

# SECURITIES AND EXCHANGE COMMISSION

## FORM 485BPOS

Post-effective amendments [Rule 485(b)]

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### FILER

#### **INVESTORS QUALITY TAX EXEMPT TRUST 35TH MULTI SERIES**

CIK: **760778** | State of Incorpor.: **DE** | Fiscal Year End: **1231**  
Type: **485BPOS** | Act: **33** | File No.: **002-95343** | Film No.: **95514078**

Business Address  
*ONE PARKVIEW PLAZA, UIT  
ADMN  
C/O VAN KAMPEN MERRITT  
INC  
OAKBROOK TERRACE IL  
60181*

Securities and Exchange Commission  
Washington, D. C. 20549-1004

Post-Effective  
Amendment No. 10

to  
Form S-6

For Registration under the Securities Act of 1933 of  
Securities of Unit Investment Trusts Registered on  
Form N-8B-2

Investors' Quality Tax-Exempt Trust, 35th Multi-Series  
(Exact Name of Trust)

Van Kampen American Capital Distributors, Inc.  
(Exact Name of Depositor)

One Parkview Plaza  
Oakbrook Terrace, Illinois 60181  
(Complete address of Depositor's principal executive offices)

|   |                           |
|---|---------------------------|
| Van Kampen American Capital Distributors, Inc.    | Chapman and Cutler        |
| Attention: Don G. Powell                          | Attention: Mark J. Kneedy |
| One Parkview Plaza                                | 111 West Monroe Street    |
| Oakbrook Terrace, Illinois 60181                  | Chicago, Illinois 60603   |
| (Name and complete address of agents for service) |                           |

( X ) Check if it is proposed that this filing will become effective  
on February 22, 1995 pursuant to paragraph (b) of Rule 485.

Ohio/15

35th MULTI-SERIES

PROSPECTUS PART ONE

NOTE: Part One of this Prospectus may not be distributed unless accompanied by  
Part Two. Please retain both parts of this Prospectus for future reference.

In the opinion of counsel, interest to the Fund and to Unitholders, with  
certain exceptions, is exempt under existing law from all Federal income  
taxes. In addition the interest income of each Trust is, in the opinion of  
counsel, exempt to the extent indicated from state and local taxes, when held  
by residents of the state where the issuer of Bonds in such Trust are located.  
Capital gains, if any, are subject to Federal tax.

#### THE TRUST

The above-named series of Investors' Quality Tax-Exempt Trust, Multi-Series  
(the "Fund") consists of a separate unit investment trust. The trust in the  
Fund is referred to herein as the "Trust". The Trust consists of  
interest-bearing obligations (the "Bonds" or "Securities") issued by or on  
behalf of municipalities and other governmental authorities, the interest on  
which is, in the opinion of recognized bond counsel to the issuing  
governmental authority, exempt from all Federal income taxes under existing  
law. In addition, the interest income of the Trust is, in the opinion of  
counsel, exempt to the extent indicated from state and local taxes, when held  
by residents of the state where the issuers of Bonds in such Trust are  
located. Each Unit represents a fractional undivided interest in the principal  
and net income of the Trust (see "Summary of Essential Information" in this  
Part One and "Description of the Fund" in Part Two).

The Units being offered by this Prospectus are issued and outstanding Units  
which have been purchased by the Sponsor in the secondary market or from the  
Trustee after having been tendered for redemption. The profit or loss  
resulting from the sale of Units will accrue to the Sponsor. No proceeds from  
the sale of Units will be received by the Fund.

#### PUBLIC OFFERING PRICE

The Public Offering Price of the Units of the Trust is equal to the aggregate

bid price of the Bonds in the portfolio divided by the number of Units outstanding, plus a sales charge. The sales charge is based upon the years to average maturity of the Bonds in the portfolio. The sales charge ranges from 1.5% of the Public Offering Price (1.523% of the aggregate bid price of the Bonds) for a Trust with a portfolio with less than two years to average maturity to 5.7% of the Public Offering Price (6.045% of the aggregate bid price of the Bonds) for a Trust with a portfolio with sixteen or more years to average maturity. See "Summary of Essential Information" in this Part One.

ESTIMATED CURRENT AND LONG-TERM RETURNS

Estimated Current and Long-Term Returns to Unitholders are indicated under "Summary of Essential Information" in this Part One. The methods of calculating Estimated Current Returns and Estimated Long-Term Return are set forth in Part Two of this Prospectus.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The Date of this Prospectus is February 22, 1995

Van Kampen American Capital  
 INVESTORS' QUALITY TAX-EXEMPT TRUST, SERIES 35  
 Summary of Essential Financial Information  
 As of December 6, 1994

Sponsor: Van Kampen American Capital Distributors, Inc.  
 Evaluator: American Portfolio Evaluation Services  
 (A division of a subsidiary of the Sponsor)  
 Trustee: The Bank of New York

The income, expense and distribution data set forth below have been calculated for Unitholders electing to receive monthly distributions. Unitholders choosing distributions semi-annually will receive a slightly higher net annual interest income because of the lower Trustee's fees and expenses under such plan.

<TABLE>  
 <CAPTION>

|   | Ohio<br>Trust   |
|---|-----------------|
| <S>   | <C>             |
| General Information   |                 |
| Principal Amount (Par Value) of Securities.....                                 | \$ 1,890,000    |
| Number of Units.....  | 3,006           |
| Fractional Undivided Interest in Trust per Unit.....                            | 1/3,006         |
| Public Offering Price: .....  |                 |
| Aggregate Bid Price of Securities in Portfolio.....                             | \$ 1,761,658.10 |
| Aggregate Bid Price of Securities per Unit.....                                 | \$ 586.05       |
| Sales charge 4.932% (4.7% of Public Offering Price excluding principal cash)... | \$ 28.89        |
| Principal Cash per Unit.....  | \$ (.24)        |
| Public Offering Price per Unit <F1>.....  | \$ 614.70       |
| Redemption Price per Unit.....  | \$ 585.81       |
| Excess of Public Offering Price per Unit over Redemption Price per Unit.....    | \$ 28.89        |
| Minimum Value of the Trust under which Trust Agreement may be terminated.....   | \$ 595,000.00   |
| Annual Premium on Portfolio Insurance.....                                      | \$ --           |
| Evaluator's Annual Fee <F3>.....  | \$ 2,138        |
| Special Information   |                 |
| Calculation of Estimated Net Annual Unit Income: .....                          |                 |
| Estimated Annual Interest Income per Unit.....                                  | \$ 53.92        |
| Less: Estimated Annual Expense excluding Insurance.....                         | \$ 2.68         |
| Less: Annual Premium on Portfolio Insurance.....                                | \$ --           |
| Estimated Net Annual Interest Income per Unit.....                              | \$ 51.24        |
| Calculation of Estimated Interest Earnings per Unit: .....                      |                 |
| Estimated Net Annual Interest Income.....                                       | \$ 51.24        |
| Divided by 12.....  | \$ 4.27         |
| Estimated Daily Rate of Net Interest Accrual per Unit.....                      | \$ .14233       |
| Estimated Current Return Based on Public Offering Price <F2>.....               | 8.33%           |
| Estimated Long-Term Return <F2>.....  | 6.12%           |

<FN>  
 <F1>Plus accrued interest to the date of settlement (five business days after purchase) of \$8.15 for the Trust.

<F2>The Estimated Current Returns and Estimated Long-Term Returns are increased for transactions entitled to a reduced sales charge.

<F3>Notwithstanding information to the contrary in Part Two of this Prospectus, the Trust Indenture provides that as compensation for its services, the Evaluator shall receive a fee of \$.30 per \$1,000 principal amount of Bonds per Trust annually. This fee may be adjusted for increases in consumer prices for

services under the category "All Services Less Rent of Shelter" in the Consumer Price Index.

</TABLE>

Evaluations for purpose of sales, purchase or redemption of Units are made as of 4:00 P.M. Eastern time on days of trading on the New York Stock Exchange next following receipt of an order for a sale or purchase of Units or receipt by The Bank of New York of Units tendered for redemption.

<TABLE>

<CAPTION>

<S> <C>  
 Minimum Principal Distribution.....\$1.00 per Unit  
 Date of Deposit.....February 14, 1985  
 Mandatory Termination Date.....December 31, 2034  
 Evaluator's Annual Supervisory Fee...Maximum of \$0.25 per Unit  
 </TABLE>

<TABLE>

<CAPTION>

<S> <C>  
 FIRST day of the month as follows: monthly - each month; semi-annual - May and  
 Record and Computation Dates...November  
 FIFTEENTH day of the month as follows: monthly - each month; semi-annual - May  
 Distribution Dates.....and November  
 \$1.24 and \$0.69 per \$1,000 principal amount of Bonds respectively, for those  
 Trustee's Annual Fee.....portions of the Trusts under the monthly and semi-annual distribution plans.  
 </TABLE>

PORTFOLIO

In selecting Bonds for the Ohio Investors' Quality Tax-Exempt Trust, Series 15, the following facts, among others, were considered: (i) either the Standard & Poor's Corporation rating of the Bonds was in no case less than "A-", or the Moody's Investors Service, Inc. rating of the Bonds was in no case less than "A", including provisional or conditional ratings, respectively (see "Description of Securities Ratings" in Part Two), (ii) the prices of the Bonds relative to other bonds of comparable quality and maturity and (iii) the diversification of Bonds as to purpose of issue and location of issuer. As of October 31, 1994, the Trust consists of 9 issues which are payable from the income of a specific project or authority. The portfolio is divided by purpose of issue as follows: Escrowed, 2 (13%); General Obligation, 2 (19%); Industrial Revenue, 1 (5%); Multi-Family, 1 (5%); Other Care Facility, 1 (25%); Pre-refunded, 1 (24%) and Single Family, 1 (9%). See "Bond Portfolio" herein and "Description of Securities Ratings" in Part Two.

PER UNIT INFORMATION

<TABLE>

<CAPTION>

|  | 1985<F1>  | 1986        | 1987        | 1988        | 1989        |
|--|-----------|-------------|-------------|-------------|-------------|
| <S>  | <C>       | <C>         | <C>         | <C>         | <C>         |
| Net asset value per Unit at beginning of period.....   | \$ 951.00 | \$ 982.73   | \$ 1,131.88 | \$ 995.40   | \$ 1,035.07 |
| Net asset value per Unit at end of period.....   | \$ 982.73 | \$ 1,131.88 | \$ 995.40   | \$ 1,035.07 | \$ 1,015.04 |
| Distributions to Unitholders of investment income including accrued interest to carry paid on Units redeemed (average Units outstanding for entire period) <F2>..... | \$ 26.88  | \$ 93.83    | \$ 90.97    | \$ 91.11    | \$ 90.74    |
| Distributions to Unitholders from Bond redemption proceeds (average Units outstanding for entire period).....  | \$ --     | \$ --       | \$ 1.65     | \$ --       | \$ 11.27    |
| Unrealized appreciation (depreciation) of Bonds (per Unit outstanding at end of period).....   | \$ (4.74) | \$ 151.76   | \$ (134.89) | \$ 39.71    | \$ (8.10)   |
| Distributions of investment income by frequency of payment <F2>  |           |             |             |             |             |
| Monthly.....   | \$ 44.25  | \$ 90.96    | \$ 90.87    | \$ 90.72    | \$ 90.01    |
| Semiannual.....  | \$ 6.35   | \$ 91.52    | \$ 91.52    | \$ 91.52    | \$ 90.90    |
| Units outstanding at end of period.....  | 3,020     | 3,020       | 3,020       | 3,019       | 3,017       |

<FN>

<F1>For the period from February 14, 1985 (date of deposit) through October 31, 1985.

<F2>Unitholders may elect to receive distributions on a monthly, quarterly or semi-annual basis.

</TABLE>

PER UNIT INFORMATION (continued)

<TABLE>

<CAPTION>

|   | 1990        | 1991      | 1992      | 1993      | 1994      |
|---|-------------|-----------|-----------|-----------|-----------|
| <S>   | <C>         | <C>       | <C>       | <C>       | <C>       |
| Net asset value per Unit at beginning of period.....        | \$ 1,015.04 | \$ 980.53 | \$ 971.14 | \$ 754.90 | \$ 718.72 |
| Net asset value per Unit at end of period.....              | \$ 980.53   | \$ 971.14 | \$ 754.90 | \$ 718.72 | \$ 645.47 |
| Distributions to Unitholders of investment income including |             |           |           |           |           |

|  |    |         |    |       |    |        |    |       |    |         |
|--|----|---------|----|-------|----|--------|----|-------|----|---------|
| accrued interest to carry paid on Units redeemed<br>(average Units outstanding for entire<br>period) <F2>.....   | \$ | 88.49   | \$ | 86.88 | \$ | 85.87  | \$ | 62.94 | \$ | 56.35   |
| Distributions to Unitholders from Bond redemption proceeds<br>(average Units outstanding for entire period)..... | \$ | 19.25   | \$ | 12.95 | \$ | 198.94 | \$ | 53.32 | \$ | 28.92   |
| Unrealized appreciation (depreciation) of Bonds (per Unit<br>outstanding at end of period).....                  | \$ | (15.25) | \$ | 3.34  | \$ | 15.25  | \$ | 17.52 | \$ | (44.69) |
| Distributions of investment income by frequency of<br>payment <F2>   |    |         |    |       |    |        |    |       |    |         |
| Monthly.....   | \$ | 88.15   | \$ | 86.44 | \$ | 83.74  | \$ | 60.22 | \$ | 55.41   |
| Semiannual.....  | \$ | 89.46   | \$ | 87.68 | \$ | 88.86  | \$ | 67.92 | \$ | 57.51   |
| Units outstanding at end of period.....  |    | 3,016   |    | 3,016 |    | 3,016  |    | 3,016 |    | 3,016   |

<FN>  
<F1>For the period from February 14, 1985 (date of deposit) through October 31, 1985.

<F2>Unitholders may elect to receive distributions on a monthly, quarterly or semi-annual basis.  
</TABLE>

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors of Van Kampen American Capital Distributors, Inc.  
and the Unitholders of Investors' Quality Tax-Exempt Trust, 35th Multi-Series:

We have audited the accompanying statement of condition (including the analysis of net assets) and the related portfolio of Investors' Quality Tax-Exempt Trust, 35th Multi-Series (Ohio Trust) as of October 31, 1994, and the related statements of operations and changes in net assets for the three years ended October 31, 1994. These statements are the responsibility of the Trustee and the Sponsor. Our responsibility is to express an opinion on such statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our procedures included confirmation of tax-exempt securities owned at October 31, 1994 by correspondence with the Trustee. An audit also includes assessing the accounting principles used and significant estimates made by the Trustee and the Sponsor, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the statements referred to above present fairly, in all material respects, the financial position of Investors' Quality Tax-Exempt Trust, 35th Multi-Series (Ohio Trust) as of October 31, 1994, and the results of operations and changes in net assets for the three years ended October 31, 1994, in conformity with generally accepted accounting principles.

GRANT THORNTON LLP

Chicago, Illinois  
December 2, 1994

<TABLE>  
INVESTORS' QUALITY TAX-EXEMPT TRUST  
35th MULTI-SERIES  
Statement of Condition  
October 31, 1994

<CAPTION>

|  |     | Ohio<br>Trust |
|--|-----|---------------|
| <S>  | <C> |               |
| Trust property   |     |               |
| Cash.....  | \$  | 15,762        |
| Tax-exempt securities at market value, (cost \$1,822,873) (note 1).....            |     | 1,883,103     |
| Accrued interest.....  |     | 47,885        |
| Receivable for securities sold.....  |     | --            |
|  | \$  | 1,946,750     |
| Liabilities and interest to Unitholders  |     |               |
| Cash overdraft.....  | \$  | --            |
| Redemptions payable.....   |     | --            |
| Interest to Unitholders.....   |     | 1,946,750     |
|  | \$  | 1,946,750     |
| Analysis of Net Assets   |     |               |
| Interest of Unitholders (3,016 Units of fractional undivided interest outstanding) |     |               |
| Cost to original investors of 3,020 Units (note 1).....                            | \$  | 3,020,000     |
| Less initial underwriting commission (note 3).....                                 |     | 147,954       |
|  |     | 2,872,046     |
| Less redemption of 4 Units.....  |     | 3,880         |

|   |              |
|---|--------------|
|   | 2,868,166    |
| Undistributed net investment income                                   |              |
| Net investment income.....  | 2,399,482    |
| Less distributions to Unitholders.....                                | 2,335,865    |
|   | 63,617       |
| Realized gain (loss) on Bond sale or redemption.....                  | (61,123)     |
| Unrealized appreciation (depreciation) of Bonds (note 2).....         | 60,230       |
| Distributions to Unitholders of Bond sale or redemption proceeds..... | (984,140)    |
| Net asset value to Unitholders.....                                   | \$ 1,946,750 |
| Net asset value per Unit (3,016 Units outstanding).....               | \$ 645.47    |

</TABLE>

The accompanying notes are an integral part of this statement.

<TABLE>

OHIO INVESTORS' QUALITY TAX-EXEMPT TRUST, SERIES 15  
Statements of Operations  
Years ended October 31,

<CAPTION>

|  | 1992       |  | 1993       |  | 1994       |
|--|------------|--|------------|--|------------|
| <S>  | <C>        |  | <C>        |  | <C>        |
| Investment income  |            |  |            |  |            |
| Interest income.....   | \$ 245,976 |  | \$ 186,657 |  | \$ 173,749 |
| Expenses   |            |  |            |  |            |
| Trustee fees and expenses.....                                     | 4,828      |  | 4,289      |  | 3,997      |
| Evaluator fees.....  | 855        |  | 2,525      |  | 2,138      |
| Supervisory fees.....  | 297        |  | 964        |  | 795        |
| Total expenses.....  | 5,980      |  | 7,778      |  | 6,930      |
| Net investment income.....   | 239,996    |  | 178,879    |  | 166,819    |
| Realized gain (loss) from Bond sale or redemption                  |            |  |            |  |            |
| Proceeds.....  | 575,000    |  | 150,800    |  | 87,250     |
| Cost.....  | 654,191    |  | 141,011    |  | 83,007     |
| Realized gain (loss).....  | (79,191)   |  | 9,789      |  | 4,243      |
| Net change in unrealized appreciation (depreciation) of Bonds...   | 45,986     |  | 52,846     |  | (134,794)  |
| NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS.\$ | 206,791    |  | \$ 241,514 |  | \$ 36,268  |

</TABLE>

<TABLE>

Statements of Changes in Net Assets  
Years ended October 31,

<CAPTION>

|   | 1992         |  | 1993         |  | 1994         |
|---|--------------|--|--------------|--|--------------|
| <S>   | <C>          |  | <C>          |  | <C>          |
| Increase (decrease) in net assets   |              |  |              |  |              |
| Operations:   |              |  |              |  |              |
| Net investment income.....  | \$ 239,996   |  | \$ 178,879   |  | \$ 166,819   |
| Realized gain (loss) on Bond sale or redemption.....  | (79,191)     |  | 9,789        |  | 4,243        |
| Net change in unrealized appreciation (depreciation) of Bonds.....  | 45,986       |  | 52,846       |  | (134,794)    |
| Net increase (decrease) in net assets resulting from operations.....  | 206,791      |  | 241,514      |  | 36,268       |
| Distributions to Unitholders from:  |              |  |              |  |              |
| Net investment income.....  | (258,983)    |  | (189,812)    |  | (169,950)    |
| Bonds sale or redemption proceeds.....  | (600,003)    |  | (160,813)    |  | (87,223)     |
| Redemption of Units   |              |  |              |  |              |
| Total increase (decrease).....  | (652,195)    |  | (109,111)    |  | (220,905)    |
| Net asset value to Unitholders  |              |  |              |  |              |
| Beginning of period.....  | 2,928,961    |  | 2,276,766    |  | 2,167,655    |
| End of period (including undistributed net investment income of \$77,681, \$66,748 and \$63,617, respectively)..... | \$ 2,276,766 |  | \$ 2,167,655 |  | \$ 1,946,750 |

</TABLE>

The accompanying notes are an integral part of these statements.

<TABLE>

35TH MULTI-SERIES  
OHIO INVESTORS' QUALITY TAX-EXEMPT TRUST  
PORTFOLIO as of October 31, 1994

<CAPTION>

| Port-<br>folio<br>Item | Aggregate<br>Principal | Name of Issuer, Title, Interest Rate and<br>Maturity Date  | Rating<br>(Note 2) | Redemption<br>Feature<br>(Note 2) | October 31,<br>1994<br>Market<br>Value<br>(Note 1) |
|------------------------|------------------------|--|--------------------|-----------------------------------|--|
| <S>                    | <C>                    | <C>  | <C>                | <C>                               | <C>  |
| A                      | \$ - 0 -               | Salem, Ohio Hospital Revenue Bonds (North<br>Columbiana Hospital) 8.000% Due 12/01/00 ....               |                    | \$                                | - 0 -  |
| B                      | 100,000                | Warren, Ohio New Public Housing Authority<br>Revenue Bonds, Series 1964 3.250% Due<br>05/01/05 .....     | AAA                | 1995 @ 101                        | 74,548   |
| C                      | 120,000                | Youngstown, Ohio New Public Housing<br>Authority Revenue Bonds, Series 1971 5.000%<br>Due 05/01/06 ..... | AAA                | 1995 @ 102                        | 107,003  |

|   |              |   |     |                               |                  |
|---|--------------|---|-----|-------------------------------|------------------|
| D | 250,000      | City of Columbus, Ohio General Obligation Unlimited Tax Various Purpose Bonds 5.750% Due 10/01/07 .....   | AA+ |                               | 240,465          |
| E | 30,000       | Ohio Water Development Authority State of Ohio Water Development Revenue Bonds Safe Water Series III 9.000% Due 12/01/10** .....  | AAA |                               | 33,591           |
| F | 225,000      | Ohio Water Development Authority State of Ohio Water Development Revenue Bonds Safe Water Series II 9.375% Due 12/01/10** .....   | AAA |                               | 265,037          |
| G | - 0 -        | Ohio Housing Finance Agency Single Family Mortgage Revenue Bonds, 1983 Series A 9.375% Due 05/15/13 .....   |     |                               | - 0 -            |
| H | 500,000      | City of North Canton, Ohio Economic Development Revenue Bonds, Series 1984 (FHA Insured Mortgage Loan -- St. Luke Lutheran Home for the Aging Project) 12.375% Due 08/01/14 ..... | AA+ | 2005 @ 103<br>1996 @ 100 S.F. | 511,440          |
| I | 500,000      | County of Lucas, Ohio Hospital Improvement Revenue Bonds (The Toledo Hospital Project) 0M-12.875% Due 08/01/14 500M-10.650% Due 08/15/14 .....                                    | AAA | 1995 @ 102                    | - 0 -<br>528,330 |
| J | 100,000      | State of Ohio Pollution Control Revenue Bonds, Series 1984 (Buckeye Power Inc. Project) 10.875% Due 11/01/14 .....  | AA  | 1995 @ 103<br>2009 @ 100      | 103,000          |
| K | 175,000      | Ohio Housing Finance Agency Single Family Mortgage Revenue Bonds, 1984 Series A 0.000% Due 08/01/15 .....   | A   | 2011 @ 58.521 S.F.            | 19,689           |
|   | \$ 2,000,000 |   |     |                               | \$ 1,883,103     |

</TABLE>

The accompanying notes are an integral part of this statement.

\*\* The issuer of these Bonds has placed funds or securities in escrow against payment of the issue on the date or dates indicated.

INVESTORS' QUALITY TAX-EXEMPT TRUST35th MULTI-SERIESNotes to Financial StatementsOctober 31, 1992, 1993 and 1994

#### NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Security Valuation - Tax-exempt municipal securities are stated at the value determined by the Evaluator, American Portfolio Evaluation Services (a division of a subsidiary of the Sponsor). The Evaluator may determine the value of the Bonds (1) on the basis of current bid prices of the Bonds obtained from dealers or brokers who customarily deal in Bonds comparable to those held by the Trust, (2) on the basis of bid prices for comparable Bonds, (3) by determining the value of the Bonds by appraisal or (4) by any combination of the above.

Security Cost - The original cost to the Trust was based on the determination by Interactive Data Services, Inc. of the offering prices of the Bonds on the date of deposit (February 14, 1985). Since the valuation is based upon the bid prices, the Trust recognized a downward adjustment of \$23,921 on the date of deposit resulting from the difference between the bid and offering prices. This downward adjustment was included in the aggregate amount of unrealized depreciation reported in the financial statements for the Trust for the period ended October 31, 1985.

Unit Valuation - The redemption price per Unit is the pro rata share of each Unit in the Trust based upon (1) the cash on hand in the Trust or monies in the process of being collected, (2) the Bonds in the Trust based on the value determined by the Evaluator and (3) interest accrued thereon, less accrued expenses of the Trust, if any.

Federal Income Taxes - The Trust is not taxable for Federal income tax purposes. Each Unitholder is considered to be the owner of a pro rata portion of such Trust and, accordingly, no provision has been made for Federal income taxes.

Other - The financial statements are presented on the accrual basis of accounting. Any realized gains or losses from securities transactions are reported on an identified cost basis.

#### NOTE 2 - PORTFOLIO

Ratings - The source of all ratings, exclusive of those designated N/R or \* is Standard & Poor's Corporation. Ratings marked \* are by Moody's Investors Service, Inc. as these Bonds are not rated by Standard & Poor's Corporation. N/R indicates that the Bond is not rated by Standard & Poor's Corporation or Moody's Investors Service, Inc. The ratings shown represent the latest published ratings of the Bonds. For a brief description of rating symbols and their related meanings, see "Description of Securities Ratings" in Part Two.

Redemption Feature - There is shown under this heading the year in which each issue of Bonds is initially or currently callable and the call price for that year. Each issue of Bonds continues to be callable at declining prices thereafter (but not below par value) except for original issue discount Bonds which are redeemable at prices based on the issue price plus the amount of original issue discount accreted to redemption date plus, if applicable, some premium, the amount of which will decline in subsequent years. "S.F." indicates a sinking fund is established with respect to an issue of Bonds. Redemption pursuant to call provisions generally will, and redemption pursuant to sinking fund provisions may, occur at times when the redeemed Bonds have an offering side evaluation which represents a premium over par. To the extent that the Bonds were deposited in the Trust at a price higher than the price at which they are redeemed, this will represent a loss of capital when compared with the original Public Offering Price of the Units. Conversely, to the extent that the Bonds were acquired at a price lower than the redemption price, this will represent an increase in capital when compared with the original Public Offering Price of the Units. Distributions will generally be reduced by the amount of the income which would otherwise have been paid with respect to redeemed Bonds and there will be distributed to Unitholders the principal amount in excess of \$1 per Unit semi-annually and any premium received on such redemption. However, should the amount available for distribution in the Principal Account exceed \$10.00 per Unit, the Trustee will make a special distribution from the Principal Account on the next succeeding monthly distribution date to holders of record on the related monthly record date. The Estimated Current Return in this event may be affected by such redemptions. For the Federal tax effect on Unitholders of such redemptions and resultant distributions, see paragraph (3) under "Federal Tax Status of the Trusts" and "Annual Unit Income and Estimated Current Returns" in Part Two.

NOTE 2 - PORTFOLIO (continued)

Unrealized Appreciation and Depreciation - An analysis of net unrealized appreciation (depreciation) at October 31, 1994 is as follows:

<TABLE>  
<CAPTION>

|                         |     | Ohio Trust |
|-------------------------|-----|------------|
| <S>                     | <C> |            |
| Unrealized Appreciation | \$  | 191,540    |
| Unrealized Depreciation |     | (131,310)  |
|                         | \$  | 60,230     |

</TABLE>

NOTE 3 - OTHER

Marketability - Although it is not obligated to do so, the Sponsor intends to maintain a market for Units and to continuously offer to purchase Units at prices, subject to change at any time, based upon the aggregate bid price of the Bonds in the portfolio of each Trust, plus interest accrued to the date of settlement. If the supply of Units exceeds demand, or for other business reasons, the Sponsor may discontinue purchases of Units at such prices. In the event that a market is not maintained for the Units, a Unitholder desiring to dispose of his Units may be able to do so only by tendering such Units to the Trustee for redemption at the redemption price.

Cost to Investors - The cost to original investors was based on the Evaluator's determination of the aggregate offering price of the Bonds per Unit on the date of an investor's purchase, plus a sales charge of 4.9% of the public offering price which is equivalent to 5.152% of the aggregate offering price of the Bonds. The secondary market cost to investors is based on the Evaluator's determination of the aggregate bid price of the Bonds per Unit on the date of an investor's purchase plus a sales charge based upon the years to average maturity of the Bonds in the portfolio. The sales charge ranges from 1.5% of the public offering price (1.523% of the aggregate bid price of the Bonds) for a Trust with a portfolio with less than two years to average maturity to 5.7% of the public offering price (6.045% of the aggregate bid price of the Bonds) for a Trust with a portfolio with sixteen or more years to average maturity.

Compensation of Evaluator - The Evaluator receives a fee for providing portfolio supervisory services for each of the Trusts (\$.25 per Unit, not to exceed the aggregate cost of the Evaluator for providing such services to all applicable Trusts). In addition, the Evaluator receives an annual fee for regularly evaluating each of the Trust's portfolios. Both fees may be adjusted for increases under the category "All Services Less Rent of Shelter" in the Consumer Price Index.

NOTE 4 - SUBSEQUENT EVENT

The following bond in the Ohio Investors' Quality Tax-Exempt Trust, Series 15 was redeemed or sold subsequent to October 31, 1994.



| Portfolio Item | Par Called<br>or Redeemed | Maturity<br>Date | Price |
|----------------|---------------------------|------------------|-------|
| J              | 100,000                   | 11/01/14         | 103   |

NATIONAL AND STATE QUALITY TRUSTS  
 INVESTORS' QUALITY  
 TAX-EXEMPT TRUST

PROSPECTUS  
 Part Two

In the opinion of counsel, interest to each Trust and to Unitholders, with certain exceptions, is excludable under existing law from gross income for Federal income taxes. In addition, except for the National Trust, the interest income of each Trust is, in the opinion of counsel, exempt to the extent indicated from state and local taxes, when held by residents of the state where the issuers of Bonds in such Trust are located. Capital gains, if any, are subject to Federal tax.

INTRODUCTION

The Fund. The objectives of the Fund are Federal and, in the case of a State Trust, state tax-exempt income and conservation of capital through an investment in a diversified portfolio of tax-exempt bonds. There is, of course, no guarantee that the Fund's objectives will be achieved. The Fund consists of a series of separate National and State unit investment trusts, some of which may be included in various series of Investors' Quality Tax-Exempt Trust, Multi-State or Multi-Series. The various trusts collectively are referred to herein as the "Trusts". The "National Trusts" include various series of The First National Dual Series Tax-Exempt Bond Trust (Income Trust), Investors' Municipal-Yield Trust and Investors' Quality Tax-Exempt Trust and the other Trusts are collectively referred to herein as the "State Trusts". Each Trust consists of interest-bearing obligations (the "Bonds" or "Securities") issued by or on behalf of municipalities and other governmental authorities, the interest on which is, in the opinion of recognized bond counsel to the issuing governmental authority, exempt from all Federal income tax under existing law. In addition, the interest income of each State Trust is, in the opinion of counsel, exempt to the extent indicated from state and local taxes, when held by residents of the state where the issuers of Bonds in such Trust are located. All the Securities deposited in each Trust were rated "A" or better by Standard & Poor's Corporation or "A" or better by Moody's Investors Service, Inc.

Public Offering Price. Units are offered at the Public Offering Price. The Public Offering Price for "secondary market" sales will be equal to the aggregate bid price of the Securities in each Trust and cash, if any, in the Principal Account held or owned by such Trust plus the sales charge referred to under "Public Offering" plus an amount equal to the accrued interest from the most recent record date of the Trust to the date of settlement (five business days after order) less distributions from the Interest Account subsequent to the most recent record date, if any. In addition, for Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series the Public Offering Price will include Purchased Interest. If the Securities in each Trust were available for direct purchase by investors, the purchase price of the Securities would not include the sales charge included in the Public Offering Price of the Units.

Estimated Current Return and Estimated Long-Term Return. The Estimated Current Return is calculated by dividing the Estimated Net Annual Interest Income per Unit by the Public Offering Price. The Estimated Net Annual Interest Income per Unit will vary with changes in fees and expenses of the Trustee and the Evaluator and with the principal prepayment, redemption, maturity, exchange or sale of Securities while the Public Offering Price will vary with changes in the bid price of the underlying Securities; therefore, there is no assurance that the present Estimated Current Returns will be realized in the future. Estimated Long-Term Return is calculated using a formula which (1) takes into consideration, and determines and factors in the relative weightings of, the market values, yields (which takes into account the amortization of premiums and the accretion of discounts) and estimated retirements of all of the Securities in the Trust and (2) takes into account the expenses and sales charge associated with each Trust Unit. Since the market values and estimated retirements of the Securities and the expenses of the Trust will change, there is no assurance that the present Estimated Long-Term Return will be realized in the future. Estimated Current Return and Estimated Long-Term Return are expected to differ because the calculation of Estimated Long-Term Return reflects the estimated date and amount of principal returned while Estimated Current Return calculations include only Net Annual Interest Income and Public

Offering Price. Neither rate reflects the true return to Unitholders which is lower because neither includes the effect of the delay in the first payment to Unitholders.

NOTE: THIS PROSPECTUS MAY BE USED ONLY WHEN ACCOMPANIED BY PART ONE

Both parts of this Prospectus should be retained for future reference.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

This Prospectus is dated as of the date of the Prospectus Part I accompanying this Prospectus Part II.

Van Kampen Merritt

#### DESCRIPTION OF THE FUND

Each series of the Fund was created under the laws of the State of New York pursuant to a Trust Indenture and Agreement (the "Trust Agreement"), dated the Date of Deposit, between Van Kampen Merritt Inc., as Sponsor, American Portfolio Evaluation Services, a division of Van Kampen Merritt Investment Advisory Corp., as Evaluator, and, except for certain Pennsylvania Trusts (see "The Trustee"), The Bank of New York, as Trustee, or their respective predecessors.

The Fund consists of the various series of the National Trust and the State Trusts, each of which contains a portfolio of interest-bearing obligations issued by or on behalf of states and territories of the United States, and political subdivisions and authorities thereof, the interest on which is, in the opinion of recognized bond counsel to the issuing authorities, excludable from gross income for Federal income tax under existing law but may be subject to state and local taxes. All issuers of Securities in a State Trust are located in the state for which such Trust is named or in United States territories or possessions and their public authorities; consequently, in the opinion of recognized bond counsel to such issuers, the related interest earned on such Securities is exempt to the extent indicated from state and local taxes of such State. Interest on certain Bonds in the National Quality AMT Trust will be a preference item for purposes of the alternative minimum tax. Accordingly, the National Quality AMT Trust may be appropriate only for investors who are not subject to the alternative minimum tax. Unless otherwise terminated as provided therein, the Trust Agreement for each Trust will terminate at the end of the calendar year prior to the fiftieth anniversary of its execution (except for the Short Term Trusts in which case the termination date is at the end of the calendar year prior to the sixth anniversary of its execution). The portfolio of any State Trust or National Quality Trust consists of Bonds maturing approximately 15 to 40 years from the Date of Deposit.

Certain of the Bonds in certain of the Trusts are "zero coupon" bonds. Zero coupon bonds are purchased at a deep discount because the buyer receives only the right to receive a final payment at the maturity of the bond and does not receive any periodic interest payments. The effect of owning deep discount bonds which do not make current interest payments (such as the zero coupon bonds) is that a fixed yield is earned not only on the original investment but also, in effect, on all discount earned during the life of such obligation. This implicit reinvestment of earnings at the same rate eliminates the risk of being unable to reinvest the income on such obligation at a rate as high as the implicit yield on the discount obligation, but at the same time eliminates the holder's ability to reinvest at higher rates in the future. For this reason, zero coupon bonds are subject to substantially greater price fluctuations during periods of changing market interest rates than are securities of comparable quality which pay interest currently. See note (6) in "Notes to Portfolio" in Part One of this Prospectus.

Each Unit of each Trust represents a fractional undivided interest in the principal and net income of such Trust. To the extent that any Units of a Trust are redeemed by the Trustee, the fractional undivided interest in such Trust represented by each unredeemed Unit will increase, although the actual interest in such Trust represented by such fraction will remain unchanged. Units will remain outstanding until redeemed upon tender to the Trustee by Unitholders, which may include the Sponsor, or until the termination of the Trust Agreement.

#### SECURITIES SELECTION

In selecting Securities for the Trusts the following facts, among others, were considered by the Sponsor: (a) either the Standard & Poor's Corporation rating of the Securities was in no case less than "A" or the Moody's Investors Service, Inc. rating of the Securities was in no case less than "A" including provisional or conditional ratings, respectively, or, if not rated, the

Securities had, in the opinion of the Sponsor, credit characteristics sufficiently similar to the credit characteristics of interest-bearing tax-exempt obligations that were so rated as to be acceptable for acquisition by a Trust (see "Description of Securities Ratings"), (b) the prices of the Securities relative to other bonds of comparable quality and maturity and (c) the diversification of Securities as to purpose of issue and location of issuer. Subsequent to the Date of Deposit, a Security may cease to be rated or its rating may be reduced below the minimum required as of the Date of Deposit. Neither event requires elimination of such Security from the portfolio of a Trust but may be considered in the Sponsor's determination as to whether or not to direct the Trustee to dispose of the Security (see "Portfolio Administration").

To the best knowledge of the Sponsor, there is no litigation pending as of the Date of Deposit in respect of any Securities which might reasonably be expected to have a material adverse effect upon the Fund or any of the Trusts. At any time after the Date of Deposit, litigation may be initiated on a variety of grounds with respect to Securities in the Fund. Such litigation, as, for example, suits challenging the issuance of pollution control revenue bonds under environmental protection statutes, may affect the validity of such Securities or the tax-free nature of the interest thereon. While the outcome of litigation of such nature can never be entirely predicted, the Fund has received or will receive opinions of bond counsel to the issuing authorities of each Security on the date of issuance to the effect that such Securities have been validly issued and that the interest thereon is exempt from Federal income tax. In addition, other factors may arise from time to time which potentially may impair the ability of issuers to meet obligations undertaken with respect to the Securities.

#### PORTFOLIO CONCENTRATIONS

Certain of the Bonds in certain of the Trusts may be general obligations of a governmental entity that are backed by the taxing power of such entity. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. All other Bonds in the Trusts are revenue bonds payable from the income of a specific project or authority and are not supported by the issuer's power to levy taxes. General obligation bonds are secured by the issuer's pledge of its faith, credit and taxing power for the payment of principal and interest. Revenue bonds, on the other hand, are payable only from the revenues derived from a particular facility or class of facilities or, in some cases, from the proceeds of a special excise tax or other specific revenue source. There are, of course, variations in the security of the different Bonds in the Fund, both within a particular classification and between classifications, depending on numerous factors.

Certain of the Bonds in certain of the Trusts are obligations which derive their payments from mortgage loans. Certain of such housing bonds may be FHA insured or may be single family mortgage revenue bonds issued for the purpose of acquiring from originating financial institutions notes secured by mortgages on residences located within the issuer's boundaries and owned by persons of low or moderate income. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. Mortgage loans are generally partially or completely prepaid prior to their final maturities as a result of events such as sale of the mortgaged premises, default, condemnation or casualty loss. Because these bonds are subject to extraordinary mandatory redemption in whole or in part from such prepayments of mortgage loans, a substantial portion of such bonds will probably be redeemed prior to their scheduled maturities or even prior to their ordinary call dates. Extraordinary mandatory redemption without premium could also result from the failure of the originating financial institutions to make mortgage loans in sufficient amounts within a specified time period. Additionally, unusually high rates of default on the underlying mortgage loans may reduce revenues available for the payment of principal of or interest on such mortgage revenue bonds. These bonds were issued under Section 103A of the Internal Revenue Code, which Section contains certain requirements relating to the use of the proceeds of such bonds in order for the interest on such bonds to retain its tax-exempt status. In each case the issuer of the bonds has covenanted to comply with applicable requirements and bond counsel to such issuer has issued an opinion that the interest on the bonds is exempt from Federal income tax under existing laws and regulations. Certain issuers of housing bonds have considered various ways to redeem bonds they have issued prior to the stated first redemption dates for such bonds. In connection with the housing bonds held by the Trust, the Sponsor has not had any direct communications with any of the issuers thereof, but at the Date of Deposit it was not aware that any of the respective issuers of such Bonds were actively considering the redemption of such Bonds prior to their respective stated initial call dates.

Certain of the Bonds in certain of the Trusts are health care revenue bonds. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. Ratings of bonds issued for health care facilities are often based on feasibility studies that contain projections of occupancy

levels, revenues and expenses. A facility's gross receipts and net income available for debt service will be affected by future events and conditions including, among other things, demand for services and the ability of the facility to provide the services required, physicians' confidence in the facility, management capabilities, competition with other health care facilities, efforts by insurers and governmental agencies to limit rates, legislation establishing state rate-setting agencies, expenses, the cost and possible unavailability of malpractice insurance, the funding of Medicare, Medicaid and other similar third party payor programs, government regulation and the termination or restriction of governmental financial assistance, including that associated with Medicare, Medicaid and other similar third party payor programs. Pursuant to recent Federal legislation, Medicare reimbursements are currently calculated on a prospective basis utilizing a single nationwide schedule of rates. Prior to such legislation Medicare reimbursements were based on the actual costs incurred by the health facility. The current legislation may adversely affect reimbursements to hospitals and other facilities for services provided under the Medicare program. Such adverse changes also may adversely affect the ratings of Securities held in the portfolios of the Fund.

Certain of the Bonds in certain of the Trusts are obligations of public utility issuers, including those selling wholesale and retail electric power and gas. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. General problems of such issuers would include the difficulty in financing large construction programs in an inflationary period, the limitations on operations and increased costs and delays attributable to environmental considerations, the difficulty of the capital market in absorbing utility debt, the difficulty in obtaining fuel at reasonable prices and the effect of energy conservation. All of such issuers have been experiencing certain of these problems in varying degrees. In addition, Federal, state and municipal governmental authorities may from time to time review existing, and impose additional, regulations governing the licensing, construction and operation of nuclear power plants, which may adversely affect the ability of the issuers of certain of the Bonds in the portfolio to make payments of principal and/or interest on such Bonds.

Certain of the Bonds in certain of the Trusts are industrial revenue bonds ("IRBs"). In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. IRBs have generally been issued under bond resolutions pursuant to which the revenues and receipts payable under the arrangements with the operator of a particular project have been assigned and pledged to purchasers. In some cases, a mortgage on the underlying project may have been granted as security for the IRBs. Regardless of the structure, payment of IRBs is solely dependent upon the creditworthiness of the corporate operator of the project or corporate guarantor. Corporate operators or guarantors may be affected by many factors which may have an adverse impact on the credit quality of the particular company or industry. These include cyclicalities of revenues and earnings, regulatory and environmental restrictions, litigation resulting from accidents or environmentally-caused illnesses, extensive competition and financial deterioration resulting from a corporate restructuring pursuant to a leveraged buy-out, takeover or otherwise. Such a restructuring may result in the operator of a project becoming highly leveraged which may impact on such operator's creditworthiness which in turn would have an adverse impact on the rating and/or market value of such Bonds. Further, the possibility of such a restructuring may have an adverse impact on the market for and consequently the value of such Bonds, even though no actual takeover or other action is ever contemplated or effected.

Certain of the Bonds in certain of the Trusts may be obligations of issuers whose revenues are derived from the sale of water and/or sewerage services. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. Such bonds are generally payable from user fees. The problems of such issuers include the ability to obtain timely and adequate rate increases, population decline resulting in decreased user fees, the difficulty of financing large construction programs, the limitations on operations and increased costs and delays attributable to environmental considerations, the increasing difficulty of obtaining or discovering new supplies of fresh water, the effect of conservation programs and the impact of "no-growth" zoning ordinances. All of such issuers have been experiencing certain of these problems in varying degrees.

Certain of the Bonds in certain of the Trusts may be obligations that are secured by lease payments of a governmental entity (hereinafter called "lease obligations"). In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. Although the lease obligations do not constitute general obligations of the municipality for which the municipality's taxing power is pledged, a lease obligation lease is ordinarily backed by the municipality's covenant to budget for, appropriate and make the payments due under the lease obligation. However, certain lease obligations

contain "non-appropriation" clauses which provide that the municipality has no obligation to make lease payments in future years unless money is appropriated for such purpose on a yearly basis. A governmental entity that enters into such a lease agreement cannot obligate future governments to appropriate for and make lease payments but covenants to take such action as is necessary to include any lease payments due in its budgets and to make the appropriations therefor. A governmental entity's failure to appropriate for and to make payments under its lease obligation could result in insufficient funds available for payment of the obligations secured thereby. Although "non-appropriation" lease obligations are secured by the leased property, disposition of the property in the event of foreclosure might prove difficult.

Certain of the Bonds in certain of the Trusts may be obligations of issuers which are, or which govern the operation of, schools, colleges and universities and whose revenues are derived mainly from ad valorem taxes or for higher education systems, from tuition, dormitory revenues, grants and endowments. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. General problems relating to school bonds include litigation contesting the State constitutionality of financing public education in part from ad valorem taxes, thereby creating a disparity in educational funds available to schools in wealthy areas and schools in poor areas. Litigation or legislation on this issue may affect the sources of funds available for the payment of school bonds in the Trusts. General problems relating to college and university obligations include the prospect of a declining percentage of the population consisting of "college" age individuals, possible inability to raise tuitions and fees sufficiently to cover increased operating costs, the uncertainty of continued receipt of Federal grants and state funding, and government legislation or regulations which may adversely affect the revenues or costs of such issuers. All of such issuers have been experiencing certain of these problems in varying degrees.

