



The Management's Discussion and Analysis provides a narrative overview and analysis of the financial activities of the State.

Management's Discussion and Analysis

The following is a discussion and analysis of the State of Missouri's (the State's) financial activities for the fiscal year ended June 30, 2006. Readers are encouraged to consider the information presented here in conjunction with additional information that is furnished in the letter of transmittal.

HIGHLIGHTS

Government-Wide:

- Assets of the State's governmental activities exceeded liabilities by \$28.0 billion; this resulted in an increase in net assets of \$487.2 million or 1.8% from the prior year. This increase can be attributed to more tax revenues being collected due to a more aggressive approach to timely collections and an improved economy. This resulted in an increase in cash and cash equivalents of \$403.5 million.
- Assets of the State's business activities exceeded liabilities by \$77.5 million, an increase in net assets of \$173.2 million or 181.1% from the prior year. This increase can also be explained primarily by a significant increase in cash and cash equivalents due to more unemployment compensation tax collections.

Fund-Level:

- Governmental fund assets exceeded liabilities by \$3.9 billion, an increase of \$817.3 million or 26.6% from the prior year. The increase was primarily due to a decrease of \$568.6 million in liabilities of which \$510.3 million was deferred revenue. This was because of more timely collections of taxes, mainly corporate income tax.

Debt Issued and Outstanding:

- The primary government's total long-term obligations related to bonds payable increased \$212.4 million or 8.8% over the prior year. The outstanding bonds payable represents 42.6% of financial assets (cash, receivables, and investments) and 7.6% of total assets. The net increase in bonds payable resulted from decreases of \$138,310,000 due to bond payments and increases of \$350,660,000 due to issuances of State Road Bonds. Additional detail is available in *Note 12*.

Revenue Limit:

- The State Constitution limits the State's ability to retain revenue collected over an amount set by a constitutional amendment known as Article X or the Hancock Amendment. Excess revenue must be refunded to the taxpayers each year. During fiscal year 2006, the State did not exceed the revenue limit.

OVERVIEW OF THE FINANCIAL STATEMENTS

The State's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-Wide Financial Statements:

The government-wide financial statements are designed to provide readers with a broad overview of the State's finances, in a manner similar to a private-sector business.

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

The *Statement of Activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of when the cash is received. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements report three activities:

Governmental Activities are primarily supported by taxes and intergovernmental revenues. They include general government, education, natural and economic resources, transportation and law enforcement, and human services.

Business-Type Activities are intended to recover all or a significant portion of their costs through user fees and charges. They include constructing and operating state park facilities, fairgrounds, historical properties and office buildings, hospital services, warehousing, merchandising, publishing maps and documents, insurance coverage, and the operation of the State Lottery, Unemployment Compensation, and the Petroleum Storage Tank Insurance funds.

Discretely Presented Component Units are operations for which the State has financial accountability, but are legally separate. They include the college and universities, Missouri Development Finance Board, Agricultural and Small Business Development Authority, and Missouri Transportation Finance Corporation.

Fund Financial Statements:

The fund financial statements present more detailed information about the government's operations than the government-wide statements. The State uses fund accounting to ensure and demonstrate compliance with statutory requirements. All of the funds of the State can be divided into three categories: governmental, proprietary, and fiduciary funds.

Governmental funds. Governmental funds are used to account for most of the basic services provided by the State. Unlike the government-wide financial statements, governmental fund financial statements focus on short-term inflows and outflows of current financial resources and utilize the modified accrual basis of accounting. This presentation focuses on when cash will be received and disbursed making the statements useful in evaluating a government's financing requirements in the near future.

Governmental funds include the general, special revenue, capital projects, debt service, and permanent funds. Major funds include general, public education, conservation and environmental protection, transportation and law enforcement, and the Missouri road fund which are presented in separate columns. Data from other governmental funds are combined into a single column for aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements in supplementary information.

In order for the user to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements, a reconciliation to facilitate this comparison is provided on the page immediately following each governmental fund financial statement.

