes no responsibility for the nature, contents, accuracy or completeness of the information set forth in this Official Statement or for the recitals contained in the Trust Agreement or the Bonds, or for the validity, sufficiency, or legal effect of any of such documents.

Except as otherwise set forth in the Trust Agreement, the Trustee has no oversight responsibility, and is not accountable, for the use or application by the Agency of any of the Bonds authenticated or delivered pursuant to the Trust Agreement or for the use or application of the proceeds of such Bonds by the Issuer. The Trustee has not evaluated the risks, benefits, or propriety of any investment in the Bonds and makes no representation, and has reached no conclusions, regarding the value or condition of any assets or revenues pledged or assigned as security for the Bonds, or the investment quality of the Bonds, about all of which the Trustee expresses no opinion and expressly disclaims the expertise to evaluate.

Additional information about the Trustee may be found at its website at <http://www.usbank.com/corporatetrust>. The U.S. Bank National Association website is not incorporated into this Official Statement by such reference and is not a part hereof.

Verification of Mathematical Accuracy

Upon delivery of the Bonds, McGladrey & Pullen LLP, Minneapolis, Minnesota, will deliver a report on the mathematical accuracy of certain computations, contained in schedules provided to them on behalf of the Agency, relating to (a) the sufficiency of the anticipated receipts from the cash and Federal Securities deposited in the Escrow Fund to defease and redeem the 1994 Bonds in full, and (b) the "yield" on the Federal Securities deposited in the Escrow Fund and on the Bonds considered by Bond Counsel in connection with the opinion rendered by such firm that the Certificates are not "arbitrage bonds" within the meaning of Section 148 of the Internal Revenue Code of 1986, as amended.

Ratings

It is expected that, at closing, Standard & Poor's Rating Services ("S&P") will assign the Bonds a rating of "AAA," conditioned upon the issuance of the Financial Guaranty Insurance Policy.

This rating reflects only the views of the rating agency, and an explanation of the significance of this rating should be obtained from the issuing rating agency. There is no assurance that this rating will continue for any given period of time or that any rating will not be revised downward or withdrawn entirely by the issuing rating agency if, in its judgment, circumstances so warrant. Any downward revision or withdrawal of the rating may have an adverse effect on the market price of the Bonds.

Underwriting

Stone & Youngberg LLC, the Underwriter of the Bonds, has agreed to purchase the Bonds from the Agency at the following purchase prices:

Series A Bonds: The purchase price will be \$27,085,140.10 (being an amount equal to the principal amount of the Bonds (\$26,255,000), plus a net original issue premium of \$960,102.35, less an underwriter's discount of \$129,962.25).

Series B Bonds: The purchase price will be \$4,786,190.50 (being an amount equal to the principal amount of the Bonds (\$4,810,000.00), less an underwriter's discount of \$23,809.50).

The purchase contract under which the Underwriter is purchasing the Bonds provides that the Underwriter will purchase all of the Bonds if any are purchased. The obligation of the Underwriter to make such purchase is subject to certain terms and conditions set forth in the contract of purchase.

The public offering prices of the Bonds may be changed from time to time by the Underwriter. The Underwriter may offer and sell Bonds to certain dealers and others at a price lower than the offering price stated on the cover page of this Official Statement.

EXECUTION

The Agency has duly authorized the execution and delivery of this Official Statement.

REDEVELOPMENT AGENCY OF THE
CITY OF RIVERSIDE

By: _____ /s/ Paul C. Sundeen _____

Title: _____ Treasurer _____

APPENDIX A

STATE OF CALIFORNIA



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INTRODUCTION TO APPENDIX A

Importance of Appendix A. Appendix A is the part of the Official Statement that provides investors with information concerning the State of California. Investors must read the entire Official Statement, including Appendix A, to obtain information essential to making an informed investment decision.

California's financial situation. In January 2003, Governor Gray Davis said that "California now faces the most serious fiscal challenge in its history...With the pace of both the national and state economies continuing to languish, and no significant rebound in sight, California has experienced the most dramatic decline in revenues since World War II..." Credit rating agencies have considered California's financial situation. Two of them reduced the State's credit ratings in December 2002 and the third did so in February 2003. See "Ratings" in the first part of this Official Statement.

California's credit history. California has always paid the principal of and interest on its general obligation bonds, general obligation commercial paper notes, lease-purchase debt and short-term obligations, including revenue anticipation notes and revenue anticipation warrants, when due.

Overview of Appendix A. Appendix A begins with a description of recent developments regarding the State's economy and finances and then discusses the types of debt instruments that the State has issued and is authorized to issue in the future. See "Recent Developments Regarding State Economy and Finances" and "State Indebtedness." A discussion of the State's current and projected cash flow, including cash flow statements, is contained under "Cash Flow."

Appendix A continues with a discussion of the State budget process and the sources and uses of State funds. See "State Finances." Current and proposed budgets and the economic assumptions underlying the revenue projections are discussed under "Current State Budget."

Governance, management and employee information is set forth under "Overview of State Government." Demographic and economic statistical information is included under "Economy and Population."

Appendix A also includes a description of material litigation involving the State (see "Litigation") as well as debt tables (see "State Debt Tables"). Finally, Appendix A incorporates by reference the Audited Annual Financial Statements of the State For the Year Ended June 30, 2002, together with certain information required by governmental accounting and financial reporting standards to be included in the Financial Statements, including a "Management's Discussion and Analysis" that describes and analyzes the financial position of the State and provides an overview of the State's activities for the fiscal year ended June 30, 2002. See "Financial Statements" below.

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RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES

In January 2003, Governor Gray Davis said that “California now faces the most serious fiscal challenge in its history...With the pace of both the national and state economies continuing to languish, and no significant rebound in sight, California has experienced the most dramatic decline in revenues since World War II....” The decline in State revenues is attributable in large part to declines in personal income tax receipts, principally due to reduced stock-market related income tax revenues, such as capital gains realizations and stock option income, in a state that derives a large share of its revenue from a sharply progressive personal income tax. The State estimates that stock market-related personal income tax revenue declined from \$17.6 billion in fiscal year 2000-01 to \$8.6 billion in fiscal year 2001-02, and to \$5.2 billion in 2002-03, a total 70 percent decline. The severe drop in revenues was the principal cause of an \$11.1 billion reduction in the Fund Balance of the General Fund from June 30, 2001 to June 30, 2002. See “Current State Budget—Summary of State Revenues and Expenditures” and the Audited Annual Financial Statements for the Year Ended June 30, 2002 incorporated by reference in this Appendix A. See “Financial Statements” below. Through the first quarter of 2003, the State’s overall economy was stagnant, with slow growth projected for the balance of 2003 and moderate growth in 2004. See “Current State Budget – Economic Assumptions.”

In the budget for the current fiscal year (July 1, 2002 to June 30, 2003), the Governor and the Legislature addressed the continuing decline in tax revenues primarily with a combination of expenditure reductions and one-time actions, such as bond and asset sales, expenditure deferrals and interfund transfers and loans. See “Current State Budget-Fiscal Year 2002-03 Budget.” By the fall of 2002, it became apparent that budgeted expenditures would exceed projected resources, and Governor Davis convened a special session of the Legislature in December 2002 to consider corrective actions. See “Current State Budget-Continuing Budget Shortfall.” The 2003-04 Governor’s Budget, as proposed on January 10, projected a shortfall or “gap” on a budgetary basis of \$34.6 billion over the combined 2002-03 and 2003-04 fiscal years absent corrective action.

The 2003-04 Governor’s Budget (incorporating requests made in December 2002) called for budget actions totaling over \$10.2 billion early in calendar year 2003 in order to achieve maximum savings. This total included \$5.5 billion for fiscal year 2002-03. In March and April, 2003, the Legislature passed revised budget adjustment legislation totaling about \$6.9 billion in spending reductions, deferrals and funding transfers (including \$3.3 billion for fiscal year 2002-03 and \$3.6 billion for fiscal year 2003-04.) These amounts reflect the adoption of legislation to permit bonding of the State’s prospective fiscal year 2003-04 payment to the Public Employees’ Retirement System. Because the budget corrections enacted for fiscal year 2002-03 were lower than requested in the 2003-04 Governor’s Budget, the budget deficit and cash shortfall of the State in 2002-03 increased. See “Current State Budget—Continuing Budget Shortfall” and “—Fiscal Year 2003-04 Budget” below.

The Governor released the May Revision to the 2003-04 Governor’s Budget on May 14, 2003 (the “May Revision”). The May Revision projected that while some corrective action was taken in March and April 2003, the pre-corrective action budget gap has increased to about \$38.2 billion, primarily due to the cancellation of the sale of a tobacco securitization bond, lost opportunities for savings with the passage of time, and increased caseload in certain health and

correctional programs. The budget proposals in the May Revision were significantly changed from the original Governor's Budget, as is explained in more detail elsewhere in this Appendix A. See "Current State Budget—Fiscal Year 2003-04 Budget." In summary, in the May Revision, the Governor proposed to address the budget challenge in three phases: (1) eliminate an estimated \$10.7 billion budget deficit accumulated through June 30, 2003, by issuing bonds to be repaid from a temporary one-half cent increase in the State sales tax, (2) balance the fiscal year 2003-04 budget with a combination of expenditure cuts (some already approved by the Legislature in March and April), fund transfers and loans, and transfer ("realignment") of certain health and social services programs from the State to counties, and (3) pursue legislative action during the balance of the 2003 Legislative session to enact structural reforms that would eliminate an estimated \$7.9 billion structural deficit for the 2004-05 fiscal year.

As part of its cash management program, the State has regularly issued short-term obligations to meet cash flow needs. See "State Indebtedness – Cash Flow Borrowings." During the current fiscal year, the State retired \$7.5 billion of short-term obligations issued near the end of the preceding fiscal year and issued \$12.5 billion of revenue anticipation notes maturing in June 2003. The State's cash flow projections released in January 2003 indicated that the revenue anticipation notes, maturing in June 2003, could be repaid without rollover borrowings, but this assumed the Legislature would approve the full amount of the immediate budget reductions requested in the 2003-04 Governor's Budget. As those actions were delayed and ultimately adopted in lower amounts, together with the cancellation of a \$2 billion sale of tobacco settlement securitization bonds, it became evident that additional cash flow borrowing would be required in June 2003.

On June 18, 2003, the State Controller issued \$10,965,000,000 of "revenue anticipation warrants" ("RAWs"), a form of cash flow borrowing (see "State Finances—State Warrants—Reimbursement Warrants"). This borrowing will provide cash resources necessary to pay the State's obligations in June 2003 (including the maturing \$12.5 billion of revenue anticipation notes) and during the summer of 2003, after the start of the fiscal year that begins on July 1, 2003. See "Cash Flow." The May Revision projects that, absent the receipt of the \$11 billion RAWs proceeds, the State would have a cash shortfall of about \$2.5 billion at June 30, 2003.

On June 20, 2003, one element of the May Revision proposal was implemented with the determination that there were insufficient General Fund moneys available to continue to fund any portion of the vehicle license fee offsets to local governments. As a result, the vehicle license fee payable by taxpayers will return within 90 days, to the pre-1999 level. See "State Finances—Sources of Tax Revenue—Vehicle License Fee" and "Current State Budget—Fiscal Year 2003-04 Budget" below.

STATE INDEBTEDNESS

General

The State Treasurer is responsible for the sale of debt obligations of the State and its various authorities and agencies. The State has always paid the principal of and interest on its general obligation bonds, general obligation commercial paper notes, lease-purchase debt and short-term obligations, including revenue anticipation notes and revenue anticipation warrants, when due.

Capital Facilities Financing

General Obligation Bonds - The State Constitution prohibits the creation of general obligation indebtedness of the State unless a bond law is approved by a majority of the electorate voting at a general election or a direct primary. General obligation bond acts provide that debt service on general obligation bonds shall be appropriated annually from the General Fund and all debt service on general obligation bonds is paid from the General Fund. Under the State Constitution, debt service on general obligation bonds is the second charge to the General Fund after the application of moneys in the General Fund to the support of the public school system and public institutions of higher education. See "State Finances—State Expenditures" below. Certain general obligation bond programs receive revenues from sources other than the sale of bonds or the investment of bond proceeds.

As of May 1, 2003, the State had outstanding \$29,636,682,000 aggregate principal amount of long-term general obligation bonds, and unused voter authorizations for the future issuance of \$24,877,499,000 of long-term general obligation bonds. This latter figure consists of \$13,136,140,000 of general obligation bonds which are authorized to be issued initially as commercial paper notes, described below, and \$11,741,359,000 of other authorized but unissued general obligation bonds. See the table "Authorized and Outstanding General Obligation Bonds" under "State Debt Tables" below. See introduction to "State Debt Tables" for information as to bonds issued after May 1, 2003.

The General Obligation Bond Law permits the State to issue as variable rate indebtedness up to 20 percent of the aggregate amount of long-term general obligation bonds outstanding. The State issued \$1.4 billion of variable rate general obligation bonds on April 15, 2003 to inaugurate this program. Additional variable rate bonds are expected to be sold in fiscal year 2003-04.

Substantial new bond authorizations were approved by the voters on March 5, 2002 (\$2.8 billion) and November 5, 2002 (\$18.6 billion). The Legislature has also approved another \$22 billion of bond authorizations to be placed on the ballot in 2004. Additional bond proposals may also be added in 2004.

Commercial Paper Program - Pursuant to legislation enacted in 1995, voter-approved general obligation indebtedness may be issued either as long-term bonds, or, for some but not all bond acts, as commercial paper notes. Commercial paper notes may be renewed or may be refunded by the issuance of long-term bonds. The State issues long-term general obligation

bonds from time to time to retire its general obligation commercial paper notes. Pursuant to the terms of the bank credit agreement presently in effect supporting the general obligation commercial paper program, not more than \$2.0 billion of general obligation commercial paper notes may be outstanding at any time; this amount may be increased or decreased in the future. Commercial paper notes are deemed issued upon authorization by the respective finance committees, whether or not such notes are actually issued. As of May 1, 2003, the finance committees had authorized the issuance of up to \$13,136,140,000 of commercial paper notes; as of that date \$148,965,000 aggregate principal amount of general obligation commercial paper notes was outstanding, but that amount is much greater as of the date of this Official Statement. See "State Debt Tables" below.

Lease-Purchase Debt - In addition to general obligation bonds, the State builds and acquires capital facilities through the use of lease-purchase borrowing. Under these arrangements, the State Public Works Board, another State or local agency or a joint powers authority issues bonds to pay for the construction of facilities such as office buildings, university buildings or correctional institutions. These facilities are leased to a State agency or the University of California under a long-term lease which provides the source of payment of the debt service on the lease-purchase bonds. In some cases, there is not a separate bond issue, but a trustee directly creates certificates of participation in the State's lease obligation, which are marketed to investors. Under applicable court decisions, such lease arrangements do not constitute the creation of "indebtedness" within the meaning of the Constitutional provisions which require voter approval. For purposes of this section of the Official Statement and the tables under "State Debt Tables" below, "lease-purchase debt" or "lease-purchase financing" means principally bonds or certificates of participation for capital facilities where the rental payments providing the security are a direct or indirect charge against the General Fund and also includes revenue bonds for a State energy efficiency program secured by payments made by various State agencies under energy service contracts. Certain of the lease-purchase financings are supported by special funds rather than the General Fund (see "State Finances-Sources of Tax Revenue"). The tables do not include equipment leases or leases which were not sold, directly or indirectly, to the public capital markets. The State had \$6,734,133,523 General Fund-supported lease-purchase debt outstanding as of May 1, 2003. The State Public Works Board, which is authorized to sell lease revenue bonds, had \$4,069,839,000 authorized and unissued as of May 1, 2003. In addition, as of that date, certain joint powers authorities were authorized to issue approximately \$81,000,000 of revenue bonds to be secured by State leases.

Non-Recourse Debt - Certain State agencies and authorities issue revenue obligations for which the General Fund has no liability. Revenue bonds represent obligations payable from State revenue-producing enterprises and projects, which are not payable from the General Fund, and conduit obligations payable only from revenues paid by private users of facilities financed by the revenue bonds. The enterprises and projects include transportation projects, various public works projects, public and private educational facilities (including the California State University and University of California systems), housing, health facilities and pollution control facilities. There are 17 agencies and authorities authorized to issue revenue obligations (excluding lease-purchase debt). State agencies and authorities had \$42,558,532,631 aggregate principal amount of revenue bonds and notes which are non-recourse to the General Fund outstanding as of December 31, 2002, as further described in the table "State Agency Revenue Bonds and Conduit Financing" under "State Debt Tables" below.

Detailed information regarding the State's long-term debt appears in the section "State Debt Tables" below.

Cash Flow Borrowings

General - As part of its cash management program, the State has regularly issued short-term obligations to meet cash flow needs. The following table shows the amount of revenue anticipation notes ("Notes" or "RANs") and revenue anticipation warrants ("RAWs") issued in the past five fiscal years and the current fiscal year. See "Prior Fiscal Years' Financial Results" and "Current State Budget" below. The State has issued RANs in 19 of the last 20 fiscal years to partially fund timing differences between revenues and expenditures, as the majority of General Fund revenues are received in the last part of the fiscal year. RANs must mature prior to the end of the fiscal year of issuance. If additional external cash flow borrowings are required, the State has issued RAWs, which can mature in a subsequent fiscal year. See "State Finances—State Warrants" below. RANs and RAWs are both payable from any "Unapplied Money" in the General Fund of the State on the maturity date, subject to the prior application of such money to support the public school system and public institutions of higher education, to pay debt service on State general obligation bonds and commercial paper notes, to reimburse other State special funds, to the extent required by law, for internal borrowings, and to pay certain other high priority obligations including employee payrolls, pension fund contributions, Medi-Cal payments, rental on lease revenue bonds and any obligations which may in the future be determined by a court to be required to be paid in cash because of federal law or the State Constitution. See "State Finances" below.

State of California Revenue Anticipation Notes and Warrants Issued Fiscal Years 1997-98 to 2002-03

<u>Fiscal Year</u>	<u>Type</u>	<u>Principal Amount (Billions)</u>	<u>Date of Issue</u>	<u>Maturity Date</u>
1997-98	Notes	\$3.00	September 9, 1997	June 30, 1998
1998-99	Notes	1.70	October 1, 1998	June 30, 1999
1999-00	Notes Series A-B	1.00	October 1, 1999	June 30, 2000
2000-01	No Notes issued			
2001-02	Notes Series A-C	5.70	October 4, 2001	June 28, 2002
	RAWs Series A	1.50	June 24, 2002	October 25, 2002
	RAWs Series B	3.00	June 24, 2002	November 27, 2002
	RAWs Series C	3.00	June 24, 2002	January 30, 2003†
2002-03	Notes Series A and C	6.00	October 16, 2002	June 20, 2003
	Notes Series B and D	3.00	October 16, 2002	June 27, 2003
	Notes Series E – G	3.50	November 6, 2002	June 20, 2003
	RAWs Series A-B	10.965	June 18, 2003	June 16, 2004

† Called by the Controller and paid on November 27, 2002.
SOURCE: State of California, Office of the Treasurer.

CASH FLOW

The first table following shows actual monthly cash flows for the 2001-02 fiscal year, as compiled by the State Controller. The second table shows monthly cash flows for the 2002-03 fiscal year prepared by the Department of Finance. Figures for July 2002-April 2003 are actual results; the remainder are estimates prepared by the Department of Finance, based on the revenue and expenditure assumptions included in the May Revision of the 2003-04 Governor's Budget released on May 14, 2003. See "Current State Budget." Differences between these cash flow statements and the budgetary basis (modified accrual) information contained in the table "Current State Budget—Summary of State Revenues and Expenditures" primarily reflect the fact that certain funds which, on a cash basis, are received and disbursed in the current fiscal year are attributed to prior fiscal years for budget purposes.

2001-02 Fiscal Year - The State issued \$5.7 billion of 2001-02 RANs (the "2001 RANs") in October 2001, that matured on June 28, 2002. To provide additional cash resources necessary to pay the State's obligations at the end of June 2002, and into the first few months of the 2002-03 fiscal year, the State Controller issued \$7.5 billion of RAWs (the "2002 RAWs"), as listed in the table under "State Indebtedness – Cash Flow Borrowings," with maturity dates in October and November 2002, and January 2003. The 2002 RAWs were repaid in October and November 2002.

2002-03 Fiscal Year - The State issued a total of \$12.5 billion of 2002-03 RANs ("2002 RANs") in October 2002, and November 2002 to partially fund its cash flow needs in the 2002-03 fiscal year, including repayment of the 2002 RAWs issued in June 2002. While the State believed when the 2002 RANs were issued that it would have sufficient cash resources in June 2003 to pay the debt service due, circumstances since that time have reduced the State's cash position to such an extent that the debt service cannot be paid without further borrowing. See "Recent Developments Regarding State Economy and Finances." The State covenanted in its Resolution for issuance of the 2002 RANs to use its best efforts to issue RAWs if necessary to pay the 2002 RANs. Accordingly, the State Controller issued \$10.965 billion of RAWs on June 18, 2003 to provide enough additional cash to pay the debt service due on the 2002 RANs and to pay other State obligations coming due in June 2003 and in the first months of the 2003-04 fiscal year. See "2003 Revenue Anticipation Warrants" below.

The original cash flow estimates for the 2002-03 fiscal year included a number of assumptions which have been achieved, including the receipt of \$6.6 billion from the sale of Department of Water Resources power revenue bonds in November 2002 and \$2.5 billion from the sale of tobacco litigation settlement payments in January 2003. (See "State Finances—Repayment of Energy Loans" and "—Tobacco Litigation" below.) The following major factors, however, have resulted in the reduction of the cash flow estimates as the year has progressed: (1) enactment by the Legislature of mid-year budget reductions in lower amounts than requested by the Governor, (2) cancellation of the second part of the planned sale of bonds secured by tobacco litigation settlement payments, which would have produced \$2 billion of receipts for the General Fund in April 2003, and (3) higher than expected expenditures for health and social services and correctional programs due to higher caseloads/population. These negative factors were partially offset by recognition of about \$1.1 billion of additional internal borrowable resources.

The 2002-03 cash flows included below are still based on a number of assumptions for the last two months of the fiscal year, which might not be achieved.

2003 Revenue Anticipation Warrants. As noted above, the Controller issued \$10,965,000,000 of 2003 Revenue Anticipation Warrants (the "2003 Warrants") on June 18, 2003. The 2003 Warrants will all mature on June 16, 2003. Cash flows prepared by the Department of Finance, based upon the Governor's May Revision to the 2003-04 Budget, project that there will be sufficient available moneys in the General Fund (including from internal borrowing) to repay the 2003 Warrants at maturity. This projection depends upon enactment of the 2003-04 Budget and associated legislation substantially as proposed by the Governor (or with alternate budget actions having the same fiscal effects), including the issuance of deficit financing bonds, all as described further below under "Current State Budget—Fiscal Year 2003-04 Budget." On the maturity date of the 2003 Warrants, payment of principal of and interest on the 2003 Warrants is subject to the prior application of moneys in the General Fund to pay Priority Payments. "Priority Payments" are payments as and when due to: (i) support the public school system and public institutions of higher learning (as provided in Section 8 of Article XVI of the Constitution of the State), (ii) pay principal of (whether at stated maturity or upon earlier redemption) and interest on general obligation bonds of the State, (iii) provide reimbursement from the General Fund to any special fund or account to the extent such reimbursement is legally required to be made to repay borrowings therefrom, and (iv) pay State employees' wages and benefits, State payments to pension and other State employee benefit trust funds, State Medi-Cal claims, and any amounts determined after the issuance of the 2003 Warrants by a court of competent jurisdiction in a final and nonappealable judgment to be required by federal law or the State Constitution to be paid with State warrants that can be cashed immediately. Priority Payments also includes payments of principal and interest on registered warrants issued to make Priority Payments.

If it appears to the Controller that there will be insufficient available money in the General Fund to pay the 2003 Warrants at maturity, the Controller has agreed to use his best efforts to offer for sale at competitive bid and issue refunding warrants to pay the 2003 Warrants in full. See "State Financing—State Warrants—Refunding Warrants" below. While no assurance can be given that the State would be able to sell refunding warrants, the State has always been able to borrow funds to meet its cash flow needs in the past and expects to take all steps necessary to continue to have access to the short-term and long-term credit markets.

If the Controller were unable to issue refunding warrants in sufficient amounts, the State may decide to borrow under seven Forward Warrant Purchase Agreements which the State has entered into with seven financial institutions ("Participants"), on a several and not joint basis (the "Forward Purchase Agreements"), that will enable the State to borrow up to \$11.2 billion (to cover principal and accrued interest) to obtain additional cash resources to pay the principal of and interest on the 2003 Warrants on their maturity date. The Forward Purchase Agreements do not constitute a guaranty of the 2003 Warrants and contain certain conditions which must be met in order for the State to obtain advances of funds from the Participants. If the State draws upon the Forward Purchase Agreements, it will deliver to the Participants registered warrants due immediately and without a maturity date. See "State Finances--State Warrants—Registered Warrants" below for a description of the nature of registered warrants and the method by which they are repaid, as it relates to other obligations of the State. As described below, repayment by the State of the registered warrants issued to Participants is subordinate, in rank of the use of

available cash resources on any day, to payment of Priority Payments (defined above) including debt service on general obligation bonds. However, the issuance of such registered warrants will severely restrict the State's cash management flexibility.

The Forward Purchase Agreements contain a number of covenants on the part of the State relating to cash flow management and cash flow borrowing. One covenant requires the State to maximize internal borrowing from special funds (see "State Finances—Inter-Fund Borrowing" and "—Internal Borrowable Resources" below). Other covenants prohibit the State from issuing any warrants or revenue anticipation notes having a maturity date prior to the maturity date of the 2003 Warrants.

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GENERAL FUND ACTUAL CASH FLOW AND BORROWABLE RESOURCES
2001-02 FISCAL YEAR (a) (In millions)

	July	August	September	October	November	December	January	February	March	April	May	June	Total
BEGINNING CASH BALANCE	\$ 3,394	\$ 389	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,394
RECEIPTS:													
Alcoholic Beverage Excise Tax	31	24	27	23	25	25	27	20	21	24	25	24	286
Corporation Tax	148	48	1,076	252	(67)	532	11	160	860	905	189	974	5,088
Cigarette Tax	11	6	17	9	12	7	5	18	8	6	3	12	114
Inheritance, Gift and Estate Taxes	88	47	72	108	86	86	117	72	91	99	71	63	1,000
Insurance Tax	6	9	334	12	318	3,372	23	7	40	538	23	271	1,591
Personal Income Tax	2,122	2,205	3,635	2,338	1,890	3,372	5,732	1,226	851	5,849	1,012	3,063	33,295
Retail Sales and Use Tax	857	2,707	1,430	947	2,798	1,490	890	2,942	1,556	724	2,951	2,077	21,369
Income from Pooled Money Investments	54	48	61	-	104	38	30	26	28	27	28	36	480
Transfer from Special Fund for Economic Uncertainties	-	-	-	-	2	7	-	-	-	-	-	-	10
Other	168	711	363	145	454	250	217	293	249	50	158	304	3,362
TOTAL, Receipts	3,485	5,805	7,015	3,834	5,314	6,125	7,053	4,764	3,704	8,222	4,460	6,824	66,805
DISBURSEMENTS:													
State Operations:													
Payroll	851	858	854	878	867	855	858	852	851	859	860	871	10,312
University of California	282	245	241	328	274	288	308	306	353	386	262	60	3,333
Debt Service (b)	(2)	850	(35)	412	124	164	(17)	120	228	186	127	153	2,310
Other State Operations	219	560	456	434	364	228	281	68	89	20	185	118	3,022
Social Services	829	1,035	988	917	185	449	578	466	492	590	175	554	7,258
Medi-Cal Assistance	762	975	738	853	855	835	844	665	775	894	1,051	812	10,049
Other Health Services	10	68	58	18	48	31	23	57	14	44	51	40	462
Schools	1,930	3,150	2,561	3,881	2,285	2,191	2,221	3,898	2,059	3,405	1,965	1,924	31,480
Teachers' Retirement	583	-	-	96	-	-	98	-	-	96	-	-	871
Transfer to Special Fund for Economic Uncertainties	-	-	-	-	-	-	-	-	-	2,392	-	-	2,392
Other	1,026	517	805	1,219	766	640	542	384	629	902	788	740	8,958
TOTAL, Disbursements	6,490	8,268	6,686	9,046	5,768	5,881	5,732	6,816	5,490	9,764	5,464	5,272	60,447
EXCESS RECEIPTS/(DEFICIT)	(3,005)	(2,453)	349	(5,212)	(454)	444	1,321	(2,052)	(1,786)	(1,542)	(1,004)	1,552	(13,842)
NET TEMPORARY LOANS:													
Special Fund for Economic Uncertainties	-	204	-	(15)	-	(56)	(134)	133	-	2,392	-	-	2,524
Other Internal Sources	-	1,860	(349)	(473)	454	(388)	(1,103)	1,835	1,786	(850)	2,204	(4,552)	424
Revenue Anticipation Notes	-	-	-	5,700	-	-	-	-	-	-	-	(5,700)	-
Revenue Anticipation Warrants	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL, Net Temporary Loans	-	2,064	(349)	5,212	454	(444)	(1,237)	1,968	1,786	1,542	2,204	(2,752)	10,448
ENDING CASH BALANCE (c)	\$ 389	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 84	\$ -	\$ -	\$ -	\$ 1,200	\$ -	\$ -
AVAILABLE BORROWABLE RESOURCES:													
Special Fund for Economic Uncertainties	\$ 204	\$ 204	\$ 204	\$ 190	\$ 190	\$ 134	\$ 133	\$ 133	\$ 133	\$ 2,525	\$ 2,525	\$ 2,525	\$ 2,525
Other Internal Sources	11,998	12,132	11,876	11,669	11,439	11,297	10,422	10,727	10,222	9,830	10,508	10,455	10,455
Revenue Anticipation Notes	-	-	-	5,700	5,700	5,700	5,700	5,700	5,700	5,700	5,700	-	-
Revenue Anticipation Warrants	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL, Available Borrowable Resources	12,202	12,336	12,080	17,559	17,329	17,131	16,255	16,560	16,055	18,055	18,733	20,480	20,480
CUMULATIVE LOAN BALANCES:													
Special Fund for Economic Uncertainties	-	204	204	190	190	134	-	133	133	2,525	2,525	2,525	2,525
Other Internal Sources	-	1,860	1,511	1,037	1,491	1,103	-	1,835	3,621	2,771	4,975	423	423
Revenue Anticipation Notes	-	-	-	5,700	5,700	5,700	5,700	5,700	5,700	5,700	5,700	-	-
Revenue Anticipation Warrants	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL, Cumulative Loan Balances	-	2,064	1,715	6,927	7,381	6,937	5,700	7,668	9,454	10,996	13,200	10,448	10,448
UNUSED BORROWABLE RESOURCES	\$ 12,202	\$ 10,272	\$ 10,365	\$ 10,632	\$ 9,948	\$ 10,194	\$ 10,555	\$ 8,892	\$ 6,601	\$ 7,059	\$ 5,533	\$ 10,032	\$ 10,032

(a) May not add to total due to rounding. Other than Beginning Cash Balances, all amounts represent end of month balances.

(b) Includes debt service on general obligation bonds only.

(c) Ending Cash Balance represents the month-end cash balance including actual funds borrowed at the end of the month.

SOURCE: State of California, Office of State Controller.

CASHFLOW STATEMENTS
ESTIMATED 2002-03 FISCAL YEAR CASHFLOW
GENERAL FUND
(Dollars in Millions)

	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
2002-03 FISCAL CASHFLOW													
BEGINNING CASH BALANCE	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$2,397	\$3,612	\$5,626	\$5,705	\$5,626	\$0
RECEIPTS:													
Alcoholic Beverage Excise Tax	\$28	\$24	\$25	\$25	\$25	\$23	\$30	\$20	\$21	\$25	\$23	\$21	\$290
Corporation Tax	180	56	1,106	184	21	1,090	-78	171	1,152	1,209	211	1,240	6,542
Cigarette Tax	17	12	-1	21	7	10	9	11	10	7	9	10	122
Inheritance, Gift and Estate Taxes	97	71	77	69	72	89	87	91	138	59	73	68	969
Insurance Tax	14	15	367	14	10	367	15	15	377	14	14	377	1,867
Personal Income Tax	2,042	1,972	3,367	2,311	1,538	3,668	5,094	1,291	983	5,500	1,257	3,052	32,075
Retail Sales and Use Tax	894	2,700	1,652	884	2,830	1,839	899	3,106	1,549	741	3,112	2,262	22,468
Income from Pooled Money Investments	17	22	21	18	18	15	12	20	15	14	11	21	198
Energy Repayment	0	0	0	164	6,456	0	0	0	0	0	0	0	6,620
Transfer from Special Fund for Economic Uncertainties	0	0	0	0	0	0	0	0	0	0	0	0	0
TOTAL Receipts	40	180	2,492	141	503	127	2,593	263	80	-1,797	388	1,778	6,789
Other	\$3,329	\$5,052	\$9,700	\$3,825	\$11,480	\$7,228	\$8,641	\$4,988	\$3,983	\$6,386	\$5,098	\$9,829	\$77,940

DISBURSEMENTS:													
University of California	\$245	\$261	\$307	\$373	\$304	\$313	\$244	\$307	\$317	\$371	\$263	\$162	\$3,143
Debt Service	0	189	208	228	119	83	-2	169	216	238	128	109	1,685
Other State Operations	1,243	1,054	1,569	1,211	1,359	1,039	1,213	928	1,039	1,274	997	788	13,701
Social Services	1,188	802	1,002	702	372	539	776	530	703	570	272	720	8,185
Medi-Cal Assistance	851	843	698	1,269	627	1,079	888	784	904	1,074	972	816	10,805
Other Health and Human Services	40	11	64	59	7	51	32	64	-11	80	45	7	449
Schools	2,092	3,484	2,550	2,286	2,306	2,773	2,183	4,081	3,308	2,531	2,441	721	30,756
Teachers' Retirement	653	0	0	108	0	0	108	0	0	108	0	-1	978
Other	762	943	1,225	506	1,029	1,202	651	530	933	984	597	703	10,045
TOTAL Disbursements	\$7,074	\$7,867	\$7,816	\$9,890	\$5,976	\$7,095	\$6,093	\$7,391	\$7,409	\$7,214	\$5,720	\$3,699	\$79,745
EXCESS RECEIPTS/(DEFICIT)	-\$3,745	-\$2,815	\$1,485	-\$3,965	\$5,505	\$132	\$2,548	-\$2,403	-\$3,427	-\$828	\$5,130	-\$1,906	-\$1,906

NET TEMPORARY LOANS:													
Special Fund for Economic Uncertainties	\$0	\$0	\$0	\$0	-\$2,241	-\$132	-\$151	\$2,525	\$0	\$0	\$0	-\$1,272	-\$1,272
Other Internal Sources	3,745	2,515	-1,485	-4,435	-763	0	0	1,093	5,441	907	543	-7,984	-423
2002 Revenue Anticipation Warrants	0	0	0	-1,500	-6,000	0	0	0	0	0	0	0	-7,500
Revenue Anticipation Notes	0	0	0	9,000	3,500	0	0	0	0	0	0	-12,500	0
2003 Revenue Anticipation Warrants	0	0	0	0	0	0	0	0	0	0	0	0	11,000
TOTAL, Net Temporary Loans	\$3,745	\$2,515	-\$1,485	\$3,065	-\$5,504	-\$132	-\$151	\$3,618	\$5,441	\$907	\$543	-\$10,756	\$1,805
ENDING CASH BALANCE	\$0	\$0	\$0	\$0	\$0	\$0	\$2,397	\$3,612	\$5,626	\$5,705	\$5,626	\$0	\$0

AVAILABLE/BORROWABLE RESOURCES:													
Special Fund for Economic Uncertainties	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525	\$2,525
Other Internal Sources	10,127	10,819	8,170	7,624	7,998	7,806	7,610	7,389	7,899	10,709	9,721	7,524	7,524
2002 Revenue Anticipation Warrants	7,500	7,500	7,500	6,000	0	0	0	0	0	0	0	0	0
Revenue Anticipation Notes	0	0	0	9,000	12,500	12,500	12,500	12,500	12,500	12,500	12,500	12,500	0
2003 Revenue Anticipation Warrants	0	0	0	0	0	0	0	0	0	0	0	0	0
TOTAL, Available/Borrowable Resources	\$20,151	\$20,843	\$18,195	\$25,148	\$23,022	\$22,831	\$22,634	\$22,413	\$22,924	\$25,734	\$24,746	\$21,049	\$21,049

CUMULATIVE LOAN BALANCES:													
Special Fund for Economic Uncertainties	\$2,525	\$2,525	\$2,525	\$2,525	\$283	\$151	\$0	\$2,525	\$2,525	\$2,525	\$2,525	\$1,253	\$1,253
Other Internal Sources	4,169	6,683	5,198	763	0	0	0	1,093	6,534	7,441	7,984	0	0
2002 Revenue Anticipation Warrants	7,500	7,500	7,500	6,000	0	0	0	0	0	0	0	0	0
Revenue Anticipation Notes	0	0	0	9,000	12,500	12,500	12,500	12,500	12,500	12,500	12,500	12,500	0
2003 Revenue Anticipation Warrants	0	0	0	0	0	0	0	0	0	0	0	0	0
TOTAL, Cumulative Loan Balances	\$14,194	\$16,708	\$15,223	\$18,288	\$12,783	\$12,661	\$12,500	\$16,118	\$21,559	\$22,466	\$23,009	\$12,253	\$12,253

UNUSED BORROWABLE RESOURCES	\$5,958	\$4,136	\$2,972	\$6,860	\$10,239	\$10,180	\$10,134	\$6,295	\$1,365	\$3,268	\$1,737	\$9,796	\$8,796
CUSHION (cash and unused borrowable resources)	\$5,958	\$4,136	\$2,972	\$6,860	\$10,239	\$10,180	\$12,531	\$9,907	\$6,991	\$8,973	\$7,363	\$8,796	\$8,796
ADJUSTED CUSHION	\$5,958	\$4,136	\$2,972	\$6,860	\$10,239	\$10,180	\$12,531	\$9,907	\$6,991	\$8,973	\$7,363	\$8,529	\$8,529

Additional Timing-Dependent Factors^{1/}

Note: Numbers may not add due to rounding. The months July 2002 through April 2003, inclusive, are actual results and the months of May and June 2003 are projections.

^{1/} Reflects the potential failure to enact suspensions of SSI/SSP COLAs by May 31 and potential disbursement of SSI/SSP July advance in June. Additional timing-dependent factors are reflected on the cash flows, a departure from the traditional presentation. While these cash flow adjustments would not normally be made, the State believes it is critical to be more conservative in this presentation due to the number and size of debt issuances proposed for 2003-04.

STATE FINANCES

The Budget Process

The State's fiscal year begins on July 1 and ends on June 30 of the following year. The State operates on a budget basis, using a modified accrual system of accounting for its General Fund, with revenues credited in the period in which they are measurable and available and expenditures debited in the period in which the corresponding liabilities are incurred.

The annual budget is proposed by the Governor by January 10 of each year for the next fiscal year (the "Governor's Budget"). Under State law, the annual proposed Governor's Budget cannot provide for projected expenditures in excess of projected revenues and balances available from prior fiscal years. Following the submission of the Governor's Budget, the Legislature takes up the proposal.

Under the State Constitution, money may be drawn from the Treasury only through an appropriation made by law. The primary source of the annual expenditure authorizations is the Budget Act as approved by the Legislature and signed by the Governor. The Budget Act must be approved by a two-thirds majority vote of each House of the Legislature. The Governor may reduce or eliminate specific line items in the Budget Act or any other appropriations bill without vetoing the entire bill. Such individual line-item vetoes are subject to override by a two-thirds majority vote of each House of the Legislature.

Appropriations also may be included in legislation other than the Budget Act. Except as noted in the next sentence, bills containing General Fund appropriations must be approved by a two-thirds majority vote in each House of the Legislature and be signed by the Governor. Bills containing appropriations for K-12 schools or community colleges ("K-14 education") only require a simple majority vote. Continuing appropriations, available without regard to fiscal year, may also be provided by statute or the State Constitution. There is litigation pending concerning the validity of such continuing appropriations. See "Litigation" below.

Funds necessary to meet an appropriation need not be in the State Treasury at the time such appropriation is enacted; revenues may be appropriated in anticipation of their receipt.

The General Fund

The moneys of the State are segregated into the General Fund and over 900 other funds, including special, bond, trust and pension funds. The General Fund consists of revenues received by the State Treasury and not required by law to be credited to any other fund, as well as earnings from the investment of State moneys not allocable to another fund. The General Fund is the principal operating fund for the majority of governmental activities and is the depository of most of the major revenue sources of the State. For additional financial data relating to the General Fund, see "Cash Flow" above and financial statements incorporated in or attached to this Appendix A. See "Financial Statements". The General Fund may be expended as a consequence of appropriation measures enacted by the Legislature and approved by the Governor, as well as appropriations pursuant to various constitutional authorizations and initiative statutes.

The Special Fund for Economic Uncertainties

The Special Fund for Economic Uncertainties (“SFEU”) is funded with General Fund revenues and was established to protect the State from unforeseen revenue reductions and/or unanticipated expenditure increases. Amounts in the SFEU may be transferred by the State Controller to the General Fund as necessary to meet cash needs of the General Fund. The State Controller is required to return moneys so transferred without payment of interest as soon as there are sufficient moneys in the General Fund. At the end of each fiscal year, the Controller is required to transfer from the SFEU to the General Fund any amount necessary to eliminate any deficit in the General Fund.

The legislation creating the SFEU (Government Code Section 16418) contains a continuous appropriation from the General Fund authorizing the State Controller to transfer to the SFEU, as of the end of each fiscal year, the lesser of (i) the unencumbered balance in the General Fund and (ii) the difference between the State’s “appropriations subject to limitation” for the fiscal year then ended and its “appropriations limit” as defined in Section 8 of Article XIII B of the State Constitution and established in the Budget Act for that fiscal year, as jointly estimated by the State’s Legislative Analyst’s Office and the Department of Finance. For a further description of Article XIII B, see “State Appropriations Limit” below. In certain circumstances, moneys in the SFEU may be used in connection with disaster relief.