Certain of the Bonds in certain of the Trusts may be obligations which are payable from and secured by revenues derived from the ownership and operation of facilities such as airports, bridges, turnpikes, port authorities, convention centers and arenas. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. The major portion of an airport's gross operating income is generally derived from fees received from signatory airlines pursuant to use agreements which consist of annual payments for leases, occupancy of certain terminal space and service fees. Airport operating income may therefore be affected by the ability of the airlines to meet their obligations under the use agreements. The air transport industry is experiencing significant variations in earnings and traffic, due to increased competition, excess capacity, increased costs, deregulation, traffic constraints and other factors, and several airlines are experiencing severe financial difficulties. The Sponsor cannot predict what effect these industry conditions may have on airport revenues which are dependent for payment on the financial condition of the airlines and their usage of the particular airport facility. Similarly, payment on Bonds related to other facilities is dependent on revenues from the projects, such as user fees from ports, tolls on turnpikes and bridges and rents from buildings. Therefore, payment may be adversely affected by reduction in revenues due to such factors as increased cost of maintenance, decreased use of a facility, lower cost of alternative modes of transportation, scarcity of fuel and reduction or loss of rents.

Certain of the Bonds in certain of the Trusts may be obligations which are payable from and secured by revenues derived from the operation of resource recovery facilities. In view of this an investment in such a Trust should be made with an understanding of the characteristics of such issuers and the risks which such an investment may entail. Resource recovery facilities are designed to process solid waste, generate steam and convert steam to electricity. Resource recovery bonds may be subject to extraordinary optional redemption at par upon the occurrence of certain circumstances, including but not limited to: destruction or condemnation of a project; contracts relating to a project becoming void, unenforceable or impossible to perform; changes in the economic availability of raw materials, operating supplies or facilities necessary for the operation of a project or technological or other unavoidable changes adversely affecting the operation of a project; administrative or judicial actions which render contracts relating to the projects void, unenforceable or impossible to perform; or impose unreasonable burdens or excessive liabilities. The Sponsor cannot predict the causes or likelihood of the redemption of resource recovery bonds in such a Trust prior to the stated maturity of the Bonds.

#### BOND REDEMPTIONS

Because certain of the Bonds in certain of the Trusts may from time to time under certain circumstances be sold or redeemed or will mature in accordance with their terms and because the proceeds from such events will be distributed to Unitholders and will not be reinvested, no assurance can be given that any Trust will retain for any length of time its present size and composition. Neither the Sponsor nor the Trustee shall be liable in any way for any

default, failure or defect in any Bond.

Certain of the Bonds in certain of the Trusts may be subject to redemption prior to their stated maturity date pursuant to sinking fund provisions, call provisions or extraordinary optional or mandatory redemption provisions or otherwise. A sinking fund is a reserve fund accumulated over a period of time for retirement of debt. A callable debt obligation is one which is subject to redemption or refunding prior to maturity at the option of the issuer. A refunding is a method by which a debt obligation is redeemed, at or before maturity, by the proceeds of a new debt obligation. In general, call provisions are more likely to be exercised when the offering side valuation is at a premium over par than when it is at a discount from par. The exercise of redemption or call provisions will (except to the extent the proceeds of the called Bonds are used to pay for Unit redemptions) result in the distribution of principal and may result in a reduction in the amount of subsequent interest distributions; it may also affect the current return on Units of the Trust involved. Each Trust portfolio contains a listing of the sinking fund and call provisions, if any, with respect to each of the debt obligations. Extraordinary optional redemptions and mandatory redemptions result from the happening of certain events. Generally, events that may permit the extraordinary optional redemption of Bonds or may require the mandatory redemption of Bonds include, among others: a final determination that the interest on the Bonds is taxable; the substantial damage or destruction by fire or other casualty of the project for which the proceeds of the Bonds were used; an exercise by a local, state or Federal governmental unit of its power of eminent domain to take all or substantially all of the project for which the proceeds of the Bonds were used; changes in the economic availability of raw materials, operating supplies or facilities or technological or other changes which render the operation of the project for which the proceeds of the Bonds were used uneconomic; changes in law or an administrative or judicial decree which renders the performance of the agreement under which the proceeds of the Bonds were made available to finance the project impossible or which creates unreasonable burdens or which imposes excessive liabilities, such as taxes, not imposed on the date the Bonds are issued on the issuer of the Bonds or the user of the proceeds of the Bonds; an administrative or judicial decree which requires the cessation of a substantial part of the operations of the project financed with the proceeds of the Bonds; an overestimate of the costs of the project to be financed with the proceeds of the Bonds resulting in excess proceeds of the Bonds which may be applied to redeem Bonds; or an underestimate of a source of funds securing the Bonds resulting in excess funds which may be applied to redeem Bonds. The Sponsor is unable to predict all of the circumstances which may result in such redemption of an issue of Bonds. See "Trust Portfolio" and note (3) in "Notes to Portfolio" in Part One of this Prospectus. See also the discussion of single family mortgage and multi-family revenue bonds above for more information on the call provisions of such bonds.

#### DISTRIBUTIONS

General. Distributions of interest received by a Trust, pro rated on an annual basis, will be made semi-annually unless the Unitholder has elected to receive them monthly or quarterly, if applicable. Distributions of funds from the Principal Account, if any, will be made on a semi-annual basis, except under certain special circumstances. See "Distributions of Interest and Principal" below. Record dates for monthly distributions for each Trust are the first day of each month and record dates for quarterly and semi-annual distributions for each Trust are the first day of the months indicated under "Per Unit Information" in Part One of this Prospectus. Distributions are made on the fifteenth day of the month subsequent to the respective record dates. Unitholders of the Short Term Trusts will only receive distributions semi-annually with record dates being May 1 and November 1 of each year. Unitholders of Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series will receive distributions of income and principal, if any, on a monthly basis.

Change of Distribution Option. The plan of distribution selected by a Unitholder of Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 212 and prior series remains in effect until changed. Unitholders purchasing Units in the secondary market will initially receive distributions in accordance with the election of the prior owner. Unitholders may change the plan of distribution in which they are participating. For the convenience of Unitholders, the Trustee will furnish a card for this purpose; cards may also be obtained upon request from the Trustee. Unitholders desiring to change their plan of distribution may so indicate on the card and return it, together with their certificate and such other documentation that the Trustee may then require, to the Trustee. Certificates should only be sent by registered or certified mail to minimize the possibility of their being lost or stolen. If the card and certificate are properly presented to the Trustee, the change will become effective for all subsequent distributions.

Distributions of Interest and Principal. Interest received by each Trust, including that part of the proceeds of any disposition of Securities which represents Purchased Interest, if any, and/or accrued interest, is credited by



the Trustee to the Interest Account for the appropriate Trust. Other receipts are credited to the Principal Account for the appropriate Trust. All distributions will be net of applicable expenses. The pro rata share of cash in the Principal Account of a Trust will be computed as of the semi-annual record date and distributions to the Unitholders as of such record date will be made on or shortly after the fifteenth day of such month. For Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series such computation and distribution will occur monthly. Proceeds received from the disposition of any of the Securities after such record date and prior to the following distribution date will be held in the Principal Account and not distributed until the next distribution date. The Trustee is not required to pay interest on funds held in any Principal or Interest Account (but may itself earn interest thereon and therefore benefits from the use of such funds) nor to make a distribution from the Principal Account unless the amount available for distribution therein shall equal at least \$1.00 per Unit.

The distribution to the Unitholders of a Trust as of each record date will be made on the following distribution date or shortly thereafter and shall consist of an amount substantially equal to such portion of the Unitholder's prorata share of the Estimated Net Annual Interest Income in the Interest Account of such Trust after deducting estimated expenses attributable as is consistent with the distribution plan chosen. Only monthly distributions will be available for Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series. Because interest payments are not received by a Trust at a constant rate throughout the year, such interest distribution may be more or less than the amount credited to such Interest Account as of the record date. For the purpose of minimizing fluctuations in the distributions from an Interest Account, the Trustee is authorized to advance such amounts as may be necessary to provide interest distributions of approximately equal amounts. The Trustee shall be reimbursed, without interest, for any such advances from funds in the applicable Interest Account on the ensuing record date. Persons who purchase Units between a record date and a distribution date will receive their first distribution on the second distribution date after the purchase, under the applicable plan of distribution. Only monthly distributions will be available for Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series. As of the first day of each month, the Trustee will deduct from the Interest Account and, to the extent funds are not sufficient therein, from the Principal Account, amounts necessary to pay the expenses of each Trust. The Trustee also may withdraw from said accounts such amounts, if any, as it deems necessary to establish a reserve for any governmental charges payable out of each Trust. Amounts so withdrawn shall not be considered a part of each Trust's assets until such time as the Trustee shall return all or any part of such amounts to the appropriate Accounts. In addition, the Trustee may withdraw from the Interest and Principal Accounts such amounts as may be necessary to cover redemptions of Units by the Trustee.

#### CERTIFICATES

The Trustee is authorized to treat as the record owner of Units that person who is registered as such owner on the books of the Trustee. Ownership of Units of the Trust is evidenced by separate registered certificates executed by the Trustee and the Sponsor. Certificates are transferable by presentation and surrender to the Trustee properly endorsed or accompanied by a written instrument or instruments of transfer. A Unitholder must sign exactly as his name appears on the face of the certificate with the signature guaranteed by a participant in the Securities Transfer Agents Medallion Program ("STAMP") or such other signature guaranty program in addition to or in substitution for, STAMP, as may be acceptable to the Trustee. In certain instances the Trustee may require additional documents such as, but not limited to, trust instruments, certificates of death, appointments as executor or administrator or certificates of corporate authority.

Although no such charge is now made or contemplated, the Trustee may require a Unitholder to pay a reasonable fee for each certificate re-issued (other than as a result of a change in plan of distribution) or transferred and to pay any governmental charge that may be imposed in connection with each such transfer or interchange. Destroyed, stolen, mutilated or lost certificates will be replaced upon delivery to the Trustee of satisfactory indemnity, evidence of ownership and payment of expenses incurred. Mutilated certificates must be surrendered to the Trustee for replacement.

#### ESTIMATED CURRENT RETURNS AND ESTIMATED LONG-TERM RETURNS

As of the opening of business on the date indicated therein, the Estimated Current Returns, and the Estimated Long-Term Returns for each Trust under the monthly, quarterly, if applicable, and semi-annual distribution plans were as set forth under "Per Unit Information" for the applicable Trust in Part One of this Prospectus. Estimated Current Return is calculated by dividing the Estimated Net Annual Interest Income per Unit by the Public Offering Price. The Estimated Net Annual Interest Income per Unit will vary with changes in fees and expenses of the Trustee and the Evaluator and with the principal prepayment, redemption, maturity, exchange or sale of Securities while the

Public Offering Price will vary with changes in the offering price of the underlying Securities and with changes in Purchased Interest for those series which contain Purchased Interest; therefore, there is no assurance that the present Estimated Current Return will be realized in the future. Estimated Long-Term Return is calculated using a formula which (1) takes into consideration, and determines and factors in the relative weightings of, the market values, yields (which takes into account the amortization of premiums and the accretion of discounts) and estimated retirements of all of the Securities in the Trust and (2) takes into account the expenses and sales charge associated with each Trust Unit. Since the market values and estimated retirements of the Securities and the expenses of the Trust will change, there is no assurance that the present Estimated Long-Term Return will be realized in the future. Estimated Current Return and Estimated Long-Term Return are expected to differ because the calculation of Estimated Long-Term Return reflects the estimated date and amount of principal returned while Estimated Current Return calculations include only Net Annual Interest Income and Public Offering Price.

THE FOLLOWING SECTION "ACCRUED INTEREST (ACCRUED INTEREST TO CARRY)" APPLIES TO INSURED MUNICIPALS INCOME TRUST AND INVESTORS' QUALITY TAX-EXEMPT TRUST, MULTI-SERIES 212 AND PRIOR SERIES ONLY.

#### ACCRUED INTEREST (ACCRUED INTEREST TO CARRY)

Accrued interest to carry consists of two elements. The first element arises as a result of accrued interest which is the accumulation of unpaid interest on a bond from the last day on which interest thereon was paid. Interest on Securities in each Trust is actually paid either monthly, quarterly, if applicable, or semi-annually to such Trust. However, interest on the Securities in each Trust is accounted for daily on an accrual basis. Because of this, each Trust always has an amount of interest earned but not yet collected by the Trustee because of coupons that are not yet due. For this reason, the Public Offering Price will have added to it the proportionate share of accrued and undistributed interest to the date of settlement.

The second element of accrued interest to carry arises because of the structure of the Interest Account. The Trustee has no cash for distribution to Unitholders of a Trust until it receives interest payments on the Securities in such Trust. The Trustee is obligated to provide its own funds, at times, in order to advance interest distributions. The Trustee will recover these advancements when such interest is received. Interest Account balances are established so that it will not be necessary on a regular basis for the Trustee to advance its own funds in connection with such interest distributions. The Interest Account balances are also structured so that there will generally be positive cash balances and since the funds held by the Trustee may be used by it to earn interest thereon, it benefits thereby. If a Unitholder sells or redeems all or a portion of his Units or if the Bonds in a Trust are sold or otherwise removed or if a Trust is liquidated, he will receive at that time his proportionate share of the accrued interest to carry computed to the settlement date in the case of sale or liquidation and to the date of tender in the case of redemption.

THE FOLLOWING SECTION "PURCHASED AND ACCRUED INTEREST" APPLIES TO INSURED MUNICIPALS INCOME TRUST AND INVESTORS' QUALITY TAX-EXEMPT TRUST, MULTI-SERIES 213 AND SUBSEQUENT SERIES ONLY.

#### PURCHASED AND ACCRUED INTEREST

Purchased Interest. Purchased Interest is a portion of the unpaid interest that has accrued on the Securities from the later of the last payment date on the Securities or the date of issuance thereof through the First Settlement Date and is included in the calculation of the Public Offering Price. Purchased Interest will be distributed to Unitholders as Units are redeemed or Securities mature or are called. See "Summary of Essential Financial Information" in Part One of this Prospectus for the amount of Purchased Interest per Unit for each Trust. Purchased Interest is an element of the price Unitholders will receive in connection with the sale or redemption of Units prior to the termination of a Trust.

Accrued Interest. Accrued Interest is an accumulation of unpaid interest on securities which generally is paid semi-annually, although a Trust accrues such interest daily. Because of this, a Trust always has an amount of interest earned but not yet collected by the Trustee. For this reasons, the Public Offering Price of Units will have added to it the proportionate share of accrued interest to the date of settlement. Unitholders will receive on the next distribution date of a Trust the amount, if any, of accrued interest paid on their Units.

As indicated in "Purchased Interest", accrued interest as of the First Settlement Date includes Purchased Interest. In an effort to reduce the amount of Purchased Interest which would otherwise have to be paid by Unitholders, the Trustee may advance a portion of such accrued interest to the Sponsor as the Unitholder of record as of the First Settlement Date. Consequently, the amount of accrued interest to be added to the Public Offering Price of Units



will include only accrued interest from the First Settlement Date to the date of settlement (other than the Purchased Interest already included therein), less any distributions from the Interest Account subsequent to the First Settlement Date. See "Distributions Distribution of Interest and Principal."

Because of the varying interest payment dates of the Securities, accrued interest at any point in time will be greater than the amount of interest actually received by a Trust and distributed to Unitholders. If a Unitholder sells or redeems all or a portion of his Units, he will be entitled to receive his proportionate share of the Purchased Interest and accrued interest from the purchaser of his Units. Since the Trustee has the use of the funds (including Purchased Interest) held in the Interest Account for distributions to Unitholders and since such Account is non-interest-bearing to Unitholders, the Trustee benefits thereby.

#### PUBLIC OFFERING PRICE

Units are offered at the Public Offering Price plus accrued undistributed interest to the settlement date. For secondary market sales the Public Offering Price will be equal to the aggregate bid price of the Securities determined in accordance with the table set forth below, which is based upon the dollar weighted average maturity of each Trust. In addition, for Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series the Public Offering Price will also include Purchased Interest. For purposes of computation, Bonds will be deemed to mature on their expressed maturity dates unless: (a) the Bonds have been called for redemption or funds or securities have been placed in escrow to redeem them on an earlier call date, in which case such call date will be deemed to be the date upon which they mature; or (b) such Bonds are subject to a "mandatory tender", in which case such mandatory tender will be deemed to be the date upon which they mature.

The effect of this method of sales charge computation will be that different sales charge rates will be applied to each Trust based upon the dollar weighted average maturity of such Trust's Portfolio, in accordance with the following schedule:

| Years To Maturity | Sales Charge | Years To Maturity | Sales Charge |
|-------------------|--------------|-------------------|--------------|
| 1                 | 1.523%       | 9                 | 4.712%       |
| 2                 | 2.041        | 10                | 4.932        |
| 3                 | 2.564        | 11                | 4.932        |
| 4                 | 3.199        | 12                | 4.932        |
| 5                 | 3.842        | 13                | 5.374        |
| 6                 | 4.058        | 14                | 5.374        |
| 7                 | 4.275        | 15                | 5.374        |
| 8                 | 4.493        | 16 to 30          | 6.045        |

The sales charges in the above table are expressed as a percentage of the aggregate bid prices of the Securities in a Trust. Expressed as a percent of the Public Offering Price (excluding Purchased Interest for those Trusts which contain Purchased Interest), the sales charge on a Trust consisting entirely of a portfolio of Bonds with 15 years to maturity would be 5.10%.

As indicated above, the price of the Units as of the opening of business on the date of Part One of this Prospectus was determined by adding to the determination of the aggregate bid price of the Securities an amount equal to the applicable sales charge expressed as a percentage of the aggregate bid price of the Securities plus Purchased Interest for those trusts which contain Purchased Interest and dividing the sum so obtained by the number of Units outstanding. This computation produced a gross commission equal to such sales charged expressed as a percentage of the Public Offering Price.

For secondary market purposes an appraisal and adjustment with respect to a Trust will be made by the Evaluator as of 4:00 P.M. Eastern time on days in which the New York Stock Exchange is open for each day on which any Unit of such Trust is tendered for redemption, and it shall determine the aggregate value of any Trust as of 4:00 P.M. Eastern time at such other times as may be necessary.

The aggregate price of the Securities in each Trust has been and will be determined on the basis of bid prices as follows: (a) on the basis of current market prices for the Securities obtained from dealers or brokers who customarily deal in bonds comparable to those held by the Trust; (b) if such prices are not available for any particular Securities, on the basis of current market prices for comparable bonds; (c) by causing the value of the Securities to be determined by others engaged in the practice of evaluation, quoting or appraising comparable bonds; or (d) by any combination of the above. Market prices of the Securities will generally fluctuate with changes in market interest rates.

Although payment is normally made five business days following the order for purchase, payment may be made prior thereto. A person will become the owner of Units on the date of settlement provided payment has been received. Cash, if any, made available to the Sponsor prior to the date of settlement for the purchase of Units may be used in the Sponsor's business and may be deemed to be a benefit to the Sponsor, subject to the limitations of the Securities Exchange Act of 1934. Delivery of certificates representing Units so ordered will be made five business days following such order or shortly thereafter. See "Redemption of Units" below for information regarding the ability to redeem Units ordered for purchase.

#### MARKET FOR UNITS

Although they are not obligated to do so, the Sponsor intends to, and certain of the dealers may, maintain a market for the Units offered hereby and to offer continuously to purchase such Units at prices, subject to change at any time, based upon the aggregate bid prices of the Securities in the portfolio of each Trust plus Purchased Interest, if any, plus interest accrued to the date of settlement and plus any principal cash on hand, less any amounts representing taxes or other governmental charges payable out of the Trust and less any accrued Trust expenses. If the supply of Units exceeds demand or if some other business reason warrants it, the Sponsor and/or the dealers may either discontinue all purchases of Units or discontinue purchases of Units at such prices. In the event that a market is not maintained for the Units and the Unitholder cannot find another purchaser, a Unitholder of any Trust desiring to dispose of his Units may be able to dispose of such Units only by tendering them to the Trustee for redemption at the Redemption Price, which is based upon the aggregate bid price of the Securities in the portfolio of such Trust plus Purchased Interest, if any, and any accrued interest. The aggregate bid prices of the underlying Securities in a Trust are expected to be less than the related aggregate offering prices. See "Redemption of Units" below. A Unitholder who wishes to dispose of his Units should inquire of his broker as to current market prices in order to determine whether there is in existence any price in excess of the Redemption Price and, if so, the amount thereof.

#### REINVESTMENT OPTION

Unitholders of the Trust may elect to have each distribution of interest income, capital gains and/or principal on their Units automatically reinvested in shares of any of the open-ended mutual funds listed under "The Sponsor" which are registered in the Unitholder's state of residence. Such mutual funds are hereinafter collectively referred to as the "Reinvestment Funds."

Each Reinvestment Fund has investment objectives which differ in certain respects from those of the Trust. The prospectus relating to each Reinvestment Fund describes the investment policies of such fund and sets forth the procedures to follow to commence reinvestment. A Unitholder may obtain a prospectus for the respective Reinvestment Funds from Van Kampen Merritt Inc. at One Parkview Plaza, Oakbrook Terrace, Illinois 60181. Texas residents who desire to reinvest may request that a broker-dealer registered in Texas send the prospectus relating to the respective fund.

After becoming a participant in a reinvestment plan, each distribution of interest income, capital gains and/or principal on the participant's Units will, on the applicable distribution date, automatically be applied, as directed by such person, as of such distribution date by the Trustee to purchase shares (or fractions thereof) of the applicable Reinvestment Fund at a net asset value as computed as of the close of trading on the New York Stock Exchange on such date, plus a sales charge of \$1.00 per \$100 of reinvestment except if the participant selects the First Investors New York Insured Tax Free Fund, Inc., in which case the sales charge will be \$1.50 per \$100 of reinvestment, or except if the participant selects the Van Kampen Merritt Money Market Fund or the Van Kampen Merritt Tax Free Money Fund in which case no sales charge applies. A minimum of one-half of such sales charge would be paid to Van Kampen Merritt Inc. for all Reinvestment Funds except First Investors New York Insured Tax Free Fund, Inc., in which case such sales charge would be paid to First Investors Management Company, Inc.

Confirmations of all reinvestments by a Unitholder into a Reinvestment Fund will be mailed to the Unitholder by such Reinvestment Fund.

A participant may at any time prior to five days preceding the next succeeding distribution date, by so notifying the Trustee in writing, elect to terminate his or her reinvestment plan and receive future distributions on his or her Units in cash. There will be no charge or other penalty for such termination. Each Reinvestment Fund, its sponsor and investment adviser shall have the right to terminate at any time the reinvestment plan relating to such Fund.

#### REDEMPTION OF UNITS

A Unitholder may redeem all or a portion of his Units by tender to the Trustee at its Unit Investment Trust Division, 101 Barclay Street, 20th Floor, New York, New York 10286 of the certificates representing the Units to be

redeemed, duly endorsed or accompanied by proper instruments of transfer with signature guaranteed (or by providing satisfactory indemnity, as in connection with lost, stolen or destroyed certificates) and by payment of applicable governmental charges, if any. Thus, redemption of Units cannot be effected until certificates representing such Units have been delivered to the person seeking redemption or satisfactory indemnity provided. No redemption fee will be charged. On the seventh calendar day following such tender, or if the seventh calendar day is not a business day, on the first business day prior thereto, the Unitholder will be entitled to receive in cash an amount for each Unit equal to the Redemption Price per Unit next computed after receipt by the Trustee of such tender of Units. The "date of tender" is deemed to be the date on which Units are received by the Trustee, except that as regards Units received after 4:00 P.M. Eastern time on days of trading on the New York Stock Exchange, the date of tender is the next day on which such Exchange is open for trading and such Units will be deemed to have been tendered to the Trustee on such day for redemption at the Redemption Price computed on that day.

Under regulations issued by the Internal Revenue Service, the Trustee will be required to withhold 20% of the principal amount of a Unit redemption if the Trustee has not been furnished the redeeming Unitholder's tax identification number in the manner required by such regulations. Any amount so withheld is transmitted to the Internal Revenue Service and may be recovered by the Unitholder only when filing a return. Under normal circumstances the Trustee obtains the Unitholder's tax identification number from the selling broker. However, at any time a Unitholder elects to tender Units for redemption, such Unitholder should provide a tax identification number to the Trustee in order to avoid this possible "back-up withholding" in the event the Trustee has not been previously provided such number.

Purchased Interest, if any, and accrued interest paid on redemption shall be withdrawn from the Interest Account of such Trust or, if the balance therein is insufficient, from the Principal Account of such Trust. All other amounts will be withdrawn from the Principal Account of such Trust. The Trustee is empowered to sell underlying Securities of a Trust in order to make funds available for redemption. Units so redeemed shall be cancelled.

The Redemption Price per Unit will be determined on the basis of the bid price of the Securities in each Trust as of 4:00 P.M. Eastern time on days of trading on the New York Stock Exchange on the date such determination is made. While the Trustee has the power to determine the Redemption Price per Unit when Units are tendered for redemption, such authority has been delegated to the Evaluator which determines the price per Unit on a daily basis. The Redemption Price per Unit is the pro rata share of each Unit in each Trust on the basis of (i) the cash on hand in such Trust or moneys in the process of being collected, (ii) the value of the Securities in such Trust based on the bid prices of the Securities therein, (iii) Purchased Interest, if any, included in Insured Municipals Income Trust and Investors' Quality Tax- Exempt Trust, Multi-Series 213 and subsequent series and (iv) interest accrued thereon, less (a) amounts representing taxes or other governmental charges payable out of such Trust and (b) the accrued expenses of such Trust. The Evaluator may determine the value of the Securities in each Trust by employing any of the methods set forth in "Public Offering Price."

The price at which Units may be redeemed could be less than the price paid by the Unitholder. As stated above, the Trustee may sell Securities to cover redemptions. When Securities are sold, the size and diversity of the affected Trust will be reduced. Such sales may be required at a time when Securities would not otherwise be sold and might result in lower prices than might otherwise be realized.

The right of redemption may be suspended and payment postponed for any period during which the New York Stock Exchange is closed, other than for customary weekend and holiday closings, or during which the Securities and Exchange Commission determines that trading on that Exchange is restricted or an emergency exists, as a result of which disposal or evaluation of the Securities in a Trust is not reasonably practicable, or for such other periods as the Securities and Exchange Commission may by order permit. Under certain extreme circumstances the Sponsor may apply to the Securities and Exchange Commission for an order permitting a full or partial suspension of the right of Unitholders to redeem their Units.

#### REPORTS PROVIDED

The Trustee shall furnish Unitholders of a Trust in connection with each distribution a statement of the amount of interest and, if any, the amount of other receipts (received since the preceding distribution) being distributed expressed in each case as a dollar amount representing the pro rata share of each Unit of a Trust outstanding. For as long as the Trustee deems it to be in the best interests of the Unitholders, the accounts of each Trust shall be audited, not less frequently than annually, by independent certified public accountants and the report of such accountants shall be furnished by the Trustee to Unitholders of the respective Trusts upon request. Within a reasonable period of time after the end of each calendar year, the Trustee shall furnish to each person who at any time during the calendar year was a

registered Unitholder of a Trust a statement (i) as to the Interest Account: interest received (including amounts representing interest received upon any disposition of Securities) and the percentage of such interest by states in which the issuers of the Securities are located, the amount of Purchased Interest, if any, deductions for applicable taxes and for fees and expenses of such Trust, for redemptions of Units, if any, and the balance remaining after such distributions and deductions, expressed in each case both as a total dollar amount and as a dollar amount representing the pro rata share of each Unit outstanding on the last business day of such calendar year; (ii) as to the Principal Account: the dates of disposition of any Securities and the net proceeds received therefrom (excluding any portion representing accrued interest), the amount paid for redemptions of Units, if any, deductions for payment of applicable taxes and fees and expenses of the Trustee and the balance remaining after such distributions and deductions expressed both as a total dollar amount and as a dollar amount representing the pro rata share of each Unit outstanding on the last business day of such calendar year; (iii) a list of the Securities held and the number of Units outstanding on the last business day of such calendar year; (iv) the Redemption Price per Unit based upon the last computation thereof made during such calendar year; and (v) amounts actually distributed during such calendar year from the Interest and Principal Accounts, separately stated, expressed both as total dollar amounts and as dollar amounts representing the pro rata share of each Unit outstanding.

In order to comply with Federal and state tax reporting requirements, Unitholders will be furnished, upon request to the Trustee, evaluations of the Securities in the Trust furnished to it by the Evaluator.

Each distribution statement will reflect pertinent information in respect of the other plan or plans of distribution so that Unitholders may be informed regarding the results of such other distribution option or options. Only monthly distributions are available for Insured Municipals Income Trust and Investors' Quality Tax-Exempt Trust, Multi-Series 213 and subsequent series.

#### FEDERAL TAX STATUS OF EACH TRUST

At the time of the closing for each Trust, Chapman and Cutler, Counsel for the Sponsor, rendered an opinion under then existing law, substantially to the effect that:

Each Trust is not an association taxable as a corporation for Federal income tax purposes and interest and accrued original issue discount on Bonds which is excludable from gross income under the Internal Revenue Code of 1986 (the "Code") will retain its status when distributed to Unitholders. A Unitholder's share of the interest on certain Bonds in the National Quality AMT Trust will be included as an item of tax preference for both individuals and corporations subject to the alternative minimum tax ("AMT Bonds"). In the case of certain corporations owning Units, interest and accrued original issue discount with respect to Bonds other than AMT Bonds held by a Trust (including the National Quality AMT Trust) may be subject to the alternative minimum tax, an additional tax on branches of foreign corporations and the environmental tax (the "Superfund Tax");

Each Unitholder is considered to be the owner of a pro rata portion of the respective Trust under subpart E, subchapter J of chapter 1 of the Internal Revenue Code of 1986 and will have a taxable event when such Trust disposes of a Security, or when the Unitholder redeems or sells his Units. Unitholders must reduce the tax basis of their Units for their share of accrued interest received by the respective Trust, if any, on Securities delivered after the Unitholders pay for their Units to the extent that such interest accrued on such Securities during the period from the Unitholder's settlement date to the date such Securities are delivered to the respective Trust and, consequently, such Unitholders may have an increase in taxable gain or reduction in capital loss upon the disposition of such Units. Gain or loss upon the sale or redemption of Units is measured by comparing the proceeds of such sale or redemption with the adjusted basis of the Units. If the Trustee disposes of Bonds (whether by sale, payment on maturity, redemption or otherwise), gain or loss is recognized to the Unitholder. The amount of any such gain or loss is measured by comparing the Unitholder's pro rata share of the total proceeds from such disposition with the Unitholder's basis for his or her fractional interest in the asset disposed of. In the case of a Unitholder who purchases Units, such basis (before adjustment for earned original issue discount and amortized bond premium, if any) is determined by apportioning the cost of the Units among each of the Trust assets ratably according to value as of the date of acquisition of the Units. The tax cost reduction requirements of said Code relating to amortization of bond premium may, under some circumstances, result in the Unitholder realizing a taxable gain when his Units are sold or redeemed for an amount equal to his original cost.

For purposes of computing the alternative minimum tax for individuals and corporations and the Superfund Tax for corporations, interest on certain private activity bonds (which includes most industrial and housing revenue bonds) issued on or after August 8, 1986 such as the AMT Bonds, is included as an item of tax preference. With the exception of certain Bonds in the National

Quality AMT Trust, the Trusts do not include any such AMT Bonds.

Sections 1288 and 1272 of the Code provide a complex set of rules governing the accrual of original issue discount. These rules provide that original issue discount accrues either on the basis of a constant compound interest rate or ratably over the term of the Bond, depending on the date the Bond was issued. In addition, special rules apply if the purchase price of a Bond exceeds the original issue price plus the amount of original issue discount which would have previously accrued based upon its issue price (its "adjusted issue price") to prior owners. The application of these rules will also vary depending on the value of the Bond on the date a Unitholder acquires his Units and the price the Unitholder pays for his Units. Investors with questions regarding these Code sections should consult with their tax advisers.

"The Revenue Reconciliation Act of 1993" (the "Tax Act") subjects tax- exempt bonds to the market discount rules of the Code effective for bonds purchased after April 30, 1993. In general, market discount is the amount (if any) by which the stated redemption price at maturity exceeds an investor's purchase price (except to the extent that such difference, if any, is attributable to original issue discount not yet accrued). Market discount can arise based on the price a Trust pays for Bonds or the price a Unitholder pays for his or her Units. Under the Tax Act, accretion of market discount is taxable as ordinary income; under prior law the accretion had been treated as capital gain. Market discount that accretes while a Trust holds a Bond would be recognized as ordinary income by the Unitholders when principal payments are received on the Bond, upon sale or at redemption (including early redemption), or upon the sale or redemption of his or her Units, unless a Unitholder elects to include market discount in taxable income as it accrues. The market discount rules are complex and Unitholders should consult their tax advisers regarding these rules and their application.

In the case of certain corporations, the alternative minimum tax and the Superfund Tax for taxable years beginning after December 31, 1986 depends upon the corporation's alternative minimum taxable income, which is the corporation's taxable income with certain adjustments. One of the adjustment items used in computing the alternative minimum taxable income and the Superfund Tax of a corporation (other than an S Corporation, Regulated Investment Company, Real Estate Investment Trust, or REMIC) is an amount equal to 75% of the excess of such corporation's "adjusted current earnings" over an amount equal to its alternative minimum taxable income (before such adjustment item and the alternative tax net operating loss deduction). "Adjusted current earnings" includes all tax exempt interest, including interest on all of the Bonds in the Trust. Unitholders are urged to consult their tax advisers with respect to the particular tax consequences to them, including the corporate alternative minimum tax, the Superfund Tax and the branch profits tax imposed by Section 884 of the Code.

Counsel for the Sponsor has also advised that under Section 265 of the Code, interest on indebtedness incurred or continued to purchase or carry Units of a Trust is not deductible for Federal income tax purposes. The Internal Revenue Service has taken the position that such indebtedness need not be directly traceable to the purchase or carrying of Units (however, these rules generally do not apply to interest paid on indebtedness incurred to purchase or improve a personal residence). Also, under Section 265 of the Code, certain financial institutions that acquire Units would generally not be able to deduct any of the interest expense attributable to ownership of such Units. Investors with questions regarding this issue should consult with their tax advisers.

In the case of certain of the Securities in the Fund, the opinions of bond counsel indicate that interest on such Securities received by a "substantial user" of the facilities being financed with the proceeds of these Securities, or persons related thereto, for periods while such Securities are held by such a user or related person, will not be excludable from Federal gross income, although interest on such Securities received by others would be excludable from Federal gross income. "Substantial user" and "related person" are defined under U.S. Treasury Regulations. Any person who believes that he or she may be a "substantial user" or a "related person" as so defined should contact his or her tax adviser.

At the time of closing for each Trust, Special Counsel to the Fund for New York tax matters have rendered opinions substantially to the effect that under then existing law, the Fund and each Trust are not associations taxable as corporations and the income of each Trust will be treated as the income of the Unitholders under the income tax laws of the State and City of New York.

All statements of law in the Prospectus concerning exclusion from gross income for Federal, state or other tax purposes are the opinions of counsel and are to be so construed.

At the respective times of issuance of the Securities, opinions relating to the validity thereof and to the exclusion of interest thereon from Federal gross income are rendered by bond counsel to the respective issuing authorities. Neither the Sponsor nor Chapman and Cutler has made any special review for the Fund of the proceedings relating to the issuance of the

Securities or of the basis for such opinions.

Section 86 of the Internal Revenue Code provides, in general, that fifty percent of Social Security benefits are includable in gross income to the extent that the sum of "modified adjusted gross income" plus fifty percent of the Social Security benefits received exceeds a "base amount". The base amount is \$25,000 for unmarried taxpayers, \$32,000 for married taxpayers filing a joint return and zero for married taxpayers who do not live apart at all times during the taxable year and who file separate returns. Modified adjusted gross income is adjusted gross income determined without regard to certain otherwise allowable deductions and exclusions from gross income and by including tax exempt interest. To the extent that Social Security benefits are includible in gross income, they will be treated as any other item of gross income.

In addition, under the Tax Act, for taxable years beginning after December 31, 1993, up to 85% of Social Security benefits are includible in gross income to the extent that the sum of "modified adjusted gross income" plus 50% of Social Security benefits received exceeds an "adjusted base amount." The adjusted base amount is \$34,000 for unmarried taxpayers, \$44,000 for married taxpayers filing a joint return, and zero for married taxpayers who do not live apart at all times during the taxable year and who file separate returns.

Although tax exempt interest is included in modified adjusted gross income solely for the purpose of determining what portion, if any, of Social Security benefits will be included in gross income, no tax exempt interest, including that received from the Fund, will be subject to tax. A taxpayer whose adjusted gross income already exceeds the base amount or the adjusted base amount must include fifty percent or eighty-five percent, respectively, of his Social Security benefits in gross income whether or not he receives any tax exempt interest. A taxpayer whose modified adjusted gross income (after inclusion of tax exempt interest) does not exceed the base amount need not include any Social Security benefits in gross income.

In the case of corporations, the alternative tax rate applicable to long-term capital gains is 35%, effective for long-term capital gains realized on or after January 1, 1993. For taxpayers other than corporations, net capital gains are subject to a maximum marginal tax rate of 28 percent. However, it should be noted that legislative proposals are introduced from time to time that affect tax rates and could affect relative differences at which ordinary income and capital gains are taxed. Under the Code, taxpayers must disclose to the Internal Revenue Service the amount of tax-exempt interest earned during the year.

For a discussion of the state tax status of income earned on Units of a State Trust, see "Tax Status" for the applicable Trust. Except as noted therein, the exemption of interest on state and local obligations for Federal income tax purposes discussed above does not necessarily result in exemption under the income or other tax laws of any State or City. The laws of the several States vary with respect to the taxation of such obligations.

#### DESCRIPTION AND STATE TAX STATUS OF STATE TRUSTS

The information below describes some of the more significant events relating to the various State Trusts and sets forth the tax status of each State Trust under applicable state law. The Sponsor makes no representation regarding the accuracy or completion of the information, but believes it to be complete and has itself relied upon such information. The portfolio of each State Trust consists of obligations issued by entities located in such state or in the Commonwealth of Puerto Rico.

Prospective investors should study with care the portfolio of Bonds in a Trust and should consult with their investment advisors as to the merits of particular issues in a portfolio.

#### Alabama Trusts

Alabama's economy has experienced a major trend toward industrialization over the past two decades. By 1990, manufacturing accounted for 26.7% of Alabama's Real Gross State Product (the total value of goods and services produced in Alabama). During the 1960s and 1970s the State's industrial base became more diversified and balanced, moving away from primary metals into pulp and paper, lumber, furniture, electrical machinery, transportation equipment, textiles (including apparel), chemicals, rubber and plastics. Since the early 1980s, modernization of existing facilities and an increase in direct foreign investments in the State has made the manufacturing sector more competitive in domestic and international markets.

Among several leading manufacturing industries have been pulp and papers and chemicals. In recent years Alabama has ranked as the fifth largest producer of timber in the nation. The State's growing chemical industry has been the natural complement of production of wood pulp and paper. Mining, oil and gas production and service industries are also important to Alabama's economy. Coal mining is by far the most important mining activity.



Major service industries that are deemed to have significant growth potential include the research and medical training and general health care industries, most notably represented by the University of Alabama medical complex in Birmingham and the high technology research and development industries concentrated in the Huntsville area.

Real Gross State Product. Real Gross State Product (RGSP) is a comprehensive measure of economic performance for the State of Alabama. Alabama's RGSP is defined as the total value of all final goods and services produced in the State in constant dollar terms. Hence, changes in RGSP reflect changes in final output. From 1984 to 1990 RGSP originating in manufacturing increased by 22.99% whereas RGSP originating in all the non-manufacturing sectors grew by 17.88%.

Those non-manufacturing sectors exhibiting large percentage increases in RGSP originating between 1984 and 1990 were 1) Services; 2) Trade; 3) Farming; and 4) Finance, Insurance and Real Estate. From 1984 to 1990 RGSP originating in services increased by 35.07%; Trade grew by 21.53%; Farming increased by 19.78%; and the gain in Finance, Insurance and Real Estate was 19.19%. The present movement toward diversification of the State's manufacturing base and a similar present trend toward enlargement and diversification of the service industries in the State are expected to lead to increased economic stability.

Employment. The recent national economic recession was felt severely in Alabama. The manufacturing growth described above reached a peak in 1979, and was followed by a decrease in activity. The national economic recession was principally responsible for this decline. The State's industrial structure is particularly sensitive to high interest rates and monetary policy, and the resulting unemployment during 1981-1984 was acute. Unemployment rates have improved as the impact of the national economic recovery has benefited the State. The economic recovery experienced on the national level since 1982 has been experienced in Alabama as well, but to a different degree and with a time lag.

Among other risks, the State of Alabama's economy depends upon cyclical industries such as iron and steel, natural resources, and timber and forest products. As a result, economic activity may be more cyclical than in certain other Southeastern states. The national economic recession in the early 1980s caused a decline in manufacturing activity and natural resource consumption, and Alabama's unemployment rate was 14.4% in 1982, significantly higher than the national average. Unemployment remains high in some rural areas of the State. A trend towards diversification of the State's economic base and an expansion of service industries may lead to improved economic stability in the future, although there is no assurance of this.

Political subdivisions of the State of Alabama have limited taxing authority. In addition, the Alabama Supreme Court has held that a governmental unit may first use its taxes and other revenues to pay the expenses of providing governmental service before paying debt service on its bonds, warrants or other indebtedness. The State has statutory budget provisions which result in a proration procedure in the event estimated budget resources in a fiscal year are insufficient to pay in full all appropriations for that year. Proration has a materially adverse effect on public entities that are dependent upon State funds subject to proration.

Deterioration of economic conditions could adversely affect both tax and other governmental revenues, as well as revenues to be used to service various revenue obligations, such as industrial development obligations. Such difficulties could affect the market value of the bonds held by the Alabama Trust and thereby adversely affect Unitholders.

The foregoing information constitutes only a brief summary of some of the financial difficulties which may impact certain issuers of Bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers in the Alabama Trust are subject. Additionally, many factors including national economic social and environmental policies and conditions, which are not within the control of the issuers of Bonds, could affect or could have an adverse impact on the financial condition of the State and various agencies and political subdivisions located in the State. The sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Alabama Trust to pay interest on or principal of the Bonds.

At the time of the closing for each Alabama Trust, Special Counsel to the Fund for Alabama tax matters rendered an opinion under then existing Alabama income tax law applicable to taxpayers whose income is subject to Alabama income taxation substantially to the effect that:

The Alabama Trust is not taxable as a corporation for purposes of the Alabama income tax;

Income of the Alabama Trust, to the extent it is taxable, will be taxable to the Unitholders, not the Alabama Trust;

Each Unitholder's distributive share of the Alabama Trust's net income will be treated as the income of the Unitholder for purposes of the Alabama income tax;

Interest on obligations held by the Alabama Trust which is exempt from the Alabama income tax will retain its tax-exempt character when the distributive share thereof is distributed or deemed distributed to each Unitholder;

Any proceeds paid to the Alabama Trust under insurance policies issued to the Sponsor or under individual policies obtained by the Sponsor, the issuer or underwriter of the respective obligations which represent maturing interest on defaulted obligations held by the Trustee will be exempt from Alabama income tax if and to the same extent as such interest would be exempt from such taxes if paid directly by the issuer of such obligations;

Each Unitholder will, for purposes of the Alabama income tax, treat his distributive share of gains realized upon the sale or other disposition of the Bonds held by the Alabama Trust as though the Bonds were sold or disposed of directly by the Unitholders; and

Gains realized on the sale or redemption of Units by Unitholders, who are subject to the Alabama income tax will be includable in the Alabama income of such Unitholders.

#### Arizona Trusts

Arizona is the nation's sixth largest state in terms of area and ranks among the leading states in three economic indices of growth. For the ten year period 1978-88, Arizona ranked second nationally in both population growth and growth in employment and third in growth of personal income.

According to figures reported by the Arizona Department of Economic Security, Arizona has been one of the fastest growing states in the nation. While the United States' population increased 11 percent between 1970 and 1980, Arizona realized a 53 percent growth rate. More recently this growth has slowed to a more manageable rate. The population of Arizona has grown consistently at a rate between 2.2% and 2.4% annually during the years 1988 through 1990, and is predicted to remain in that range through 1992. The 1990 census results indicate that the population of Arizona rose 35% between 1980 and 1990, a rate exceeded only in Nevada and Alaska. Nearly 950,000 residents were added during this period.

General Economic Conditions. The following brief summary regarding the economy of Arizona is based upon information drawn from publicly available sources and is included for the purpose of providing the information about general economic conditions that may or may not affect issuers of the Arizona Municipal Obligations. The Sponsor has not independently verified any of the information contained in such publicly available documents.

Arizona is the nation's sixth largest state in terms of area. Arizona's main economic/employment sectors include services, tourism and manufacturing. Mining and agriculture are also significant, although they tend to be more capital than labor intensive. Services is the single largest economic sector. Many of these jobs are directly related to tourism.

According to Arizona economic indicators released as of June 1992, unemployment figures show 7.2 percent of Arizona's population are unemployed, compared to a national level of 7.5 percent unemployment at the same time. Maricopa County reported 6.1 percent unemployment and Pima County reported 5.0 percent unemployment. Significant employers in the state include the government, the service industry and the trade industry. Building permits were down in all areas of the state except for Pima County. In addition, home sales were down approximately 28 percent from the previous year, and retail sales were down approximately 7 percent from the previous year.