Proprietary funds. Proprietary funds are used to account for activities similar to private businesses in which goods and services are sold for specified fees. Generally, the State uses enterprise funds to account for activities that provide goods and services to the general public. These include constructing and operating state park facilities, fairgrounds, historical properties and office buildings, hospital services, warehousing, merchandising, publishing maps and documents, and the operation of the State Lottery, Unemployment Compensation, and the Petroleum Storage Tank Insurance funds. Internal service funds report activities that provide supplies and services for the State's other programs and activities. The State uses internal service funds to account for insurance and health-care plans, as well as administrative services for other state agencies, such as fleet management, data processing, and telecommunication services. Because these services predominately benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary funds focus on economic resources and utilize the full accrual basis of accounting. The proprietary fund financial statements provide separate information for the State Lottery, Unemployment Compensation, and Petroleum Storage Tank Insurance, which are considered major enterprise funds. All internal service funds are combined into a single column in the proprietary fund financial statements. Non-major enterprise funds are also combined into a single column for aggregated presentation. Individual fund data for the non-major enterprise and internal service funds is provided in the form of combining statements in supplementary information.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside State government. Fiduciary funds are *not* reflected in the government-wide financial statements because the resources of those funds are not available to support the State's own programs. The accounting used for fiduciary funds is similar to that used for proprietary funds.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents required supplementary information (RSI) including a budgetary comparison schedule for the general fund and major special revenue funds. Other supplementary information includes the combining statements for the general, non-major governmental, non-major enterprise, internal service, fiduciary, and non-major component unit funds. It also includes the statistical section as well as budgetary comparison schedules for the Missouri road fund, non-major special revenue, debt service, and permanent funds.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net Assets:

The following table displays the current and prior year government-wide condensed Statement of Net Assets.

STATEMENT OF NET ASSETS						
(In Thousands of Dollars)						
	Governmental Activities		Business-Type Activities		Total	
	2006	2005*	2006	2005*	2006	2005*
ASSETS:						
Current and Other Assets	\$ 5,728,275	\$ 5,470,550	\$ 518,706	\$ 397,484	\$ 6,246,981	\$ 5,868,034
Capital Assets, Net	28,012,060	27,514,455	39,607	43,304	28,051,667	27,557,759
<i>Total Assets</i>	<u>33,740,335</u>	<u>32,985,005</u>	<u>558,313</u>	<u>440,788</u>	<u>34,298,648</u>	<u>33,425,793</u>
LIABILITIES:						
Long-Term Liabilities	4,446,002	4,107,517	227,662	233,646	4,673,664	4,341,163
Other Liabilities	1,306,615	1,377,014	253,106	302,754	1,559,721	1,679,768
<i>Total Liabilities</i>	<u>5,752,617</u>	<u>5,484,531</u>	<u>480,768</u>	<u>536,400</u>	<u>6,233,385</u>	<u>6,020,931</u>
NET ASSETS:						
Invested in Capital Assets	25,840,886	25,572,008	39,599	43,304	25,880,485	25,615,312
Restricted	3,813,145	3,250,204	3,942	12,407	3,817,087	3,262,611
Unrestricted	(1,666,313)	(1,321,738)	34,004	(151,323)	(1,632,309)	(1,473,061)
<i>Total Net Assets</i>	<u>\$ 27,987,718</u>	<u>\$ 27,500,474</u>	<u>\$ 77,545</u>	<u>\$ (95,612)</u>	<u>\$ 28,065,263</u>	<u>\$ 27,404,862</u>

*Fiscal year 2005 amounts have been restated.

The State's total net assets increased \$660.4 million or 2.4% during fiscal year 2006. This increase resulted primarily from an increase of \$378.9 million in current and other assets. Capital assets net of related debt and restricted net assets, which do not represent resources available to pay day-to-day operating expenses, increased by \$819.6 million or 2.8%.

Invested in capital assets net of related debt, such as bonds payable or capital lease obligations, is the largest component of the State's net assets at 92.2% or \$25.9 billion. These assets include land, infrastructure, buildings, and equipment which are not easily converted to cash or readily available to pay state debts as they come due.

Restricted net assets of the primary government totaled \$3.8 billion or 13.6% of total net assets, vs. 11.9% from the prior year. Net assets are restricted for several reasons including constitutional, legal, or external requirements. Examples of restricted net assets include lottery proceeds restricted for public education, funds restricted for debt service, and certain sales taxes restricted for the maintenance of highways or state parks and conservation areas. Also, many federal funds are restricted to funding certain programs.

Changes in Net Assets:

The following table displays the current and prior year government-wide condensed Statement of Activities.