For budgeting and accounting purposes, any appropriation made from the SFEU is deemed an appropriation from the General Fund. For year-end reporting purposes, the State Controller is required to add the balance in the SFEU to the balance in the General Fund so as to show the total moneys then available for General Fund purposes.

See the caption “Current State Budget” below for information concerning the recent balances in the SFEU and projections of the balances for the current and upcoming fiscal years. As in any year, the Budget Act and related trailer bills are not the only pieces of legislation which appropriate funds. Other factors including re-estimates of revenues and expenditures, existing statutory requirements, and additional legislation introduced and passed by the Legislature may impact the fiscal year-end balance in the SFEU.

Inter-Fund Borrowings

Inter-fund borrowing is used to meet temporary imbalances of receipts and disbursements in the General Fund. As of May 31, 2003, \$11.0 billion of outstanding loans from the SFEU or other special funds was used to pay expenditures of the General Fund. This amount represents internal borrowings made to fund the General Cash Revolving Fund, an initial step toward issuance of the 2003 Warrants (see “Cash Flow—2003 Revenue Anticipation Warrants”). See “State Warrants” and “Exhibit 1—State Controller’s Statement of General Fund Cash Receipts and Disbursements, July 1, 2002 through May 31, 2003 (Unaudited).” In addition, as of this date, the State had \$12.5 billion of short-term external loans maturing in late June 2003. See “State Indebtedness—Cash Flow Borrowings” above.

In the event the General Fund is or will be exhausted, the State Controller is required to notify the Governor and the Pooled Money Investment Board (the “PMIB,” comprised of the

State Director of Finance, the State Treasurer and the State Controller). The Governor may then order the State Controller to direct the transfer of all or any part of the moneys not needed in special funds to the General Fund from such special funds, as determined by the PMIB. All money so transferred must be returned to the special fund from which it was transferred as soon as there is sufficient money in the General Fund to do so. Transfers cannot be made from a special fund which will interfere with the objective for which such special fund was created, or from certain specific funds. When moneys transferred to the General Fund in any fiscal year from any special fund pursuant to the inter-fund borrowing mechanism exceed ten percent of the total additions to such special fund as shown in the statement of operations of the preceding fiscal year as set forth in the Budgetary (Legal Basis) annual report of the State Controller, interest must be paid on such excess at a rate determined by the PMIB to be the current earning rate of the Pooled Money Investment Account. See also, "Cash Flow—2003 Revenue Anticipation Warrants" above for a description of certain covenants of the State relating to internal borrowings.

Any determination of whether a proposed borrowing from one of the special funds is permissible must be made with regard to the facts and circumstances existing at the time of the proposed borrowing. The Attorney General of the State has identified certain criteria relevant to such a determination. For instance, amounts in the special funds eligible for inter-fund borrowings are legally available to be transferred to the General Fund if a reasonable estimate of expected General Fund revenues, based upon legislation already enacted, indicates that such transfers can be paid from the General Fund promptly if needed by the special funds or within a short period of time if not needed. In determining whether this requirement has been met, the Attorney General has stated that consideration may be given to the fact that General Fund revenues are projected to exceed expenditures entitled to a higher priority than payment of internal transfers, i.e., expenditures for the support of the public school system and public institutions of higher education and the payment of debt service on general obligation bonds of the State.

At the November 1998 election, voters approved Proposition 2. This proposition requires the General Fund to repay loans made from certain transportation special accounts (such as the State Highway Account) at least once per fiscal year, or up to 30 days after adoption of the annual budget act. Since the General Fund may reborrow from the transportation accounts soon after the annual repayment is made, the proposition is not expected to have any adverse impact on the State's cash flow.

In addition to temporary inter-fund borrowings described in this section, some of the budget solutions in the 2002-03 and other recent fiscal years have included other transfers and long-term loans from special funds to the General Fund, specified in legislation. In some cases, such loans and transfers have the effect of reducing internal borrowable resources. See "Current State Budget."

The following chart shows internal borrowable resources available for temporary loans to the General Fund on June 30 of each of the fiscal years 1999-00 through 2001-02 and estimates for 2002-03 and 2003-04:

**Internal Borrowable Resources
(Cash Basis)
(Millions)**

	June 30				
	2000	2001	2002*	2003**	2004***
Available Internal Borrowable Resources	\$9,427.2	\$12,342.4	\$12,979.7	\$10,048.6	\$7,075.9
Outstanding Loans					
From Special Fund for Economic Uncertainties	-0-	-0-	2,524.5	1,519.9	509.0
From Special Funds and Accounts	-0-	-0-	423.5	0	2,418.8
Total Outstanding Internal Loans	-0-	-0-	2,948.0	1,519.9	2,927.8
Unused Internal Borrowable Resources	\$9,427.2	\$12,342.4	\$10,031.7	\$8,528.7	\$4,148.1

* At June 30, 2002, the State also had outstanding \$7.5 billion of external borrowings in the form of revenue anticipation warrants. See "State Indebtedness – Cash Flow Borrowings".

**Department of Finance estimates as of May 18, 2003. At June 30, 2003, the State will have outstanding \$11.0 billion of external borrowings in the form of revenue anticipation warrants. These amounts are based on the cashflow that includes additional timing-dependent factors.

***Department of Finance estimates as of May 18, 2003. These amounts are based on the cashflow that includes additional timing-dependent factors.

SOURCE: State of California, Department of Finance. Information for the fiscal years ended June 30, 2000 through June 30, 2002, are actual figures. For the fiscal years ending June 30, 2003, and June 30, 2004, these figures were estimated as of May 18, 2003, by the Department of Finance.

State Warrants

No money may be drawn from the State Treasury except upon a warrant duly issued by the State Controller. The State Controller is obligated to draw every warrant on the fund out of which it is payable for the payment of money directed by State law to be paid out of the State Treasury; however, a warrant may not be drawn unless authorized by law and unless unexhausted specific appropriations provided by law are available to meet it. State law provides two methods for the State Controller to respond if the General Fund has insufficient "Unapplied Money" available to pay a warrant when it is drawn, referred to generally as "registered warrants" and "reimbursement warrants." "Unapplied Money" consists of money in the General Fund for which outstanding warrants have not already been drawn and which would remain in the General Fund if all outstanding warrants previously drawn and then due were paid. Unapplied Money may include moneys transferred to the General Fund from the SFEU and internal borrowings from the Special Funds (to the extent permitted by law).

Registered Warrants

If a warrant is drawn on the General Fund for an amount in excess of the amount of Unapplied Money in the General Fund, after deducting from such Unapplied Money the amount, as estimated by the State Controller, required by law to be set apart for obligations having priority over obligations to which such warrant is applicable, the warrant must be registered by the State Treasurer on the reverse side as not paid because of the shortage of funds in the General Fund. The State Controller then delivers such a "registered warrant" to persons or entities (e.g., suppliers and local governments) otherwise entitled to receive payments from the State. A registered warrant bears interest at a rate designated by the Pooled Money Investment Board ("PMIB"), a State agency, up to a maximum of five percent per annum or at a higher rate if issued in connection with some form of credit enhancement such as the Forward Purchase Agreements. Registered warrants may or may not have a fixed maturity date. Registered warrants that have no fixed maturity date, and registered warrants that bear a maturity date but, for lack of Unapplied Moneys, were not paid at maturity, are paid, together with all interest due, when the Controller, with the approval of the PMIB, determines payment will be made. The State Controller then notifies the State Treasurer, who publishes a notice that the registered warrants in question are payable. The duties of the Controller and the PMIB are ministerial in nature, and the Controller and the PMIB may not legally refuse to pay the principal of or interest on any registered warrants on any date Unapplied Moneys are available in the General Fund after all Priority Payments (defined above under "Cash Flow—2003 Revenue Anticipation Warrants") have been made on that date.

As described above under "Cash Flow—2003 Revenue Anticipation Warrants," if the State is required to obtain advances under the Forward Purchase Agreements described therein to pay some or all of the 2003 Warrants (defined above) at maturity, the State will issue registered warrants without a maturity date to the Participants (defined above), bringing into effect the daily application of Unapplied Moneys in the General Fund described in the previous paragraph. The adverse results from issuing registered warrants could include: (1) the State would be required by law to pay the registered warrants before issuing warrants that could be cashed immediately to persons or entities (e.g., suppliers and certain local governments) otherwise entitled to payments from the State General Fund, and the State's ability to manage its cash would therefore be limited; (2) default under the State's bank credit facilities backing the State's general obligation bond commercial paper program (which would bar the State from renewing up to \$2 billion in maturing short-term commercial paper notes); and (3) default under the State's bank credit facilities backing the State's variable rate general obligation bonds (which would increase the State's borrowing costs and debt service payments).

Reimbursement Warrants

In lieu of issuing individual registered warrants to numerous creditors, State law provides an alternative procedure whereby the Governor, upon request of the Controller, may authorize utilizing the General Cash Revolving Fund in the State Treasury to borrow from other State special funds to meet payments authorized by law. The Controller may then issue "reimbursement warrants" in the financial market at competitive bid to reimburse the General Cash Revolving Fund, thereby increasing cash resources for the General Fund to cover required payments. The General Cash Revolving Fund exists solely to facilitate the issuance of

reimbursement warrants. Reimbursement warrants may have a fixed maturity date. The 2003 Warrants are reimbursement warrants issued pursuant to these provisions.

The principal of and interest on reimbursement warrants must be paid by the Treasurer on their respective maturity dates from any Unapplied Money in the General Fund and available for such payment. In the event that Unapplied Money is not available for payment on the respective maturity dates of reimbursement warrants, and refunding warrants (see “—Refunding Warrants”) have not been sold at such times as necessary to pay such reimbursement warrants, such reimbursement warrants will be paid, together with all interest due thereon (including interest accrued at the original interest rate after the maturity date), at such times as the Controller, with the approval of the PMIB, may determine.

Refunding Warrants

If there is not sufficient Unapplied Money in the General Fund to pay maturing reimbursement warrants, the Controller is authorized under State law, with the written approval of the Treasurer, to offer and sell a new issue of reimbursement warrants as refunding warrants to refund the prior, maturing reimbursement warrants. Proceeds of such refunding warrants must be used exclusively to repay the maturing warrants. In all other respects, refunding warrants have the same legal status and provisions as reimbursement warrants, as described above.

The State issued reimbursement warrants on several occasions in order to meet its cash needs during the period 1992-1994, when State revenues were severely reduced because of an economic recession. Facing renewed economic pressures, the State has issued reimbursement warrants in June 2002 and June 2003. See “Recent Developments Regarding State Economy and Finances,” “State Indebtedness – Cash Flow Borrowings,” and “Cash Flow.”

Investment of Funds

Moneys on deposit in the State’s Centralized Treasury System are invested by the Treasurer in the Pooled Money Investment Account (the “PMIA”). As of April 30, 2003, the PMIA held approximately \$37.3 billion of State moneys, and \$22.6 billion invested for about 3,039 local governmental entities through the Local Agency Investment Fund (“LAIF”). The assets of the PMIA as of April 30, 2003, are shown in the following table:

Analysis of the Pooled Money Investment Account Portfolio*

<u>Type of Security</u>	<u>Amount (Millions)</u>	<u>Percent of Total</u>
U.S. Treasury Bills and Notes	\$ 6,713	11.2%
Commercial Paper (corporate)	13,794	23.0
Certificates of Deposits	11,105	18.5
Corporate Bonds	2,053	3.4
Federal Agency Securities	11,849	19.7
Bankers Acceptances	--	--
Bank Notes	400	0.7
Loans Per Government Code	8,553	14.3
Time Deposits	5,520	9.2
Repurchases	--	--
Reverse Repurchases	--	--
	<u>\$59,988</u>	<u>100.0%</u>

*Totals may differ due to rounding.

SOURCE: State of California, Office of the Treasurer.

The State's treasury operations are managed in compliance with the California Government Code and according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA operates with the oversight of the PMIB (consisting of the State Treasurer, the State Controller and the Director of Finance). The LAIF portion of the PMIA operates with the oversight of the Local Agency Investment Advisory Board (consisting of the State Treasurer and four other appointed members).

The Treasurer does not invest in leveraged products or inverse floating rate securities. The investment policy permits the use of reverse repurchase agreements subject to limits of no more than 10 percent of the PMIA. All reverse repurchase agreements are cash matched either to the maturity of the reinvestment or an adequately positive cash flow date which is approximate to the maturity of the reinvestment.

The average life of the investment portfolio of the PMIA as of April 30, 2003, was 138 days.

Pension Trusts

The pension contribution liability for the three principal retirement systems in which the State participates, the California Public Employee's Retirement System ("CalPERS"), the California State Teachers' Retirement System ("CalSTRS") and the University of California Retirement System ("UCRS"), is included in the financial statements of the State and described in Note 20 to the Audited Annual Financial Statements of the State of California for the year ended June 30, 2002 (the "Audited Financial Statements"), incorporated by reference in this Appendix A. See "Financial Statements."

The three largest defined benefit retirement plans contained in the retirement systems and the State's share of the excess of the actuarial value of assets over the actuarial accrued liability

or unfunded actuarial accrued liability of those plans at June 30, 2002 (June 30, 2001, for CalSTRS) was reported to be as follows:

<u>Name of Plan</u>	Excess of Actuarial Value of Assets Over Actuarial Accrued Liabilities (Unfunded Actuarial Accrued Liability)
Public Employees' Retirement Fund (CalPERS)	\$ (6.653) billion
State Teachers' Retirement Fund Defined Benefit Program (CalSTRS)	(2.227) billion
University of California Retirement Plan	11.549 billion

The actuarial information for CalSTRS for the year ended June 30, 2002, is not yet available, as that information is only updated every other year. However, according to CalSTRS, its investment portfolio market value as of July 31, 2002, was \$92,599,000,000, compared to \$102,975,000,000 as of July 31, 2001. CalPERS reports that its investment portfolio market value as of July 31, 2002, was \$135,500,000,000, compared to \$155,300,000,000 as of July 31, 2001. These declines in investment portfolio value will adversely affect the foregoing data when new actuarial calculations are made later in 2003.

The State's contribution to the CalPERS and the UC Retirement System are actuarially determined each year, while the State's contribution to the CalSTRS is established by statute. The following table shows the State's contributions to CalPERS for 1997-98 through 2003-04:

1997-98	\$1,223,000,000
1998-99	766,100,000
1999-00	463,600,000
2000-01	156,700,000
2001-02	677,200,000
2002-03	1,190,000,000
2003-04	2,213,000,000

Due to investment losses and increased retirement benefits, the State contribution to the CalPERS has increased from \$156.7 million in 2000-01 to \$2.213 billion in 2003-04. Details concerning the three largest plans and information concerning the other plans contained in the retirement systems are included in Note 20 to the Audited Financial Statements. See "Financial Statements" below.

Repayment of Energy Loans

The Department of Water Resources of the State ("DWR") borrowed money from the General Fund of the State for DWR's power supply program between January and June 2001. DWR has issued approximately \$11.25 billion in revenue bonds in several series and in the fall of 2002 used the net proceeds of the revenue bonds to repay outstanding loans from banks and commercial lenders in the amount of approximately \$3.5 billion and a loan from the General Fund in the amount of \$6.1 billion plus accrued interest of approximately \$500 million. Issuance

of the DWR revenue bonds had been delayed since mid-2001 by a number of factors, including administrative and legal challenges.

The loans from the General Fund and the banks and commercial lenders financed DWR's power supply program costs during 2001 that exceeded DWR's revenues from the sale of electricity. The general purpose of the power supply program has been to provide to customers of the three major investor-owned electric utilities in the State (the "IOUs") the portion of their power not provided by the IOUs. The power supply program has become self-supporting and no additional loans from the General Fund are authorized. As of January 1, 2003, the DWR's authority to enter into new power purchase contracts terminated, and the IOUs resumed responsibility for obtaining electricity for their customers.

The primary source of money to pay debt service on the DWR revenue bonds is revenues derived from customers of the IOUs resulting from charges set by the California Public Utilities Commission. The DWR revenue bonds are not a debt or liability of the State and do not directly or indirectly or contingently obligate the State to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment.

Constraints on the Budgetary Process

Over the years, a number of laws and constitutional amendments have been enacted, often from voter initiatives, which restrict the use of State General Fund or special fund revenues, or otherwise limit the Legislature and Governor's discretion in enacting budgets. Prior examples of such provisions are Proposition 98, which mandates a minimum percentage of General Fund revenues to be spent on local education, and Proposition 10, which raised taxes on tobacco products but mandated how the additional revenues would be expended. See "Proposition 98" and "Sources of Tax Revenue—Taxes on Tobacco Products" below.

An initiative statute, called the "After School Education and Safety Program of 2002," was approved by the voters on November 5, 2002, and will require the State to expand funding for before and after school programs in the State's public elementary and middle schools. Beginning with the 2004-05 fiscal year and in the first year that non-Proposition 98 appropriations exceed the base level by \$1.5 billion, the initiative will require the State to appropriate up to \$550 million annually, depending on the amount above the trigger level. (The initiative defines the base level as the fiscal year during the period July 1, 2000, through June 30, 2004, for which the State's non-guaranteed General Fund appropriations are the highest as compared to any other fiscal year during that period. Using May 2003 data, the 2000-01 fiscal year is the base year.) Since non-Proposition 98 General Fund appropriations proposed in the May Revision of the 2003-04 Governor's Budget ("May Revision") are \$3.95 billion below the "trigger" amount, the initiative is unlikely to require implementation of the funding increase for several years. By comparison, the May Revision includes about \$121.6 million for these programs, \$428.4 million below the amount which the initiative would require if the full funding increase were in effect.

A proposed amendment to the State Constitution ("ACA 11") will appear on the March 2004 ballot, and would require the annual transfer of a portion of General Fund revenues to the Twenty-First Century Infrastructure Fund to fund State and local infrastructure projects. Under

the proposed amendment, beginning in 2006-07, one percent of General Fund revenues would be transferred to the fund, if General Fund revenues meet specified levels. This transfer could increase annually until it reaches a maximum of three percent by 2013-14. The proposal contains specific triggers that protect the General Fund when certain inflation adjusted revenue levels are not met. The proposal also contains provisions that limit the transfer amount based on debt service or qualified education spending relative to revenue growth.

While ACA 11 could result in significant transfers of General Fund revenues to the Twenty-First Century Infrastructure Investment Fund, it is unlikely that the necessary conditions will be met for several years, i.e., General Fund revenues grow by four percent after adjusting for inflation. The yearly increase also would likely be delayed most years with the result that transfers would not reach the three percent level by 2013-14. Based on revenue projections in the May Revision and a yearly inflation rate of 2.9 percent, the first transfer would be approximately \$1 billion in 2010-11 and would not grow for many years. One aspect of this proposed amendment would be to automatically set aside a portion of one-time revenue windfalls for one-time infrastructure expenditures.

Welfare Reform

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (P.L. 104-193, the "Law") fundamentally reformed the nation's welfare system. The Law includes provisions to: (i) convert Aid to Families with Dependent Children ("AFDC"), an entitlement program, to Temporary Assistance for Needy Families ("TANF"), a block grant program with lifetime time limits on TANF recipients, work requirements and other changes; (ii) deny certain federal welfare and public benefits to legal noncitizens (subsequent federal law has amended this provision), allow states to elect to deny additional benefits (including TANF) to legal noncitizens, and generally deny almost all benefits to illegal immigrants; and (iii) make changes in the Food Stamp program, including to reduce maximum benefits and impose work requirements. The block grant formula under the Law is operative through June 30, 2003.

Chapter 270, Statutes of 1997, embodies California's response to the federal welfare reforms. Effective January 1, 1998, California Work Opportunity and Responsibility to Kids ("CalWORKs") replaced the former AFDC and Greater Avenues to Independence programs. Consistent with the federal law, CalWORKs contains time limits on the receipt of welfare aid, both lifetime as well as current period. The centerpiece of CalWORKs is the linkage of eligibility to work participation requirements.

Welfare caseloads have declined considerably with the implementation of the CalWORKs program. The 2003-04 CalWORKs caseload is projected to be 466,000, down from 480,000 cases in 2002-03. This represents a major decline in caseload from the rapid growth of the early 1990s, when caseload peaked at 921,000 cases in 1994-95.

In 2003-04, California will continue to meet, but not exceed, the federally-required \$2.7 billion combined State and county maintenance of effort ("MOE") requirement. In an effort to keep program expenditures within the TANF Block Grant and TANF MOE amounts, the May Revision to the 2003-04 Governor's Budget proposes to suspend the statutory cost-of-living adjustment for cash grants.

The May Revision proposes a one-time augmentation of \$156.9 million for employment services to enable recipients to leave aid and become self sufficient. The May Revision proposes total CalWORKs-related expenditures of \$7.0 billion for 2003-04, including child care transfer amounts for the Department of Education and the State's general TANF reserve. The May Revision includes a TANF reserve of \$270 million, which is available for unanticipated needs in any program for which TANF Block Grant funds are appropriated, including CalWORKs benefits, employment services, county administration, and child care costs. It may be needed for such pressures as litigation or the cost of increased participation rate requirements that have been proposed at the federal level with the reauthorization of the TANF program.

For fiscal year 2003-04, CalWORKs assistance payments, administration, and employment services are proposed for realignment. Under this proposal, the county share-of-cost for assistance payments would increase from 2.5 percent to 30 percent, totaling \$782.3 million, and counties would be given a 30 percent share-of-cost for administration and employment services, totaling \$358.8 million, along with a dedicated revenue stream. All of the CalWORKs-related programs are currently administered by the counties, and increasing the counties' share-of-cost will serve as an incentive for the counties to pursue the most cost-effective approaches to service delivery ultimately resulting in the movement of more recipients from welfare to work. Shifting these programs to counties also allows for additional county expenditures to be counted towards the TANF MOE, affording General Fund reductions in other components of the CalWORKs program.

Authorization for the TANF program currently ends June 30, 2003 (having been extended several times from its original September 30, 2002 expiration date). For the TANF program to continue, the U.S. Congress must pass, and the President must sign, legislation reauthorizing the program prior to that date. Although reauthorization could simply involve extending the funding period, it is more likely that Congress and the President will consider several key policy changes. It is unknown at this time how California's TANF funding will be affected by reauthorization.

Local Governments

The primary units of local government in California are the counties, which range in population from 1,200 in Alpine County to approximately 10 million in Los Angeles County. Counties are responsible for the provision of many basic services, including indigent health care, welfare, jails, and public safety in unincorporated areas. There are also 477 incorporated cities and thousands of special districts formed for education, utilities, and other services. The fiscal condition of local governments has been constrained since "Proposition 13" was enacted by California voters in 1978. Proposition 13 reduced and limited the future growth of property taxes and limited the ability of local governments to impose "special taxes" (those devoted to a specific purpose) without two-thirds voter approval. Proposition 218, another initiative constitutional amendment enacted in 1996, further limited the ability of local governments to raise taxes, fees, and other exactions. Counties, in particular, have had fewer options to raise revenues than many other local government entities, while they have been required to maintain many services.

In the aftermath of Proposition 13, the State provided aid to local governments from the General Fund to make up some of the loss of property tax moneys, including assuming principal responsibility for funding K-12 schools and community colleges. During the recession of the early 1990s, the Legislature eliminated most of the remaining components of post-Proposition 13 aid to local government entities other than K-14 education districts by requiring cities and counties to transfer some of their property tax revenues to school districts. However, the Legislature also provided additional funding sources, such as sales taxes, and reduced certain mandates for local services. The 2002 Budget Act expands such transfers to temporarily include community redevelopment agencies, which were not included in the original transfers. These agencies will have to pay \$75 million to schools in 2002-03. The 2003-04 May Revision proposes to increase this payment to \$250 million in 2003-04 with the amount increasing over time until schools receive the amount of property taxes that would have been received in the absence of redevelopment, estimated at approximately \$1.25 billion. The 2002 Budget Act and related legislation continue to provide significant assistance to local governments, including \$308 million for various local public safety programs. This amount includes \$116.3 million for the Citizens' Option for Public Safety ("COPS") program to support local front-line law enforcement, \$116.3 million for county juvenile justice and crime prevention programs, \$18.5 million for local law enforcement technology grants, \$18.5 million to 37 specified small and rural county sheriffs' departments, and \$38.2 million for reimbursement of jail booking fees. The 2003-04 May Revision proposes to continue funding at these levels for COPS, juvenile justice, rural law enforcement, and local law enforcement technology grants as well as to provide \$40.15 million for open space subvention reimbursements to cities and counties, for a total of \$310 million for local public safety programs in 2003-04.

A program to offset a portion of the vehicle license fees paid by vehicle owners was established in 1998. The amount of this offset has increased from 25 percent in 1999 to the current level of 67.5 percent. This offset is expected to provide tax relief of \$3.985 billion in 2002-03. Since 1999, the General Fund has backfilled the offset so that the tax relief did not result in a revenue loss to local governments. However, as the amount paid by taxpayers has been reduced, the amount backfilled by the General Fund has increased. Section 10754 of the Revenue and Taxation Code requires the Department of Motor Vehicles and the Department of Housing and Community Development, as appropriate, to reduce the vehicle license fee (VLF) offsets and restore the VLF "during any period in which insufficient moneys are available to be transferred from the General Fund to fully fund the offsets." On June 20, 2003, it was determined that insufficient General Fund moneys were available to continue to fund any portion of the vehicle license fee offsets to local governments. Accordingly, the vehicle license fees paid by taxpayers will return within 90 days to the pre-1999 level. This action will reduce General Fund expenditures by about \$4.2 billion in fiscal year 2003-04 and result in a reduction of approximately \$825 million in transfers to local governments if alternate funding is not provided to cover the period of time needed for the Department of Motor Vehicles to phase out the offset from vehicle registration bills.

Prior to legislation enacted in 1997, local governments provided the majority of funding for the State's trial court system. The legislation consolidated the trial court funding at the State level in order to streamline the operation of the courts, provide a dedicated revenue source, and relieve fiscal pressure on the counties. This resulted in decreasing the county contribution for court operations by \$415 million and allowed cities to retain \$68 million in fine and penalty

revenue previously remitted to the State. The State's trial court system will receive approximately \$1.7 billion in State resources and \$475 million in resources from the counties in 2002-03 and 2003-04.

The entire statewide welfare system was changed in response to the change in federal welfare law enacted in 1996 (see "Welfare Reform" above). Under the CalWORKs program, counties are given flexibility to develop their own plans, consistent with State law, to implement the program and to administer many of its elements, with costs for administrative and supportive services capped at the 1996-97 levels. As noted above, counties are also given financial incentives if, at the individual county level or statewide, the CalWORKs program produces savings associated with specified standards. Counties are still required to provide "general assistance" aid to certain persons who cannot obtain welfare from other programs.

Following discussions with the Legislature, counties, and others, the Administration proposed in the May Revision a much smaller State-local Realignment compared with the January Governor's Budget proposal. Realignment, as proposed in the May Revision, would transfer the financial responsibility for various mental health, children and youth services, and social services programs from the State to local governments. The May Revision also proposes to fund these new responsibilities with income and tobacco tax increases. Other programs originally proposed for realignment in the Governor's Budget are under legislative consideration for realignment in 2004-05. See "Current State Budget."

State Appropriations Limit

The State is subject to an annual appropriations limit imposed by Article XIII B of the State Constitution (the "Appropriations Limit"). The Appropriations Limit does not restrict appropriations to pay debt service on voter-authorized bonds.

Article XIII B prohibits the State from spending "appropriations subject to limitation" in excess of the Appropriations Limit. "Appropriations subject to limitation," with respect to the State, are authorizations to spend "proceeds of taxes," which consist of tax revenues, and certain other funds, including proceeds from regulatory licenses, user charges or other fees to the extent that such proceeds exceed "the cost reasonably borne by that entity in providing the regulation, product or service," but "proceeds of taxes" exclude most State subventions to local governments, tax refunds and some benefit payments such as unemployment insurance. No limit is imposed on appropriations of funds which are not "proceeds of taxes," such as reasonable user charges or fees and certain other non-tax funds.

There are various types of appropriations excluded from the Appropriations Limit. For example, debt service costs of bonds existing or authorized by January 1, 1979, or subsequently authorized by the voters, appropriations required to comply with mandates of courts or the federal government, appropriations for qualified capital outlay projects, appropriations for tax refunds, appropriations of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990 levels, and appropriation of certain special taxes imposed by initiative (e.g., cigarette and tobacco taxes) are all excluded. The Appropriations Limit may also be exceeded in cases of emergency.

The Appropriations Limit in each year is based on the Limit for the prior year, adjusted annually for changes in State per capita personal income and changes in population, and adjusted, when applicable, for any transfer of financial responsibility of providing services to or from another unit of government or any transfer of the financial source for the provisions of services from tax proceeds to non-tax proceeds. The measurement of change in population is a blended average of statewide overall population growth, and change in attendance at local school and community college ("K-14") districts. The Appropriations Limit is tested over consecutive two-year periods. Any excess of the aggregate "proceeds of taxes" received over such two-year period above the combined Appropriations Limits for those two years, is divided equally between transfers to K-14 districts and refunds to taxpayers.

The Legislature has enacted legislation to implement Article XIII B which defines certain terms used in Article XIII B and sets forth the methods for determining the Appropriations Limit. California Government Code Section 7912 requires an estimate of the Appropriations Limit to be included in the Governor's Budget, and thereafter to be subject to the budget process and established in the Budget Act.

The following table shows the Appropriations Limit for 1999-00 through 2003-04. Because of the extraordinary surge of revenues in 1999-00, the State exceeded its Appropriations Limit by \$975 million in that year. Since the excess revenues are calculated over a two-year period, there were no excess revenues for the combined 1999-00 and 2000-01 fiscal years.

As of the release of the 2003-04 May Revision, the Department of Finance projects the Appropriations Subject to Limit to be \$18.347 billion and \$10.984 billion under the Appropriations Limit in fiscal years 2002-03 and 2003-04, respectively.

**State Appropriations Limit
(Millions)**

	Fiscal Years				
	1999-00	2000-01	2001-02	2002-03	2003-04
State Appropriations Limit	\$50,673	\$54,073	\$59,318	\$59,591	\$61,724*
Appropriations Subject to Limit	(51,648)	(51,648)	(40,953)*	(41,244)*	(50,740)*
Amount (Over)/Under Limit	\$ (975)	\$ 2,425	\$ 18,365*	\$18,347*	\$10,984*

*Estimated/Projected

SOURCE: State of California, Department of Finance.

Proposition 98

On November 8, 1988, voters of the State approved Proposition 98, a combined initiative constitutional amendment and statute called the "Classroom Instructional Improvement and Accountability Act." Proposition 98 changed State funding of public education below the university level and the operation of the State Appropriations Limit, primarily by guaranteeing K-14 schools a minimum share of General Fund revenues. Proposition 98 (as modified by Proposition 111, enacted on June 5, 1990) guarantees K-14 schools the greater of (a) in general, a fixed percent of General Fund revenues ("Test 1"), (b) the amount appropriated to K-14 schools in the prior year, adjusted for changes in the cost of living (measured as in Article XIII B

by reference to State per capita personal income) and enrollment (“Test 2”), or (c) a third test, which replaces Test 2 in any year the percentage growth in per capita General Fund revenues from the prior year plus one half of one percent is less than the percentage growth in State per capita personal income (“Test 3”). Under Test 3, schools receive the amount appropriated in the prior year adjusted for changes in enrollment and per capita General Fund revenues, plus an additional small adjustment factor. If Test 3 is used in any year, the difference between Test 3 and Test 2 becomes a “credit” (called the “maintenance factor”) to schools and the basis of payments in future years when per capita General Fund revenue growth exceeds per capita personal income growth. Proposition 98 implementing legislation adopted prior to the end of the 1988-89 fiscal year determined the K-14 schools’ funding guarantee under Test 1 to be 40.3 percent of the General Fund tax revenues, based on 1986–87 appropriations. However, that percent has been adjusted to approximately 35 percent to account for a subsequent redirection of local property taxes, since such redirection directly affects the share of General Fund revenues to schools.

The Proposition 98 guarantee is funded from two sources: local property taxes and General Fund. Any amount not funded by local property taxes is funded by the General Fund. Thus, given a policy decision to fund the minimum guarantee or to fund in excess of the guarantee, property tax collections represent an offset to General Fund costs. This is true regardless of whether the year in question is a Test 1, Test 2, or Test 3 year.

Proposition 98 permits the Legislature, by two-thirds vote of both houses with the Governor’s concurrence, to suspend the K-14 schools’ minimum funding formula for a one-year period. Proposition 98 also contains provisions for the transfer of certain State tax revenues in excess of the Article XIII B limit to K-14 schools (see “State Finances—State Appropriations Limit” above).

The State’s emphasis on improving education resources has resulted in estimated K-12 spending of \$6,638 and \$6,869 per-pupil in fiscal years 2002-03 and 2003-04, respectively. These amounts are 52 percent and 57 percent above the 1994-95 level (\$4,351 per pupil).

Although total revenues (General Fund subject to the State Appropriations Limit (SAL) and local property taxes) have increased significantly since 1994-95, the projected level of General Fund SAL revenue decreased \$324 million from Governor’s Budget estimates (from \$65.088 billion to \$64.764 billion). The combined effect of this decrease in revenue, an increase in average daily attendance (from 1.48 percent to 1.75 percent) and a \$401 million decrease in anticipated local revenue (from \$15.013 billion to \$14.612 billion), has increased the calculation of the General Fund share of the minimum K-14 funding level \$317 million for 2002-03 (from approximately \$28.9 billion to approximately \$29.2 billion). The revised 2002-03 Proposition 98 appropriations of \$29.337 billion reflect \$2.6 billion of enacted mid-year reductions. Because of a combination of factors, the minimum guarantee decreased \$84 million (from \$43.911 billion to \$43.827 billion), resulting in a \$122.3 million overappropriation in the current year.

The revenue projection for 2003-04 exceeds the revised 2002-03 estimates by approximately \$2.385 billion. The General Fund share of the guarantee will increase approximately \$392 million, from \$29.3 billion in 2002-03 to \$29.7 billion in 2003-04. The

2003-04 May Revision proposes Proposition 98 funding at the minimum, with enrollment growth fully funded and total K-14 education funding of approximately \$45.6 billion (\$6,869 per K-12 pupil), an increase of 3.5 percent per pupil compared to the revised 2002-03 level. See “Current State Budget” for further discussion of education funding.

Sources of Tax Revenue

The following is a summary of the State’s major revenue sources. Further information on State revenues is contained under “Current State Budget” and “State Finances—Recent Tax Receipts” below. See the table below entitled “Comparative Yield of State Taxes—All Funds, 1998-99 Through 2003–04” for a comparison, by amount received, of the sources of the State’s tax revenue.

The 2003-04 May Revision includes the following General Fund revenue proposals:

- A one-year suspension of the teacher retention tax credit estimated to generate \$175 million General Fund in 2003-04.
- A loan to the General Fund of any excess sales tax revenues on gasoline, which would otherwise be designated as Public Transportation Account spillover, estimated to generate \$87 million General Fund in 2003-04.
- A one-year suspension of the natural heritage preservation tax credit and Employment Development Department (EDD) participation in the Treasury Offset Program, estimated to generate \$15 million General Fund in 2003-04.

To fund the transfer of responsibility for various programs proposed for realignment, the 2003-04 May Revision proposes the following tax increases. These revenues would not be deposited in the General Fund:

- Adding a 10.3 percent personal income tax bracket at \$150,000 for single filers and \$300,000 for joint filers, estimated to generate \$1.56 billion in 2003-04.
- A \$0.23 per pack increase in the tobacco excise tax estimated to generate \$267 million in 2003-04. The 2003-04 May Revision also proposes an additional \$0.40 per pack increase in 2004-05.

In addition, the 2003-04 May Revision proposes a temporary one-half cent sales tax increase to repay deficit financing bonds expected to be sold in 2003-04. This sales tax increase is expected to become operative on October 1, 2003, and will automatically cease when the bonds are repaid. Revenues from this tax increase will not be deposited in the General Fund.

Personal Income Tax

The California personal income tax, which accounts for a significant portion of General Fund tax revenues, is closely modeled after the federal income tax law. It is imposed on net taxable income (gross income less exclusions and deductions), with rates ranging from 1.0 percent to 9.3 percent. Personal, dependent and other credits are allowed against the gross tax liability. In addition, taxpayers may be subject to an alternative minimum tax (AMT), which is much like the federal AMT. The personal income tax structure is highly progressive. For

instance, it is estimated that the top 1 percent of taxpayers pay 39.5 percent of the total personal income tax.

Taxes on capital gains realizations and stock options, which are largely linked to stock market performance, had become a larger component of personal income taxes over the last half of the 1990s. For example, these two income sources contributed almost a quarter of all General Fund tax revenue in 2000–01, a dramatic increase from their 5.6 percent share in 1995-96. The increasing influence that these stock market-related income sources had on personal income tax revenues linked to the highly progressive structure added a significant dimension of volatility. Just as the State’s remarkable revenue growth was driven by stock-market related gains, the current drop-off largely reflects the market’s decline. The 2003-04 May Revision forecast estimates that capital gains realizations and stock options accounted for roughly 12 percent of General Fund tax revenues in 2001-02, and will account for about 7.5 percent in 2002-03 and in 2003-04. See “Current State Budget—Economic Assumptions” below.

As noted above, the 2003-04 May Revision proposes to add a 10.3 percent personal income tax bracket at \$150,000 for single filers and \$300,000 for joint filers in 2003-04, and dedicate the increased revenues to local governments for the increased costs under State-Local Program Realignment. The 2003-04 May Revision also includes proposals for a one-year suspension of the teacher tax credit and the natural heritage preservation tax credit and EDD participation in the Treasury Offset Program.

The personal income tax is adjusted annually by the change in the consumer price index to prevent taxpayers from being pushed into higher tax brackets without a real increase in income.

Sales Tax

The sales tax is imposed upon retailers for the privilege of selling tangible personal property in California. Most retail sales and leases are subject to the tax. However, exemptions have been provided for certain essentials such as food for home consumption, prescription drugs, gas delivered through mains and electricity. Other exemptions provide relief for a variety of sales ranging from custom computer software to aircraft. Pursuant to federal law, out-of-state sales to Californians over the Internet are not taxed by the State at this time.

The breakdown of the basic 7.25 percent rate imposed on a statewide basis in 2002 is as follows:

- 5.00 percent represents the State General Fund tax rate.
- 2.00 percent is dedicated to cities and counties.
- 0.25 percent is dedicated to county transit systems.

Legislation in July 1991 raised the sales tax rate by 1.25 percent to its current level. Of this amount, 0.25 percent was added to the General Fund tax rate, and the balance was dedicated to cities and counties. One-half percent was a permanent addition to counties, but with the money earmarked to trust funds to pay for health and welfare programs whose administration

was transferred to counties. Another 0.5 percent of the State General Fund tax rate that was scheduled to terminate after June 30, 1993, was extended until December 31, 1993, and allocated to local agencies for public safety programs. Voters in a special election on November 2, 1993, approved a constitutional amendment to permanently extend this 0.5 percent sales tax for local public safety programs.

The 2003-04 May Revision proposes a temporary one-half cent sales tax increase beginning October 1, 2003. The revenues from this tax would be dedicated to the repayment of deficit financing bonds anticipated to be issued in 2003-04, and the tax would automatically cease when the bonds are retired.

Pursuant to prior law, 0.25 percent of a basic 5.00 percent State tax rate could be terminated upon certification by the Director of Finance by November 1 in any year that the balance in the budget reserve for two consecutive years exceeded 4 percent of General Fund revenues. The 0.25 percent rate would be reinstated if the Director of Finance subsequently determined that the reserve would not exceed 4 percent of General Fund revenues. Pursuant to this law, a 0.25 percent cut in the State sales tax occurred on January 1, 2001.

Legislation enacted as part of the 2001-02 Budget revised this test to provide that 0.25 percent of the basic 5.00 percent State tax rate may be suspended in any calendar year beginning on and after January 1, 2002, upon certification by the Director of Finance by November 1 in any year in which both of the following occur: (1) the General Fund reserve is expected to exceed 3 percent of revenues in that fiscal year and (2) actual revenues for the period May 1 through September 30 equal or exceed the May Revision forecast. The 0.25 percent rate will be reinstated the following year if the Director of Finance subsequently determines conditions (1) or (2) above are not met for that fiscal year. The reserve was not sufficient to trigger an additional year of reduction for calendar year 2002 or 2003. The 2003-04 May Revision forecast estimates that the reserve level will again be insufficient to trigger a reduction for calendar year 2004. See "Current State Budget" below.

Corporation Tax

Corporation tax revenues are derived from the following taxes:

1. The franchise tax and the corporate income tax are levied at an 8.84 percent rate on profits. The former is imposed on corporations for the privilege of doing business in California, while the latter is imposed on corporations that derive income from California sources but are not sufficiently present to be classified as doing business in the State.
2. Banks and other financial corporations are subject to the franchise tax plus an additional tax at the rate of 2 percent on their net income. This additional tax is in lieu of personal property taxes and business license taxes.
3. The alternative minimum tax (AMT) is similar to that in federal law. In general, the AMT is based on a higher level of net income computed by adding back certain tax preferences. This tax is imposed at a rate of 6.65 percent.

4. A minimum franchise tax of up to \$800 is imposed on corporations subject to the franchise tax but not on those subject to the corporate income tax. New corporations are exempted from the minimum franchise tax for the first two years of incorporation.

5. Sub-Chapter S corporations are taxed at 1.5 percent of profits.

Taxpayers with net operating losses (i.e., an excess of allowable deductions over gross income) are allowed to carry forward those losses for tax purposes and deduct a portion in subsequent years. Chapter 488, Statutes of 2002 (AB 2065), suspends the use of any carryover losses for the 2002 and 2003 tax years, but allows taxpayers to deduct those losses beginning in the 2004 tax year and extends the expiration date for those losses by two years. That Chapter also increases the percent of a taxpayer's net operating loss ("NOL") that can be carried forward from 65 percent to 100 percent beginning January 1, 2004, for NOLs generated after that date. About 85 percent of NOL is deducted from corporation taxes with the balance deducted from personal income tax.