On June 27, 1991, America West Airlines filed a Chapter 11 reorganization petition in bankruptcy. America West was at one time the sixth largest employer in Maricopa County, employing approximately 10,000 persons within the county, and 15,000 nationwide. The airline now employs close to 7,000 employees nationwide. The effect of the America West bankruptcy on the state economy and, more particularly, the Phoenix economy, is uncertain.

Similarly, jobs will be lost by the anticipated closing of Williams Air Force Base in Chandler, Arizona, in 1993. Williams Air Force Base was selected as one of the military installations to be closed as a cost-cutting measure by the Defense Base Closure and Realignment Commission, whose recommendations were subsequently approved by the President and the United States House of Representatives. Williams Air Force Base injects approximately \$340 million in the local economy annually, and employs 1,851 civilians.

In 1986, the value of Arizona real estate began a steady decline, reflecting a market which had been overbuilt in the previous decade with a resulting surplus of completed inventory. This decline adversely affected both the



construction industry and those Arizona financial institutions which had aggressively pursued many facets of real estate lending. In the near future, Arizona's financial institutions are likely to continue to experience problems until the excess inventories of commercial and residential properties are absorbed. The problems of the financial institutions have adversely affected unemployment and economic activity. Longer-term prospects are brighter, since population growth is still strong by most standards, and Arizona's climate and tourist industry still continue to stimulate the State's economy. However, the previously robust pace of growth by financial institutions is not likely to be repeated over an extended period.

Arizona operates on a fiscal year beginning July 1 and ending June 30. Fiscal year 1992 refers to the year ending June 30, 1992.

Total General Fund revenues of \$3.4 billion are expected during fiscal year 1992. Approximately 45.8% of this budgeted revenue comes from sales and use taxes, 38.9% from income taxes (both individual and corporate) and 5.3% from property taxes. All taxes total approximately \$3.3 billion, or 93% of the General Fund revenues. Non-tax revenue includes items such as income from the state lottery, licenses, fees and permits, and interest. Lottery income totals approximately 34.6% of non-tax revenue.

For fiscal year 1992, the budget calls for expenditures of \$2.7 billion. These expenditures fell into the following major categories: education (51.3%), health and welfare (29.3%), protection and safety (9.8%), general government (7.6%) and inspection and regulation, natural resources and transportation (2.0%). The State's general fund revenues for fiscal year 1993 are budgeted at \$3.6 billion and total general fund expenditures for fiscal year 1993 are budgeted at \$3.65 billion. Fiscal year 1993's proposed expenditures fall into the following major categories: education (55.4%), health and welfare (27.8%), protection and safety (9.0%), general government (6.2%) and inspection and regulation and natural resources (1.6%).

Most or all of the Bonds of the Arizona Trust are not obligations of the State of Arizona, and are not supported by the State's taxing powers. The particular source of payment and security for each of the Bonds is detailed in the instruments themselves and in related offering materials. There can be no assurances, however, with respect to whether the market value or marketability of any of the Bonds issued by an entity other than the State of Arizona will be affected by the financial or other condition of the State or of any entity located within the State. In addition, it should be noted that the State of Arizona, as well as counties, municipalities, political subdivisions and other public authorities of the state, are subject to limitations imposed by Arizona's constitution with respect to ad valorem taxation, bonded indebtedness and other matters. For example, the legislature cannot appropriate revenues in excess of 7% of the total personal income of the state in any fiscal year. These limitations may affect the ability of the issuers to generate revenues to satisfy their debt obligations.

Local governments have experienced many of the same fiscal difficulties for many of the same reasons and, in several cases, have been prevented by Constitutional limitations on bonded indebtedness from securing necessary funds to undertake street, utility and other infrastructure expansions, improvements and renovations in order to meet the needs of rapidly increasing populations. In this regard, the voters of the cities of Phoenix and Tucson in 1984 authorized the issuance of general obligation and revenue bonds aggregating \$525 million and \$330 million, respectively, and in May 1986, the voters of Maricopa County, in which the City of Phoenix is located, and Pima County, in which the City of Tucson is located, authorized the issuance of bonds aggregating \$261 million and \$219.4 million, respectively, to finance various short- and long-term capital projects, including infrastructure expansions, improvements and replacements. Also, in 1986, the voters in Maricopa and Pima Counties voted a 1/2% increase in the State sales taxes to pay for highway construction in those counties. In April 1988 the voters of the City of Phoenix authorized the issuance of general obligation bonds aggregating \$1.1 billion.

Although most of the Bonds in the Arizona Trust are revenue obligations of local governments or authorities in the State, there can be no assurance that the fiscal and economic conditions referred to above will not affect the market value or marketability of the Bonds or the ability of the respective obligors to pay principal of and interest on the Bonds when due.

The State of Arizona was recently sued by four named school districts with an additional fifty school districts within the state participating in the suit, claiming that the State's funding system for school buildings and equipment is unconstitutional. The lawsuit does not seek damages, but requests that the court order the State to create a new financing system that sets minimum standards for buildings and furnishings that apply on a statewide basis. A superior court ruling has upheld the constitutionality of the State's school funding system. This decision has been appealed and is currently in the State Court of Appeals. It is unclear, at this time, what affect any judgment would have on state finances or school district budgets. The U.S. Department of Education recently determined that Arizona's educational funding system did

not meet federal requirements of equity. This determination could mean a loss in federal funds of approximately \$50 million.

Certain other circumstances are relevant to the market value, marketability and payment of any hospital and health care revenue bonds in the Arizona Trust. The Arizona Legislature attempted unsuccessfully in its 1984 regular and special sessions to enact legislation designed to control health care costs, ultimately adopting three referenda measures placed on the November 1984 general election ballot which in various ways would have regulated hospital and health care facility expansions, rates and revenues. At the same time, a coalition of Arizona employers proposed two initiatives voted on in the November 1984 general election which would have created a State agency with power to regulate hospital and health care facility expansions and rates generally. All of these referenda and initiative propositions were rejected by the voters in the November 1984 general election. Pre-existing State certificate-of-need laws regulating hospital and health care facilities' expansions and services have expired, and a temporary moratorium prohibiting hospital bed increases and new hospital construction projects and a temporary freeze on hospital rates and charges at June 1984 levels has also expired. Because of such expirations and increasing health care costs, it is expected that the Arizona Legislature will at future sessions continue to attempt to adopt legislation concerning these matters. The effect of any such legislation or of the continued absence of any legislation restricting hospital bed increases and limiting new hospital construction on the ability of Arizona hospitals and other health care providers to pay debt service on their revenue bonds cannot be determined at this time.

Arizona does not participate in the federally administered Medicaid program. Instead, the state administers an alternative program, AHCCCS, which provides health care to indigent persons meeting certain financial eligibility requirements, through managed care programs. In fiscal year 1992, AHCCCS will be financed approximately 52.7% by federal funds, 33.1% by state funds, and 13.6% by county funds.

Under state law, hospitals retain the authority to raise rates with notification and review by, but not approval from, the Department of Health Services. Hospitals in Arizona have experienced profitability problems along with those in other states. At least two Phoenix based hospitals have defaulted on or reported difficulties in meeting their bond obligations during the past three years.

Insofar as tax-exempt Arizona public utility pollution control revenue bonds are concerned, the issuance of such bonds and the periodic rate increases needed to cover operating costs and debt service are subject to regulation by the Arizona Corporation Commission, the only significant exception being the Salt River Project Agricultural Improvement and Power District which, as a Federal instrumentality, is exempt from rate regulation. On July 15, 1991, several creditors of Tucson Electric Power Company ("Tucson Electric") filed involuntary petitions under Chapter 11 of the U.S. Bankruptcy Code to force Tucson Electric to reorganize under the supervision of the bankruptcy court. On December 31, 1991, the Bankruptcy Court approved the utility's motion to dismiss the July petition after five months of negotiations between Tucson Electric and its creditors to restructure the utility's debts and other obligations. In January 1993, Tucson Electric asked the Arizona Corporation Commission for a 9.6% average rate increase. Tucson Electric serves approximately 270,000 customers, primarily in the Tucson area. Inability of any regulated public utility to secure necessary rate increases could adversely affect, to an indeterminable extent, its ability to pay debt service on its pollution control revenue bonds.

At the time of the closing for each Arizona Trust, Special Counsel to the Fund for Arizona tax matters rendered an opinion under then existing Arizona income tax law applicable to taxpayers whose income is subject to Arizona income taxation substantially to the effect that:

For Arizona income tax purposes, each Unitholder will be treated as the owner of a pro rata portion of the Arizona Trust, and the income of the Trust therefore will be treated as the income of the Unitholder under State law;

For Arizona income tax purposes, interest on the Bonds which is excludable from Federal gross income and which is exempt from Arizona income taxes when received by the Arizona Trust, and which would be excludable from Federal gross income and exempt from Arizona income taxes if received directly by a Unitholder, will retain its status as tax-exempt interest when received by the Arizona Trust and distributed to the Unitholders;

To the extent that interest derived from the Arizona Trust by a Unitholder with respect to the Bonds is excludable from Federal gross income, such interest will not be subject to Arizona income taxes;

Each Unitholder will receive taxable gain or loss for Arizona income tax purposes when Bonds held in the Arizona Trust are sold, exchanged, redeemed or paid at maturity, or when the Unitholder redeems or sells Units, at a price that differs from original cost as adjusted for amortization of Bond discount

or premium and other basis adjustments, including any basis reduction that may be required to reflect a Unitholder's share of interest, if any, accruing on Bonds during the interval between the Unitholder's settlement date and the date such Bonds are delivered to the Arizona Trust, if later;

Amounts paid by the Insurer under an insurance policy or policies issued to the Trust, if any, with respect to the Bonds in the Trust which represent maturing interest on defaulted obligations held by the Trustee will be exempt from State income taxes if, and to the same extent as, such interest would have been so exempt if paid by the issuer of the defaulted obligations;

Arizona law does not permit a deduction for interest paid or incurred on indebtedness incurred or continued to purchase or carry Units in the Arizona Trust, the interest on which is exempt from Arizona income taxes; and

Neither the Bonds nor the Units will be subject to Arizona property taxes, sales tax or use tax.

#### Arkansas Trusts

The Constitution of Arkansas specifically prohibits the creation of any State general obligation debt unless authorized in a Statewide general election. Although the State of Arkansas defaulted on some of its general obligation debt during the depression in the later 1930's, it has not failed to pay the principal and interest on any of its general obligations when due since that time.

Act 496 of 1981, as amended, the "Arkansas Water Resources Development Act of 1981," ("Act 496") authorized the issuance of State Water Resources Development General Obligation Bonds by the State of Arkansas, acting by and through the Arkansas Soil and Water Conservation Commission. The issuance of bonds pursuant to Act 496 was approved by the electors of the State at the general election on November 2, 1982. The total principal amount of bonds issued during any fiscal biennium may not exceed \$15,000,000, and the total principal of all bonds issued under Act 496 may not exceed \$100,000,000. All Bonds to be issued under Act 496 shall be direct general obligations of the State, the principal and interest of which are payable from the general revenues of the State. Pursuant to Act 496, the State of Arkansas has issued and outstanding two series of bonds in the aggregate principal amount of \$28,075,000 under Act 496.

Deficit spending has been prohibited by statute in Arkansas since 1945. The Revenue Stabilization Law requires that before any State spending can take place, there must be an appropriation by the General Assembly and there must be funds available in the fund from which the appropriation has been made. The State is prohibited from borrowing money to put into any State fund from which appropriations can be paid.

Information regarding the financial condition of the State is included for the purpose of providing information about general economic conditions that may affect issuers of the Bonds in Arkansas. The Arkansas economy represents approximately 2.0% of the total United States' economy. Its small size causes the Arkansas economy to follow the national economy. Fluctuations in the national economy are often mirrored by coinciding or delayed fluctuations in the Arkansas economy.

Arkansas' economy is both agricultural and manufacturing based. Only five states generate a larger proportion of earnings from agriculture, and only 17 states generate a larger proportion of earnings from manufacturing. Similarly, only 10 states have a larger proportion of employment in agriculture and only 18 states have a larger proportion of employment in manufacturing. Thus, the State of Arkansas feels the full force of the business cycle and also sees the growth swing from positive to negative as conditions in agriculture change.

Agriculture has had a depressant effect on the Arkansas economy regardless of the phase the business cycle was in. In recent years, agricultural employment in Arkansas has been on the decline. In both 1987 and 1988, agricultural employment declined by 1.6%. Agriculture employment also declined in 1989 by 1.6% and should continue to decline according to State forecasters as labor intensive production is shifted to less labor intensive production.

Employment in Arkansas' construction industry decreased 2.3% in 1988. This followed a 5.6% decline in 1987. In 1989, State forecasters anticipated a decline in growth rate of 2.5%. A further decline of 0.7% is expected in 1990.

During the past two decades, Arkansas' economic base has shifted from agriculture to light manufacturing. In 1986, Arkansas ranked fifth in the United States with a 2.1% growth of new manufacturing jobs. The diversification of economic interest shares lessened Arkansas' cyclical sensitivity to impact by any single sector. During 1988, total employment increased by 3.4% and total nonagricultural wage and salary employment increased by 2.8%. Total employment growth in Arkansas exceeded the growth rate of total employment in the United States. The average unemployment rate declined from 8.1% in 1987 to 7.7% in 1988. The increase in earnings along

with the rise in employment generated a 6.9% increase in total personal income in 1988.

Counties and municipalities may issue general obligation bonds (pledging an ad valorem tax), special obligation bonds (pledging other specific tax revenues) and revenue bonds (pledging only specific revenues from sources other than tax revenues). School districts may issue general obligation bonds (pledging ad valorem taxes). Revenue bonds may also be issued by agencies and instrumentalities of counties, municipalities and the State of Arkansas but as in all cases of revenue bonds, neither the full faith and credit nor the taxing power of the State of Arkansas or any municipality or county thereof is pledged to the repayment of those bonds. Revenue bonds can be issued only for public purposes, including, but not limited to, industry, housing, health care facilities, airports, port facilities and water and sewer projects.

At the time of the closing for each Arkansas Trust, Special Counsel to each Arkansas Trust for Arkansas tax matters rendered an opinion under then existing Arkansas income tax law applicable to taxpayers whose income is subject to Arkansas income taxation substantially to the effect that:

The opinion of Chapman and Cutler, counsel for Van Kampen Merritt Inc., concludes that each Trust, including the Arkansas Trust, will be governed for Federal tax purposes by the provisions of Subchapter J of Chapter 1 of the Code. Although there are no Arkansas income tax statutes similar to Subchapter J of Chapter 1 of the Code, Arkansas statutory provisions operate to reach the same result that is reached under the Federal system. Arkansas law defines Arkansas gross income for residents similarly to the definition of Federal gross income, and that definition of Arkansas gross income specifically excludes interest on obligations of the State of Arkansas or any political subdivision thereof.

Based upon the foregoing and, in reliance upon the opinion of Chapman and Cutler, counsel to Van Kampen Merritt Inc., the Sponsor, and upon an examination of such other documents and an investigation of such other matters of law as we have deemed necessary, it is our opinion that the application of existing Arkansas income tax law to Arkansas Unitholders would be as follows:

The Arkansas Trust is not taxable as a corporation or otherwise for purposes of Arkansas income taxation;

Each Arkansas Unitholder will be treated as the owner of a pro rata portion of the Arkansas Trust for Arkansas income tax purposes, and the income of the Arkansas Trust will therefore be treated as the income the Arkansas Unitholders under Arkansas law;

Interest on bonds, issued by the State of Arkansas, or by or on behalf of political subdivisions, agencies or instrumentalities thereof, that would be exempt from Federal income taxation when paid directly to an Arkansas Unitholder will be exempt from Arkansas income taxation when received by the Arkansas Trust and attributed to such Arkansas Unitholder and when distributed to such Arkansas Unitholder; and

Distribution of income to Arkansas Unitholders consisting of gains realized upon the sale or other disposition of obligations held by the Arkansas Trust will be subject to Arkansas income taxation to the extent that such income would be subject to Arkansas income taxation if the obligations were held or sold or otherwise disposed of directly by the Arkansas Unitholders.

#### California Trusts

The Trust will invest substantially all of its assets in California Municipal Obligations. The Trust is therefore susceptible to political, economic or regulatory factors affecting issuers of California Municipal Obligations. These include the possible adverse effects of certain California constitutional amendments, legislative measures, voter initiatives and other matters that are described below. The following information provides only a brief summary of the complex factors affecting the financial situation in California (the "State") and is derived from sources that are generally available to investors and are believed to be accurate. No independent verification has been made of the accuracy or completeness of any of the following information. It is based in part on information obtained from various State and local agencies in California or contained in official statements for various California Municipal Obligations.

There can be no assurance that future statewide or regional economic difficulties, and the resulting impact on State or local governmental finances generally, will not adversely affect the market value of California Municipal Obligations held in the portfolio of the Fund or the ability of particular obligors to make timely payments of debt service on (or related to) those obligations.

California's economy is the largest among the 50 states and one of the largest in the world. The State's population of almost 32 million represents 12.8% of the total United States population and grew by 27% in the 1980s. Total

personal income in the State, at an estimated \$640 billion in 1992, accounts for 13% of all personal income in the nation. Total employment is almost 14 million, the majority of which is in the service, trade and manufacturing sectors.

Reports issued by the State Department of Finance and the Commission on State Finance (the "COSF") indicate that the State's economy is suffering its worst recession since the 1930s, with prospects for recovery slower than for the nation as a whole. The State has experienced the worst job losses of any post-war recession and employment levels are not expected to stabilize until late 1994 or 1995. The largest job losses have been in Southern California, led by declines in the aerospace and construction industries. Weaknesses statewide occurred in manufacturing, construction, services and trade. Additional military base closures will have further adverse effects on the State's economy later in the decade. Unemployment is expected to average 9% in 1993, and is expected to remain high in 1994. The State's economy is only expected to pull out of the recession slowly once the national recovery has begun. Delay in recovery will exacerbate shortfalls in State revenues.

Certain California Municipal Obligations may be obligations of issuers which rely in whole or in part, directly or indirectly, on ad valorem property taxes as a source of revenue. The taxing powers of California local governments and districts are limited by Article XIII A of the California Constitution, enacted by the voters in 1978 and commonly known as "Proposition 13." Briefly, Article XIII A limits to 1% of full cash value the rate of ad valorem property taxes on real property and generally restricts the reassessment of property to 2% per year, except upon new construction or change of ownership (subject to a number of exemptions). Taxing entities may, however, raise ad valorem taxes above the 1% limit to pay debt service on voter-approved bonded indebtedness.

Under Article XIII A, the basic 1% ad valorem tax levy is applied against the assessed value of property as of the owner's date of acquisition (or as of March 1, 1975, if acquired earlier), subject to certain adjustments. This system has resulted in widely varying amounts of tax on similarly situated properties. Several lawsuits have been filed challenging the acquisition-based assessment system of Proposition 13, and on June 18, 1992 the U.S. Supreme Court announced a decision upholding Proposition 13.

Article XIII A prohibits local governments from raising revenues through ad valorem property taxes above the 1% limit; it also requires voters of any governmental unit to give two-thirds approval to levy any "special tax." Court decisions allowed non-voter approved levy of "general taxes" which were not dedicated to a specific use. In response to these decisions, however, the voters of the State in 1986 adopted an initiative statute which imposed significant new limits on the ability of local entities to raise or levy general taxes, except by receiving majority local voter approval. Significant elements of this initiative, "Proposition 62", have been overturned in recent court cases. An initiative proposed to re-enact the provisions of Proposition 62 as a constitutional amendment was defeated by the voters in November 1990, but such a proposal may be renewed in the future.

California and its local governments are subject to an annual "appropriations limit" imposed by Article XIII B of the California Constitution, enacted by the voters in 1979 and significantly amended by Propositions 98 and 111 in 1988 and 1990, respectively. Article XIII B prohibits the State or any covered local government from spending "appropriations subject to limitation" in excess of the appropriations limit imposed. "Appropriations subject to limitation" are authorizations to spend "proceeds of taxes," which consists 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 of providing the product or service, but "proceeds of taxes" excludes most State subventions to local governments. No limit is imposed on appropriations or funds which are not "proceeds of taxes," such as reasonable user charges or fees and certain other non-tax funds, including bond proceeds.

Among the expenditures not included in the Article XIII B appropriations limit are (1) the debt service cost of bonds issued or authorized prior to January 1, 1979, or subsequently authorized by the voters, (2) appropriations arising from certain emergencies declared by the Governor, (3) appropriations for certain capital outlay projects, (4) appropriations by the State of post-1989 increases in gasoline taxes and vehicle weight fees, and (5) appropriations made in certain cases of emergency.

The appropriations limit for each year is adjusted annually to reflect changes in cost of living and population, and any transfers of service responsibilities between government units. The definitions for such adjustments were liberalized in 1990 by Proposition 111 to follow more closely growth in California's economy.

"Excess" revenues are measured over a two-year cycle. Local governments must return any excess to taxpayers by rate reduction. The State must refund 50% of any excess, with the other 50% paid to schools and community colleges. With more liberal annual adjustment factors since 1988, and depressed revenues since 1990 because of the recession, few governments are currently operating

near their spending limits, but this condition may change over time. Local governments may by voter approval exceed their spending limits for up to four years.

During fiscal year 1986-87, State receipts from proceeds of taxes exceeded its appropriations limit by \$1.1 billion, which was returned to taxpayers. Appropriations subject to limitation were under the State limit by \$1.2 billion, \$259 million, \$1.6 million, \$7.5 billion and \$5.2 billion for the five most recent fiscal years ending with 1991-92. State appropriations are expected to be \$4.2 billion under the limit for Fiscal Year 1992-93.

Because of the complex nature of Articles XIII A and XIII B of the California Constitution, the ambiguities and possible inconsistencies in their terms, and the impossibility of predicting future appropriations or changes in population and cost of living, and the probability of continuing legal challenges, it is not currently possible to determine fully the impact of Article XIII A or Article XIII B on California Municipal Obligations or on the ability of the State or local governments to pay debt service on such California Municipal Obligations. It is not presently possible to predict the outcome of any pending litigation with respect to the ultimate scope, impact or constitutionality of either Article XIII A or Article XIII B, or the impact of any such determinations upon State agencies or local governments, or upon their ability to pay debt service on their obligations. Future initiative or legislative changes in laws or the California Constitution may also affect the ability of the State or local issuers to repay their obligations.

As of January 1, 1994, California had approximately \$17.7 billion of general obligation bonds outstanding, and \$6.3 billion remained authorized but unissued. In addition, at June 30, 1993, the State had lease-purchase obligations, payable from the State's General Fund, of approximately \$4.0 billion. In Fiscal Year 1992-93, debt service on general obligation bonds and lease-purchase debt was approximately 4.1% of General Fund revenues. The State has paid the principal of and interest on its general obligation bonds, lease-purchase debt and short-term obligations when due.

The principal sources of General Fund revenues in 1992-93 were the California personal income tax (44% of total revenues), the sales tax (38%), bank and corporation taxes (12%), and the gross premium tax on insurance (3%). California maintains a Special Fund for Economic Uncertainties (the "Economic Uncertainties Fund"), derived from General Fund.

Throughout the 1980s, State spending increased rapidly as the State population and economy also grew rapidly, including increased spending for many assistance programs to local governments, which were constrained by Proposition 13 and other laws. The largest State program is assistance to local public school districts. In 1988, an initiative (Proposition 98) was enacted which (subject to suspension by a two-thirds vote of the Legislature and the Governor) guarantees local school districts and community college districts a minimum share of State General Fund revenues (currently about 33%).

Since the start of 1990-91 Fiscal Year, the State has faced adverse economic, fiscal, and budget conditions. The economic recession seriously affected State tax revenues. It also caused increased expenditures for health and welfare programs. The State is also facing a structural imbalance in its budget with the largest programs supported by the General Fund (education, health, welfare and corrections) growing at rates significantly higher than the growth rates for the principal revenue sources of the General Fund. As a result, the State entered a period of budget imbalance, with expenditures exceeding revenues for four of the five fiscal years ending in 1991-92; revenues were about equal in 1992-93. By June 30, 1993, the State's General Fund had an accumulated deficit, on a budget basis, of approximately \$2.2 billion.

As a consequence of the large budget imbalances built up over two consecutive years, the State used up all of its available cash resources. In late June 1992, the State was required to issue \$475 million of short-term revenue anticipation warrants to cover obligations coming due on June 30 and July 1. These warrants were repaid on July 24, 1992.

At the outset of the 1992-93 Fiscal Year, the State estimated that approximately \$7.9 billion of budget actions would be required to end the 1992-93 Fiscal Year without a budget deficit. The difficulty of taking those actions delayed enactment of a budget for more than two months past the start of the 1992-93 Fiscal Year. With the failure to enact a budget by July 1, 1992, the State had no legal authority to pay many of its vendors until the budget was passed; nevertheless, certain obligations (such as debt service, school apportionments, welfare payments and employee salaries) were payable because of continuing or special appropriations or court orders. However, the State Controller did not have enough cash to pay all of these ongoing obligations as they came due, as well as valid obligations incurred in the prior fiscal year.

Because of the delay in enacting the budget, the State could not carry out its normal cash flow borrowing, and starting on July 1, 1992, the Controller was



required to issue "registered warrants" in lieu of normal warrants backed by cash to pay many State obligations. Available cash was used to pay constitutionally mandated and priority obligations. Between July 1 and September 3, 1992, the Controller issued an aggregate of approximately \$3.8 billion of registered warrants, all of which were called for redemption by September 4, 1992 following enactment of the 1992-93 Budget Act and issuance by the State of \$3.3 billion of Interim Notes.

The 1992-93 Budget Bill was signed on September 2, 1992. The 1992-93 Budget Act provides for expenditures of \$57.4 billion and consists of General Fund expenditures of \$40.8 billion and Special Fund and Bond Fund expenditures of \$16.6 billion. The Department of Finance estimated there would be a balance in the Special Fund for Economic Uncertainties of \$28 million on June 30, 1993.

The \$7.9 billion budget gap was closed through a combination of increased revenues and transfers and expenditure cuts. The principle reductions were in health and welfare, K-12 schools and community colleges, State aid to local governments, higher education (partially offset by increased student fees) and various other programs. In addition, funds were transferred from special funds, collections of State revenues were accelerated, and other adjustments were made.

As in the prior year, the economic and fiscal assumptions on which the 1992-93 Budget Act was based proved to be too optimistic. As the recession in the State continued for a third year, State revenues again lagged projections. The Department of Finance projected revenues in 1992-93 \$2.4 billion below projections and expenditures \$300 million higher. As a result, the Department predicted the General Fund ended at June 30, 1993 with a fund balance deficit of about \$2.2 billion, almost unchanged from June 30, 1992. The projected negative balance of the Special Fund for Economic Uncertainties were \$2 billion.

1993-94 Budget. The 1993-94 Budget represents the third consecutive year of extremely difficult budget choices for the State, in view of the continuing recession. The Budget Act, signed on June 30, 1993, provides for General Fund expenditures of \$38.5 billion, a 6.3% decline from the prior year. Revenues are projected at \$40.6 billion, about \$400 million below the prior year. To bring the budget into balance, the Budget Act and related legislation provided for transfer of \$2.6 billion of local property taxes to school districts, thus relieving State support obligations; reductions in health and welfare expenditures; reductions in support for higher education institutions; a two-year suspension of the renters' tax credit; and miscellaneous cuts in general government spending and certain one-time and accounting adjustments. There were no general state tax increases, but a 0.5% temporary state sales tax scheduled to expire on June 30 was extended for six months, and dedicated to support local government public safety costs.

As part of the 1993-94 Budget, the Governor implemented a plan to repay the accumulated \$2.8 billion deficit in the Special Fund for Economic Uncertainties over 18 months, funding the deficit with external borrowing maturing not later than December 31, 1994. About \$1.6 billion of the deficit was repaid by December 1993, with the balance to be paid by December 31, 1994. Taking this borrowing into account, the Department of Finance projected in July, 1993 that the Special Fund for Economic Uncertainties would have a balance of about \$600 million at June 30, 1994, and about \$100 million at June 30, 1995.

The 1994-95 Governor's Budget Proposal, released January 7, 1994, projects that because of the continuation of the recession, the 1993-94 fiscal year will end with a negative fund balance \$1.7 billion worse than originally planned, even though state revenues have been close to projections through the first six months of the 1993-94 fiscal year.

To produce a balanced budget in 1994-95, the Governor proposes further cuts in health and welfare costs, and requests additional federal aid of over \$3 billion for costs associated with undocumented foreign immigrants and for health and welfare programs. There is no assurance these funds will be appropriated by the Congress.

On January 17, 1994 a major earthquake struck Los Angeles, causing widespread property damage in public and private structures and facilities, estimated preliminarily at in excess of \$15 billion. Large amounts of federal aid are expected, and additional state resources will be made available. It is too soon to assess the short or long term impacts of the earthquake on the regional and state economies, and on the fiscal condition of local and state government.

The State's severe financial difficulties for the current and upcoming budget years will result in continued pressure upon various local governments, particularly school districts and counties which depend on State aid. Despite efforts in recent years to increase taxes and reduce governmental expenditures, there can be no assurance that the State will not face budget gaps in the future.

State general obligation bonds are currently rated "Aa" by Moody's and "A+" by S&P. Both of these ratings were recently reduced from "AAA" levels which the State held until late 1991. There can be no assurance that such ratings will be maintained in the future. It should be noted that the creditworthiness of obligations issued by local California issuers may be unrelated to the creditworthiness of obligations issued by the State of California, and that there is no obligation on the part of the State to make payment on such local obligations in the event of default.

The State is involved in certain legal proceedings (described in the State's recent financial statements) that, if decided against the State, may require the State to make significant future expenditures or may substantially impair revenues.

There are a number of state agencies, instrumentalities and political subdivisions of the State that issue Municipal Obligations, some of which may be conduit revenue obligations payable from payments from private borrowers. These entities are subject to various economic risks and uncertainties, and the credit quality of the securities issued by them may vary considerably from the credit quality of obligations backed by the full faith and credit of the State.

Property tax revenues received by local governments declined more than 50% following passage of Proposition 13. Subsequently, the California Legislature enacted measures to provide for the redistribution of the State's General Fund surplus to local agencies, the reallocation of certain State revenues to local agencies and the assumption of certain governmental functions by the State to assist municipal issuers to raise revenues. Through 1990-91, local assistance (including public schools) accounted for around 75% of General Fund spending. To reduce State General Fund support for school districts, the 1992-93 Budget Act caused local governments to transfer \$1.3 billion of property tax revenues to school districts, representing loss of almost half the post-Proposition 13 "bailout" aid. The 1993-94 Budget Act transfers about \$2.6 billion of local property taxes to school districts, the largest share (\$2 billion) coming from counties, and the balance from cities (\$288 million), special districts (\$244 million) and redevelopment agencies (\$65 million). In order to make up this shortfall to cities and counties, the Legislature has dedicated 0.5% sales tax to local public safety purposes through December 31, 1993. Voters at a statewide election in November, 1993 will vote on a permanent extension of this sales tax for local public safety. In addition, the Legislature has changed laws to relieve local governments of certain mandates, allowing them to reduce costs.

To the extent the State should be constrained by its Article XIII B appropriations limit, or its obligation to conform to Proposition 98, or other fiscal considerations, the absolute level, or the rate of growth, of State assistance to local governments may continue to be reduced. Any such reductions in State aid could compound the serious fiscal constraints already experienced by many local governments, particularly counties. At least one rural county (Butte) publicly announced that it might enter bankruptcy proceedings in August 1990, although such plans were put off after the Governor approved legislation to provide additional funds for the county. Other counties have also indicated that their budgetary condition is extremely grave. The Richmond Unified School District (Contra Costa County) entered bankruptcy proceedings in May 1991, but the proceedings have been dismissed.

California Municipal Obligations which are assessment bonds may be adversely affected by a general decline in real estate values or a slowdown in real estate sales activity. In many cases, such bonds are secured by land which is undeveloped at the time of issuance but anticipated to be developed within a few years after issuance. In the event of such reduction or slowdown, such development may not occur or may be delayed, thereby increasing the risk of a default on the bonds. Because the special assessments or taxes securing these bonds are not the personal liability of the owners of the property assessed, the lien on the property is the only security for the bonds. Moreover, in most cases the issuer of these bonds is not required to make payments on the bonds in the event of delinquency in the payment of assessments or taxes, except from amounts, if any, in a reserve fund established for the bonds.

Certain California long-term lease obligations, though typically payable from the general fund of the municipality, are subject to "abatement" in the event the facility being leased is unavailable for beneficial use and occupancy by the municipality during the term of the lease. Abatement is not a default, and there may be no remedies available to the holders of the certificates evidencing the lease obligation in the event abatement occurs. The most common cases of abatement are failure to complete construction of the facility before the end of the period during which lease payments have been capitalized and uninsured casualty losses to the facility (e.g., due to earthquake). In the event abatement occurs with respect to a lease obligation, lease payments may be interrupted (if all available insurance proceeds and reserves are exhausted) and the certificates may not be paid when due.

Several years ago the Richmond Unified School District (the "District") entered into a lease transaction in which certain existing properties of the



District were sold and leased back in order to obtain funds to cover operating deficits. Following a fiscal crisis in which the District's finances were taken over by a State receiver (including a brief period under bankruptcy court protection), the District failed to make rental payments on this lease, resulting in a lawsuit by the Trustee for the Certificate of Participation holders, in which the State was a named defendant (on the grounds that it controlled the District's finances). One of the defenses raised in answer to this lawsuit was the invalidity of the original lease transaction. The trial court upheld the validity of the lease, and the case is expected to be settled, but if it is not, further appeals may occur. Any ultimate judgment against the Trustee may have adverse implications for lease transactions of a similar nature by other California entities.

The repayment of industrial development securities secured by real property may be affected by California laws limiting foreclosure rights of creditors. Securities backed by health care and hospital revenues may be affected by changes in State regulations governing cost reimbursements to health care providers under Medi-Cal (the State's Medicaid program), including risks related to the policy of awarding exclusive contracts to certain hospitals.

Limitations on ad valorem property taxes may particularly affect "tax allocation" bonds issued by California redevelopment agencies. Such bonds are secured solely by the increase in assessed valuation of a redevelopment project area after the start of redevelopment activity. In the event that assessed values in the redevelopment project decline (for example, because of a major natural disaster such as an earthquake), the tax increment revenue may be insufficient to make principal and interest payments on these bonds. Both Moody's and S&P suspended ratings on California tax allocation bonds after the enactment of Article XIII A and Article XIII B, and only resumed such ratings on a selective basis.

Proposition 87, approved by California voters in 1988, requires that all revenues produced by a tax rate increase go directly to the taxing entity which increased such tax rate to repay that entity's general obligation indebtedness. As a result, redevelopment agencies (which, typically, are the Issuers of tax allocation securities) no longer receive an increase in tax increment when taxes on property in the project area are increased to repay voter-approved bonded indebtedness.

The effect of these various constitutional and statutory changes upon the ability of California municipal securities issuers to pay interest and principal on their obligations remains unclear. Furthermore, other measures affecting the taxing or spending authority of California or its political subdivisions may be approved or enacted in the future. Legislation has been or may be introduced which would modify existing taxes or other revenue-raising measures or which either would further limit or, alternatively, would increase the abilities of state and local governments to impose new taxes or increase existing taxes. It is not presently possible to determine the impact of any such legislation on California Municipal Obligations in which the Fund may invest, future allocations of state revenues to local governments or the abilities of state or local governments to pay the interest on, or repay the principal of, such California Municipal Obligations.

Substantially all of California is within an active geologic region subject to major seismic activity. Any California Municipal Obligation in the Portfolio could be affected by an interruption of revenues because of damaged facilities, or, consequently, income tax deductions for casualty losses or property tax assessment reductions. Compensatory financial assistance could be constrained by the inability of (i) an Issuer to have obtained earthquake insurance coverage at reasonable rates; (ii) an insurer to perform on its contracts of insurance in the event of widespread losses; or (iii) the Federal or State government to appropriate sufficient funds within their respective budget limitations.

At the time of the closing for each California Trust, Special Counsel to each California Trust for California tax matters, rendered an opinion under then existing California income tax law applicable to taxpayers whose income is subject to California income taxation substantially to the effect that:

the California Trust is not an association taxable as a corporation and the income of the California Trust will be treated as the income of the Unitholders under the income tax laws of California;

amounts treated as interest on the underlying Securities in the California Trust which are exempt from tax under California personal income tax and property tax laws when received by the California Trust will, under such laws, retain their status as tax-exempt interest when distributed to Unitholders. However, interest on the underlying Securities attributed to a Unitholder which is a corporation subject to the California franchise tax laws may be includable in its gross income for purposes of determining its California franchise tax. Further, certain interest which is attributable to a Unitholder subject to the California personal income tax and which is treated as an item of tax preference for purposes of the federal alternative minimum tax pursuant to Section 57(a)(5) of the Internal Revenue Code of 1986 may also be treated

as an item of tax preference that must be taken into account in computing such Unitholder's alternative minimum taxable income for purposes of the California alternative minimum tax enacted by 1987 California Statutes, chapter 1138. However, because of the provisions of the California Constitution exempting the interest on bonds issued by the State of California, or by local governments within the state, from taxes levied on income, the application of the new California alternative minimum tax to interest otherwise exempt from the California personal income tax in some cases may be unclear;

under California income tax law, each Unitholder in the California Trust will have a taxable event when the California Trust disposes of a Security (whether by sale, exchange, redemption, or payment at maturity) or when the Unitholder redeems or sells Units. Because of the requirement that tax cost basis be reduced to reflect amortization of bond premium, under some circumstances a Unitholder may realize taxable gains when Units are sold or redeemed for an amount equal to, or less than, their original cost. The total cost of each Unit in the California Trust to a Unitholder is allocated among each of the Bond issues held in the California Trust (in accordance with the proportion of the California Trust comprised by each Bond issue) in order to determine his per Unit tax cost for each Bond issue; and the tax cost reduction requirements relating to amortization of bond premium will apply separately to the per Unit tax cost of each Bond issue. Unitholders' bases in their Units, and the bases for their fractional interest in each Trust asset, may have to be adjusted for their pro rata share of accrued interest received, if any, on Securities delivered after the Unitholders' respective settlement dates;

under the California personal property tax laws, bonds (including the Securities in the California Trust) or any interest therein is exempt from such tax; and

any proceeds paid under the insurance policy issued to the California Trust with respect to the Securities which represent maturing interest on defaulted obligations held by the Trustee will be exempt from California personal income tax if, and to the same extent as, such interest would have been so exempt if paid by the issuer of the defaulted obligations; and

under Section 17280(b)(2) of the California Revenue and Taxation Code, interest on indebtedness incurred or continued to purchase or carry Units of the California Trust is not deductible for the purposes of the California personal income tax. While there presently is no California authority interpreting this provision, Section 17280(b)(2) directs the California Franchise Tax Board to prescribe regulations determining the proper allocation and apportionment of interest costs for this purpose. The Franchise Tax Board has not yet proposed or prescribed such regulations. In interpreting the generally similar Federal provision, the Internal Revenue Service has taken the position that such indebtedness need not be directly traceable to the purchase or carrying of Units (although the Service has not contended that a deduction for interest on indebtedness incurred to purchase or improve a personal residence or to purchase goods or services for personal consumption will be disallowed). In the absence of conflicting regulations or other California authority, the California Franchise Tax Board generally has interpreted California statutory tax provisions in accord with Internal Revenue Service interpretations of similar Federal provisions.

At the respective times of issuance of the Securities, opinions relating to the validity thereof and to the exemption of interest thereon from Federal income tax and California personal income tax are rendered by bond counsel to the respective issuing authorities. Except in certain instances in which Special Counsel acted as bond counsel to issuers of Securities, and as such made a review of proceedings relating to the issuance of certain Securities at the time of their issuance, Special Counsel has not made any special review for the California Trusts of the proceedings relating to the issuance of the Securities or of the basis for such opinions.

#### Colorado Trust

The State Constitution requires that expenditures for any fiscal year not exceed revenues for such fiscal year. By statute, the amount of General Fund revenues available for appropriation is based upon revenue estimates which, together with other available resources, must exceed annual appropriations by the amount of the unappropriated reserve (the "Unappropriated Reserve"). The Unappropriated Reserve requirement for fiscal year 1991, 1992 and 1993 was set at 3%. For fiscal year 1992 and thereafter, General Fund appropriations are also limited to an amount equal to the cost of performing certain required reappraisals of taxable property plus an amount equal to the lesser of (i) five percent of Colorado personal income or (ii) 106% of the total General Fund appropriations for the previous fiscal year. This restriction does not apply to any General Fund appropriations which are required as a result of a new federal law, a final state or federal court order or moneys derived from the increase in the rate or amount of any tax or fee approved by a majority of the registered electors of the State voting at any general election. In addition, the limit on the level of General Fund appropriations may be exceeded for a given fiscal year upon the declaration of a State fiscal emergency by the State General Assembly.

The 1991 fiscal year end fund balance was \$16.3 million, which was \$62.8 million below the 3% Unappropriated Reserve requirement. As of the end of the 1992 fiscal year, the fund balance was \$133.3 million, which was \$49.1 million over the 3% Unappropriated Reserve requirement. Based on June 20, 1993 estimates, the 1993 fiscal year ending fund balance is expected to be \$281.8 million, or \$189.7 million over the 3% required Unappropriated Reserve.

On November 3, 1992, voters in Colorado approved a constitutional amendment (the "Amendment") which, in general became effective December 31, 1992, and which could restrict the ability of the State and local governments to increase revenues and impose taxes. The Amendment applies to the State and all local governments, including home rule entities ("Districts"). Enterprises, defined as government-owned businesses authorized to issue revenue bonds and receiving under 10% of annual revenue in grants from all Colorado state and local governments combined, are excluded from the provisions of the Amendment.

The provisions of the Amendment are unclear and would probably require judicial interpretation. Among other provisions, beginning November 4, 1992, the Amendment requires voter approval prior to tax increases, creation of debt, or mill levy or valuation for assessment ratio increases. The Amendment also limits increases in government spending and property tax revenues to specified percentages. The Amendment requires that District property tax revenues yield no more than the prior year's revenues adjusted for inflation, voter approved changes and (except with regard to school districts) local growth in property values according to a formula set forth in the Amendment. School districts are allowed to adjust tax levies for changes in student enrollment. Pursuant to the Amendment, local government spending is to be limited by the same formula as the limitation for property tax revenues. The Amendment limits increases in expenditures from the State general fund and program revenues (cash funds) to the growth in inflation plus the percentage change in State population in the prior calendar year. The basis for spending and revenue limits for fiscal year 1994 and later years will be the prior fiscal year's spending and property taxes collected in the prior calendar year. Debt service changes, reductions and voter-approved revenue changes are excluded from the calculation bases. The Amendment would also prohibit new or increased real property transfer tax rates, new State real property taxes and local District income taxes.

According to the Colorado Economic Perspective, Fourth Quarter, FY 1992-93, June 20, 1993 (the "Economic Report"), inflation for 1992 was 3.7% and population grew at the rate of 2.7% in Colorado. Accordingly, under the Amendment, increases in State expenditures during the 1994 fiscal year will be limited to 6.4% over expenditures during the 1993 fiscal year. The 1993 fiscal year is the base year for calculating the limitation for the 1994 fiscal year. For the 1993 fiscal year, the Office of State Planning and Budgeting estimates that general fund revenues will total \$3,341.7 million and that program revenues (cash funds) will total \$1,753.4 million, or total estimated base revenues of \$5,095.1 million. Expenditures for the 1994 fiscal year, therefore, cannot exceed \$5,421.2 million. However, the 1994 fiscal year general fund and program revenues (cash funds) are projected to be only \$5,220.4 million, or \$200.8 million less than expenditures allowed under the spending limitation.

There is also a statutory restriction on the amount of annual increases in taxes that the various taxing jurisdictions in Colorado can levy without electoral approval. This restriction does not apply to taxes levied to pay general obligation debt.

As the State experienced revenue shortfalls in the mid-1980s, it adopted various measures, including impoundment of funds by the Governor, reduction of appropriations by the General Assembly, a temporary increase in the sales tax, deferral of certain tax reductions and inter-fund borrowings. On a GAAP basis, the State had unrestricted General Fund balances at June 30 of approximately \$100.3 million in fiscal year 1988, \$134.8 million in fiscal year 1989, \$116.6 million in fiscal year 1990, \$16.3 million in fiscal year 1991 and \$133.3 million in fiscal year 1992. The fiscal year 1993 unrestricted general fund is currently estimated to be \$281.8 million.

For fiscal year 1992, the following tax categories generated the following respective revenue percentages of the State's \$2,995.8 million total gross receipts: individual income taxes represented 53.7% of gross fiscal year 1992 receipts; excise taxes represented 33.4% of gross fiscal year 1992 receipts; and corporate income taxes represented 3.7% of gross fiscal year 1992 receipts. The final budget for fiscal year 1993 projects general fund revenues of approximately \$3,341.7 million and appropriations of approximately \$3,046.7 million. The percentages of general fund revenue generated by type of tax for fiscal year 1993 are not expected to be significantly different from fiscal year 1992 percentages.

Under its constitution, the State of Colorado is not permitted to issue general obligation bonds secured by the full faith and credit of the State. However, certain agencies and instrumentalities of the State are authorized to

issue bonds secured by revenues from specific projects and activities. The State enters into certain lease transactions which are subject to annual renewal at the option of the State. In addition, the State is authorized to issue short-term revenue anticipation notes. Local governmental units in the State are also authorized to incur indebtedness. The major source of financing for such local government indebtedness is an ad valorem property tax. In addition, in order to finance public projects, local governments in the State can issue revenue bonds payable from the revenues of a utility or enterprise or from the proceeds of an excise tax, or assessment bonds payable from special assessments. Colorado local governments can also finance public projects through leases which are subject to annual appropriation at the option of the local government. Local governments in Colorado also issue tax anticipation notes. The Amendment requires prior voter approval for the creation of any multiple fiscal year debt or other financial obligation whatsoever, except for refundings at a lower rate or obligations of an enterprise.