STATEMENT OF ACTIVITIES						
(In Thousands of Dollars)						
	Governmental Activities		Business-Type Activities		Total	
	2006	2005*	2006	2005*	2006	2005*
REVENUES:						
Program Revenues:						
Charges for Services	\$ 1,610,044	\$ 1,453,667	\$ 989,701	\$ 857,674	\$ 2,599,745	\$ 2,311,341
Operating Grants and Contributions	7,757,468	7,767,831	603,727	542,984	8,361,195	8,310,815
General Revenues:						
Sales and Use Taxes	2,974,842	3,003,405	---	---	2,974,842	3,003,405
Income Taxes	5,654,104	5,172,616	---	---	5,654,104	5,172,616
Unemployment and Other Taxes	1,576,924	1,686,767	---	---	1,576,924	1,686,767
Other Revenues	305,152	238,301	(2,154)	3,213	302,998	241,514
<i>Total Revenues</i>	<u>19,878,534</u>	<u>19,322,587</u>	<u>1,591,274</u>	<u>1,403,871</u>	<u>21,469,808</u>	<u>20,726,458</u>
EXPENSES:						
General Government	980,806	1,035,396	---	---	980,806	1,035,396
Education	5,773,117	5,669,627	---	---	5,773,117	5,669,627
Natural and Economic Resources	849,952	834,269	---	---	849,952	834,269
Transportation and Law Enforcement	2,025,179	2,189,839	---	---	2,025,179	2,189,839
Human Services	9,890,571	9,771,651	---	---	9,890,571	9,771,651
State Lottery	---	---	665,846	575,667	665,846	575,667
Unemployment Compensation	---	---	412,937	501,098	412,937	501,098
Petroleum Storage Tank	---	---	13,243	25,944	13,243	25,944
Veterans' Homes	---	---	46,643	58,760	46,643	58,760
All Other Expenses	130,438	126,202	20,675	13,345	151,113	139,547
<i>Total Expenses</i>	<u>19,650,063</u>	<u>19,626,984</u>	<u>1,159,344</u>	<u>1,174,814</u>	<u>20,809,407</u>	<u>20,801,798</u>
Increase (Decrease) in Net Assets before						
Contributions & Transfers	228,471	(304,397)	431,930	229,057	660,401	(75,340)
<i>Transfers</i>	<u>258,773</u>	<u>207,159</u>	<u>(258,773)</u>	<u>(207,159)</u>	<u>---</u>	<u>---</u>
Change in Net Assets	487,244	(97,238)	173,157	21,898	660,401	(75,340)
<i>Net Assets - July 1</i>	<u>27,500,474</u>	<u>27,597,712</u>	<u>(95,612)</u>	<u>(117,510)</u>	<u>27,404,862</u>	<u>27,480,202</u>
<i>Net Assets - June 30</i>	<u>\$ 27,987,718</u>	<u>\$ 27,500,474</u>	<u>\$ 77,545</u>	<u>\$ (95,612)</u>	<u>\$ 28,065,263</u>	<u>\$ 27,404,862</u>

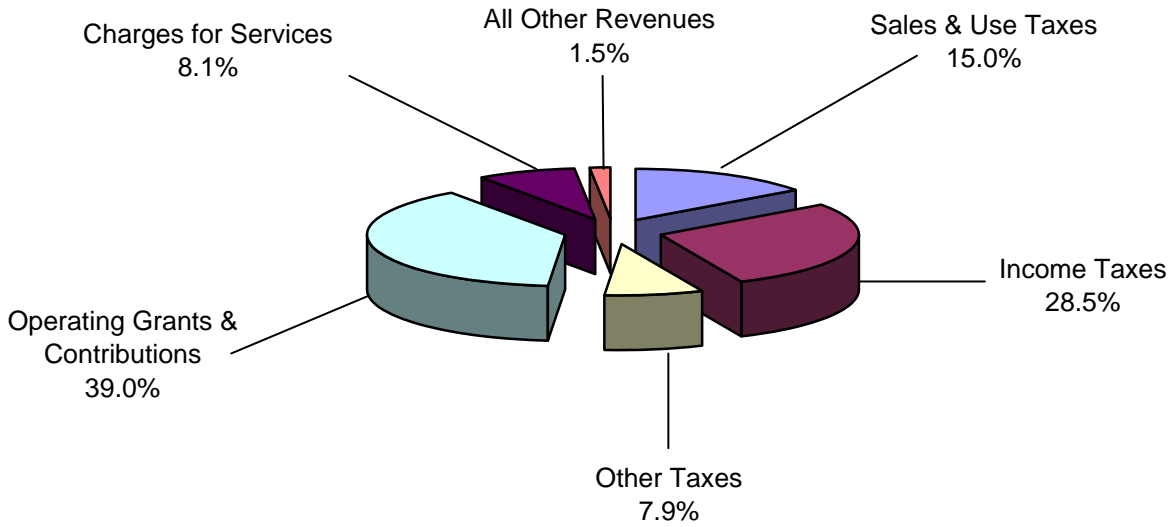
*Fiscal year 2005 amounts have been restated.