The May Revision continues to include the 2003-04 Governor's Budget proposals to (1) prevent banks from utilizing Regulated Investment Companies to avoid California tax by improperly sheltering income; (2) clarify that the Manufacturers' Investment Credit (MIC) is intended to apply to manufacturing activities as specified in the Standard Industrial Code; (3) extend the sunset date of the MIC; and (4) clarify that current law does not allow Subpart F income to be excluded from a water's edge combined report. These proposals are estimated to generate \$95 million of additional revenue in 2003-04, if approved by the Legislature.

Insurance Tax

The majority of insurance written in California is subject to a 2.35 percent gross premium tax. For insurers, this premium tax takes the place of all other state and local taxes except those on real property and motor vehicles. Exceptions to the 2.35 percent rate are certain pension and profit-sharing plans which are taxed at the lesser rate of 0.5 percent, surplus lines and nonadmitted insurance at 3 percent and ocean marine insurers at 5 percent of underwriting profits.

Other Taxes

Other General Fund major taxes and licenses include: Estate, Inheritance and Gift Taxes; Cigarette Taxes; Alcoholic Beverage Taxes; Horse Racing License Fees and Trailer Coach License Fees.

The California estate tax is based on the State death tax credit allowed against the federal estate tax. The California estate tax is designed to pick up the maximum credit allowed against the federal estate tax return. The federal Economic Growth and Tax Reconciliation Act of 2001 phases out the federal estate tax by 2010. As part of this, the Act reduced the State pick-up tax by 25 percent in 2002, 50 percent in 2003, and 75 percent in 2004, and eliminates it beginning in 2005. The provisions of this federal Act sunset after 2010; at that time, the federal estate tax will be reinstated along with the State's estate tax, unless future federal legislation is enacted to make the provisions permanent.

Special Fund Revenues

The California Constitution and statutes specify the uses of certain revenue. Such receipts are accounted for in various special funds. In general, special fund revenues comprise four categories of income:

- Receipts from tax levies which are allocated to specified functions, such as motor vehicle taxes and fees and certain taxes on tobacco products.
- Charges for special services to specific functions, including such items as business and professional license fees.
- Rental royalties and other receipts designated for particular purposes (e.g., oil and gas royalties).
- Motor vehicle related taxes and fees accounted for about 41 percent of all special fund revenues and transfers in 2001-02. Principal sources of this income are motor vehicle fuel taxes, registration and weight fees and vehicle license fees. During fiscal year 2001-02, \$7.1 billion was derived from the ownership or operation of motor vehicles. This was 15 percent below the 2000-01 level. About \$3.1 billion of this revenue was returned to local governments. The remainder was available for various State programs related to transportation and services to vehicle owners. These amounts (as well as those shown below in the table "Comparative Yield of State Taxes—All Funds") include the additional fees and taxes derived from the passage of Proposition 111 in June 1990.

Vehicle License Fee

Vehicle license fees, over and above the costs of collection and refunds authorized by law, are constitutionally defined local revenues. Chapter 322, Statutes of 1998 ("Chapter 322"), established a vehicle license fee ("VLF") offset program, scheduled to be implemented in successive stages if General Fund revenues met certain targets. Pursuant to Chapter 322, vehicle license fees were reduced (offset) by 25 percent beginning January 1, 1999. Later legislation increased the offset to 35 percent for 2000 and the first half of calendar year 2001, and to 67.5 percent July 1, 2001. These offset levels are expected to reduce vehicle license fee revenues by \$3.985 billion in fiscal year 2002-03.

Under Chapter 322, a continuous appropriation from the General Fund "backfills" the vehicle license fee revenue that local governments would otherwise lose due to the fee reductions. Chapter 322 also provided that if there were insufficient General Fund moneys to fully backfill the VLF offset, the percentage offset would be reduced proportionately (i.e., the license fee payable by drivers would be increased) to assure that local governments are not disadvantaged. On June 20, 2003, it was determined that insufficient General Fund moneys were available to continue to fund any portion of the VLF offsets to local governments as of that date. See "Local Governments" above. Accordingly, the VLF paid by taxpayers will return within 90 days to the pre-1999 level of two percent of a vehicle's depreciated value and the State will not be obligated to make any offset payments from the General Fund in 2003-04.

A State legislator and a taxpayers group have each made statements to the press in which they threaten to bring suit in the event the VLF is increased. To date, no such action has been served on the State.

Taxes on Tobacco Products

On November 8, 1988, voters approved Proposition 99, which imposed, as of January 1, 1989, an additional 25 cents per pack excise tax on cigarettes, and a new, equivalent excise tax on other tobacco products. The initiative requires that funds from this tax be allocated to anti-tobacco education and research, to indigent health services, and to environmental and recreation programs.

Proposition 10, approved in 1998, increased the excise tax imposed on distributors selling cigarettes in California to 87 cents per pack effective January 1, 1999. At the same time, this proposition imposed a new excise tax on cigars, chewing tobacco, pipe tobacco, and snuff at a rate equivalent to the tax increase on cigarettes of 50 cents per pack. In addition, the higher excise tax on cigarettes automatically triggered an additional increase in the tax on other tobacco products effective July 1, 1999, with the proceeds going to the Cigarette and Tobacco Products Surtax Fund. Thus, this Proposition increased the total excise tax on other tobacco products by an amount equivalent to an increase in the cigarette tax of one dollar per pack. There is litigation pending challenging the enactment of these new taxes. See "Litigation."

The State excise tax on cigarettes of 87 cents per pack and other tobacco product taxes are earmarked as follows:

1. Fifty cents of the per-pack tax on cigarettes, and the equivalent rate levied on non-cigarette tobacco products, are deposited in the California Children and Families First Trust Fund and are allocated primarily for early childhood development programs.

2. Twenty-five cents of the per-pack tax on cigarettes and the equivalent rates levied on non-cigarette tobacco products are allocated to the Cigarette and Tobacco Products Surtax Fund. These funds are appropriated for anti-tobacco education and research, indigent health services, and environmental and recreation programs. This portion of the excise tax was imposed on January 1, 1989, after voters approved Proposition 99 of 1988.

3. Ten cents of the per-pack tax is allocated to the State's General Fund.

4. The remaining two cents of the per-pack tax is deposited into the Breast Cancer Fund. Legislation enacted in 1993 added the additional per pack excise tax for the purpose of funding breast cancer research.

The 2003-04 Governor's Budget proposed to increase the tobacco excise tax by \$1.10 per pack of cigarettes, to \$1.97 per pack, effective July 1, 2003, with the proceeds dedicated to local governments for the increased costs under State-Local Program Realignment. The 2003-04 May Revision replaces this proposal with a two step per pack excise tax increase. On July 1, 2003, the excise tax per pack would increase 23 cents, to \$1.10. On July 1, 2004, the excise tax per pack would increase an additional 40 cents, to \$1.50. These proposals would also increase the tax on other tobacco products, beginning July 1, 2004, at a rate equivalent to the 23 cents per pack tax increase on cigarettes, and beginning July 1, 2005, at a rate equivalent to the 40 cents per pack tax, with the proceeds going to the Cigarette and Tobacco Products Surtax Fund.

Tobacco Litigation

In 1998, the State (together with 45 other states and certain U.S. jurisdictions) signed a settlement agreement with the four major cigarette manufacturers. The State agreed to drop its lawsuit and not to sue in the future for monetary damages. Tobacco manufacturers agreed to billions of dollars in payments and restrictions on marketing activities. Under the settlement, the companies agreed to pay California governments approximately \$25 billion (subject to adjustments) over a period of 25 years. Payments continue in perpetuity, with current projections of \$1.2 billion in 2025, steadily increasing each year to \$1.6 billion in 2045. Under a separate Memorandum of Understanding, half of the money will be paid to the State and half to local governments (all counties and the cities of San Diego, Los Angeles, San Francisco and San Jose).

The specific amount to be received by the State and local governments is subject to adjustment. Details in the settlement allow reduction of the companies' payments for decreases in cigarette shipment volumes by the settling manufacturers, payments owed to certain "Previously Settled States" and certain types of offsets for disputed payments, among other things. However, settlement payments are adjusted upward each year by at least 3% for inflation, compounded annually. For example, the "third annual" payment, received in April 2002, was approximately 12 percent lower than the base settlement amount due to the combined impact of: (i) the inflation adjustment, which increased the base payment by 9.7%; (ii) the volume adjustment, which reduced the inflation-adjusted base payment by approximately 18.8%; (iii) the Previously Settled States reduction, which further reduced the State's receipts by 12.45%; and (iv) the State's receipt of approximately \$20.5 million as a result of a disputed payment. Future payment estimates have been reduced in a similar manner, assuming a 3% annually compounded inflation increase and declining shipments, based upon a forecast of U.S. Cigarette Consumption prepared by Global Insight, Inc.

During fiscal year 2001-02, the General Fund received \$478 million in settlement payments. Of that amount, \$76 million was deposited in the General Fund and \$402 million was deposited into a special fund to pay certain health care costs. The May Revision forecasts payments to the State totaling \$474 million and \$174 million in 2002-03 and 2003-04, respectively, which will be deposited in a special fund to pay certain healthcare costs.

Chapter 414, Statutes of 2002, allows the issuance of revenue bonds to generate \$4.5 billion for the General Fund during the 2002-03 fiscal year secured by the Tobacco Settlement revenues received by the State beginning in the 2003-04 fiscal year. An initial sale producing \$2.5 billion in revenue was completed in January 2003. The second part of the sale, originally scheduled in April 2003, has been cancelled because of uncertainties in the market for the bonds.

Recent Tax Receipts

The following table shows the trend of major General Fund and total taxes per capita and per \$100 of personal income for the past four years, the current fiscal year, and the budget year.

<u>Fiscal Year</u>	<u>Trend of State Taxes per Capita(a)</u>		<u>Taxes per \$100 of Personal Income</u>	
	<u>General Fund</u>	<u>Total</u>	<u>General Fund</u>	<u>Total</u>
1998-99	\$1,771.02	\$2,121.72	\$6.25	\$7.48
1999-00	2,095.53	2,447.03	7.04	8.22
2000-01	2,223.15	2,589.79	6.88	8.02
2001-02(b)	1,806.41	2,112.36	5.56	6.50
2002-03(c)	1,818.48	2,120.11	5.64	6.57
2003-04(c)	1,865.78	2,370.23	5.69	7.23

- (a) Data reflect population figures based on the 2000 Census.
 (b) Preliminary.
 (c) Estimated.

SOURCE: State of California, Department of Finance.

The following table gives the actual and estimated revenues by major source for the last four years, the current fiscal year, and the upcoming budget year.

COMPARATIVE YIELD OF STATE TAXES—ALL FUNDS 1998-99 THROUGH 2003-04 (Modified Accrual Basis) (Thousands of Dollars)

<u>Year Ending June 30</u>	<u>Sales and Use(a)</u>	<u>Personal Income</u>	<u>Corporation</u>	<u>Tobacco (b)</u>	<u>Inheritance, Estate and Gift</u>	<u>Insurance</u>	<u>Alcoholic Beverages</u>	<u>Horse Racing</u>	<u>Motor Vehicle Fuel (c)</u>	<u>Motor Vehicle Fees (d)</u>
1999	22,890,693	30,894,865	5,724,237	976,512	890,490	1,253,972	273,112	61,185	3,025,226	5,610,374
2000	25,525,788	39,578,237	6,638,898	1,216,651	928,146	1,299,777	282,166	44,130	3,069,694	5,263,245
2001	26,616,073	44,618,532	6,899,322	1,150,869	934,709	1,496,556	288,450	42,360	3,142,142	5,286,542
2002	26,004,521	33,051,107	5,333,030	1,102,806	890,627	1,595,846	292,627	42,247	3,295,903	3,836,795
2003(e)	24,872,747 (f)	32,100,000	6,664,011	1,068,200	694,800	1,863,150	290,000	44,455	3,307,244	3,923,911
2004(e)	27,794,512 (f,g)	35,016,000(h)	7,074,011	1,271,200	436,500	1,918,150	288,000	44,985	3,313,301	7,704,472

- (a) For fiscal years 1998-99 through 2003-04, numbers include local tax revenue from the 0.5 percent rate increase enacted by Chapter 85, Statutes of 1991, for the State-local realignment program. The 0.5% rate is equivalent to about \$2.3 billion. The figures also reflect a 0.25 percent reduction during calendar year 2001.
- (b) Proposition 10 (November 1998) increased the cigarette tax to \$0.87 per pack and added the equivalent of \$1.00 tax to other tobacco products. The 2003-04 May Revision proposes to increase the cigarette tax by \$0.23 per pack, to \$1.10 per pack, in 2003-04 to finance increased costs to local governments under State-Local Program Realignment. This increase (estimated in the amount of \$267 million) is included in 2003-04 estimates.
- (c) Motor vehicle fuel tax (gasoline), use fuel tax (diesel and other fuels), and jet fuel.
- (d) Registration and weight fees, motor vehicle license fees and other fees. Vehicle license fee values reflect a 25 percent reduction for 1999; a 35 percent reduction for 2000 and the first half of 2001; a 67.5 percent reduction for the second half of 2001 through 2003, and no reduction in 2004.

- (e) Estimated.
- (f) The figures do not include voter approved local revenue, the 0.50 percent Local Public Safety Fund revenue, the 1.0 percent local city and county operations revenue (Bradley-Burns), or the 0.25 percent county transportation funds revenue.
- (g) The 2003-04 May Revision proposes a temporary one-half cent sales tax increase beginning October 1, 2003. The revenues from this proposal would be dedicated to the repayment of deficit financing bonds anticipated to be sold in 2003-04. When the bonds are retired, the sales tax would automatically be reduced one-half cent. This increase (estimated in the amount of \$1.742 billion) is included in the 2003-04 estimates.
- (h) The 2003-04 May Revision proposes to add a 10.3 percent personal income tax bracket in 2003-04 to finance increased costs to local governments under State-Local Program Realignment. This increase (estimated in the amount of \$1.56 billion) is included in 2003-04 estimates.

NOTE: This table shows taxes which provide revenue both to the General Fund and State special funds. Also, some revenue sources are dedicated (or proposed to be dedicated) to local governments. This accounts for differences between the information in this table and the table on page A-42.

SOURCE: Fiscal years 1998-99 through 2001-02: State of California, Office of the State Controller.
Fiscal years 2002-03 and 2003-04: State of California, Department of Finance.

State Expenditures

The following table summarizes the major categories of State expenditures, including both General Fund and special fund programs.

GOVERNMENTAL COST FUNDS					
(Budgetary Basis)					
Schedule of Expenditures by Function and Character					
Fiscal Years 1997-98 to 2001-02					
(Thousands)					
	<u>1997-98</u>	<u>1998-99</u>	<u>1999-00</u>	<u>2000-01</u>	<u>2001-02</u>
Function					
Legislative, Judicial, Executive					
Legislative.....	\$ 209,690	\$ 219,814	\$ 232,323	\$ 262,370	\$ 265,312
Judicial.....	766,932	1,346,131	1,372,681	1,478,710	1,633,518
Executive.....	919,606	958,189	1,241,219	1,352,128	1,371,891
State and Consumer Services.....	771,444	829,745	856,096	950,192	1,100,942
Business, Transportation and Housing					
Business and Housing.....	136,558	136,893	156,499	601,053	240,237
Transportation.....	3,924,428	4,462,905	5,549,520	4,417,139	6,052,926
Technology, Trade and Commerce.....	62,235	130,796	488,489	140,833	81,832
Resources.....	1,323,860	1,695,323	1,858,844	3,349,003	2,284,269
Environmental Protection.....	605,584	600,060	689,678	869,539	993,144
Health and Human Services.....	18,059,611	19,616,132	21,806,291	24,204,531	26,563,743
Correctional Programs.....	3,901,296	4,181,474	4,412,542	4,952,927	5,242,369
Education					
Education-K through 12.....	21,574,341	22,783,975	26,356,838	28,720,596	28,078,228
Higher Education.....	7,022,658	7,838,117	8,553,343	9,655,954	9,945,193
General Government					
General Administration.....	764,615	859,703	982,923	1,294,587	2,475,564
Debt Service.....	1,979,211	1,988,176	2,072,960	2,270,649	2,432,942
Tax Relief.....	453,030	450,213	1,840,129	4,655,826	3,028,703
Shared Revenues.....	3,892,036	4,151,197	3,677,687	4,385,429	5,528,996
Brown vs. US Dept. of Health and Human Services					96,000
Other Statewide Expenditures.....	1,373,823	891,070	580,307	635,475	476,170
Expenditure Adjustment for Encumbrances.....	(162,630)	(461,310)	(628,506)	(1,943,208)	(681,856)
Credits for Overhead Services by General Fund.....	(125,678)	(144,041)	(170,594)	(197,343)	(251,575)
Statewide Indirect Cost Recoveries.....	(48,963)	(32,791)	(37,423)	(36,610)	(47,862)
Total.....	\$67,403,687	\$72,501,771	\$81,891,846	\$92,019,780	\$96,910,686
Character					
State Operations.....	\$20,199,031	\$21,092,849	\$22,864,874	\$24,850,286	\$27,994,343
Local Assistance.....	46,666,925	50,734,442	58,369,828	66,087,018	67,993,721
Capital Outlay.....	537,731	674,480	657,144	1,082,476	922,622
Total.....	\$67,403,687	\$72,501,771	\$81,891,846	\$92,019,780	\$96,910,686

SOURCE: State of California, Office of the State Controller.

PRIOR FISCAL YEARS' FINANCIAL RESULTS

Following a severe recession in the early 1990s, the State's financial condition improved markedly starting in 1995-96, due to a combination of better than expected revenues, slowdown in growth of social welfare programs, and continued spending restraint based on actions taken in earlier years. The economy grew strongly between 1994 and 2000, generally outpacing the nation, and as a result, for the five fiscal years from 1995-96 to 1999-00, the General Fund tax

revenues (a total of more than \$16 billion over these five years) exceeded the estimates made at the time the budgets were enacted. These additional funds were largely directed to school spending as mandated by Proposition 98, to make up shortfalls from reduced federal health and welfare aid in 1995-96 and 1996-97 and to fund new program initiatives, including education spending above Proposition 98 minimums, tax reductions, aid to local governments and infrastructure expenditures.

2000 Budget Act. The 2000 Budget Act, signed by the Governor on June 30, 2000, assumed General Fund revenues and transfers of \$73.9 billion, a 3.8 percent increase over 1999-00 estimates. The 2000 Budget Act appropriated \$78.8 billion from the General Fund, a 17.3 percent increase over 1999-00, and reflected the use of \$5.5 billion from the Special Fund for Economic Uncertainties (SFEU) available from surpluses in the prior year. About \$7.0 billion of the increased spending in 2000-01 was for one-time expenditures and investments. Because of the State's strong cash position, the Administration did not undertake a revenue anticipation note borrowing in 2000-01.

The 2002-03 Governor's Budget released on January 10, 2002, provided final 2000-01 revenue and expenditures. Expenditures in 2000-01 were \$78.0 billion, about \$2.0 billion below the 2001 Budget Act estimates, with revenues of \$71.4 billion. The 2002-03 Governor's Budget reported that the June 30, 2001 SFEU balance, the budget reserve, was approximately \$1.3 billion. This figure recognized the disbursement prior to June 30, 2001, of about \$6.2 billion from the General Fund to make loans for the DWR power supply program (see "State Finances—Repayment of Energy Loans" above). (At the time of enactment of the 2001 Budget Act, the Department of Finance had estimated the June 30, 2001 balance in the SFEU at \$6.3 billion, but without recognition of the loans as an expenditure for budget purposes.)

2001 Budget Act. The Fiscal Year 2001 Budget Act was signed by the Governor on July 26, 2001. The spending plan for 2001-02 included General Fund expenditures of \$78.8 billion, a reduction of \$1.3 billion from the prior year. It was expected that this could be accomplished without serious program cuts because such a large part of the 2000 Budget Act comprised one-time expenditures. The spending plan utilized more than half of the budget surplus as of June 30, 2001, but still left a projected balance in the SFEU at June 30, 2002, of \$2.6 billion, the largest appropriated reserve in State history. The 2001 Budget Act assumed that, during the course of the fiscal year, the \$6.2 billion advanced by the General Fund to the Department of Water Resources for power purchases would be repaid with interest. See "State Finances—Repayment of Energy Loans" above.

The final estimate of fiscal year 2001-02 revenues and expenditures, included in the 2003-04 Governor's Budget in January 2003, showed an unprecedented drop in revenues compared to the prior year. The final estimate for the three largest tax sources was \$59.7 billion, a drop of over \$13 billion from 2000-01, the vast bulk of which was attributable to reduced personal income taxes from stock option and capital gains activity. This revenue shortfall and the delay of the DWR power revenue bonds past June 30, 2002, resulted in a substantial budgetary deficit and cash flow difficulties. The Department of Finance estimates that, on a budgetary basis, the General Fund had a \$2.1 billion deficit at June 30, 2002. See "Recent Developments Regarding State Economy and Finances," "State Indebtedness—Cash Flow

Borrowings” above and “Current State Budget—Summary of State Revenues and Expenditures” below.

Within a few months of the start of the 2001-02 fiscal year, the Administration recognized that economic growth and stock market levels were not meeting projections, and that revenues were falling below projections. Accordingly, the Governor imposed an immediate spending freeze for many State agencies in November 2001, and the Legislature approved spending reductions and deferrals totaling \$2.3 billion for the 2001-02 fiscal year in January 2002. Despite these steps, as noted above, the State ended the fiscal year in a substantial deficit. See “Current State Budget—Fiscal Year 2002-03 Budget” below.

The 2001 Budget Act as initially enacted included Proposition 98 per pupil spending increases of 4.9 percent. Total General Fund spending of \$32.4 billion for K-12 education fully funded enrollment and cost of living increases and also provided additional funding for a number of programs. Higher education funding was increased to allow for enrollment increases at both the University of California and the California State University system with no fee increases. Health and human services generally were fully funded for anticipated caseload growth. Funding for many of these programs was subsequently reduced as a result of the mid-year corrections noted above.

The 2001 Budget Act altered the six-year transportation funding plan started in the 2000-01 fiscal year. The Legislature postponed for two years the transfer of sales taxes on gasoline to support transportation programs, and this transfer will take place during the 2003-04 to 2007-08 fiscal years. As a result, \$2.5 billion of these sales tax revenues will remain in the General Fund over the 2001-02 and 2002-03 fiscal years. To allow all current projects to remain on schedule through 2002-03, the legislation authorized certain internal loans from other transportation accounts. Part of the Budget Act compromise was an agreement to place on the March 2002 statewide ballot a constitutional amendment which would make permanent, after 2007-08, the dedication of sales taxes on gasoline to transportation purposes. This measure was approved by the voters.

CURRENT STATE BUDGET

The discussion below of the fiscal year 2002-03 budget, the proposed 2003-04 budget and the table under “Summary of State Revenues and Expenditures” are based on estimates and projections of revenues and expenditures for the current fiscal year and future fiscal years and must not be construed as statements of fact. These estimates and projections are based upon various assumptions, which may be affected by numerous factors, including future economic conditions in the State and the nation, and there can be no assurance that the estimates will be achieved. See “Recent Developments Regarding State Economy and Finances” above and “Current State Budget—Revenue and Expenditure Assumptions” below.

Fiscal Year 2002-03 Budget

Background. The 2002-03 Governor’s Budget, released on January 10, 2002 (the “2002-03 Governor’s Budget”), projected a fall-off in General Fund revenues due to the national economic recession combined with the stock market decline, which began in mid-2000.

Personal Income Tax receipts, which include stock option and capital gains realizations, were particularly affected by the slowing economy and stock market decline. As a result, the Administration projected a combined budget gap for 2001-02 and 2002-03 of approximately \$12.5 billion.

The May Revision to the 2002-03 Governor's Budget, released in May 2002, projected further deterioration in revenues of \$9.5 billion and additional costs of \$1.6 billion over the 2001-02 and 2002-03 fiscal years. As a result, the combined budget gap for 2001-02 and 2002-03 rose from the \$12.5 billion estimated in January to \$23.6 billion.

The 2002 Budget Act was signed by the Governor on September 5, 2002. The budget bill passed by the Legislature did not differ substantially from the Governor's May Revision proposal. The Governor only vetoed \$219 million of General Fund expenditures from the budget bill passed by the Legislature. The 2002 Budget Act addressed a \$23.6 billion gap between expenditures and resources through a combination of program reductions, loans, fund shifts, accelerations and transfers, and modest tax changes.

As described below under "Continuing Budget Shortfall," the revenue estimates have proved to be substantially overstated, as expected economic recovery has not occurred, among other factors. Based on revised estimates in the 2003-04 May Revision, released on May 14, 2003, revenues and transfers in 2002-03 will be \$70.8 billion, with expenditures of \$78.1 billion, resulting in a cumulative budget deficit through June 30, 2003, of about \$10.7 billion. As part of the May Revision, the Governor proposed to eliminate that deficit by issuing long-term bonds, and the Administration accordingly has accrued the bond proceeds in fiscal year 2002-03, so that the estimate for the June 30, 2003 SFEU balance is now effectively zero. See "Summary of State Revenues and Expenditures" below.

The 2002 Budget Act addressed a \$23.6 billion gap between expenditures and resources through a combination of program reductions, loans, fund shifts, accelerations and transfers, and modest tax changes:

1. Program cost savings in the 2001-02 and 2002-03 fiscal years were expected to total about \$7.458 billion. However, some of these savings will not be realized.
2. The receipt of \$4.5 billion in 2002-03 from the securitization (sale) of a large portion of the State's future receipt of payment from tobacco companies from the settlement of litigation against those companies. This sale was scheduled to close in two segments. The first sale closed in January 2003, producing General Fund revenues of \$2.5 billion. The second sale was expected to occur in April 2003 and generate up to \$2.0 billion of General Fund revenues, but that sale has been cancelled because of unsettled market conditions. See "State Finances—Tobacco Litigation" above.
3. A total of \$2.028 billion in loans from various funds, including \$1.218 billion from transportation funds. These long-term loans are not included in reports of inter-fund borrowing. See "State Finances—Interfund Borrowing."
4. The shift of \$1.328 billion of expenditures from the General Fund to other funding sources, such as special funds and proposed future bond funds.

5. The receipt of \$1.2 billion additional revenues in 2002-03 from a two-year suspension of the net operating loss provisions in current law.

6. General Fund savings of \$1.728 billion from the deferral of \$1.047 billion of education expenditures from 2001-02 to early 2002-03 and \$681 million of education expenditures from 2002-03 to early 2003-04. These deferrals were not expected to significantly impact underlying programs.

7. General Fund savings of \$1.083 billion (\$223 million in 2001-02 and \$860 million in 2002-03) from the Treasurer's Debt Restructuring Plan to amortize the State's long-term debt to more closely approximate level annual debt service costs rather than the level annual principal. The plan also included the issuance of refunding debt to pay selected maturities of general obligation bonds due between February 2002 and June 2004. The savings identified here are from the first of two phases of refunding bonds; the second phase will reduce costs in fiscal year 2003-04.

8. Anticipated increases in federal funding for health and human services programs, security/bioterrorism and other areas totaling about \$1.081 billion.

9. Additional revenue of \$1.651 billion in 2002-03 due to Federal Tax Conformity and Tax Compliance (\$1.081 billion); increasing the withholding on stock option and bonus income from 6 percent to 9.3 percent (\$400 million); and suspending the teacher retention credit for one year (\$170 million). Federal Tax Conformity and Tax Compliance includes revenue generated from the following: (a) the conformity of California tax law with federal tax law regarding accounting for bad debt reserves for large banks, (b) the pension and individual retirement account conformity package included in the Governor's Budget, which was passed by the Legislature and signed by the Governor on May 8, 2002, (c) waiving penalties and interest on delinquent accounts, (d) increasing collections activities, (e) ensuring proper auditing of tax credits and (f) improving the effectiveness of the tax protest and settlement programs.

10. Accelerations and transfers from other funds to the General Fund totaling \$1.585 billion.

Other elements of the final budget agreement were enactment of ACA 11 (See "State Finances – Constraints on the Budgetary Process" above) and a law requiring spending in the 2003-04 fiscal year not to exceed revenues in the year.

Continuing Budget Shortfall

Within a few months after the 2002 Budget Act was adopted, it became evident that economic growth, which had been expected to accelerate in the second half of 2002 and into 2003, was instead remaining stagnant, with net job losses statewide. As a result, revenue projections for the 2002-03 fiscal year were substantially overstated. In mid-November 2002, the Legislative Analyst issued a report (the "LAO Report") indicating that, absent corrective actions, the General Fund would have a budget deficit of about \$6.1 billion by the end of the 2002-03 fiscal year (compared to the \$1 billion reserve balance predicted in the 2002 Budget Act) and a cumulative budget deficit over \$21 billion by the end of the 2003-04 fiscal year. Furthermore, even given accelerating economic growth in 2003 and beyond (which is not assured), there

would, unless corrective actions were taken, continue to be a substantial deficit between revenues and expenditures, in a potential range from \$12-16 billion annually, through at least fiscal year 2007-08.

In the summer of 2002, the Governor notified all State agencies to prepare 2003-04 budget proposals for a minimum of 20 percent cut in funding. On November 21, 2002, the Governor further directed State agencies to take immediate action to reduce any non-critical or non-essential activities by not filling any vacant positions; to cancel, postpone or amend contracts, grants, purchase orders and similar commitments; to eliminate additional non-essential vacant positions; to delay construction or signing of new leases for space; to cancel or postpone non-essential trips; and to generate new proposals for current year program reductions.

Shortly after the LAO Report was released, the Governor announced that the Administration also projected a substantial budget gap in 2002-03 and 2003-04, and he called a special session of the Legislature to begin on December 9, 2002, to consider legislation for mid-year spending cuts and other budgetary actions. On December 6, 2002, the Governor released proposals for immediate action to reduce the budget gap by about \$10.2 billion (\$5.5 billion for 2002-03). The Governor requested action on these proposals early in 2003 in order to maximize savings in 2002-03 fiscal year. The Legislature passed budget adjustment legislation in March and April, 2003, totaling about \$6.9 billion in spending reductions, deferrals and funding transfers (\$3.3 billion for 2002-03 and \$3.6 billion for 2003-04). The largest part of the reductions (including a \$1.1 billion deferral into the 2003-04 fiscal year) are for K-12 education funding. The totals reflect the enactment of legislation in May 2003 permitting the sale of about \$1.9 billion of pension obligation bonds to fund the State's 2003-04 payments to the Public Employees' Retirement System.

The Governor has revised his budget proposals to address the limited actions taken by the Legislature since the release of the Governor's Budget. These new proposals are described below under "Fiscal Year 2003-04 Budget."

Fiscal Year 2003-04 Budget

Governor's Budget. The 2003-04 Governor's Budget, released on January 10, 2003 (the "2003-04 Governor's Budget"), projected a significant downward revision in State revenues as a result of the longer than expected economic recovery. The decline was mainly due to weak personal income tax revenues, which dropped by nearly 26 percent in 2001-02 and are expected to decline by another 0.5 percent in 2002-03. As a result, the Administration projected a \$34.6 billion budget shortfall for 2002-03 and 2003-04.

The 2003-04 Governor's Budget projected revenues from the three largest tax sources to be about \$61.7 billion in 2002-03, more than \$6 billion lower than projected in the 2002 Budget Act. Most of the decline is attributable to the personal income tax revenues, which are particularly impacted by the stock market's decline. The 2003-04 Governor's Budget projected total revenues and transfers of \$73.1 billion and \$69.2 billion in 2002-03 and 2003-04, respectively. The estimate for 2002-03 included about \$2.8 billion of transfers and loans.

The Administration proposed the following major actions to close the \$34.6 billion budget shortfall for the 2002-03 and 2003-04 fiscal years combined:

1. Expenditure reductions totaling \$20.7 billion. This amount included reductions of \$6.2 billion for K-12 education, \$2.1 billion for higher education, \$3.3 billion for health and human services, and \$2.7 billion for general government. This amount also included \$4.2 billion of savings from reducing the vehicle license fee backfill to cities and counties.

2. General Fund savings totaling \$8.2 billion due to the realignment of various programs, including Mental Health and Substance Abuse, Children and Youth, Healthy Communities, Long-Term Care and Court Security. Under realignment, the responsibility for these programs would be transferred to the cities and counties, and the State-local cost ratios for some programs would be changed. Realignment was estimated to cost counties and trial courts \$8.3 billion. However, the Budget also proposed revenue increases to support the increased financial obligations of counties under realignment (\$4.6 billion from a one-cent sales tax increase, \$2.6 billion from the addition of 10 percent and 11 percent personal income tax brackets, and \$1.2 billion from a \$1.10 cigarette tax increase).

3. Fund shifts from the General Fund to other fund sources totaling \$1.9 billion (\$816 million included in the Mid-Year Spending Reduction Proposals).

4. Transfers and other revenue of \$2.1 billion. This amount included \$1.5 billion from revenue sharing agreements that are anticipated to result from compact negotiations with the Indian tribes.

5. Loans and borrowing of \$1.7 billion. This amount included \$1.5 billion from pension bonds or a loan to fund the 2003-04 retirement obligations to CalPERS and CalSTRS.

The Legislative Analyst's Office released a report following publication of the 2002-03 Governor's Budget, in which the two-year budget gap was projected to be around \$26 billion, as compared to the Governor's estimate of \$34.6 billion. About \$3 billion of the difference was attributed to somewhat more optimistic economic and revenue forecasts by the LAO, compared to the Department of Finance. The balance of the difference, about \$5.5 billion, represented a difference in methods and timing by which the two agencies identified future spending requirements; this difference does not impact actual budgetary solutions, as the Governor had proposed spending reductions to offset the higher estimate of program requirements.

May Revision. On May 14, 2003, the Governor released the May Revision to the Governor's Budget (the "May Revision") which provided the latest revenue and economic forecasts, and revised budget proposals for fiscal year 2003-04. The economic projections are described below under "Revenue and Expenditure Assumptions."

The May Revision reduced the revenue estimate for 2002-03 to \$70.8 billion from the Governor's Budget estimate of \$73.1 billion. This results mostly from loss of \$2 billion of revenues due to the cancellation of the sale of tobacco securitization bonds in April 2003 (See "Tobacco Litigation" above). Otherwise, tax revenues for the second half of 2002-03 have been very close to the Governor's Budget projections, with some weakness in personal income tax offset by stronger than projected corporation tax receipts. Personal income tax withholding,

however, which can be indicative of future economic performance, has been slightly above earlier projections. The May Revision, therefore, has slightly increased the projections for tax revenues for 2003-04.

As a result principally of the loss of the tobacco securitization proceeds, the lost opportunities for savings because of legislative action in lower amounts than requested by the Governor, and higher than expected caseloads/populations for certain health and social services and correctional programs and required school payments, the May Revision has increased the estimated budget gap from \$34.6 billion to \$38.2 billion. The Governor made a number of fundamental changes in the May Revision from his earlier budget proposals. The most significant changes are the following:

1. A proposal to eliminate \$10.7 billion of the accumulated budget deficit as of June 30, 2003 by issuing bonds during fiscal year 2003-04. The bonds would be repaid from a temporary one-half cent sales tax increase estimated to generate about \$1.7 billion in 2003-04 and \$2.4 billion in 2004-05. Once the bonds are repaid, the sales tax increase would automatically be terminated. These bonds would have to be authorized by new legislation, which is presently under consideration along with other budget-related bills.

2. Elimination of most of the local government realignment proposal, leaving only about \$1.7 billion for transfer of certain mental health, child abuse prevention and child welfare and adult welfare programs to counties. To fund this shift, the Governor proposed increases in tobacco taxes of 23 cents per pack in 2003-04 and an additional 40 cents per pack in 2004-05, and the creation of a single new 10.3% personal income tax bracket for the highest income taxpayers. The remainder of the realignment proposals are under consideration in the 2003 legislative session for implementation in 2004-05.

3. Reduction of about \$2 billion from the total program cuts and savings, allowing restoration of funding for a number of education, public safety and health programs. The May Revision continued to assume \$4.2 billion of savings in 2003-04 from not funding vehicle license fee offsets. On June 20, 2003, it was determined that insufficient General Fund moneys were available to fund any portion of the vehicle license fee offsets to local governments, and as of that date the offsets were suspended. See "State Finances—Sources of Tax Revenue—Vehicle License Fees" above.

4. A variety of other proposals for funding shifts, transfers and borrowing (aside from the deficit financing bonds) remain in the May Revision proposals. This includes the previously-mentioned pension bond issue, now estimated in the amount of \$1.9 billion. The pension bonds have been authorized in statute, and by the Pension Bond Committee, which is the issuer of such bonds. A validation lawsuit is underway.

The following table summarizes the Administration's plan to close the \$38.2 billion budget gap.

ADDRESSING THE OVERALL \$38.2 BILLION GAP

(dollars in millions)

	Jan 10	May Revision	Percentage at May Revision
Cuts/Savings ^{1/}	\$20,728.3	\$18,875.4	49.4%
Realignments ^{2/}	8,154.0	1,732.4	4.5%
Fund Shifts	1,902.7	2,076.3	5.5%
Transfers	2,114.3	1,912.6	5.0%
Loans/Borrowing	1,683.3	2,901.5	7.6%
Deficit Financing ^{3/}		10,700.0	28.0%
Totals	\$34,582.7	\$38,198.2	100%

Note: Numbers may not add due to rounding.

^{1/} Includes VLF offset suspension starting July 1, 2003 for a total saving of \$4.2 billion.

^{2/} Dedicated tax revenue will be provided to local governments for these programs.

^{3/} A new temporary ½ cent sales tax will be raised to provide debt payments.

The May Revision, as summarized above, addresses the State's budgetary challenges in three phases:

- First, the accumulated budget deficit through June 30, 2003, is funded with the issuance of \$10.7 billion deficit financing bonds, anticipated in 2003-04.

- Second, remaining cuts, savings, fund shifts, transfers and borrowing will balance the budget for fiscal year 2003-04.

- The third element of the May Revision is a recognition that the steps taken to bring the 2003-04 budget into balance do not totally solve the underlying "structural deficit" between revenues and expenditures. If no further action is taken (assuming accuracy of revenue and expenditure estimates), there would be an estimated \$7.9 billion operating deficit in fiscal year 2004-05. The Governor proposed that the Legislature and Administration address longer-term budget solutions over the balance of the 2003 Legislative session. The Governor did not make specific proposals in the May Revision, but will explore the realignment proposals and other steps. The Governor also recognized that some budget choices could be placed before the voters in the March 2004 primary election.

Summary of State Revenues and Expenditures

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE--GENERAL FUND (Budgetary Basis)(a) FISCAL YEARS 1999-00 THROUGH 2003-04 (Millions)

	<u>1999-00</u>	<u>2000-01</u>	<u>2001-02</u>	<u>Estimated^(b) 2002-03^(c)</u>	<u>Projected^(b) 2003-04^(c)</u>
Fund Balance--Beginning of Period	\$ 3,907.7	\$ 9,639.7	\$ 9,017.5	\$ (2,109.8)	\$ 1,409.9
Restatements					
Prior Year Revenue, Transfer Accrual Adjustments	(204.6)	(158.8)	729.8	169.5	--
Prior Year Expenditure, Accrual Adjustments	<u>217.1</u>	<u>(229.9)</u>	<u>217.4</u>	<u>(45.2)</u>	<u>--</u>
Fund Balance--Beginning of Period, as Restated	\$ 3,920.2	\$ 9,251.0	\$ 8,505.1	\$ (1,985.5)	\$ 1,409.9
Revenues	\$71,555.6	\$77,609.9	\$ 64,060.3	\$67,799.2	\$69,205.3
Other Financing Sources					
Deficit Financing Bond ^(d)				10,700.0	
Transfers from Other Funds	423.3	6,561.8 ^(e)	2,143.3	2,951.9	1,728.7
Other Additions	<u>48.1</u>	<u>46.3</u>	<u>33.9</u>	<u>--</u>	<u>--</u>
Total Revenues and Other Sources	\$72,027.0	\$84,218.0	\$ 66,237.5	\$81,451.1	\$70,934.0
Expenditures					
State Operations	\$15,942.8	\$17,641.7	\$ 19,085.7	\$18,208.9	\$17,469.0
Local Assistance	49,974.7	58,441.4	57,142.0	59,698.9	52,885.9
Capital Outlay	186.2	2,044.3	323.5	147.9	77.8
Unclassified	--	--	--	--	--
Other Uses					
Transfer to Other Funds	<u>203.8</u>	<u>6,324.1^(d)</u>	<u>301.2</u>	<u>--^(f)</u>	<u>--^(f)</u>
Total Expenditures and Other Uses	\$66,307.5	\$84,451.5	\$ 76,852.4	\$ 78,055.7	\$ 70,432.7
Revenues and Other Sources Over or (Under) Expenditures and Other Uses	\$ 5,719.5	\$ (233.5)	\$(10,614.9)	\$ 3,395.4	\$ 501.3
Fund Balance					
Reserved for Encumbrances	\$ 701.3	\$ 1,834.3	\$ 1,491.5	\$ 1,401.9	\$ 1,401.9
Reserved for Unencumbered Balances of Continuing Appropriations ^(g)	1,115.2	1,436.7	827.3	270.0	174.9
Reserved for School Loans ^(h)	699.7	349.7	--	--	--
Unreserved--Undesignated ⁽ⁱ⁾	<u>7,123.5</u>	<u>5,396.8</u>	<u>(4,428.6)</u>	<u>(262.0)</u>	<u>334.4</u>
Fund Balance--End of Period	\$ 9,639.7	\$ 9,017.5	\$ (2,109.8)	\$ 1,409.9	\$ 1,911.2

Footnotes on following page.

SOURCE: Fiscal years 1999-00 to 2001-02: State of California, Office of the State Controller.
Fiscal years 2002-03 and 2003-04: State of California, Department of Finance.