Based on data published by the State of Colorado, Office of State Planning and Budgeting as presented in the Economic Report, over 50% of non-agricultural employment in Colorado in 1992 was concentrated in the retail and wholesale trade and service sectors, reflecting the importance of tourism to the State's economy and of Denver as a regional economic and transportation hub. The government and manufacturing sectors followed as the fourth and fifth largest employment sectors in the State, representing approximately 18.3% and 11.5%, respectively, of non-agricultural employment in the State in 1992.

According to the Economic Report, during the first quarter of 1993, 45,900 net new jobs were generated in the Colorado economy, an increase of 24.4% over the first quarter of 1992. However, the unemployment rate rose from an average of 5.5% during the first quarter of 1992 to 5.8% during the first quarter of 1993. Total retail sales increased by 9.8% during the first quarter of 1993 as compared to the same period in 1992.

Personal income rose 6.6% in Colorado during 1992 and 5.5% in 1991. In 1992, Colorado was the twelfth fastest growing state in terms of personal income growth. However, because of heavy migration into the state and a large increase in low-paying retail sector jobs, per capita personal income in Colorado increased by only 3.8% in 1992, 0.1% below the increase in per capita personal income for the nation as a whole.

Economic conditions in the State may have continuing effects on other governmental units within the State (including issuers of the Bonds in the Colorado Trust), which, to varying degrees, have also experienced reduced revenues as a result of recessionary conditions and other factors.

At the time of the closing for each Colorado Trust, Special Counsel to the Fund for Colorado tax matters rendered an opinion under then existing Colorado income tax law applicable to taxpayers whose income is subject to Colorado income taxation substantially to the effect that:

Because Colorado income tax law is based upon the Federal law, the Colorado Trust is not an association taxable as a corporation for purposes of Colorado income taxation.

With respect to Colorado Unitholders, in view of the relationship between Federal and Colorado tax computations described above:

Each Colorado Unitholder will be treated as owning a pro rata share of each asset of the Colorado Trust for Colorado income tax purposes in the proportion that the number of Units of such Trust held by the Unitholder bears to the total number of outstanding Units of the Colorado Trust, and the income of the Colorado Trust will therefore be treated as the income of each Colorado Unitholder under Colorado law in the proportion described;

Interest on Bonds that would not be includable in income for Colorado income tax purposes when paid directly to a Colorado Unitholder will be exempt from Colorado income taxation when received by the Colorado Trust and attributed to such Colorado Unitholder and when distributed to such Colorado Unitholder;

Any proceeds paid under an insurance policy or policies issued to the Colorado Trust with respect to the Bonds in the Colorado Trust which represent maturing interest on defaulted obligations held by the Trustee will be excludable from Colorado adjusted gross income if, and to the same extent as, such interest would have been so excludable if paid in the normal course by the issuer of the defaulted obligations;

Any proceeds paid under individual policies obtained by issuers of Bonds in the Colorado Trust which represent maturing interest on defaulted obligations held by the Trustee will not be includable in income for Colorado income tax purposes if, and to the same extent as, such interest would have been so excludable if paid in the normal course by the issuer of the defaulted obligations;

Each Colorado Unitholder will realize taxable gain or loss when the Colorado

Trust disposes of a Bond (whether by sale, exchange, redemption, or payment at maturity) or when the Colorado Unitholder redeems or sells Units at a price that differs from original cost as adjusted for amortization of bond discount or premium and other basis adjustments (including any basis reduction that may be required to reflect a Colorado Unitholder's share of interest, if any, accruing on Bonds during the interval between the Colorado Unitholder's settlement date and the date such Bonds are delivered to the Colorado Trust, if later);

Tax cost reduction requirements relating to amortization of bond premium may, under some circumstances, result in Colorado Unitholders realizing taxable gain when their Units are sold or redeemed for an amount equal to or less than their original cost; and

If interest on indebtedness incurred or continued by a Colorado Unitholder to purchase Units in the Colorado Trust is not deductible for federal income tax purposes, it also will be non-deductible for Colorado income tax purposes.

Unitholders should be aware that all tax-exempt interest, including their share of interest on the Bonds paid to the Colorado Trust, is taken into account for purposes of determining eligibility for the Colorado Property Tax/Rent/Heat Rebate.

#### Connecticut Trusts

Investors should be aware that manufacturing was historically the most important economic activity within the State of Connecticut but, in terms of number of persons employed, manufacturing has declined in the last ten years while both trade and service-related industries have become more important, and in 1992 manufacturing accounted for only 20.1% of total non-agricultural employment in Connecticut. Defense-related business represents a relatively high proportion of the manufacturing sector; reductions in defense spending have already had a substantial adverse effect on Connecticut's economy, and the State's largest defense contractors have announced substantial planned labor force reductions scheduled to occur over the next four years. Connecticut is now in a recession, the depth and duration of which are uncertain. Moreover, while unemployment in the State as a whole has generally remained below the national level, as of May 1993, the estimated rate of unemployment in Connecticut on a seasonally adjusted basis was 7.4%, compared to 6.9% for the United States as a whole, and certain geographic areas in the State have been affected by high unemployment and poverty. The State derives over 70% of its revenues from taxes imposed by it, the most important of which have been the sales and use taxes and the corporation business tax, each of which is sensitive to changes in the level of economic activity in the State, but the Connecticut income tax on individuals, trusts, and estates enacted in 1991 is expected to supersede each of them in importance. There can be no assurance that general economic difficulties or the financial circumstances of the State or its towns and cities will not adversely affect the market value of the Bonds in the Connecticut Trust or the ability of the obligors to pay debt service on such Bonds.

The General Fund budget adopted by Connecticut for the 1986-87 fiscal year contemplated both revenues and expenditures of \$4,300,000,000. The General Fund ended the 1986-87 fiscal year with a surplus of \$365,200,000. The General Fund budget for the 1987-88 fiscal year contemplated General Fund revenues and expenditures of \$4,915,800,000. However, the General Fund ended the 1987-88 fiscal year with a deficit of \$115,600,000. The General Fund budget adopted for the 1988-89 fiscal year anticipated that General Fund expenditures of \$5,551,000,000 and certain educational expenses of \$206,700,000 not previously paid through the General Fund would be funded in part from surpluses of prior years and in part from higher tax revenues projected to result from tax laws in effect for the 1987-88 fiscal year and stricter enforcement thereof; a substantial deficit was projected during the third quarter of the 1988-89 fiscal year, but largely because of tax law changes that took effect before the end of the fiscal year, the deficit was kept to \$28,000,000. The General Fund budget adopted for the 1989-90 fiscal year anticipated expenditures of approximately \$6,224,500,000 and, by virtue of tax increase legislation enacted to take effect generally at the beginning of the fiscal year, revenues slightly exceeding such amount. However, largely because of tax revenue shortfalls, the General Fund ended the 1989-90 fiscal year with a deficit for the year of \$259,500,000, wiping out reserves for such events built up in prior years. The General Fund budget adopted for the 1990-91 fiscal year anticipated expenditures of \$6,433,000,000, but no significant new or increased taxes were enacted. Primarily because of significant declines in tax revenues and unanticipated expenditures reflective of economic adversity, the General Fund ended the 1990-91 fiscal year alone with a further deficit of \$809,000,000.

A General Fund budget for the 1991-92 fiscal year was not enacted until August 22, 1991. This budget anticipates General Fund expenditures of \$7,007,861,328 and revenues of \$7,426,390,000. Projected decreases in revenues resulting from a 25% reduction in the sales tax rate effective October 1, 1991, the repeal of the taxes on the capital gains and interest and dividend income of resident individuals for years starting after 1991, and the phase-out of the

corporation business tax surcharge over two years commencing with taxable years starting after 1991 were expected to be more than offset by a new general income tax imposed at effective rates not to exceed 4.5% on the Connecticut taxable income of resident and non-resident individuals, trusts and estates. The General Fund ended the 1991-92 Fiscal year with an operating surplus of \$110,000,000. The General Fund budget for the 1992-93 fiscal year anticipated General Fund expenditures of \$7,372,062,859 and revenues of \$7,372,210,000. The General Fund ended the 1992-93 fiscal year with an operating surplus of \$113,500,000. Balanced General Fund budgets for the biennium ending June 30, 1995, have been adopted appropriating expenditures of \$7,828,900,000 for the 1993-94 fiscal year and \$8,266,000,000 for the 1994-95 fiscal year. In addition, expenditures of Federal, State and local funds in the ten years started July 1, 1984 for repair of the State's roads and bridges now projected at \$9,500,000,000 are anticipated, the State's share of which would be financed by bonds expected to total \$3,700,000,000 and by direct payments both of which would be supported by a Special Transportation Fund first created by the General Assembly for the 1984-85 fiscal year.

To fund operating cash requirements, prior to the 1991-92 fiscal year the State borrowed up to \$750,000,000 pursuant to authorization to issue commercial paper and on July 29, 1991, it issued \$200,000,000 of General Obligation Temporary Notes, none of which temporary borrowings are currently outstanding. To fund the cumulative General Fund deficit for the 1989-90 and 1990-91 fiscal years, the legislation enacted August 22, 1991, authorized the State Treasurer to issue Economic Recovery Notes up to the aggregate amount of such deficit, which must be payable no later than June 30, 1996; at least \$50,000,000 of such Notes, but not more than a cap amount, is to be retired each fiscal year commencing with the 1991-92 fiscal year, and any unappropriated surplus up to \$205,000,000 in the General Fund at the end of each of the three fiscal years commencing with the 1991-92 fiscal year must be applied to retire such Notes as may remain outstanding at those times. On September 25, 1991, and October 24, 1991, the State issued \$640,710,000 and \$325,002,000, respectively, of such Economic Recovery Notes, of which \$705,610,000 was outstanding as of October 1, 1993.

As a result of the State's budget problems, the ratings of its general obligation bonds were reduced by Standard & Poor's from AA+ to AA on March 29, 1990, and by Moody's from Aa1 to Aa2 on April 9, 1990. Moreover, because of these problems, on September 13, 1991, Standard & Poor's reduced its ratings of the State's general obligation bonds and certain other obligations that depend in part on the creditworthiness of the State to AA. On March 7, 1991, Moody's downgraded its ratings of the revenue bonds of four Connecticut hospitals because of the effects of the State's restrictive controlled reimbursement environment under which they have been operating.

General obligation bonds issued by Connecticut municipalities are payable primarily only from ad valorem taxes on property subject to taxation by the municipality. Certain Connecticut municipalities have experienced severe fiscal difficulties and have reported operating and accumulated deficits in recent years. The most notable of these is the City of Bridgeport, which filed a bankruptcy petition on June 7, 1991. The State opposed the petition. The United States Bankruptcy Court for the District of Connecticut has held that Bridgeport has authority to file such a petition but that its petition should be dismissed on the grounds that Bridgeport was not insolvent when the petition was filed. Regional economic difficulties, reductions in revenues, and increased expenses could lead to further fiscal problems for the State and its political subdivisions, authorities, and agencies. Difficulty in payment of debt service on borrowings could result in declines, possibly severe, in the value of their outstanding obligations and increases in their future borrowing costs.

The assets of the Connecticut Trust will consist of obligations (the "Bonds"); certain of the Bonds have been issued by or on behalf of the State of Connecticut or its political subdivisions or other public instrumentalities, state or local authorities, districts, or similar public entities created under the laws of the State of Connecticut ("Connecticut Bonds") and the balance of the Bonds have been issued by or on behalf of entities classified for the relevant purposes as territories or possessions of the United States, including one or more of Puerto Rico, Guam, or the Virgin Islands, the interest on the obligations of which Federal law would prohibit Connecticut from taxing if received directly by the Unitholders. Certain Connecticut Bonds in the Connecticut Trust were issued prior to the enactment of the Connecticut income tax on the Connecticut taxable income of individuals, trusts, and estates (the "Connecticut Income Tax"); therefore, bond counsel to the issuers of such Bonds did not opine as to the exemption of the interest on such Bonds from such tax. However, the Sponsor and special counsel to the Trusts for Connecticut tax matters believe that such interest will be so exempt. Interest on Bonds in the Connecticut Trust issued by other issuers, if any, is, in the opinion of bond counsel to such issuers, exempt from state taxation.

The Connecticut income tax was enacted in August, 1991. Generally, a Unitholder recognizes gain or loss for purposes of this tax to the same extent as he recognizes gain or loss for Federal income tax purposes. Ordinarily this would mean that gain or loss would be recognized by a Unitholder upon the



maturity, redemption, sale, or other disposition by the Connecticut Trust of a Bond held by it, or upon the redemption, sale, or other disposition of a Unit of a Connecticut Trust held by the Unitholder.

However, on June 19, 1992, Connecticut legislation was adopted that provides that gains and losses from the sale or exchange of Connecticut Bonds held as capital assets will not be taken into account for purposes of the Connecticut Income Tax for taxable years starting on or after January 1, 1992. It is not clear whether this provision would apply to gain or loss recognized by a Unitholder upon the maturity or redemption of a Connecticut Bond held by the Connecticut Trust or, to the extent attributable to Connecticut Bonds held by the Connecticut Trust, to gain or loss recognized by a Unitholder upon the redemption, sale, or other disposition of a Unit of the Connecticut Trust held by the Unitholder. Unitholders are urged to consult their own tax advisors concerning these matters.

At the time of the closing for each Connecticut Trust, Special Counsel to the Fund for Connecticut tax matters rendered an opinion under then existing Connecticut income tax law applicable to taxpayers whose income is subject to Connecticut income taxation substantially to the effect that:

The Connecticut Trust is not liable for any tax on or measured by net income imposed by the State of Connecticut.

Interest income of the Connecticut Trust from a Bond issued by or on behalf of the State of Connecticut, any political subdivision thereof, or public instrumentality, state or local authority, district, or similar public entity created under the laws of the State of Connecticut (a "Connecticut Bond"), or from a Bond issued by United States territories or possessions the interest on which Federal law would prohibit Connecticut from taxing if received directly by a Unitholder from the issuer thereof, is not taxable under the Connecticut tax on the Connecticut taxable income of individuals, trusts, and estates (the "Connecticut Income Tax"), when any such interest is received by the Connecticut Trust or distributed by it to such a Unitholder.

Insurance proceeds received by the Connecticut Trust representing maturing interest on defaulted Bonds held by the Connecticut Trust is not taxable under the Connecticut Income Tax if, and to the same extent as, such interest would not be taxable thereunder if paid directly to the Connecticut Trust by the issuer of such Bonds.

Gains and losses recognized by a Unitholder for Federal income tax purposes upon the maturity, redemption, sale, or other disposition by the Connecticut Trust of a Bond held by the Connecticut Trust or upon the redemption, sale, or other disposition of a Unit of the Connecticut Trust held by a Unitholder are taken into account as gains or losses, respectively, for purposes of the Connecticut Income Tax, except that, in the case of a Unitholder holding a Unit of the Connecticut Trust as a capital asset, such gains and losses recognized upon the sale or exchange of a Connecticut Bond held by the Connecticut Trust are excluded from gains and losses taken into account for purposes of such tax and no opinion is expressed as to the treatment for purposes of such tax of gains and losses recognized upon the maturity or redemption of a Connecticut Bond held by the Connecticut Trust or, to the extent attributable to Connecticut Bonds, of gains and losses recognized upon the redemption, sale, or other disposition by a Unitholder of a Unit of the Connecticut Trust held by him.

The portion of any interest income or capital gain of the Connecticut Trust that is allocable to a Unitholder that is subject to the Connecticut corporation business tax is includable in the gross income of such Unitholder for purposes of such tax. An interest in a Unit of the Connecticut Trust that is owned by or attributable to a Connecticut resident at the time of his death is includable in his gross estate for purposes of the Connecticut succession tax and the Connecticut estate tax.

#### Delaware Trusts

The State ended fiscal 1989 with a cumulative cash balance of \$185.4 million, more than 15% of total expenditures for the year. The Budgetary Reserve Fund was fully funded at the 5% level or \$62.5 million during the fiscal year. General Fund revenue grew by 8.9% during fiscal 1989. General fund expenditures were \$1,092.2 million in fiscal 1989, an increase of 5.1% over fiscal 1988. The increase funded additional spending in welfare programs, teacher compensation, and a salary increase for State employees.

Projected General Fund revenue of \$1,139.4 million for fiscal 1990 is 5.3% higher than fiscal 1989. This growth reflects the continuing strength of the Delaware economy, although this estimate, issued March 19, 1990, is \$18.7 million less than an estimate issued in December, 1989, reflecting a cooling of the Delaware economy and decreased franchise taxes because of mergers and acquisitions. Taken with the unencumbered balance from the previous year, \$1,324.8 million is available for expenditure in fiscal 1990. Projected General Fund expenditures of \$1,176.7 million are 9.7% greater than spending in fiscal 1989.

The State Constitution was amended in May 1980 to limit tax increases. Any tax increase or the imposition of any new tax must be passed by a three-fifths vote of each house of the General Assembly, rather than by a simple majority vote, except for tax increases to meet debt service on outstanding obligations of the State for which insufficient revenue is available when such debt service is due. The intended impact of this amendment is to make it easier to lower expenditures than to increase taxes. The amendment also provides that the State shall appropriate, prior to each fiscal year of the State, sums sufficient to meet debt service in the following fiscal year, a practice the State has always followed.

The State Constitution limits annual appropriations by majority vote of both houses of the General Assembly to 98% of estimated General Fund revenue plus the unencumbered General Fund balance from the previous fiscal year. Any appropriation exceeding this limit may be made in the event of certain emergencies with the approval of a three-fifths vote of the members of each house of the General Assembly, but no appropriation may be made exceeding 100% of estimated General Fund revenue plus the unencumbered General Fund balance from the previous fiscal year.

The State Constitution also provides that the excess of any unencumbered General Fund revenue at the end of a fiscal year must be placed in a reserve account ("Budgetary Reserve Account") within 45 days following the end of the fiscal year. The Budgetary Reserve Account is designed to provide a cushion against unanticipated deficits. The money in the Budgetary Reserve Account accumulates until the fund reaches a maximum of 5% of the General Fund estimated revenue (including tax money that may be refunded) for the ensuing fiscal year. Transfers of \$9.2 million were made to fund the Budgetary Reserve Account for fiscal 1989. Transfers are made in August based on June projections. Access to these monies is authorized with the approval of the three-fifths vote of the members of each house of the General Assembly for use only in the event of the necessity to fund an unanticipated General Fund deficit or to provide funds required as a result of the enactment of legislation reducing taxes.

There is no Constitutional debt limit of the State. The Delaware Code presently provides that the total amount of authorized bonds issued and unissued for the payment of which the full faith and credit of the State may be pledged shall not exceed 1.5 times the total gross revenue deposited in the State's General Fund for the preceding fiscal year. Applying that calculation, the current debt limit is \$1,799 million. As of May 1, 1990, the amount of general obligation debt outstanding will be \$398.4 million, and the amount of authorized, but unissued general obligation bonds was approximately \$72.0 million. Bonds or bond anticipation notes issued by the State to provide the local share of the cost of school construction are not included in the calculation of the aforesaid debt limit, no rare revenue anticipation notes of the State. There is no debt limit applicable to the issuance of revenue anticipation notes; however there has not been a State issue of revenue notes since fiscal 1977 and the State does not plan to issue revenue notes in fiscal 1990.

Under Delaware Code, the authorization of general obligation debt of the State is limited in any State fiscal year to an amount equal to (a) 75% of the principal retirement of general obligations debt of the State in the prior State fiscal year plus (b) the amount of previously authorized and unissued general obligation debt and/or guaranteed debt the authorization for which is repealed in such fiscal year. This law can be supplemented, amended or repealed by subsequently enacted legislation.

Since the employment impact of the Financial Center Development Act was initially felt in 1982, the Delaware unemployment rate has been below the national and regional average. For calendar 1989, Delaware unemployment was 3.5% compared to 4.4% in the region and 5.3% in the United States. Delaware per capita personal income has been above the national level since 1980. For 1987, the latest year for which figures are available, Delaware per capita personal income was 106% of the national average.

General obligation debt of Delaware is rated AA by Moody's and AA+ by Standard and Poor's.

There is no pending litigation attacking the constitutionality of any Delaware revenue source or the method of collection from that source.

At the time of the closing for each Delaware Trust, Special Counsel to each Delaware Trust for Delaware tax matters rendered an opinion under then existing Delaware income tax law applicable to taxpayers whose income is subject to Delaware income taxation substantially to the effect that:

Distributions of interest income to Unitholders that would not be taxable if received directly by a Delaware resident are not subject to personal income tax under the Delaware personal income tax imposed by 30 Del. C. et seq.;

Distributions of interest income to Unitholders which are estates or trusts



that would not be taxable if received directly by a Delaware resident estate or trust are not subject to the personal income tax imposed by 30 Del. C. et seq.;

Distributions of interest income to Unitholders which are corporations that would not be taxable for Delaware income tax purposes if received directly by a corporation will not be subject to the Delaware corporate income tax imposed by 30 Del. C. 1 et seq.;

To the extent that any gain or loss from the sale of obligations held by the Fund or from the sale of a Unit by a Unitholder is includable or deductible in the calculation of a resident individual's, estate's or trust's adjusted gross income for federal income tax purposes, any such gain or loss will be includable or deductible in the calculation of taxable income for the purposes of Delaware resident personal income taxes;

To the extent that any gain or loss from the sale of obligations held by the Fund or from the sale of a Unit by a Unitholder is includable or deductible in the calculation of taxable income for purposes of federal income tax imposed upon a corporation, such gain or loss shall not be includable or deductible in the calculation of taxable income for purposes of the Delaware corporate income tax since gains or losses from the sale or other disposition of securities issued by the State of Delaware or political subdivisions thereof are not included in computing the taxable income of a corporation for Delaware corporate income tax purposes.

Any proceeds paid under insurance policies issued to the Trustee or obtained by issuers or underwriters of the Bonds, the Sponsor, or others which represent interest on defaulted obligations held by the Trustee will be excludable from Delaware gross income for individuals, trusts and estates, or corporations, if, and to the same extent as, such proceeds would have been so excludable from federal income taxation;

Interest income received by a Unitholder is not exempt from the franchise tax imposed on banking organizations under 5 Del. C. et seq. and the franchise tax imposed on building and loan associates imposed under 5 Del. C. et seq.; and

The Units are not exempt from Delaware inheritance, estate and gift tax.

#### Florida Trusts

Florida's economy has in the past been highly dependent on the construction industry and construction related manufacturing. This dependency has declined in recent years and continues to do so as a result of continued diversification of the State's economy. For example, in 1980 total contract construction employment as a share of total non-farm employment was just over seven percent and in 1990 the share had edged downward to six percent. This trend is expected to continue as Florida's economy continues to diversify. Florida, nevertheless, has a dynamic construction industry with single and multi-family housing starts accounting for 9.48% of total U.S. housing starts in 1991 while the State's population is 5.3% of the U.S. total population. Florida's housing starts since 1980 have represented an average of 11.5% of the U.S.'s total annual starts, and except for the recession years 1980-82, and the recession beginning in 1990, starts have exceeded 160,000 a year.

A driving force behind the State's construction industry has been the State's rapid rate of population growth. Although Florida currently is the fourth most populous state, its annual population growth is now projected to decline as the number of people moving into the State is expected to hover near the mid 200,000 range annually well into the 1990s. This population trend should provide plenty of fuel for business and home builders to keep construction activity lively in Florida for some time to come. However, other factors do influence the level of construction in the State. For example, Federal tax reform in 1986 and other changes to the Federal income tax code have eliminated tax deductions for owners of two or more residential real estate properties and have lengthened depreciation schedules on investment and commercial properties. Economic growth and existing supplies of commercial buildings and homes also contribute to the level of construction activity in the State.

Since 1980, the State's job creation rate is well over twice the rate for the nation as a whole, and its growth rate in new non-agricultural jobs is the fastest of the 11 most populous states and second only to California in the absolute number of new jobs created. Contributing to the State's rapid rate of growth in employment and income is international trade. Since 1980, the State's unemployment rate has generally been below that of the U.S. Only in the last two years has the State's unemployment rate moved ahead of the national average. According to the U.S. Department of Commerce, the Florida Department of Labor and Employment Security, and the Florida Consensus Economic Estimating Conference (together the "Organization"), the State's unemployment rate was 5.9% during 1990. As of April 1992, the Organization forecasts that when final numbers are in, the unemployment rate for 1991 will be 7.3% and estimates that it will be 8.1% for 1992. The State's non-farm employment is expected to decline 1.5% in 1991-92 and rise 1.8% in 1992-93,

mirroring the path of employment growth nationally. The State's two largest and fastest growing private employment categories are the service and trade sectors. Together, they account for more than 50% of the total non-farm employment growth between 1991-92 and 1992-93. Employment in these sectors is expected to decline 3.6% for trade and growth and 1.5% for services in 1991-92 and are expected to grow 0.7% and 3.7% in 1992-93, respectively. The service sector has overtaken the trade sector and is now the State's largest employment category.

Tourism is one of Florida's most important industries. Approximately 39.3 million tourists visited the State in 1991, as reported by the Florida Department of Commerce. In terms of business activities and state tax revenues, tourists in Florida in 1991 represented an estimated 4.4 million additional residents. Visitors to the State tend to arrive equally by air and car. The State's tourism industry over the years has become more sophisticated, attracting visitors year-round and, to a degree, reducing its seasonality. Tourist arrivals should be slightly negatively impacted as a result of Hurricane Andrew, but should recover and approximate in 1993-94 the number expected prior to the storm. When the final numbers are in, it is expected that by the end of the State's current fiscal year, 41.9 million domestic and international tourists will have visited the State, up 7.8% from the 39 million tourists that visited Florida in 1991-92. In 1993-94, tourist arrivals should approximate 43.2 million.

The State's per capita personal income in 1990 of \$18,539 was slightly below the national average of \$18,696 and significantly ahead of that for the southeast United States, which was \$16,514. Growth in real personal income in the State is expected to follow a course similar to that of the nation, growing at 0.3% in 1991-92 and 2.7% in 1992-93. Between 1990-91 and 1992-93, real personal income per capita in the State is expected to average 0.5% less than the 1990-91 level.

Compared to other states, Florida has a proportionately greater retirement age population which comprises 18.3% (as of April 1, 1991) of the State's population and is forecast to grow at an average annual rate of over 1.96% through the 1990s. Thus, property income (dividends, interest, and rent) and transfer payments (Social Security and pension benefits, among other sources of income) are relatively more important sources of income. For example, Florida's total wages and salaries and other labor income in 1990 was 54.9% of total income, while a similar figure for the nation for 1990 was 64.8%. Transfer payments are typically less sensitive to the business cycle than employment income and, therefore, act as stabilizing forces in weak economic periods. While many of the U.S.'s senior citizens choose the State as their place of retirement, the State is also recognized as attracting a significant number of working age people. Since 1980, the prime working age population (18-44) has grown at an average annual rate of 3.6%.

In fiscal year 1991-92, approximately 64% of the State's total direct revenue to its three operating funds will be derived from State taxes, with federal grants and other special revenue accounting for the balance. State sales and use tax, corporate income tax, and beverage tax amounted to 68%, 7% and 5%, respectively, of total receipts by the General Revenue Fund during fiscal 1991-92. In that same year, expenditures for education, health and welfare, and public safety amounted to 53%, 30% and 13.3%, respectively, of total expenditures from the General Revenue Fund.

Hurricane Andrew left some parts of south Florida devastated. Post-Hurricane Andrew clean up and rebuilding have changed the outlook for the State's economy. Single and multi-family housing starts in 1992-93 are projected to reach a combined level of 116,800, and to increase to 148,100 in 1993-94. Lingering recessionary effects on consumers and tight credit are two of the reasons for relatively slow core construction activity, as well as lingering effects from the 1986 tax reform legislation discussed above. However, construction is one of the sectors most severely affected by Hurricane Andrew. The construction figures above include, over the two year period, more than 20,000 additional housing starts as a result of destruction by Hurricane Andrew. Total construction expenditures are forecasted to increase 11.1% this year and increase 23.7% next year.

The State Constitution and statutes mandate that the State budget, as a whole, and each separate fund within the State budget, be kept in balance from currently available revenues each fiscal year. If the Governor or Comptroller believes a deficit will occur in any State fund, by statute, he must certify his opinion to the Administrative Commission, which then is authorized to reduce all State agency budgets and releases by a sufficient amount to prevent a deficit in any fund. Additionally, the State Constitution prohibits issuance of State obligations to fund State operations.

Estimated fiscal year 1991-92 General Revenue plus Working Capital funds available total \$11,228.1 million. Compared to 1991-92 Estimated General Revenues of \$11,138.6 million, the State was left with unencumbered reserves of \$89.5 million at the end of its fiscal year. Estimated fiscal year 1992-93 General Revenue plus Working Capital funds available total \$11,980.1 million, a 6.7% increase over 1991-1992. The \$11,859.2 million in combined Estimated

Revenues and revenue generating measures represents an increase of 9.5% over the previous year's Estimated Revenues. In a June 1992 Special Session of the State Legislature, the Legislature passed a number of tax rate and base increases to raise an additional \$378.5 million in the State's 1992-93 fiscal year. With effective General Revenue appropriations at \$11,861.9 million, unencumbered reserves at the end of the fiscal year are estimated at \$118.2 million. Current estimates make it likely that this figure will increase when revenue collections for 1991-92 are finalized.

The State's sales and use tax (6%) currently accounts for the State's single largest source of tax receipts. Slightly less than 10% of the State's sales and use tax is designated for local governments and is distributed to the respective counties in which collected for such use by such counties and the municipalities therein. In addition to this distribution, local governments may (by referendum) assess a 0.5% or a 1.0% discretionary sales tax within their county. Proceeds from this local option sales tax are earmarked for funding local infrastructure programs and acquiring land for public recreation or conservation or protection of natural resources as provided under Florida law. Certain charter counties have other taxing powers in addition, and non-consolidated counties with a population in excess of 800,000 may levy a local option sales tax to fund indigent health care. It alone cannot exceed 0.5% and when combined with the infrastructure surtax cannot exceed 1.0%. For the fiscal year ended June 30, 1992, sales and use tax receipts (exclusive of the tax on gasoline and special fuels) totalled \$8,375.5 million, an increase of 2.7% over fiscal year 1990-91.

The State imposes an alcoholic beverage wholesale tax (excise tax) on beer, wine, and liquor. This tax is one of the State's major tax sources, with revenues totalling \$435.2 million in fiscal year ending June 30, 1992. Alcoholic beverage tax receipts declined 1.0% over the previous year. The revenues collected from this tax are deposited into the State's General Revenue Fund.

The second largest source of State tax receipts is the tax on motor fuels. However, these revenues are almost entirely dedicated trust funds for specific purposes and are not included in the State's General Revenue Fund.

The State imposes a corporate income tax. All receipts of the corporate income tax are credited to the General Revenue Fund. For the fiscal year ended June 30, 1992, receipts from this source were \$801.3 million, an increase of 14.2% from fiscal year 1990-91.

The State also imposes a stamp tax on deeds and other documents relating to realty, corporate shares, bonds, certificates of indebtedness, promissory notes, wage assignments, and retail charge accounts. The documentary stamp tax collections totaled \$472.4 million during fiscal year 1991-92, a 0.5% increase from the previous fiscal year. For the fiscal year 1990-91, 76.21% of the documentary stamp tax revenues was deposited to the General Revenue Fund. Beginning in fiscal year 1992-93, 71.29% of these taxes are to be deposited to the General Revenue Fund.

On January 12, 1988, the State began its own lottery. State law requires that lottery revenues be distributed 50% to the public in prizes, 38% for use in enhancing education, and the balance, 12.0% for costs of administering the lottery. Fiscal year 1991-92 lottery ticket sales totalled \$2.19 billion, providing education with \$835.4 million.

The State's severance tax applies to oil, gas, and sulphur production, as well as the severance of phosphate rock and other solid minerals. Total collections from severance taxes total \$67.2 million during fiscal year 1991-92, down 6.9% from the previous year. Beginning in fiscal year 1989-90, 60.0% of this amount was transferred to the General Revenue Fund. The 60.0% allocation is expected to continue.

At the end of fiscal 1992, approximately \$4.52 billion in principal amount of debt secured by the full faith and credit of the State was outstanding. In addition, since July 1, 1992, the State issued about \$274 million in principal amount of full faith and credit bonds.

The State Constitution and statutes mandate that the State budget, as a whole, and each separate fund within the State budget, be kept in balance from currently available revenues each fiscal year. If the Governor or Comptroller believe a deficit will occur in any State fund, by statute, he must certify his opinion to the Administrative Commission, which then is authorized to reduce all State agency budgets and releases by a sufficient amount to prevent a deficit in any fund. Additionally, the State Constitution prohibits issuance of State obligations to fund State operations.

Currently under litigation are several issues relating to State actions or State taxes that put at risk substantial amounts of General Revenue Fund monies. Accordingly, there is no assurance that any of such matters, individually or in the aggregate, will not have a material adverse affect on Florida's financial position.

In the wake of the U.S. Supreme Court decision holding that a Hawaii law unfairly discriminated against out-of-state liquor producers, suits have been filed in the State's courts contesting a similar State law (in effect prior to 1985) that seek \$384 million in tax refunds. A trial court, in a ruling that was subsequently upheld by the State's Supreme Court, found the State law in question to be unconstitutional but made its ruling operate prospectively, thereby denying any tax refunds. The issue of whether the unconstitutionality of the tax should be applied retroactively was recently decided by the United States Supreme Court. The Supreme Court found in favor of the taxpayers. On remand from the U.S. Supreme Court, the Florida Supreme Court, on January 15, 1991, mandated further proceedings to fashion a "clear and certain remedy" consistent with constitutional restrictions and the opinion of the U.S. Supreme Court. The Florida Department of Revenue has proposed to the Florida Supreme Court that the Department be allowed to collect back tax from those who received a tax preference under the prior law. If the Department's proposal is rejected and tax refunds are ordered to all potential claimants, a liability of approximately \$298 million could result. The case is now before the Florida Circuit Court, Second Judicial District. That court will hear the affected parties' response to the Department's proposed collection of the tax at the higher rate charged to out-of-staters.

Florida law provides preferential tax treatment to insurers who maintain a home office in the State. Certain insurers challenged the constitutionality of this tax preference and sought a refund of taxes paid. Recently, the State Supreme Court ruled in favor of the State. Similar issues have been raised in other cases where insurers have challenged taxes imposed on premiums received for certain motor vehicle service agreements. These four cases and pending refund claims total about \$200 million.

Florida maintains a bond rating of Aa and AA from Moody's Investors Service and Standard & Poor's Corporation, respectively, on the majority of its general obligation bonds, although the rating of a particular series of revenue bonds relates primarily to the project, facility, or other revenue sources from which such series derives funds for repayment. While these ratings and some of the information presented above indicate that Florida is in satisfactory economic health, there can be no assurance that there will not be a decline in economic conditions or that particular Municipal Obligations purchased by the Fund will not be adversely affected by any such changes.

The sources for the information above include official statements and financial statements of the State of Florida. While the Sponsor has not independently verified this information, the Sponsor has no reason to believe that the information is not correct in all material respects.

At the time of the closing for each Florida Trust, Chapman and Cutler, Counsel to each Florida Trust for Florida tax matters, rendered an opinion under then existing Florida income tax law applicable to taxpayers whose income is subject to Florida income taxation substantially to the effect that:

For Florida state income tax purposes, the Florida Trust will not be subject to the Florida income tax imposed by Chapter 220, Florida Statutes. In addition, Florida does not impose any income taxes at the local level.

Because Florida does not impose an income tax on individuals, non-corporate Unitholders residing in Florida will not be subject to any Florida income taxation on income realized by the Florida Trust. Any amounts paid to the Florida Trust or to non-corporate Unitholders residing in Florida under an insurance policy issued to the Florida Trust or the Sponsor which represent maturing interest on defaulted obligations held by the Trustee will not be subject to the Florida income tax imposed by Chapter 220, Florida Statutes.

Corporate Unitholders with commercial domiciles in Florida will be subject to Florida income or franchise taxation on income realized by the Florida Trust and on payments of interest pursuant to any insurance policy. Other corporate Unitholders will be subject to Florida income or franchise taxation on income realized by the Florida Trust (or on payments of interest pursuant to any insurance policy) only to the extent that the income realized does not constitute "non-business income" as defined by Chapter 220.

Units will be subject to Florida estate tax only if held by Florida residents. However, the Florida estate tax is limited to the amount of the credit for state death taxes provided for in Section 2011 of the Internal Revenue Code.

Neither the Bonds nor the Units will be subject to the Florida ad valorem property tax, the Florida intangible personal property tax or Florida sales or use tax.

#### Georgia Trusts

Georgia ended its 1992 fiscal year on June 30, 1992 with four straight months of strong revenue collections, enabling the State to avoid spending cuts or worker layoffs. Georgia's revenues in June 1992 were 6.3% above those in June 1991. This performance followed three previous months with revenue collections of more than 6% over the 1991 period. With final figures in for the 1992

fiscal year, Georgia fell only \$10 million, or 0.1%, short of revenue expected to cover 1992 expenditures. This difference was made up from money allocated for but not used by State agencies. The Governor plans to reduce the budget for fiscal 1993 by \$75 million, to \$8.10 billion, with the cuts based on a new revenue estimate for fiscal 1994. These reductions combined with \$44 million collected from a tax-annuity program would give the state a surplus of about \$120 million for fiscal 1993.

The Georgia economy has performed relatively well during recent years and generally has expanded at a rate greater than the national average during that period. However, growth in 1988 and 1989 through 1992 has slowed somewhat and was modest compared to the robust pace of the early 1980s. Georgia's leading economic indicators currently suggest that the rate of growth of the Georgia economy will continue at the pace of 1988 and 1989 and more closely match the national economy. According to November 1992 figures, the seasonably adjusted unemployment rate in Georgia is 6.4%. Although many areas of the economy are expected to continue to perform strongly, some areas such as the primary metals, carpet and apparel industries are still experiencing periods of weakness, and others, such as construction and construction-related manufacturing activities (e.g., lumber, furniture and stone/clay products), currently show signs of weakening. In addition, aircraft manufacturers located within the State are in a tenuous position due to reductions in the Federal Defense budget. Presently, Georgia continues to lead the nation in the production of pulp, pulpwood and paper. Other industries show potential for great expansion, but policy considerations, tax reform laws, foreign competition, and other factors may render these industries less productive. Since Bonds in the Georgia Trust (other than general obligation bonds issued by the state) are payable from revenue derived from a specific source or authority, the impact of a pronounced decline in the national economy or difficulties in significant industries within the state could result in a decrease in the amount of revenues realized from such source or by such authority and thus adversely affect the ability of the respective issuers of the Bonds in the Georgia Trust to pay the debt service requirements on the Bonds. Similarly, such adverse economic developments could result in a decrease in tax revenues realized by the State and thus could adversely affect the ability of the state to pay the debt service requirements of any Georgia general obligation bonds in the Georgia Trust.

Currently Moody's rates Georgia general obligation bonds Aaa and Standard & Poor's rates such bonds AA+.

Several lawsuits have been filed against the State asserting that the decision in Davis v. Michigan Department of Treasury, 489 U.S. 803 (1989), invalidates the State's tax treatment of Federal Retirement Benefits for years prior to 1989. Under the State's applicable 3 year statute of limitation the maximum potential liability under these suits calculated to April 1, 1992 would appear to be no greater than 128 million dollars. The plaintiffs in these suits, however, have requested refunds for a period from 1980 which could result in a maximum potential liability in the range of 591 million dollars. Any such liability would be predicated on a holding by a State of Georgia court or the United States Supreme Court that the Davis decision is applicable to the State's prior method of taxing Federal Retirement Benefits, that the Davis decision is to be given a retroactive effect, i.e., that the decision affects prior tax years and that a refund remedy is appropriate. A trial court decision in Georgia's "test case" has held that no refunds are due; the Georgia Supreme Court has the case under consideration. In this "test case" the plaintiff has dropped his claims for 1980-1984 refunds.

At the time of the closing for each Georgia Trust, Special Counsel to the Fund for Georgia tax matters rendered an opinion under then existing Georgia income tax law applicable to taxpayers whose income is subject to Georgia income taxation substantially to the effect that:

For Georgia income tax purposes, the Georgia Trust is not an association taxable as a corporation, and the income of the Georgia Trust will be treated as the income of the Unitholders. Interest on the Georgia Bonds which is exempt from Georgia income tax when received by the Georgia Trust, and which would be exempt from Georgia income tax if received directly by a Unitholder, will retain its status as tax-exempt interest when distributed by the Georgia Trust and received by the Unitholders.

If the Trustee disposes of a Georgia Bond (whether by sale, exchange, payment on maturity, retirement or otherwise) or if a Unitholder redeems or sells his Unit, the Unitholder will recognize gain or loss for Georgia income tax purposes to the same extent that gain or loss would be recognized for federal income tax purposes (except in the case of Georgia Bonds issued before March 11, 1987 issued with original issue discount owned by the Georgia Trust in which case gain or loss for Georgia income tax purposes would be determined by accruing said original issue discount on a ratable basis.) Due to the amortization of bond premium and other basis adjustments required by the Internal Revenue Code, a Unitholder, under some circumstances, may realize taxable gain when his or her Units are sold or redeemed for an amount equal to their original cost.

Because obligations or evidences of debt of Georgia, its political subdivisions and public institutions and bonds issued by the Government of Puerto Rico are exempt from the Georgia intangible personal property tax, the Georgia Trust will not be subject to such tax as the result of holding such obligations, evidences of debt or bonds. Although there currently is no published administrative interpretation or opinion of the Attorney General of Georgia dealing with the status of bonds issued by a political subdivision of Puerto Rico, we have in the past been advised orally by representatives of the Georgia Department of Revenue that such bonds would also be considered exempt from such tax. Based on that advice, and in the absence of a published administrative interpretation to the contrary, we are of the opinion that the Georgia Trust would not be subject to such tax as the result of holding bonds issued by a political subdivision of Puerto Rico.

Amounts paid under an insurance policy or policies issued to the Georgia Trust, if any, with respect to the Georgia Bonds in the Georgia Trust which represent maturing interest on defaulted obligations held by the Trustee will be exempt from State income taxes if, and to the extent as, such interest would have been so exempt if paid by the issuer of the defaulted obligations.

We express no opinion regarding whether a Unitholder's ownership of an interest in the Georgia Trust is subject to the Georgia intangible personal property tax. Although the application of the Georgia intangible property tax to the ownership of the Units by the Unitholders is not clear, representatives of the Georgia Department of Revenue have in the past advised us orally that, for purposes of the intangible property tax, the Department considers a Unitholder's ownership of an interest in the Georgia Trust as a whole to be taxable intangible property separate from any ownership interest in the underlying tax-exempt Bonds.

Neither the Georgia Bonds nor the Units will be subject to Georgia sales or use tax.

#### Kansas Trusts

Since the Kansas Trust will invest substantially all of its assets in Kansas municipal securities, the Kansas Trust is susceptible to political and economic factors affecting issuers of Kansas municipal securities. As of 1991, 2,494,566 people lived in Kansas, representing a 0.69% increase in population since the 1990 census. Based on these numbers, Kansas ranked thirty-second in the nation in population size. According to the Kansas Department of Commerce, in 1991 Kansas ranked twenty-first in the nation in terms of per capita income. Historically, agriculture and mining constituted the principal industries in Kansas. Since the 1950s, however, manufacturing, governmental services and the services industry have steadily grown, and as of 1993 approximately 15.7% of Kansas workers were in the manufacturing sector, 20.8% in the government sector and 23.3% in the services sector (not including transportation, public utilities, trade, finance, insurance, and real estate), while the farming and mining sectors combined for approximately 5.0% of the work force. The 1991 unemployment rate was 4.4%, and the seasonally adjusted rate for December 1992 was 4.2%. By constitutional mandate, Kansas must operate within a balanced budget and public debt may only be incurred for extraordinary purposes and then only to a maximum of \$1 million. As of November 12, 1992, Kansas had no general obligation bonds outstanding.

At the time of the closing for each Kansas Trust, Special Counsel to each Kansas Trust for Kansas tax matters, rendered an opinion under then existing Kansas income tax law applicable to taxpayers whose income is subject to Kansas income taxation substantially to the effect that:

The Trust is not an association taxable as a corporation for Kansas income tax purposes;

Each Unitholder of the Trust will be treated as the owner of a pro rata portion of the Trust, and the income and deductions of the Trust will therefore be treated as income of the Unitholder under Kansas law;

Interest on Bonds issued after December 31, 1987 by the State of Kansas or any of its political subdivisions will be exempt from income taxation imposed on individuals, corporations and fiduciaries (other than insurance companies, banks, trust companies or savings and loan associations) however, interest on Bonds issued prior to January 1, 1988 by the State of Kansas or any of its political subdivisions will not be exempt from income taxation imposed on individuals, corporations and fiduciaries (other than insurance companies, banks, trust companies or savings and loan associations) unless the laws of the State of Kansas authorizing the issuance of such Bonds specifically exempt the interest on the Bonds from income taxation by the State of Kansas;

Interest on Bonds issued by the State of Kansas or any of its political subdivisions will be subject to the tax imposed on banks, trust companies and savings and loan associations under Article 11, Chapter 79 of the Kansas statutes;

Interest on Bonds issued by the State of Kansas or any of its political



subdivisions will be subject to the tax imposed on insurance companies under Article 40, Chapter 28 of the Kansas statutes unless the laws of the State of Kansas authorizing the issuance of such Bonds specifically exempt the interest on the Bonds from income taxation by the State of Kansas; interest on the Bonds which is exempt from Kansas income taxation when received by the Trust will continue to be exempt when distributed to a Unitholder (other than a bank, trust company or savings and loan association);

Each Unitholder of the Trust will recognize gain or loss for Kansas income tax purposes if the Trustee disposes of a Bond (whether by sale, exchange, payment on maturity, retirement or otherwise) or if the Unitholder redeems or sells Units of the Trust to the extent that such transaction results in a recognized gain or loss for federal income tax purposes;

Interest received by the Trust on the Bonds is exempt from intangibles taxation imposed by any counties, cities and townships pursuant to present Kansas law; and

No opinion is expressed regarding whether the gross earnings derived from the Units is subject to intangibles taxation imposed by any counties, cities and townships pursuant to present Kansas law.