As shown on the above schedule, total revenue collections increased by \$743.4 million or 3.6% during fiscal year 2006, while total expenses only increased by \$7.6 million. The increase in revenue was due primarily to an increase in income taxes of \$481.5 million or 9.3% from the prior fiscal year which was mainly caused by an increase in individual income tax. There was also an increase of \$288.4 million or 12.5% in charges for services which was primarily due to Medicaid revenues.

Governmental Activities:

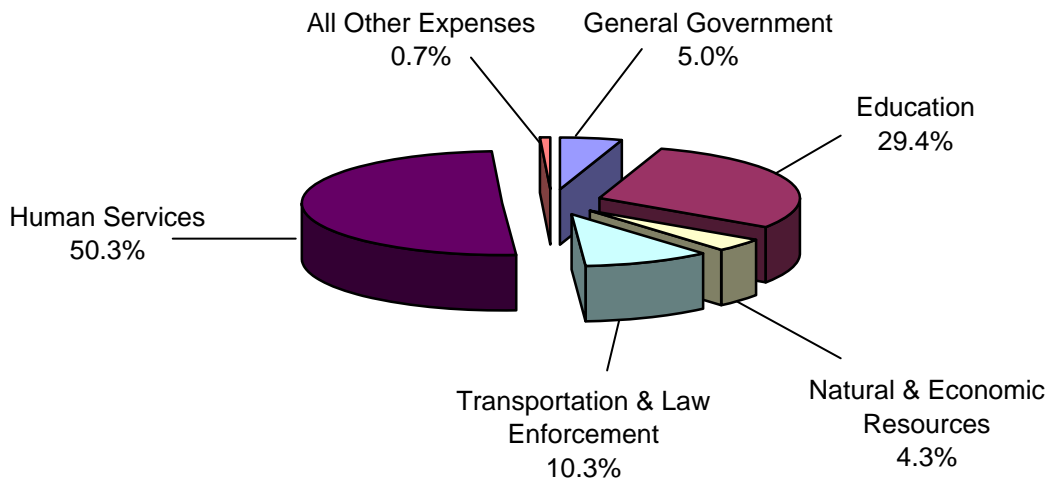
The following chart depicts revenues of the governmental activities for the fiscal year:

Revenues by Source



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

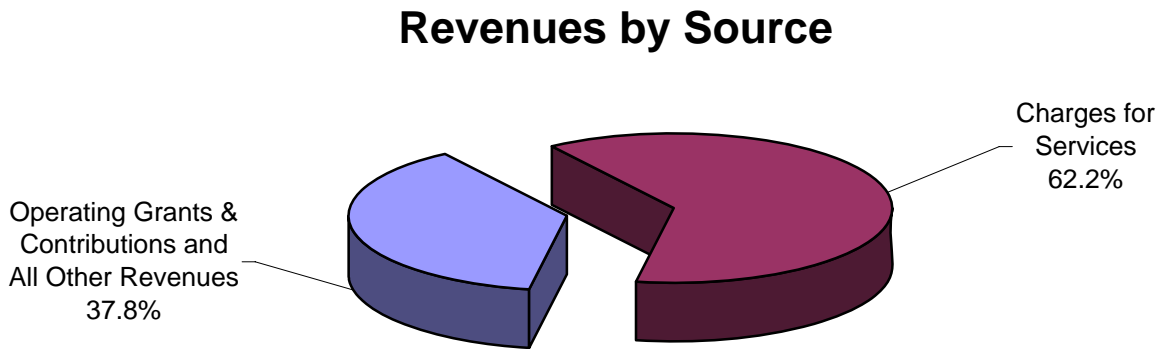
Expenses by Function



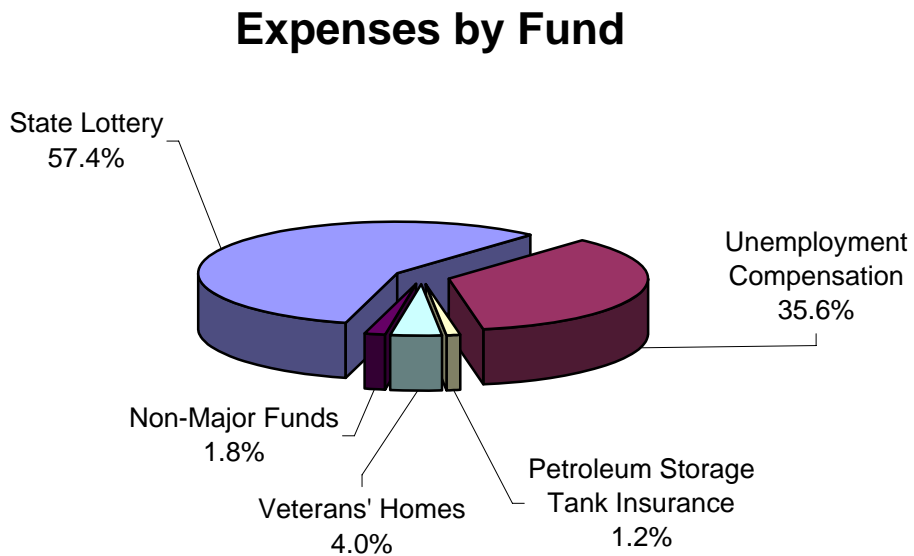
Business-Type Activities:

Net assets of the business-type activities increased by \$173.2 million during the fiscal year due primarily to an increase in unemployment compensation revenues and a decrease of unemployment compensation payments.

The following chart depicts revenues of the business-type activities for the fiscal year:



The following chart depicts expenses of the business-type activities for the fiscal year:



FUND STATEMENT ANALYSIS

Governmental Funds:

At the end of fiscal year 2006, the State's governmental funds reported combined ending fund balances of \$3.9 billion, an increase of \$817.3 million or 26.6% over fiscal year 2005. Approximately 61.1% is unreserved and available for spending at the government's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed: 1) for budget reserve, 2) to pay debt service, 3) for loans receivable, and 4) for a variety of other purposes.

Fund balances (in thousands) for governmental funds are as follows:

	General Fund	Public Education	Conservation and Environmental Protection	Transportation and Law Enforcement	Missouri Road Fund	Non- Major	Total
Unreserved	\$ 988,240	\$ 254,239	\$ 358,510	\$ 300,428	\$ 150,059	\$ 327,664	\$ 2,379,140
Reserved	526,159	46	714,225	5,382	124,383	144,457	1,514,652
Total	\$ 1,514,399	\$ 254,285	\$ 1,072,735	\$ 305,810	\$ 274,442	\$ 472,121	\$ 3,893,792

The general fund is the chief operating fund of the State. At the end of fiscal year 2006, the State's general fund reported a total fund balance of \$1.5 billion. The net increase in fund balance during fiscal year 2006 was \$609.9 million. Revenues of the general fund totaled \$15.8 billion in fiscal year 2006, an increase of \$933.4 million from fiscal year 2005. The major contributing factor to this was an increase in revenue from taxes of \$783.5 million from fiscal year 2005 to fiscal year 2006. The most significant increase was individual income tax, which increased \$492.1 million, and an increase of \$174.5 million in revenue from corporate income tax.

The public education fund category provides general and special education services to the children of the State and other related functions such as library services and student loans. Total fund balance increased by \$24.4 million. Expenditures of the public education funds totaled \$3.9 billion in fiscal year 2006, an increase of \$164.7 million from fiscal year 2005. The major factor that contributed to this was an increase of \$153.7 million in the education expenditures for an increase in aid to educational institutions and school districts.

The conservation and environmental protection fund category provides for the preservation of the State's wildlife and environment. The fund balance increased by \$78.6 million. Revenues of the conservation and environmental protection funds totaled \$354.4 million for fiscal year 2006, an increase of \$30.6 million from fiscal year 2005. The major contributing factor was an increase of \$12.3 million in sales and use tax revenue relating to accounts receivable. Another factor was an increase of \$13.6 million in the contributions and intergovernmental revenues due mainly to an increase of \$8.6 million in federal receipts from the U.S. Environmental Protection Agency.

The transportation and law enforcement fund category provides transportation services, road construction and maintenance, and the enforcement of vehicle laws and traffic safety. The fund balance increased by \$111.2 million. Revenues increased \$94.3 million during fiscal year 2006. The major factor contributing to this was an increase of \$106.1 million in motor vehicle sales tax revenue relating to accounts receivable.