- (a) These statements have been prepared on a budgetary basis in accordance with State law and some modifications would be necessary in order to comply with generally accepted accounting principles ("GAAP"). The Supplementary Information contained in the State's Audited Annual Financial Statements for the year ended June 30, 2003, incorporated by reference in this Appendix A, contains a description of the differences between the budgetary basis and the GAAP basis of accounting and a reconciliation of the June 30, 2002 fund balance between the two methods.
- (b) Estimates are shown net of reimbursements and abatements.
- (c) Estimated as of the 2003-04 May Revision, May 14, 2003.
- (d) Reflects the Administration's proposal to finance the cumulative deficit over several years through the issuance of \$10.7 billion bonds in 2003-04 that would be repaid from a temporary one-half cent sales tax dedicated for that purpose. For accounting purposes, this is shown in 2002-03 to reflect that the accumulated deficit has been eliminated as of the start of fiscal year 2003-04.
- (e) "Transfers to Other Funds" includes the \$6.2 billion General Fund loan to the Department of Water Resources Electric Power Purchase Fund. See "State Finances—Repayment of Energy Loans" and "Current State Budgets" in this Appendix A, above. "Transfers from Other Funds" includes this loan as a receivable in 2000-01. The loan was subsequently repaid with interest as follows: \$116 million in July 2001, \$164 million in October 2002, and \$6.456 billion in November 2002. The loan was reported in the State's Budgetary/Legal Basis Annual Report as an asset of the General Fund and a liability of the Department of Water Resources Electric Power Purchase Fund.
- (f) "Transfer to Other Funds" is included either in the expenditure totals detailed above or as "Transfer from Other Funds."
- (g) For purposes of determining whether the General Fund budget, in any given fiscal year, is in a surplus or deficit condition, Chapter 1238, Statutes of 1990, amended Government Code Section 13307. As part of the amendment, the unencumbered balances of continuing appropriations which exist when no commitment for an expenditure is made should be an item of disclosure, but the amount shall not be deducted from the fund balance. Accordingly, the General Fund condition included in the 2003-04 Governor's Budget includes the unencumbered balances of continuing appropriations as a footnote to the statement (\$1.307 billion in 2001-02, \$270.0 million in 2002-03 and \$174.9 million in 2003-04). However, in accordance with Government Code Section 12460, the State's Budgetary/Legal Basis Annual Report reflects a specific reserve for the encumbered balance for continuing appropriations.
- (h) During 1995, a reserve was established in the General Fund balance for the \$1.7 billion of previously recorded school loans which had been authorized by Chapter 703, Statutes of 1992 and Chapter 66, Statutes of 1993. These loans were repaid from future General Fund appropriations as part of the settlement of litigation. This accounting treatment is consistent with the State's audited financial statements prepared in accordance with GAAP.
- (i) Includes Special Fund for Economic Uncertainties (SFEU). The Department of Finance generally includes in its estimates of the SFEU and set aside reserves, if any, the items reported in the table under "Reserved for Unencumbered Balances of Continuing Appropriations," "Reserved for School Loans," and "Unreserved—Undesignated." The Department of Finance estimates an \$8 million SFEU balance on June 30, 2003, (see footnote (d) above) and projects a \$509 million balance on June 30, 2004, based upon the 2003-04 May Revision submitted on May 14, 2003.

Revenue and Expenditure Assumptions

See "Recent Developments Regarding State Economy and Finances" above.

The table below presents the Department of Finance's budget basis statements of major General Fund revenue sources and expenditures for the 2001-02 fiscal year and the 2003-04 Revision estimate for the 2002-03 fiscal year and the Governor's revised proposal for the 2003-04 fiscal year.

<u>Source</u>	Revenues (Millions)			
	Fiscal Years			
	2001-02^(a) Actual	2002-03^(b) Enacted	2002-03^(c) Revised	2003-04^(e) Proposed
Personal Income Tax.....	\$33,047	\$37,626	\$32,100	\$33,456
Sales and Use Tax.....	21,355	22,958	22,445	23,507
Corporation Tax.....	5,333	7,327	6,664	7,074
Insurance Tax.....	1,596	1,759	1,863	1,918
Deficit Financing Bond ^(d)			10,700	
All Other.....	<u>10,908^(c)</u>	<u>9,488^(f)</u>	<u>7,679^(g)</u>	<u>4,979</u>
Total Revenues and Transfers	<u>\$72,239</u>	<u>\$79,158</u>	<u>\$81,451</u>	<u>\$70,934</u>

<u>Function</u>	Expenditures (Millions)			
	Fiscal Years			
	2001-02^(a) Actual	2002-03^(b) Enacted	2002-03^(c) Revised	2003-04^(c) Proposed
K-12 Education.....	\$29,923	\$30,769	\$29,548	\$29,080
Health and Human Services.....	21,820	21,633	23,456	21,124
Higher Education.....	9,645	9,759	9,543	8,837
Youth and Adult Correctional.....	5,641	5,285	5,833	5,729
Legislative, Judicial and Executive.....	2,612	2,464	2,484	2,428
Tax Relief.....	3,029	4,422	4,639	667
Resources.....	1,382	1,041	1,119	922
State and Consumer Services.....	690	471	480	439
Business, Transportation and Housing.....	639	228	208	426
All Other.....	<u>1,371</u>	<u>650</u>	<u>746</u>	<u>781</u>
Total Expenditures	<u>\$76,752</u>	<u>\$76,722</u>	<u>\$78,056</u>	<u>\$70,433</u>

SOURCE: State of California, Department of Finance. Figures in this table may differ from those shown on page A-30; see "Note" on that page.

(a) Figures for 2001-02, prepared by the Department of Finance, are slightly different than the figures on page A-39, prepared by the State Controller's Office, because of certain differences in accounting methods used by the two offices.

(b) 2002 Budget Act, September 5, 2002.

(c) 2003-04 May Revision, May 14, 2003.

(d) Reflects the Administration's proposal to finance the cumulative deficit over several years through the issuance of \$10.7 billion bonds in 2003-04 that would be repaid from a temporary one-half cent sales tax dedicated for that purpose.

(e) Reflects the repayment of \$6.2 billion in advances (plus interest of \$525 million) made from the general Fund to the Department of Water Resources for the power supply program described under "State Finances – Repayment of Energy Loans." Repayment was made as follows: \$116 million in July 2001, \$164 million in October 2002, and \$6.456 billion in November 2002.

(f) Includes \$4.5 billion for tobacco securitization bond proceeds and about \$2.5 billion in inter-fund loans and transfers.

(g) Includes \$2.5 billion for tobacco securitization bond proceeds and about \$2.8 billion in inter-fund loans and transfers. The Budget Act reflected \$4.5 billion for tobacco securitization bond proceeds; however, the second sale (\$2.0 billion) has been cancelled. See "State Finances—Tobacco Litigation" above.

Economic Assumptions

The revenue and expenditure assumptions set forth have been based upon certain estimates of the performance of the California and national economies in calendar years 2003 and 2004. In the 2003-04 May Revision of the Governor's Budget, the Department of Finance projects that the California economy will grow slowly in 2003 and moderately in 2004.

The California economy has tracked the national economy quite closely in the last year. Both economies have been sluggish. From April 2002 to April 2003, nonfarm payroll employment fell by 0.1 percent in the State and 0.3 percent in the nation. Over that year, state unemployment varied narrowly, never exceeding 6.9 percent or falling below 6.6 percent. The national unemployment rate also was steady but averaged about 0.9 percentage points below the State rate. In addition, homebuilding was strong in both the State and the nation, as were housing markets.

Economic output appears to be growing in both the nation and California. Inflation-adjusted Gross Domestic Product has grown for six consecutive quarters. Statistics on Gross State Product are not as timely as those on (national) Gross Domestic Product, but the U.S. Commerce Department recently estimated that total wages and salaries of California workers, including bonuses and employee stock option income, grew by 2.1 percent from the fourth quarter of 2001 to the fourth quarter of 2002. (From the fourth of 2000 to the fourth quarter of 2001, they fell by 1.6 percent.) In addition, personal state income tax withholdings were up 4.0 percent in the first four months of 2003 from a year earlier. State sales tax revenues also increased over that period.

The annual revision to the State's employment statistics revealed that the California recession was deeper than previously thought, especially in Bay Area high-tech centers. While nonfarm payroll employment fell by 290,000 jobs, or 2.0 percent, in the State between March 2001 and January 2002, it fell by about 105,000 jobs, or 10 percent, in the San Jose metropolitan area and 75,000 jobs, or 7 percent, in the San Francisco metropolitan area. Together, the two metropolitan areas accounted for more than 60 percent of net job loss in the State.

Job growth in Southern California and much of the Central Valley has been better than that in the San Francisco Bay Area. Labor markets in the San Diego and Riverside-San Bernardino metropolitan areas, in particular, have held up better.

The State's travel and tourism industry was recently set back by the war in Iraq and the SARS epidemic. The already-struggling air travel industry was particularly hit hard as travelers worried about being infected by SARS or being a victim of a terrorist attack on an airplane. With its heavy reliance on Asian visitors, San Francisco's tourism industry was especially affected. Small businesses in California's Asian communities have also been hurt. The effects of the war and SARS might well be temporary, however. Travel and tourism appears to have rebounded somewhat with the cessation of major military operations and the ebbing of the SARS epidemic in most affected countries.

Low mortgage rates and doubts about the stock market kept residential real estate markets strong in the first quarter of 2003. The median price of existing homes sold in the State hit a new record high of \$352,780 in March, up more than 15 percent from a year earlier. Sales were off a bit—down 3.2 percent in March and 3.5 percent for the entire first quarter—but still at high levels. However, some expensive real estate markets—Santa Barbara, Santa Clara, and Santa Cruz Counties and the San Francisco metropolitan area—saw sharp drops in sales in March from year-earlier levels.

While few jobs are being created in the State now, growing wages and salaries and personal income tax withholdings suggest that economic output is increasing. Job growth may remain slow for the rest of 2003 before picking up in 2004. Some industries still have too much capacity, dampening prospects for a strong recovery in the near-term. Moreover, if productivity continues to grow as quickly as in the last year, improvement in the labor markets will likely come first in the form of fewer layoffs and longer workweeks for employed workers. Actual employment gains will trail behind, and declines in the unemployment rate will come even later.

Many businesses have cut costs aggressively in the last two years, and a growing number are showing profits. When demand picks up in the economy, profits should grow quickly, and that should lead to more capital spending. In addition, the new federal income tax cuts, signed by the President on May 28, 2003, should stimulate the State economy in the second half of 2003. Furthermore, it is expected that California will continue to track the national economy.

The Department of Finance set out the following estimates for the State's economic performance in calendar years 2003 and 2004, which were used in predicting revenues and expenditures for the May Revision of the 2003-04 Governor's Budget. Also shown is the Department of Finance's previous forecast for the same calendar years, which were contained in the 2003-04 Governor's Budget.

	<u>For Calendar Year 2003</u>		<u>For Calendar Year 2004</u>	
	<u>Governor's Budget^(a)</u>	<u>May Revision^(b)</u>	<u>Governor's Budget^(a)</u>	<u>May Revision^(b)</u>
Non-farm wage and salary employment (000)	14,623	14,608	14,928	14,922
Percent Change	0.7%	0.6%	2.1%	2.1%
Personal income (\$ billions)	\$1,176	\$1,174	\$1,238	\$1,232
Percent Change	3.3%	3.1%	5.3%	4.9%
Housing Permits (Units 000)	157	179	162	174
Consumer Price Index (percent change)	2.8%	2.9%	3.2%	2.4%

(a) 2003-04 Governor's Budget Summary: January 10, 2003.

(b) 2003-04 May Revision: May 14, 2003.

SOURCE: State of California, Department of Finance.

FINANCIAL STATEMENTS

The Audited Annual Financial Statements of the State of California For the Year Ended June 30, 2002 (the "Financial Statements") are available. As of June 30, 2002, the State of California has implemented a new financial reporting model, as required by the Governmental Accounting Standards Board ("GASB") in conformity with accounting principles generally accepted in the United States of America. The GASB sets standards of accounting and financial reporting for state and local governments, which have significantly changed the presentation of the financial statements. The Financial Statements consists of an Independent Auditor's Report, a Management Discussion and Analysis, Basic Financial Statements of the State for the Year Ended June 30, 2002 ("Basic Financial Statements"), and Supplementary Information. Only the Basic Financial Statements have been audited, as described in the Independent Auditor's Report. A description of the new accounting and financial reporting standards is contained in Note 1 of the Basic Financial Statements.

Potential investors may also obtain or review a copy of the Financial Statements from the following sources:

1. By obtaining from any Nationally Recognized Municipal Securities Information Repository, or any other source, a copy of the State of California's Official Statement dated February 13, 2003, relating to the issuance of \$900,000,000 General Obligation Bonds. The Financial Statements are printed in full in such Official Statement. No part of the February 13, 2003 Official Statement is incorporated into this document except the Financial Statements.

2. By accessing the Internet Website of the State Controller (www.sco.ca.gov) and clicking on the icons for California Government--"State and Local," then "State Government," then finding the heading "Publications" and clicking on the icon "Comprehensive Annual Financial Report--Year Ended June 30 2002" in that order or by contacting the Office of the State Controller at (916) 445-2636.

3. By accessing the Internet Website of the State Treasurer (www.treasurer.ca.gov) and clicking on the icons for "Financial Information" and "Audited General Purpose Financial Statements" in that order, or by contacting the Office of the State Treasurer at (800) 900-3873.

The State Controller's unaudited report of cash receipts and disbursements for the period July 1, 2002 through May 31, 2003 is also included as Exhibit 1 to this Appendix A, and is available on the Controller's Website.

Periodic reports on revenues and/or expenditures during the fiscal year are issued by the Administration, the State Controller's Office and the Legislative Analyst's Office. The State Controller issues a monthly report on cash receipts and disbursements recorded on the Controller's records. The Department of Finance issues a monthly Bulletin which reports the most recent revenue receipts as reported by State departments, comparing those receipts to budget projections. The Administration also formally updates its budget projections three times during each fiscal year, in January, May, and at budget enactment. These bulletins and reports are available on the Internet at websites maintained by the agencies and by contacting the agencies at their offices in Sacramento, California. Such bulletins and reports are not part of or incorporated into the Official Statement. Investors are cautioned that interim financial information is not necessarily indicative of results for a fiscal year. Information which may appear in the Official Statement from the Department of Finance concerning monthly receipts of "agency cash" may differ from the State Controller's reports of cash receipts for the same periods because of timing differences in the recording of in-transit items.

OVERVIEW OF STATE GOVERNMENT

Organization of State Government

The State Constitution provides for three separate branches of government: the legislative, the judicial and the executive. The Constitution guarantees the electorate the right to make basic decisions, including amending the Constitution and local government charters. In addition, the State voters may directly influence State government through the initiative, referendum and recall processes.

California's Legislature consists of a forty-member Senate and an eighty-member Assembly. Assembly members are elected for two-year terms, and Senators are elected for four-year terms. Assembly members are limited to three terms in office and Senators to two terms. The Legislature meets almost year round for a two-year session. The Legislature employs the Legislative Analyst, who provides reports on State finances, among other subjects. The Bureau of State Audits, headed by the State Auditor, an independent office since 1993, annually issues an auditor's report based on an examination of the General Purpose Financial Statements of the State Controller, in accordance with generally accepted accounting principles.

The Governor is the chief executive officer of the State and is elected for a four-year term. The Governor presents the annual budget and traditionally presents an annual package of bills constituting a legislative program. In addition to the Governor, State law provides for seven other statewide elected officials in the executive branch. The current elected statewide officials, their party affiliation and the dates on which they were first elected are as follows:

<u>Office</u>	<u>Name</u>	<u>Party Affiliation</u>	<u>First Elected</u>
Governor	Gray Davis	Democrat	1998
Lieutenant Governor	Cruz Bustamante	Democrat	1998
Controller	Steve Westly	Democrat	2002
Treasurer	Philip Angelides	Democrat	1998
Attorney General.....	Bill Lockyer	Democrat	1998
Secretary of State	Kevin Shelley	Democrat	2002
Superintendent of Public Instruction	Jack O'Connell	Democrat	2002
Insurance Commissioner.....	John Garamendi	Democrat	2002

The current term for each office expires in January 2007. Persons elected to statewide offices are limited to two terms in office (eight years) from the dates shown above. (Mr. Garamendi previously served as elected Insurance Commissioner before term limits were enacted.)

The executive branch is principally administered through twelve major agencies and departments: Business, Transportation and Housing Agency, Child Development and Education Agency, Environmental Protection Agency, Department of Finance, Department of Food and Agriculture, Health and Human Services Agency, Labor and Workforce Development Agency (formerly Department of Industrial Relations), Resources Agency, State and Consumer Services Agency, Department of Veterans Affairs, Technology, Trade and Commerce Agency, and Youth and Adult Correctional Agency. In addition, some State programs are administered by boards and commissions, such as The Regents of the University of California, Public Utilities Commission, Franchise Tax Board and California Transportation Commission, which have authority over certain functions of State government with the power to establish policy and promulgate regulations. The appointment of members of boards and commissions is usually shared by the Legislature and the Governor, and often includes ex officio members.

California has a comprehensive system of public higher education comprised of three segments: the University of California, the California State University System and California Community Colleges. The University of California provides undergraduate, graduate and professional degrees to students. Approximately 47,000 degrees were awarded in the 2001-02 school year. About 186,600 full-time students were enrolled at the nine UC campuses and the Hastings College of Law in the 2001-02 school year. The California State University System, provides undergraduate and graduate degrees to students. Approximately 76,000 degrees were awarded in the 2001-02 school year. About 316,400 full-time students were enrolled at the 23 campuses in the 2001-02 school year. The third sector consists of 108 campuses operated by 72 community college districts which provide associate degrees and certificates. Approximately 114,000 associate degrees and certificates were awarded in the 2001-02 school year. About 1.8 million students were enrolled in California's community colleges in the fall of 2002.

Employee Relations

In 2002-03, the State work force is comprised of approximately 327,000 personnel years, of which approximately 119,000 personnel years represent employees of institutions of higher education. Of the remaining 208,000 personnel years, approximately 158,000 are subject to collective bargaining and approximately 50,000 are excluded from collective bargaining. The

California State Employees' Association (CSEA) represents 9 of the 21 collective bargaining units, or approximately 50 percent of those employees subject to collective bargaining.

State law provides that State employees, defined as any civil service employee of the State and teachers under the jurisdiction of the Department of Education or the Superintendent of Public Instruction, and excluding certain other categories, have a right to form, join, and participate in the activities of employee organizations for the purpose of representation on all matters of employer-employee relations. The chosen employee organization has the right to represent its members, except that once an employee organization is recognized as the exclusive representative of a bargaining unit, only that organization may represent employees in that unit.

The scope of representation is limited to wages, hours, and other terms and conditions of employment. Representatives of the Governor are required to meet and confer in good faith and endeavor to reach agreement with the employee organization, and, if agreement is reached, to prepare a memorandum of understanding and present it to the Legislature for ratification. The Governor and the recognized employee organization are authorized to agree mutually on the appointment of a mediator for the purpose of settling any disputes between the parties, or either party could request the Public Employment Relations Board to appoint a mediator.

Memoranda of Understanding for the 21 collective bargaining units will expire as follows: on or before July 2, 2003, for 17 units, on or before July 2, 2004, for one unit, and on or before July 2, 2006, for the three remaining units. The Administration has proposed to reopen negotiations with four of the bargaining units to achieve savings in State personnel costs, as a result of the State's difficult fiscal condition. The State has not experienced a major work stoppage since 1972.

ECONOMY AND POPULATION

Introduction

California's economy, the largest among the 50 states and one of the largest in the world, has major components in high technology, trade, entertainment, agriculture, manufacturing, tourism, construction and services. California's economy slipped into a recession in early 2001, losing about 290,000 jobs between March 2001 and January 2002. The recession was concentrated in the State's high-tech sector and, geographically, in the San Francisco Bay Area. Employment grew by about 79,000 jobs between January 2002 and May 2002 as the State began to recover. The recovery then stalled, however, and since then, the economy has been sluggish, with unemployment varying narrowly between 6.6 percent and 6.9 percent and employment falling by about 38,000 between May 2002 and April 2003. See "Current State Budget—Economic Assumptions."

Population and Labor Force

The State's July 1, 2002 population of over 35 million represented over 12 percent of the total United States population.

California's population is concentrated in metropolitan areas. As of the April 1, 2000 census, 97 percent resided in the 25 Metropolitan Statistical Areas in the State. As of July 1,

2000, the 5-county Los Angeles area accounted for 48 percent of the State's population, with over 16.0 million residents, and the 10-county San Francisco Bay Area represented 21 percent, with a population of over 7.0 million.

The following table shows California's population data for 1994 through 2002.

<u>Year</u>	<u>California Population</u>	<u>% Increase Over Preceding Year</u>	<u>United States Population</u>	<u>% Increase Over Preceding Year</u>	<u>California as % of United States</u>
1994	31,523,080	0.7%	263,125,821	1.2%	12.0
1995	31,711,094	0.6	266,278,393	1.2	11.9
1996	31,962,050	0.8	269,394,284	1.2	11.9
1997	32,451,746	1.5	272,646,925	1.2	11.9
1998	32,861,779	1.3	275,854,104	1.2	11.9
1999	33,417,247	1.7	279,040,168	1.2	12.0
2000	34,036,376	1.9	282,224,348	1.1	12.1
2001	34,698,173	1.9	285,317,559	1.1	12.2
2002	35,301,480	1.7	288,368,698	1.1	12.2

(a) Population as of July 1.

SOURCE: U. S. figures from U.S. Department of Commerce, Bureau of the Census; California figures from State of California, Department of Finance.

The following table presents civilian labor force data for the resident population, age 16 and over, for the years 1993 to 2002.

<u>Year</u>	<u>Labor Force Trends</u>	<u>Labor Force 1993-2002 (Thousands)</u>	<u>Unemployment Rate (%)</u>	
	<u>Labor Force</u>	<u>Employment</u>	<u>California</u>	<u>United States</u>
1993	15,360	13,918	9.4%	6.9%
1994	15,450	14,122	8.6	6.1
1995	15,412	14,203	7.8	5.6
1996	15,520	14,400	7.2	5.4
1997	15,960	14,954	6.3	4.9
1998	16,336	15,367	5.9	4.5
1999	16,596	15,732	5.2	4.2
2000	16,884	16,049	4.9	4.0
2001	17,183	16,260	5.4	4.8
2002	17,405	16,242	6.7	5.8

SOURCE: State of California, Employment Development Department.

Employment, Income, Construction and Export Growth

The following table shows California's non-agricultural employment distribution and growth for 1992 and 2002.

<u>Industry Sector</u>	<u>Employment (Thousands)</u>		<u>% Distribution of Employment</u>	
	<u>1992</u>	<u>2002 p/</u>	<u>1992</u>	<u>2002 p/</u>
Mining	35.4	23.5	0.3%	0.2%
Construction	471.7	759.9	3.9	5.2
<u>Manufacturing</u>				
Nondurable goods	708.4	689.8	5.8	4.7
High Technology	584.4	467.1	4.8	3.2
Other Durable Goods	597.6	659.2	4.9	4.5
Transportation and Utilities	607.4	720.7	5.0	4.9
Wholesale and Retail Trade	2,834.8	3,362.4	23.3	22.9
Finance, Insurance And Real Estate	791.9	847.4	6.5	5.8
Services	3,426.3	4,678.2	28.2	31.9
<u>Government</u>				
Federal	345.9	256.9	2.9	1.7
State and Local	<u>1,749.7</u>	<u>2,193.0</u>	<u>14.4</u>	<u>15.0</u>
TOTAL NON-AGRICULTURAL	<u>12,153.5</u>	<u>14,658.1</u>	<u>100%</u>	<u>100%</u>

p/ Preliminary

SOURCE: State of California, Employment Development Department.

The following tables show California's total and per capita income patterns for selected years.

Total Personal Income in California 1994-2002^(a)

<u>Year</u>	<u>Millions</u>	<u>% Change^(b)</u>	<u>California % of U.S.</u>
1994 ^(c)	\$ 735,104	2.9%	12.5%
1995	771,470	4.9	12.5
1996	812,404	5.3	12.4
1997	861,557	6.1	12.4
1998	931,564	8.1	12.6
1999	994,862	6.8	12.8
2000	1,099,375	10.5	13.1
2001	1,128,256	2.6	13.0
2002 ^(d)	1,138,718	0.9	12.8

(a) BEA's estimates as of September 23, 2002.

(b) Change from prior year.

(c) Reflects Northridge earthquake, which caused an estimated \$15 billion drop in personal income.

(d) Estimated by California Department of Finance.

Note: Omits income for government employees overseas.

SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis (BEA); State of California, Department of Finance.

Per Capita Personal Income 1994-2002^(a)

<u>Year</u>	<u>California</u>	<u>% Change^(b)</u>	<u>United States</u>	<u>% Change^(b)</u>	<u>California% of U.S.</u>
1994 ^(c)	\$23,348	2.3%	\$22,340	3.7%	104.5%
1995	24,339	4.2	23,255	4.1	104.7
1996	25,373	4.2	24,270	4.4	104.5
1997	26,521	4.5	25,412	4.7	104.4
1998	28,240	6.5	26,893	5.8	105.0
1999	29,712	5.2	27,880	3.7	106.6
2000	32,363	8.9	29,760	6.7	108.7
2001	32,655	0.9	30,413	2.2	107.4
2002	32,996	1.0	30,941	1.7	106.6

(a) Latest estimates by BEA. (b) Change from prior year.

(c) Reflects Northridge earthquake, which caused an estimated \$15 billion drop in personal income.

Note: Omits income for government employees overseas.

SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis (BEA).

The following tables show California's residential and non-residential construction.

Residential Construction Authorized by Permits

<u>Year</u>	<u>Units</u>			<u>Valuation^(a) (millions)</u>
	<u>Total</u>	<u>Single</u>	<u>Multiple</u>	
1995	85,293	68,689	16,604	\$13,879
1996	94,283	74,923	19,360	15,289
1997	111,716	84,780	26,936	18,752
1998	125,707	94,298	31,409	21,976
1999	140,137	101,711	38,426	25,783
2000	148,540	105,595	42,945	28,142
2001	148,757	106,902	41,855	28,804
2002 ^{p/}	165,781	122,370	43,411	32,901

(a) Valuation includes additions and alterations.

^{p/} Preliminary

SOURCE: Construction Industry Research Board

Nonresidential Construction
(Thousands of dollars)

<u>Year</u>	<u>Commercial</u>	<u>Industrial</u>	<u>Other</u>	<u>Additions and Alterations</u>	<u>Total</u>
1995	\$2,308,911	\$ 732,874	\$1,050,693	\$4,062,273	\$ 8,154,751
1996	2,751,925	1,140,574	1,152,443	4,539,219	9,584,161
1997	4,271,378	1,598,428	1,378,220	5,021,792	12,269,818
1998	5,419,251	2,466,530	1,782,337	5,307,901	14,976,019
1999	5,706,719	2,256,166	2,350,213	6,269,194	16,582,292
2000	6,962,031	2,206,169	2,204,754	7,252,004	18,624,958
2001	6,195,368	1,552,047	2,584,321	6,421,551	16,753,287
2002 ^{P/}	5,196,958	1,227,754	2,704,530	5,391,901	14,521,143

^{P/} Preliminary

SOURCE: Construction Industry Research Board

The following table shows California's export growth for the period from 1995 through 2002.

Exports Through California Ports
(In millions)

<u>Year</u>	<u>Exports^(a)</u>	<u>% Change</u>
1995	\$116,825.5	22.2%
1996	124,120.0	6.2
1997	131,142.7	5.7
1998	116,282.4	-11.3
1999	122,092.8	5.0
2000	148,554.6	21.7
2001	127,255.3	-14.3
2002	111,340.1	-12.5

(a) "free along ship" Value Basis

SOURCE: U.S. Department of Commerce, Bureau of the Census

LITIGATION

The State is a party to numerous legal proceedings. The following are the most significant pending proceedings, as reported by the Office of the Attorney General. See "Litigation" in the main body of the Official Statement.

Continuing Appropriation Challenge

Howard Jarvis Taxpayers Association et al. v. Kathleen Connell involves a complaint for certain declaratory and injunctive relief challenging the authority of the State Controller to make

payments from the State Treasury in the absence of a State budget. The trial court issued a preliminary injunction that, among other things, prohibited the State Controller from making any payments pursuant to any continuing appropriation. Following an appeal, the Court of Appeal upheld the Controller's authority to make payments pursuant to continuing appropriations in absence of a State budget. Thus the Controller may make payments of principal and interest on State bonds, provided there is a continuing appropriation for such bonds. The Supreme Court granted the Controller's Petition for Review (Case No. S108099, also referred to by the Court as *White v. Davis*) on a procedural issue unrelated to continuing appropriations. On May 1, 2003, the Supreme Court ordered that the Court of Appeal's decision upholding the Controller's authority to make payments pursuant to continuing appropriations during any period when enactment of the annual budget is delayed past June 30, be published thus providing valid legal precedent on this issue. Pursuant to the rules of court, the Supreme Court decision became final on June 2, 2003.

Actions Seeking Flood-Related Damages

In January of 1997, California experienced major flooding with preliminary estimates of property damage of approximately \$1.6 to \$2.0 billion. In *McMahon v. State*, (Sacramento County Superior Court, Case No. 02-AS-06058), a substantial number of plaintiffs have joined suit against the State, local agencies, and private companies and contractors seeking compensation for the damages they suffered as a result of the flooding. A trial date has been scheduled for December 1, 2003. The State is vigorously defending the action.

Paterno v. State of California, is a coordinated action involving 3,000 plaintiffs seeking recovery for damages caused by the Yuba River flood of February 1986. The trial court found liability in inverse condemnation and awarded damages of \$500,000 to a sample of plaintiffs. The State's potential liability to the remaining plaintiffs ranges from \$800 million to \$1.5 billion. In 1992, the State and plaintiffs filed appeals of the decision in the sample plaintiffs' action, and upon remand, plaintiffs' inverse condemnation cause of action was re-tried. The trial court ruled that plaintiffs take nothing from defendants. The outcome of this trial controls with regard to the claims of all other plaintiffs. Plaintiffs filed an appeal with the Court of Appeal (Third Appellate District, Case No. CO40553), and briefing is completed.

Tax Refund Cases The State is involved in the appeal of two refund actions, *California Assn. of Retail Tobacconists (CART), et al. v. Board of Equalization, et al.*, and *Cigarettes Cheaper!, et al. v. Board of Equalization, et al.*, which have been consolidated for appeal as *California Association of Retail Tobacconists v. State of California, Board of Equalization, et al.* (Court of Appeal, Forth Appellate District, Division 1, Case No. D037599), that challenge the constitutionality of Proposition 10, which established the Children and Families Commission ("CFC") and local county commissions and increased the excise tax on tobacco products for the purpose of funding early childhood development programs through the CFC and local commissions. Plaintiffs contend Proposition 10 is unconstitutional under various provisions of the California Constitution, levies an impermissible double tax on certain tobacco products, and violates numerous other provisions of law. There is exposure as to the entire \$750 million per year collected under Proposition 10 together with interest, which could amount to several billion dollars by the time the case is finally resolved. This appeal follows judgment in favor of all

defendants as to all counts, and on June 10, 2003, the Appellate Court affirmed that judgment. It is not known whether plaintiffs will seek Supreme Court review of this decision.

Four pending cases allege that Revenue and Tax Code section 24402, which establishes a corporate tax deduction for dividends received that are based on the amount of the dividend-paying corporation's income subject to California franchise taxes, violates the commerce clause of the United States Constitution. *Microsoft Corporation v. Franchise Tax Board* is pending in the San Francisco County Superior Court (Case No. 400 444). *Montgomery Ward LLC v. Franchise Tax Board* is pending in San Diego Superior Court (Case No. 802767). In *General Motors Corp. v. Franchise Tax Board* (Court of Appeal, Second Appellate District, Division 2, B165665) and *Farmer Brothers Company v. Franchise Tax Board* (Court of Appeal, Second Appellate District, Division 1, B160061), the trial courts determined that Section 24402 violates the commerce clause and the Franchise Tax Board appealed. In *Farmers Brothers*, the Court of Appeal affirmed the trial court decision. A final decision adverse to the State in any of these cases could ultimately result in refunds of approximately \$400 million to similarly situated taxpayers, with an ongoing annual loss of revenue of approximately \$60 million. The State is vigorously litigating these cases.

Five pending cases challenge, as a violation of the due process and commerce clauses of the United States Constitution the Franchise Tax Board's treatment of receipts from investment of cash in short-term financial instruments, and the resulting impact on the apportionment of corporate income allegedly earned outside of California to the corporation's California tax obligation. *The Limited Stores, Inc. v. Franchise Tax Board* is pending in the Third Appellate District of the Court of Appeal (Case No. A012915) and *Toys "R" Us, Inc. v. Franchise Tax Board* is pending in Sacramento County Superior Court (Case No. 01-AS-04316). The other three cases are *Microsoft Corporation v. Franchise Tax Board*, *General Motors Corporation v. Franchise Tax Board*, and *Montgomery Ward LLC v. Franchise Tax Board*, the same cases described above in the discussion of cases challenging Revenue and Tax Code Section 24402. The trial courts in *General Motors* and *The Limited Stores* have ruled in favor of the Franchise Tax Board on this issue, and those decisions have been appealed by the plaintiffs. The trials in *Toys "R" Us, Inc.* and *Microsoft Corporation* are complete and post-trial briefing is underway in both cases. Other taxpayers have raised this same issue in administrative actions. A final decision in favor of any of these plaintiffs could result in tax refunds to similarly situated taxpayers in an amount exceeding \$500 million, with a potential future annual revenue loss of \$50 million. The State is vigorously litigating these cases.

In *Eisenhower Medical Center, et al. v. State Board of Equalization* (San Francisco Superior Court, Case No. 994985), 117 hospitals claim that certain intravenous sets and diagnostic substances are "medicines" within the meaning of the Revenue and Tax Code, and thus are exempt from sales and use taxes. The State Board of Equalization ("SBE") does not consider intravenous sets (other than those used primarily for feeding) and diagnostic substances to be medicines and, therefore, those items are subject to sales and use taxes. The trial court ruled in favor of the SBE, and an appeal is expected. Due to a retroactive regulatory change that the SBE adopted during the pendency of this case, specified types of enteral feeding supplies are now exempt from sales and use taxes. Therefore, even if the State prevails on appeal, refunds will be required in the amount of approximately \$10 million. Should the plaintiffs ultimately prevail on all contested issues, estimated refunds to plaintiffs and others similarly situated

hospitals would total approximately \$400 million and estimated future revenue loss would be \$70 million per year.

In *County of Orange v. Bezaire, et al.*, (Court of Appeal, Fourth Appellate District, Division 3, Case No. G032412), the County has appealed a trial court judgment that the Orange County assessor's office received property taxes from two taxpayers in excess of the amounts collectable under Article XIII A of the California Constitution (sometimes referred to as "Proposition 13"). The legal claim in this class action lawsuit focuses on the constitutionality of the practice of the Orange County assessor's office to increase or "recapture" the assessed values of real properties that temporarily decline and then increase in value. The trial court's judgment will bind only the County of Orange and its assessor's office, however, the effects of a final determination by an appellate court that the contested assessment practices are contrary to Proposition 13 could result in an increase in the State general fund component of the financing guarantee to public schools established by Proposition 98 (see "State Finances – Proposition 98" above) in an amount in excess of several billion dollars.

Tobacco Settlement Revenue Challenges

In *FORCES Action Project et al. v. State of California et al.* (U.S. Court of Appeals for the Ninth Circuit, Case No. 02-15336), various smokers' rights groups challenge the 1998 Master Settlement Agreement (the "MSA") as it pertains to California, Utah and the City and County of San Francisco. Plaintiffs assert a variety of constitutional challenges, including that the settlement represents an unlawful tax on smokers. The federal district court dismissed the complaint for lack of subject matter jurisdiction because the plaintiffs lacked standing to sue, and also concluded that the plaintiffs' claims against the State and its officials are barred by the 11th Amendment. The 9th Circuit Court of Appeals affirmed the district court's dismissal of plaintiffs' claims, and following remand, and again following a petition for rehearing, affirmed the district court's denial of plaintiffs' motion for leave to amend their complaint. It is not yet known whether the plaintiffs will seek review by the Supreme Court.

In *Grand River Enterprises Six Nations, Ltd., et al. v. Lockyer et al.* (U.S. District Court, S.D. New York, Case No. 02 CIV 5068 JFK), six cigarette manufacturers sued the Attorneys General of 31 states, challenging (1) the States' escrow statutes, which require tobacco product manufacturers that did not participate in the MSA and certain other tobacco product manufacturers to pay money into escrow accounts and (2) several states' complementary contraband statutes, which make it illegal for distributors to sell cigarettes made by the nonparticipating tobacco product manufacturers which have not made their required deposits into escrow. Plaintiffs claim that these statutes violate the 1st and 14th amendments of the United States Constitution, as well as the commerce clause, and federal antitrust laws. They seek a permanent injunction against implementation and enforcement of these statutes. "Diligent enforcement" of the escrow deposit statute protects the State from reductions in MSA payments from participating manufacturers who lose market share to nonparticipating manufacturers. The Attorneys General of 30 of the states, including California, are coordinating the defense of this case through the National Association of Attorneys General Tobacco Project. The participating Attorneys General moved to dismiss the case for lack of personal jurisdiction over the out-of-state Attorneys General and, alternatively, for failure to state a claim on which relief can be

granted. Oral argument was heard on March 13, 2003. The matter has been taken under submission.

Environmental Cleanup Matter

In a federal Environmental Protection Agency (“U.S. EPA”) administrative abatement action entitled *In the Matter of: Leviathan Mine, Alpine County, California, Regional Water Quality Control Board, Lahontan Region, State of California* (U.S. EPA Region IX CERCLA Docket No. 00-16(a)), the State, as owner of the Leviathan Mine, is a party though the Lahontan Regional Water Quality Control Board (“Board”), which is the State entity responsible for performing certain environmental remediation at the Leviathan Mine site. Also a party is ARCO, the successor in interest to the mining company that caused certain pollution of the mine site. The Leviathan Mine site is listed on the U.S. EPA “Superfund” List, and both remediation costs and costs for Natural Resource Damages may be imposed on the State. The Board has undertaken certain remedial action at the mine site, but the U.S. EPA’s decision on the interim and final remedies are pending. ARCO has filed several state law claims against the State with the California Victim Compensation and Government Claims Board (an administrative agency with which certain claims must be filed as a prerequisite to litigation seeking damages against the State which was formerly named the Board of Control, the “Government Claims Board”), but litigation on these claims have been tolled by agreement of the parties until at least October, 2004. It is possible these matters could result in a potential loss to the State in excess of \$400 million.

Energy-Related Matters

In *People v. ACN Energy, Inc., et al.* (Sacramento County Superior Court, Case No. 01AS05497), the court is considering whether and to what extent compensation is due to market participants which have claimed compensation as a result of the Governor’s issuance of executive orders, under the California Emergency Service Act, “commandeering” power purchase arrangements held by Pacific Gas & Electric Company (“PG&E”) and Southern California Edison (“SCE”), referred to as “block forward contracts”. In this action the State seeks a declaration that the State is not liable for damages as a result of these orders, nor for compensation for inverse condemnation, and that any damages suffered by any of the defendants is offset by payments made by the Department of Water Resources for electricity received under the “commandeered” “block forward contracts”. Complaints and cross-complaints for inverse condemnation, recovery under the Emergency Services Act and other causes of action brought by PG&E, Reliant Energy Services, Dynegy Power Marketing, Williams Energy Services, Sempra Energy Trading, the California Power Exchange, Mirant Americas Energy, Duke Energy Trading and Marketing, and numerous other market participants have been joined with the declaratory relief action in Judicial Council Coordination Proceeding No. 4203, in Sacramento County Superior Court. In an administrative proceeding action before the Government Claims Board (which was dismissed on procedural grounds), the California Power Exchange stated claims for “commandeering” the “block forward contracts” in the amount of approximately \$1 billion.

In *Pacific Gas and Electric Company v. The State of California* (Sacramento County Superior Court, Case No. 02A505360), PG&E filed a complaint for breach of contract alleging

that statutes enacted in 1996 as part of the restructuring of the electric power industry in California ("AB 1890") established a "regulatory contract" between the State and PG&E that authorized PG&E to sell the output of its retained generation facilities in interstate power markets at prices regulated by FERC and to sell the facilities themselves, and that by amending AB 1890 in 2001, the State deprived PG&E of the right to such sales and thereby breached that "regulatory contract". PG&E's complaint seeks damages in an amount to be proven, but in an administrative proceeding before the Government Claims Board, in which PG&E's claims were denied, PG&E sought damages of at least \$4.3 billion to compensate for the losses alleged in this action. In January 2002, the court sustained the demurrer of the State without leave to amend, dismissing the lawsuit. Plaintiffs have filed a notice of appeal in this matter.

In a government claim filed on February 21, 2003, with the Government Claims Board, Allegheny Energy Supply Company, LLC ("Allegheny") and Allegheny Trading Finance Company ("ATFC") seek recovery from the State of California and various State departments and agencies in an amount exceeding \$5 billion. The government claim arises out of a contract entered into between the California Department of Water Resources ("DWR") and Allegheny, which Allegheny subsequently assigned to ATFC. Claimants allege that challenges filed with the Federal Energy Regulatory Commission ("FERC") by the California Electricity Oversight Board and the California Public Utilities Commission, seeking to have the contract reformed or abrogated under the Federal Power Act, constitute a breach of the contract by DWR. Claimants also allege that those FERC actions, and other public statements and actions by State and DWR employees and agents pertaining to attempts by the State and DWR to renegotiate the contract, caused Allegheny to be unable to securitize future payments under the contract, and otherwise caused Allegheny's credit rating, and the credit rating of Allegheny's parent company, Allegheny Energy, Inc., to be reduced. Claimants' specific claims are for breach of contract, tortious interference in prospective business advantage, conspiracy to tortiously interfere in prospective business advantage, fraud and negligent misrepresentation. The Government Claims Board rejected the contract claims as complex, and returned the tort claims as untimely filed. In a related proceeding, DWR filed a complaint in Sacramento Superior Court against Allegheny on January 29, 2003, seeking declaratory relief that the contract is void (Case No. 03AS00488).