#### Kentucky Trusts

The Commonwealth of Kentucky leads the nation in total tonnage of coal produced and ranks among the top 10 states in the value of all minerals produced. Tobacco is the dominant agricultural crop and Kentucky ranks second among the states in the total cash value of tobacco raised. The manufacturing mix in the state reflects a significant diversification. In addition to the traditional concentration of tobacco processing plants and bourbon distilleries, there is considerable durable goods production, such as automobiles, heavy machinery, consumer appliances, and office equipment. The State's parks system and the horse breeding and racing industry, symbolized by the Kentucky Derby, play an important role in an expanding tourist business in the state.

Current economic problems, including particularly the continuing high unemployment rate, have had varying effects on the differing geographic areas of the State and the political subdivisions located within such geographic areas. Although revenue obligations of the State or its political subdivisions may be payable from a specific source or project, there can be no assurance that further economic difficulties and the resulting impact on State and local governmental finances will not adversely affect the market value of the Bonds in the Kentucky Trust or the ability of the respective obligors to pay debt service of such Bonds.

Prospective investors should study with care the portfolio of Bonds in the Kentucky Trust and should consult with their investment advisors as to the merits of particular issues in the portfolio.

At the time of the closing for each Kentucky Trust, Special Counsel to each Kentucky Trust for Kentucky tax matters rendered an opinion under then existing Kentucky income tax law applicable to taxpayers whose income is subject to Kentucky income taxation substantially to the effect that:

Because Kentucky income tax law is based upon the Federal law and in explicit reliance upon the opinion of Chapman and Cutler referred to above, and in further reliance on the determination letter to us of the Revenue Cabinet of Kentucky dated May 10, 1984, it is our opinion that the application of existing Kentucky income tax law would be as follows:

Each Kentucky Unitholder will be treated as the owner of a pro rata portion of the Kentucky Trust for Kentucky income tax purposes, and the income of the Kentucky Trust will therefore be treated as the income of the Kentucky Unitholders under Kentucky law;

Interest on Bonds that would be exempt from Federal income taxation when paid directly to a Kentucky Unitholder will be exempt from Kentucky income taxation when: (i) received by the Kentucky Trust and attributed to such Kentucky Unitholder; and (ii) when distributed to such Kentucky Unitholder;

Each Kentucky Unitholder will realize taxable gain or loss when the Kentucky Trust disposes of a Bond (whether by sale, exchange, redemption or payment of maturity) or when the Kentucky Unitholder redeems or sells Units at a price that differs from original cost as adjusted for amortization or accrual, as appropriate, of bond discount or premium and other basis adjustments including any basis reduction that may be required to reflect a Kentucky Unitholder's share of interest, if any, accruing on Bonds during the interval between the Kentucky Unitholder's settlement date and the date such Bonds are delivered to the Kentucky Trust, if later);

Tax cost reduction requirements relating to amortization of bond premium may, under some circumstances, result in Kentucky Unitholders realizing taxable gain when their Units are sold or redeemed for an amount equal to or less than



their original cost;

Units of the Kentucky Trust, to the extent the same represent an ownership in obligations issued by or on behalf of the Commonwealth of Kentucky or governmental units of the Commonwealth of Kentucky, the interest on which is exempt from Federal and Kentucky income taxation will not be subject to ad valorem taxation by the Commonwealth of Kentucky or any political subdivision thereof; and

If interest on indebtedness incurred or continued by a Kentucky Unitholder to purchase Units in the Kentucky Trust is not deductible for Federal income tax purposes, it also will be nondeductible for Kentucky income tax purposes.

#### Maine

The State of Maine, which includes nearly one-half of the total land area of the six New England states, currently has a population of 1,213,000. The structure of the Maine economy is quite similar to that of the nation as a whole, except that Maine has proportionately more activity in manufacturing and tourism, and less activity in finance and services.

During the 1980s Maine's economy grew rapidly. However, due largely to an overheating of the New England construction/real estate markets in 1987-88, the New England and Maine economies were much softer in 1989 and the first portion of 1990. The last quarter of strong growth in Maine was the first quarter in 1988. The Maine Economic Growth Index, a broad measure of overall growth corrected for inflation, rose only 0.7% in 1989. The United States Economic Growth Index reflected an increase of 2.7% during the same period.

During the period 1980 through 1988 state employment increased by 23%, resulting in an unemployment rate of 3.8% in 1988. The unemployment rate for 1989 rose to 4.1%. Income growth exceeded national averages for the period 1982 through 1986, with per capita income increasing 36010, while the national average was a 28% increase. The latest information available from the Maine State Planning Office shows personal income growth remained strong for 1989, although it was weakened substantially to 79%. Adjusted for inflation, real income growth in 1989 is approximately 24% which is well below the 1988 figure of 5.3%.

The regional economic slowdown in the northeast is expected to continue for the near to intermediate term. Prospects for some of Maine's major industries are not optimistic in light of the regional slowdown. The value of Maine construction contract awards in 1989 was \$260,000,000 below the awards for calendar year 1988, off some 21%. This slowdown diminishes prospects for the wood products industry, as well as construction employment.

As indicated above, the real estate market continues to be extremely soft. Data collected by the Maine Real Estate Institute indicated a shrinkage of roughly \$230,000,000 in real estate sales volume for calendar year 1989 from the previous year. Continued unavailability of credit continues to affect this sector of the economy.

The economic slowdown has had resulting impact upon consumer spending and the retail sector. Maine's retail sales declined by 1% in 1989, although that decline is attributable in its entirety to two retail sectors suffering significant declines. The building supply sector suffered a decline of 7.6% and the auto transportation group suffered a decline of 6.5%.

The Constitution of the State of Maine provides that the Legislature shall not create any debt which exceeds \$2,000,000 except to suppress insurrection, to repel invasion or for purposes of war except when two-thirds of the Legislature and a minority of the voters authorize the issuance of debt. The Constitution also provides that tax anticipation loans must be repaid during the fiscal year of issuance. Constitutional amendments have been adopted which also allow the Legislature to authorize the issuance of bonds: to insure payments on revenue bonds of up to \$4,800,000 for local public school building projects; in the amount of up to \$4,000,000 to guarantee student loans; to insure payments on up to \$1,000,000 of mortgage loans for Indian housing; to insure payments on up to \$4,000,000 of mortgage loans or small business loans to war veterans; and to insure payments on up to \$90,000,000 of mortgage loans for industrial, manufacturing, fishing, agricultural, and recreational enterprises. This last authorization has been limited statutorily to a maximum of \$87,500,000 available for issue through the Finance Authority of Maine.

The State operates under a biennial budget which is formulated in even-numbered years and presented for approval to the Legislature in odd-numbered years. The economic strength evidenced during the 1980s enabled the State to accumulate high levels of general fund unappropriated surpluses. As of its fiscal year ended December 31, 1989, the State had an unappropriated general fund surplus of \$161,000,000. In order to balance the fiscal 1990 budget, the State will draw down on the total balance to about \$60,000,000 of general fund expenditures during 1990. Further, the State projects a continued decrease in sales tax revenues. Since proposal of its 1990-91 budget the State has reduced estimates for sales tax twice for the biennium. The estimates were

reduced by \$89,000,000 in June 1989 and \$105,000,000 in January 1990. Corresponding reductions were made in individual and corporate income tax projections. The State's revenue and expenditure package established as of the close of the most recent legislative session closed a \$210,000,000 revenue shortfall projected in January 1990 and allows for a 1% surplus at fiscal year end. As of August 1990, State revenues were 0.1% ahead of new budget estimates.

Maine's outstanding general obligations are currently rated AAA by Standard & Poor's Corporation and Aa1 by Moody's Investors Service, Inc. Maine has currently slowed its issuance of general obligation debt as a result of the State's fiscal situation. Maine has \$555,500,000 of outstanding general obligation debt and \$155,200,000 in authorized unissued debt. Nevertheless, due in large part to the State's low debt burden and rapid debt amortization, the public rating agencies do not consider debt burden a negative factor.

The Portfolio may contain obligations of the Maine Municipal Bond Bank. All Maine Municipal Bond Bank debt is secured by loan repayments of borrowing municipalities and the State's moral obligation pledge. The state of the economy in Maine could impact the ability of municipalities to pay debt service on their obligations. Maine Municipal Bond Bank debt continues to carry a AA rating from Standard & Poor's Corporation and a Aa rating from Moody's Investors Service, Inc.

The Portfolio may contain obligations issued by Regional Waste Systems, Inc., a quasi-municipal corporation organized pursuant to an interlocal agreement among approximately 20 Southern Maine communities ("RWS") or other quasi-municipal solid waste disposal facilities. RWS and other similar solid waste disposal projects operate regional solid waste disposal facilities and process the solid waste of the participating municipalities as well as the solid waste of other non-municipal users. The continued viability of such facilities is dependent, in part, upon the approach taken by the State of Maine with respect to solid waste disposal generally. Pursuant to a Public Law 1989 Chapter 585, the newly formed Maine Waste Management Agency is charged with preparation and adoption by rule of an analysis and a plan for the management, reduction and recycling of solid waste for the State of Maine. The plan to be developed by the Maine Waste Management Agency is based on the waste management priorities and recycling goals established by State law. Pursuant to State law, Maine has established minimum goals for recycling and composting requiring that a minimum of 25% of the municipal solid waste stream be recycled or composted by 1992 and 50% be recycled or composted by 1994. Although RWS may participate in the mandated recycling activities, its principal existing facility consists of a mass burn 250 ton per day furnace boiler with associated equipment for production of electric energy. Thus, the source material for the RWS' primary facility could be substantially reduced as a result of implementation of the State's recycling goals. Other mass burn solid waste disposal facilities in the State have experienced seasonal shortages in waste fuel.

Revenue bonds are issued by the Maine Health and Higher Education Facilities Authority to finance hospitals and other health care facilities. The revenues of such facilities consist, in varying but typically material amounts, of payment from insurers and third-party reimbursement programs, including Medicaid, Medicare and Blue Cross. The health care industry in Maine is becoming increasingly competitive. The utilization of new programs and modified benefits by third-party reimbursement programs and the advent of alternative health care delivery systems such as health maintenance organizations contribute to the increasingly competitive nature of the health care industry. This increase in competition could adversely impact the ability of health care facilities in Maine to satisfy their financial obligations.

Further, health care providers are subject to regulatory actions, changes in law and policy changes by agencies that administer third-party reimbursement programs and regulate the health care industry. Any such changes could adversely impact the financial condition of such facilities.

The foregoing information constitutes only a brief summary of some of the financial difficulties which may impact certain issuers of Bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers in the Maine Trust are subject. Additionally, many factors including national economic, social and environmental policies and conditions, which are not within the control of the issuers of Bonds, could affect or could have an adverse impact on the financial condition of the State and various agencies and political subdivisions located in the State. The Sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Maine Quality Trust to pay interest on or principal of the Bonds.

The assets of the Maine Trust will consist of interest-bearing obligations issued by or on behalf of the State of Maine (the "State") or counties, municipalities, authorities or political subdivisions thereof (the "Maine Bonds") or by the Commonwealth of Puerto Rico, Ouam and the United States Virgin Islands (the "Possession Bonds") (collectively, the "Bonds").

Neither the Sponsor nor its counsel have independently examined the Bonds to be deposited in and held in the Maine Quality Trust. However, although no opinion is expressed herein regarding such matters, it is assumed that: (i) the Bonds were validly issued, (ii) the interest thereon is excludible from gross income for Federal income tax purposes, (iii) interest on the Maine Bonds, if received directly by a Unitholder, would be exempt from the Maine income tax applicable to individuals, trusts and estates and corporations ("Maine Income Tax"), and (iv) interest on the Bonds will not be taken into account by individuals and corporations in computing an additional tax ("Maine Minimum Tax") or in the case of corporations, a surcharge ("Maine Corporate Income Tax Surcharge") imposed under the Maine Income Tax. The opinion set forth below does not address the taxation of persons other than full time residents of Maine.

In the opinion of Chapman and Cutler, special counsel to the Fund for Maine tax matters, under existing law as of the date of this prospectus and based upon the assumptions set forth above:

the Maine Quality Trust is not an association taxable as a corporation, thus each Unitholder of the Trust will be essentially treated as the owner of a pro rata portion of the Maine Trust and the income of such portion of the Maine Trust will be treated as the income of the Unitholder for Maine Income Tax purposes;

interest on the Bonds which is exempt from the Maine Income Tax when received by the Maine Trust, and which would be exempt from the Maine Income Tax and the Maine Minimum Tax if received directly by a Unitholder, will retain its status as exempt from the Maine Income Tax and the Maine Minimum Tax when received by the Maine Trust and distributed to the Unitholder;

to the extent that interest derived from the Maine Trust by a Unitholder with respect to the Possession Bonds is excludible from gross income for Federal income tax purposes pursuant to 48 U.S.C. § 745, 48 U.S.C. § 1423a and 48 U.S.C. § 1403, such interest will not be subject to the Maine Income Tax;

each Unitholder of the Maine Trust will recognize gain or loss for Maine Income Tax purposes if the Trustee disposes of a bond (whether by redemption, sale or otherwise) or if the Unitholder redeems or sells Units of the Maine Trust to the extent that such a transaction results in a recognized gain or loss to such Unitholder for Federal income tax purposes; and

the Maine Income Tax does not permit a deduction of interest paid or incurred on indebtedness incurred or continued to purchase or carry Units in the Maine Trust, the interest on which is exempt from the Tax.

Prospective Purchasers subject to the Maine Franchise Tax should be advised that for purposes of the Maine Franchise Tax, interest on the Bonds received by the Trust and distributed to a Unitholder subject to such tax will be added to the Unitholder's Federal taxable income and therefore will be taxable.

#### Maryland Trusts

The public indebtedness of the State of Maryland, its instrumentalities and its local governments is divided into three basic types. The State, and the counties and municipalities of the State, issue general obligation bonds for capital improvements and for various projects to the payment of which an ad valorem property tax is exclusively pledged.

Certain authorities of the State and certain local governments issue obligations payable solely from specific non-tax, enterprise fund revenues and for which the issuer has no liability and has given no moral obligation assurance. The principal of and interest on bonds issued by these bodies are payable solely from various sources, principally fees generated from use of the facilities or enterprises financed by the bonds.

The special authorities of the State and local government entities have outstanding bonds backed exclusively by revenues derived from projects and facilities financed by the bond issue. The holders of these bonds have no claim against the general credit of the State or any governmental unit for the payment of those bonds.

There is no general debt limit imposed on the State of Maryland by the State Constitution or public general laws, but a special committee created by statute annually makes an estimate of the maximum amount of new general obligation debt that the State may prudently authorize.

There can be no assurance that particular bond issues may not be adversely affected by changes in State or local economic or political conditions. Investors are, therefore, advised to study with care the Portfolio for the Maryland Trust appearing elsewhere in this Prospectus and consult their own investment advisers as to the merits of particular issues in that Portfolio.

At the time of the closing for each Maryland Trust, Special Counsel to each Maryland Trust for Maryland tax matters rendered an opinion under then existing Maryland income tax law applicable to taxpayers whose income is subject to Maryland income taxation substantially to the effect that:

For Maryland State and local income tax purposes, the Maryland Trust will not be recognized as an association taxable as a corporation, but rather as a fiduciary whose income will not be subject to Maryland State and local income taxation;

To the extent that interest derived from the Maryland Trust by a Unitholder with respect to the obligations of the State of Maryland and its political subdivisions is excludable from Federal gross income, such interest will not be subject to Maryland State or local income taxes. Interest paid to a "financial institution" will be subject to the Maryland State franchise tax on financial institutions;

In the case of taxpayers who are individuals, Maryland presently imposes an income tax on items of tax preference with reference to such items as defined in the Internal Revenue Code, as amended from time to time, for purposes of calculating the federal alternative minimum tax. Interest paid on certain private activity bonds constitutes a tax preference item for the purpose of calculating the federal alternative minimum tax. Accordingly, if the Maryland Trust holds such bonds, 50% of the interest on such bonds in excess of a threshold amount is taxable in Maryland; and

Capital gain, including gain realized by a Unitholder from the redemption, sale or other disposition of a Unit, will be included in the Maryland taxable base of Unitholders for Maryland State and local income taxation purposes. However, Maryland defines the taxable net income of individuals as Federal adjusted gross income with certain modifications. Likewise, the Maryland taxable net income of corporations is Federal taxable income with certain modifications. There is available to Maryland income taxpayers a modification which allows those taxpayers to subtract from the Maryland taxable base the gain included in Federal adjusted gross income or Federal taxable income, as the case may be, which is realized from the disposition of Securities by the Maryland Trust. Consequently, by making that modification, a Unitholder who is entitled to make the subtraction modification will not be subject to Maryland State or local income tax with respect to gain realized upon the disposition of Securities by the Maryland Trust. Profit realized by a "financial institution" from the sale or exchange of Bonds will be subject to the Maryland Franchise Tax.

These opinions relate only to the treatment of the Maryland Trust and the Units under the Maryland State and local income tax laws and Maryland franchise tax laws. Unitholders should consult tax counsel as to other Maryland tax consequences not specifically considered in these opinions. For example, no opinion is expressed as to the treatment of the Units under the Maryland inheritance and estate tax laws.

#### Massachusetts Trusts

The Massachusetts Economy. At the present time, the Massachusetts economy is experiencing a slowdown. While Massachusetts had benefitted from an annual job growth rate of approximately 2% since the early 1980s, by 1989 employment had started to decline. Nonagricultural employment declined 0.7% in fiscal 1989, 4.0% in fiscal 1990, 5.5% in fiscal 1991, 1.5% in fiscal 1992, and 0.8% in fiscal 1993. A comparison of total, nonagricultural employment in August 1992 with that in August 1993 indicates a decline of 0.4%.

From 1980 to 1989, Massachusetts' unemployment rate was significantly lower than the national average. By 1990, however, unemployment reached 6.0%, exceeding the national average for the first time since 1977. Massachusetts' unemployment rate averaged 9.0% in fiscal 1991 and 8.5% in fiscal 1992. The Massachusetts unemployment rate was 8.2% as of January 1993, and 6.8% as of July 1993.

In recent years, per capita personal income growth in Massachusetts has slowed, after several years during which it was among the highest in the nation. Between the first quarter of fiscal 1991 and the first quarter of fiscal 1992, aggregate personal income in Massachusetts increased 2.6% as compared to 4.1% for the nation as a whole. Between the second quarter of 1991 and the second quarter of 1992, aggregate personal income in Massachusetts increased 3.9% as compared to 4.7% for the nation as a whole.

The Commonwealth, while the third most densely populated state according to the 1990 census, has experienced only a modest increase in population from 1980 to 1990 at a rate equal to approximately one-half the rate of increase in the United States population as a whole. Preliminary information compiled by the Commonwealth suggests that out-migration has increased in recent years.

Massachusetts possesses a diversified economic base which includes traditional manufacturing, high technology and service industries, served by an extensive transportation system and related facilities. The Massachusetts service

sector, at approximately 33.5% of the state work force in August of 1993, is the largest sector in the Massachusetts economy. Government employment is below the national average, representing less than 14% of the Massachusetts work force. In recent years, the construction, manufacturing and trade sectors have experienced the greatest decreases in employment in Massachusetts, with more modest declines taking place in the government, finance, insurance and real estate, and service sectors. From 1990 to December of 1992, manufacturing employment in Massachusetts declined by some 12.5%, and more recently, from August 1992 to August 1993, declined by about 4.2%. At the same time, there has occurred a reversal of the dramatic growth which occurred during the 1980's in the finance, insurance and real estate sector and in the construction sector of the Massachusetts economy.

Over the next decade, Massachusetts has a very full public construction agenda which is expected not only to improve mobility, but to provide a substantial number of construction and related employment opportunities, including the six billion dollar Central Artery Tunnel project involving the construction of a third tunnel under Boston Harbor linking the MassPike and downtown Boston with Logan International Airport, and the depression into tunnels of the Central Artery that traverses the City of Boston. Federal funds are expected to cover approximately 90% of the cost of this project. The Central Artery/Tunnel project is expected to employ approximately 5,000 on-site workers and 10,000 auxiliary workers during the peak years of construction in the mid-1990s.

State Finances. In fiscal years 1987 through 1991, Commonwealth spending exceeded revenues. Spending in five major expenditure categories Medicaid, debt service, public assistance, group health insurance and transit subsidies-grew at rates well in excess of the rate of inflation for the comparable period. During the same period, the Commonwealth's tax revenues repeatedly failed to meet official forecasts. That revenue shortfall combined with steadily escalating costs contributed to serious budgetary and financial difficulties which have affected the credit standing and borrowing abilities of Massachusetts and certain of its public bodies and municipalities, and which may have contributed to higher interest rates on debt obligations issued by them.

More conservative revenue forecasting for fiscal 1992 together with significant efforts to restrain spending during fiscal 1991 and reductions in budgeted program expenditures for fiscal 1992 and fiscal 1993 have moderated these difficulties. Significant spending commitments for public education are contained in recent education reform legislation enacted in June of 1993. In July and August of 1993, the Executive Office for Administration and Finance announced a series of actions affecting state workers (including a hiring freeze, layoffs and the elimination of positions) intended to keep expected fiscal 1994 expenditures with current appropriations. Notwithstanding these actions, a continuation, or worsening, of the present slowdown and its effect on the financial condition of the Commonwealth and its public authorities and municipalities could result in a decline in the market values of, or default on existing obligations including the Bonds deposited in the Massachusetts Trust.

The foregoing information constitutes only a brief summary of some of the general factors which may impact certain issuers of Bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers of obligations held by the Massachusetts Trust are subject. Additionally, many factors including national economic, social and environmental policies and conditions, which are not within the control of the issuers of Bonds, could affect or could have an adverse impact on the financial condition of the Commonwealth and various agencies and political subdivisions located in the Commonwealth. The Sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of the Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Massachusetts Trust to pay interest on or principal of the Bonds.

At the time of the closing for each Massachusetts Trust Special Counsel to each Massachusetts Trust for Massachusetts tax matters, rendered an opinion under then existing Massachusetts income tax law applicable to taxpayers whose income is subject to Massachusetts income taxation substantially to the effect that:

For Massachusetts income tax purposes, a Massachusetts Trust will be treated as a corporate trust under Section 8 of Chapter 62 of the Massachusetts General Laws and not as a grantor trust under Section 10(e) of Chapter 62 of the Massachusetts General Laws.

A Massachusetts Trust will not be held to be engaging in business in Massachusetts within the meaning of said Section 8 and will, therefore, not be subject to Massachusetts income tax.

Massachusetts Unitholders who are subject to Massachusetts income taxation under Chapter 62 of Massachusetts General Laws will not be required to include their respective shares of the earnings of or distributions from a Massachusetts Trust in their Massachusetts gross income to the extent that

such earnings or distributions represent tax-exempt interest for federal income tax purposes received by a Massachusetts Trust on obligations issued by Massachusetts, its counties, municipalities, authorities, political subdivisions or instrumentalities, or issued by United States territories or possessions.

Any proceeds of insurance obtained by the Trustee of the Trust or by the issuer of a Bond held by a Massachusetts Trust which are paid to Massachusetts Unitholders and which represent maturing interest on defaulted obligations held by the Trustee will be excludable from Massachusetts gross income of a Massachusetts Unitholder if, and to the same extent as, such interest would have been so excludable if paid by the issuer of the defaulted Bond.

A Massachusetts Trust's capital gains and/or capital losses realized upon disposition of Bonds held by it will be includable pro rata in the federal gross income of Massachusetts Unitholders who are subject to Massachusetts income taxation under Chapter 62 of the Massachusetts General Laws, and such gains and/or losses will be included as capital gains and/or losses in the Massachusetts Unitholder's Massachusetts gross income, except where capital gain is specifically exempted from income taxation under acts authorizing issuance of said Bonds.

Gains or losses realized upon sale or redemption of Units by Massachusetts Unitholders who are subject to Massachusetts income taxation under Chapter 62 of the Massachusetts General Laws will be includable in their Massachusetts gross income.

In determining such gain or loss Massachusetts Unitholders will, to the same extent required for federal tax purposes, have to adjust their tax bases for their Units for accrued interest received, if any, on Bonds delivered to the Trustee after the Unitholders pay for their Units and for amortization of premiums, if any, on obligations held by a Massachusetts Trust.

The Units of a Massachusetts Trust are not subject to any property tax levied by Massachusetts or any political subdivision thereof, nor to any income tax levied by any such political subdivision. They are includable in the gross estate of a deceased Massachusetts Unitholder who is a resident of Massachusetts for purposes of the Massachusetts Estate Tax.

#### Michigan Trusts

Investors should be aware that the economy of the State of Michigan has, in the past, proven to be cyclical, due primarily to the fact that the leading sector of the State's economy is the manufacturing of durable goods. While the State's efforts to diversify its economy have proven successful, as reflected by the fact that the share of employment in the State in the durable goods sector has fallen from 33.1 percent in 1960 to 17.9 percent in 1990, durable goods manufacturing still represents a sizable portion of the State's economy. As a result, any substantial national economic downturn is likely to have an adverse effect on the economy of the State and on the revenues of the State and some of its local governmental units.

In May 1986, Moody's Investors Service raised the State's general obligation bond rating to "A1". In October 1989, Standard & Poor's Corporation raised its rating on the State's general obligation bonds to "AA".

The State's economy could continue to be affected by changes in the auto industry, notably consolidation and plant closings resulting from competitive pressures and over-capacity. Such actions could adversely affect State revenues and the financial impact on the local units of government in the areas in which plants are closed could be more severe.

General Motors Corporation has announced the scheduled closing of several of its plants in Michigan in 1993 and 1994. The impact these closures will have on the State's revenues and expenditures is not currently known. The impact on the financial condition of the municipalities in which the plants are located may be more severe than the impact on the State itself.

In recent years, the State has reported its financial results in accordance with generally accepted accounting principles. For each of the five fiscal years ending with the fiscal year ended September 30, 1989, the State reported positive year-end General Fund balances and positive cash balances in the combined General Fund/School Aid Fund. For the fiscal years ending September 30, 1990 and 1991, the State reported negative year-end General Fund Balances of \$310.4 million and \$169.4 million, respectively, but ended the 1992 fiscal year with its general fund in balance. In the 1993 fiscal year, the State took actions to eliminate a projected year-end general fund deficit of \$370 million, but the results of such actions are not yet known, since the state's final Financial Reports for the 1993 year have not yet been released. A positive cash balance in the combined General Fund/School Aid Fund was recorded at September 30, 1990. In the 1991 thru 1993 fiscal years, the State experienced deteriorating cash balances which have necessitated short term borrowing and the deferral of certain scheduled cash payments. The State borrowed \$900 million for cash flow purposes in the 1993 fiscal year, which



was repaid on September 30, 1993. The State's Budget Stabilization Fund was nearly depleted with a \$168 million transfer to the General Fund for the 1992 State fiscal year.

The Michigan Constitution of 1963 limits the amount of total revenues of the State raised from taxes and certain other sources to a level for each fiscal year equal to a percentage of the State's personal income for the prior calendar year. In the event that the State's total revenues exceeds the limit by 1 percent or more, the Michigan Constitution of 1963 requires that the excess be refunded to taxpayers.

On March 15, 1994, Michigan voters approved a school finance reform amendment to the State's Constitution which, among other things, increases the State sales tax rate from 4% to 6% and places a cap on property assessment increases for all property taxes. Such approval triggers the effectiveness of legislation under which, the State's income tax rate will be cut from 4.6% to 4.4%. Some property taxes will be reduced and school funding will be provided from a combination of property taxes and state revenues, some of which will be provided from other new or increased State taxes. The legislation also contains other proposals that may reduce or alter the revenues of local units of government, and tax increment bonds could be particularly affected. While the ultimate impact of the constitutional amendment and related legislation cannot yet be accurately predicted, investors should be alert to the potential effect of such measures upon the operations and revenues of Michigan local units of government.

Although all or most of the Bonds in each Michigan Trust are revenue obligations or general obligations of local governments or authorities rather than general obligations of the State of Michigan itself, there can be no assurance that any financial difficulties the State may experience will not adversely affect the market value or marketability of the Bonds or the ability of the respective obligors to pay interest on or principal of the Bonds, particularly in view of the dependency of local governments and other authorities upon State aid and reimbursement programs and, in the case of bonds issued by the State Building Authority, the dependency of the State Building Authority on the receipt of rental payments from the State to meet debt service requirements upon such bonds. In the 1991 fiscal year, the State deferred certain scheduled cash payments to municipalities, school districts, universities and community colleges. While such deferrals were made up at specified later dates, similar future deferrals could have an adverse impact on the cash position of some local governmental units. Additionally, the State reduced revenue sharing payments to municipalities below that level provided under formulas by \$10.9 million in the 1991 fiscal year and \$34.4 million in the 1992 fiscal year and froze the 1993 revenue sharing payments at the 1992 level.

The Michigan Trust may contain general obligation bonds of local units of government pledging the full faith and credit of the local unit which are payable from the levy of ad valorem taxes on taxable property within the jurisdiction of the local unit. Such bonds issued prior to December 22, 1978, or issued after December 22, 1978 with the approval of the electors of the local unit, are payable from property taxes levied without limitation as to rate or amount. With respect to bonds issued after December 22, 1978, and which were not approved by the electors of the local unit, the tax levy of the local unit for debt service purposes is subject to constitutional, statutory and charter tax rate limitations. In addition, several major industrial corporations have instituted challenges of their ad valorem property tax assessments in a number of local municipal units in the State. If successful, such challenges could have an adverse impact on the ad valorem tax bases of such units which could adversely affect their ability to raise funds for operating and debt service requirements.

At the time of the closing for each Michigan Trust, Special Counsel to each Michigan Trust for Michigan tax matters rendered an opinion under then existing Michigan income tax law applicable to taxpayers whose income is subject to Michigan income taxation substantially to the effect that:

The Michigan Trust and the owners of Units will be treated for purposes of the Michigan income tax laws and the Single Business Tax in substantially the same manner as they are for purposes of the Federal income tax laws, as currently enacted. Accordingly, we have relied upon the opinion of Chapman and Cutler as to the applicability of Federal income tax under the Internal Revenue Code of 1986 to the Michigan Trust and the Holders of Units.

Under the income tax laws of the State of Michigan, the Michigan Trust is not an association taxable as a corporation; the income of a Michigan Trust will be treated as the income of the Unitholders and be deemed to have been received by them when received by a Michigan Trust. Interest on the underlying Bonds which is exempt from tax under these laws when received by a Michigan Trust will retain its status as tax exempt interest to the Unitholders.

For purposes of the foregoing Michigan tax laws, each Unitholder will be considered to have received his pro rata share of Bond interest when it is received by a Michigan Trust, and each Unitholder will have a taxable event



when the Michigan Trust disposes of a Bond (whether by sale, exchange, redemption or payment at maturity) or when the Unitholder redeems or sells his Certificate to the extent the transaction constitutes a taxable event for Federal income tax purposes. The tax cost of each unit to a Unitholder will be established and allocated for purposes of these Michigan tax laws in the same manner as such cost is established and allocated for Federal income tax purposes.

Under the Michigan Intangibles Tax, a Michigan Trust is not taxable and the pro rata ownership of the underlying Bonds, as well as the interest thereon, will be exempt to the Unitholders to the extent the Michigan Trust consists of obligations of the State of Michigan or its political subdivisions or municipalities, or of obligations of possessions of the United States.

The Michigan Single Business Tax replaced the tax on corporate and financial institution income under the Michigan Income Tax, and the Intangible Tax with respect to those intangibles of persons subject to the Single Business Tax the income from which would be considered in computing the Single Business Tax. Persons are subject to the Single Business Tax only if they are engaged in "business activity", as defined in the Act. Under the Single Business Tax, both interest received by a Michigan Trust on the underlying Bonds and any amount distributed from a Michigan Trust to a Unitholder, if not included in determining taxable income for Federal income tax purposes, is also not included in the adjusted tax base upon which the Single Business Tax is computed, of either the Michigan Trust or the Unitholders. If the Michigan Trust or the Unitholders have a taxable event for Federal income tax purposes when a Michigan Trust disposes of a Bond (whether by sale, exchange, redemption or payment at maturity) or the Unitholder redeems or sells his Certificate, an amount equal to any gain realized from such taxable event which was included in the computation of taxable income for Federal income tax purposes (plus an amount equal to any capital gain of an individual realized in connection with such event but excluded in computing that individual's Federal taxable income) will be included in the tax base against which, after allocation, apportionment and other adjustments, the Single Business Tax is computed. The tax base will be reduced by an amount equal to any capital loss realized from such a taxable event, whether or not the capital loss was deducted in computing Federal taxable income in the year the loss occurred. Unitholders should consult their tax advisor as to their status under Michigan law.

Any proceeds paid under an insurance policy issued to the Trustee of a Trust, or paid under individual policies obtained by issuers of Bonds, which, when received by the Unitholders, represent maturing interest on defaulted obligations held by the Trustee, will be excludable from the Michigan income tax laws and the Single Business Tax if, and to the same extent as, such interest would have been so excludable if paid by the issuer of the defaulted obligations. While treatment under the Michigan Intangibles Tax is not premised upon the characterization of such proceeds under the Internal Revenue Code, the Michigan Department of Treasury should adopt the same approach as under the Michigan income tax laws and the Single Business tax.

As the Tax Reform Act of 1986 eliminates the capital gain deduction for tax years beginning after December 31, 1986, the federal adjusted gross income, the computation base for the Michigan Income Tax, of a Unitholder will be increased accordingly to the extent such capital gains are realized when the Michigan Trust disposes of a Bond or when the Unitholder redeems or sells a Unit, to the extent such transaction constitutes a taxable event for Federal income tax purposes.

#### Minnesota Trusts

In the early 1980s the State of Minnesota experienced financial difficulties due to a downturn in the State's economy resulting from the national recession. As a consequence, the State's revenues were significantly lower than anticipated in the July 1, 1979 to June 30, 1981 biennium and the July 1, 1981 to June 30, 1983 biennium.

In response to revenue shortfalls, the legislature broadened and increased the State sales tax, increased income taxes (by increasing rates and eliminating deductions) and reduced appropriations and deferred payment of State aid, including appropriations for and aids to local governmental units. The State's fiscal problems affected other governmental units within the State, such as local government, school districts and state agencies, which, in varying degrees, also faced cash flow difficulties. In certain cases, revenues of local governmental units and agencies were reduced by the recession.

Because of the State's fiscal problems, Standard & Poor's Corporation reduced its rating on the State's outstanding general obligation bonds from AAA to AA+ in August 1981 and to AA in March 1982. Moody's Investors Service, Inc. lowered its rating on the State's outstanding general obligation bonds from Aaa to Aa in April 1982. The State's economy recovered in the July 1, 1983 to June 30, 1985 biennium, and substantial reductions in the individual income tax were enacted in 1984 and 1985. Standard & Poor's raised its rating on the State's outstanding general obligation bonds to AA+ in January 1985. In 1986,

1987 and 1991, legislation was required to eliminate projected budget deficits by raising additional revenue, reducing expenditures, including aid to political subdivisions and higher education, and making other budgetary adjustments. A budget forecast released by the Minnesota Department of Finance on February 27, 1992 projected a \$569 million budget shortfall, primarily attributable to reduced income tax receipts, for the biennium ending June 30, 1993. Planning estimates for the biennium ending June 30, 1995 projected a budget shortfall of \$1.75 billion (less a \$400 million reserve). The State responded by enacting legislation in 1992 that made substantial accounting changes, reduced the budget reserve (cash flow account) by \$160 million to \$240 million, reduced appropriations for state agencies and higher education, imposed a sales tax on purchases by local governmental units and adopted other tax and spending changes. The 1993 legislature enacted further tax and spending changes. An end-of-legislative-session budget forecast released by the Department of Finance on June 15, 1993 for the biennium ending June 30, 1995 projects a General Fund surplus of \$16 million at the end of the biennium, after applying a projected \$297 million surplus from June 30, 1993 and after reserving \$360 million for the cash flow account. Total budgeted expenditures and transfers for the biennium are \$16.5 billion.

State grants and aids represent a large percentage of the total revenues of cities, towns, counties and school districts in Minnesota. Even with respect to Bonds that are revenue obligations of the State and not general obligations of the issuer, there can be no assurance that the fiscal problems referred to above will not adversely affect the market value or marketability of the Bonds or the ability of the respective obligors to pay interest on and principal of the Bonds.

At the time of the closing for each Minnesota Trust, Special Counsel to each Minnesota Trust for Minnesota tax matters rendered an opinion under then existing Minnesota income tax law applicable to taxpayers whose income is subject to Minnesota income taxation substantially to the effect that:

We understand that the Minnesota Trust will have no income other than (i) interest income on bonds issued by the State of Minnesota and its political and governmental subdivisions, municipalities and governmental agencies and instrumentalities and on bonds issued by possessions of the United States which would be exempt from Federal and Minnesota income taxation when paid directly to an individual, trust or estate (and the term "Bonds" as used herein refers only to such Bonds), (ii) gain on the disposition of such Bonds, and (iii) proceeds paid under certain insurance policies issued to the Trustee or to the issuers of the Bonds which represent maturing interest or principal payments on defaulted Bonds held by the Trustee.

"Taxable income" for Minnesota income tax purposes is the same as "taxable income" for Federal income tax purposes with certain modifications that (with one exception) do not apply to the present circumstances. The exception is that corporations must add to Federal taxable income the amount of any interest received on the obligations of states and their agencies and instrumentalities, political and governmental subdivisions, and municipalities. The terms "trust" and "corporation" have the same meanings for Minnesota income tax purposes, as relevant to the Minnesota tax status of the Minnesota Trust, as for Federal income tax purposes.

In view of the relationship between Federal and Minnesota law described in the preceding paragraph and the opinion of Chapman and Cutler with respect to Federal tax treatment of the Minnesota Trust and its Unitholders:

the Minnesota Trust will be treated as a trust rather than a corporation for Minnesota income tax purposes and will not be deemed the recipient of any Minnesota taxable income;

each Unitholder of a Minnesota Trust will be treated as the owner of a pro rata portion of the Minnesota Trust for Minnesota income tax purposes and the income of the Minnesota Trust will therefore be treated as the income of the Unitholders under Minnesota law;

interest on the Bonds will be exempt from Minnesota income taxation of Unitholders who are individuals, trusts and estates when received by the Minnesota Trust and attributed to such Unitholders and when distributed to such Unitholders (except as hereinafter provided with respect to "industrial development bonds" and "private activity bonds" held by "substantial users");

interest on the Bonds will be includible in the Minnesota taxable income (subject to allocation and apportionment) of Unitholders that are corporations;

each Unitholder will realize taxable gain or loss when the Minnesota Trust disposes of a Bond (whether by sale, exchange, redemption or payment at maturity) or when the Unitholder redeems or sells Units at a price which differs from original cost as adjusted for amortization of bond discount or premium and other basis adjustments (including any basis reduction that may be required to reflect a Unitholder's share of interest, if any, accruing on Bonds during the interval between the Unitholder's settlement date and the

date such Bonds are delivered to the Minnesota Trust, if later);

tax cost reduction requirements relating to amortization of bond premium may, under some circumstances, result in Unitholders realizing taxable gain when their Units are sold or redeemed for an amount equal to or less than their original cost;

any proceeds paid under the insurance policy issued to the Trustee with respect to the Bonds which represent maturing interest on defaulted obligations held by the Trustee will be excludible from Minnesota gross income if, and to the same extent as, such interest would have been so excludible if paid by the issuer of the defaulted obligations;

any proceeds paid under individual insurance policies obtained by issuers of Bonds which represent maturing interest on defaulted obligations held by the Trustee will be excludible from Minnesota gross income if, and to the same extent as, such interest would have been so excludible if paid in the normal course by the issuer of the defaulted obligations;

net capital gains of Unitholders attributable to the Bonds will be fully includible in the Minnesota taxable income of Unitholders (subject to allocation and apportionment in the case of corporate Unitholders); and

interest on Bonds includible in the computation of "alternative minimum taxable income" for Federal income tax purposes will also be includible in the computation of "alternative minimum taxable income" for Minnesota income tax purposes.

Interest income attributable to Bonds that are "industrial development bonds" or "private activity bonds," as those terms are defined in the Internal Revenue Code, will be taxable under Minnesota law to a Unitholder who is a "substantial user" of the facilities financed by the proceeds of such Bonds (or a "related person" to such a "substantial user") to the same extent as if such Bonds were held by such Unitholder.

#### Missouri Trusts

The following discussion regarding constitutional limitations and the economy of the State of Missouri is included for the purpose of providing general information that may or may not affect issuers of the Bonds in Missouri.

In November 1981, the voters of Missouri adopted a tax limitation amendment to the constitution of the State of Missouri (the "Amendment"). The Amendment prohibits increases in local taxes, licenses, or fees by political subdivisions without approval of the voters of such political subdivision. The Amendment also limits the growth in revenues and expenditures of the State to the rate of growth in the total personal income of the citizens of Missouri. The limitation may be exceeded if the General Assembly declares an emergency by a two-thirds vote. The Amendment did not limit revenue growth at the state level in fiscal 1982 through 1988 with the exception of fiscal 1984. Management Report No. 85-20, which was issued on March 5, 1985 by State Auditor Margaret Kelly, indicates that state revenues exceeded the allowable increase by \$30.52 million in fiscal 1984, and a taxpayer lawsuit has been filed pursuant to the Amendment seeking a refund of the revenues in excess of the limit.

The economy of Missouri is diverse and includes manufacturing, retail and wholesale trade, services, agriculture, tourism and mining. In recent years, growth in the wholesale and retail trade had offset the more slowly growing manufacturing and agricultural sectors of the economy. In 1991, the unemployment rate in Missouri was 6.6%, and according to preliminary seasonally adjusted figures, the rate dropped to 5.4% in December 1992. There can be no assurance that general economic conditions or the financial circumstances of Missouri or its political subdivisions will not adversely affect the market value of the Bonds or the ability of the obligor to pay debt service on such Bonds.

Currently, Moody's Investors Service rates Missouri general obligation bonds "Aaa" and Standard & Poor's Corporation rates Missouri general obligation bonds "AAA". Although these ratings indicate that the State of Missouri is in relatively good economic health, there can be, of course, no assurance that this will continue or that particular bond issues may not be adversely affected by changes in the State or local economic or political conditions.

The foregoing information constitutes only a brief summary of some of the general factors which may impact certain issuers of Bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers of obligations held by the Missouri Trust are subject. Additionally, many factors including national economic, social and environmental policies and conditions, which are not within the control of the issuers of the Bonds, could affect or could have an adverse impact on the financial condition of the State and various agencies and political subdivisions located in the State. The Sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of the

Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Missouri Trust to pay interest on or principal of the Bonds.

At the time of the closing for each Missouri Trust, Special Counsel for Missouri tax matters rendered an opinion under then existing Missouri income tax law applicable to taxpayers whose income is subject to Missouri income taxation substantially to the effect that:

The assets of the Missouri Trust will consist of debt obligations issued by or on behalf of the State of Missouri (the "State") or counties, municipalities, authorities or political subdivisions thereof (the "Missouri Bonds") or by the Commonwealth of Puerto Rico, Guam and the United States Virgin Islands (the "Possession Bonds") (collectively, the "Bonds").

Neither the Sponsor nor its counsel have independently examined the Bonds to be deposited in and held in the Missouri Trust. However, although no opinion is expressed herein regarding such matters, it is assumed that: (i) the Bonds were validly issued, (ii) the interest thereon is excludable from gross income for Federal income tax purposes and (iii) interest on the Missouri Bonds, if received directly by a Unitholder, would be exempt from the Missouri income tax applicable to individuals and corporations ("Missouri state income tax"). The opinion set forth below does not address the taxation of persons other than full time residents of Missouri.

In the opinion of Chapman and Cutler, counsel to the Sponsor under existing law:

The Missouri Trust is not an association taxable as a corporation for Missouri income tax purposes, and each Unitholder of the Missouri Trust will be treated as the owner of a pro rata portion of the Missouri Trust and the income of such portion of the Missouri Trust will be treated as the income of the Unitholder for Missouri state income tax purposes.

Interest paid and original issue discount, if any, on the Bonds which would be exempt from the Missouri state income tax if received directly by a Unitholder will be exempt from the Missouri state income tax when received by the Missouri Trust and distributed to such Unitholder; however, no opinion is expressed herein regarding taxation of interest paid and original issue discount, if any, on the Bonds received by the Missouri Trust and distributed to Unitholders under any other tax imposed pursuant to Missouri law, including but not limited to the franchise tax imposed on financial institutions pursuant to Chapter 148 of the Missouri Statutes.

To the extent that interest paid and original issue discount, if any, derived from the Missouri Trust by a Unitholder with respect to Possession Bonds is excludable from gross income for Federal income tax purposes pursuant to 48 U.S.C. §745, 48 U.S.C. §1423a, and 48 U.S.C. §1403, such interest paid and original issue discount, if any, will not be subject to the Missouri state income tax; however, no opinion is expressed herein regarding taxation of interest paid and original issue discount, if any, on the Bonds received by the Missouri Trust and distributed to Unitholders under any other tax imposed pursuant to Missouri law, including but not limited to the franchise tax imposed on financial institutions pursuant to Chapter 148 of the Missouri Statutes.