Expenditures of the transportation and law enforcement fund category totaled \$376.8 million for fiscal year 2006, a decrease of \$387.1 million. At the same time, transfers out from this fund category to the Missouri road fund increased by \$436.9 million to accommodate the increase in road construction expenditures under the "Smoother, Safer, Sooner" road construction initiative.

The Missouri road fund accounts for revenues from highway users' fees, federal reimbursements for highway projects, and bond proceeds to be used for costs of constructing and maintaining an adequate state highway system. The fund balance increased by \$15.9 million in fiscal year 2006. Revenues of the Missouri road fund increased during fiscal year 2006 by \$35.0 million primarily due to an increase of \$19.3 million in revenues from licenses, fees, and permits. Out of this amount, \$12.8 million of the increase is from motor vehicle licenses or permits.

Expenditures for the Missouri road fund totaled \$2.0 billion for fiscal year 2006, an increase of \$677.9 million. The expenditure increases were \$314.3 million in transportation and law enforcement and \$367.9 million in capital outlay. The major factor for the increase was significant progress made on the Department of Transportation's "Smoother, Safer, Sooner" road construction initiative.

Proprietary Funds:

The State has three major proprietary funds: State Lottery, Unemployment Compensation, and the Petroleum Storage Tank Insurance Fund. The State Lottery was established in 1986 to account for the sale of lottery tickets and lottery operations. Since 1992, public education has been the sole beneficiary of lottery proceeds. Unemployment Compensation accounts for contributions and payments collected from Missouri employers under the provision of the "Unemployment Compensation Law". This tax finances benefits for workers who become unemployed through no fault of their own. The Petroleum Storage Tank Insurance Fund accounts for moneys collected from transport load fees and participating owners of petroleum storage tanks. The fund pays cleanup expenses from petroleum leaks or spills from underground storage tanks and certain above ground storage tanks as well as third party property damage or bodily injury resulting from such discharges. This fund is one of the largest insurers of tanks in the country.

The State Lottery Fund's net assets decreased by \$6.0 million. Expenses increased by \$90.2 million during the fiscal year which was partially offset by an increase in revenues. The increase in expenses was mainly due to an \$84.5 million increase in prizes expensed.

The Unemployment Compensation Fund's net assets increased by \$164.6 million due primarily to a decrease of \$88.2 million in unemployment benefit expenses and an increase in employer contributions of \$81.2 million.

The Petroleum Storage Tank Insurance Fund's net assets increased by \$13.7 million. Expenses decreased by \$12.7 million primarily due to a decrease of \$12.1 million in environmental cleanup.

GENERAL FUND BUDGETARY HIGHLIGHTS

The original budget is the first complete appropriated budget that is truly agreed to and finally passed, and signed by the Governor. The final budget includes emergency and supplemental appropriations, transfers, and increases to estimated appropriations.

Budgeted appropriations for fiscal year 2006 from the general fund were \$16.8 billion original budget and \$17.2 billion revised budget. Actual spending was \$16.2 billion. Reasons for the budget variances include:

- Federal grants received were lower than appropriation authority.
- Multiple year grants are appropriated in one year but the expenditures may occur over several years.
- Appropriation authority exceeded cash available for expenditures.

Budgeted revenues/transfers in for fiscal year 2006 for the general fund was \$15.4 billion original budget and \$15.7 billion revised budget. Actual revenue/transfers in was \$16.7 billion. A reason for the budget variances is that revenue growth in fiscal year 2006 outpaced economic growth forecasts for the State. This was due to the 2005 hurricane season and the resulting spike in energy prices not having as severe an impact as feared. Corporate profits also surged nationally and contributed to robust gains in taxable receipts at both the state and national levels. Further, sustained strength of consumer spending, particularly in the housing sector, as well as continued business investment kept the economy growing at a steady pace.

Refer to the *Notes to RSI*, Budgetary Reporting, on page 92 for more information on budgetary variances.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets:

The State's investment in capital assets for its governmental and business-type activities as of June 30, 2006, was \$28.1 billion (net of accumulated depreciation). This investment in capital assets includes construction in progress, infrastructure in progress, land, land improvements, buildings and improvements, equipment, and infrastructure.