Escheated Property Claims

In five pending cases, plaintiffs claim that the State Controller has a constitutional and statutory duty to give notice prior to the time the Controller sells property that has escheated to the State (in these cases, shares of stock): *Fong v. Connell* (Court of Appeal, Third District, Case No. C042007); *Harris v. Connell* (Court of Appeal, Second District, Case No. B160741); *Lusby-Taylor v. Connell* (U.S. Court of Appeals for the Ninth Circuit, Case No. 02-16511); *Orfield v. Connell* (Los Angeles County Superior Court, Case No. BC288429); and *Suever v. Connell* (United States District Court, Northern District, Case No. C03-001556). The plaintiffs also claim that the Controller failed to comply with statutory notice requirements when it first received property that had escheated to the State. The plaintiffs seek damages, which the *Fong* plaintiffs have articulated as being in the amount of the difference between the amount they were paid for the stock upon its sale, and either the current value of the stock or the highest market value of the stock between the date the Controller sold the stock and the present. All of these cases, except *Fong* are styled as class actions, though in *Lusby-Taylor* and *Harris*, that issue was not determined prior to the trial court decisions that are being appealed. In *Fong*, the trial court

denied plaintiffs' request for leave to amend their complaint to add class allegations, but the issue has been raised on appeal. If one or more of these cases are successful as a class action and the class ultimately prevails on the merits, damages for the class could be in excess of \$500 million. The State has prevailed at the trial court in *Fong*, *Harris* and *Lusby-Taylor*. Both *Suever* and *Orfield* are in the early stages of litigation in the trial court. The State is vigorously defending all of these actions.

Action Seeking Damages for Alleged Violations of Privacy Rights

In *Gail Marie Harrington-Wisely, et al. v. State of California, et al.*, (Los Angeles County Superior Court, Case No. BC 227373), a proposed class action, plaintiffs seek damages for alleged violations of prison visitors' rights resulting from the Department of Corrections' use of a body imaging machine to search visitors entering state prisons for contraband. If this action is certified as a class action, and a court were to award damages pursuant to the California Civil Code for every use of the body imaging machine, damages could be as high as \$3 billion. The State is vigorously defending this action.

Actions Seeking Program Modifications

In the following cases, plaintiffs seek court orders or judgments that would require the State to modify existing programs and, except as specified, do not seek monetary damages. Nevertheless, a judgment against the State in any one of these cases could require changes in the challenged program that could result in increased programmatic costs to the State in a future fiscal year in excess of \$400 million. Alternatively, in some circumstances, it may be possible that a judgment against the State could be addressed by legislative changes to the program that would cost less.

In *Williams, et al., v. State of California, et al.*, (San Francisco County Superior Court, Case No. 312236), a class action for declaratory relief and injunction brought by public school students against the State, the Board of Education, and Department of Education and the Superintendent of Public Instruction, the class alleges inadequacies in the public education system and seeks a variety of programmatic changes to the system. The State is vigorously defending this action. Trial is set for August 2004.

In *Natural Resources Defense Council et al., v. California Department of Transportation et al.*, (United States District Court, Central District, Case No. 93-6073-ER- (JRX)), plaintiffs obtained an injunction requiring the Department of Transportation (the "Department") to comply with National Pollution Discharge Elimination System ("NPDES") requirements under the federal Clean Water Act ("Act") in connection with storm water discharges from State highways and construction sites in an area that includes most of Los Angeles and Ventura Counties. There is an established dispute resolution procedure intended to resolve disputes without a return to federal court. Subsequent modifications of the injunction have provided for, among other things, studies of pilot projects to address control of the sources of storm water pollution and the performance of studies of pilot projects to retrofit highways with storm water pollution control facilities. There has been no agreement regarding what measures arising out of the pilot projects and studies will be implemented. Plaintiffs' position is that the Department should be required to retrofit its facilities to treat storm water, regardless of whether any construction is otherwise

planned in any given area. For planning purposes, the Department is including an additional 3 percent in the cost of future statewide construction and maintenance projects to pay for compliance measures. This 3 percent increase amounts to \$500 million through fiscal year 2006–07. While the impact of a judgment of the scope sought by plaintiffs is difficult to determine, it is possible that a judgment that would require the State to retrofit all its highway facilities throughout the State could cost billions of dollars.

The following three cases seek reforms to State programs for the treatment of institutionalized disabled persons. Some rough estimates suggest the financial impact of a judgment against the State defendants in any of these cases could be as high as \$1 billion per year in programmatic costs going forward. The State is vigorously defending these actions.

In *Charles Davis, et al. v. California Health and Human Services Agency, et al.*, (United States District Court – Northern District, Case No. C00-2532 SBA), the plaintiffs brought a class action under a number of federal acts, including the ADA, seeking declaratory and injunctive relief. Plaintiffs allege that disabled persons institutionalized at San Francisco’s Laguna Honda Hospital, a 1,200 bed skilled nursing facility, who require long term care should be assessed as to whether they can be treated at home or in community-based facilities, and then provided appropriate care.

In *Stephen Sanchez, et al. v. Grantland Johnson, et al.*, (United States District Court – Northern District, Case No. C-00-01593 CW), the plaintiffs have brought a class action seeking declaratory and injunctive relief, alleging, in part, that provider rates for community-based services for developmentally disabled individuals are discriminatory under the ADA, and violate the Social Security Act, Civil Rights Act and the Rehabilitation Act, because they result in unnecessary institutionalization of developmentally disabled persons.

In *Capitol People First v. Department of Developmental Services* (Alameda County Superior Court, Case No. 2002-038715) a consortium of state and national law firms and public-interest groups brought suit against the Departments of Finance, California Department of Developmental Services and California Department of Health Services, alleging violations of the Lanterman Act, the ADA, and section 504 of the Rehabilitation Act by defendants needlessly isolate thousands of people with developmental disabilities in large facilities. The case seeks sweeping reforms, including requiring the State to offer a full range of community-based services.

STATE DEBT TABLES

The tables which follow provide information on outstanding State debt, authorized but unissued general obligation bonds and commercial paper notes, debt service requirements for State general obligation and lease-purchase bonds, and authorized and outstanding State revenue bonds. For purposes of these tables, “General Fund bonds,” also known as “non-self liquidating bonds,” are general obligation bonds expected to be paid from the General Fund without reimbursement from any other fund. Although the principal of general obligation commercial paper notes in the “non-self liquidating” category is legally payable from the General Fund, the State expects that principal of such commercial paper notes will be paid only from the issuance of new commercial paper notes or the issuance of long-term general obligation bonds to retire

the commercial paper notes. Interest on “non-self liquidating” general obligation commercial paper notes is payable from the General Fund.

“Enterprise Fund bonds,” also known as “self liquidating bonds,” are general obligation bonds for which program revenues are expected to be sufficient to reimburse in full the General Fund for debt service payments, but any failure to make such a reimbursement does not affect the obligation of the State to pay principal and interest on the bonds from the General Fund.

As of June 18, 2003, the total amount of General Obligation Commercial Paper Notes outstanding was \$821,965,000. All of the outstanding commercial paper notes are planned to be retired from the proceeds of the sale of long-term general obligation bonds in June 2003.

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS

As of May 1, 2003
(Thousands)

	Voter Authorization		Bonds Outstanding (a)	CP Program Authorized (b)	Unissued (c)
	Date	Amount			
GENERAL FUND BONDS (Non-Self Liquidating)					
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Act of 2002.....	3/5/2002	\$ 2,600,000	\$ 0	\$ 262,640	\$ 2,337,360
California Library Construction and Renovation Bond Act of 1988.....	11/8/1988	75,000	47,545	0	2,595
California Library Construction and Renovation Bond Act of 2000.....	3/7/2000	350,000	490	52,300	297,200
California Park and Recreational Facilities Act of 1984.....	6/5/1984	370,000	134,940	n.a.	1,100
California Parklands Act of 1980.....	11/4/1980	285,000	32,465	n.a.	0
California Safe Drinking Water Bond Law of 1976.....	6/8/1976	175,000	41,475	n.a.	2,500
California Safe Drinking Water Bond Law of 1984.....	11/6/1984	75,000	25,850	n.a.	0
California Safe Drinking Water Bond Law of 1986.....	11/4/1986	100,000	60,795	n.a.	0
California Safe Drinking Water Bond Law of 1988.....	11/8/1988	75,000	47,955	6,265	0
California Wildlife, Coastal, and Park Land Conservation Act of 1988.....	6/7/1988	776,000	422,475	n.a.	2,000
Class Size Reduction Public Education Facilities Bond Act of 1998 (HI Ed).....	11/3/1998	2,500,000	1,693,870	514,305	7,350
Class Size Reduction Public Education Facilities Bond Act of 1998 (K-12).....	11/3/1998	6,700,000	5,953,945	506,300	263,000
Clean Air and Transportation Improvement Bond Act of 1990.....	6/5/1990	1,990,000	1,257,030	297,300	0
Clean Water and Water Conservation Bond Law of 1978.....	6/6/1978	375,000	35,805	n.a.	40,925
Clean Water and Water Reclamation Bond Law of 1988.....	11/8/1988	65,000	46,130	0	0
Clean Water Bond Law of 1970.....	11/3/1970	250,000	4,000	n.a.	0
Clean Water Bond Law of 1974.....	6/4/1974	250,000	8,695	n.a.	0
Clean Water Bond Law of 1984.....	11/6/1984	325,000	81,855	n.a.	0
Community Parklands Act of 1986.....	6/3/1986	100,000	42,180	n.a.	0
County Correctional Facility Capital Expenditure and Youth Facility Bond Act of 1988.....	11/8/1988	500,000	299,915	0	0
County Correctional Facility Capital Expenditure Bond Act of 1986.....	6/3/1986	495,000	218,255	n.a.	0
County Jail Capital Expenditure Bond Act of 1981.....	11/2/1982	280,000	60,450	n.a.	0
County Jail Capital Expenditure Bond Act of 1984.....	6/5/1984	250,000	51,150	n.a.	0
Earthquake Safety and Public Buildings Rehabilitation Bond Act of 1990.....	6/5/1990	300,000	197,895	70,000	0
Fish and Wildlife Habitat Enhancement Act of 1984.....	6/5/1984	85,000	26,115	n.a.	3,000
Hazardous Substance Cleanup Bond Act of 1984.....	11/6/1984	100,000	7,500	n.a.	0
Higher Education Facilities Bond Act of 1986.....	11/4/1986	400,000	133,150	n.a.	0
Higher Education Facilities Bond Act of 1988.....	11/8/1988	600,000	293,145	3,805	7,000
Higher Education Facilities Bond Act of June 1990.....	6/5/1990	450,000	249,120	5,000	0
Higher Education Facilities Bond Act of June 1992.....	6/2/1992	900,000	649,690	8,840	270
Housing and Emergency Shelter Trust Fund Act of 2002.....	11/5/2002	2,100,000	0	980,000	1,120,000
Housing and Homeless Bond Act of 1990.....	6/5/1990	150,000	6,440	n.a.	0
Kindergarten - University Public Education Facilities Bond Act of 2002 (K-12).....	11/5/2002	11,400,000	3,502,000	7,898,000	0
Kindergarten - University Public Education Facilities Bond Act of 2002 (HI-Ed).....	11/5/2002	1,650,000	0	282,000	1,368,000
Lake Tahoe Acquisitions Bond Act.....	8/2/1982	85,000	28,995	n.a.	0

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS
(Continued)

	Voter Authorization		Bonds		CP Program	
	Date	Amount	Outstanding (a)	Authorized (b)	Unissued (c)	
New Prison Construction Bond Act of 1981.....	6/8/1982	\$ 495,000	\$ 49,250	\$	\$	
New Prison Construction Bond Act of 1984.....	6/5/1984	300,000	37,500	n.a.	0	
New Prison Construction Bond Act of 1986.....	11/4/1986	500,000	178,480	n.a.	1,500	
New Prison Construction Bond Act of 1988.....	11/8/1988	817,000	399,895	0	12,260	
New Prison Construction Bond Act of 1990.....	6/5/1990	450,000	234,410	8,100	0	
Passenger Rail and Clean Air Bond Act of 1990.....	6/5/1990	1,000,000	583,565	13,900	0	
Public Education Facilities Bond Act of 1996 (K-12).....	3/26/1996	2,025,000	1,685,040	67,535	0	
Public Education Facilities Bond Act of 1996 (Hi-Ed).....	3/26/1996	975,000	867,560	30,950	8,700	
1988 School Facilities Bond Act.....	11/8/1988	800,000	413,445	7,000	0	
1990 School Facilities Bond Act.....	6/5/1990	800,000	440,145	3,745	0	
1992 School Facilities Bond Act.....	11/3/1992	900,000	585,587	8,094	0	
Safe, Clean Reliable Water Supply Act of 1996.....	11/5/1996	995,000	443,755	314,200	211,800	
Safe Drinking Water Bond Act of 2000.....	3/7/2000	1,970,000	294,000	817,200	856,800	
Safe Neighborhood Parks Bond Act of 2000.....	3/7/2000	2,100,000	660,730	311,415	1,117,000	
School Building and Earthquake Bond Act of 1974.....	11/5/1974	40,000	31,990	n.a.	0	
School Facilities Bond Act of 1988.....	6/7/1988	800,000	369,730	n.a.	0	
School Facilities Bond Act of 1990.....	11/6/1990	800,000	475,160	3,500	0	
School Facilities Bond Act of 1992.....	6/2/1992	1,900,000	1,187,830	20,400	0	
Seismic Retrofit Bond Act of 1996.....	3/26/1996	2,000,000	1,586,120	289,645	0	
Senior Center Bond Act of 1984.....	11/6/1984	50,000	9,750	n.a.	0	
State Beach, Park, Recreational and Historical Facilities Bonds.....	6/4/1974	250,000	495	n.a.	0	
State School Building Lease-Purchase Bond Law of 1982.....	11/2/1982	500,000	33,005	n.a.	0	
State School Building Lease-Purchase Bond Law of 1984.....	11/6/1984	450,000	120,250	n.a.	0	
State School Building Lease-Purchase Bond Law of 1986.....	11/4/1986	800,000	290,900	n.a.	0	
State, Urban, and Coastal Park Bond Act of 1976.....	11/2/1976	280,000	14,870	n.a.	0	
Veterans' Homes Bond Act of 2000.....	3/7/2000	50,000	0	45,000	5,000	
Voting Modernization Bond Act of 2002.....	3/5/2002	200,000	0	155,000	45,000	
Water Conservation and Water Quality Bond Law of 1986.....	6/3/1986	150,000	70,210	n.a.	27,600	
Water Conservation Bond Law of 1988.....	11/8/1988	60,000	32,915	10,701	5,234	
Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002.....	11/5/2002	3,440,000	72,000	143,000	3,225,000	
Total General Fund Bonds.....		\$ 63,078,000	\$ 26,829,907	\$ 13,136,140	\$ 10,968,174	
ENTERPRISE FUND BONDS (Self Liquidating)						
California Water Resources Development Bond Act of 1959.....	11/8/1960	\$ 1,750,000	\$ 827,090	\$	\$ 167,600	
Veterans Bonds.....	(d)	4,510,000	1,979,685	0	605,585	
Total Enterprise Fund Bonds.....		\$ 6,260,000	\$ 2,806,775	\$ 0	\$ 773,185	
TOTAL GENERAL OBLIGATION BONDS.....		\$ 69,338,000	\$ 29,636,682	\$ 13,136,140	\$ 11,741,359	

(a) Includes the initial value of capital appreciation bonds rather than the accreted value.
(b) Represents the total amount of commercial paper authorized by Finance Committees that could be issued for new money projects. Of this amount, no more than \$2 billion of commercial paper can be issued at any time. Currently, there is \$148,965,000 of commercial paper issued and outstanding. The bond acts marked as "n.a." are not legally permitted to utilize commercial paper, or all bonds were issued before the commercial paper program began.
(c) Treats full commercial paper authorization as issued; see footnote (b).
(d) Various dates.

SOURCE: State of California, Office of the Treasurer.

OUTSTANDING STATE DEBT
FISCAL YEARS 1997-98 THROUGH 2001-02
(Dollars in Thousands Except for Per Capita Information)

	<u>1997-98</u>	<u>1998-99</u>	<u>1999-00</u>	<u>2000-01</u>	<u>2001-02</u>
Outstanding Debt (a)					
General Obligation Bonds					
General Fund (Non-Self Liquidating).....	\$ 14,932,766	\$ 16,202,211	\$ 17,869,616	\$ 20,472,893	\$ 22,115,362
Enterprise Fund (Self Liquidating).....	3,906,950	3,674,020	3,474,900	3,396,215	3,211,310
Total.....	\$ 18,839,716	\$ 19,876,231	\$ 21,344,516	\$ 23,869,108	\$ 25,326,672
Lease-Purchase Debt.....	6,639,620	6,671,534	6,627,944	6,413,260	6,341,935
Total Outstanding General Obligation Bonds and Lease-Purchase Debt.....	\$ 25,479,336	\$ 26,547,765	\$ 27,972,460	\$ 30,282,368	\$ 31,668,607
Bond Sales During Fiscal Year					
Non-Self Liquidating General Obligation Bonds...	\$ 1,667,820	\$ 2,294,650	\$ 2,750,000	\$ 4,419,665	\$ 3,905,025
Self Liquidating General Obligation Bonds.....	447,535	80,000	126,500	358,625	111,325
Lease-Purchase Debt.....	\$ 1,245,190	\$ 456,410	\$ 293,235	\$ 214,585	\$ 229,105
Debt Service (b)					
Non-Self Liquidating General Obligation Bonds...	\$ 1,878,026	\$ 1,934,628	\$ 2,045,566	\$ 2,279,636	\$ 2,367,570
Lease-Purchase Debt.....	\$ 577,987	\$ 652,131	\$ 654,485	\$ 670,228	\$ 647,568
General Fund Receipts (b)					
Non-Self Liquidating General Obligation Bonds Debt Service as a Percentage of General Fund Receipts.....	3.40%	3.31%	2.83%	2.91%	3.55%
Lease-Purchase Debt Service as a Percentage of General Fund Receipts.....	1.05%	1.11%	0.91%	0.86%	0.97%
Population (c)					
Non-Self Liquidating General Obligation Bonds Outstanding Per Capita.....	\$ 460.15	\$ 493.04	\$ 534.74	\$ 601.44	\$ 636.79
Lease-Purchase Debt Outstanding Per Capita.....	\$ 204.60	\$ 203.02	\$ 198.34	\$ 188.41	\$ 182.61
Personal Income (d)					
Non-Self Liquidating General Obligation Bonds Outstanding as Percentage of Personal Income....	1.73%	1.74%	1.79%	1.87%	1.98%
Lease-Purchase Debt Outstanding as Percentage of Personal Income.....	0.77%	0.72%	0.66%	0.59%	0.57%

(a) As of last day of fiscal year. Includes the initial value of capital appreciation bonds rather than the accreted value.

(b) Calculated on a cash basis; debt service costs of bonds issued in any fiscal year largely appear in subsequent fiscal year.

(c) As of July 1, the beginning of the fiscal year.

(d) Annual Totals: US BEA, revised 1997-2000; DOF Estimated 2001.

California Department of Finance.

SOURCES: Population: State of California, Department of Finance

Personal Income: State of California, Department of Finance; United States, Department of Commerce, Bureau of Economic Analy.

Outstanding Debt, Bonds Sales During Fiscal Year and Debt Service: State of California, Office of the Treasurer.

General Fund Receipts: State of California, Office of the State Controller.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR GENERAL FUND GENERAL OBLIGATION BONDS (a) (d)
(Non-Self Liquidating)
As of May 1, 2003**

Fiscal Year Ending June 30	Current Debt		
	Interest	Principal (b)	Total
2003.....	\$ 82,819,030.90	\$ 71,280,000.00	\$ 154,099,030.90 (c)
2004.....	1,326,899,996.59	1,330,800,000.00	2,657,699,996.59
2005.....	1,273,690,880.09	1,244,789,388.71	2,518,480,268.80
2006.....	1,199,736,682.50	1,173,910,000.00	2,373,646,682.50
2007.....	1,130,766,248.43	1,204,445,000.00	2,335,211,248.43
2008.....	1,065,131,625.43	1,276,788,078.31	2,341,919,703.74
2009.....	993,197,851.25	1,282,835,000.00	2,276,032,851.25
2010.....	920,714,500.56	1,328,295,000.00	2,249,009,500.56
2011.....	848,797,993.59	1,297,369,045.16	2,146,167,038.75
2012.....	774,127,895.05	950,470,000.00	1,724,597,895.05
2013.....	724,561,846.25	819,030,000.00	1,543,591,846.25
2014.....	684,041,585.89	694,185,000.00	1,378,226,585.89
2015.....	649,870,982.19	706,490,000.00	1,356,360,982.19
2016.....	612,705,380.21	636,410,000.00	1,249,115,380.21
2017.....	578,201,530.85	666,180,000.00	1,244,381,530.85
2018.....	543,644,612.23	682,480,000.00	1,226,124,612.23
2019.....	507,771,892.25	725,995,000.00	1,233,766,892.25
2020.....	470,016,511.00	749,920,000.00	1,219,936,511.00
2021.....	432,186,624.75	695,450,000.00	1,127,636,624.75
2022.....	396,363,433.50	828,320,000.00	1,224,683,433.50
2023.....	352,707,532.70	820,675,000.00	1,173,382,532.70
2024.....	312,011,567.84	762,860,000.00	1,074,871,567.84
2025.....	273,513,209.08	737,385,000.00	1,010,898,209.08
2026.....	236,129,306.34	717,740,000.00	953,869,306.34
2027.....	199,272,012.59	730,815,000.00	930,087,012.59
2028.....	162,130,604.09	709,675,000.00	871,805,604.09
2029.....	126,728,090.00	741,745,000.00	868,473,090.00
2030.....	89,074,895.75	790,170,000.00	879,244,895.75
2031.....	49,442,704.50	495,740,000.00	545,182,704.50
2032.....	26,194,945.00	366,890,000.00	393,084,945.00
2033.....	8,419,287.50	190,770,000.00	199,189,287.50
Total	\$ 17,050,871,258.90	\$ 25,429,906,512.18	\$ 42,480,777,771.08

(a) Does not include commercial paper outstanding.

(b) Includes scheduled mandatory sinking fund payments as well as serial maturities.

(c) Total represents the debt service requirements on June 1, 2003.

(d) Does not include debt service payments on \$1,400,000,000 State of California General Obligation Variable Rate Bonds due 2033.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR ENTERPRISE FUND GENERAL OBLIGATION BONDS(a)
(Self Liquidating)
As of May 1, 2003**

Fiscal Year Ending <u>June 30</u>	Current Debt		
	<u>Interest</u>	<u>Principal (b)</u>	<u>Total</u>
2003.....	\$ 43,379,977.86	\$ 5,000,000.00	\$ 48,379,977.86 (c)
2004.....	157,752,380.00	116,875,000.00	274,627,380.00
2005.....	149,284,837.25	131,840,000.00	281,124,837.25
2006.....	139,887,998.50	144,455,000.00	284,342,998.50
2007.....	129,362,629.76	176,545,000.00	305,907,629.76
2008.....	117,220,702.29	187,905,000.00	305,125,702.29
2009.....	105,132,351.25	178,725,000.00	283,857,351.25
2010.....	93,545,886.55	168,695,000.00	262,240,886.55
2011.....	83,950,470.77	126,905,000.00	210,855,470.77
2012.....	76,437,886.00	169,860,000.00	246,297,886.00
2013.....	68,092,160.62	171,035,000.00	239,127,160.62
2014.....	60,721,567.25	136,035,000.00	196,756,567.25
2015.....	54,714,273.15	118,935,000.00	173,649,273.15
2016.....	48,788,367.00	122,130,000.00	170,918,367.00
2017.....	42,549,819.39	130,125,000.00	172,674,819.39
2018.....	36,508,729.09	105,235,000.00	141,743,729.09
2019.....	31,151,899.21	101,050,000.00	132,201,899.21
2020.....	26,763,528.05	66,260,000.00	93,023,528.05
2021.....	23,192,791.29	60,385,000.00	83,577,791.29
2022.....	19,895,027.39	56,870,000.00	76,765,027.39
2023.....	17,273,135.76	38,275,000.00	55,548,135.76
2024.....	15,128,625.52	40,535,000.00	55,663,625.52
2025.....	12,831,771.91	43,880,000.00	56,711,771.91
2026.....	10,584,088.75	38,415,000.00	48,999,088.75
2027.....	8,956,152.50	20,745,000.00	29,701,152.50
2028.....	7,987,927.50	14,315,000.00	22,302,927.50
2029.....	6,890,681.25	25,420,000.00	32,310,681.25
2030.....	5,404,392.50	28,100,000.00	33,504,392.50
2031.....	3,892,867.50	25,920,000.00	29,812,867.50
2032.....	2,395,225.00	27,375,000.00	29,770,225.00
2033.....	812,977.50	28,930,000.00	29,742,977.50
Total	\$ 1,600,491,128.36	\$ 2,806,775,000.00	\$ 4,407,266,128.36

(a) Does not include commercial paper outstanding.

(b) Includes scheduled mandatory sinking fund payments as well as serial maturities.

(c) Total represents the debt service requirements on June 1, 2003.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR LEASE-PURCHASE DEBT
As of May 1, 2003**

Fiscal Year Ending <u>June 30</u>	Current Debt		
	<u>Interest</u>	<u>Principal (a)</u>	<u>Total</u>
2003.....	\$ 78,756,706.00	\$ 29,535,000.00	\$ 108,291,706.00 (b)
2004.....	354,163,513.22	326,516,386.24	680,679,899.46
2005.....	339,130,734.05	352,219,507.20	691,350,241.25
2006.....	319,233,879.68	371,892,554.60	691,126,434.28
2007.....	305,550,391.34	324,818,920.44	630,369,311.78
2008.....	286,328,148.60	333,166,787.98	619,494,936.58
2009.....	273,545,420.94	355,107,732.44	628,653,153.38
2010.....	249,949,348.25	343,676,633.76	593,625,982.01
2011.....	221,063,614.93	356,310,000.00	577,373,614.93
2012.....	202,396,701.31	339,700,000.00	542,096,701.31
2013.....	184,531,289.95	348,540,000.00	533,071,289.95
2014.....	166,276,851.81	351,520,000.00	517,796,851.81
2015.....	147,363,465.52	370,130,000.00	517,493,465.52
2016.....	127,649,752.49	351,330,000.00	478,979,752.49
2017.....	108,490,296.59	356,280,000.00	464,770,296.59
2018.....	89,600,584.79	370,835,000.00	460,435,584.79
2019.....	70,421,629.21	329,065,000.00	399,486,629.21
2020.....	53,156,840.70	299,060,000.00	352,216,840.70
2021.....	38,862,540.49	232,480,000.00	271,342,540.49
2022.....	26,705,616.62	202,390,000.00	229,095,616.62
2023.....	17,810,594.13	147,340,000.00	165,150,594.13
2024.....	11,258,070.63	56,175,000.00	67,433,070.63
2025.....	8,244,482.50	59,185,000.00	67,429,482.50
2026.....	5,574,756.25	45,215,000.00	50,789,756.25
2027.....	3,273,798.75	47,475,000.00	50,748,798.75
2028.....	922,862.50	34,170,000.00	35,092,862.50
Total	\$ 3,690,261,891.25	\$ 6,734,133,522.66	\$ 10,424,395,413.91

(a) Includes scheduled mandatory sinking fund payments as well as serial maturities.

(b) Total represents the remaining debt service requirements from June 1, 2003 through June 30, 2003.

SOURCE: State of California, Office of the Treasurer.

**STATE PUBLIC WORKS BOARD AND
OTHER LEASE-PURCHASE FINANCING
OUTSTANDING ISSUES**

May 1, 2003

<u>Name of Issue</u>	<u>Outstanding</u>
<u>GENERAL FUND SUPPORTED ISSUES:</u>	
State Public Works Board	
California Community Colleges	\$ 544,955,000
Department of the Youth Authority	17,615,000
Department of Corrections *	2,318,984,291
Energy Efficiency Program (Various State Agencies) (a)	83,785,000
The Regents of The University of California * (b)	1,179,854,232
Trustees of The California State University	607,945,000
Various State Office Buildings	1,098,245,000
Total State Public Works Board Issues	\$ 5,851,383,523
Total Other State Building Lease Purchase Issues(c)	\$ 882,750,000
Total General Fund Supported Issues	\$ 6,734,133,523
<u>SPECIAL FUND SUPPORTED ISSUES:</u>	
East Bay State Building Authority Certificates of Participation	
(State of California Department of Transportation) *	\$ 67,047,955
San Bernardino Joint Powers Financing Authority	
(State of California Department of Transportation)	55,380,000
San Francisco State Building Authority	
(State of California Department of General Services Lease) (d)	41,590,000
Total Special Fund Supported Issues	\$ 164,017,955
TOTAL	\$ 6,898,151,478

* Includes the initial value of capital appreciation bonds rather than the accreted value.

(a) This program is self-liquidating based on energy cost savings.

(b) The Regents' obligations to the State Public Works Board are payable from lawfully available funds of The Regents which are held in The Regents' treasury funds and are separate from the State General Fund. A portion of The Regents' annual budget is derived from General Fund appropriations.

(c) Includes \$180,450,000 Sacramento City Financing Authority Lease Revenue Bonds State of California - Cal EPA Building, 1998 Series A, which are supported by lease rentals from the California Environmental Protection Agency; these rental payments are subject to annual appropriation by the State Legislature.

(d) The sole tenant is the California Public Utilities Commission.

SOURCE: State of California, Office of the Treasurer.

**STATE AGENCY REVENUE BONDS
AND CONDUIT FINANCING
As of December 31, 2002**

<u>Issuing Agency</u>	<u>Outstanding^(a)</u>
<u>State Programs Financing:</u>	
California State University.....	\$ 625,118,000
California Transportation Commission.....	--
Department of Water Resources - Central Valley Project.....	2,398,180,000
Department of Water Resources - Power Supply Program.....	11,263,500,000
The Regents of the University of California ^(b)	3,962,335,000
Trade and Commerce Agency.....	--
<u>Housing Financing:</u>	
California Housing Finance Agency.....	8,158,493,913
Veterans Revenue Debenture.....	534,040,000
<u>Conduit Financing:</u>	
California Alternative Energy and Advanced Transportation Financing Authority.....	58,610,000
California Educational Facilities Authority.....	2,632,319,951
California Health Facilities Financing Authority.....	6,396,805,195
California Infrastructure and Economic Development Bank ^(c)	1,831,618,173
California Passenger Rail Financing Commission.....	--
California Pollution Control Financing Authority.....	4,602,162,399
California School Finance Authority.....	90,000
California Student Loan Authority.....	95,260,000
California Urban Waterfront Area Restoration Financing Authority.....	--
TOTAL.....	\$ 42,558,532,631

^(a) Totals for California State University, Department of Water Resources-Central Valley Project, and Veterans Revenue Debenture were provided by the State of California, Office of the Treasurer. All other totals were provided by the listed issuing agency.

^(b) Includes \$319,635,000 in Certificates of Participation.

^(c) Does not include \$6 billion of "rate reduction bonds" issued by special purpose trusts for the benefit of four investor-owned electric utility companies representing interests in certain electric rate surcharges.

STATEMENT of GENERAL FUND CASH RECEIPTS and DISBURSEMENTS

May 2003



STEVE WESTLY
California State Controller

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STEVE WESTLY
California State Controller
June 10, 2003

Users of the Statement of General Fund Cash Receipts and Disbursements

Attached are the Statements of General Fund Cash Receipts and Disbursements for the period July 1, 2002 through May 31, 2003. These statements reflect the State of California's General Fund cash position and compare actual receipts and disbursements for the 2002-03 fiscal year to cash flow estimates prepared by the Department of Finance for the 2003-04 May Revision as well as the 2002-03 Budget Act. These statements are prepared in compliance with Government Code section 12461.1, as well as Item 0840-001-0001, Provision 10, of the 2002-03 Budget Act, using records compiled by the State Controller.

Since February 2003, certain General Fund payments were made by the General Cash Revolving Fund (GCRF). The GCRF was established as a preliminary step in the process to borrow externally by issuing Revenue Anticipation Warrants (RAWs). The issuance of the RAWs is authorized by Government Code section 16381 and will enable the General Fund to meet its obligations. The GCRF amounts have been combined with the General Fund for reporting purposes because they represent major General Fund type activities. (See Attachment C for details.)

Attachment A compares actual receipts and disbursements to date for the 2002-03 fiscal year to cash flow estimates published in the 2003-04 May Revision. The May Revision cash flow reflects an expected decrease of \$9.8 billion in receipts, and an expected increase of \$1.8 billion in disbursements from the Budget Act estimate for the 2002-03 fiscal year. These cash flow estimates are predicated on projections and assumptions made by the Department of Finance in preparation of the May Revision.

Attachment B compares actual receipts and disbursements to date for the 2002-03 fiscal year to cash flow estimates prepared by the Department of Finance based upon the 2002-03 Budget Act. Prior year actual amounts are also displayed for comparative purposes.

These statements are also available on the Internet at the State Controller's Web site at <http://www.sco.ca.gov/ard/state/index.shtml> under the category Monthly Statement of General Fund Cash Receipts and Disbursements.

Any questions concerning this report may be directed to Walter Barnes, Chief Deputy Controller, Finance at (916) 445-3028.

Sincerely,

A handwritten signature in black ink that reads "Steve Westly". The signature is written in a cursive, slightly slanted style.

STEVE WESTLY
State Controller

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2003-04 May Revision Estimates
(Amounts in thousands)
Attachment A

	July 1 through May 31				2002 Actual
	2003 (a)		Actual Over or (Under) Estimate		
	Actual	Estimate (b)	Amount	%	
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ 3,394,277
Add Receipts:					
Revenues	61,343,543	60,861,612	481,931	0.8	57,773,811
Nonrevenues	7,564,727	8,248,924	(684,197)	(8.3)	2,007,444
Total Receipts	68,908,270	69,110,536	(202,266)	(0.3)	59,781,255
Less Disbursements:					
State Operations (a)	17,606,934	17,793,447	(186,513)	(1.0)	17,774,429
Local Assistance (a)	57,684,686	57,920,763	(236,077)	(0.4)	54,432,640
Capital Outlay	148,154	151,470	(3,316)	(2.2)	381,166
Nongovernmental	125,133	179,568	(54,435)	(30.3)	2,587,317
Total Disbursements	75,564,907	76,045,248	(480,341)	(0.6)	75,175,552
Receipts Over / (Under) Disbursements	(6,656,637)	(6,934,712)	278,075	-	(15,394,297)
Net Increase / (Decrease) in Temporary Loans	7,425,720	12,561,012	(5,135,292)	(40.9)	13,200,000
GENERAL FUND ENDING CASH BALANCE	769,083	5,626,300	(4,857,217)	(86.3)	1,199,980
Special Fund for Economic Uncertainties	-	-	-	-	-
TOTAL CASH	\$ 769,083	\$ 5,626,300	\$ (4,857,217)	(86.3)	\$ 1,199,980
BORROWABLE RESOURCES					
Available Borrowable Resources	\$ 25,685,111	\$ 24,745,617	\$ 939,494	3.8	\$ 18,732,764
Outstanding Loans (a) (c)	23,500,000	23,008,992	491,008	2.1	13,200,000
Unused Borrowable Resources	\$ 2,185,111	\$ 1,736,625	\$ 448,486	25.8	\$ 5,532,764

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- The General Cash Revolving Fund (GCRF) disbursements and loans have been combined with the General Fund for reporting purposes because they represent major General Fund type activities. See Attachment C for details.
- A Statement of Estimated Cash Flow for the 2002-03 fiscal year prepared by the Department of Finance for the May Revision to 2003-04 Governor's Budget. Any projections or estimates are set forth as such and not as representations of fact.
- Cumulative loan balance of \$23.5 billion is comprised of \$11.0 billion in internal borrowing and \$12.5 billion in external borrowing of which \$5.6 billion remains in the Special Deposit Revenue Anticipation Notes Proceeds Account.
- Includes Horse Racing Fees that were previously displayed separately.
- Negative balances are the result of repayments received that are greater than disbursements made.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of May		July 1 through May 31				
	2003	2002	2003 (a)		2002		
			Actual	Estimate (b)	Actual Over or (Under) Estimate		Actual
				Amount	%		
REVENUES							
Alcoholic Beverage Excise Tax	\$ 24,150	\$ 24,631	\$ 269,661	\$ 268,511	\$ 1,150	0.4	\$ 271,918
Corporation Tax	214,373	188,548	5,305,405	5,302,032	3,373	0.1	4,113,743
Cigarette Tax	11,040	3,275	115,660	113,620	2,040	1.8	102,262
Estate, Inheritance, and Gift Tax	51,752	71,032	880,766	902,014	(21,248)	(2.4)	938,439
Insurance Companies Tax	15,033	23,130	1,491,367	1,490,334	1,033	0.1	1,320,615
Personal Income Tax	1,339,190	1,011,806	29,104,953	29,022,763	82,190	0.3	30,232,120
Retail Sales and Use Taxes	2,988,692	2,951,163	20,082,666	20,205,974	(123,308)	(0.6)	19,293,123
Pooled Money Investment Interest	24,729	27,791	190,029	176,300	13,729	7.8	445,585
Not Otherwise Classified (d)	74,492	43,196	3,903,036	3,380,064	522,972	15.5	1,056,006
Total Revenues	4,743,451	4,344,572	61,343,543	60,861,612	481,931	0.8	57,773,811
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	-	-	-	-	-	-	10,280
Transfers from Other Funds	36,139	35,919	929,172	1,139,024	(209,852)	(18.4)	1,512,100
Transfers from Electric Power Fund	-	-	6,094,067	6,619,547	(525,480)	(7.9)	116,300
Miscellaneous	116,147	79,794	541,488	490,353	51,135	10.4	368,764
Total Nonrevenues	152,286	115,713	7,564,727	8,248,924	(684,197)	(8.3)	2,007,444
Total Receipts	\$ 4,895,737	\$ 4,460,285	\$ 68,908,270	\$ 69,110,536	\$ (202,266)	(0.3)	\$ 59,781,255

See notes on page A1.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of May		July 1 through May 31				
	2003	2002	2003 (a)		2002		
			Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
STATE OPERATIONS (e)							
Legislative/Judicial/Executive	\$ 63,571	\$ 96,431	\$ 1,198,609 (a)	\$ 1,211,163	\$ (12,554)	(1.0)	\$ 1,158,191
State and Consumer Services	36,144	37,752	424,530	424,326	204	-	427,219
Business, Transportation and Housing	116	10,979	7,444	8,197	(753)	(9.2)	25,135
Technology, Trade and Commerce	5,466	2,201	26,132	23,327	2,805	12.0	35,735
Resources	42,986	62,971	830,635	811,273	19,362	2.4	1,006,841
Environmental Protection Agency	5,745	19,452	139,645	143,438	(3,793)	(2.6)	359,499
Health and Human Services:							
Health Services	14,558	29,570	241,287	243,408	(2,121)	(0.9)	237,901
Mental Health Hospitals	2,922	29,805	487,319	510,506	(23,187)	(4.5)	471,747
Other Health and Human Services	50,381	9,386	605,422	606,213	(791)	(0.1)	513,939
Education:							
University of California	70,357	262,540	3,112,031 (a)	3,304,511	(192,480)	(5.8)	3,272,056
State Universities and Colleges	230,897	213,426	2,422,916	2,414,016	8,900	0.4	2,385,224
Other Education	10,160	14,298	171,218	175,060	(3,842)	(2.2)	177,799
Corrections and Youth Authority	464,167	436,129	5,095,085 (a)	5,119,494	(24,409)	(0.5)	4,522,950
General Government	69,626	119,859	1,034,306 (a)	1,070,759	(36,453)	(3.4)	1,046,174
Public Employees Retirement							
System	(164)	(41,011)	123,200	26,460	96,740	365.6	(53,780)
Debt Service	124,631	127,453	1,573,493 (a)	1,576,675	(3,182)	(0.2)	2,156,406
Interest on Loans	9,541	2,438	113,662	124,621	(10,959)	(8.8)	31,393
Total State Operations	1,201,104	1,433,679	17,606,934	17,793,447	(186,513)	(1.0)	17,774,429
LOCAL ASSISTANCE (e)							
Public Schools - K-12	2,020,414	1,669,606	25,067,401 (a)	25,115,179	(47,778)	(0.2)	24,676,177
Community Colleges	207,034	199,704	2,503,902 (a)	2,482,294	21,608	0.9	2,586,411
Contributions to State Teachers' Retirement System	-	-	975,522	975,522	-	-	871,774
Other Education	69,539	95,773	2,321,767 (a)	2,439,470	(117,703)	(4.8)	2,274,505
Corrections and Youth Authority	10,213	9,981	150,993	153,572	(2,579)	(1.7)	122,888
Dept. of Alcohol and Drug Program	(708)	6,805	237,838	243,693	(5,855)	(2.4)	228,191
Dept. of Health Services:							
Medical Assistance Program	841,472	1,050,796	9,858,975 (a)	9,989,889	(130,914)	(1.3)	9,237,021
Other Health Services	28,791	50,590	425,122	441,146	(16,024)	(3.6)	421,853
Dept. of Developmental Services	79,565	10,841	1,337,276 (a)	1,267,401	69,875	5.5	1,397,852
Dept. of Mental Health	(43,009)	(62,737)	407,697 (a)	458,719	(51,022)	(11.1)	398,328
Dept. of Social Services:							
SSI/SSP/IHSS	125,307	36,791	3,801,003 (a)	3,730,312	70,691	1.9	3,320,628
CalWORKs	133,339	78,146	2,528,920 (a)	2,527,603	1,317	0.1	2,424,452
Other Social Services	66,144	60,033	1,183,404 (a)	1,207,590	(24,186)	(2.0)	959,684
Tax Relief	391,786	449,455	4,242,417 (a)	4,282,012	(39,595)	(0.9)	2,683,877
School Facility Aid Program	-	-	15,566	15,566	-	-	18,122
Other Local Assistance	104,669	318,079	2,626,883 (a)	2,590,795	36,088	1.4	2,810,877
Total Local Assistance	4,034,556	3,973,863	57,684,686	57,920,763	(236,077)	(0.4)	54,432,640

See notes on page A1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)
 (Amounts in thousands)

	Month of May		July 1 through May 31				
	2003	2002	2003 (a)		2002		
			Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
CAPITAL OUTLAY	4,848	32,992	148,154	151,470	(3,316)	(2.2)	381,166
NONGOVERNMENTAL (e)							
Transfer to Special Fund for Economic Uncertainties	-	-	-	-	-	-	2,391,514
Transfer to Other Funds	5,000	1,241	167,689	179,209	(11,520)	(6.4)	300,918
Transfer to Revolving Fund Advance:	(12,209)	(297)	69,291	81,500	(12,209)	(15.0)	73,885
State-County Property Tax Administration Program	-	4,256	9,677	9,677	-	-	52,451
Social Welfare Federal Fund	(12,706)	1,330	94,220	143,926	(49,706)	(34.5)	4,701
Tax Relief and Refund Account	19,000	17,500	32,100	13,100	19,000	145.0	19,800
Counties for Social Welfare	-	-	(247,844)	(247,844)	-	-	(255,952)
Total Nongovernmental	(915)	24,030	125,133	179,568	(54,435)	(30.3)	2,587,317
Total Disbursements	\$ 5,239,593	\$ 5,464,564	\$ 75,564,907	\$ 76,045,248	\$ (480,341)	(0.6)	\$ 75,175,552
TEMPORARY LOANS (e)							
Special Fund for Economic Uncertainties	\$ -	\$ -	\$ - (a)	\$ -	\$ -	-	\$ 2,524,519
Other Internal Sources	1,034,463	2,204,259	8,052,020 (a)	7,561,012	491,008	6.5	4,975,481
Revenue Anticipation Warrants	-	-	(7,500,000)	(7,500,000)	-	-	-
Revenue Anticipation Notes (c)	-	-	6,873,700	12,500,000	(5,626,300)	(45.0)	5,700,000
Net Increase / (Decrease) Loans	\$ 1,034,463	\$ 2,204,259	\$ 7,425,720	\$ 12,561,012	\$ (5,135,292)	(40.9)	\$ 13,200,000

See notes on page A1.