Each Unitholder of the Missouri Trust will recognize gain or loss for Missouri state income tax purposes if the Trustee disposes of a bond (whether by redemption, sale, or otherwise) or if the Unitholder redeems or sells Units of the Missouri Trust to the extent that such a transaction results in a recognized gain or loss to such Unitholder for Federal income tax purposes. Due to the amortization of bond premium and other basis adjustments required by the Internal Revenue Code, a Unitholder under some circumstances, may realize taxable gain when his or her Units are sold or redeemed for an amount equal to their original cost.

Any insurance proceeds paid under policies which represent maturing interest on defaulted obligations which are excludable from gross income for Federal income tax purposes will be excludable from Missouri state income tax to the same extent as such interest would have been paid by the issuer of such Bonds held by the Missouri Trust; however, no opinion is expressed herein regarding taxation of interest paid and original issue discount, if any, on the Bonds received by the Missouri Trust and distributed to Unitholders under any other tax imposed pursuant to Missouri law, including but not limited to the franchise tax imposed on financial institutions pursuant to Chapter 148 of the Missouri Statutes.

The Missouri state income tax does not permit a deduction of interest paid or incurred on indebtedness incurred or continued to purchase or carry Units in the Trust, the interest on which is exempt from such Tax.

The Missouri Trust will not be subject to the Kansas City, Missouri Earnings and Profits Tax and each Unitholder's share of income of the Bonds held by the Missouri Trust will not generally be subject to the Kansas City, Missouri

Earnings and Profits Tax or the City of St. Louis Earnings Tax (except in the case of certain Unitholders, including corporations, otherwise subject to the St. Louis City Earnings Tax).

#### Nebraska Trusts

The assets of the Nebraska Trust will consist of interest-bearing obligations issued by or on behalf of the State of Nebraska (the "State") or counties, municipalities, authorities or political subdivisions thereof (the "Nebraska Bonds") or by the Commonwealth of Puerto Rico, Guam and the United States Virgin Islands (the "Possession Bonds") (collectively, the "Bonds");

Neither the Sponsor nor its counsel have independently examined the Bonds to be deposited in and held in the Nebraska Trust. With respect to certain Nebraska Bonds which may be held by the Nebraska Trust, the opinions of bond counsel to the issuing authorities for such bonds have indicated that the interest on such Bonds is included in computing the Nebraska Alternative Minimum Tax imposed by Section 77-2715(2) of the Revised Nebraska Statutes (the "Nebraska Minimum Tax") (the "Nebraska AMT Bonds"). However, although no opinion is expressed herein regarding such matters, it is assumed that: (i) the Bonds were validly issued, (ii) the interest thereon is excludible from gross income for Federal income tax purposes, (iii) none of the Bonds (other than the Nebraska AMT Bonds, if any) are "specified private activity bonds" the interest on which is included as an item of tax preference in the computation of the Alternative Minimum Tax for federal income tax purposes, (iv) interest on the Nebraska Bonds (other than the Nebraska AMT Bonds, if any), if received directly by a Unitholder, would be exempt from both the Nebraska income tax, imposed by Section 77-2714 et seq. of the Revised Nebraska Statutes (other than the Nebraska Minimum Tax) (the "Nebraska State Income Tax") and the Nebraska Minimum Tax imposed by Section 77-2715(2) of the Revised Nebraska Statutes (the "Nebraska Minimum Tax"), and (v) interest on the Nebraska AMT Bonds, if any, if received directly by a Unitholder, would be exempt from the Nebraska State Income Tax. The opinion set forth below does not address the taxation of persons other than full time residents of Nebraska;

At the time of closing for each Nebraska Trust, Special Counsel to each Nebraska Trust for Nebraska tax matters, rendered an opinion under then existing Nebraska income tax law applicable to taxpayers whose income is subject to Nebraska income taxation substantially to the effect that:

The Nebraska Trust is not an association taxable as a corporation, each Unitholder of the Nebraska Trust will be treated as the owner of a pro rata portion of the Nebraska Trust, and the income of such portion of the Nebraska Trust will therefore be treated as the income of the Unitholder for both Nebraska State Income Tax and the Nebraska Minimum Tax purposes;

Interest on the Bonds which is exempt from both the Nebraska State Income Tax and the Nebraska Minimum Tax when received by the Nebraska Trust, and which would be exempt from both the Nebraska State Income Tax and the Nebraska Minimum Tax if received directly by a Unitholder, will retain its status as exempt from such taxes when received by the Nebraska Trust and distributed to a Unitholder;

Interest on the Nebraska AMT Bonds, if any, which is exempt from the Nebraska State Income Tax but is included in the computation of the Nebraska Minimum Tax when received by the Nebraska Trust, and which would be exempt from the Nebraska State Income Tax but would be included in the computation of the Nebraska Minimum Tax if received directly by a Unitholder, will retain its status as exempt from the Nebraska State Income Tax but included in the computation of the Nebraska Minimum Tax when received by the Nebraska Trust and distributed to a Unitholder;

To the extent that interest derived from the Nebraska Trust by a Unitholder with respect to the Possession Bonds is excludable from gross income for Federal income tax purposes pursuant to 48 U.S.C. Section 745, 48 U.S.C. Section 1423a and 48 U.S.C. Section 1403, such interest will not be subject to either the Nebraska State Income Tax or the Nebraska Minimum Tax.

Each Unitholder of the Nebraska Trust will recognize gain or loss for both Nebraska State Income Tax and Nebraska Minimum Tax purposes if the Trustee disposes of a Bond (whether by redemption, sale or otherwise) or if the Unitholder redeems or sells Units of the Nebraska Trust to the extent that such a transaction results in a recognized gain or loss to such Unitholder for Federal income tax purposes.

The Nebraska State Income Tax does not permit a deduction for interest paid or incurred on indebtedness incurred or continued to purchase or carry Units in the Nebraska Trust, the interest on which is exempt from such Tax.

In the case of a Unitholder subject to the State financial institutions franchise tax, the income derived by such Unitholder from his pro rata portion of the Bonds held by the Nebraska Trust may affect the determination of such Unitholder's maximum franchise tax.

Neither the Sponsor nor its counsel have examined any of the Bonds to be deposited and held in the Nebraska Trust or the proceedings for the issuance thereof or the opinions of bond counsel with respect thereto, and therefore express no opinion as to the exemption from either the Nebraska State Income Tax or the Nebraska Minimum Tax of interest on the Nebraska Bonds if received directly by a Unitholder.

#### New Jersey Trusts

Each New Jersey Trust consists of a portfolio of Bonds. The Trust is therefore susceptible to political, economic or regulatory factors affecting issuers of the Bonds. The following information provides only a brief summary of some of the complex factors affecting the financial situation in New Jersey (the "State") and is derived from sources that are generally available to investors and is believed to be accurate. It is based in part on information obtained from various State and local agencies in New Jersey. No independent verification has been made of any of the following information.

New Jersey is the ninth largest state in population and the fifth smallest in land area. With an average of 1,050 people per square mile, it is the most densely populated of all the states. The State's economic base is diversified, consisting of a variety of manufacturing, construction and service industries, supplemented by rural areas with selective commercial agriculture. Historically, New Jersey's average per capita income has been well above the national average, and in 1991 the state ranked second among States in per capita personal income (\$26,457).

The New Jersey Economic Policy Council, a statutory arm of the New Jersey Department of Commerce and Economic Development, has reported in New Jersey Economic Indicators, a monthly publication of the New Jersey Department of Labor, Division of Labor Market and Demographic Research, that in 1988 and 1989 employment in New Jersey's manufacturing sector failed to benefit from the export boom experienced by many Midwest states and the State's service sectors, which had fueled the State's prosperity since 1982, lost momentum. In the meantime, the prolonged fast growth in the State in the mid 1980s resulted in a tight labor market situation, which has led to relatively high wages and housing prices. This means that, while the incomes of New Jersey residents are relatively high, the State's business sector has become more vulnerable to competitive pressures.

The onset of the national recession (which officially began in July 1990 according to the National Bureau of Economic Research) caused an acceleration of New Jersey's job losses in construction and manufacturing. In addition, the national recession caused an employment downturn in such previously growing sectors as wholesale trade, retail trade, finance, utilities and trucking and warehousing. Reflecting the downturn, the rate of unemployment in the State rose from a low of 3.6% during the first quarter of 1989 to an estimated 7.1% in December 1993, which is higher than the national average of 6.4% in December 1993. Economic recovery is likely to be slow and uneven in New Jersey, with unemployment receding at a correspondingly slow pace, due to the fact that some sectors may lag due to continued excess capacity. In addition, employers even in rebounding sectors can be expected to remain cautious about hiring until they become convinced that improved business will be sustained. Also, certain firms will continue to merge or down size to increase profitability.

Debt Service. The primary method for State financing of capital projects is through the sale of the general obligation bonds of the State. These bonds are backed by the full faith and credit of the State tax revenues and certain other fees are pledged to meet the principal and interest payments and if provided, redemption premium payments, if any, required to repay the bonds. As of June 30, 1993, there was a total authorized bond indebtedness of approximately \$8.98 billion, of which \$3.6 billion was issued and outstanding, \$4.0 billion was retired (including bonds for which provision for payment has been made through the sale and issuance of refunding bonds) and \$1.38 billion was unissued. The debt service obligation for such outstanding indebtedness is \$119.9 million for fiscal year 1994.

New Jersey's Budget and Appropriation System. The State operates on a fiscal year beginning July 1 and ending June 30. At the end of fiscal year 1989, there was a surplus in the State's general fund (the fund into which all State revenues not otherwise restricted by statute are deposited and from which appropriations are made) of \$411.2 million. At the end of fiscal year 1990, there was a surplus in the general fund of \$1 million. At the end of fiscal year 1991, there was a surplus in the general fund of \$1.4 million. New Jersey closed its fiscal year 1992 with a surplus of \$760.8 million. It is estimated that New Jersey closed its fiscal year 1993 with a surplus of \$361.3 million.

In order to provide additional revenues to balance future budgets, to redistribute school aid and to contain real property taxes, on June 27, 1990, and July 12, 1990, Governor Florio signed into law legislation which was estimated to raise approximately \$2.8 billion in additional taxes (consisting of \$1.5 billion in sales and use taxes and \$1.3 billion in income taxes), the



biggest tax hike in New Jersey history. There can be no assurance that receipts and collections of such taxes will meet such estimates.

The first part of the tax hike took effect on July 1, 1990, with the increase in the State's sales and use tax rate from 6% to 7% and the elimination of exemptions for certain products and services not previously subject to the tax, such as telephone calls, paper products (which has since been reinstated), soaps and detergents, janitorial services, alcoholic beverages and cigarettes. At the time of enactment, it was projected that these taxes would raise approximately \$1.5 billion in additional revenue. Projections and estimates of receipts from sales and use taxes, however, have been subject to variance in recent fiscal years.

The second part of the tax hike took effect on January 1, 1991, in the form of an increased state income tax on individuals. At the time of enactment, it was projected that this increase would raise approximately \$1.3 billion in additional income taxes to fund a new school aid formula, a new homestead rebate program and state assumption of welfare and social services costs. Projections and estimates of receipts from income taxes, however, have also been subject to variance in recent fiscal years. Under the legislation, income tax rates increased from their previous range of 2% to 3.5% to a new range of 2% to 7%, with the higher rates applying to married couples with incomes exceeding \$70,000 who file joint returns, and to individuals filing single returns with incomes of more than \$35,000.

The Florio administration has contended that the income tax package will help reduce local property tax increases by providing more state aid to municipalities. Under the income tax legislation the State will assume approximately \$289 million in social services costs that previously were paid by counties and municipalities and funded by property taxes. In addition, under the new formula for funding school aid, an extra \$1.1 billion is proposed to be sent by the State to school districts beginning in 1991, thus reducing the need for property tax increases to support education programs.

Effective July 1, 1992, the State's sales and use tax rate decreased from 7% to 6%.

On June 29, 1993, Governor Florio signed the New Jersey Legislature's \$15.9 billion budget for Fiscal Year 1994. The balanced budget does not rely on any new taxes, college tuition increases or any commuter fare increases, while providing a surplus of more than \$400 million. Whether the State can achieve a balanced budget depends on its ability to enact and implement expenditure reductions and to collect the estimated tax revenues. The Fiscal Year 1994 Appropriations Act forecasts sales and use tax collections of \$3.920 billion, a 7.5% increase from receipts estimated in the Revised Revenue Estimates for Fiscal Year 1993. It also forecasts gross income tax collections of \$4.748 billion, a 10.6% increase from receipts estimated for Fiscal Year 1993, and corporation business tax collections of \$1.1 billion, a 15.4% increase from receipts estimated for Fiscal Year 1993. However, projections and estimates of receipts from taxes have been subject to variance in recent years as a result of several factors, most recently a significant slowdown in the national, regional and State economies, sluggish employment and uncertainties in taxpayer behavior as a result of actual and proposed changes in Federal tax laws.

Litigation. The State is a party in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Such litigation includes, but is not limited to, claims asserted against the State arising from alleged torts, alleged breaches of contracts, condemnation proceedings and other alleged violations of State and Federal laws. Included in the State's outstanding litigation are cases challenging the following: the formula relating to State aid to public schools, the method by which the State shares with its counties maintenance recoveries and costs for residents in State institutions, unreasonably low Medicaid payment rates for long-term facilities in New Jersey, the obligation of counties to maintain Medicaid or Medicare eligible residents of institutions and facilities for the developmentally disabled, taxes paid into the Spill Compensation Fund (a fund established to provide money for use by the State to remediate hazardous waste sites and to compensate other persons for damages incurred as a result of hazardous waste discharge) based on Federal preemption, various provisions and the constitutionality of the Fair Automobile Insurance Reform Act of 1990, the State's method of funding the judicial system, certain provisions of New Jersey's hospital rate-setting system, the adequacy of Medicaid reimbursement for services rendered by doctors and dentists to Medicaid eligible children, the Commissioner of Health's calculation of the hospital assessment required by the Health Care Cost Reduction Act of 1991, refusal of the State to share with Camden County federal funding the State recently received for disproportionate share hospital payments made to county psychiatric facilities, and recently enacted legislation calling for a revaluation of several New Jersey public employee pension funds in order to provide additional revenues for the State's general fund. Adverse judgments in these and other matters could have the potential for either a significant loss of revenue or a significant unanticipated expenditure by the State.



At any given time, there are various numbers of claims and cases pending against the State, State agencies and employees seeking recovery of monetary damages that are primarily paid out of the fund created pursuant to the New Jersey Tort Claims Act. In addition, at any given time, there are various numbers of contract claims against the State and State agencies seeking recovery of monetary damages. The State is unable to estimate its exposure for these claims.

Debt Ratings. For many years, both Moody's Investors Service, Inc. and Standard and Poor's Corporation rated New Jersey general obligation bonds Aaa and "AAA", respectively. On July 3, 1991, however, Standard and Poor's Corporation downgraded New Jersey general obligation bonds to "AA+." On June 4, 1992, Standard and Poor's Corporation placed New Jersey general obligation bonds on Credit Watch with negative implications, citing as its principal reason for its caution the unexpected denial by the federal government of New Jersey's request for \$450 million in retroactive Medicaid payments for psychiatric hospitals. These funds were critical to closing a \$1 billion gap in the State's \$15 billion budget for fiscal year 1992 which ended on June 30, 1992. Under New Jersey state law, the gap in the budget must be closed before the new budget year begins on July 1, 1992. Standard and Poor's suggested the State could close fiscal 1992's budget gap and help fill fiscal 1993's hole by a reversion of \$700 million of pension contributions to its general fund under a proposal to change the way the State calculates its pension liability.

On July 6, 1992, Standard and Poor's Corporation reaffirmed its "AA+" rating for New Jersey general obligation bonds and removed the debt from its Credit Watch list, although it stated that New Jersey's long-term financial outlook was negative. Standard and Poor's Corporation was concerned that the State was entering fiscal 1993 with only a \$26 million surplus and remained concerned about whether the sagging State economy would recover quickly enough to meet lawmakers' revenue projections. It also remained concerned about the recent federal ruling leaving in doubt how much the State was due in retroactive Medicaid reimbursements and a ruling by a federal judge, now on appeal, of the State's method for paying for uninsured hospital patients. There can be no assurance that these ratings will continue or that particular bond issues may not be adversely affected by changes in the State or local economic or political conditions.

On August 24, 1992, Moody's Investors Service, Inc. downgraded New Jersey general obligation bonds to "Aa1," stating that the reduction reflects a developing pattern of reliance on nonrecurring measures to achieve budgetary balance, four years of financial operations marked by revenue shortfalls and operating deficits, and the likelihood that serious financial pressures will persist.

Although New Jersey recently received \$412 million in settlement of its \$450 million dispute with the federal government for retroactive Medicaid reimbursements, neither Moody's nor Standard and Poor's has revised its rating for New Jersey general obligation bonds.

At the time of the closing for each New Jersey Trust, Special Counsel to each New Jersey Trust for New Jersey tax matters rendered an opinion under then existing New Jersey income tax law applicable to taxpayers whose income is subject to New Jersey income taxation substantially to the effect that:

The New Jersey Trust will be recognized as a trust and not an association taxable as a corporation. The New Jersey Trust will not be subject to the New Jersey Corporation Business Tax or the New Jersey Corporation Income Tax.

With respect to the non-corporate Unitholders who are residents of New Jersey, the income of the New Jersey Trust which is allocable to each such Unitholder will be treated as the income of such Unitholder under the New Jersey Gross Income Tax. Interest on the underlying Bonds which would be exempt from New Jersey Gross Income Tax if directly received by such Unitholder will retain its status as tax-exempt interest when received by the New Jersey Trust and distributed to such Unitholder. Any proceeds paid under the insurance policy issued to the Trustee of a New Jersey Trust with respect to the Bonds or under individual policies obtained by issuers of Bonds which represent maturing interest on defaulted obligations held by the Trustee will be exempt from New Jersey Gross Income Tax if, and to the same extent as, such interest would have been so exempt if paid by the issuer of the defaulted obligations.

A non-corporate Unitholder will not be subject to the New Jersey Gross Income Tax on any gain realized either when the New Jersey Trust disposes of a Bond (whether by sale, exchange, redemption, or payment at maturity), when the Unitholder redeems or sells his Units or upon payment of any proceeds under the insurance policy issued to the Trustee of a New Jersey Trust with respect to the Bonds or under individual policies obtained by issuers of Bonds which represent maturing principal on defaulted obligations held by the Trustee. Any loss realized on such disposition may not be utilized to offset gains realized by such Unitholder on the disposition of assets the gain on which is subject to the New Jersey Gross Income Tax.

Units of the New Jersey Trust may be taxable on the death of a Unitholder

under the New Jersey Transfer Inheritance Tax Law or the New Jersey Estate Tax Law.

If a Unitholder is a corporation subject to the New Jersey Corporation Business Tax or New Jersey Corporation Income Tax, interest from the Bonds in a New Jersey Trust which is allocable to such corporation will be includable in its entire net income for purposes of the New Jersey Corporation Business Tax or New Jersey Corporation Income Tax, less any interest expense incurred to carry such investment to the extent such interest expense has not been deducted in computing Federal taxable income. Net gains derived by such corporation on the disposition of the Bonds by a New Jersey Trust or on the disposition of its Units will be included in its entire net income for purposes of the New Jersey Corporation Business Tax or New Jersey Corporation Income Tax. Any proceeds paid under the insurance policy issued to the Trustee of the New Jersey Trust with respect to the Bonds or under individual policies obtained by issuers of Bonds which represent maturing interest or maturing principal on defaulted obligations held by the Trustee will be included in its entire net income for purposes of the New Jersey Corporation Business Tax or New Jersey Corporation Income Tax if, and to the same extent as, such interest or proceeds would have been so included if paid by the issuer of the defaulted obligations.

#### New York Trusts

A resident of New York State (or New York City) will be subject to New York State (or New York City) personal income tax with respect to gains realized when New York Obligations held in the New York Trust are sold redeemed or paid at maturity or when his Units are sold or redeemed, such gain will equal the proceeds of sale, redemption or payment less the tax basis of the New York Obligation or Unit (adjusted to reflect (a) the amortization of premium or discount, if any, on New York Obligations held in the Trust, (b) accrued original issue discount, with respect to each New York Obligation which, at the time the New York Obligation was issued had original issue discount, and (c) the deposit of New York Obligations with accrued interest in the Trust after the Unitholder's settlement date).

Interest or gain from the New York Trust derived by a Unitholder who is not a resident of New York State (or New York City) will not be subject to New York State (or New York City) personal income tax, unless the Units are property employed in a business, trade, profession or occupation carried on in New York State (or New York City).

Amounts paid on defaulted New York Obligations held by the Trustee under policies of insurance issued with respect to such New York Obligations will be excludable from income for New York State and New York City income tax purposes, if and to the same extent as, such interest would have been excludable if paid by the respective issuer.

For purposes of the New York State and New York City franchise tax on corporations, Unitholders which are subject to such tax will be required to include in their entire net income any interest or gains distributed to them even though distributed in respect of New York obligations.

If borrowed funds are used to purchase Units in the Trust, all (or part) of the interest on such indebtedness will not be deductible for New York State and New York City tax purposes. The purchase of Units may be considered to have been made with borrowed funds even though such funds are not directly traceable to the purchase of Units in any New York Trust.

The Portfolio of the New York Trust includes certain obligations issued by New York State (the "State"), by its various public bodies (the "Agencies"), and/or by other entities located within the State, including the City of New York (the "City").

Some of the more significant events relating to the financial situation in New York are summarized below. This section provides only a brief summary of the complex factors affecting the financial situation in New York and is based in part on Official Statements issued by, and on other information reported by the State, the City and the Agencies in connection with the issuance of their respective securities.

There can be no assurance that future statewide or regional economic difficulties, and the resulting impact on State or local government finances generally, will not adversely affect the market value of New York Municipal Obligations held in the portfolio of the Trust or the ability of particular obligors to make timely payments of debt service on (or relating to) those obligations.

The State has historically been one of the wealthiest states in the nation. For decades, however, the State economy has grown more slowly than that of the nation as a whole, gradually eroding the State's relative economic affluence. Statewide, urban centers have experienced significant changes involving migration of the more affluent to the suburbs and an influx of generally less affluent residents. Regionally, the older Northeast cities have suffered

because of the relative success that the South and the West have had in attracting people and business. The City has also had to face greater competition as other major cities have developed financial and business capabilities which make them less dependent on the specialized services traditionally available almost exclusively in the City.

The State has for many years had a very high state and local tax burden relative to other states. The burden of State and local taxation, in combination with the many other causes of regional economic dislocation, has contributed to the decisions of some businesses and individuals to relocate outside, or not locate within, the State.

A national recession commenced in mid-1990. The downturn continued throughout the State's 1990-91 fiscal year and was followed by a period of weak economic growth during the 1991 calendar year. For calendar year 1992, the national economy continued to recover, although at a rate below all post-war recoveries. For calendar year 1993, the economy is expected to grow faster than 1992, but still at a very moderate rate, as compared to other recoveries. The national recession has been more severe in the State because of factors such as a significant retrenchment in the financial services industry, cutbacks in defense spending, and an overbuilt real estate market.

1993-94 Fiscal Year. On April 5, 1993, the State Legislature approved a \$32.08 billion budget. Following enactment of the budget the 1993-94 State Financial Plan was formulated on April 16, 1993. This Plan projects General Fund receipts and transfers from other funds at \$32.367 billion and disbursements and transfers to other funds at \$32.300 billion. In comparison to the Governor's recommended Executive Budget for the 1993-94 fiscal year as revised on February 18, 1993, the 1993-94 State Financial Plan reflects increases in both receipts and disbursements in the General Fund of \$811 million.

While a portion of the increased receipts was the result of a \$487 million increase in the State's 1992-93 positive year-end margin at March 31, 1993 to \$671 million, the balance of such increased receipts is based upon (i) a projected \$269 million increase in receipts resulting from improved 1992-93 results and the expectation of an improving economy, (ii) Projected additional payments of \$200 million from the Federal government as reimbursements for indigent medical care, (iii) the early payment of \$50 million of personal tax returns in 1992-93 which otherwise would have been paid in 1993-94; offset by (iv) the State Legislature's failure to enact \$195 million of additional revenue-raising recommendations proposed by the Governor. There can be no assurances that all of the projected receipts referred to above will be received.

Despite the \$811 million increase in disbursements included in the 1993-94 State Financial Plan, a reduction in aid to some local government units can be expected. To offset a portion of such reductions, the 1993-94 State Financial Plan contains a package of mandate relief, cost containment and other proposals to reduce the costs of many programs for which local governments provide funding. There can be no assurance, however, that localities that suffer cuts will not be adversely affected, leading to further requests for State financial assistance.

There can be no assurance that the State will not face substantial potential budget gaps in the future resulting from a significant disparity between tax revenues projected from a lower recurring receipts base and the spending required to maintain State programs at current levels. To address any potential budgetary imbalance, the State may need to take significant actions to align recurring receipts and disbursements.

1992-93 Fiscal Year. Before giving effect to a 1992-93 year-end deposit to the refund reserve account of \$671 million, General Fund receipts in 1992-93 would have been \$716 million higher than originally projected. This year-end deposit effectively reduced 1992-93 receipts by \$671 million and made those receipts available for 1993-94.

The State's favorable performance primarily resulted from income tax collections that were \$700 million higher than projected which reflected both stronger economic activity and tax-induced one-time acceleration of income into 1992. In other areas larger than projected business tax collections and unbudgeted receipts offset the loss of \$200 million of anticipated Federal reimbursement and losses of, or shortfalls in, other projected revenue sources.

For 1992-93, disbursements and transfers to other funds (including the deposit to the refund reserve account discussed above) totalled \$30.829 billion, an increase of \$45 million above projections in April 1992.

Fiscal year 1992-93 was the first time in four years that the State did not incur a cash-basis operating deficit in the General Fund requiring the issuance of deficit notes or other bonds, spending cuts or other revenue raising measures.

Indebtedness. As of March 31, 1993, the total amount of long-term State general

obligation debt authorized but unissued stood at \$2.4 billion. As of the same date, the State had approximately \$5.4 billion in general obligation bonds. The State issued \$850 million in tax and revenue anticipation notes ("TRANS") on April 28, 1993. The State does not project the need to issue additional TRANS during the State's 1993-94 fiscal year.

The State projects that its borrowings for capital purposes during the State's 1993-94 fiscal year will consist of \$460 million in general obligation bonds and \$140 million in new commercial paper issuances. In addition, the State expects to issue \$140 million in bonds for the purpose of redeeming outstanding bond anticipation notes. The Legislature has authorized the issuance of up to \$85 million in certificates of participation during the State's 1993-94 fiscal year for personal and real property acquisitions during the State's 1993-94 fiscal year. The projection of the State regarding its borrowings for the 1993-94 fiscal year may change if actual receipts fall short of State projections or if other circumstances require.

In June 1990, legislation was enacted creating the 'New York Local Government Assistance Corporation' (LGAC), a public benefit corporation empowered to issue long-term obligations to fund certain payments to local governments traditionally funded through the State's annual seasonal borrowing. To date, LGAC has issued its bonds to provide net proceeds of \$3.28 billion. LGAC has been authorized to issue additional bonds to provide net proceeds of \$703 million during the State's 1993-94 fiscal year.

Ratings. The \$850 million in TRANS issued by the State in April 1993 were rated 5P-1-Plus by S&P on April 26, 1993, and M1G-1 by Moody's on April 23, 1993, which represents the highest ratings given by such agencies and the first time the State's TRANS have received these ratings since its May 1989 TRANS issuance. Both agencies cited the State's improved fiscal position as a significant factor in the upgrading of the April 1993 TRANS.

Moody's rating of the State's general obligation bonds stood at A on April 23, 1993, and S&P's rating stood at A- with a stable outlook on April 26, 1993, an improvement from S&P's negative outlook prior to April 1993. Previously, Moody's lowered its rating to A on June 6, 1990, its rating having been A1 since May 27, 1986. S&P lowered its rating from A to A- on January 13, 1992. S&P's previous ratings were A from March 1990 to January 1992, AA- from August 1987 to March 1990 and A1 from November 1982 to August 1987.

Moody's, in confirming its rating of the State's general obligation bonds, and S&P, in improving its outlook on such bonds from negative to stable, noted the State's improved fiscal condition and reasonable revenue assumptions contained in the 1993-94 State budget.

The City accounts for approximately 41% of the State's population and personal income, and the City's financial health affects the State in numerous ways.

In response to the City's fiscal crisis in 1975, the State took a number of steps to assist the City in returning to fiscal stability. Among other actions, the State Legislature (i) created MAC to assist with long-term financing for the City's short-term debt and other cash requirements and (ii) created the State Financial Control Board (the 'Control Board') to review and approve the City's budgets and City four-year financial plans (the financial plans also apply to certain City-related public agencies (the "Covered Organizations")).

In February 1975, the New York State Urban Development Corporation ("UDC"), which had approximately \$1 billion of outstanding debt, defaulted on certain of its short-term notes. Shortly after the UDC default, the City entered a period of financial crisis. Both the State Legislature and the United States Congress enacted legislation in response to this crisis. During 1975, the State Legislature (i) created MAC to assist with long-term financing for the City's short-term debt and other cash requirements and (ii) created the State Financial Control Board (the 'Control Board') to review and approve the City's budgets and City four-year financial plans (the financial plans also apply to certain City-related public agencies (the 'Covered Organizations')).

Over the past three years, the rate of economic growth in the City has slowed substantially, and the City's economy is currently in recession. The City projects, and its current four-year financial plan assumes, a recovery early in the 1993 calendar year. The Mayor is responsible for preparing the City's four-year financial plan, including the City's current financial plan. The City Comptroller has issued reports concluding that the recession of the City's economy will be more severe and last longer than is assumed in the financial plan.

Fiscal Year 1993 and 1993-1996 Financial Plan. The City's 1993 fiscal year results are projected to be balanced in accordance with generally accepted accounting principles ('OAAP'). The City was required to close substantial budget gaps in its 1990, 1991 and 1992 fiscal years in order to maintain balanced operating results.

The City's modified Financial Plan dated February 9, 1993 covering fiscal years 1993-1996 projects budget gaps for 1994 through 1996. The Office of the State Deputy Controller for the City of New York has estimated that under the modified Financial Plan budget gaps will be \$102 million for fiscal year 1994, \$196 million for fiscal year 1995 and \$354 million for fiscal year 1996, primarily due to anticipated higher spending on labor costs.

However, the City's modified Plan is dependent upon a gap-closing program, certain elements of which the staff of Control Board identified on March 25, 1993 to be at risk due to projected levels of State and Federal aid and revenue and expenditures estimates which may not be achievable. The Control Board indicated that the City's modified Financial Plan does not make progress towards establishing a balanced budget process. The Control Board's report identified budget gap risks of \$1.0 billion, \$1.9 billion, \$2.3 billion and \$2.6 billion in fiscal years 1994 through 1997, respectively.

On June 3, 1993, the Mayor announced that State and federal aid for Fiscal Year 1993-1994 would be \$280 million less than projected and that in order to balance the City's budget \$176 million of previously announced contingent budget cuts would be imposed. The Mayor indicated that further savings would entail serious reductions in services. The State Comptroller on June 14, 1993 criticized efforts by the Mayor and City Council to balance the City's budget which rely primarily on one-shot revenues. The Comptroller added that the City's budget should be based on recurring revenues that fund recurring expenditures.' Given the foregoing factors, there can be no assurance that the City will continue to maintain a balanced budget, or that it can maintain a balanced budget without additional tax or other revenue increases or reductions in City services, which could adversely affect the City's economic base.

Pursuant to State law, the City prepares a four-year annual financial plan, which is reviewed and revised on a quarterly basis and which includes the City's capital, revenue and expense projections. The City is required to submit its financial plans to review bodies, including the Control Board. If the City were to experience certain adverse financial circumstances, including the occurrence or the substantial likelihood and imminence of the occurrence of an annual operating deficit of more than \$100 million or the loss of access to the public credit markets to satisfy the City's capital and seasonal financing requirements, the Control Board would be required by State law to exercise certain powers, including prior approval of City financial plans, proposed borrowings and certain contracts.

The City depends on the State for State aid both to enable the City to balance its budget and to meet its cash requirements. As a result of the national and regional economic recession, the State's projections of tax revenues for its 1991 and 1992 fiscal years were substantially reduced. For its 1993 fiscal year, the State, before taking any remedial action reflected in the State budget enacted by the State Legislature on April 2, 1992 reported a potential budget deficit of \$4.8 billion. If the State experiences revenue shortfalls or spending increases beyond its projections during its 1993 fiscal year or subsequent years, such developments could also result in reductions in projected State aid to the City. In addition, there can be no assurance that State budgets in future fiscal years will be adopted by the April 1 statutory deadline and that there will not be adverse effects on the City's cash flow and additional City expenditures as a result of such delays.

The City's projections set forth in its financial plan are based on various assumptions and contingencies which are uncertain and which may not materialize. Changes in major assumptions could significantly affect the City's ability to balance its budget as required by State law and to meet its annual cash flow and financing requirements. Such assumptions and contingencies include the timing of any regional and local economic recovery, the absence of wage increases in excess of the increases assumed in its financial plan, employment growth, provision of State and Federal aid and mandate relief, State legislative approval of future State budgets, levels of education expenditures as may be required by State law, adoption of future City budgets by the New York City Council, and approval by the Governor or the State Legislature and the cooperation of MAC with respect to various other actions proposed in such financial plan.

The City's ability to maintain a balanced operating budget is dependent on whether it can implement necessary service and personnel reduction programs successfully. As discussed above, the City must identify additional expenditure reductions and revenue sources to achieve balanced operating budgets for fiscal years 1994 and thereafter. And such proposed expenditure reductions will be difficult to implement because of their size and the substantial expenditure reductions already imposed on City operations in the past two years.

Attaining a balanced budget is also dependent upon the City's ability to market its securities successfully in the public credit markets. The City's financing program for fiscal years 1993 through 1996 contemplates issuance of \$15.7 billion of general obligation bonds primarily to reconstruct and rehabilitate the City's infrastructure and physical assets and to make capital

investments. A significant portion of such bond financing is used to reimburse the City's general fund for capital expenditures already incurred. In addition, the City issues revenue and tax anticipation notes to finance its seasonal working capital requirements. The terms and success of projected public sales of City general obligation bonds and notes will be subject to prevailing market conditions at the time of the sale, and no assurance can be given that the credit markets will absorb the projected amounts of public bond and note sales. In addition, future developments concerning the City and public discussion of such developments, the City's future financial needs and other issues may affect the market for outstanding City general obligation bonds and notes. If the City were unable to sell its general obligation bonds and notes, it would be prevented from meeting its planned operating and capital expenditures.

The City Comptroller, the staff of the Control Board, the Office of the State Deputy Comptroller for the City of New York (the "OSDC") and other agencies and public officials have issued reports and made public statements which, among other things, state that projected revenues may be less and future expenditures may be greater than those forecast in the financial plan. In addition, the Control Board and other agencies have questioned whether the City has the capacity to generate sufficient revenues in the future to meet the costs of its expenditure increases and to provide necessary services. It is reasonable to expect that such reports and statements will continue to be issued and to engender public comment.

The City achieved balanced operating results as reported in accordance with GAAP for the 1992 fiscal year. During the 1990 and 1991 fiscal years, the City implemented various actions to offset a projected budget deficit of \$3.2 billion for the 1991 fiscal year, which resulted from declines in City revenue sources and increased public assistance needs due to the recession. Such actions included \$822 million of tax increases and substantial expenditure reductions.

The quarterly modification to the City's financial plan submitted to the Control Board on May 7, 1992 (the "1992 Modification") projected a balanced budget in accordance with GAAP for the 1992 fiscal year after taking into account a discretionary transfer of \$455 million to the 1993 fiscal year as the result of a 1992 fiscal year surplus. In order to achieve a balanced budget for the 1992 fiscal year, during the 1991 fiscal year, the City proposed various actions for the 1992 fiscal year to close a projected gap of \$3.3 billion in the 1992 fiscal year.

On November 19, 1992, the City submitted to the Control Board the Financial Plan for the 1993 through 1996 fiscal years, which is a modification to a financial plan submitted to the Control Board on June 11, 1992 (the "June Financial Plan"), and which relates to the City, the Board of Education ("BOE") and the City University of New York ("CUNY"). The 1993-1996 Financial Plan projects revenues and expenditures of \$29.9 billion each for the 1993 fiscal year balanced in accordance with GAAP.

During the 1992 fiscal year, the City proposed various actions to close a previously projected gap of approximately \$1.2 billion for the 1993 fiscal year. The gap-closing actions for the 1993 fiscal year proposed during the 1992 fiscal year and outlined in the City's June Financial Plan included \$489 million of discretionary transfers from the 1992 fiscal year. The 1993-1996 City Financial Plan includes additional gap-closing actions to offset an additional potential \$81 million budget gap.

The 1993-1996 Financial Plan sets forth actions to close a previously projected gap of approximately \$1.2 billion in the 1993 fiscal year. The gap-closing actions for the 1993 fiscal year include \$489 million of discretionary transfers from a City surplus in the 1992 fiscal year.

The 1993-1996 Financial Plan also sets forth projections and outlines a proposed gap-closing program for the 1993 through 1996 fiscal years to close projected budget gaps of \$1.7 billion, \$2.0 billion and \$2.6 billion, respectively, in the 1994 through 1996 fiscal years. On February 9, 1993, the City issued a modification to the 1993-1996 Financial Plan (the "February Modification"). The February Modification projects budget gaps for fiscal years 1994, 1995 and 1996 of \$2.1 billion, \$3.1 billion and \$3.8 billion, respectively.

Various actions proposed in the 1993-1996 Financial Plan are subject to approval by the Governor and approval by the State Legislature, and the proposed increase in Federal aid is subject to approval by Congress and the President. The State Legislature has in the past failed to approve certain proposals similar to those that the 1993-1996 Financial Plan assumes will be approved by the State Legislature during the 1993 fiscal year. If these actions cannot be implemented, the City will be required to take other actions to decrease expenditures or increase revenues to, maintain a balanced financial plan.

On March 9, 1993, OSDC issued a report on the February Modification. The report expressed concern that the budget gaps projected for fiscal years 1994



through 1996 are the largest the City has faced at this point in the financial planning cycle in at least a decade, and concluded that the February Modification represented a step backward in the City's efforts to bring recurring revenues into line with recurring expenditures.

The City is a defendant in a significant number of lawsuits. Such litigation includes, but is not limited to, actions commenced and claims asserted against the City arising out of alleged constitutional violations, torts, breaches of contracts and other violations of law and condemnation proceedings. While the ultimate outcome and fiscal impact, if any, on the proceedings and claims are not currently predictable, adverse determinations in certain of them might have a material adverse effect upon the City's ability to carry out its financial plan. As of June 30, 1992, legal claims in excess of \$341 billion were outstanding against the City for which the City estimated its potential future liability to be \$2.3 billion.

As of the date of this prospectus, Moody's rating of the City's general obligation bonds stood at Baa and S&P's rating stood at A. On February 11, 1991, Moody's had lowered its rating from A.

On March 30, 1993, in confirming its Baa rating, Moody's noted that:

The financial plan for fiscal year 1994 and beyond shows an ongoing imbalance between the City's expenditures and revenues. The key indication of this structural imbalance is not necessarily the presence of sizable out-year budget gaps, but the recurring use of one-shot actions to close gaps. One-shots constitute a significant share of the proposed gap-closing program for fiscal year 1994, and they represent an even larger share of those measures which the City seems reasonably certain to attain. Several major elements of the program, including certain state actions, federal counter cyclical aid and part of the city's tax package, remain uncertain. However, the gap closing plan may be substantially altered when the executive budget is offered later this spring.

On March 30, 1993, S&P affirmed its A- rating with a negative outlook, stating that:

The City's key credit factors are marked by a high and growing debt burden, and taxation levels that are relatively high, but stable. The City's economy is broad-based and diverse, but currently is in prolonged recession, with slow growth prospects for the foreseeable future.

The rating outlook is negative, reflecting the continued fiscal pressure facing the City, driven by continued weakness in the local economy, rising spending pressures for education and labor costs of city employees, and increasing costs associated with rising debt for capital construction and repair.

The current financial plan for the City assumes substantial increases in aid from national and state governments. Maintenance of the current rating, and stabilization of the rating outlook, will depend on the City's success in realizing budgetary aid from these governments, or replacing those revenues with ongoing revenue-raising measures or spending reductions under the City's control. However, increased reliance on non-recurring budget balancing measures that would support current spending, but defer budgetary gaps to future years, would be viewed by S&P as detrimental to New York City's single-A- rating.

Previously, Moody's had raised its rating to A in May, 1988, to Baa in December, 1985, to Baa in November, 1983 and to Ba in November, 1981. S&P had raised its rating to A- in November, 1987, to BBB+ in July, 1985 and to BBB in March, 1981.

On May 9, 1990, Moody's revised downward its rating on outstanding City revenue anticipation notes from MIG-1 to MIG-2 and rated the \$900 million Notes then being sold MIG-2. On April 30, 1991 Moody's confirmed its MIG-2 rating for the outstanding revenue anticipation notes and for the \$1.25 billion in notes then being sold. On April 29, 1991, S&P revised downward its rating on City revenue anticipation notes from SP-1 to SP-2.

As of December 31, 1992, the City and MAC had, respectively, \$20.3 billion and \$4.7 billion of outstanding net long-term indebtedness.

Certain Agencies of the State have faced substantial financial difficulties which could adversely affect the ability of such Agencies to make payments of interest on, and principal amounts of, their respective bonds. The difficulties have in certain instances caused the State (under so-called "moral obligation" provisions which are non-binding statutory provisions for State appropriations to maintain various debt service reserve funds) to appropriate funds on behalf of the Agencies. Moreover, it is expected that the problems faced by these Agencies will continue and will require increasing amounts of State assistance in future years. Failure of the State to appropriate necessary amounts or to take other action to permit those Agencies having financial difficulties to meet their obligations could result in a



default by one or more of the Agencies. Such default, if it were to occur, would be likely to have a significant adverse effect on investor confidence in, and therefore the market price of, obligations of the defaulting Agencies. In addition, any default in payment on any general obligation of any Agency whose bonds contain a moral obligation provision could constitute a failure of certain conditions that must be satisfied in connection with Federal guarantees of City and MAC obligations and could thus jeopardize the City's long-term financing plans.

As of September 30, 1992, the State reported that there were eighteen Agencies that each had outstanding debt of \$100 million or more. These eighteen Agencies had an aggregate of \$62.2 billion of outstanding debt, including refunding bonds, of which the State was obligated under lease-purchase, contractual obligation or moral obligation provisions on \$25.3 billion.

The State is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Such litigation includes, but is not limited to, claims asserted against the State arising from alleged torts, alleged breaches of contracts, condemnation proceedings and other alleged violations of State and Federal laws. Included in the State's outstanding litigation are a number of cases challenging the constitutionality or the adequacy and effectiveness of a variety of significant social welfare programs primarily involving the State's mental hygiene programs. Adverse judgments in these matters generally could result in injunctive relief coupled with prospective changes in patient care which could require substantial increased financing of the litigated programs in the future.

The State is also engaged in a variety of claims wherein significant monetary damages are sought. Actions commenced by several Indian nations claim that significant amounts of land were unconstitutionally taken from the Indians in violation of various treaties and agreements during the eighteenth and nineteenth centuries. The claimants seek recovery of approximately six million acres of land as well as compensatory and punitive damages.

The U.S. Supreme Court on March 30, 1993 referred to a Special Master for determination of damages in an action by the State of Delaware to recover certain unclaimed dividends, interest and other distributions made by issuers of securities held by New York based-brokers incorporated in Delaware. (State of Delaware v. State of New York.) The State had taken such unclaimed property under its Abandoned Property Law. The State expects that it may pay a significant amount in damages during fiscal year 1993-94 but it has indicated that it has sufficient funds on hand to pay any such award, including funds held in contingency reserves. The State's 1993-94 Financial Plan includes the establishment of a \$100 million contingency reserve fund which would be available to fund such an award which some reports have estimated at \$100-\$800 million.

In *Schulz v. State of New York*, commenced May 24, 1993 ("Schulz 1993"), petitioners have challenged the constitutionality of mass transportation bonding programs of the New York State Thruway Authority and the Metropolitan Transportation Authority. On May 24, 1993, the Supreme Court, Albany County, temporarily enjoined the State from implementing those bonding programs. In previous actions Mr. Schulz and others have challenged on similar grounds bonding programs for the New York State Urban Development Corporation and the New York Local Government Assistance Corporation. While there have been no decisions on the merits in such previous actions, by an opinion dated May 11, 1993, the New York Court of Appeals held in a proceeding commenced on April 29, 1991 in the Supreme Court, Albany County (*Schulz v. State of New York*), that petitioners had standing as voters under the State Constitution to bring such action.

Petitioners in *Schulz 1993* have asserted that issuance of bonds by the two Authorities is subject to approval by statewide referendum. At this time there can be no forecast of the likelihood of success on the merits by the petitioners, but a decision upholding this constitutional challenge could restrict and limit the ability of the State and its instrumentalities to borrow funds in the future. The State has not indicated that the temporary injunction issued by the Supreme Court in this action will have any immediate impact on its financial condition or interfere with projects requiring immediate action.

Adverse developments in the foregoing proceedings or new proceedings could adversely affect the financial condition of the State in the future.