Capital Assets of the State include (in thousands):

	Governmental Activities	Business-Type Activities	Total
Construction in Progress	\$ 565,743	\$ 4,544	\$ 570,287
Infrastructure in Progress	2,797,922	---	2,797,922
Land	2,558,380	6,463	2,564,843
Land Improvements	149,127	6,846	155,973
Buildings and Improvements	2,381,243	26,600	2,407,843
Equipment	1,142,745	47,310	1,190,055
Infrastructure	39,108,601	---	39,108,601
<i>Subtotal</i>	48,703,761	91,763	48,795,524
Less Accumulated Depreciation	(20,691,701)	(52,156)	(20,743,857)
Total Capital Assets, Net	\$ 28,012,060	\$ 39,607	\$ 28,051,667

Additional information on capital assets can be found in *Note 5* of this report.

Long-Term Debt:

At the end of fiscal year 2006, the State had total general obligation and other bonded debt outstanding of \$2.6 billion. Of this amount, \$739.9 million comprises debt backed by the full faith and credit of the government.

Principal amounts retired in fiscal year 2006 were \$50,975,000 for general obligation bonds and \$87,335,000 for other revenue bonds.

The State of Missouri is proud to be one of only six states to maintain a Triple-A credit rating from all three major credit rating agencies (Moody's Investor Services, Inc., Standard and Poor's, and Fitch Ratings, Inc.) on the State's General Obligation Bonds.

Outstanding Bonds Payable of the State include (in thousands):

	Governmental Activities	Component Units	Total
General Obligation Bonds	\$ 739,935	\$ ---	\$ 739,935
Other Bonds	1,873,140	1,075,274	2,948,414
Total	\$ 2,613,075	\$ 1,075,274	\$ 3,688,349

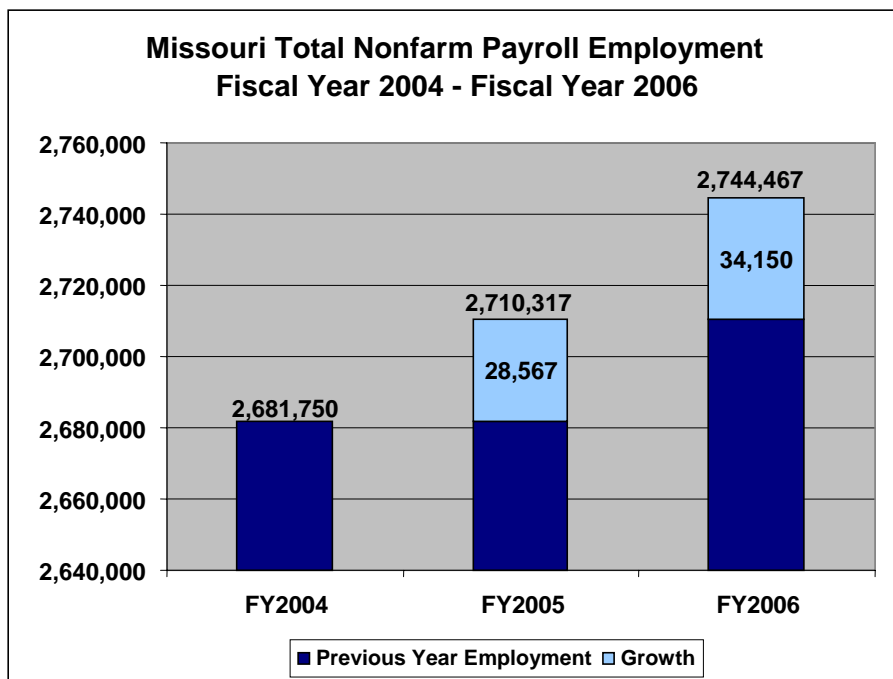
Additional information on long-term debt can be found in *Notes 11, 12, and 13* of this report.

ECONOMIC OUTLOOK AND NEXT YEAR'S BUDGET

The State of Missouri completed fiscal year 2006 with a balanced budget. Net general revenue collections increased 9.2% from fiscal year 2005 ending with an amount of \$7.3 billion. Also, consumer spending kept the economy growing at a steady pace. The approved budget for fiscal year 2007 anticipates an increase of 0.4% from fiscal year 2006.

Missouri's economic future remains positive as evidenced by economic indicators and statistics. Personal income growth in the second quarter of 2006 was 1.8% compared to a national growth rate of 1.7%. Missouri ranked 9th among the states in quarter-to-quarter personal income growth. Exports increased from \$9.7 billion in fiscal year 2005 to \$11.4 billion in fiscal year 2006. The Purchasing Manager's Index, which measures key factors such as inventories, prices, and employment, remained above 50 during fiscal year 2006. A score above 50 indicates an expanding economy.