(Concluded)

COMPARATIVE STATEMENT OF REVENUES RECEIVED
All Governmental Cost Funds
(Amounts in thousands)

	July 1 through May 31			
	General Fund		Special Funds	
	2003	2002	2003	2002
MAJOR TAXES, LICENSES, AND INVESTMENT INCOME:				
Alcoholic Beverage Excise Taxes	\$ 269,661	\$ 271,918	\$ -	\$ -
Corporation Tax	5,305,405	4,113,743	8	5
Cigarette Tax	115,660	102,262	925,959	842,890
Estate, Inheritance, and Gift Tax	880,766	938,439	-	-
Insurance Companies Tax	1,491,367	1,320,615	-	-
Motor Vehicle Fuel Tax:				
Gasoline Tax	-	-	2,553,708	2,541,116
Diesel & Liquid Petroleum Gas	-	-	436,304	423,366
Jet Fuel Tax	-	-	2,253	2,112
Vehicle License Fees	-	-	1,724,600	1,794,745
Motor Vehicle Registration and Other Fees	-	-	1,833,054	1,783,286
Personal Income Tax	29,104,953	30,232,120	322	404
Retail Sales and Use Taxes	20,082,666	19,293,123	4,295,570	4,186,224
Pooled Money Investment Interest	190,029	445,585	489	982
Total Major Taxes, Licenses, and Investment Income	57,440,507	56,717,805	11,772,267	11,575,130
NOT OTHERWISE CLASSIFIED:				
Alcoholic Beverage License Fee	2,288	2,188	37,072	33,027
Electrical Energy Tax	-	-	474,666	242,330
Private Rail Car Tax	6,416	6,383	-	-
Penalties on Traffic Violations	-	-	68,518	74,552
Health Care Receipts	11,563	12,620	-	-
Revenues from State Lands	65,585	15,013	9,218	26,901
Abandoned Property	234,281	305,332	-	-
Trial Court Revenues	288	538	-	-
Horse Racing Fees	2,979	3,007	34,871	37,448
Miscellaneous	3,579,636	710,925	5,224,919	6,176,647
Not Otherwise Classified	3,903,036	1,056,006	5,849,264	6,590,905
Total Revenues, All Governmental Cost Funds	\$ 61,343,543	\$ 57,773,811	\$ 17,621,531	\$ 18,166,035

See notes on page A1.

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2002-03 Budget Act Estimates
(Amounts in thousands)
Attachment B

	July 1 through May 31				2002 Actual
	2003 (a)		Actual Over or (Under) Estimate		
	Actual	Estimate (b)	Amount	%	
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ 3,394,277
Add Receipts:					
Revenues	61,343,543	68,589,485	(7,245,942)	(10.6)	57,773,811
Nonrevenues	7,564,727	11,159,085	(3,594,358)	(32.2)	2,007,444
Total Receipts	68,908,270	79,748,570	(10,840,300)	(13.6)	59,781,255
Less Disbursements:					
State Operations (a)	17,606,934	15,796,585	1,810,349	11.5	17,774,429
Local Assistance (a)	57,684,686	56,787,561	897,125	1.6	54,432,640
Capital Outlay	148,154	83,478	64,676	77.5	381,166
Nongovernmental	125,133	254,148	(129,015)	(50.8)	2,587,317
Total Disbursements	75,564,907	72,921,772	2,643,135	3.6	75,175,552
Receipts Over / (Under) Disbursements	(6,656,637)	6,826,798	(13,483,435)	(197.5)	(15,394,297)
Net Increase / (Decrease) in Temporary Loans	7,425,720	2,052,020	5,373,700	261.9	13,200,000
GENERAL FUND ENDING CASH BALANCE	769,083	8,878,818	(8,109,735)	(91.3)	1,199,980
Special Fund for Economic Uncertainties	-	1,035,500	(1,035,500)	(100.0)	-
TOTAL CASH	\$ 769,083	\$ 9,914,318	\$ (9,145,235)	(92.2)	\$ 1,199,980
BORROWABLE RESOURCES					
Available Borrowable Resources	\$ 25,685,111	\$ 20,430,963	\$ 5,254,148	25.7	\$ 18,732,764
Outstanding Loans (a) (c)	23,500,000	12,500,000	11,000,000	88.0	13,200,000
Unused Borrowable Resources	\$ 2,185,111	\$ 7,930,963	\$ (5,745,852)	(72.4)	\$ 5,532,764

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- (a) The General Cash Revolving Fund (GCRF) disbursements and loans have been combined with the General Fund for reporting purposes because they represent major General Fund type activities. See Attachment C for details.
- (b) A Statement of Estimated Cash Flow for the 2002-03 fiscal year prepared by the Department of Finance for the Budget Act of 2002. Any projections or estimates are set forth as such and not as representations of fact.
- (c) Cumulative loan balance of \$23.5 billion is comprised of \$11.0 billion in internal borrowing and \$12.5 billion in external borrowing of which \$5.6 billion remains in the Special Deposit Revenue Anticipation Notes Proceeds Account.
- (d) Includes Horse Racing Fees that were previously displayed separately.
- (e) Negative balances are the result of repayments received that are greater than disbursements made.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of May		July 1 through May 31				
			2003 (a)		2002		
	2002	2002	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
REVENUES							
Alcoholic Beverage Excise Tax	\$ 24,150	\$ 24,631	\$ 269,661	\$ 264,706	\$ 4,955	1.9	\$ 271,918
Corporation Tax	214,373	188,548	5,305,405	5,843,934	(538,529)	(9.2)	4,113,743
Cigarette Tax	11,040	3,275	115,660	119,660	(4,000)	(3.3)	102,262
Estate, Inheritance, and Gift Tax	51,752	71,032	880,766	747,472	133,294	17.8	938,439
Insurance Companies Tax	15,033	23,130	1,491,367	1,392,985	98,382	7.1	1,320,615
Personal Income Tax	1,339,190	1,011,806	29,104,953	33,897,771	(4,792,818)	(14.1)	30,232,120
Retail Sales and Use Taxes	2,988,692	2,951,163	20,082,666	20,630,040	(547,374)	(2.7)	19,293,123
Pooled Money Investment Interest	24,729	27,791	190,029	185,109	4,920	2.7	445,585
Not Otherwise Classified (d)	74,492	43,196	3,903,036	5,507,808	(1,604,772)	(29.1)	1,056,006
Total Revenues	4,743,451	4,344,572	61,343,543	68,589,485	(7,245,942)	(10.6)	57,773,811
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	-	-	-	1,489,019	(1,489,019)	(100.0)	10,280
Transfers from Other Funds	36,139	35,919	929,172	2,778,167	(1,848,995)	(66.6)	1,512,100
Transfers from Electric Power Fund	-	-	6,094,067	6,614,994	(520,927)	(7.9)	116,300
Miscellaneous	116,147	79,794	541,488	276,905	264,583	95.6	368,764
Total Nonrevenues	152,286	115,713	7,564,727	11,159,085	(3,594,358)	(32.2)	2,007,444
Total Receipts	\$ 4,895,737	\$ 4,460,285	\$ 68,908,270	\$ 79,748,570	\$ (10,840,300)	(13.6)	\$ 59,781,255

See notes on page B1.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of May		July 1 through May 31				2002 Actual
	2003	2002	2003 (a)		Actual Over or (Under) Estimate		
			Actual	Estimate (b)	Amount	%	
STATE OPERATIONS (e)							
Legislative/Judicial/Executive	\$ 63,571	\$ 96,431	\$ 1,198,609 (a)	\$ 981,738	\$ 216,871	22.1	\$ 1,158,191
State and Consumer Services	36,144	37,752	424,530	422,010	2,520	0.6	427,219
Business, Transportation and Housing	116	10,979	7,444	7,688	(244)	(3.2)	25,135
Technology, Trade and Commerce	5,466	2,201	26,132	24,530	1,602	6.5	35,735
Resources	42,986	62,971	830,635	772,842	57,793	7.5	1,006,841
Environmental Protection Agency	5,745	19,452	139,645	148,414	(8,769)	(5.9)	359,499
Health and Human Services:							
Health Services	14,558	29,570	241,287	241,163	124	0.1	237,901
Mental Health Hospitals	2,922	29,805	487,319	469,631	17,688	3.8	471,747
Other Health and Human Services	50,381	9,386	605,422	534,871	70,551	13.2	513,939
Education:							
University of California	70,357	262,540	3,112,031 (a)	3,123,371	(11,340)	(0.4)	3,272,056
State Universities and Colleges	230,897	213,426	2,422,916	2,530,414	(107,498)	(4.2)	2,385,224
Other Education	10,160	14,298	171,218	156,285	14,933	9.6	177,799
Corrections and Youth Authority	464,167	436,129	5,095,085 (a)	4,436,866	658,219	14.8	4,522,950
General Government	69,626	119,859	1,034,306 (a)	257,118	777,188	302.3	1,046,174
Public Employees Retirement System	(164)	(41,011)	123,200	38,450	84,750	220.4	(53,780)
Debt Service	124,631	127,453	1,573,493 (a)	1,560,732	12,761	0.8	2,156,406
Interest on Loans	9,541	2,438	113,662	90,462	23,200	25.6	31,393
Total State Operations	1,201,104	1,433,679	17,606,934	15,796,585	1,810,349	11.5	17,774,429
LOCAL ASSISTANCE (e)							
Public Schools - K-12	2,020,414	1,669,606	25,067,401 (a)	25,977,286	(909,885)	(3.5)	24,676,177
Community Colleges	207,034	199,704	2,503,902 (a)	2,752,233	(248,331)	(9.0)	2,586,411
Contributions to State Teachers' Retirement System	-	-	975,522	975,522	-	-	871,774
Other Education	69,539	95,773	2,321,767 (a)	2,403,457	(81,690)	(3.4)	2,274,505
Corrections and Youth Authority	10,213	9,981	150,993	93,522	57,471	61.5	122,888
Dept. of Alcohol and Drug Program	(708)	6,805	237,838	202,510	35,328	17.4	228,191
Dept. of Health Services:							
Medical Assistance Program	841,472	1,050,796	9,858,975 (a)	9,031,123	827,852	9.2	9,237,021
Other Health Services	28,791	50,590	425,122	29,870	395,252	1,323.2	421,853
Dept. of Developmental Services	79,565	10,841	1,337,276 (a)	1,377,266	(39,990)	(2.9)	1,397,852
Dept. of Mental Health	(43,009)	(62,737)	407,697 (a)	516,940	(109,243)	(21.1)	398,328
Dept. of Social Services:							
SSI/SSP/HSS	125,307	36,791	3,801,003 (a)	3,566,822	234,181	6.6	3,320,628
CalWORKs	133,339	78,146	2,528,920 (a)	2,421,681	107,239	4.4	2,424,452
Other Social Services	66,144	60,033	1,183,404 (a)	980,665	202,739	20.7	959,684
Tax Relief	391,786	449,455	4,242,417 (a)	4,025,459	216,958	5.4	2,683,877
School Facility Aid Program	-	-	15,566	13,087	2,479	18.9	18,122
Other Local Assistance	104,669	318,079	2,626,883 (a)	2,420,118	206,765	8.5	2,810,877
Total Local Assistance	4,034,556	3,973,863	57,684,686	56,787,561	897,125	1.6	54,432,640

See notes on page B1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)

(Amounts in thousands)

	Month of May		July 1 through May 31				
	2003	2002	2003 (a)		2002		
			Actual	Estimate (b)	Actual Over or (Under) Estimate		Actual
				Amount	%		
CAPITAL OUTLAY	4,848	32,992	148,154	83,478	64,676	77.5	381,166
NONGOVERNMENTAL (e)							
Transfer to Special Fund for Economic Uncertainties	-	-	-	-	-	-	2,391,514
Transfer to Other Funds	5,000	1,241	167,689	398,691	(231,002)	(57.9)	300,918
Transfer to Revolving Fund Advance:	(12,209)	(297)	69,291	(16,234)	85,525	-	73,885
State-County Property Tax Administration Program	-	4,256	9,677	9,677	-	-	52,451
Social Welfare Federal Fund	(12,706)	1,330	94,220	109,928	(15,708)	(14.3)	4,701
Tax Relief and Refund Account	19,000	17,500	32,100	-	32,100	-	19,800
Counties for Social Welfare	-	-	(247,844)	(247,914)	70	-	(255,952)
Total Nongovernmental	(915)	24,030	125,133	254,148	(129,015)	(50.8)	2,587,317
Total Disbursements	\$ 5,239,593	\$ 5,464,564	\$ 75,564,907	\$ 72,921,772	\$ 2,643,135	3.6	\$ 75,175,552
TEMPORARY LOANS (e)							
Special Fund for Economic Uncertainties	\$ -	\$ -	\$ -	(a) \$ (2,524,519)	\$ 2,524,519	-	\$ 2,524,519
Other Internal Sources	1,034,463	2,204,259	8,052,020	(a) (423,461)	8,475,481	-	4,975,481
Revenue Anticipation Warrants	-	-	(7,500,000)	(7,500,000)	-	-	-
Revenue Anticipation Notes (c)	-	-	6,873,700	12,500,000	(5,626,300)	(45.0)	5,700,000
Net Increase / (Decrease) Loans	\$ 1,034,463	\$ 2,204,259	\$ 7,425,720	\$ 2,052,020	\$ 5,373,700	261.9	\$ 13,200,000

See notes on page B1.

(Concluded)

**GENERAL CASH REVOLVING FUND
STATEMENT OF CASH RECEIPTS AND DISBURSEMENTS
(Amounts in thousands)
Attachment C**

	July 1 through May 31, 2003
GENERAL CASH REVOLVING FUND BEGINNING CASH BALANCE	\$ -
Add Receipts:	
Special Fund Loans	11,000,000
Government Code section 16381	
Less Disbursements:	
Government Code section 16381	
State Operations	
Legislative/Judicial/Executive	154,151
Education:	
University of California	233,418
Corrections and Youth Authority	178,311
General Government	91,165
Debt Service	231,181
Total State Operations	888,226
Local Assistance	
Public Schools - K-12	7,458,712
Community Colleges	440,361
Other Education	236,503
Dept. of Health Services:	
Medical Assistance Program	1,137,182
Dept. of Developmental Services	204,811
Dept. of Mental Health	5,853
Dept. of Social Services:	
SSI/SSP/IHSS	12,532
Calworks	37,875
Other Social Services	34,995
Tax Relief	308,097
Other Local Assistance	234,853
Total Local Assistance	10,111,774
Total Disbursements	11,000,000
GENERAL CASH REVOLVING FUND ENDING CASH BALANCE	\$ -

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APPENDIX B

SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The following is a brief summary of certain provisions of the Trust Agreement (the "Trust Agreement") authorizing the Bonds and the Riverside State Building Lease, dated as of April 26, 1994, as amended (the "Lease") that are not otherwise described in the text of this Official Statement. Such summary is not intended to be definitive, and reference is made to the actual Trust Agreement and Lease (copies of which may be obtained from the Agency) for the complete terms thereof.

DEFINITIONS

"Act" means Article 10 and Article 11 of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code (commencing with Section 53570) and all laws amendatory thereof or supplemental thereto.

"Additional Bonds" means all lease revenue bonds of the Agency authorized by and at any time Outstanding pursuant hereto and executed, issued and delivered in accordance with the Trust Agreement.

"Additional Rental" means the amounts specified as such in the Lease.

"Annual Debt Service" means, for any Lease Year, the sum of (1) the interest payable on all Outstanding Bonds in such Lease Year, assuming that all Outstanding Serial Bonds are retired as scheduled and that all Outstanding Term Bonds are redeemed or paid from sinking account payments as scheduled (except to the extent that such interest is to be paid from the proceeds of sale of any Bonds), (2) the principal amount of all Outstanding Serial Bonds maturing by their terms in such Lease Year, and (3) the principal amount of all Outstanding Term Bonds required to be redeemed or paid in such Lease Year (together with the redemption premium, if any, thereon).

"Authorized Denominations" means \$5,000 and any integral multiple thereof, and, in the case of Additional Bonds, the amount specified in the Supplemental Trust Agreement authorizing the issuance thereof.

"Base Rental" means the amounts referred to as such in the Lease, as such amounts may be adjusted from time to time in accordance with the terms thereof, but does not include Additional Rental.

"Bonds" means the 2003 Bonds and all Additional Bonds of any series authorized by and at any time Outstanding pursuant to the Trust Agreement.

"Business Day" means a day of the year other than a Saturday or Sunday or a day on which State offices or banking institutions located in the State are required or authorized to remain closed.

"Certificate of the Agency" means an instrument in writing signed by the Chairperson, Vice-Chairperson, Executive Director or Secretary of the Agency, or by any other officer of the Agency duly authorized by the Executive Director for that purpose.

"Construction Costs" means any costs associated with the design, construction, acquisition, installation, delivery and financing of improvements to the portion of the Project leased back by the Agency from the Department, including but not limited to, administration, engineering, legal and financial costs, costs of tenant improvements for sublessees and sublessee allowances and concessions, all as determined by the Agency.

"Construction Fund" means the fund by that name established pursuant to the Trust Agreement.

"Costs of Issuance" means all the costs of issuance, preparation, sale, execution and delivery of the Bonds and other costs related to the financing provided thereby, including, but not limited to, all printing and document preparation expenses in connection with the Bonds, the Trust Agreement and other legal documents, the preliminary and final official statements pertaining to the Bonds and all other agreements, instruments, certificates or other documents executed and delivered in connection therewith; fees of the rating agencies rating the Bonds; CUSIP Service Bureau charges; insurance premiums and fees incurred in connection with the Municipal Bond Insurance Policy; legal fees and expenses of counsel with respect to the financing; the initial fees and expenses of the Trustee and its counsel and any paying agent and its counsel (including without limitation origination or acceptance fees and first annual fees payable in advance); and other fees and expenses incurred in connection with the issuance of the Bonds or the implementation of the refinancing for the Project, to the extent such fees and expenses are approved by a Written Request of the Agency.

"Costs of Issuance Fund" means the fund by that name established pursuant to the Trust Agreement.

"Demised Premises" or "Premises" means the Project and the Site.

"Department" means the Department of General Services of the State of California, or its successors and assigns.

"Escrow Bank" means U.S. Bank National Association, its successors and assigns.

"Escrow Agreement" means that certain Escrow Deposit and Trust Agreement dated as of July 1, 2003, by and between the Agency and the Escrow Bank.

"Escrow Fund" means the fund by that name established pursuant to the Escrow Agreement.

"Financial Newspaper" means The Wall Street Journal or The Bond Buyer or any other newspaper or journal printed in the English language publishing financial news and selected by the Trustee, whose decision shall be final and conclusive.

"Fiscal Year" means the twelve-month period terminating on June 30 of each year, or any other annual accounting period hereafter selected and designated by the Agency as its Fiscal Year in accordance with applicable law.

"Holder" or "Bondholder" means any person who shall be the registered owner of any Outstanding Bond.

"Independent Certified Public Accountant" means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the Agency and who, or each of whom:

- (1) is in fact independent and not under the domination of the Agency;
- (2) does not have a substantial financial interest, direct or indirect, in the operations of the Agency; and
- (3) is not connected with the Agency as a member, officer or employee of the Agency, but who may be regularly retained to audit the accounting records of and make reports thereon to the Agency.

"Information Services" means Financial Information, Incorporated's "Daily Called Bond Service," 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor, Mergent/MIS," 5250 77 Center Drive, Suite 150, Charlotte, NC 28217, Attention: Called Bonds Department; and Kenny S&P, 55 Water Street, 45th Floor, New York, New York 10041, Attention: Notification Department; or in accordance with then-current guidelines of the Securities and Exchange Commission, such other services providing information with respect to called bonds, or no such services, as the Agency may indicate in a certificate of the Agency delivered to the Trustee.

"Insurer" means Ambac Assurance Corporation.

"Interest Account" means the account by that name established pursuant to the Trust Agreement. Within the Interest Account, the Trustee shall establish and maintain a separate subaccount for each series of the Bonds as provided in the Trust Agreement.

"Interest Payment Date" means, as long as any of the Bonds are Outstanding, October 1, 2003 and each April 1 and October 1 thereafter.

"Law" means the Community Redevelopment Law of the State of California, being Part 1 of Division 24 of the California Health and Safety Code (commencing with Section 33000).

"Lease" means that certain Riverside/State Building Lease, dated as of April 26, 1994, as amended by the following four amendments: (i) Amendment to Riverside/State Building Lease and Leaseback Agreement, dated September 15, 1994; (ii) Second Amendment to Riverside/State Building Lease and Leaseback Agreement dated March 14, 1996; (iii) Third Amendment to Riverside/State Building Lease and Leaseback Agreement dated March 4, 1998; and (iv) Fourth Amendment to Riverside/State Building Lease and Leaseback Agreement dated February 6, 2003, each by and between the Agency and the Department and also including any amendments or supplements hereinafter entered into.

"Leaseback" means that certain Leaseback Agreement, dated as of April 26, 1994, by and between the Department of the Agency, including any amendments or supplements thereto.

"Lease Year" means the period from each October 1 to and including the following September 30, during the term of the Lease.

"Maximum Annual Debt Service" means the amount of debt service for that payment date on which the Annual Debt Service for the Bonds is the largest, beginning with the next occurring Interest Payment Date and ending with the Interest Payment Date on which the last Outstanding Bonds mature by their terms.

"Municipal Bond Insurance Policy" means the municipal bond insurance policy issued by the Insurer insuring the payment when due of the principal of and interest on the Insured Bonds as provided therein.

"1994 Bonds" means the Agency's Lease Revenue Bonds (State of California Department of General Services Lease) 1994 Series A and 1994 Series B issued pursuant to the 1994 Indenture.

"1994 Indenture" means the Indenture of Trust, dated as of September 15, 1994, by and between the Agency and U.S. Bank National Association, as successor trustee, pursuant to which the 1994 Bonds were issued.

"Opinion of Counsel" means a written opinion of counsel of recognized national standing in the field of law relating to municipal bonds and the tax status of interest on bonds issued by states and their political subdivisions, appointed and paid by the Agency.

"Outstanding," when used as of any particular time with reference to the Bonds, means (subject to the provisions of the Trust Agreement) all Bonds except:

- (1) Bonds theretofore canceled by the Trustee or surrendered to the Trustee for cancellation;
- (2) Bonds paid or deemed to have been paid in accordance with the Trust Agreement (except as otherwise provided in the Trust Agreement); and
- (3) Bonds in lieu of or in substitution for which other Bonds shall have been executed, issued and delivered by the Agency pursuant hereto.

"Permitted Investments" means:

A. Direct obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury, and CATS and TIGRS) or obligations the principal of and interest on which are unconditionally guaranteed by the United States of America;

B. Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are backed by the full faith and credit of the United States of America (stripped securities are only permitted if they have been stripped by the agency itself):

1. U.S. Export-Import Bank
Direct obligations or fully guaranteed certificates of beneficial ownership
2. Farmers Home Administration
Certificates of beneficial ownership
3. Federal Financing Bank
4. Federal Housing Administration Debentures
5. General Services Administration
Participation Certificates
6. Government National Mortgage Association (GNMA)
GNMA - guaranteed mortgage-backed bonds
GNMA - guaranteed pass-through obligations
7. U.S. Maritime Administration
Guaranteed Title XI financing

8. U.S. Department of Housing and Urban Development

Project Notes
Local Authority Bonds
New Communities Debentures - U.S. government guaranteed debentures
U.S. Public Housing Notes and Bonds - U.S. government guaranteed public housing notes and bonds;

C. Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following non-full faith and credit U.S. government agencies (stripped securities are only permitted if they have been stripped by the agency itself):

1. Federal Home Loan Bank System

Senior debt obligations

2. Federal Home Loan Mortgage Corporation

Participation Certificates
Senior debt obligations

3. Federal National Mortgage Association (FNMA or "Fannie Mae")

Mortgage-backed securities and senior debt obligations

4. Student Loan Marketing Association (SLMA or "Sallie Mae")

Senior debt obligations

5. Resolution Funding Corp. (REFCORP) obligations

6. Farm Credit System

Consolidated systemwide bonds and notes;

D. Money market funds registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933, and having a rating by Standard & Poor's Rating Service, a division of McGraw-Hill Companies, Inc. ("S&P") of AA-Am-G; AAA-m or AA-m and, if rated by Moody's Investors Service ("Moody's"), rated Aaa, Aa1 or Aa2;

E. Certificates of deposit secured at all times by collateral described in (A) and/or (B) and/or (C) above. Such certificates must be issued by commercial banks, savings and loan associations or mutual savings banks. The collateral must be held by a third party and the Bondholders must have a perfected first security interest in the collateral;

F. Certificates of deposit, savings accounts, deposit accounts or money market deposits which are fully insured by FDIC, including BIF and SAIF;

G. Investment Agreements, including GIC's Forward Purchase Agreements and Reserve Fund Put Agreements acceptable to the Insurer;

H. Commercial paper rated, at the time of purchase, "Prime - 1" by Moody's and "A-1" or better by S&P;

I. Bonds or notes issued by any state or municipality which are rated by Moody's and S&P in one of the two highest rating categories assigned by such agencies;

J. Federal funds or bankers acceptances with a maximum term of one year of any bank which has an unsecured, uninsured and unguaranteed obligation rating of "Prime - 1" or "A3" or better by Moody's and "A-1" or "A" or better by S&P;

K. Repurchase agreements for 30 days or less, which must follow the following criteria. Repurchase agreements which exceed 30 days must be acceptable to the Insurer.

1. The repurchase agreement must be between the Trustee or the Agency and a dealer bank or securities firm which is:

a. A primary dealer on the Federal Reserve reporting dealer list which is rated A or better by S&P and Moody's, or

b. A bank rated "A" or above by S&P and Moody's;

2. The written agreement must include the following:

a. Securities which are acceptable for transfer are:

(1) Direct obligations of the United States government, or

(2) Obligations of federal agencies backed by the full faith and credit of the United States of America (or the Federal National Mortgage Association (FNMA) or the Federal Home Loan Mortgage Corporation (FHLMC)),

b. The term of the repurchase agreement may be up to 30 days,

c. The collateral must be delivered to the Agency or the Trustee (if Trustee is not supplying the collateral) or third party acting as agent for the Trustee (if the Trustee is supplying the collateral) before/simultaneous with payment (perfection by possession of certificated securities),

d. Valuation of Collateral:

(1) The securities must be valued weekly, marked-to market at current market plus accrued interest; and

(2) The value of the collateral must be equal to 104% of the amount of money transferred by the Trustee entity to the dealer, bank or security firm under the repurchase agreement plus accrued interest. If the value of securities held as collateral is reduced below 104% of the value of the money transferred by the Trustee, then additional cash and/or acceptable securities must be transferred as collateral to bring the value of the collateral to 104%; provided, however, if the

securities used as collateral are those of FNMA or FHLMC, then the value of collateral must equal at least 105% of the amount of money transferred by the Trustee; and

3. A legal opinion which must be delivered to the Trustee or the Agency stating that the Repurchase Agreement meets guidelines under state law for legal investment of public funds; and

L. The Local Agency Investment Fund in the State Treasury of the State of California as permitted by the State Treasurer pursuant to Section 16429.1 of the California Government Code (provided for any funds invested by the Trustee, the Trustee is entitled to deposit and withdraw funds directly in its own name as Trustee).

"Principal Account" means the account by that name established pursuant to the Trust Agreement. Within the Principal Account the Trustee shall establish and maintain a separate subaccount for each series of the Bonds as provided in the Trust Agreement.

"Principal Office" means the corporate trust office of the Trustee located in Los Angeles, California; provided, however, that the Trustee may designate in writing to the Agency, the Department and the Owners such other office or agency from time to time for purposes of registration, transfer, exchange, payment or redemption of Bonds.

"Project" means the State office building acquired, installed and constructed on the Site and leased to the Department, all pursuant to the Lease and further described in Exhibit A to the Lease.

"Rebate Fund" means the fund by that name established pursuant to the Trust Agreement.

"Representation Letter" means that certain blanket issuer letter of representations executed by the Agency and delivered to DTC.

"Reserve Account" means the account by that name established pursuant to the Trust Agreement. With the Reserve Account, the Trustee shall establish and maintain a separate subaccount for each series of the Bonds as provided in the Trust Agreement.

"Reserve Account Requirement" means, as of any date of calculation, (a) with respect to the 2003 Series A Bonds, an amount equal to the least of (i) \$2,341,500 (ii) 10% of the aggregate principal amount of the 2003 Series A Bonds then Outstanding, (iii) Maximum Annual Debt Service on the 2003 Series A Bonds in the then current Lease Year or any future Lease Year, or (iv) 125% of average Annual Debt Service on the 2003 Series A Bonds payable in each Lease Year between the date of calculation and the last maturity of the 2003 Series A Bonds, (b) with respect to the 2003 Series B Bonds, an amount equal to \$370,832; and (c) with respect to a series of Additional Bonds, the amount specified in the Supplemental Trust Agreement providing for the issuance of such series of Additional Bonds.

"Revenue Fund" means the fund by that name established pursuant to the Trust Agreement.

"Revenues" means all Base Rental payments received by or on behalf of the Agency pursuant to the Lease, and all other benefits, charges, income, proceeds, profits, receipts, rents, proceeds of insurance and revenues derived by the Agency from the ownership, operation or use of the Demised Premises, including interest or profits from the investment of money in any account or fund (other than the Rebate Fund) pursuant to the Trust Agreement.

"Securities Depositories" means The Depository Trust Company, 711 Stewart Avenue, Garden City, New York 11530, Fax-(516) 227-4039 or 4190; Midwest Securities Trust Company, Capital Structures-Call Notification, 440 South LaSalle Street, Chicago, Illinois 60605, Fax-(312) 663-2343; Philadelphia Depository Trust Company, Reorganization Division, 1900 Market Street, Philadelphia, Pennsylvania 19103, Attention: Bond Department, Fax-(215) 496-5058; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other securities depositories as the Agency may designate in a certificate of the Agency delivered to the Trustee.

"Serial Bonds" means Bonds for which no sinking account payments are provided.

"Site" means that certain real property described in Exhibit A to the Lease.

"State" means the State of California.

"Supplemental Trust Agreement" means any trust agreement then in full force and effect which has been duly executed and delivered by the Agency and the Trustee amendatory hereof or supplemental hereto; but only if and to the extent that such Supplemental Trust Agreement is specifically authorized under the Trust Agreement.

"Surplus Account" means the account by that name established pursuant to the Trust Agreement.

"Term Bonds" means Bonds which are payable on or before their specified maturity dates from sinking account payments established for that purpose and calculated to retire such Bonds on or before their specified maturity dates.

"2003 Bonds" means the \$31,065,000 initial aggregate principal amount Redevelopment Agency of the City of Riverside Lease Revenue Refunding Bonds (State of California Department of General Services Project) 2003 Series A (Tax-Exempt) and 2003 Series B (Taxable).

"2003 Series A Bonds" means the \$26,255,000 initial aggregate principal amount 2003 Bonds captioned as "2003 Series A Bonds (Tax-Exempt)".

"2003 Series A Reserve Subaccount" means the subaccount by that name established in the Reserve Account pursuant to the Trust Agreement.

"2003 Series B Bonds" means the \$4,810,000 initial aggregate principal amount 2003 Bonds captioned as "2003 Series B Bonds (Taxable)".

"2003 Series B Reserve Subaccount" means the subaccount by that name established in the Reserve Account pursuant to the Trust Agreement.

"Written Request" means an instrument in writing signed by the Chairperson, Vice-Chairperson, Executive Director or Secretary of the Agency, or by an authorized officer of the Department, as appropriate, or by any other officer of the Agency or the Department duly authorized for that purpose.

THE TRUST AGREEMENT

Establishment of Funds and Accounts; Flow of Funds

Costs of Issuance Fund. The Trust Agreement establishes a separate fund to be known as the "Costs of Issuance Fund," which shall be held by the Trustee in trust. The moneys in the Costs of Issuance Fund shall be used and withdrawn by the Trustee from time to time to pay the Costs of Issuance upon submission of a Written Request of the Agency stating the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against said fund. On the date six months following the Closing Date, or upon the earlier Written Request of the Agency stating that all known Costs of Issuance have been paid, all amounts, if any, remaining in the Costs of Issuance Fund shall be withdrawn therefrom by the Trustee and transferred to the Agency to be applied for its lawful purposes under the Law.

Construction Fund. The Trust Agreement establishes with the Trustee a special fund designated the "Construction Fund" into which the Trustee shall deposit the amount set forth in the Trust Agreement. The Trustee shall disburse moneys in the Construction Fund on such dates and in such amounts for Construction Costs, all as may be set forth in a Written Request of the Agency. In making such disbursements for the Construction Fund, the Trustee may conclusively rely upon the representations made by the Agency in such Written Request. If the Agency determines not to apply all moneys on deposit in the Construction Fund to Construction Costs, the Agency may deliver a Written Request to the Trustee to transfer any moneys remaining in the Construction Fund to any of the following accounts: (i) the 2003 Series B Bonds Interest Subaccount; (ii) the 2003 Series B Bonds Principal Subaccount (with instructions to apply such moneys to scheduled principal payment of the 2003 Series B Bonds or to the optional redemption of Series 2003 B Bonds); or (iii) to the Surplus Account. Moneys in the Construction Fund are not pledged to repayment of the Series 2003 Bonds.

Revenue Fund

Receipt and Deposit of Revenues in the Revenue Fund. All Revenues when and as received shall be received by the Agency or by the Trustee on behalf of the Agency in trust under the Trust Agreement for the benefit of the Holders and shall be deposited when and as received by the Agency or by the Trustee on behalf of the Agency in the Revenue Fund. All Revenues shall be accounted for through and held in trust in the Revenue Fund, and the Agency shall have no beneficial right or interest in any of the Revenues except only as provided in the Trust Agreement.

Within the Revenue Fund, the Trust Agreement directs the Trustee to establish the following accounts:

- (i) the 2003 Series A Bonds Revenue Account; and
- (ii) the 2003 Series B Bonds Revenue Account

All payments of Base Rental received by the Trustee under the Lease shall be deposited in the 2003 Series A Bonds Revenue Account and the 2003 Series B Bonds Revenue Account, as appropriate, based upon Schedule I and Schedule II to the Lease, as adjusted pursuant to the terms thereof.

Subject to the provisions of the Trust Agreement, all money in the Revenue Fund shall be set aside by the Trustee in the following respective special accounts and subaccounts within the Revenue Fund in the following order of priority under the Trust Agreement. In the event the Revenues received by the Trustee and deposited in any of the accounts created under the Trust Agreement at any time are insufficient to make required deposits in full into the subaccounts within any such account, the Trustee shall deposit such moneys transferred to such account on a pro rata basis into the various subaccounts within such account.

(a) **Interest Account**

(1) On or before the last Business Day of each March and September of each year, beginning on the last Business Day of September, 2003, the Trustee shall set aside from the respective account of the Revenue Fund and deposit in the respective subaccount of the Interest Account that an amount of money which, together with any money contained therein, is equal to the aggregate amount of interest becoming due and payable on all Outstanding 2003 Series A Bonds and 2003 Series B Bonds, respectively, on the next succeeding Interest Payment Date.

(2) All money in the Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying the interest on the applicable series of Bonds as it shall become due and payable (including accrued interest on any Bonds purchased or redeemed prior to maturity).

(3) With respect to any series of Additional Bonds, the Trustee (if so instructed by the Supplemental Trust Agreement providing for the issuance of such series of Additional Bonds) shall establish and maintain a separate subaccount within the Interest Account. Moneys in any such Interest Subaccount shall be applied by the Trustee to pay interest on such series of Additional Bonds.

(b) **Principal Account**

(1) On or before the last Business Day of each September of each year, beginning on the last Business Day of September, 2004, the Trustee shall set aside from the applicable account in the Revenue Fund and deposit into the applicable subaccount in the Principal Account an amount of money equal to the aggregate principal amount of all Outstanding 2003 Serial Bonds of the applicable series maturing on the next succeeding October 1. On or before the last Business Day of each September of each year, beginning on the last Business Day of September, 2003, the Trustee shall set aside from the Revenue Fund and deposit into the applicable subaccount of the Principal Account an amount of money equal to the aggregate principal amount of all sinking payments required to be made on the next succeeding October 1 into the respective sinking accounts for all Outstanding 2003 Term Bonds of the applicable series.

(2) No deposit need be made in the applicable subaccount of the Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal of all Outstanding 2003 Serial Bonds of the applicable series maturing by their terms on such October 1 plus the aggregate amount of all sinking account payments required to be made during the year ending on such October 1 for all Outstanding 2003 Term Bonds of the applicable series.

(3) With respect to any series of Additional Bonds, the Trustee (if so instructed by the Supplemental Trust Agreement providing for the issuance of such series of Additional Bonds) shall establish and maintain a separate subaccount within the Principal Account. Moneys in any such Principal Subaccount shall be applied by the Trustee to pay principal payments, including sinking payments for Term Bonds, with respect to such series of Additional Bonds.

(4) All money in the applicable subaccounts of the Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal of the applicable series of the Bonds as they shall become due and payable, except that any money in any sinking account payment shall be used and withdrawn by the Trustee only to purchase or to redeem or to pay Term Bonds for which such sinking account payment was created.

(c) **Reserve Account**

(1) The Trust Agreement establishes in the Reserve Account, the 2003 Series A Bonds Reserve Subaccount and the 2003 Series B Bonds Reserve Subaccount. On or before the last Business Day of each March and September of each year, beginning on the last Business Day of September, 2004, the Trustee shall set aside from the applicable account of the Revenue Fund and deposit in the applicable subaccount of the Reserve Account that amount of money which shall be required to maintain the applicable subaccount of the Reserve Account in the full amount of the Reserve Account Requirement for the applicable series of Bonds or such larger amount as shall be required to be maintained in the applicable subaccount of the Reserve Account by any Supplemental Trust Agreement. No deposit need be made in a subaccount of the Reserve Account so long as there shall be on deposit therein a sum equal to at least the amount required by this paragraph to be on deposit therein.

(2) In lieu of making the deposit to a subaccount of the Reserve Account in compliance with the provisions of the Trust Agreement, or in lieu of making such deposit in compliance with the provisions of the Trust Agreement, or in replacement of moneys then on deposit in the applicable subaccount of the Reserve Account (which shall be transferred by the Trustee to the Revenue Fund), the Agency may deliver to the Trustee at the sole cost and expense of the Agency an irrevocable letter of credit issued by a financial institution having unsecured debt obligations rated in one of the two highest rating categories by a nationally recognized rating agency, in an amount (together with an insurance policy or surety bond (as described in (3) below) securing an amount, plus moneys and Permitted Investments, on deposit in the applicable subaccount of the Reserve Account) equal to the applicable Reserve Account Requirement. Such letter of credit shall have a term no less than three (3) years. At least one (1) year prior to the stated expiration of such letter of credit, the Agency, shall deliver to the Trustee either (i) a replacement letter of credit, with substantially the terms as the previous letter of credit and issued by a financial institution having unsecured debt obligations rated in one of the two highest rating categories by a nationally recognized rating agency, (ii) an extension of the letter of credit for at least an additional year, or (iii) an insurance policy or surety bond satisfying the requirements of (3) below. Upon delivery of such replacement letter of credit, extended letter of credit, insurance policy, or surety bond, the Trustee shall deliver the expiring letter of credit, insurance policy or surety bond to or upon the order of the Agency. If the Agency fails to deposit a replacement letter of credit, extended letter of credit, insurance policy or surety bond with the Trustee, the Agency shall obtain lawfully available funds in order to make quarterly deposits with the Trustee so that an amount equal to the Reserve Account Requirement is on deposit in the applicable subaccount of the Reserve Account no later than the stated expiration date of the letter of credit. If a drawing is made on the letter of credit, the Agency shall make such payments as may be required by the terms of the letter of credit or any obligations related thereto (but no less than quarterly pro rata payments) so that the letter of credit shall, absent the delivery to the Trustee of an insurance policy or surety bond satisfying the requirements of (3) below) or the deposit in the applicable subaccount of the Reserve Account of an amount sufficient to increase the balance in the applicable subaccount of the Reserve Account to the applicable Reserve Account Requirement, be reinstated in the amount of such drawing within one year of the date of such drawing.

(3) In lieu of making a deposit to the applicable subaccount of the Reserve Account in compliance with the provisions of the Trust Agreement, or in lieu of making such deposit in compliance with the provisions of the Trust Agreement, or in replacement of moneys then on deposit in the applicable subaccount of the Reserve Account, the Agency may also deliver to the Trustee an insurance policy or surety bond securing an amount, together with moneys, Permitted Investments or letters of credit on deposit in the applicable subaccount of the Reserve Account, no less than the Reserve Account Requirement, issued by an insurance company whose unsecured debt obligations (or for which obligations secured by such insurance company's insurance policies) are rated in one of the two highest

rating categories by a nationally recognized rating agency. In the event that such insurance policy or surety bond for any reason lapses or expires, the Agency shall immediately implement subsection (i) or (iii) of the third sentence of the preceding paragraph or make the required deposits to the Reserve Account. The Agency shall provide written notice to any nationally recognized rating agency then rating the Bonds if a letter of credit, insurance policy or surety bond is delivered to the Trustee pursuant to the provisions of the Trust Agreement. If the Agency exercises its option to substitute an insurance policy or surety bond as set forth above for the moneys held by the Trustee in the applicable subaccount of the Reserve Account, the moneys then on deposit in the applicable Subaccount of the Reserve Account shall be available to be withdrawn by the Agency and used by the Agency for any purpose permitted by the Law, for other capital expenditures of the Agency, as applicable, whether or not related to the Demised Premises, so long as in the case of moneys so withdrawn from the 2003 Series A Bonds Reserve Subaccount, such use will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the 2003 Series A Bonds.