Certain localities in addition to New York City could have financial problems leading to requests for additional State assistance. Both the Revised 1992-93 State Financial Plan and the recommended 1993-94 State Financial Plan include a significant reduction in State aid to localities in such programs as revenue sharing and aid to education from projected base-line growth in such programs. It is expected that such reductions will result in the need for localities to reduce their spending or increase their revenues. The potential impact on the State of such actions by localities is not included in projections of State revenues and expenditures in the State's 1993-94 fiscal year.

Fiscal difficulties experienced by the City of Yonkers ("Yonkers") resulted in the creation of the Financial Control Board for the City of Yonkers (the "Yonkers Board") by the State in 1984. The Yonkers Board is charged with oversight of the fiscal affairs of Yonkers. Future actions taken by the Governor or the State Legislature to assist Yonkers could result in allocation of State resources in amounts that cannot yet be determined.

Municipalities and school districts have engaged in substantial short-term and long-term borrowings. In 1991, the total indebtedness of all localities in the State was approximately \$31.6 billion, of which \$16.8 billion was debt of New York City (excluding \$6.7 billion in MAC debt). State law requires the Comptroller to review and make recommendations concerning the budgets of those local government units other than New York City authorized by State law to issue debt to finance deficits during the period that such deficit financing is outstanding. Fifteen localities had outstanding indebtedness for State financing at the close of their fiscal year ending in 1991. In 1992, an unusually large number of local government units requested authorization for deficit financings. According to the Comptroller, ten local government units have been authorized to issue deficit financing in the aggregate amount of \$131.1 million.

Certain proposed Federal expenditure reductions could reduce, or in some cases eliminate, Federal funding of some local programs and accordingly might impose substantial increased expenditure requirements on affected localities. If the State, New York City or any of the Agencies were to suffer serious financial difficulties jeopardizing their respective access to the public credit markets, the marketability of notes and bonds issued by localities within the State, including notes or bonds in the New York Trust, could be adversely affected. Localities also face anticipated and potential problems resulting from certain pending litigation, judicial decisions, and long-range economic trends. The longer-range potential problems of declining urban population, increasing expenditures, and other economic trends could adversely affect localities and require increasing State assistance in the future.

At the time of the closing for each New York Trust, Special Counsel to each New York Trust for New York tax matters rendered an opinion under then existing New York income tax law applicable to taxpayers whose income is subject to New York income taxation substantially to the effect that:

The New York Trust is not an association taxable as a corporation and the income of the New York Trust will be treated as the income of the Unitholders under the income tax laws of the State and City of New York. Individuals who reside in New York State or City will not be subject to State and City tax on interest income which is exempt from Federal income tax under section 103 of the Internal Revenue Code of 1986 and derived from obligations of New York State or a political subdivision thereof, although they will be subject to New York State and City tax with respect to any gains realized when such obligations are sold, redeemed or paid at maturity or when any such Units are sold or redeemed.

#### North Carolina Trust

General obligations of a city, town or county in North Carolina are payable from the general revenues of the entity, including ad valorem tax revenues on property within the jurisdiction. Revenue bonds issued by North Carolina political subdivisions include (1) revenue bonds payable exclusively from revenue-producing governmental enterprises and (2) industrial revenue bonds, college and hospital revenue bonds and other "private activity bonds" which are essentially non-governmental debt issues and which are payable exclusively by private entities such as non-profit organizations and business concerns of all sizes. State and local governments have no obligation to provide for payment of such private activity bonds and in many cases would be legally prohibited from doing so. The value of such private activity bonds may be affected by a wide variety of factors relevant to particular localities or industries, including economic developments outside of North Carolina.

Section 23-48 of the North Carolina General Statutes appears to permit any city, town, school district, county or other taxing district to avail itself of the provisions of Chapter 9 of the United States Bankruptcy Code, but only with the consent of the Local Government Commission of the State and of the holders of such percentage or percentages of the indebtedness of the issuer as may be required by the Bankruptcy Code (if any such consent is required). Thus, although limitations apply, in certain circumstances political subdivisions might be able to seek the protection of the Bankruptcy Code.

State Budget and Revenues. The North Carolina State Constitution requires that the total expenditures of the State for the fiscal period covered by each budget not exceed the total of receipts during the fiscal period and the surplus remaining in the State Treasury at the beginning of the period. The State's fiscal year runs from July 1st through June 30th.

In 1990 and 1991, the State had difficulty meeting its budget projections. Lower than anticipated revenues coupled with increases in State spending

requirements imposed by the federal government led to projected budget deficits for fiscal 1989-1990 and fiscal 1990-1991. Consequently, the Governor ordered cuts in budgeted State expenditures for both fiscal years.

When similar budget deficits were projected for the next two fiscal years, the General Assembly addressed the problem through a broad array of State spending reductions in existing programs or previously budgeted increases and tax increases. The taxes include a one-cent increase in the sales tax, a three-cent increase in the excise tax on cigarettes, an increase in the corporate tax rate (from 7 to 7.75 percent, as well as a four-year surtax, starting at 4% of the regular income tax for tax year 1991 and reducing by 1% for each of the following three years), an increase in the individual income tax rate for married couples with income of more than \$100,000 and individuals with income over \$60,000, and other taxes.

The effect of the budget reductions and tax increases resulted in a small budget surplus (approximately \$160 million) for the 1991-1992 fiscal year (ended June 30, 1992). The State netted a larger budget surplus (approximately \$342 million) for the 1992-1993 fiscal year (ended June 30, 1993). The \$9 billion budget for 1993-1994 adopted by the General Assembly did not include any new tax measures. The 1993-1994 budget does not include new spending cuts and estimated increased revenues totalling \$30.6 million.

Both the nation and the State have experienced a modest economic recovery in recent months. However, it is unclear what effect these developments, as well as the reduction in government spending or increase in taxes may have on the value of the Debt Obligations in the North Carolina Trust. No clear upward trend has developed, and both the State and the national economies must be watched carefully.

The fiscal condition of the State might be affected adversely by litigation concerning the legality of certain State tax provisions following the decision of the United States Supreme Court in *Davis v. Michigan Dept. of Treasury* (decided March 28, 1989). In *Davis*, the United States Supreme Court held unconstitutional a Michigan statute exempting from state income taxation retirement benefits paid by the state of Michigan or its local governments, but not exempting retirement benefits paid by the federal government.

Subsequent to *Davis*, certain federal retirees and federal military personnel plaintiffs brought an action in North Carolina state court seeking refund of the illegal taxes. *Swanson, et al. v. State of North Carolina, et al.* (Wake County, North Carolina Superior Court, No. 90 CVS 3127) ("*Swanson State*").

The amount of refunds claimed by federal retirees in the *Swanson* action has not been calculated. Plaintiffs have asserted that the plaintiff class contains about 100,000 taxpayers; the State has asserted that the claims would aggregate at least \$140 million (which might not include interest).

In a 4-3 decision, the North Carolina Supreme Court found for the defendants, declaring the State would not be required to refund taxes illegally collected prior to the decision in *Davis*. Because of this determination, the Court did not need to decide what remedies would be available if *Davis* were held to apply retroactively. The Court reaffirmed its decision following reconsideration.

Plaintiffs in *Swanson State* applied for review by the U.S. Supreme Court. The U.S. Supreme Court vacated the judgment and remanded the case to the North Carolina Supreme Court for reconsideration in light of the U.S. Supreme Court's holding in *Harper v. Virginia Dept. of Taxation* (No. 91-794) ("*Harper*"). In *Harper*, which also involved the disparate income tax treatment of retired state and federal employees and the question of retroactive application of the decision in *Davis*, the Supreme Court held that the Commonwealth of Virginia must provide "meaningful backward-looking relief" to the plaintiffs, if the Commonwealth did not have a predeprivation process adequate to satisfy due process requirements. The case was remanded to the Supreme Court of Virginia to determine whether a remedy was required and, if so, what form it would take.

The impact of *Harper* on the estimated \$140 million of refund claims in *Swanson State* has yet to be determined. The North Carolina Supreme Court must determine whether North Carolina law provides an adequate predeprivation process, and, if not, what remedy should be fashioned to satisfy due process requirements.

General. The population of the State has increased 13% from 1980, from 5,880,095 to 6,647,351 as reported by the 1990 federal census. Although North Carolina is the tenth largest State in population, it is primarily a rural state, having only five municipalities with populations in excess of 100,000.

The labor force has undergone significant change during recent years. The State has moved from an agricultural to a service and goods producing economy. Those persons displaced by farm mechanization and farm consolidations have, in large measure, sought and found employment in other pursuits. Due to the wide dispersion of non-agricultural employment, the people have been able to

maintain, to a large extent, their rural habitation practices. During the period 1980 to 1990, the State labor force grew about 19% (from 2,855,200 to 3,401,000), and per capita income grew from \$7,999 to \$16,203, an increase of 102.6%.

The current economic profile of the State consists of a combination of industry, agriculture and tourism. As of May 1991, the State was reported to rank tenth among the states in non-agricultural employment and eighth in manufacturing employment. Employment indicators have fluctuated somewhat in the annual periods since June of 1989. The following table reflects the fluctuations in certain key employment categories.

| Category (All Seasonally Adjusted)                                   | June 1989 | June 1990 | June 1991 | June 1992 |
|--|-----------|-----------|-----------|-----------|
| Civilian Labor Force   | 3,286,000 | 3,312,000 | 3,228,000 | 3,275,000 |
| Nonagricultural Employment   | 3,088,000 | 3,129,000 | 3,059,000 | 3,077,000 |
| Goods Producing Occupations (mining, construction and manufacturing) | 1,042,200 | 1,023,100 | 973,600   | 974,600   |
| Service Occupations  | 2,045,800 | 2,106,300 | 2,085,400 | 2,103,100 |
| Wholesale/Retail Occupations   | 713,900   | 732,500   | 704,100   | 694,700   |
| Government Employees   | 482,200   | 496,400   | 496,700   | 502,000   |
| Miscellaneous Services   | 563,900   | 587,300   | 596,300   | 615,300   |
| Agricultural Employment  | 54,900    | 58,900    | 88,700    | 102,800   |

The unemployment rate in June 1993 was 5.4% of the labor force, as compared with an unemployment rate of 7.0% nationwide.

The diversity of agriculture in North Carolina and a continuing push in marketing efforts have protected farm income from some of the wide variations that have been experienced in other states where most of the agricultural economy is dependent on a small number of agricultural commodities.

Gross agricultural income in 1991 was \$4.98 billion, including approximately \$4,924,071,000 income from commodities. As of 1991, the State was tenth in the nation in gross agricultural income. Tobacco production is a leading source of agricultural income in the State, accounting for 21.4% of gross agricultural income. Tobacco farming in North Carolina has been and is expected to continue to be affected by major Federal legislation and regulatory measures regarding tobacco production and marketing and by international competition. Measures adverse to tobacco farming could have negative effects on farm income and the North Carolina economy generally. Eggs and poultry products accounted for revenues of approximately \$1.5 billion in 1991.

According to the State Commissioner of Agriculture, based on 1991 figures, the State ranked first in the nation in the production of flue-cured tobacco, total tobacco, turkeys and sweet potatoes; second in the production of cucumbers for pickles; third in the value of poultry products and trout; fourth in commercial broilers and peanuts; sixth in barley tobacco, greenhouse and nursery receipts, hogs and strawberries; and seventh in the number of chickens (excluding broilers), peaches and apples. The number of farms has been decreasing; in 1992 there were approximately 60,000 farms in the State (down from approximately 72,000 in 1987, a decrease of about 17% in five years). However, a strong agribusiness sector also supports farmers with farm inputs (fertilizer, insecticide, pesticide and farm machinery) and processing of commodities produced by farmers (vegetable canning and cigarette manufacturing).

The State Department of Commerce, Travel and Tourism Division, has reported that in 1991 approximately \$7 billion was spent on tourism in the State with 1992 revenues from tourism expected to exceed \$7.3 billion. In 1990, traveler expenditures directly generated more than 141,000 jobs within the State, 4.5 percent of total nonagricultural employment in that year.

Bond Ratings. Currently, Moody's rates North Carolina general obligation bonds as Aaa and Standard & Poor's rates such bonds as AAA. Standard & Poor's placed North Carolina general obligation bonds on "credit watch" in June of 1990 and continued to monitor the State's economy closely through 1990 and 1991.

In June of 1992 Standard & Poor's revised its outlook on the State's AAA-rated general obligation bonds to stable from negative. Among the reasons for the revision were the revenue spending measures adopted since 1991.

The rating agencies presumably will monitor the results of the legislative approach to the fiscal difficulties.

Thus, although both rating agencies have reaffirmed the AAA rating of North Carolina's outstanding general obligation bonds for the present time, there can be no assurance that these ratings will continue, that local government bond ratings will not decline or that particular bond issues may not be adversely affected by changes in economic, political or other conditions that

do not affect the ratings.

The Sponsor believes the information summarized above describes some of the more significant events relating to the North Carolina Trust. The sources of this information are the official statements of issuers located in North Carolina, State agencies, publicly available documents, publications of rating agencies and news reports of statements by State officials and employees and by rating agencies. The Sponsor and its counsel have not independently verified any of the information contained in the official statements and other sources and counsel have not expressed any opinion regarding the completeness or materiality of any matters contained in this Prospectus other than the tax opinions set forth below under North Carolina Taxes.

At the time of the closing for each North Carolina Trust, Special Counsel to each North Carolina Trust for North Carolina tax matters rendered an opinion under then existing North Carolina income tax law applicable to taxpayers whose income is subject to North Carolina income taxation substantially to the effect that.

Upon the establishing of the North Carolina Trust and the Units thereunder:

The North Carolina Trust is not an "association" taxable as a corporation under North Carolina law with the result that income of the North Carolina Trust will be deemed to be income of the Unitholders;

Interest on the Bonds that is exempt from North Carolina income tax when received by the North Carolina Trust will retain its tax-exempt status when received by the Unitholders;

Unitholders will realize a taxable event when the North Carolina Trust disposes of a Bond (whether by sale, exchange, redemption or payment at maturity) or when a Unitholder redeems or sells his Units (or any of them), and taxable gains for Federal income tax purposes may result in gain taxable as ordinary income for North Carolina income tax purposes. However, when a bond has been issued under an act of the North Carolina General Assembly that provides that all income from such Bond, including any profit made from the sale thereof, shall be free from all taxation by the State of North Carolina, any such profit received by the North Carolina Trust will retain its tax-exempt status in the hands of the Unitholders;

Unitholders must amortize their proportionate shares of any premium on a Bond. Amortization for each taxable year is accomplished by lowering the Unitholder's basis (as adjusted) in his Units with no deduction against gross income for the year; and

The Units are exempt from the North Carolina tax on intangible personal property so long as the corpus of the North Carolina Trust remains composed entirely of Bonds or, pending distribution, amounts received on the sale, redemption or maturity of the Bonds and the Trustee periodically supplies to the North Carolina Department of Revenue at such times as required by the Department of Revenue a complete description of the North Carolina Trust and also the name, description and value of the obligations held in the corpus of the North Carolina Trust.

The opinion of Special Counsel is based, in part, on the opinion of Chapman and Cutler regarding Federal tax status.

#### Ohio Trusts

The Ohio Trust will invest substantially all of its net assets in securities issued by or on behalf of (or in certificates of participation in lease purchase obligations of) the State of Ohio, political subdivisions of the State, or agencies or instrumentalities of the State or its political subdivisions (Ohio Obligations). The Ohio Trust is therefore susceptible to general or particular political, economic or regulatory factors that may affect issuers of Ohio Obligations. The following information constitutes only a brief summary of some of the complex factors that may have an effect. This information does not apply to "conduit" obligations on which the public issuer itself has no financial responsibility. This information is derived from official statements of certain Ohio issuers published in connection with their issuance of securities and from other publicly available documents, and is believed to be accurate. No independent verification has been made of any of the following information.

The creditworthiness of Ohio Obligations of local issuers is generally unrelated to that of obligations issued by the State itself, and the State has no responsibility to make payments on those local obligations. There may be specific factors that at particular times in connection with investment in particular Ohio Obligations or in those obligations of particular Ohio issuers. It is possible the investment may be in particular Ohio Obligations, or in those of particular issuers as to which those factors apply. However, the information below is intended only as a general summary, and is not intended as a discussion of any specific factors that may affect any particular issue or issuer.

Ohio is the seventh most populous state. Its 1990 Census count of 10,847,000 indicates a 0.5% population increase from 1980.

While diversifying more into the service and other non-manufacturing areas, the Ohio economy continues to rely in part on durable goods manufacturing largely concentrated in motor vehicles and equipment, steel, rubber products and household appliances. As a result, general economic activity, as in many other industrially-developed states, tends to be more cyclical than in some other states and in the nation as a whole. Agriculture also is an important segment of the economy, with over half the State's area devoted to farming and approximately 20% of total employment is in agribusiness.

In prior years, the State's overall unemployment rate was commonly somewhat higher than the national figure. For example, the reported 1990 average monthly State rate was 5.7%, compared to the 5.5% national figure. However, for both 1991 and 1992 the State rate below the nationals (6.4% and 7.2%) were rates (6.7% and 7.4%). The unemployment rate, and its effects vary among particular geographic areas of the State.

There can be no assurance that future national, regional or state-wide economic difficulties, and the resulting impact on State or local government finances generally, will not adversely affect the market value of Ohio Obligations held in the Ohio Trust portfolio or the ability of particular obligors to make timely payments of debt service on (or lease payments relating to) those Obligations.

The State operates on the basis of a fiscal biennium for its appropriations and expenditures, and is precluded by law from ending its July 1 to June 30 fiscal year (FY) or fiscal biennium in a deficit position. Most State operations are financed through the General Revenue Fund (GRF), for which personal income and sales-use taxes are the major sources. Growth and depletion of GRF ending fund balances show a consistent pattern related to national economic conditions, with the FY-ending balance reduced during less favorable and increased during more favorable economic periods. The State has well-established procedures for, and has timely taken, necessary actions to ensure a resource/expenditure balances during less favorable economic periods. These procedures include general and selected reductions in appropriations spending.

Key biennium ending fund balances at June 30, 1989 were \$475.1 million in the GRF and \$353 million in the Budget Stabilization Fund (BSF, a cash and budgetary management fund). In FYs 1990-91, necessary corrective steps were taken to respond to lower receipts and higher expenditures in certain categories than earlier estimated. Those steps included selected reductions in appropriations spending and the transfer of \$64 million from the BSF to the GRF. The State reported June 30, 1991 ending fund balances of \$135.3 million (GRF) and \$300 million (BSF).

To allow time to certain Senate and House budget differences for the latest complete biennium that began July 1, 1991, an interim appropriations act was enacted effective July 1, 1991; it included State debt service and lease rental GRF appropriations for the entire 1992-93 biennium, while continuing most other appropriations for a month. The general appropriations act for the entire biennium was passed on July 11, 1991 and signed by the Governor. Pursuant to it, \$200 million was transferred from the BSF to the GRF in FY 1992.

Based on updated FY financial results and the economic forecast in the course of FY 1992, both in light of the continuing uncertain nationwide economic situation, there was projected and timely addressed an FY 1992 imbalance in GRF resources and expenditures. GRF receipts significantly below original forecasts primarily from lower collections of certain taxes, particularly sales and use taxes and personal income taxes. Higher expenditure levels resulted from higher spending in certain areas, particularly human services including Medicaid. As an initial action, the Governor ordered most State agencies to reduce GRF appropriations spending in the final six months of the FY 1992 by a total of approximately \$184 million. As authorized by the General Assembly, the \$100.4 million BSF balance and additional amounts from certain other funds, were transferred late in the FY to the GRF, and adjustments in the timing of certain tax payments made. Other administrative revenue and spending actions resolved the remaining GRF imbalance.

A significant GRF shortfall (approximately \$520 million) was then projected for FY 1993. It was addressed by appropriate legislative and administrative actions. As a first step the Governor ordered, effective July 1, 1992, \$300 million in selected GRF spending reductions. Executive and legislative action in December 1992--a combination of tax revisions and additional appropriations spending reductions--resulted in a balance of GRF resources and expenditures in the 1992-93 biennium. The State reported an ending GRF fund balance at June 30, 1993 of approximately \$111 million, and, as a first step to BSF replenishment, OBM has deposited \$21 million in the BSF.

No spending reductions were applied to appropriations needed for debt service



or lease rentals on any State obligations.

The GRF appropriations act for the current 1994-95 biennium was passed and signed by the Governor on July 1, 1993. It includes all necessary GRF appropriations for biennial State debt service and lease rental payments.

The State's incurrence or assumption of debt without a vote of the people is, with limited exceptions, prohibited by current State Constitutional provisions. The State may incur debt to cover casual deficits or failures in revenues or to meet expenses not otherwise provided for. The Constitution expressly precludes the State from assuming the debts of any local government or corporation. (An exception in both cases is for any debt incurred to repel invasion, suppress insurrection or defend the State in war).

By 13 constitutional amendments, the last adopted in 1993, Ohio voters have authorized the incurrence of State debt to which taxes or excises were pledged. At December 7, 1993, \$596.6 million (excluding certain highway bonds payable primarily from highway use charges) of this debt was outstanding or awaiting delivery. The only such State debt then still authorized to be incurred are portions of the highway bonds, and the following: (a) up to \$100 million of obligations for coal research and development may be outstanding at any one time (\$47.1 million outstanding); (b) \$1.2 billion of obligations authorized for local infrastructure improvements, no more than \$120 million may be issued in any calendar year (\$525.2 million outstanding, \$600 million remaining to be issued); and (c) up to \$200 million in general obligation bonds for parks and recreation purposes may be outstanding at any one time (no more than \$50 million to be issued in any one year, and none have been issued).

The Constitution also authorizes the issuance of State obligations for certain purposes, the owners of which do not have the right to have excises or taxes levied to pay debt service. Those special obligations include obligations issued by the Ohio Public Facilities Commission and the Ohio Building Authority; \$4.14 billion of were outstanding or awaiting delivery at December 7, 1993.

A 1990 constitutional amendment authorizes greater State and political subdivision participation (including financing) in the provision of housing. The General Assembly may for that purpose authorize the issuance of State obligations secured by a pledge of all or such portion as it authorizes of State revenues or receipts (but not by a pledge of the State's full faith and credit).

State and local agencies issue revenue obligations that are payable from revenues from or relating to certain facilities (but not from taxes). By judicial interpretation, these obligations are not "debt" within constitutional provisions. In general, payment obligations under lease-purchase agreements of Ohio public agencies (in which certificates of participation may be issued) are limited in duration to the issuer's fiscal period, and are renewable only upon appropriations being made available for the subsequent fiscal period.

Local school districts in Ohio receive a major portion (on a state-wide basis, recently approximately 46%) of their operating moneys from State subsidies, but are dependent on local property taxes, and in 97 districts from voter-authorized income taxes, for significant portions of their budgets. Litigation, similar to that in other states, is pending questioning the constitutionality of Ohio's system of school funding. A small number of the State's 612 local school districts have in any year required special assistance to avoid year-end deficits. A current program provides for school district cash need borrowing directly from commercial lenders, with diversion of State subsidy distributions to repayment if needed; in FY 1991 under this program 26 districts borrowed a total of \$41.8 million (including over \$27 million by one district), and in FY 1992 borrowings totaled \$68.6 million (including \$46.6 million for one district). FY 1993 loans totalled \$94.5 million for 43 districts (including \$75 million for one).

Ohio's 943 incorporated cities and villages rely primarily on property and municipal income taxes for their operations, and, with other local governments, receive local government support and property tax relief moneys distributed by the State. For those few municipalities that on occasion have faced significant financial problems, there are statutory procedures for a joint State/local commission to monitor the municipality's fiscal affairs, and for development of a financial plan to eliminate deficits and cure any defaults. Since inception in 1979, these procedures have been applied to 23 cities and villages; for 18 of them the fiscal situation was resolved and the procedures terminated.

At present the State itself does not levy any ad valorem taxes on real or tangible personal property. Those taxes are levied by political subdivisions and other local taxing districts. The Constitution has since 1934 limited the amount of the aggregate levy (including a levy for unvoted general obligations) of property taxes by all overlapping subdivisions, without a vote of the electors or a municipal charter provision, to 1% of true value in



money, and statutes limit the amount of that aggregate levy to 10 mills per \$1 of assessed valuation (commonly referred to as the "ten-mill limitation"). Voted general obligations of subdivisions are payable from property taxes unlimited as to amount or rate.

Commencing in 1985, Ohio municipalities may be permitted under Ohio law to subject interest on certain of the obligations held by the Ohio Trust to income Taxes imposed on their residents and entities doing business therein.

At the time of the closing for each Ohio Trust, Special Council to each Ohio Trust for Ohio tax matters rendered an opinion under then existing Ohio income tax law applicable to taxpayers whose income is subject to Ohio income taxation substantially to the effect that:

The Ohio Trust is not taxable as a corporation or otherwise for purposes of the Ohio personal income tax, the Ohio corporation franchise tax or the Ohio dealers in intangibles tax.

Income of an Ohio Trust will be treated as the income of the Unitholders for purposes of the Ohio personal income tax, Ohio municipal income taxes and the Ohio corporation franchise tax in proportion to the respective interest therein of each Unitholder.

Interest on obligations issued by or on behalf of the State of Ohio, political subdivisions thereof, or agencies or instrumentalities thereof ("Ohio Obligations"), or by the governments of Puerto Rico, the Virgin Islands or Guam ("Territorial Obligations") held by the Trust is exempt from the Ohio personal income tax, Ohio municipal income taxes and Ohio school district income taxes, and is excluded from the net income base of the Ohio corporation franchise tax when distributed or deemed distributed to Unitholders.

Proceeds paid to the Ohio Trust under insurance policies representing maturing interest on defaulted obligations held by the Ohio Trust will be exempt from Ohio income tax, Ohio municipal income taxes and the net income base of the Ohio corporation franchise tax if, and to the same extent as, such interest would be exempt from such taxes if paid directly by the issuer of such obligations.

Gains and losses realized on the sale, exchange or other disposition by the Ohio Trust of Ohio Obligations are excluded in determining adjusted gross and taxable income for purposes of the Ohio personal income tax, Ohio municipal income taxes and Ohio school district income taxes, and are excluded from the net income base of the Ohio corporation franchise tax when distributed or deemed distributed to Unitholders.

#### Oregon Trusts

Oregon's nonagricultural employment growth in 1988 exceeded the United States' rate for the third consecutive year. While the decade of 1970 to 1980 marked a time of rapid growth, the early years of the 1980s were a period of retrenchment and job losses. Oregon finally regained prerecessionary nonagricultural employment levels (compared to 1979) in 1986, and continued growing quickly through 1988.

The service and retail and wholesale trade sectors have contributed most of the job gains. In 1979, services comprised 18 percent and retail and wholesale trade 24 percent of total nonagricultural employment. Manufacturing contributed 22 percent. By 1988, services grew to 23 percent, retail and wholesale trade rose to 25 percent, but manufacturing shrank to 19 percent. During the period 1979 to 1988, services and retail and wholesale trade added 110,000 jobs while manufacturing jobs dropped by 14,000.

Total state population and personal income followed similar trends. From 1975 to 1980, both population and personal income exceeded national growth rates. In the late 1970s, Oregon's population grew at a rate of two to three times the national average. The early 1980s marked a reversal of this trend, and population and personal income growth slowed to rates below the national average.

Recent economic trends have been favorable. In early 1987, the State's unemployment rate dipped below the national rate, and State employment growth exceeded the national average. Increased demand for wood products, primary metals, and machinery and rapidly growing nonmanufacturing sectors helped push the growth rates upward.

A mild climate, varied topography and rich soil support the nearly 100 agricultural commodities grown in Oregon and valued in terms of gross farm sales at over \$2.3 billion in 1988. Much of this agricultural activity occurs in the Willamette River Valley in the western portion of the State. This valley also contains most of the State's population and much of the manufacturing activity.

Portland, located at the confluence of the Columbia and Willamette Rivers, remains Oregon's largest city and the hub of economic activity. The greater

Portland area is a highly diversified manufacturing center. It is also the home of the Port of Portland, a significant seaport for trade between the western United States and the Pacific Rim nations.

Outside the Willamette Valley, those areas not devoted primarily to agriculture rely on the wood products industry and tourism. Although the wood products industry is still sensitive to economic fluctuations, increased automation and improved management are enabling the industry to reach all-time high production levels with fewer workers.

Oregon's economy grew moderately in the two decades immediately following World War II. From 1950 to 1970, nonagricultural employment growth averaged 2.7 percent per year. In the 1970s, however, the State experienced rapid growth as population increased and economic diversification continued. Oregon's growth significantly outpaced the national average: from 1975 to 1980 nonagricultural employment growth averaged 6.1 percent per year and per capita income rose above the U.S. average.

The early 1980s recessions hit Oregon hard. In 1982, nonagricultural employment fell by 5.7 percent with much of the loss from the wood products industry. Oregon remains slightly more sensitive to economic cycles than the national average due to the forest products component of its economy. Although recessionary periods continue to be somewhat more pronounced in Oregon than in the nation as a whole, the higher proportion of nonmanufacturing jobs and restructuring of the lumber and wood industry has provided more stability.

While the high technology industries added a significant number of jobs in the late 1970s and early 1980s, the State has followed national trends and lost jobs as a result of a slump in the semi-conductor, electronics and instruments industries. In recent years, these industries have stabilized and started adding workers.

The high interest rates experienced early in the 1980s had a significant impact on certain sectors of the Oregon economy. The recession-sensitive wood products, housing, and construction industries were particularly hard hit. Rural counties of eastern and southern Oregon which depend on one or a combination of these industries experienced the greatest impact. Many of these counties have since diversified more and have benefited significantly from improved tourism traffic. In urban areas generally, and in Portland in particular, the diverse economic base has given a measure of insulation from the impacts of the recession.

By 1984, the State began to recover and experienced a higher employment growth rate at 4.2 percent, but this rate was still lower than the U.S. rate. The State finally surpassed prerecessionary employment levels in 1986 and has recently been growing faster than the U.S. average.

Tourism has been strong throughout the 1980s, due in part to the plentiful supplies of relatively low-cost automobile fuel and improved national economy. Oregon's wood products industry is undergoing a permanent restructuring, as many mills have automated and improved their productivity greatly. The State has committed itself to greater diversification of the economy by pursuing more foreign trade in the considerable markets of the Pacific Rim countries.

Between 1979 and 1988, total nonagricultural wage and salary employment in Oregon rose from 1,056,200 to 1,152,300, an increase of 9.1 percent. During this period, however, employment exhibited three different trends.

In 1979, a dramatic rise in interest rates severely hurt credit-sensitive industries such as construction and lumber and wood products and plunged the Nation into the worst recession since the 1930s. Oregon's housing-dependent economy was especially hard hit. Between 1979 and 1982, wage and salary employment plummeted by 9 percent to 960,000, a loss of 95,400 jobs.

While the severity of the recession eliminated many jobs, both in manufacturing (42,800) and non-manufacturing (52,600), it also caused interest rates and the inflation rate eventually to drop significantly. This improvement, plus more stimulative federal monetary and fiscal policies, set the stage for another period of economic expansion beginning in early 1983. In the six year period between 1982 and 1988, Oregon's wage and salary employment increased by 20 percent to reach a new all-time high of 1,152,300, a gain of 191,500 jobs.

The current expansion differs from previous recovery periods. During the last six years, manufacturing employment has risen by 28,600 jobs but is still about 14,200 below its 1979 pre-recession peak of 228,500. This slow rate of recovery largely reflects increased competition from foreign imports, automation and increased productivity. In the first half of the 1980s, the rising foreign exchange value of the dollar made U.S. exported goods more expensive overseas, while foreign imports became cheaper to U.S. consumers. Although the dollar's exchange value has been falling since 1985, imports have captured a greater share of U.S. markets. Manufacturing firms in Oregon and the Nation have responded by reducing their costs, restructuring their operations and automating production processes wherever possible. In some

cases, these efficiencies have resulted in few jobs even though production volumes have recovered and reached new all-time highs. Oregon's primary industry, lumber and wood products, is one such example.

About 85 percent of the 191,500 new wage and salary jobs added in the 1982-1988 period came in non-manufacturing. Although every non-manufacturing industrial category except mining, communications and utilities increased employment, the service and trade industries accounted for eight out of every ten new non-manufacturing jobs. Job growth was especially strong in food stores, eating and drinking places, health care and business services.

In its 1989 Regular Session, the Oregon Legislature approved General Fund appropriations totaling \$4,585,476,617 for the 1989-1991 biennium. This is a 22 percent increase compared to estimated 1987-1989 expenditures.

A complete analysis of State General Fund finances for 1989-1991 will not be available until after the impact of all legislative actions affecting expenditures are compiled.

The following is a summary of the September 1, 1989 quarterly Economic and Revenue Forecast required by ORS 291.342.

The much heralded "soft landing" scenario appears the most likely course for the U.S. economy over the short term. Such a scenario implies an extended period of lower growth, an easing of inflationary pressures, and little improvement in the unemployment rate. The greatest short-term risk to the soft landing is overreaction by the Federal Reserve in easing credit. Easing would stimulate growth and a rise in inflation in the shortrun, which would later induce Federal tightening and plunge the economy into a recession.

In late 1989 and early 1990, the anticipated soft landing will reduce employment growth in Oregon and the U.S. Overall, Oregon employment is expected to increase by 13,600 over the next year (second quarter to second quarter), and 7,700 over the following year. This means that, relative to the May forecast, 3,100 fewer jobs will be generated in the next year. Still, employment growth in Oregon is expected to exceed gains nationwide in 1989.

The primary reasons for the slowdown in Oregon are: (1) expected timber supply reductions, which will directly reduce lumber and wood products and transportation employment; (2) a gradual slowdown in construction, as apartment vacancy rates begin to rise and Oregon's population growth rate begins to slow; and (3) the ending of Oregon's retail trade boom, which brought increased competition in the form of many new retail chains and stores to Oregon.

Total Oregon employment increased by 8,400 in the second quarter, 1,200 less than anticipated in the May 1989 forecast. Manufacturing employment increased by 700, while non-manufacturing employment increased by 7,700.

Total General Fund collections in 1987-1989 were \$49.4 million above the May 15 forecast and \$211.4 million above the estimate made at the close of the 1987 Regular Session. Both Corporate Excise and Income Tax receipts and all other General Fund revenues exceeded the close of Regular Session estimate by more than two percent. Therefore, ORS 291.349 (known as the "two percent kicker" law) requires that all unanticipated revenues be returned to the taxpayers. Corporate income taxpayers will receive a 19.7 percent credit on their tax year 1989 liabilities to return the \$36.2 million in unanticipated Corporate Excise and Income Tax revenues. Personal income taxpayers will receive a 9.8 percent credit on their tax year 1989 liabilities to return unanticipated receipts of \$175.2 million from all noncorporate General Fund revenue sources.

More than 40 bills passed by the 1989 Legislature changed expected General Fund revenue receipts. Altogether, these bills raised expected 1989-1991 receipts by \$25.4 million, with expected Personal Income Taxes increasing \$29.9 million, Corporate Excise and Income Taxes increasing by \$4.9 million, and all other General Fund revenues decreasing by \$9.4 million. The Legislature appropriated \$4,585.5 million for the 1989-1991 period, leaving an ending balance of \$121.7 million.

The September General Fund revenue forecast anticipates that the State will receive \$9.6 million more during 1989-1991 than was anticipated at the close of the 1989 Regular Session. This, combined with the surge in 1987-1989 revenues, pushes the expected 1989-1991 ending balance to \$181.0 million.

The September Personal Income Tax forecast for 1989-1991 has been increased by \$39.8 million because the high final payments individuals made during the 1989 filing season are expected to continue. The Corporate Excise and Income Tax forecast has been lowered by \$10.2 million, again reflecting receipts during the critical April filing season. Expected Insurance Tax receipts have been decreased by \$21.4 million because of an unanticipated weakening in commercial insurance premiums.

The foregoing information constitutes only a brief summary of some of the

financial difficulties which may impact certain issuers of Bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers in the Oregon Trust are subject. Additionally, many factors including national economic, social and environmental policies and conditions, which are not within the control of the issuers of Bonds, could affect or could have an adverse impact on the financial condition of the State and various agencies and political subdivisions located in the State. The Sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Oregon Trust to pay interest on or principal of the Bonds.

The assets of the Oregon Trust will consist of interest-bearing obligations issued by or on behalf of the State of Oregon (the "State") or counties, municipalities, authorities or political subdivisions thereof (the "Oregon Bonds") or by the Commonwealth of Puerto Rico, Guam and the United States Virgin Islands (the "Possession Bonds") (collectively, the "Bonds"). Neither the Sponsor nor its counsel have independently examined the Bonds to be deposited in and held in the Oregon Quality Trust. However, although no opinion is expressed herein regarding such matters, it is assumed that: (i) the Bonds were validly issued; (ii) the interest thereon is excludible from gross income for federal income tax purposes; and (iii) interest on the Bonds, if received directly by an Oregon Unitholder, would be exempt from the Oregon income tax applicable to individuals (the "Oregon Personal Income Tax").

At the time of the closing for each Oregon Trust, Special Counsel to each Oregon Trust for Oregon tax matters rendered an opinion under then existing Oregon income tax law applicable to taxpayers whose income is subject to Oregon income taxation substantially to the effect that:

The Oregon Trust is not an association taxable as a corporation and based upon an administrative rule of the Oregon State Department Revenue, each Oregon Unitholder of the Oregon Trust will be essentially treated as the owner of a pro rata portion of the Oregon Trust and the income of such portion of the Oregon Trust will be treated as the income of the Oregon Unitholder for Oregon Personal Income Tax purposes;

Interest on the Bonds which is exempt from the Oregon Personal Income Tax when received by the Oregon Trust, and which would be exempt from the Oregon Personal Income Tax if received directly by an Oregon Unitholder, will retain its status as exempt from such tax when received by the Oregon Trust and distributed to an Oregon Unitholder;

To the extent that interest derived from the Oregon Trust by a Unitholder with respect to the Possession Bonds is excludable from gross income for Federal income tax purposes pursuant to 48 U.S.C. Section 745, 48 U.S.C. Section 1423a and 48 U.S.C. Section 1403, such interest will not be subject to the Oregon Personal Income Tax. Each Unitholder of the Oregon Trust will recognize gain or loss for Oregon Personal Income Tax purposes if the Trustee disposes of a bond (whether by redemption, sale or otherwise) or if the Unitholder redeems or sells Units of the Oregon Trust to the extent that such a transaction results in a recognized gain or loss to such Unitholder for Federal income tax purposes; and

The Oregon Personal Income Tax does not permit a deduction of interest paid or incurred on indebtedness incurred or continued to purchase or carry Units in the Oregon Trust, the interest on which is exempt from such Tax.

Investors should consult their tax advisors regarding collateral tax consequences under Oregon law relating to the ownership of the Units, including, but not limited to, the calculation of "net pension income" tax credits for retirees and the applicability of other Oregon taxes.

We have not examined any of the Bonds to be deposited and held in the Oregon Trust or the proceedings for the issuance thereof or the opinions of bond counsel with respect thereto and therefore express no opinion as to the exemption from the Oregon Personal Income Tax of interest on the Bonds if received directly by an Oregon Unitholder. In addition, prospective purchasers subject to the Oregon corporate income tax should be advised that for purposes of the Oregon Corporate Income (Excise) Tax, interest on the Bonds received by the Trust and distributed to a Unitholder subject to such tax will be added to the corporate Unitholder's federal taxable income and therefore will be taxable.

#### Pennsylvania Trusts

Investors should be aware of certain factors that might affect the financial conditions of the Commonwealth of Pennsylvania. Pennsylvania historically has been identified as a heavy industry state although that reputation has changed recently as the industrial composition of the Commonwealth diversified when the coal, steel and railroad industries began to decline. The major new sources of growth in Pennsylvania are in the service sector, including trade, medical and the health services, education and financial institutions. Pennsylvania's agricultural industries are also an important component of the

Commonwealth's economic structure, accounting for more than \$3.6 billion in crop and livestock products annually, while agribusiness and food related industries support \$38 billion in economic activity annually.

Back to back recessions in the early 1980's reduced the manufacturing sector's employment levels moderately during 1980 and 1981, sharply during 1982, and even further in 1983. Non-manufacturing employment has increased steadily since 1980 to its 1992 level of 81.3 percent of total Commonwealth employment. Consequently, manufacturing employment constitutes a diminished share of total employment within the Commonwealth. Manufacturing, contributing 18.7 percent of 1992 non-agricultural employment, has fallen behind both the services sector and the trade sector as the largest single source of employment within the Commonwealth. In 1992 the services sector accounted for 29.3 percent of all non-agricultural employment while the trade sector accounted for 22.7 percent.

From 1983 to 1989, Pennsylvania's annual average unemployment rate dropped from 11.8 percent to 4.5 percent, falling below the national rate in 1986 for the first time in over a decade. Pennsylvania's annual average unemployment rate remained below the national average from 1986 until 1990. Slower economic growth caused the unemployment rate in the Commonwealth to rise to 6.9 percent in 1991 and 7.5 percent in 1992. In April 1993 the seasonally adjusted unemployment rate for the Commonwealth was 6.6 percent compared to 7.0 percent for the United States.

It should be noted that the creditworthiness of obligations issued by local Pennsylvania issuers may be unrelated to the creditworthiness of obligations issued by the Commonwealth of Pennsylvania, and there is no obligation on the part of the Commonwealth to make payment on such local obligations in the event of default.

Financial information for the General Fund is maintained on a budgetary basis of accounting. A budgetary basis of accounting is used for the purpose of ensuring compliance with the enacted operating budget and is governed by applicable statutes of the Commonwealth and by administrative procedures. The Commonwealth also prepares annual financial statements in accordance with generally accepted accounting principles ("GAAP"). The budgetary basis financial information maintained by the Commonwealth to monitor and enforce budgetary control is adjusted at fiscal year-end to reflect appropriate accruals for financial reporting in conformity with GAAP.

Fiscal 1991 Financial Results. GAAP Basis: During fiscal 1991 the General Fund experienced an \$861.2 million operating deficit resulting in a fund balance deficit of \$980.9 million at June 30, 1991. The operating deficit was a consequence of the effect of a national recession that restrained budget revenues and pushed expenditures above budgeted levels. At June 30, 1991, a negative unreserved-undesignated balance of \$1,146.2 million was reported. During fiscal 1991 the balance in the Tax Stabilization Reserve Fund was used to maintain vital state spending and only a minimal balance remains in that fund.

Budgetary Basis: A deficit of \$453.6 million was recorded by the General Fund at June 30, 1991. The deficit was a consequence of higher than budgeted expenditures and lower than estimated revenues during the fiscal year brought about by the national economic recession that began during the fiscal year. A number of actions were taken throughout the fiscal year by the Commonwealth to mitigate the effects of the recession on budget revenues and expenditures. Actions taken, together with normal appropriation lapses, produced \$871 million in expenditure reductions and revenue increases for the fiscal year. The most significant of these actions were a \$214 million transfer from the Pennsylvania Industrial Development Authority, a \$134 million transfer from the Tax Stabilization Reserve Fund, and a pooled financing program to match federal Medicaid funds replacing \$145 million of state funds.

Fiscal 1992 Financial ResultsGAAP Basis. During fiscal 1992 the General Fund reported a \$1.1 billion operating surplus. This operating surplus was achieved through legislated tax rate increases and tax base broadening measures enacted in August 1991 and by controlling expenditures through numerous cost reduction measures implemented throughout the fiscal year. As a result of the fiscal 1992 operating surplus, the fund balance has increased to \$87.5 million and the unreserved-undesignated deficit has dropped to \$138.6 million from its fiscal 1991 level of \$1,146.2 million.

Budgetary Basis: Eliminating the budget deficit carried into fiscal 1992 from fiscal 1991 and providing revenues for fiscal 1992 budgeted expenditures required tax revisions that are estimated to have increased receipts for the 1992 fiscal year by over \$2.7 billion. Total revenues for the fiscal year were \$14,516.8 million, a \$2,654.5 million increase over cash revenues during fiscal 1991. Originally based on forecasts for an economic recovery, the budget revenue estimates were revised downward during the fiscal year to reflect continued recessionary economic activity. Largely due to the tax revisions enacted for the budget, corporate tax receipts totalled \$3,761.2 million, up from \$2,656.3 million in fiscal 1991, sales tax receipts increased by \$302 million to \$4,499.7 million, and personal income tax receipts totalled

\$4,807.4 million, an increase of \$1,443.8 million over receipts in fiscal 1991.

As a result of the lowered revenue estimate during the fiscal year, increased emphasis was placed on restraining expenditure growth and reducing expenditure levels. A number of cost reductions were implemented during the fiscal year and contributed to \$296.8 million of appropriation lapses. These appropriation lapses were responsible for the \$8.8 million surplus at fiscal year-end, after accounting for the required ten percent transfer of the surplus to the Tax Stabilization Reserve Fund.

Spending increases in the fiscal 1992 budget were largely accounted for by increases for education, social services and corrections programs. Commonwealth funds for the support of public schools were increased by 9.8 percent to provide a \$438 million increase to \$4.9 billion for fiscal 1992. The fiscal 1992 budget provided additional funds for basic and special education and included provisions designed to help restrain the annual increase of special education costs, an area of recent rapid cost increases. Child welfare appropriations supporting county operated child welfare programs were increased \$67 million, more than 31.5 percent over fiscal 1991. Other social service areas such as medical and cash assistance also received significant funding increases as costs have risen quickly as a result of the economic recession and high inflation rates of medical care costs. The costs of corrections programs, reflecting the marked increase in the prisoner population, increased by 12 percent. Economic development efforts, largely funded from bond proceeds in fiscal 1991, were continued with General Fund appropriations for fiscal 1992.

The budget included the use of several Medicaid pooled financing transactions. These pooling transactions replaced \$135 million of Commonwealth funds, allowing total spending under the budget to increase by an equal amount.