Missouri's unemployment rate continued to drop in fiscal year 2006. At June 2006, the unemployment rate was 4.7% compared to the June 2005 unemployment rate of 5.3%. The national unemployment rate was 4.6% in June 2006.



Sources: MERIC and U.S. Bureau of Labor Statistics

Due to the fact that Missouri is a manufacturing, financial, and agricultural state, its economy tends to mimic that of the nation. The national economy is expected to grow at a steadier pace in fiscal year 2007; consequently Missouri's employment is expected to continue to grow in 2007. The graph above shows total nonfarm employment in Missouri. At the end of fiscal year 2006, total employment was approximately 2.7 million, up 34,000 from fiscal year 2005. The increase in total employment for fiscal year 2006 was greater than the increase in fiscal year 2005. The increase was due to increased employment in all industries except manufacturing, information, and other services.

In spite of continued growth, Missouri faces several funding challenges in mandatory programs such as education, health care, and the prison system.

Funding remains a challenge for Missouri schools. A revision to the school funding formula was made in 2005 in response to a lawsuit filed by 257 of the 524 Missouri schools against the State in January of 2004 over both the equity in funding between schools and the overall adequacy of school funding. The revision in the school funding formula calls for \$800 million to be phased in by the 2012–2013 school year. However, an amended lawsuit was filed in November 2005 and is expected to go to trial in January 2007. Plaintiffs seek approximately \$2 billion annually. In fiscal year 2007, funding for Missouri Public schools increased by \$173.4 million for a total funding level of approximately \$1.07 billion.

State universities and community colleges have seen both substantial funding cuts and tuition increases during past years. In fiscal year 2007, funding for higher education in Missouri will increase by nearly \$20 million. This includes an increase of \$17.2 million for public four-year colleges and universities and \$2.7 million for community colleges.

Over 900,000, or 1 in 6, Missourians will receive Medicaid in fiscal year 2007. Expected Medicaid growth over expected revenue growth for the Medicare system in fiscal year 2006 prompted the State to implement changes to sustain the program, including reducing income eligibility levels, annual reverification of Medicaid eligibility, general relief medical assistance programs, and \$474 million in funding cuts. The Medicaid Reform Commission was also formed with the purpose of making recommendations to the General Assembly on redesigning, reforming, or restructuring a new Medicaid system to be enacted on June 30, 2008. For fiscal year 2007, the Medicare system is receiving increased funding of \$617 million, including increased funding for existing medicare programs and increased funding for pharmacy costs to fund drugs that are excluded under the Medicare Modernization Act – Part D.

The Medicare program is also at risk from potential changes at the federal level, which includes reducing the Medicaid provider rate cap from 6% to 3%, significantly affecting Missouri. This reduction would apply to hospitals, nursing homes, pharmacies, and managed care and could result in a loss of approximately \$500 million in provider taxes, plus federal match of approximately \$800 million, for a total loss of \$1.3 billion. The loss of these funds would have to be replaced by State funds or the Medicaid program would have to be significantly reduced.

Tougher crime laws, rising costs, and budgetary pressures have made it increasingly costly for the State's correctional facilities. The cost of maintaining these facilities will rise to approximately \$641 million for fiscal year 2007, up from \$589 million in fiscal year 2006. This is due partly to an increase in the prison population. The percentage increase in the male population from December 31, 2004 to December 31, 2005 was 0.008%, while the increase in the female prison population during that time period was 0.046%. In fiscal year 2007, \$120 million in revenue bonds were issued to build a new women's prison at Chillicothe.

Despite funding challenges, the State is working to stimulate the economy, increase efficiency, and decrease costs. In the past year, Missouri has passed House Bill 1270 which established the Missouri Renewable Fuel Standard Act, which requires most Missouri gasoline to contain at least 10% ethanol by January 1, 2008. This law benefits consumers, the economy, the environment, and Missouri farmers. Division of Facilities Management and Design & Construction were consolidated in fiscal year 2006, which eliminated the duplication of services that previously existed between the two divisions, increasing efficiency and decreasing costs. Also, Missouri created the Healthcare Technology Fund, which will recommend ways to encourage the implementation of technologies intended to improve the safety, quality, and costs of health care services in the State.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the State's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Office of Administration, Division of Accounting, P.O. Box 809, Jefferson City, MO 65102.