(4) All money in the Reserve Account and the subaccounts therein shall be used and withdrawn by the Trustee solely for the purpose of replenishing the applicable subaccount of the Interest Account or the Principal Account in such order, in the event of any deficiency at any time in either of such accounts or subaccounts therein for the purpose of paying the principal of, redemption premium, if any, or interest on the applicable series of Bonds or for the retirement of all the Bonds then Outstanding. So long as the Agency is not in default under the Trust Agreement, any amount in the applicable subaccount of the Reserve Account in excess of the amount required by the Trust Agreement to be on deposit therein may be withdrawn from the applicable subaccount of the Reserve Account and deposited in the Revenue Fund.

(d) **Surplus Account.** On or before October 2 of each year, beginning October 2, 2003, the Trustee shall deposit in the Surplus Account all money remaining in the Revenue Fund after any deposit required by the Trust Agreement to the Rebate Fund and the deposits required by subsections (a), (b) and (c) above of the Trust Agreement have been made. Thereafter, on October 15 of each year, commencing October 15, 2003, provided the Trustee shall not have received any notice that the Agency is in default under the Trust Agreement or that the Department is in default under the Lease, all moneys on deposit in the Surplus Account on such date shall be released by the Trustee and transferred to the Agency for use by the Agency for any lawful purpose under the Law.

Final Surplus

After (a)(i) payment or redemption or provision for payment or redemption of all amounts due with respect to the Bonds and payment of all fees and expenses to the Trustee, or (ii) defeasance of the Bonds pursuant to the Trust Agreement, and (b) the transfer of any additional amounts required to be deposited into the Rebate Fund, any amounts remaining in any of the funds, accounts or subaccounts established under the Trust Agreement (except for the Rebate Fund) and not required for such purposes shall after payment of any amounts due to the Trustee and payment of any amounts due to the Agency as evidenced by a Certificate of the Agency, be remitted to the Agency and used for any lawful purpose under the Law, and released from the pledge and lien created under the Trust Agreement.

Additional Rental

In the event the Trustee receives Additional Rental pursuant to the Lease, the Trustee shall establish a separate fund for such Additional Rental and deposit any such amounts therein and such Additional Rental shall be applied by the Trustee solely to the payment of any costs in respect of which such Additional Rental was received, and shall not be commingled in any way with any other funds received by the Trustee pursuant to the Lease or the Trust Agreement.

Deposit and Investment of Moneys in Accounts and Funds

Moneys in the Interest Account (and the subaccounts therein), the Principal Account (and the subaccounts therein), the Reserve Account (and the subaccounts therein), the Surplus Account, the Administrative Expense Account and the Costs of Issuance Fund shall be invested by the Trustee in Permitted Investments as specified by the Agency and shall be promptly confirmed in writing by the Agency with the Trustee within at least one (1) Business Day. In the absence of any such direction provided by the Agency, the Trustee shall invest any such moneys in Permitted Investments described in clause (D) of the definition thereof which by their terms mature prior to the date on which such moneys are required to be paid out under the Trust Agreement.

Obligations purchased as an investment of moneys in any fund shall be deemed to be part of such fund or account. Whenever in the Trust Agreement any moneys are required to be transferred by the Agency to the Trustee, such transfer may be accomplished by transferring a like amount of Permitted Investments which by their terms mature prior to the date on which such moneys are required to be paid out under the Trust Agreement. All interest or gain derived from the investment of amounts in any of the funds or accounts (and subaccounts therein) established under the Trust Agreement (other than with respect to funds held by the Agency) shall be retained in the respective funds and accounts to be used for the purposes thereof; provided, however, that all interest or gain from the investment of amounts in the respective subaccounts of the Reserve Account shall be deposited by the Trustee in the Interest Account, but only to the extent that the amount remaining in the respective subaccounts of the Reserve Account following such deposit is equal to the Reserve Requirement for the applicable series of Bonds.

The Agency acknowledges that to the extent regulations of the Controller of the Currency or other applicable regulatory entity grant the Agency the right to receive brokerage confirmations of security transactions as they occur, the Agency specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Agency periodic cash transaction statements which include detail for all investment transactions made by the Trustee under the Trust Agreement.

Moneys credited to any fund or account (or subaccount therein) under the Trust Agreement which are uninvested pending disbursement or receipt of proper investment directions or as directed by the Agency as provided therein, may be deposited to and held in a non-interest bearing demand deposit account established with the commercial banking department of the Trustee or any bank affiliated with the Trustee.

The Trustee may make any investments under the Trust Agreement through its own bond or investment department or trust investment department, or those of its parent or any affiliate. The Trustee or any of its affiliates may act as sponsor, advisor or manager in connection with any investments made by the Trustee under the Trust Agreement.

Issuance of Additional Bonds

Conditions for the Issuance of Additional Bonds. The Agency may at any time issue Additional Bonds payable from the Revenues as provided in the Trust Agreement and secured by a pledge of and charge and lien upon the Revenues as provided herein equal to the pledge, charge and lien securing the Outstanding Bonds theretofore issued under the Trust Agreement, but only subject to the following specific conditions, which are conditions precedent to the issuance of any such Additional Bonds:

(a) The Agency shall be in compliance with all agreements and covenants contained in the Trust Agreement.

(b) The issuance of such Additional Bonds shall have been authorized pursuant to the Law and shall have been provided for by a Supplemental Trust Agreement which shall specify the following:

(1) The purpose for which such Additional Bonds are to be issued; provided that such Additional Bonds shall be applied solely for the purposes of (i) financing or refinancing the completion of and/or acquisition, installation and construction of additions, betterments, extensions or improvements to the Demised Premises, including payment of all costs incidental to or connected with such financing, and/or (ii) refunding any Bonds then Outstanding, including payment of all costs incidental to or connected with such refunding;

(2) The authorized principal amount and designation of such Additional Bonds;

(3) The date and the maturity dates of and the sinking account payment dates, if any, for such Additional Bonds; provided that (i) each maturity date shall fall upon October 1, (ii) all such Additional Bonds of like maturity shall be identical in all respects, except as to number and denomination, (iii) serial maturities for Serial Bonds or sinking account payments for Term Bonds, or any combination thereof, shall be established to provide for the retirement of such Additional Bonds on or before their respective maturity dates and (iv) the Annual Debt Service for each Fiscal Year after the issuance of such Additional Bonds shall be as nearly equal as practicable, taking into account the useful life of the additions or improvements, if any, to the Demised Premises so financed;

(4) The interest payment date for such Additional Bonds; provided that the interest payment dates shall be on April 1 and October 1 in each year, except that the first interest payment date may be on either April 1 or October 1 which occurs not more than twelve (12) months following the date of issuance of the Additional Bonds;

(5) The denomination or denominations of and method of numbering such Additional Bonds;

(6) The redemption premium, if any, and the redemption terms, if any, for such Additional Bonds;

(7) The amount, if any, to be deposited from the proceeds of sale of such Additional Bonds in the Interest Account;

(8) The amount, if any, to be deposited from the proceeds of sale of such Additional Bonds in the applicable subaccount of the Reserve Account; provided that the Reserve Account shall be increased at or prior to the time such Additional Bonds become Outstanding to an amount at least equal to the Reserve Account Requirement on all Bonds to be Outstanding after the issuance of such Additional Bonds, and provided further that an amount at least equal to the Reserve Account Requirement shall thereafter be maintained in the Reserve Account; and provided further that such deposit may be in the form of an irrevocable letter of credit, insurance policy or surety bond as provided for in the Trust Agreement;

(9) The amount, if any, to be deposited from the proceeds of sale of such Additional Bonds in the funds and accounts established under the Trust Agreement;

(10) The forms of such Additional Bonds; and

(11) Such other provisions as are necessary or appropriate and not inconsistent with the Trust Agreement.

(c) The Base Rental payable by the Department under the Lease shall be an amount at least sufficient to pay the interest on and principal of such Additional Bonds as the same become due and accompanied by a Certificate of the Agency or the Department to the effect that such Base Rental is consistent with the fair rental value for the Demised Premises.

Nothing contained herein shall limit the issuance of any lease revenue bonds of the Agency payable from the Revenues and secured by a pledge of and charge and lien upon the Revenues if after the issuance and delivery of such lease revenue bonds none of the Bonds theretofore issued under the Trust Agreement will be Outstanding.

Procedure for the Issuance of Additional Bonds. At any time after the sale of any Additional Bonds in accordance with the Act, the Agency shall execute such Additional Bonds for issuance under the Trust Agreement and shall deliver them to the Trustee, and thereupon such Additional Bonds shall be authenticated and delivered by the Trustee to the purchaser thereof upon the Written Request of the Agency, but only upon receipt by the Trustee of the following documents or money or securities, all of such documents dated or certified, as the case may be, as of the date of delivery of such Additional Bonds by the Trustee (unless the Trustee shall accept any of such documents bearing a prior date):

(a) A certified copy of the Supplemental Trust Agreement authorizing the issuance of such Additional Bonds;

(b) A Written Request of the Agency as to the delivery of such Additional Bonds;

(c) An Opinion of Counsel to the effect that (1) the Agency has the right and power under the Act to execute and deliver the Supplemental Trust Agreement and the Supplemental Trust Agreement has been duly and lawfully executed and delivered by the Agency, is in full force and effect and is valid and binding upon the Agency (except as enforcement may be limited by bankruptcy, insolvency, reorganization and other similar laws relating to the enforcement of creditors' rights and by equitable principles), (2) the Supplemental Trust Agreement creates the valid pledge of and charge and lien upon the Revenues which it purports to create as provided therein, subject to the application thereof to the purposes and on the conditions permitted by the Trust Agreement, (3) such Additional Bonds are valid and binding special obligations of the Agency (except as enforcement may be limited by bankruptcy, insolvency, reorganization and other similar laws relating to the enforcement of creditors' rights and by equitable principles) and entitled to the benefits of the Act and hereof, and such Additional Bonds have been duly and validly authorized, executed, issued and delivered in accordance with the Act and the Trust Agreement, (4) the amendment to the Lease required by the Trust Agreement has been duly authorized, executed and delivered, and (5) the delivery of such Additional Bonds will not have an adverse effect on the exclusion from gross income for federal income tax purposes of the interest on the 2003 Series A Bonds;

(d) A Certificate of the Agency containing such statements as may be reasonably necessary to show compliance with the conditions for the issuance of such Additional Bonds contained herein; and

(e) Such further documents, money or securities as are required by the provisions of the Supplemental Trust Agreement providing for the issuance of such Additional Bonds.

Insurance

The Agency will maintain or cause to be maintained fire, lightning and extended coverage insurance, public liability insurance and rental interruption insurance with respect to the Project, all as provided in the Lease.

Application of Insurance Proceeds. If the Premises or any portion thereof shall be damaged or destroyed, the Agency shall make an election either to redeem Bonds or to repair or replace the Demised Premises or affected portion thereof in accordance with the provisions of and subject to the conditions set forth in the Lease. Notwithstanding the provisions of the Lease, the Agency shall, within 90 days of the occurrence of the event of damage or destruction, notify the Trustee and the Department in writing of its election. The proceeds of any insurance (other than any rental interruption insurance), including the proceeds of any self-insurance, received on account of any damage or destruction of the Demised Premises or a portion thereof shall as soon as possible be deposited with the Trustee and be held by the Trustee in a special account and made available for and, to the extent necessary, shall be applied to redeem Bonds in accordance with the Trust Agreement or applied to the cost of repair or replacement of the Demised Premises or the affected portion thereof, in either case upon receipt of a Written Request of the Agency. The Trustee may conclusively rely on any such Written Request. Pending such application, such proceeds may be invested by the Trustee as directed by the Agency in Permitted Investments that mature not later than such times that such moneys are expected to be needed.

The proceeds of any insurance, including the proceeds of any self-insurance, remaining after the property which was damaged or destroyed is restored to and made available to the Department in substantially the same condition as that which existed prior to the damage or destruction or the redemption, or provision for the redemption, of Bonds as required by the Trust Agreement, in each case as evidenced by a Written Certificate of the Agency to such effect, shall be deposited into the Accounts of the Reserve Fund to the extent that the amount therein is less than the Reserve Requirement. Any amounts not required to be so deposited into the Reserve Fund pursuant to the preceding sentence shall, if there is first delivered to the Trustee a Certificate of the Agency to the effect that the annual fair rental value of the Demised Premises after such damage or destruction, and after any repairs or replacements made as a result of such damage or destruction, is at least equal to the maximum amount of Base Rental payments becoming due under the Lease in the then current Lease Year or any subsequent Lease Year, be paid to the Agency to be used for any lawful purpose under the Law. If the Agency cannot deliver the certificate described in the preceding sentence, then any excess amounts shall be transferred to the Revenue Fund and used to redeem Bonds pursuant to the Trust Agreement.

Eminent Domain. If the Demised Premises or any portion thereof shall be taken by eminent domain proceedings (or sold to a government threatening to exercise the power of eminent domain) then the provisions set forth in the Lease shall apply. Notwithstanding the provisions of the Lease, the Agency shall, within 90 days of the conclusion of the eminent domain proceeding, notify the Trustee and the Department in writing of whether or not the Demised Premises will be replaced or the Bonds redeemed. The proceeds of any condemnation award shall as soon as possible be deposited with the Trustee and be held by the Trustee in a special account and made available for and, to the extent necessary, shall be applied to redeem Bonds in accordance with the Trust Agreement or applied to the cost of replacement of the Demised Premises, in either case upon receipt of a Written Request of the Agency. The Trustee may conclusively rely on any such Written Request. Pending such application, such proceeds may be invested by the Trustee as directed by the Agency in Permitted Investments that mature not later than such times that such moneys are expected to be needed.

The proceeds of any condemnation award remaining after the Demised Premises have been replaced by property available to the Department under the Lease in substantially the same condition and fair rental value as that which existed prior to the eminent domain proceedings or the redemption, or provision for the redemption, of Bonds as required by the Trust Agreement, in each case as evidenced by a Written Request of

the Agency to such effect, shall be deposited into the Accounts of the Reserve Fund to the extent that the amount therein less than the Reserve Requirement. Any amounts not required to be so deposited into the Reserve Fund pursuant to the preceding sentence shall, if there is first delivered to the Trustee a Certificate of the Agency to the effect that the annual fair rental value of the replacement Demised Premises is at least equal to the maximum amount of Base Rental payments becoming due under the Lease in the then current Lease Year or any subsequent Lease Year, be paid to the Agency to be used for any lawful purpose under the Law. If the Agency cannot deliver the certificate described in the preceding sentence, then any excess amounts shall be transferred to the Revenue Fund and used to redeem Bonds pursuant to the Trust Agreement.

Title Insurance. Proceeds of any policy of title insurance received by the Trustee in respect of the Demised Premises or any portion thereof shall be applied and disbursed by the Trustee as follows:

(i) If the Agency (with the written consent of the Department) determines that the title defect giving rise to such proceeds has not materially affected the Department's right to the use and possession of the Demised Premises and will not result in an abatement of Base Rental payable by the Department under the Lease, upon the Written Request of the Agency to the Trustee such proceeds shall be deposited into the Accounts of the Reserve Fund to the extent that the amount therein is less than the Reserve Requirement. Amounts not required to be so deposited shall, if there is first delivered to the Trustee a Certificate of the Agency to the effect that the annual fair rental value of the Demised Premises, notwithstanding the title defect for which the payment was made, is at least equal to the maximum amount of Base Rental becoming due under the Lease in the then current Lease Year or any subsequent Lease Year, be paid to the Agency to be used for any lawful purpose under the Law. If the Agency cannot deliver the certificate described in the preceding sentence, then such amounts shall be transferred to the Redemption Account of the Bond Fund and used to redeem Bonds pursuant to the Trust Agreement.

(ii) If any portion of the Demised Premises has been affected by such title defect, and if the Agency determines that such title defect will result in an abatement of Base Rental payable by the Department under the Lease, then either (a) the Agency shall provide a Written Request of the Agency to the Trustee to disburse to or upon the order of the Agency the insurance proceeds to remove the title defect, or (b) the Trustee shall, if not notified in writing by the Agency within 90 days of the receipt by the Trustee of the insurance proceeds that the Agency will use the proceeds to remove the title defect, deposit such proceeds in the Revenue Fund, and such proceeds shall be applied to the redemption of Bonds in the manner provided in the Trust Agreement.

Removal or Resignation of Trustee

The Agency may with the consent of the Insurer, so long as the Agency is not in default under the Trust Agreement, remove the trustee initially appointed and any successor thereto and may appoint a successor or successors thereto by an instrument in writing; provided that any such successor shall be a bank or trust company doing business and having a principal office in San Francisco or Los Angeles, California, having a combined capital (exclusive of borrowed capital) and surplus of at least one hundred million dollars (\$100,000,000) and subject to supervision or examination by federal or state authority. If such bank or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for such purpose the combined capital and surplus of such bank or trust company shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. The Trustee, or any successor trustee, may at any time resign by giving written notice of such resignation to the Insurer and the Agency and by mailing to the Holders notice of such resignation. Upon receiving such notice of resignation, the Agency shall promptly appoint a successor trustee by an instrument in writing. Any removal or resignation of a trustee and appointment of a successor trustee shall become effective only upon the acceptance of appointment by the successor trustee. If, within thirty (30)

days after notice of the removal or resignation of the Trustee, or any successor trustee, no successor trustee shall have been appointed and shall have accepted such appointment, the removed or resigning trustee may petition any court of competent jurisdiction for the appointment of a successor trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor trustee having the qualifications required by the Trust Agreement.

Amendment of Trust Agreement

The Trust Agreement and the rights and obligations of the Agency and of the Holders may be amended at any time by a Supplemental Trust Agreement which shall become binding when the written consents of the Insurer and the Holders of sixty percent (60%) in aggregate principal amount of the Bonds then Outstanding, exclusive of Bonds disqualified as provided in the Trust Agreement, are filed with the Trustee. No such amendment shall (1) extend the maturity of or reduce the interest rate on or otherwise alter or impair the obligation of the Agency to pay the principal of, redemption premium, if any, or interest on any Bond at the time and place and at the rate and in the currency provided herein without the express written consent of the Holder of such Bond, or (2) permit the creation by the Agency of any pledge of or charge or lien upon the Revenues as provided in the Trust Agreement superior to or on a parity with the pledge, charge and lien created by the Trust Agreement for the benefit of the Bonds, or (3) reduce the percentage of Bonds required for the written consent to any such amendment.

The Trust Agreement and the rights and obligations of the Agency and of the Holders may also be amended at any time by a Supplemental Trust Agreement which shall become binding upon execution and delivery thereof without the consent of any of the Holders, but only to the extent permitted by law and after receipt of an approving Opinion of Counsel and only for any one or more of the following purposes:

(a) to add to the agreements and covenants required herein to be performed by the Agency other agreements and covenants thereafter to be performed by the Agency which shall not materially adversely affect the interests of the Holders, or to surrender any right or power reserved herein to or conferred herein on the Agency;

(b) to make such provisions for the purpose of curing any ambiguity, inconsistency or omission, or of correcting, curing or supplementing any defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement which the Agency may deem desirable or necessary and not inconsistent with the Trust Agreement and which shall not materially adversely affect the interests of the Holders; or

(c) to provide for the issuance of any Additional Bonds and to provide the terms of such Additional Bonds, subject to the conditions and upon compliance with the procedure set forth in the Trust Agreement.

Any provision of the Trust Agreement expressly recognizing or granting rights in or to the Insurer may not be amended in any manner which affects the rights of the Insurer under the Trust Agreement without the prior written consent of the Insurer.

Covenants of The Agency

Punctual Payment and Performance. The Agency will punctually pay the principal of, redemption premium, if any, and interest to become due on every Bond issued hereunder in strict conformity with the terms of the Trust Agreement and of the Bonds, and will faithfully observe and perform all the agreements and covenants contained in the Trust Agreement and in the Bonds.

Against Encumbrances. The Agency will not make any pledge of or place or permit to be placed any charge or lien upon the Demised Premises or any part thereof or upon the Revenues except as provided in the Trust Agreement, and will not issue any bonds, notes or obligations payable from the Revenues or secured by a pledge of or charge or lien upon the Revenues except the Bonds.

Against Sale or Other Disposition of the Demised Premises. The Agency will not sell or otherwise dispose of the Demised Premises or any part thereof essential to its proper operation or to the maintenance of the Revenues. The Agency will not enter into any agreement which impairs the operation of the Demised Premises or any part thereof necessary to secure adequate Revenues for the payment of the principal of, redemption premium, if any, and interest on the Bonds, or which would otherwise impair the rights of the Holders with respect to the Revenues or the operation of the Demised Premises. Any real or personal property constituting part of the Demised Premises which has become nonoperative or which is not needed for the efficient and proper operation of the Demised Premises or any material or equipment constituting part of the Demised Premises which has become worn out may be sold at not less than the market value thereof if such sale will not reduce the Revenues and if the net proceeds of such sale are treated as Revenues and applied in the manner provided in the Trust Agreement.

Tax Covenants: Rebate Fund.

(a) In addition to the other accounts created pursuant to the Trust Agreement, there is also created a Rebate Fund. There shall be deposited in the Rebate Fund such amounts as are required to be deposited therein pursuant to the Tax Certificate. All money at any time deposited in the Rebate Fund shall be held by the Trustee in trust, to the extent required to satisfy the Rebate Requirement (as defined in the Tax Certificate), for payment to the United States of America.

(b) The Agency shall not use or permit the use of any proceeds of the 2003 Bonds or any funds of the Agency, directly or indirectly, in any manner, and shall not take or omit to take any action, that would cause any of the 2003 Series A Bonds to be treated as an obligation not described in Section 103(a) of the Internal Revenue Code.

(c) Without limiting the generality of (b) above, the Agency specifically covenants to comply with the provisions and procedures of the Tax Certificate.

Maintenance and Operation of the Demised Premises. The Agency will maintain and preserve or cause to be maintained and preserved the Demised Premises in good order, condition and repair at all times and will operate the Demised Premises or cause the Demised Premises to be operated in an efficient and economical manner for its intended purposes under the Lease.

Payment of Claims. The Agency will pay and discharge or cause to be paid and discharged solely from the Revenues any and all lawful claims for labor, materials or supplies which, if unpaid, might become a legal charge or lien upon the Demised Premises or the Revenues or any part thereof or upon any funds under the control of the Agency or the Trustee superior to or on a parity with the charge and lien upon the Revenues securing the Bonds, or which might impair the security of the Bonds.

Payment of Taxes and Compliance with Governmental Regulations. The Agency will pay and discharge or cause to be paid and discharged solely from the Revenues all applicable taxes, assessments and other governmental charges that may be levied, assessed or charged upon the Demised Premises or any part thereof or upon the Revenues or any part thereof promptly as and when the same shall become due and payable. The Agency will duly observe and conform with all valid applicable regulations and requirements of any governmental authority relative to the operation of the Demised Premises or any part thereof, but the

Agency shall not be required to comply with any such regulations or requirements so long as the application or the validity thereof shall be contested in good faith.

Events of Default And Remedies

Defaults. The following events shall be events of default:

(a) if default shall be made in the due and punctual payment of the interest on any Bond when and as the same shall become due and payable;

(b) if default shall be made in the due and punctual payment of the principal of or redemption premium, if any, on any Bond when and as the same shall become due and payable, whether at maturity as therein expressed or by proceedings for redemption; or

(c) if default shall be made by the Agency in the performance of any of the other agreements or covenants required herein to be performed by the Agency, and such default shall have continued for a period of sixty (60) days after the Agency shall have been given notice in writing of such default by the Trustee.

Acceleration of Maturities. Upon the occurrence and continuance of an event of default, the Trustee may, with the consent of the Insurer, or shall upon the written request of the Holders of not less than twenty-five percent (25 %) in aggregate principal amount of the Bonds then Outstanding, with the consent of the Insurer by notice in writing to the Agency, declare the principal of all Bonds then Outstanding and the interest accrued thereon to be due and payable immediately, and upon any such declaration the same shall become due and payable, anything contained in the Trust Agreement or in the Bonds to the contrary notwithstanding and the Trustee, upon provision for indemnification from the holders satisfactory to it, shall exercise the remedies set forth in the Trust Agreement and in the Lease (if there has been a default under the Lease).

The preceding paragraph, however, is subject to the following conditions: (i) if, at any time after the principal of the Bonds then Outstanding shall have been so declared due and payable and before any judgment or decree for the payment of the money due shall have been obtained or entered, and (ii) if each of the following conditions has occurred or will occur: (a) the Department or the Agency shall deposit with the Trustee a sum sufficient to pay all matured interest on all the Bonds and all principal of the Bonds matured prior to such declaration, with interest at the rate borne by such Bonds on such overdue interest and principal, and the reasonable expenses of the Trustee, and (b) any and all other defaults known to the Trustee (other than in the payment of interest on and principal of the Bonds due and payable solely by reason of such declaration) shall have been made good or cured, then and in every such case the Holders of not less than twenty-five percent (25 %) in aggregate principal amount of Bonds then Outstanding, with the consent of the Insurer by written notice to the Agency and to the Trustee, may on behalf of the Holders of all the Bonds then Outstanding rescind and annul such declaration and its consequences; but no such rescission and annulment shall extend to or shall affect any subsequent default or shall impair or exhaust any right or power consequent thereon.

Application of Funds Upon Acceleration

All moneys in the accounts and funds provided in the Trust Agreement upon the date of the declaration of acceleration by the Trustee as provided in the Trust Agreement and all Revenues (other than Revenues on deposit in the Rebate Fund) thereafter received by the Agency under the Trust Agreement shall be transmitted to the Trustee and shall be applied by the Trustee in the following order:

First, to the payment of the costs and expenses of the Trustee in providing for the declaration of such event of default and to the payment of the costs and expenses of the Trustee, if any, in carrying out the provisions of the Trust Agreement, including without limitation those of its attorneys and advisors; and

Second, upon presentation of the several Bonds, and the stamping thereon of the amount of the payment if only partially paid or upon the surrender thereof if fully paid, to the payment of the whole amount then owing and unpaid upon the Bonds for interest and principal with interest on the overdue interest and principal at the rate borne by such Bonds. If such money shall be insufficient to pay in full the whole amount so owing and unpaid upon the Bonds, then to the payment of such interest, principal and interest on overdue interest and principal without preference or priority among such interest, principal and interest on overdue interest and principal ratably to the aggregate of such interest, principal and interest on overdue interest and principal.

Non-Disturbance of Commercial Tenants. Upon the occurrence of an Event of Default the Trustee may enforce the rights of the Agency under the Lease, including the right to re-enter and relet the Premises. See "The Lease- Defaults and Remedies" herein. However, the Trustee in this connection has agreed not to disturb the tenants of the ground floor of the Demised Premises which have entered into a pre-approved form of non-disturbance agreement with the Agency. Basically, the non-disturbance agreement provides that such tenant will be allowed to continue to occupy its space so long as it is not in default under the terms of its lease.

Other Remedies of Holders

Any Holder shall have the right for the equal benefit and protection of all Holders similarly situated:

(a) by mandamus or other suit or proceeding at law or in equity to enforce his or her rights against the Agency or any member, officer or employee of the Agency, and to compel the Agency or any such member, officer or employee to perform and carry out his or her duties under the Act and the agreements and covenants with the Holders contained in the Trust Agreement;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Holders; or

Consent of the Insurer Upon Default

Anything in the Trust Agreement to the contrary notwithstanding, upon the occurrence and continuance of an event of default as defined herein, the Insurer shall be entitled to control and direct the enforcement of all rights and remedies granted to the Bondholders or the Trustee for the benefit of the Bondholders under the Trust Agreement, including, without limitation: (i) the right to accelerate the principal of the Bonds as described in the Trust Agreement, and (ii) the right to annul any declaration of acceleration, and the Insurer shall also be entitled to approve all waivers of events of default.

Remedies Not Exclusive

No remedy herein conferred upon or reserved to the Holders or the Trustee is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given under the Trust Agreement or now or hereafter existing at law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by the Act or any other law.

Discharge of Trust Agreement

(a) If the Agency shall pay or cause to be paid or there shall otherwise be paid to the Holders of all Outstanding Bonds the principal thereof, redemption premium, if any, and interest thereon at the times and in the manner stipulated in the Trust Agreement, then the Holders of such Bonds shall cease to be entitled to the pledge of and charge and lien upon the Revenues as provided in the Trust Agreement, and the agreements, covenants and other obligations of the Agency to the Holders of such Bonds under the Trust Agreement shall thereupon cease, terminate and become void and be discharged and satisfied; provided, however, that the following agreements, covenants and other obligations shall not be discharged and satisfied until such Bonds are paid in full: (i) the obligation of the Trustee to pay or cause to be paid to the Holders all sums due with respect to the Bonds from such moneys or investments that may have been set aside for such purposes in accordance with the Trust Agreement; (ii) the obligation of the Trustee to register, transfer and exchange Bonds pursuant to the provisions of the Trust Agreement; and (iii) the obligation of the Agency to pay the amounts owing to the Trustee under the Trust Agreement. If the Agency shall discharge the Bonds, as provided above, the Trustee shall execute and deliver to the Agency all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee shall pay over or deliver to the Agency all money or securities held by him pursuant hereto which are not required for the payment of the principal of, redemption premium, if any, and interest on such Bonds.

(b) Any Outstanding Bonds shall, prior to the maturity date or redemption date thereof, be deemed to have been paid within the meaning of and with the effect expressed in subsection (a) above if:

(1) in case any of such Bonds are to be redeemed on any date prior to their maturity date, the Agency shall have given to the Trustee, in form satisfactory to it, irrevocable instructions to mail a notice of redemption of such Bonds in accordance with the provisions of the Trust Agreement;

(2) there shall have been deposited with the Trustee either:

(i) money in an amount which shall be sufficient and/or;

(ii) Permitted Investments of the type described in clause (i) or clause (ii) of the definition of Permitted Investments and which are not subject to redemption prior to maturity except by the holder thereof (including any such Permitted Investments issued or held in book-entry form on the books of the Department of the Treasury of the United States of America) or tax-exempt securities rated AAA or its equivalent by a nationally recognized securities rating agency, including Standard & Poor's Ratings Group, Moody's Investors Service and Fitch Investors Service, Inc., the interest on and principal of which when paid will provide money which, together with the money, if any, deposited with the Trustee at the same time, shall be sufficient;

to pay when due the interest to become due on such Bonds on and prior to the maturity date or redemption date thereof, as the case may be, and the principal of and redemption premium, if any, on such Bonds; and,

(3) in the event such Bonds are not by their terms subject to redemption within the next succeeding sixty (60) days, the Agency shall have given the Trustee, in form satisfactory to it, irrevocable instructions to mail, as soon as practicable, a notice to the Holders of such Bonds that the deposit required by clause (2) above has been made with the Trustee and that such Bonds are deemed to have been paid in accordance with the provisions of the

Trust Agreement and stating the maturity date or redemption date upon which money is to be available for the payment of the principal of and redemption premium, if any, on such Bonds.

(c) Notwithstanding anything in the Trust Agreement to the contrary, in the event that the principal and/or interest due on the Bonds shall be paid by the Insurer pursuant to the Municipal Bond Insurance Policy, the Bonds shall remain Outstanding for all purposes, and be defeased or otherwise satisfied and not be considered paid by the Agency, and the assignment and pledge of the Revenues and all covenants, agreements and other obligations of the Agency to the Bondholders shall continue to exist and shall run to the benefit of the Insurer, and the Insurer shall be subrogated to the rights of such Bondholders.

THE LEASE

Term

The Lease commenced on the date of recordation of the Lease in the office of the County Recorder of the County of Riverside and shall terminate on the earlier of (1) payment in full and retirement of the Bonds; (2) the purchase by the Department of the Agency's right, title and interest in the Premises; or (3) at midnight on October 1, 2024. In the event that the Bonds have not been fully paid and retired as of October 1, 2024, the Lease will remain in effect until the Bonds are retired but in no event beyond October 1, 2034.

Rental

Base Rental. Under the Lease, the Department promises to pay Base Rental to the Agency as set forth in schedules to the Lease. Such Base Rental shall be due and payable at least one Business Day prior to April 1 and October 1 in each year. Each such payment of Base Rental shall be for the use of the Premises for the six-month period ending on the first day of each April or October, as applicable.

Application of Rental Payments. Payments of Base Rental and Additional Rental for each rental payment period during the term of the Lease shall constitute the total rental for such rental payment period, and shall be paid by the Department in each rental payment period for and in consideration of the use and possession, and the continued quiet enjoyment, of the Premises during each such rental payment period for which such rental is paid. The parties to the Lease have agreed and determined that such total rental represents the fair rental value of the Premises. In making such determination, consideration has been given to the costs of the acquisition and improvement of the Premises, other obligations of the parties under the Lease, the uses and purposes which may be served by the Premises and the benefits therefrom which will accrue to the Department and the general public.

Each installment of rental payable under the Lease shall be paid in lawful money of the United States of America to or upon the order of the Agency in Riverside, California, or such other place as the Agency shall designate. Pursuant to the Trust Agreement, the Agency has designated that the Trustee shall reserve the Base Rental Payments from the Department. Any such installment of rental accruing under the Lease which shall not be paid when due shall be treated pursuant to California Government Code Section 926.17, or, if not applicable, shall bear interest at the legal rate of interest per annum at which judgments for money in the State of California bear interest from the date when the same is due under the Lease until the same shall be paid. Notwithstanding any dispute between the Agency and the Department, the Department shall make all rental payments when due without deduction or offset of any kind and shall not withhold any rental payments pending the final resolution of such dispute.

All rental payments received pursuant to the Lease shall be applied first to the Base Rental due thereunder and thereafter to all Additional Rental due thereunder, but no such application of any payments which are less than the total rental due and owing shall be deemed a waiver of any default under the Lease.

Abatement. Except to the extent of (i) amounts held by the Trustee and which are not attributable to Base Rental which has been abated and in the Reserve Account, (ii) amounts received in respect of rental interruption insurance or Liquidated Damages, if any, and (iii) amounts, if any, otherwise legally available to the Department or the Agency and deposited with the Trustee for the purpose of making payments in respect of the Bonds, the rental shall be abated during any period in which, by reason of any material damage or destruction or condemnation of the Premises or any portion thereof, there is substantial interference with the use and possession of the Premises or any portion thereof by the Department. In such event, the Department shall give written notice to the Agency and the Trustee detailing the event, the nature of the interference and the time at which such proportionate abatement of rental began. The amount of rental abatement shall be such that the resulting rental payments in any Lease Year during which such interference continues, excluding any amounts described in clauses (i), (ii) or (iii) above, do not exceed the fair rental value of the portions of the Premises as to which such damage, destruction or condemnation does not substantially interfere with the use and right of possession of the Department, as evidenced by a certificate of an officer of the Department approved by the Agency. Such abatement shall continue for the period commencing with the date of interference resulting from such damage, destruction or condemnation and ending when such use and possession are restored and as a result the Premises are again in a fully tenantable condition. In the event of any such damage, destruction or condemnation, the Lease shall continue in full force and effect, except as set forth therein. The resulting rental payments shall be applied first to the payment of Base Rental and second to the payment of Additional Rental. The Department waives the benefits of California Civil Code Sections 1932(2) and 1933(4) and any and all other rights to terminate the Lease by virtue of any such damage or destruction.

Covenants of the Department

Appropriation. The Department covenants to take such action within its power as may be necessary to include all such rental payments due under the Lease in its annual budgets and to make the necessary annual allocations for all such rental payments. Upon written request, the Department will furnish to the Agency and the Trustee copies of each annual budget submitted by the Governor of the State of California to the California State Legislature within 10 days after such submission.

Insurance. (a) The Department will maintain or cause to be maintained fire, lightning and extended coverage insurance on the Premises (and earthquake insurance if the premiums, coverage and availability are reasonable as determined in good faith by the Department), in an amount equal to 100% of the then current replacement cost of the Premises excluding the then value of the Site as unimproved (except that such insurance may be subject to deductible clauses of not to exceed \$500,000 for anyone loss).

(b) In the event of any damage to or destruction of the Premises caused by the perils covered by the insurance required above, the proceeds of such insurance shall be utilized, in the discretion of the Agency, either (i) to redeem Outstanding Bonds, to the extent possible and in accordance with the provisions of the Indenture, but only if the Base Rental payments due after such a redemption would be sufficient to retire the Bonds which will remain Outstanding in accordance with their terms, and provided that, in the event the Premises can be repaired or rebuilt within the period covered by rental interruption insurance as provided in the Lease, and if the Agency shall have sufficient funds from the proceeds of insurance or otherwise for the necessary repairing or rebuilding, the Agency shall not redeem Outstanding Bonds as described in this clause (i) without the Department's consent, or (ii) to repair, reconstruct or replace the Premises to the end that the Premises shall be restored to at least the same condition that they were in prior to such damage or destruction, insofar as the same may be accomplished by the use of such proceeds.

(c) The Department will maintain or cause to be maintained public liability insurance with limits of not less than \$3,000,000 to protect the Department and the Agency and their members, officers and employees and the Trustee and its officers and employees from all direct or contingent loss or liability for damages from bodily injury or death occasioned by reason of the operation of the Premises and for property damage resulting from any casualty attributable to the operation of the Premises except that such insurance may be subject to a deductible clause for anyone accident of not to exceed \$150,000.

(d) As an alternative to providing the insurance required by the preceding paragraph, the Department, with the consent of the Agency and the Trustee, may provide other kinds of insurance or methods or plans of protection, including self-insurance, if and to the extent such other kinds of insurance or methods or plans of protection shall afford reasonable protection to the Department, the Agency, the Trustee and the officers, agents and employees of each, in light of all circumstances giving consideration to cost, availability and plans or methods of protection adopted by other governmental entities of and within the State. Before another method or plan may be provided by the Department, there shall be filed with the Agency and the Trustee a certificate of the Chief of the Office of Insurance and Risk Management of the Department or of an actuary or other qualified risk assessor stating that, in the opinion of the signer, the substitute method or plan of protection is in accordance with the requirements of the preceding paragraph, and, when effective, would afford adequate protection to the Department, the Agency, the Trustee and the officers, agents and employees of each, against loss and damage from hazards and risks covered thereby. There shall also be filed a certificate of the Department setting forth the details of such substitute method or plan.

(e) The Department will maintain or cause to be maintained rental interruption or use and occupancy insurance to cover loss, total or partial, of the use of the Premises as a result of any of the hazards covered by the insurance required by paragraphs (a) and (c) above in an amount not less than the amount of Base Rental due pursuant to the Lease for any period of three consecutive years, taking into account the "stepped rental" element of the Base Rental so that the actual amount of Base Rental will be available through rental interruption insurance in each of such three consecutive years.

(f) The Department will maintain a CLTA policy or policies of title insurance for the Premises' in an amount as required by the Lease. Such policy or policies of title insurance shall insure the leasehold interest of the Department and shall show title to the Premises in the name of the Agency, subject to the Lease and such other encumbrances as will not, in the opinion of the Department and the Agency, materially affect the use and possession by the Department of the Premises and will not result in the abatement of Base Rental payable by the Department hereunder.

Default and Remedies

If the Department should default in the performance or observance of any agreement or covenant contained in the Lease or if the Department assigns its interest in the Lease without complying with the applicable assignment provisions or if the Department files a petition for bankruptcy or similar proceeding or if the Department abandons the Premises, then (i) in the case of a default in the timely payment of Base Rental or Additional Rental, immediately, or (ii) in the case of any other default under the Lease, 60 days after notice of such default has been given to the Department by the Agency or the Trustee or such additional time as is reasonably necessary, in the sole discretion of the Agency, to correct any such default, it shall be lawful for the Agency, or the Trustee as its assignee, to exercise any and all remedies available pursuant to law or granted pursuant to the Lease. Upon the breach of any agreement and covenant of the Lease to be performed or observed by the Department, the Agency may exercise any and all rights of entry upon the Premises, and also, at its option, with or without such entry, may terminate the Lease; provided, however, that no termination shall be effected either by operation of law or acts of the parties to the Lease except upon express written notice from the Agency to the Department terminating this Lease, as set forth below. In the event of such default and

notwithstanding any entry by the Agency, the Agency may at any time thereafter, with or without notice and demand and without limiting any other rights *or* remedies the Agency may have:

(1) Maintain the Lease in full force and effect and recover rent and other monetary charges as they become due, without terminating the Department's right to possession, regardless of whether or not the Department has abandoned the Premises. In the event the Agency elects not to terminate the Lease, it shall have the right to attempt to relet the Premises as the agent for the account of the Department at such rent, upon such conditions and for such term, and to do all other acts to maintain or preserve the Premises, including the removal of persons or property therefrom, as the Agency deems necessary or advisable; provided, however, that no such actions shall be deemed to terminate the Lease. If the Agency elects to attempt to relet the Premises as set forth above, the rental received from such reletting shall be applied first to the expenses of reletting and collection, including expenses necessary for repair or restoration of the Premises to its original condition (taking into account normal wear and tear), reasonable attorneys' fees and any real estate commission actually paid, second to the payment of Base Rental in accordance with the Lease, and third to the payment of Additional Rental, and if a sufficient sum shall not be thus realized to pay such sums and other charges, then the Department shall pay to the Agency or its assignee any net deficiency existing on the date when Base Rental or Additional Rental is due under the Lease; provided, however, that such reentry and reletting under this paragraph shall be done only with the consent of the Department, which consent is irrevocably given under the Lease. All property removed from the Premises may be stored by the Agency at the Department's sole cost and expense.

(2) Terminate the Department's right to possession by giving a written notice of termination to the Department. On the date specified in such notice (which shall be not less than 30 days after the giving of such notice), the Department's right to possession and the Lease shall terminate, unless on or before such date all arrears of rental and all other sums payable by the Department under the Lease, and all costs and expenses incurred by or on behalf of the Agency thereunder, including attorney's fees incurred in connection with such defaults, shall have been paid by the Department and all other defaults under or breaches of the Lease by the Department at the time existing shall have been fully remedied to the satisfaction of the Agency. Upon such termination, the Agency may recover, in addition to all other damages available by contract or at law, from the Department the unpaid rental which had been earned at the time of termination.

(3) So long as the Agency or its assignee does not terminate the Department's right to possession of the Premises, the Lease shall continue in effect and the Agency or its assignee shall have the right, pursuant to Section 1951.4 of the California Civil Code, to enforce all of its rights and remedies under the Lease, including the right to recover Base Rental payments as they become due under the Lease. Any reentry shall be allowed by the Department without hindrance, and the Agency and its assignee shall not be liable in damages for any such reentry in such event or be guilty of trespass.

Option To Purchase

The Department shall have the option to purchase the Premises, including all improvements then located upon the Premises. The Department may exercise the option to purchase at any time during the term of the Lease, for a purchase price of the amount necessary to pay all principal, premium, if any, and accrued interest with respect to all of the Bonds then Outstanding. If the purchase is effective on the date of the end of the term of the Lease or on or after the date of the retirement of the Bonds, then the purchase price shall be \$1.00 plus the discounted extension of the Leaseback Agreement described in the Lease.

The Department shall exercise its option to purchase by giving notice thereof to the Agency and the Trustee not later than 30 days prior to the Business Day on which it desires to purchase the Agency's right, title and interest in the Premises. If the Business Day on which the Department intends to exercise its option under the Lease is not an Interest Payment Date, the option price shall be the amount necessary to pay all principal,

premium, if any, and accrued interest on the Bonds payable; from the Base Rental due under the Lease on the date of such purchase, plus an amount equal to the amount of interest to accrue on such Bonds until the next succeeding Interest Payment Date.

If the Business Day on which the Department intends to exercise its option is, in accordance with the terms of the Indenture, a date on which the Bonds are subject to optional redemption, then the Department shall give notice to the Agency and the Trustee of its intention to exercise its option under the Lease not later than five days prior to the date on which the Trustee is required to send notice of redemption to the Bond Owners pursuant to the Indenture, and on such purchase date the Department shall deposit with the Trustee an amount equal to the option price determined by reference to the Lease.

If the Business Day on which the Department intends to exercise its option under the Lease is not a date on which the Bonds are subject to optional redemption, then the option price shall be payable in installments. Each installment (i) shall be payable at each time at which the principal portion of Base Rental would have been payable if such option had not been exercised, until the due date of the final installment specified below, and (ii) shall equal the principal amount of each Base Rental payment referred to in clause (i) above. Each such installment shall bear interest until paid at a rate equal to the rate which would have been payable with respect to the payments of Base Rental referred to in clause (i) above. At the option of the Department, the final installment shall be payable on (A) the final maturity date of the Bonds then Outstanding, or (B) any date on which the Bonds are subject to optional redemption pursuant to the terms of the Indenture, in an amount equal to the amount determined by reference to the Lease; provided, however, that the Department must designate the date of such final installment not later than the date on which the purchase option granted in the Lease is exercised, and provided further that the Department shall only choose a final installment date which, in the opinion of nationally recognized bond counsel, would not adversely affect the exclusion from gross income for federal income tax purposes of the interest with respect to the Series A Bonds.

In order to secure its obligations to pay the installments referred to in the Lease, the Department, concurrently with the exercise of its option under the Lease, shall deposit or cause to be deposited with the Trustee, in trust, cash and/or investments in such amount as will, together with the interest to accrue thereon without the need for further positive yielding investment, be fully sufficient to pay the installments (including all principal, premium, if any, and interest) referred to above at the times at which such installments are required to be paid. Such deposit shall be in addition to the Base Rental, if any, due on such date. The excess, if any, of the amounts so deposited over the installments actually required to be paid by the Department shall be remitted to the Department.

On any Business Day as to which the Department shall have exercised the option granted it pursuant to the Lease, and shall have paid or made provision (as set forth above) for the payment of the required option price, the Agency and its assignee shall execute and deliver to the Department a quitclaim deed conveying to the Department or its nominee, the Agency's right, title and interest so purchased if the Department shall exercise the option provided in the Lease to purchase the Agency's right, title and interest in the Premises prior to the expiration of the term of the Lease, and the Agency and its assignee shall execute and deliver the quitclaim deed as aforesaid, then the Lease shall terminate, but such termination shall not affect the Department's obligation to pay the option price on the terms set forth in the Lease.

Leaseback

The Agency agrees to lease back from the Department, for the full term of the Lease, the ground floor portion of the Building as well as the other portions of the Premises, if any, designated in the Leaseback Agreement (the "Leaseback Area"). The base rent payable to the Department for the Leaseback Area shall be the same rate per rentable square foot as the Base Rental which the Department is paying the Agency for such areas, with the Agency being responsible for all Additional Rental associated with the Leaseback Area as

reasonably calculated by the Department following consultation with representatives of the Agency. The Department shall at all times remain liable for the performance of the covenants and conditions on its part to be performed under the Lease, including, without limitation, the obligation of the Department to pay Base Rental thereunder.

Assignment and Sublease

Except as provided in the Lease, the Department shall not mortgage, pledge, assign or transfer any interest of the Department in the Lease by voluntary act or by operation of law or otherwise. The Department may sublease all or any portion of the Premises, may grant concessions involving the use of any portion of the Premises, whether such concessions purport to convey a leasehold interest or a license to use a portion of the Premises; and may assign its right to purchase the Agency's right, title and interest in the Premises. The Lease provides that the Department shall at all times remain liable for the performance of the covenants and conditions on its part to be performed under the Lease, notwithstanding any subletting or granting of concessions which may be made thereunder.

Changes to the Premises

The Department shall have the right during .the term of the Lease to make additions, betterments, extensions or improvements to the Premises or to attach fixtures, structures or signs to the Premises if such additions, betterments, extensions or improvements or fixtures, structures or signs are necessary or beneficial for the use of the Premises by the Department and so long as there is no diminution in fair rental value of the Premises as a result of the Department's exercise of its rights as set forth in the Lease. Title to all personal property or fixtures placed in or on any of the improvements on the Premises shall remain in the Department. The title to any personal property, improvements or fixtures placed on the Premises by any sublessee or licensee of the Department shall be controlled by the concession contracts or subleases entered into by the Department.

Right of Entry

The Agency and the Trustee shall have the right to enter the Premises during normal business hours to inspect the same for any purpose connected with the Agency's or the Department's rights or obligations under the Lease, and for all other lawful purposes.

Liens; Prosecution of Suits

In the event the Department shall at any time during the term of the Lease cause any additions, betterments, extensions or improvements to the Premises to be acquired or constructed or materials to be supplied in or upon the Premises, the Department shall pay or cause to be paid when due all sums of money that may become due, or purporting to be due, for any labor, services, materials, supplies or equipment furnished or alleged to have been furnished to or for the Department in, upon or about the Premises and shall keep the Premises free of any and all lawful mechanics' or materialmen's liens or other lawful liens against the Premises or the Agency's interest therein. In the event any such lien attaches to or is filed against the Premises or the Agency's interest therein, the Department shall cause each such lien to be fully discharged and released at the time the performance of any obligation secured by any such lien matures or becomes due, except that if the Department desires to contest any such lien it may do so. If any such lien shall be reduced to final judgment and such judgment or such process as may be issued for the enforcement thereof is not promptly stayed, or if so stayed and said stay thereafter expires, the Department shall forthwith pay or cause to be paid and discharged such judgment. The Department shall promptly, upon request of the Agency or its assignee, from time to time take or cause to be taken such action as may be necessary or proper to remedy or cure any defect in or cloud upon the title to the Premises whether now existing or hereafter developing and shall prosecute or cause to be prosecuted all such suits, actions and other proceedings as may be appropriate for such purpose.

APPENDIX C

FORM OF CONTINUING DISCLOSURE AGREEMENTS

CONTINUING DISCLOSURE AGREEMENT

(Department)

This Continuing Disclosure Agreement (this "Disclosure Agreement") is executed and delivered as of the 1st day of July, 2003 between the Department of General Services of the State of California (the "Department") and U.S. Bank National Association (the "Trustee" and "Dissemination Agent") in connection with the issuance by the Redevelopment Agency of the City of Riverside (the "Agency") of \$31,065,000 principal amount of Redevelopment Agency of the City of Riverside Lease Revenue Refunding Bonds (State of California Department of General Services Project) 2003 Series A (Tax-Exempt) and 2003 Series B (Taxable) (the "Bonds"). The Bonds are being issued pursuant to a Trust Agreement dated as of July 1, 2003, between the Agency and the Trustee (the "Trust Agreement"). The proceeds of the Bonds are being used to defease and refund the Agency's outstanding Lease Revenue Bonds (State of California Department of General Services Lease) 1994 Series A and 1994 Series B (the "Prior Bonds"). Proceeds of the Prior Bonds were used to finance the acquisition and improvement of the Demised Premises (as defined in the Trust Agreement), which are leased to the Department, pursuant to the Riverside State Building Lease dated April 26, 1994, as amended, between the Agency, as lessor, and the Department, as lessees (the "Lease"). The Department and the Trustee, as Dissemination Agent, agree as follows:

SECTION 1. Nature of the Disclosure Agreement. This Disclosure Agreement is executed to assist the Participating Underwriter in complying with S.E.C. Rule 15c2-12 (the "Rule"), and is made for the benefit of the Holders and Beneficial Owners of the Bonds from time to time, but shall not be deemed to create any monetary liability on the part of the Department or the Trustee to any other persons, including Holders or Beneficial Owners of the Bonds based on the Rule (as defined below). The sole remedy in the event of any failure of the Department or the Trustee as Dissemination Agent to comply with this Disclosure Agreement shall be an action to compel performance of any act required hereunder. The Department and the Trustee acknowledge that the Agency has undertaken no responsibility with respect to any reports, notices or disclosures provided or required under this Agreement, and has no liability to any person, including any Holder or Beneficial Owner of the Bonds, with respect to the Rule under this Agreement.

SECTION 2. Definitions. In addition to the definitions set forth in the Trust Agreement, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this section, the following capitalized terms shall have the following meanings:

"Annual Report" shall mean the Annual Report filed by the Department pursuant to, and as described in, Sections 3 and 4 of this Disclosure Agreement.

"Beneficial Owner" shall mean any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

"Disclosure Representative" shall mean the designated officer of the Department or his or her designee, or such other person as the Department shall designate in writing to the Trustee and Dissemination Agent from time to time.

"Dissemination Agent" shall mean the Trustee, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the Department.

"Listed Events" shall mean any of the events listed in Section 5(a) of this Disclosure Agreement.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository certified by the Securities and Exchange Commission (the "S.E.C.") to be the recipient of information of the nature of the Annual Reports required by this Disclosure Agreement.

"Official Statement" shall mean the official statement relating to the Bonds, dated June 30, 2003.

"Participating Underwriter" means Stone & Youngberg LLC, the original underwriter of the Bonds, required to comply with the Rule in connection with the offering of the Bonds.

"Repository" shall mean each National Repository and the State Repository.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the S.E.C. under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"State" shall mean the State of California.

"State Repository" shall mean any public or private repository or entity within the State created for the purpose of receiving information of the nature of the Annual Reports or reports of material events required by this Disclosure Agreement and recognized as such by the S.E.C. As of the date of this Disclosure Agreement, there is no State Repository.

SECTION 3. Provision of Annual Reports.

(a) On behalf of the State, the Department shall, or upon written direction shall cause, the Dissemination Agent to, not later than April 1 of each year in which any Bonds are Outstanding, commencing with the report for the 2002-03 Fiscal Year, provide an Annual Report consistent with the requirements of this Disclosure Agreement to each Repository, to the Participating Underwriter and to the Bond Insurer at One State Street Plaza, New York, NY 10004; provided that the audited financial statements of the State may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. Subject to the foregoing, not later than fifteen (15) Business Days prior to said date, the Department shall provide such Annual Report to the Dissemination Agent and the Trustee. The Department shall provide a written certification with each Annual Report furnished to the Dissemination Agent and the Trustee to the effect that such Annual Report constitutes the Annual Report required to be furnished by the Department hereunder. The Dissemination Agent and Trustee may conclusively rely upon such certification of the Department.

(b) If by fifteen (15) Business Days prior to the date specified in subsection (a) for providing the Annual Report to the Repositories, the Trustee has not received a copy of the Annual Report, the Trustee shall contact the Department and the Dissemination Agent to inquire if the Department is in compliance with subsection (a).

(c) If the Dissemination Agent is unable to verify that an Annual Report has been provided to the Repositories by the date required in subsection (a), the Dissemination Agent shall send a notice to the Municipal Securities Rulemaking Board in substantially the form attached as Exhibit A.

(d) The Dissemination Agent shall:

(i) determine each year prior to the date for providing the Annual Report the name and address of each National Repository and each State Repository, if any; and

(ii) if the Annual Report has been furnished to the Dissemination Agent, file a report with the Department and (if the Dissemination Agent is not the Trustee) the Trustee certifying that the Annual Report has been provided pursuant to this Disclosure Agreement, stating the date it was provided, and listing all the Repositories to which it was provided.

SECTION 4. Content of Annual Reports.

The Annual Report shall contain or include by reference the following:

(a) The audited General Purpose Financial Statements of the State for the fiscal year ended on the previous June 30, prepared in accordance with generally accepted accounting principles promulgated to apply to government entities from time to time by the Governmental Accounting Standards Board. If the State's audited financial statements are not available by the time the Annual Report is required to be filed pursuant to this Continuing Disclosure Agreement, the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the Official Statement, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available;

(b) Financial information relating to the State's General Fund budget for the fiscal year ended on the previous June 30 and for the fiscal year in which the Annual Report is issued, which information shall describe the sources of revenues, the principal categories of expenditures, and changes in fund balances and include a summary of expected State revenues and budgeted expenditures, significant assumptions relating to revenue and expenditure expectations, including updating the tables in the Official Statement under the following captions: "Summary of State Revenues and Expenditures" on pages A-__ through A-__ of the Official Statement and "Revenue and Expenditure Assumptions" on page A-__ of the Official Statement;

(c) Information concerning the total amount of the State's authorized and outstanding debt, long-term lease obligations, and other long-term liabilities as of the end of the most recent June 30, which debt is supported by payments from the State's General Fund and which includes short-term debt. Such information shall include schedules of debt service of outstanding general obligation bonds and lease-purchase debt. This shall be accomplished by updating the tables in the Official Statement which appear in Appendix A -- The State of California -- State Indebtedness"; "Authorized and Outstanding General Obligation Bonds"; "Outstanding State Debt"; "Schedule of Debt Service Requirements for General Fund General Obligation Bonds"; "Schedule of Debt Service Requirements for Enterprise Fund General Obligation Bonds"; "Schedule of Debt Service Requirements for Lease-Purchase Debt"; "State Public Works Board and Other Lease-Purchase Financing Outstanding Issues"; and "State Agency Revenue Bonds and Conduit Financing"; and

(d) A Statement confirming that the insurance required by the Lease is in effect or, if insurance is not in effect, naming the reason therefor.

The Annual Report may consist of one or more documents. Any or all of the items listed above may be included in the Annual Report by reference to other documents which have been filed by the State with each of the Repositories, including any final official statement (in which case such final official statement must also be available from the Municipal Securities Rulemaking Board). The Department shall clearly identify in the Annual Report each such document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the Department shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

- (1) principal and interest payment delinquencies;
- (2) non-payment related defaults;
- (3) modifications to rights of Bondholders;
- (4) optional, contingent or unscheduled bond calls;
- (5) defeasances;
- (6) rating changes;
- (7) adverse tax opinions or events adversely affecting the tax-exempt status of the Bonds;
- (8) unscheduled draws on the debt service reserves reflecting financial difficulties;
- (9) unscheduled draws on credit enhancements reflecting financial difficulties;
- (10) substitution of credit or liquidity providers, or their failure to perform;
- (11) release, substitution or sale of property securing repayment of the Bonds;
- (12) occurrence of any event which causes the Department not to have beneficial use and occupancy of the Project.

(b) The Trustee shall, promptly upon obtaining actual knowledge of the occurrence of any of the Listed Events contact the Disclosure Representative, inform such person of the event, and request that the Department promptly notify the Dissemination Agent in writing whether the Listed Event is material and, if so, to report the event pursuant to subsection (f). For purposes of this Disclosure Agreement, "actual knowledge" of the occurrence of such Listed Events shall mean actual knowledge by the officer at the Principal Office (as defined in the Trust Agreement) with regular responsibility for the administration of the Trust Agreement.

(c) Whenever the Department obtains knowledge of the occurrence of a Listed Event, whether because of a notice from the Trustee pursuant to subsection (b) or otherwise, the Department shall as soon as possible determine if such event is material under applicable federal securities laws.

(d) If the Department has determined that knowledge of the occurrence of a Listed Event is material, the Department shall promptly notify the Dissemination Agent and the Trustee in writing. Such notice shall instruct the Dissemination Agent to report the occurrence pursuant to subsection (f) and, if the Trust Agreement requires such event to be reported to the Owners, shall instruct the Trustee to report the occurrence to Owners.

(e) If in response to a request under subsection (b), the Department determines that the Listed Event is not material, the Department shall so notify the Dissemination Agent and the Trustee in writing and instruct the Dissemination Agent and the Trustee not to report the occurrence.

(f) If the Dissemination Agent has been instructed by the Department to report the occurrence of a Listed Event, the Dissemination Agent shall file a notice of such occurrence with the Municipal Securities Rulemaking Board and each State Repository, with copies to the Department [and to the Bond Insurer]. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(8) and (9) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to the Owners of affected Bonds pursuant to the Trust Agreement.

SECTION 6. Termination of Reporting Obligation. The obligations of the Department, the Trustee and the Dissemination Agent under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the outstanding Bonds. If such termination occurs prior to the final maturity of the Bonds, the Department shall give notice of such termination in the same manner as for a Listed Event under Section 5(b). If the Department's obligations under the Lease are assumed by some other entity, such person shall be responsible for compliance with this Disclosure Agreement in the same manner as if it were the Department, and the Department shall have no further responsibility hereunder.

SECTION 7. Dissemination Agent. The Department may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out the obligations under this Disclosure Agreement, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The initial Dissemination Agent shall be the Trustee.

SECTION 8. Amendment: Waiver. Notwithstanding any other provision of this Disclosure Agreement, the parties may amend or waive any provision of this Disclosure Agreement (provided that neither the Trustee nor the Dissemination Agent shall be obligated to enter in any amendment that modifies or increases its duties or obligations hereunder), provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4 or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Bonds in the same manner as provided in the Trust Agreement for amendments to the Trust Agreement with the consent of Holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Agreement, the Department shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or, in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the State. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (I) notice of such change shall be given in the same manner as for a Listed Event under Section 5(b), and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 9. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the Department from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If the Department chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Agreement, the Department shall have no obligation under this Disclosure Agreement to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 10. Duties, Immunities and Liabilities of Trustee and Dissemination Agent. The Dissemination Agent and the Trustee shall have only such duties with respect to this Disclosure Agreement as are specifically set forth herein, and the Department agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or wilful misconduct. The Dissemination Agent shall be paid compensation by the Department for its services provided hereunder in accordance with its schedule of fees as amended from time to time and all expenses, legal fees and advances made or incurred by the Dissemination Agent in the performance of its duties hereunder. The Dissemination Agent shall have no duty or obligation to review any information provided to it hereunder and shall not be deemed to be acting in any fiduciary capacity for the Department, the Owners or the Bonds, or any other party. The obligations of the Department under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

SECTION 11. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity (except the right of the Trustee or any Bondholder or Beneficial Owner to enforce the provisions of this Disclosure Agreement on behalf of the Bondholders). This Disclosure Agreement is not intended to create any monetary rights on behalf of any person based upon the Rule.

SECTION 12. Counterparts. This Disclosure Agreement may be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

SECTION 13. Partial Invalidity. If any one or more of the agreements or covenants or portions thereof required hereby to be performed by or on the part of the Department shall be contrary to law, then such agreement or agreements, such covenant or covenants or such portions thereof shall be null and void and shall be deemed separable from the remaining agreements and covenants or portions thereof and shall in no way affect the validity hereof, and the Holders of the Bonds shall retain all the benefits afforded to them hereunder. The Department hereby declares that it would have executed and delivered this Disclosure Agreement and each and every other article, section, paragraph, subdivision, sentence, clause and phrase hereof irrespective of the fact that any one or more articles, sections, paragraphs, subdivisions, sentences, clauses or phrases hereof or the application thereof to any person or circumstance may be held to be unconstitutional, unenforceable or invalid.

SECTION 14. Notices. Any notices or communications used by this Continuing Disclosure Agreement may be given as follows:

To the Department: State of California Department of General Services
Executive Office
P.O. Box 989052
West Sacramento, CA 95798-9052

To the Trustee or
Dissemination Agent: U.S. Bank National Association
550 South Hope Street, Suite 500
Los Angeles, CA 90071

To the Participating
Underwriter: Stone & Youngberg LLC
One Ferry Building
San Francisco, CA 94111

SECTION 15. Governing Law. The laws of the State of California shall govern this Disclosure Agreement, the interpretation thereof and any right or liability arising hereunder.

IN WITNESS WHEREOF, the Department and the Trustee, as Dissemination Agent, have caused this Disclosure Agreement to be executed by their respective officers as of the date first above written.

CALIFORNIA STATE DEPARTMENT OF GENERAL SERVICES

By: _____
Title: _____

U.S. BANK NATIONAL ASSOCIATION, as Trustee and Dissemination Agent

By: _____
Authorized Officer

EXHIBIT A

NOTICE TO MUNICIPAL SECURITIES RULEMAKING BOARD
OF FAILURE TO FILE ANNUAL REPORT

Name of Obligated Party: State of California Department of General Services (the "Department")

Name of Bond Issue: \$31,065,000 Redevelopment Agency of the City of Riverside, Lease Revenue Refunding Bonds (State of California Department of General Services Project, 2003 Series A (Tax-Exempt) and 2003 Series B (Taxable))

Date of Delivery: July 8, 2003

NOTICE IS HEREBY GIVEN that the Department has not provided an Annual Report with respect to the above-named Notes as required by Section 3 of the Continuing Disclosure Agreement dated as of July 1, 2003 between the Department and U.S. Bank National Association. [The Department anticipates that the Annual Report will be filed by _____.]

Dated: _____

U.S. BANK NATIONAL ASSOCIATION, as
Dissemination Agent

cc: State of California Department of General Services
Executive Director, Redevelopment Agency of the City of Riverside

CONTINUING DISCLOSURE AGREEMENT
(Agency)

This Continuing Disclosure Agreement (this "Disclosure Agreement") is executed and delivered as of the 1st day of July, 2003 between the Redevelopment Agency of the City of Riverside (the "Agency") and U.S. Bank National Association (the "Trustee" and "Dissemination Agent") in connection with the issuance by the Agency of \$31,065,000 principal amount of Redevelopment Agency of the City of Riverside Lease Revenue Refunding Bonds (State of California Department of General Services Project) 2003 Series A (Tax-Exempt) and 2003 Series B (Taxable (the "Bonds"). The Bonds are being issued pursuant to a Trust Agreement dated as of July 1, 2003, between the Agency and the Trustee (the "Trust Agreement"). The proceeds of the Bonds are being used to defease and refund the Agency's outstanding Lease Revenue Bonds (State of California Department of General Services Lease) 1994 Series A and 1994 Series B (the "Prior Bonds"). Proceeds of the Prior Bonds were used to finance the acquisition and improvement of the Demised Premises (as defined in the Trust Agreement), which are leased to the Department, pursuant to the Riverside State Building Lease dated April 26, 1994, as amended, between the Agency, as lessor, and the Department, as lessees (the "Lease"). The Agency and the Trustee, as Dissemination Agent, agree as follows:

SECTION 1. Nature of the Disclosure Agreement. This Disclosure Agreement is executed to assist the Participating Underwriter in complying with S.E.C. Rule 15c2-12 (the "Rule"), and is made for the benefit of the Holders and Beneficial Owners of the Bonds from time to time, but shall not be deemed to create any monetary liability on the part of the Trustee to any other persons, including Holders or Beneficial Owners of the Bonds based on the Rule (as defined below). The sole remedy in the event of any failure of the Agency or the Trustee as Dissemination Agent to comply with this Disclosure Agreement shall be an action to compel performance of any act required hereunder.

SECTION 2. Definitions. In addition to the definitions set forth in the Trust Agreement, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this section, the following capitalized terms shall have the following meanings:

"Beneficial Owner" shall mean any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

"Disclosure Representative" shall mean the Executive Director of the Agency or his or her designee, or such other person as the Agency shall designate in writing to the Trustee and Dissemination Agent from time to time.

"Dissemination Agent" shall mean the Trustee, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the Agency.

"Listed Events" shall mean any of the events listed in Section 2(a) of this Disclosure Agreement.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository certified by the Securities and Exchange Commission (the "S.E.C.") to be the recipient of information of the nature of the Annual Reports required by this Disclosure Agreement.

"Official Statement" shall mean the official statement relating to the Bonds, dated June 30, 2003.

"Participating Underwriter" means Stone & Youngberg LLC, the original underwriter of the Bonds, required to comply with the Rule in connection with the offering of the Bonds.

"Repository" shall mean each National Repository and the State Repository.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the S.E.C. under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"State" shall mean the State of California.

"State Repository" shall mean any public or private repository or entity within the State created for the purpose of receiving information of the nature of the Annual Reports or reports of material events required by this Disclosure Agreement and recognized as such by the S.E.C. As of the date of this Disclosure Agreement, there is no State Repository.

SECTION 2. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 2, the Agency shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

- (1) principal and interest payment delinquencies;
- (2) non-payment related defaults;
- (3) modifications to rights of Bondholders;
- (4) optional, contingent or unscheduled bond calls;
- (5) defeasances;
- (6) rating changes;
- (7) adverse tax opinions or events adversely affecting the tax-exempt status of the Bonds;
- (8) unscheduled draws on the debt service reserves reflecting financial difficulties;
- (9) unscheduled draws on credit enhancements reflecting financial difficulties;
- (10) substitution of credit or liquidity providers, or their failure to perform;
- (11) release, substitution or sale of property securing repayment of the Bonds;
- (12) occurrence of any event which causes the Department not to have beneficial use and occupancy of the Project.

(b) The Trustee shall, promptly upon obtaining actual knowledge of the occurrence of any of the Listed Events contact the Disclosure Representative, inform such person of the event, and request that the Agency promptly notify the Dissemination Agent in writing whether the Listed Event is material and, if so, to report the event pursuant to subsection (f). For purposes of this Disclosure Agreement, "actual knowledge" of the occurrence of such Listed Events shall mean actual knowledge by the officer at the Principal Office (as defined in the Trust Agreement) with regular responsibility for the administration of the Trust Agreement.

(c) Whenever the Agency obtains knowledge of the occurrence of a Listed Event, whether because of a notice from the Trustee pursuant to subsection (b) or otherwise, the Agency shall as soon as possible determine if such event is material under applicable federal securities laws.

(d) If the Agency has determined that knowledge of the occurrence of a Listed Event is material, the Agency shall promptly notify the Dissemination Agent and the Trustee in writing. Such notice shall instruct the Dissemination Agent to report the occurrence pursuant to subsection (f) and, if the Trust Agreement requires such event to be reported to the Owners, shall instruct the Trustee to report the occurrence to Owners.

(e) If in response to a request under subsection (b), the Agency determines that the Listed Event is not material, the Agency shall so notify the Dissemination Agent and the Trustee in writing and instruct the Dissemination Agent and the Trustee not to report the occurrence.

(f) If the Dissemination Agent has been instructed by the Agency to report the occurrence of a Listed Event, the Dissemination Agent shall file a notice of such occurrence with the Municipal Securities Rulemaking Board and each State Repository, with copies to the Agency [and the Insurer]. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(8) and (9) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to the Owners of affected Bonds pursuant to the Trust Agreement.

SECTION 3. Termination of Reporting Obligation. The obligations of the Agency, the Trustee and the Dissemination Agent under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the outstanding Bonds. If such termination occurs prior to the final maturity of the Bonds, the Agency shall give notice of such termination in the same manner as for a Listed Event under Section 2(b).

SECTION 4. Dissemination Agent. The Agency may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out the obligations under this Disclosure Agreement, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The initial Dissemination Agent shall be the Trustee.

SECTION 5. Amendment: Waiver. Notwithstanding any other provision of this Disclosure Agreement, the parties may amend or waive any provision of this Disclosure Agreement (provided that neither the Trustee nor the Dissemination Agent shall be obligated to enter into any amendment that modifies or increases its duties or obligations hereunder), provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 2(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Bonds in the same manner as provided in the Trust Agreement for amendments to the Trust Agreement with the consent of Holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds.

SECTION 6. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the Agency from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If the Agency chooses to include any information in any notice of occurrence of a Listed Event in addition to that

To the Participating
Underwriter:

Stone & Youngberg LLC
One Ferry Building
San Francisco, CA 94111

SECTION 12. Governing Law. The laws of the State of California shall govern this Disclosure Agreement, the interpretation thereof and any right or liability arising hereunder.

IN WITNESS WHEREOF, the Agency and the Trustee, as Dissemination Agent, have caused this Disclosure Agreement to be executed by their respective officers as of the date first above written.

REDEVELOPMENT AGENCY OF THE CITY OF
RIVERSIDE

By: _____
Title: _____

U.S. BANK NATIONAL ASSOCIATION, as Trustee and
Dissemination Agent

By: _____
Authorized Officer

APPENDIX D

BOOK-ENTRY ONLY SYSTEM

The following description of the Depository Trust Company ("DTC"), the procedures and record keeping with respect to beneficial ownership interests in the Bonds, payment of principal, interest and other payments on the Bonds to DTC Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in the Bonds and other related transactions by and between DTC, the DTC Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, the issuer of the Bonds (the "Issuer") makes no representations concerning these matters and neither the DTC Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters, but should instead confirm the same with DTC or the DTC Participants, as the case may be.

No assurances can be given that DTC, DTC Participants or Indirect Participants will distribute to the Beneficial Owners (a) payments of interest, principal or premium, if any, with respect to the Bonds, (b) certificates representing ownership interest in or other confirmation or ownership interest in the Bonds, or (c) redemption or other notices sent to DTC or Cede & Co., its nominee, as the registered owner of the Bonds, or that they will so do on a timely basis, or that DTC, DTC Participants or DTC Indirect Participants will act in the manner described in this Appendix. The current "Rules" applicable to DTC are on file with the Securities and Exchange Commission and the current "Procedures" of DTC to be followed in dealing with DTC Participants are on file with DTC.

DTC and its Participants. The Depository Trust Company ("DTC"), New York, NY, 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 security 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, the world's largest depository, 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 and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (respectively, "NSCC", "GSCC", "MBSCC", and "EMCC", also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC

Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Book-Entry Only System. Purchases of the 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 Security ("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. Beneficial Owners are, however, 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 the 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 may be requested by an authorized representative of DTC. The deposit of the 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 Security documents. For example, Beneficial Owners of the Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar 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 any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer 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).

Payments of principal of, premium, if any, and interest evidenced by 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 Authority or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments

by 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 Participant and not of DTC (nor its nominee), the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal of, premium, if any, and interest evidenced by the Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

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

The Authority 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.

Discontinuance of DTC Services. In the event that (a) DTC determines not to continue to act as securities depository for the Bonds, or (b) the Issuer determines that DTC will no longer so act and delivers a written certificate to the Trustee to that effect, then the Issuer will discontinue the Book-Entry Only System with DTC for the Bonds. If the Issuer determines to replace DTC with another qualified securities depository, the Issuer will prepare or direct the preparation of a new single separate, fully registered Bond for each maturity of the Bonds registered in the name of such successor or substitute securities depository as are not inconsistent with the terms of the Trust Agreement. If the Issuer fails to identify another qualified securities depository to replace the incumbent securities depository for the Bonds, then the Bonds will no longer be restricted to being registered in the Bond registration books in the name of the incumbent securities depository or its nominee, but will be registered in whatever name or names the incumbent securities depository or its nominee transferring or exchanging the Bonds designates.

If the Book-Entry Only System is discontinued, the following provisions would also apply: (i) the Bonds will be made available in physical form, (ii) principal of, and redemption premiums, if any, on, the Bonds will be payable upon surrender thereof at the corporate trust office of the Trustee, (iii) interest on the Bonds will be payable by check mailed by first-class mail or, upon the written request of any Owner of \$1,000,000 or more in aggregate principal amount of Bonds received by the Trustee on or prior to the 15th day of the calendar month immediately preceding the interest payment date, by wire transfer in immediately available funds to an account with a financial institution within the continental United States of America designated by such Owner, and (iv) the Bonds will be transferable and exchangeable as provided in the Trust Agreement.

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APPENDIX E

SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY

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Financial Guaranty Insurance Policy

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

Obligor:

Policy Number:

Obligations:

Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

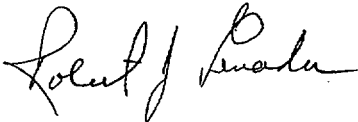
In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.



President

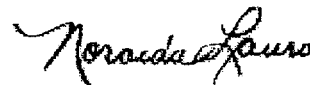


Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.



Form No.: 2B-0012 (1/01)

Authorized Officer of Insurance Trustee

Endorsement

Policy for:

Attached to and forming part of Policy No.:

Effective Date of Endorsement:

In the event that Ambac Assurance Corporation were to become insolvent, any claims arising under the Policy would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Nothing herein contained shall be held to vary, alter, waive or extend any of the terms, conditions provisions, agreements or limitations of the above mentioned Policy other than as above stated.

In Witness Whereof, Ambac has caused this Endorsement to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

Ambac Assurance Corporation



President

Secretary

APPENDIX F

PROPOSED FORM OF BOND COUNSEL OPINIONS

(SERIES A BONDS)

Redevelopment Agency of the City of Riverside
3900 Main Street
Riverside, CA 92522

Re: \$26,255,000 Redevelopment Agency of the City of Riverside Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series A (Tax-Exempt)

Ladies and Gentlemen:

We have acted as bond counsel in connection with the issuance and sale by the Redevelopment Agency of the City of Riverside (the "Agency"), a public body corporate and politic, organized and existing under the Community Redevelopment Law of the State of California (Part 1 of Division 24 of the California Health and Safety Code, as amended), of \$26,255,000 aggregate principal amount its Bonds designated Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series A (Tax-Exempt) (the "Series A Bonds"). Concurrently with the issuance of the Series A Bonds, the Agency is issuing \$4,810,000 aggregate principal amount of its bonds designated Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series B (Taxable) (the "Series B Bonds"). The Series A Bonds are issued pursuant to Articles 10 and 11 of Chapter 3 of Part 1 of Division 24 of Title 5 of the California Government Code (commencing with Section 53570) (the "Act") and other applicable provisions of law of the State of California and a Trust Agreement, dated as of July 1, 2003, by and between the Agency and U.S. Bank National Association, as trustee (the "Trustee"). The Series A Bonds are secured on a parity with the Series B Bonds by the Revenues, as defined in and pledged under the Trust Agreement, consisting primarily of Base Rental payments to be made by the Department of General Services of the State of California (the "Department") to the Agency pursuant to that certain lease designated "Riverside/State Building Lease," dated as of April 26, 1994, as amended (the "Lease"), by and between the Department and the Agency, for the use and possession of the Demised Premises (as defined in the Trust Agreement).

As bond counsel, we have examined copies certified to us as being true and complete copies of the proceedings of the Agency for the authorization and issuance of the Series A Bonds. In this connection, we have also examined such certificates of public officials and officers of the Agency as we have considered necessary for the purposes of this opinion.

We have, with your approval, assumed that all items submitted to us as originals are authentic and that all items submitted as copies conform to the originals.

On the basis of such examination and assumptions, and in reliance thereon, and of our consideration of such questions of law as we have deemed relevant in the circumstances, we are of the opinion that:

1. The Series A Bonds have been duly authorized and issued and constitute the legally valid and binding obligations of the Agency, enforceable in accordance with their terms and the terms of the Trust Agreement.

2. The Trust Agreement has been duly authorized, executed and delivered by the Agency and constitutes the legally valid and binding obligation of the Agency, enforceable in accordance with its terms. The Series A Bonds are entitled to the benefits of the Trust Agreement. The Trust Agreement creates the valid pledge which it purports to create, to secure the payment of the principal of and interest on the Series A Bonds, of the Revenues and any other amounts held in any fund or account established pursuant to the Trust Agreement for the Series A Bonds, other than the Rebate Fund, subject to the provisions of the Trust Agreement permitting the application of such amounts for the purposes and on the terms and conditions set forth in the Trust Agreement. The Trust Agreement also creates a valid assignment to the Trustee, for the benefit of the owners from time to time of the Series A Bonds, of certain rights of the Agency in the Lease, including the right to receive payments of Base Rental from the Department (to the extent and as more particularly described in the Trust Agreement).

3. The Internal Revenue Code of 1986, as amended (the "Code"), sets forth certain investment, rebate and related requirements which must be met subsequent to the issuance and delivery of the Series A Bonds for the interest on the Series A Bonds to be and remain excluded from gross income for purposes of federal income taxation. Noncompliance with such requirements could cause the interest on the Series A Bonds to be subject to federal income taxation retroactive to the date of issue of the Series A Bonds. Pursuant to the Trust Agreement, the Agency has covenanted to comply with the requirements of the Code and pursuant to the Lease, the Department has covenanted to comply with the requirements of the Code. We are of the opinion that, assuming compliance with the aforementioned covenant, the interest on the Series A Bonds is excluded from gross income for purposes of federal income taxation under existing statutes, regulations, rulings and court decisions. We are further of the opinion that interest on the Series A Bonds is not a specific preference item for purposes of the alternative minimum tax provisions of the Code. However, interest on the Series A Bonds received by corporations will be included in corporate adjusted current earnings, a portion of which may increase the alternative minimum taxable income of such corporations. Although the interest on the Series A Bonds is excluded from gross income for federal tax purposes, the accrual or receipt of interest on the Series A Bonds may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend on the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences.

4. Interest on the Series A Bonds is exempt from personal income taxes of the State of California under present State law.

The rights of the owners of the Series A Bonds and the enforceability of the Series A Bonds and the Trust Agreement may be subject to bankruptcy, insolvency, moratorium and other similar laws affecting creditors' rights heretofore or hereafter enacted and their enforcement may be subject to the exercise of judicial discretion in accordance with general principles of equity.

Respectfully submitted,

(SERIES B BONDS)

Redevelopment Agency of the City of Riverside
3900 Main Street
Riverside, CA 92522

Re: \$4,810,000 Redevelopment Agency of the City of Riverside Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series B (Taxable)

Ladies and Gentlemen:

We have acted as bond counsel in connection with the issuance and sale by the Redevelopment Agency of the City of Riverside (the "Agency"), a public body corporate and politic, organized and existing under the Community Redevelopment Law of the State of California (Part 1 of Division 24 of the California Health and Safety Code, as amended), of \$4,810,000 aggregate principal amount its Bonds designated Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series B (Taxable) (the "Series B Bonds"). Concurrently with the issuance of the Series B Bonds, the Agency is issuing \$26,255,000 aggregate principal amount of its bonds designated Lease Revenue Refunding Bonds (State of California Department of General Services Project), 2003 Series A (Tax-Exempt) (the "Series A Bonds"). The Series B Bonds are issued pursuant to Articles 10 and 11 of Chapter 3 of Part 1 of Division 24 of Title 5 of the California Government Code (commencing with Section 53570) (the "Act") and other applicable provisions of law of the State of California and a Trust Agreement, dated as of July 1, 2003, by and between the Agency and U.S. Bank National Association, as trustee (the "Trustee"). The Series B Bonds are secured on a parity with the Series A Bonds by the Revenues, as defined in and pledged under the Trust Agreement, consisting primarily of Base Rental payments to be made by the Department of General Services of the State of California (the "Department") to the Agency pursuant to that certain lease designated "Riverside/State Building Lease," dated as of April 26, 1994, as amended (the "Lease"), by and between the Department and the Agency, for the use and possession of the Demised Premises (as defined in the Trust Agreement).

As bond counsel, we have examined copies certified to us as being true and complete copies of the proceedings of the Agency for the authorization and issuance of the Series B Bonds. In this connection, we have also examined such certificates of public officials and officers of the Agency as we have considered necessary for the purposes of this opinion.

We have, with your approval, assumed that all items submitted to us as originals are authentic and that all items submitted as copies conform to the originals.

On the basis of such examination and assumptions, and in reliance thereon, and of our consideration of such questions of law as we have deemed relevant in the circumstances, we are of the opinion that:

1. The Series B Bonds have been duly authorized and issued and constitute the legally valid and binding obligations of the Agency, enforceable in accordance with their terms and the terms of the Trust Agreement.

2. The Trust Agreement has been duly authorized, executed and delivered by the Agency and constitutes the legally valid and binding obligation of the Agency, enforceable in accordance with its terms. The Series B Bonds are entitled to the benefits of the Trust Agreement. The Trust Agreement creates the valid pledge which it purports to create, to secure the payment of the principal of and interest on the Series B Bonds, of the Revenues and any other amounts held in any fund or account established pursuant to the Trust

Agreement for the Series B Bonds, other than the Rebate Fund, subject to the provisions of the Trust Agreement permitting the application of such amounts for the purposes and on the terms and conditions set forth in the Trust Agreement. The Trust Agreement also creates a valid assignment to the Trustee, for the benefit of the owners from time to time of the Series B Bonds, of certain rights of the Agency in the Lease, including the right to receive payments of Base Rental from the Department (to the extent and as more particularly described in the Trust Agreement).

3. Interest on the Series B Bonds is not excluded from gross income for purposes of federal income taxation.

4. Interest on the Series B Bonds is exempt from personal income taxes of the State of California under present State law.

The rights of the owners of the Series B Bonds and the enforceability of the Series B Bonds and the Trust Agreement may be subject to bankruptcy, insolvency, moratorium and other similar laws affecting creditors' rights heretofore or hereafter enacted and their enforcement may be subject to the exercise of judicial discretion in accordance with general principles of equity.

Respectfully submitted,

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