Fiscal 1993 Budget. The latest budget estimates project expenditures from Commonwealth funds for fiscal 1993 to be \$13.857 billion, representing only a \$5.2 million increase over fiscal 1992 expenditures. The fiscal 1993 budget is balanced within the official revenue estimate and a planned draw-down of the \$8.8 million beginning budgetary basis surplus carried forward from Fiscal 1992. The Fiscal 1993 budget was amended on May 28, 1993, through the enactment of \$165.1 million of supplemental appropriations. This small increase in expenditures is the result of revenues being constrained by a personal income tax rate reduction effective July 1, 1992, a low rate of economic growth, higher tax refund reserves to cushion against adverse decisions on pending tax litigations, and the receipt of Federal funds for expenditures previously paid out of Commonwealth funds. The amended fiscal 1993 budget restored partial funding for private educational institutions that normally receive state appropriations but whose appropriations were item-vetoed by the Governor from the originally adopted fiscal 1993 budget. Also restored by the amended budget were certain grants to the counties to help pay operating costs of the local judicial system.

Commonwealth revenue sources are estimated for the fiscal 1993 budget to total \$14.592 billion, a \$74.9 million increase over actual fiscal 1992 revenues, representing an increase of approximately one-half of one percent. The projected low revenue growth for fiscal 1993 is caused by the Commonwealth's expectation that current weak growth in employment, consumer income, and retail sales will continue, and by the reduction in the personal income tax rate from 3.1 percent to 2.8 percent on July 1, 1992. In addition, tax refund reserves were increased \$209.0 million to \$548.0 million for fiscal 1993 to allow for potential tax refunds that might be payable from any adverse judicial decision in a number of pending tax litigations. In January 1993, the refund estimate was reduced to \$530 million.

Through May 1993, fiscal 1993 total General Fund revenue collections were \$7.1 million (0.05 percent) above estimate, as fiscal year-to-date shortfalls in receipts of corporation taxes (\$30.3 million) and personal income tax (\$37.2 million) were offset mainly by above estimate sales tax and miscellaneous revenue collections.

Fiscal 1994 Budget (Budgetary Basis). The enacted 1994 fiscal year budget provides for \$14.999 billion of appropriations of Commonwealth funds. The largest increase in appropriations is for the Department of Public Welfare-\$235 million-to meet the increasing costs of medical care and rising case loads. Other large increases are education \$196 million-including \$130 million to increase state educational subsidies for the most needy school districts and \$104 million for correctional institutions to pay operating costs and lease payments for five new prisons and to expand the capacity of two existing facilities.

The budget estimates revenue growth of 4.0 percent over revised fiscal 1993 estimates. The revenue estimate is based on an expectation of continued economic recovery, but at a slow rate. Sale tax receipts are projected to rise 5.1 percent over the fiscal 1993 estimate while personal income tax receipts are projected to increase by 2.4 percent, a rate that is low because of the tax rate reduction in July 1992.



All outstanding general obligation bonds of the Commonwealth are rated AA by S&P and A1 by Moody's.

Any explanation concerning the significance of such ratings must be obtained from the rating agencies. There is no assurance that any ratings will continue for any period of time or that they will not be revised or withdrawn.

The City of Philadelphia is the largest city in the Commonwealth with an estimated population of 1,585,577 according to the 1990 Census. Philadelphia functions both as a City and a first-class county for the purpose of administering various governmental programs.

Legislation providing for the establishment of the Pennsylvania Intergovernmental Cooperation Authority ("PICA") to assist first class cities in remedying fiscal emergencies was enacted by the General Assembly and approved by the Governor in June 1991. PICA is designed to provide assistance through the issuance of funding debt to liquidate budget deficits and to make factual findings and recommendations to the assisted city concerning its budgetary and fiscal affairs. An intergovernmental cooperation agreement between Philadelphia and PICA was approved by City Counsel on January 3, 1992, and approved by the PICA Board and signed by the Mayor on January 8, 1992. At this time, Philadelphia is operating under a revised five-year plan approved by PICA on April 6, 1992. Full implementation of the five-year plan was delayed due to labor negotiations that were not completed until October 1992, three months after the expiration of the old labor contracts. The terms of the new labor contracts are estimated to cost approximately \$144.0 million more than what was budgeted in the original five-year plan. The Mayor and his Administration have amended the plan to bring it back in balance and their plan is presently being considered by PICA and City Council.

In June 1992, PICA issued \$474,555,000 of its Special Tax Revenue Bonds to provide financial assistance to Philadelphia and to liquidate the cumulative General Fund balance deficit. In March 1993, Philadelphia filed an amended five-year plan with PICA, in which the General Fund balance deficit for the Fiscal Year ended June 30, 1993, is projected to be \$6.6 million. The fiscal 1994 budget, approved by City Council, projects no deficit and a balanced budget for the year ending June 30, 1994. PICA approved the fiscal 1994 budget plan on April 14, 1993.

As of the date hereof, the ratings on the City's long-term obligations supported by payments from the City's General Fund are rated Ba by Moody's and B by S&P. Any explanation concerning the significance of such ratings must be obtained from the rating agencies. There is no assurance that any ratings will continue for any period of time or that they will not be revised or withdrawn.

The foregoing information constitutes only a brief summary of some of the financial difficulties which may impact certain issuers of bonds and does not purport to be a complete or exhaustive description of all adverse conditions to which the issuers of the Bonds in the Pennsylvania Trust are subject. Additionally, many factors including national economic, social and environmental policies and conditions, which are not within the control of the issuers of Bonds, could have an adverse impact on the financial condition of the State and various agencies and political subdivisions located in the State. The sponsor is unable to predict whether or to what extent such factors or other factors may affect the issuers of Bonds, the market value or marketability of the Bonds or the ability of the respective issuers of the Bonds acquired by the Pennsylvania Trust to pay interest on or principal of the Bonds.

At the time of the closing for each Pennsylvania Trust, Special Counsel to each Pennsylvania Trust for Pennsylvania tax matters rendered an opinion under then existing Pennsylvania income tax law applicable to taxpayers whose income is subject to Pennsylvania income taxation substantially to the effect that:

Units evidencing fractional undivided interest in the Pennsylvania Trust, which are represented by obligations issued by the Commonwealth of Pennsylvania, any public authority, commission, board or other agency created by the Commonwealth of Pennsylvania, any political subdivision of the Commonwealth of Pennsylvania or any public authority created by any such political subdivision are not taxable under any of the personal property taxes presently in effect in Pennsylvania;

distributions of interest income to Unitholders are not subject to personal income tax under the Pennsylvania Tax Reform Code of 1971; nor will such interest be taxable under the Philadelphia School District Investment Income Tax imposed on Philadelphia resident individuals;

a Unitholder may have a taxable event under the Pennsylvania state and local income taxes referred to in the preceding paragraph upon the redemption or sale of his Units but not upon the disposition of any of the Securities in a Pennsylvania Trust to which the Unitholder's Units relate; Units will be taxable under the Pennsylvania inheritance and estate taxes;

Units are subject to Pennsylvania inheritance and estate taxes;

a Unitholder which is a corporation may have a taxable event under the Pennsylvania Corporate Net Income Tax when it redeems or sells its Units. Interest income distributed to Unitholders which are corporations is not subject to Pennsylvania Corporate Net Income Tax or Mutual Thrift Institutions Tax. However, banks, title insurance companies and trust companies may be required to take the value of the Units into account in determining the taxable value of their Shares subject to Shares Tax;

any proceeds paid under the insurance policy issued to the Trustee or obtained by the issuers of the Bonds with respect to the Bonds which represent maturing interest on defaulted obligations held by the Trustee will be excludable from Pennsylvania gross income if, and to the same extent as, such interest would have been so excludable if paid by the issuer of the defaulted obligations; and

the Fund is not taxable as a corporation under Pennsylvania tax laws applicable to corporations.

In rendering its opinion, Special Counsel has not, for timing reasons, made an independent review of proceedings related to the issuance of the Bonds. It has relied on Van Kampen Merritt Inc. for assurance that the Bonds have been issued by the Commonwealth of Pennsylvania or by or on behalf of municipalities or other governmental agencies within the Commonwealth.

#### South Carolina Trusts

Although all or most of the Bonds in the South Carolina Trust are revenue obligations or general obligations of local governments or authorities rather than general obligations of the State of South Carolina itself, there can be no assurance that any financial difficulties the State may experience will not adversely affect the market value or marketability of the Bonds or the ability of the respective obligors to pay interest on or principal of the Bonds. The information regarding the financial condition of the State is included for the purpose of providing information about general economic conditions that may affect issuers of the Bonds in South Carolina.

From the early 1920's to the present time, the State's economy has been dominated by the textile industry with over one out of every three manufacturing workers directly or indirectly related to the textile industry. While the textile industry is still the major industrial employer in the State, since 1950 the State's economy has undergone a gradual transition. The economic base of the State has diversified as the trade and service sectors developed and with the added development of the durable goods manufacturing industries, South Carolina's economy now resembles more closely that of the United States.

Personal income in the State increased by 4.2% in the fiscal year ended June 30, 1992, while that of the U.S. increased by 4.0%. For this same fiscal year, unemployment in South Carolina was 6.1%, compared with the national rate of 7.1%.

The State Constitution requires the General Assembly to provide a balanced budget and requires that if there be a deficit, such deficit shall be provided for in the succeeding fiscal year. The State Constitution also provides that the State Budget and Control Board may, if a deficit appears likely, effect such reductions in appropriations as may be necessary to prevent a deficit. At the November 6, 1984 general election there was approved a constitutional amendment providing that annual increases in State appropriations may not exceed the average growth rate of the economy of the State and that the annual increase in the number of State employees may not exceed the average growth of population of the State. The State Constitution also establishes a General Reserve Fund to be maintained in an amount equal to 4% of General Fund Revenue for the latest fiscal year. Despite the efforts of the State Budget and Control Board, deficits were experienced in each of the fiscal years ended June 30, 1981, June 30, 1982, June 30, 1985 and June 30, 1986. All deficits have been funded out of the General Reserve Fund. For the fiscal years ending June 30, 1983 and 1984, the State had cash surpluses. As of June 30, 1985 the balance in the General Fund reserve was \$89,100,000.

At its July 1985 meeting the State Budget and Control Board, acting upon advice that a shortfall in General Fund revenues for the fiscal year ending June 30, 1985 might develop, froze all supplemental appropriations pending the final accounting of the General Fund for fiscal year 1985. On August 8, 1985, the Office of the Comptroller General advised the State Budget and Control Board that General Fund expenditures for the fiscal year ended June 30, 1985 did exceed General Fund revenues by \$11,936,636. Obedient to the constitutional mandate that a casual deficit shall be provided for in the succeeding fiscal year, the State Budget and Control Board delayed certain hiring and capital improvements scheduled to be made in fiscal year 1986 in an amount sufficient to meet the fiscal year 1985 budget shortfall. In January of the fiscal year ended June 30, 1986 the State Budget and Control Board was

advised of a possible shortfall of \$46,346,968. The Board immediately reduced State agency appropriations by the amount of the anticipated shortfall. Notwithstanding this action, at the end of fiscal year 1986, it became apparent that a shortfall would result. In August of 1986, the State Budget and Control Board voted to fund the deficit by transferring \$37,353,272 from the Reserve Fund to the General Fund, bringing the balance in the Reserve Fund to \$51.8 million.

At the November 5, 1986 meeting of the Budget and Control Board, the Board of Economic Advisors advised that it had reduced its revenue estimate for the current fiscal year by \$87,434,452. As required by the provisions of the Capital Expenditure Fund, the Board applied \$27,714,661 budgeted for this fund to the anticipated shortfall. This action left a remaining shortfall of \$59,719,791 which the Budget and Control Board funded by imposing a 2.6% cut in expenditures. In a February 1987 meeting of the Board, a further cut in expenditures of 0.8% was ordered.

After net downward revisions of \$122 million in estimated revenues during the year, the actual revenue collections exceeded the final estimate by \$37 million, resulting in a surplus for the fiscal year ending June 30, 1987, of \$20.5 million. The General Reserve Fund received \$6.6 million during the year in accordance with the Appropriation Act, and \$17 million of the year-end surplus was transferred to the General Reserve Fund, bringing the balance in the General Reserve Fund to \$75.4 million at June 30, 1987.

On August 5, 1988, it was announced that for the fiscal year ending June 30, 1988, the Budgetary General Fund had a surplus of \$107.5 million. The surplus resulted from a \$117.3 million excess of revenues over expenditures. The State will use \$52.6 million of the surplus to fund supplemental appropriations, \$28.3 million to fund the Capital Reserve, and \$20.5 million for an early buy-out of a school bus lease agreement. The General Assembly will decide how the State will spend the remaining \$6.1 million.

The General Reserve Fund received \$25.1 million during the 1987-88 fiscal year in accordance with the Appropriation Act. During the year, the General Assembly reduced the required funding of the General Reserve Fund from 4% to 3% of the latest completed fiscal year's actual revenue. The General Assembly used \$14.4 million of the resulting excess to fund the 1987-1988 Supplemental Appropriation Act, leaving \$86.1 million in the General Reserve Fund at June 30, 1988. The full-funding amount at that date, however, was only \$80.8 million. In accordance with the 1988-1989 Appropriation Act, the excess of \$5.3 million will help fund 1988-1989 appropriations.

At the November 8, 1988 general election there was approved a constitutional amendment reducing from 4% to 3% the amount of General Fund revenue which must be kept in the General Reserve Fund, and removing the provisions requiring a special vote to adjust this percentage. The amendment also created a Capital Reserve Fund equal to 2% of General Fund revenue. Before March 1 of each year, the Capital Reserve Fund must be used to offset mid-year budget reductions before mandating cuts in operating appropriations, and after March 1, the Capital Reserve Fund may be appropriated by a special vote in separate legislation by the General Assembly to finance in cash previously authorized capital improvement bond projects, retire bond principal or interest on bonds previously issued, and for capital improvements or other nonrecurring purposes which must be ranked in order of priority of expenditure. Monies in the Capital Reserve Fund not appropriated or any appropriation for a particular project or item which has been reduced due to application of the monies to year-end deficit must go back to the General Fund.

For the fiscal year ended June 30, 1989, the State had a surplus of \$129,788,135. At June 30, 1989, the balance in the General Reserve Fund was \$87,999,428.

Because of anticipated revenue shortfalls for the fiscal year 1989-1990, the State Budget and Control Board committed \$42.4 million of the \$58.7 million Capital Reserve Fund in April, 1990. Lack of sufficient funding at year end resulted in an additional use of \$4.5 million from the Capital Reserve Fund. After the above reductions, the State had a fiscal year 1989-1990 surplus of \$13,159,892 which was used to fund supplemental appropriations of \$1,325,000 and the Capital Reserve Fund at \$11,834,892. At June 30, 1990, the balance in the General Reserve Fund was \$94,114,351.

During 1990-91 fiscal year, the State Budget and Control Board has approved mid-year budget changes in November of 1990 and again in February of 1991, to offset lower revenue estimates. Those changes included committing the Capital Reserve Fund appropriation (\$62,742,901) and reducing agency appropriations in an additional amount necessary to offset (together with automatic expenditure reductions that are tied to revenue levels) what would otherwise be a projected deficit of approximately \$132.6 million. On May 14 and May 21, 1991, the Budget and Control Board, responding to April revenue figures and unofficial estimates indicating an additional shortfall of \$30 to \$50 million, ordered an immediate freeze on all personnel activities, from hiring to promotions; a freeze on purchasing, with limited exceptions; and an indefinite halt to new contracts and contract renewals. The Board also asked the General

Assembly for the power to furlough government workers periodically during the next fiscal year.

In the past, the State's budgetary accounting principles allowed revenue to be recorded only when the State received the related cash. On July 30, 1991, the Budget and Control Board approved a change in this principle for sales tax revenue beginning with the fiscal year ended June 30, 1991. The Board's resolution requires that sales taxes collected by merchants in June and received by the State in July be reported as revenue in June rather than in July. This change resulted in a \$5.2 million decrease in reported 1990-91 sales tax revenue and a one-time \$83.1 million addition to fund balance. The one-time adjustment increases the fund balance to the level it would be if the new principle had been in effect in years before 1990-91. Following such action, the year-end balance in the General Reserve Fund was \$33.4 million.

At its July 30, 1991, meeting the Budget and Control Board also took action with respect to the 1991-92 fiscal year. On July 26, 1991, the Board of Economic Advisors advised the Budget and Control Board that it projected a revenue shortfall of \$148 million for the fiscal year 1991-92 budget of \$3.581 billion. In response, the Budget and Control Board eliminated the two percent (2%) Capital Reserve Fund appropriation of \$65.9 million and reduced other expenditures across the board by three percent (3%). On February 10, 1992, the Board of Economic Advisors advised the Budget and Control Board that it had revised its estimate of revenues for the current fiscal year downward by an additional \$55 million. At its February 11, 1992 meeting, the Budget and Control Board responded by imposing an additional one percent (1%) across the board reduction of expenditures (except with respect to approximately \$10 million for certain agencies.) At its February 13, 1992 meeting, the Budget and Control Board restored a portion of the one percent (1%) reduction to four (4) education-related agencies totalling approximately \$5.7 million. These expenditure reduction measures, when coupled with revenue increases projected by the Budget and Control Board, resulted in an estimated balance of approximately \$1.4 million in the General Fund for the fiscal year 1991- 92. Subsequently, the Budget and Control Board announced that the State had incurred a \$54 million deficit for fiscal year 1991-92. This deficit will be offset by the General Reserve Fund and a small amount saved by state agencies and local government, leaving the State with an estimated \$7.5 million balance for the 1991-92 fiscal year.

Responding to these recurrent operating deficits, Standard & Poor's Corp. has placed the State's AAA-rated general debt on its Credit Watch, and on January 29, 1993, this rating was reduced to AA+.

On August 22, 1992, the Budget and Control Board adopted a plan to reduce appropriations under the 1992 Appropriations Act because of revenue shortfall projections of approximately \$200 million for the 1992-93 fiscal year. These reductions were based on the rate of growth in each agency's budget over the past year. On September 15, 1992, the Supreme Court of South Carolina enjoined the Budget and Control Board from implementing its proposed plan for budget reductions on the grounds that the Board had authority to make budget reductions only across the board based on total appropriations. In response to this decision, the Board instituted a 4% across the board reduction which, together with funds from the Capital Reserve Fund, was sufficient to balance the budget for the current fiscal year.

Prospective investors should study with care the portfolio of Bonds in the South Carolina Trust and should consult with their investment advisers as to the merits of particular issues in the portfolio.

At the time of the closing for each South Carolina Trust, Special Counsel for each South Carolina Trust for South Carolina tax matters rendered an opinion under then existing South Carolina income tax law applicable to taxpayers whose income is subject to South Carolina income taxation substantially to the effect that:

By the provision of paragraph (j) of Section 3 of Article 10 of the South Carolina Constitution (revised 1977) intangible personal property is specifically exempted from any and all ad valorem taxation;

Pursuant to the provisions of Section 12-1-60 the interest of all bonds, notes or certificates of indebtedness issued by or on behalf of the State of South Carolina and any authority, agency, department or institution of the State and all counties, school districts, municipalities, divisions and subdivisions of the State and all agencies thereof are exempt from income taxes and that the exemption so granted extends to all recipients of interest paid thereon through the Trust. (This opinion does not extend to so-called 63-20 obligations);

The income of the Trust would be treated as income to each Unitholder of the Trust in the proportion that the number of Units of the Trust held by the Unitholder bears to the total number of Units of the Trust outstanding. For this reason, interest derived by the Trust that would not be includable in income for South Carolina income tax purposes when paid directly to a South Carolina Unitholder will be exempt from South Carolina income taxation when

received by the Trust and attributed to such South Carolina Unitholder;

Each Unitholder will recognize gain or loss for South Carolina state income tax purposes if the Trustee disposes of a Bond (whether by sale, payment on maturity, retirement or otherwise) or if the Unitholder redeems or sells his Unit; and

The Trust would be regarded, under South Carolina law, as a common trust fund and therefore not subject to taxation under any income tax law of South Carolina.

The above described opinion of Special Counsel has been concurred in by an informal ruling of the South Carolina Tax Commission pursuant to Section 12-3-170 of the South Carolina Code.

#### Virginia Trusts

The Commonwealth's financial condition is supported by a broad-based economy, including manufacturing, tourism, agriculture, ports, mining and fisheries. Manufacturing continues to be a major source of employment, ranking behind only services, wholesale and retail trade, and government (Federal, state and local). The Federal government is a major employer in Virginia due to the heavy concentration of Federal employees in the metropolitan Washington, D.C. segment of Northern Virginia and the military employment in the Hampton Roads area, which houses the nation's largest concentration of military installations. However, the expected retrenchment of the military sector as a consequence of the end of the Cold War remains a cloud on the economic horizon.

In recent years per capita personal income in Virginia has consistently been above the national average. However, while total personal income has continued to rise during the current recession, it has not always kept pace with both inflation and the population, either nationally or in Virginia. Real personal income in Virginia fell for seven consecutive quarters, ending with the last quarter of 1991, with a slow recovery being evidenced in 1992. The annualized rate of growth in real personal income in Virginia for the second quarter of 1992 was 0.5 percent compared to a national rate of 0.3 percent. Virginia's real per capita income has exceeded that for both the nation and the southeast region since the early 1980s, although the differentials have decreased since 1989. Virginia's nonagricultural employment figures mirror the national economy although the recent recession has hit Virginia harder than the nation as a whole with employment declining at an average annual rate of 1.6 percent since 1990 in Virginia, compared to 0.7 percent nationally. With respect to unemployment, Virginia's unemployment rate has consistently been below that of the nation. For the decade of 1980 to 1990, the differential has been two percentage points, although it decreased to below one percentage point in 1991 and the first six months of 1992.

Employment trends in Virginia have varied from sector to sector and from region to region. For example, manufacturing and trade sectors in 1980 each employed more workers than the service sector. Now the service sector is the largest employer in Virginia and mining and manufacturing are now at lower levels than in 1980. Highest rates of unemployment are concentrated in southwest Virginia where mining jobs have been lost and the lowest unemployment rates are seen in Northern Virginia where much federally related employment is concentrated. Not surprisingly, there is great overlap between areas of lowest unemployment and those of highest per capita income. Economic recovery from the recent recession is expected to be long and slow in Virginia, although in the long term, a growing and more diversified export sector holds promise that should mitigate current concerns.

The Commonwealth of Virginia has historically operated on a fiscally conservative basis and is required by its Constitution to have a balanced biennial budget. At the end of the June 30, 1992, fiscal year, the General Fund had an ending fund balance computed on a budgetary cash basis of \$195.2 million, of which \$15 million was in required reserve; \$142.3 million thereof was designated for expenditure during the next fiscal year, leaving an undesignated, unreserved fund balance of \$52.8 million, the first such undesignated fund balance since 1988. Computed on a modified accrual basis in accordance with generally accepted accounting principles, the General Fund balance at the end of the fiscal year ended June 30, 1992, was minus \$121.8 million, compared with a General Fund balance at the end of the fiscal year ended June 30, 1991, of -\$265.1 million. Contributing to the reduction were \$256.4 million in deferred credits, representing estimated tax refunds associated with income taxes withheld for the period January through June, 1992, and an accrual for estimated medicaid claims of \$155.8 million.

As of June 30, 1992, total debt of the Commonwealth aggregated \$7.3 billion. Of that amount, \$1.5 billion was tax-supported. Outstanding general obligation debt backed by the full faith and credit of the Commonwealth was \$582.7 million at June 30, 1992. Of that amount, \$544.4 million was also secured by revenue-producing capital projects. Debt service on the balance equaled 0.2% of total General Fund expenditures in fiscal year 1992.

The Virginia Constitution contains limits on the amount of general obligation bonds which the Commonwealth can issue. These limits are substantially in excess of current levels of outstanding bonds, and at June 30, 1992 would permit an additional total of approximately \$5.00 billion of bonds secured by revenue-producing projects and approximately \$5.50 billion of unsecured general obligation bonds, with not more than approximately \$1.39 billion of the latter to be issued in any four-year period. Bonds which are not secured by revenue-producing projects must be approved in a state-wide election.

In November of 1992 the Constitution of Virginia was amended to establish a permanent Revenue Stabilization Fund. This Fund will go into effect in the 1994-96 biennium. In anticipation of the first required deposit (\$40.5 million) to the fund, the Governor included, and the General Assembly approved, a \$30.0 million down payment.

The current biennium started on July 1, 1992 and will end on June 30, 1994. The amended biennial budget appropriated a total of \$29,090.6 million: \$6,416.0 million in general funds and \$7,907.1 million in nongeneral funds in fiscal 1993, and \$6,852.1 million in general funds and \$7,915.3 million in nongeneral funds in fiscal 1994.

The amended Appropriations Act assumed that general fund revenues would increase by 7.1 percent in fiscal 1993 and 6.0 percent in fiscal 1994. Currently, year-to-date general fund growth for the 11 months of fiscal 1993 is 9.7 percent. When general fund revenues are adjusted for one-time corporate payments, the year-to-date growth declines to 7.9 percent.

The Commonwealth of Virginia maintains ratings of AAA by Standard & Poor's and Aaa by Moody's on its general obligation indebtedness, reflecting in part its sound fiscal management, diversified economic base and low debt ratios. There can be no assurance that these conditions will continue. Nor are these same conditions necessarily applicable to securities which are not general obligations of the Commonwealth. Securities issued by specific municipalities, governmental authorities or similar issuers may be subject to economic risks or uncertainties peculiar to the issuers of such securities or the sources from which they are to be paid.

At the time of the closing for each Virginia Trust, Special Counsel to each Virginia Trust for Virginia tax matters rendered an opinion under then existing Virginia income tax law applicable to taxpayers whose income is subject to Virginia income taxation substantially to the effect that:

The assets of the Trust will consist of interest-bearing obligations issued by or on behalf of the Commonwealth of Virginia ("Virginia") or counties, municipalities, authorities or political subdivisions thereof (the "Bonds").

Neither the Sponsor nor its counsel have independently examined the Bonds to be deposited in and held in the Trust. However, although no opinion is expressed herein regarding such matters, it is assumed that: (i) the Bonds were validly issued, (ii) the interest thereon is excludible from gross income for federal income tax purposes and (iii) the interest thereon is exempt from income tax imposed by Virginia that is applicable to individuals and corporations (the "Virginia Income Tax"). The opinion set forth below does not address the taxation of persons other than full time residents of Virginia.

The Virginia Trust is not an association taxable as a corporation for purposes of the Virginia Income Tax and each Unitholder of the Trust will be treated as the owner of a pro rata portion of the assets held by the Trust and the income of such portion of the Virginia Trust will be treated as income of the Unitholder for purposes of the Virginia Income Tax;

Income on the Bonds which is exempt from Virginia Income Tax when received by the Virginia Trust, and which would be exempt from Virginia Income Tax if received directly by a Unitholder, will retain its status as exempt from such tax when received by the Trust and distributed to such Unitholder;

Each Unitholder will recognize gain or loss for purposes of the Virginia Income Tax if the Trustee disposes of a bond (whether by redemption, sale or otherwise) or if the Unitholder redeems or sells Units of the Trust to the extent that such a transaction results in a recognized gain or loss to such Unitholder for federal income tax purposes, except as described in this paragraph. Virginia has by law provided that all income from certain tax-exempt obligations issued under the laws of Virginia, including any profits made from the sale of such Bonds, shall be exempt from all taxation by Virginia. Although we express no opinion, the Virginia Department of Taxation has indicated that the gain on the sale of such tax-exempt obligations, recognized for federal income tax purposes, would not be subject to Virginia income taxation. Accordingly, any such gain relating to the disposition of any Bond that would not be subject to Virginia Income Tax if the Bond was held directly by a Unitholder will retain its tax-exempt status for purposes of the Virginia Income Tax when the Bond is disposed of by the Virginia Trust or when the Unitholder is deemed to have disposed of his pro rata portion of such Bond upon the disposition of his Unit, provided that such gain can be determined with reasonable certainty and substantiated; and



The Virginia Income Tax does not permit a deduction of interest paid on indebtedness incurred or continued to purchase or carry Units in the Virginia Trust to the extent that interest income related to the ownership of Units is exempt from the Virginia Income Tax.

In the case of Unitholders subject to the Virginia Bank Franchise Tax, the income derived by such a Unitholder from his pro rata portion of the Bonds held by the Virginia Trust may affect the determination of such Unitholder's Bank Franchise Tax. Prospective investors subject to the Virginia Bank Franchise Tax should consult their tax advisors.

#### THE SPONSOR

Van Kampen Merritt Inc., a Delaware corporation, is the Sponsor of the Fund. Van Kampen Merritt Inc. is primarily owned by Clayton, Dubilier & Rice, Inc., a New York-based private investment firm. Van Kampen Merritt, Inc. management owns a significant minority equity position. Van Kampen Merritt Inc. specializes in the underwriting and distribution of unit investment trusts and mutual funds. The Sponsor is a member of the National Association of Securities Dealers, Inc. and has its principal office at One Parkview Plaza, Oakbrook Terrace, Illinois 60181 (708-684-6000). It maintains a branch office in Philadelphia and has regional representatives in Atlanta, Dallas, Los Angeles, New York, San Francisco, Seattle and Tampa. As of September 30, 1993, the total stockholders' equity of Van Kampen Merritt Inc. was \$200,885,000 (unaudited). (This paragraph relates only to the Sponsor and not to the Trusts or to any other person. The information is included herein only for the purpose of informing investors as to the financial responsibility of the Sponsor and its ability to carry out its contractual obligations. More detailed financial information will be made available by the Sponsor upon request.) As of November 30, 1993, the Sponsor and its affiliates managed or supervised approximately \$38.5 billion of investment products, of which over \$25 billion is invested in municipal securities. The Sponsor and its affiliates managed \$23 billion of assets consisting of \$8.2 billion for 19 mutual funds, \$8.3 billion for 33 closed-end funds and \$6.5 billion for 51 institutional accounts. The Sponsor has also deposited over \$23.5 billion of unit investment trusts. Based on cumulative assets deposited, the Sponsor believes that it is the largest sponsor of insured municipal unit investment trusts, primarily through the success of its Insured Municipal Income Trust or the IM-IT trust. The Sponsor also provides surveillance and evaluation services at cost for approximately \$15.5 billion of unit investment trust assets outstanding. Since 1976, the Sponsor has opened over one million retail investor accounts through retail distribution firms. Van Kampen Merritt Inc. is the sponsor of the various series of the trusts listed below and the distributor of the mutual funds and closed-end funds listed below. Unitholders may only invest in the trusts, mutual funds and closed-end funds which are registered for sale in the state of residence of such Unitholder. Van Kampen Merritt Inc. is the sponsor of the various series of the following unit investment trusts: Investors' Quality Tax-Exempt Trust; Investors' Quality Tax-Exempt Trust, Multi-Series; Investors' Quality Municipals Trust, AMT Series; Insured Municipals Income Trust; Insured Municipals Income Trust, Insured Multi-Series; California Insured Municipals Income Trust; New York Insured Municipals Income Trust; Pennsylvania Insured Municipals Income Trust; Insured Tax Free Bond Trust; Insured Tax Free Bond Trust, Insured Multi-Series; Investors' Corporate Income Trust; Investors' Governmental Securities-Income Trust; Van Kampen Merritt International Bond Income Trust; Van Kampen Merritt Utility Income Trust; Van Kampen Merritt Insured Income Trust; Van Kampen Merritt Blue Chip Opportunity Trust; Van Kampen Merritt Blue Chip Opportunity and Treasury Trust; Van Kampen Merritt Emerging Markets Income Trust; Van Kampen Merritt Global Telecommunications Trust; and Van Kampen Merritt Global Energy Trust. Van Kampen Merritt Inc. is the distributor of the following mutual funds: Van Kampen Merritt U.S. Government Fund; Van Kampen Merritt California Insured Tax Free Fund; Van Kampen Merritt Tax-Free High Income Fund; Van Kampen Merritt Insured Tax-Free Income Fund; Van Kampen Merritt High Yield Fund; Van Kampen Merritt Growth and Income Fund; Van Kampen Merritt Pennsylvania Tax-Free Income Fund; Van Kampen Merritt Money Market Fund; Van Kampen Merritt Tax Free Money Fund; Van Kampen Merritt Municipal Income Fund; Van Kampen Merritt Short-Term Global Income Fund; Van Kampen Merritt Adjustable Rate U.S. Government Fund; Van Kampen Merritt Value Municipal Income Trust; Van Kampen Merritt California Value Municipal Income Trust; Van Kampen Merritt Massachusetts Value Municipal Income Trust; Van Kampen Merritt New Jersey Value Municipal Income Trust; Van Kampen Merritt New York Value Municipal Income Trust; Van Kampen Merritt Ohio Value Municipal Income Trust; and Van Kampen Merritt Pennsylvania Value Municipal Income Trust. Van Kampen Merritt Inc. is the distributor of the following closed-end funds: Van Kampen Merritt Municipal Income Trust; Van Kampen Merritt California Municipal Trust; Van Kampen Merritt Intermediate Term High Income Trust; Van Kampen Merritt Limited Term High Income Trust; Van Kampen Merritt Prime Rate Income Trust; Van Kampen Merritt Investment Grade Municipal Trust; Van Kampen Merritt Municipal Trust; Van Kampen Merritt California Quality Municipal Trust; Van Kampen Merritt Florida Quality Municipal Trust; Van Kampen Merritt New York Quality Municipal Trust; Van Kampen Merritt Ohio Quality Municipal Trust; Van Kampen Merritt Pennsylvania Quality Municipal Trust; Van Kampen Merritt Trust for Investment Grade Municipals; Van Kampen

Merritt Trust for Insured Municipals; Van Kampen Merritt Trust for Investment Grade CA Municipals; Van Kampen Merritt Trust for Investment Grade FL Municipals; Van Kampen Merritt Trust for Investment Grade NJ Municipals; Van Kampen Merritt Trust for Investment Grade NY Municipals; Van Kampen Merritt Trust for Investment Grade PA Municipals; Van Kampen Merritt Municipal Opportunity Trust; Van Kampen Merritt Advantage Municipal Income Trust; Van Kampen Merritt Advantage Pennsylvania Municipal Income Trust; Van Kampen Merritt Strategic Sector Municipal Trust; and Van Kampen Merritt Limited Term Municipal Income Fund.

If the Sponsor shall fail to perform any of its duties under the Trust Agreement or become incapable of acting or become bankrupt or its affairs are taken over by public authorities, then the Trustee may (i) appoint a successor Sponsor at rates of compensation deemed by the Trustee to be reasonable and not exceeding amounts prescribed by the Securities and Exchange Commission, (ii) terminate the Trust Agreement and liquidate the Trust as provided therein or (iii) continue to act as Trustee without terminating the Trust Agreement.

All costs and expenses incurred in creating and establishing the Fund, including the cost of the initial preparation, printing and execution of the Trust Agreement and the certificates, legal and accounting expenses, advertising and selling expenses, expenses of the Trustee, initial evaluation fees and other out-of-pocket expenses have been borne by the Sponsor at no cost to the Fund.

#### THE TRUSTEE

Except for the various series of the Pennsylvania Trusts referred to in the next paragraph, the Trustee is The Bank of New York, a trust company organized under the laws of New York. The Bank of New York has its offices at 101 Barclay Street, New York, New York 10286 (800-221-7668). The Bank of New York is subject to supervision and examination by the Superintendent of Banks of the State of New York and the Board of Governors of the Federal Reserve System, and its deposits are insured by the Federal Deposit Insurance Corporation to the extent permitted by law. The Trustee commenced operations on February 3, 1986 when it acquired the unit investment trust division of Fidata Trust Company, New York. The duties of the Trustee are primarily ministerial in nature. It did not participate in the selection of Bonds for the portfolios of any of the Trusts.

In the case of the various series of Investors' Municipal Pennsylvania Unit Trusts and Tax-Exempt Trusts for Pennsylvania Residents, First Combined Series (Investors' Municipal Pennsylvania Unit Trust, 3rd Series), the Trustee is United States Trust Company of New York, with its principal place of business at 45 Wall Street, New York, New York 10005 and its corporate trust office at 770 Broadway, New York, New York 10003. United States Trust Company of New York, established in 1853, has, since its organization, engaged primarily in the management of trust and agency accounts for individuals and corporations. The Trustee is a member of the New York Clearing Housing Association and is subject to supervision and examination by the Superintendent of Banks of the State of New York, the Federal Deposit Insurance Corporation and the Board of Governors of the Federal Reserve System.

In accordance with the Trust Agreement, the Trustee shall keep proper books of record and account of all transactions at its office for the Trust. Such records shall include the name and address of, and the certificates issued by the Trust to, every Unitholder of the Trust. Such books and records shall be open to inspection by any Unitholder at all reasonable times during the usual business hours. The Trustee shall make such annual or other reports as may from time to time be required under any applicable state or Federal statute, rule or regulation (see "Unitholder Explanations-Public Offering Reports Provided"). The Trustee is required to keep a certified copy or duplicate original of the Trust Agreement on file in its office available for inspection at all reasonable times during the usual business hours by any Unitholder, together with a current list of the Securities held in the Trust.

Under the Trust Agreement, the Trustee or any successor trustee may resign and be discharged of the Trusts created by the Trust Agreement by executing an instrument in writing and filing the same with the Sponsor. The Trustee or successor trustee must mail a copy of the notice of resignation to all Fund Unitholders then of record, not less than 60 days before the date specified in such notice when such resignation is to take effect. The Sponsor upon receiving notice of such resignation is obligated to appoint a successor trustee promptly. If, upon the Trustee's resignation, no successor trustee has been appointed and has accepted the appointment within 30 days after notification, the retiring Trustee may apply to a court of competent jurisdiction for the appointment of a successor. The Sponsor may remove the Trustee and appoint a successor trustee as provided in the Trust Agreement at any time with or without cause. Notice of such removal and appointment shall be mailed to each Unitholder by the Sponsor. Upon execution of a written acceptance of such appointment by such successor trustee, all the rights, powers, duties and obligations of the original trustee shall vesting the successor. The resignation or removal of a Trustee becomes effective only when the successor trustee accepts its appointment as such or when a court of

competent jurisdiction appoints a successor trustee.

Any corporation into which a Trustee may be merged or with which it may be consolidated, or any corporation resulting from any merger or consolidation to which a Trustee shall be a party, shall be the successor trustee. The Trustee must be a banking corporation organized under the laws of the United States or any state and having at all times an aggregate capital, surplus and undivided profits of not less than \$5,000,000.

#### EXPENSES OF THE TRUST

The Sponsor will not receive any fees in connection with its activities relating to a Trust. However, in connection with certain series of the Trusts American Portfolio Evaluation Services, a division of Van Kampen Merritt Investment Advisory Corp., a wholly-owned subsidiary corporation of the Sponsor, will receive an annual supervisory fee as indicated under "Summary of Essential Financial Information" in Part One of this Prospectus for providing portfolio supervisory services for such series of such Trusts. Such fee (which is based on the number of Units outstanding on January 1 of each year) may exceed the actual costs of providing such supervisory services for such series of such Trust, but at no time will the total amount received for portfolio supervisory services rendered to all such series of such Trusts in any calendar year exceed the aggregate cost to the Evaluator of supplying such services in such year. In addition, for regularly evaluating Trust portfolios, the Evaluator shall receive an annual evaluation fee as also indicated under "Summary of Essential Financial Information". For its services the Trustee receives a fee based on the aggregate outstanding principal amount of Securities in each Trust as of the opening of business on January 2 and July 2 of each year as set forth under "Per Unit Information" in Part I of this Prospectus. The Trustee's fees are payable monthly on or before the fifteenth day of each month from the Interest Account of each Trust to the extent funds are available and then from the Principal Account of each Trust, with such payments being based on each Trust's portion of such expenses. The Trustee's fees will not be increased in future years in order to make up for any reduction in the Trustee's fees described in Part I of this Prospectus under "Per Unit Information" for the applicable Trust. Since the Trustee has the use of the funds being held in the Principal and Interest Accounts for future distributions, payment of expenses and redemptions and since such Accounts are non-interest bearing to Unitholders, the Trustee benefits thereby. Part of the Trustee's compensation for its services to each Trust is expected to result from the use of these funds. For a discussion of the services rendered by the Trustee pursuant to its obligations under the Trust Agreement, see "Public Offering Reports Provided" and "Trust Administration and Expenses".

Both the Evaluator's fees and the Trustee's fees may be increased without approval of the Unitholders by amounts not exceeding proportionate increases under the category "All Services Less Rent of Shelter" in the Consumer Price Index published by the United States Department of Labor or, if such category is no longer published, in a comparable category. The Sponsor and the dealers will receive sales commissions and may realize other profits (or losses) in connection with the sale of Units as described under "Public Offering".

The following additional charges may be incurred by the Trusts: (a) fees of the Trustee for extraordinary services, (b) expenses of the Trustee (including legal and auditing expenses) and of counsel designated by the Sponsor, (c) various governmental charges, (d) expenses and costs of any action taken by the Trustee to protect the Trusts and the rights and interests of Unitholders, (e) indemnification of the Trustee for any loss, liability or expenses incurred by it in the administration of the Fund without negligence, bad faith or willful misconduct on its part and (f) expenditures incurred in contacting Unitholders upon termination of the Trust.

The fees and expenses set forth herein are payable out of the respective Trusts. When such fees and expenses are paid by or owing to the Trustee, they are secured by a lien on the portfolio of the applicable Trust. If the balances in the Interest and Principal Accounts are insufficient to provide for amounts payable by a Trust, the Trustee has the power to sell Securities to pay such amounts.

#### PORTFOLIO ADMINISTRATION

The Trustee is empowered to sell, for the purpose of redeeming Units tendered by any Unitholder, and for the payment of expenses for which funds may not be available, such of the Bonds designated by the Evaluator as the Trustee in its sole discretion may deem necessary. The Evaluator, in designating such Securities, will consider a variety of factors, including (a) interest rates, (b) market value and (c) marketability. The Sponsor, in connection with the respective Trusts, may direct the Trustee to dispose of Bonds upon default in payment of principal or interest, institution of certain legal proceedings, default under other documents adversely affecting debt service, default in payment of principal or interest on other obligations of the same issuer, decline in projected income pledged for debt service on revenue bonds or decline in price or the occurrence of other market or credit factors, including advance refunding (i.e., the issuance of refunding securities and

the deposit of the proceeds thereof in trust or escrow to retire the refunded securities on their respective redemption dates), so that in the opinion of the Sponsor the retention of such Bonds would be detrimental to the interest of the Unitholders. Because of such restrictions on the Trustee under certain circumstances the Sponsor may seek a full or partial suspension of the right of Unitholders to redeem their Units. See "Public Offering Redemption of Units". The Sponsor is empowered, but not obligated, to direct the Trustee to dispose of Bonds in the event of an advanced refunding.

The Sponsor is required to instruct the Trustee to reject any offer made by an issuer of any of the Securities to issue new obligations in exchange or substitution for any Security pursuant to a refunding or refinancing plan, except that the Sponsor may instruct the Trustee to accept or reject such an offer or to take any other action with respect thereto as the Sponsor may deem proper if (1) the issuer is in default with respect to such Security or (2) in the written opinion of the Sponsor the issuer will probably default with respect to such Security in the reasonably foreseeable future. Any obligation so received in exchange or substitution will be held by the Trustee subject to the terms and conditions of the Trust Agreement to the same extent as Securities originally deposited thereunder. Within five days after the deposit of obligations in exchange or substitution for underlying Securities, the Trustee is required to give notice thereof to each Unitholder of the Trust thereby affected, identifying the Securities eliminated and the Securities substituted therefor. Except as provided herein, the acquisition by a Trust of any securities other than the Securities initially deposited is not permitted.

If any default in the payment of principal or interest on any Security occurs and no provision for payment is made therefor within 30 days, the Trustee is required to notify the Sponsor thereof. If the Sponsor fails to instruct the Trustee to sell or to hold such Security within 30 days after notification by the Trustee to the Sponsor of such default, the Trustee may in its discretion sell the defaulted Security and not be liable for any depreciation or loss thereby incurred.

#### PURCHASE OF UNITS BY THE SPONSOR

The Trustee shall notify the Sponsor of any tender of Units for redemption. If the Sponsor's bid in the secondary market at that time equals or exceeds the Redemption Price per Unit, it may purchase such Units by notifying the Trustee before the close of business on the second succeeding business day and by making payment therefor to the Unitholder not later than the day on which the Units would otherwise have been redeemed by the Trustee. Units held by the Sponsor may be tendered to the Trustee for redemption as any other Units.

The offering price of any Units acquired by the Sponsor will be in accord with the Public Offering Price described in the then currently effective prospectus describing such Units. Any profit resulting from the resale of such Units will belong to the Sponsor which likewise will bear any loss resulting from a lower offering or Redemption Price subsequent to its acquisition of such Units.

#### AMENDMENT OR TERMINATION

The Sponsor and the Trustee have the power to amend the Trust Agreement without the consent of any of the Unitholders when such an amendment is (a) to cure an ambiguity or to correct or supplement any provision of the Trust Agreement which may be defective or inconsistent with any other provision contained therein or (b) to make such other provisions as shall not adversely affect the interest of the Unitholders (as determined in good faith by the Sponsor and the Trustee), provided that the Trust Agreement may not be amended to increase the number of Units issuable thereunder or to permit the deposit or acquisition of securities either in addition to or in substitution for any of the Securities initially deposited in a Trust, except for the substitution of certain refunding securities for such Securities. In the event of any amendment, the Trustee is obligated to notify promptly all Unitholders of the substance of such amendment.

A Trust may be terminated by the Trustee when the value of such Trust, as shown by any semi-annual evaluation, is less than that indicated under "Summary of Essential Financial Information" in Part One of this Prospectus. In addition, all Trusts other than those indicated in the next sentence may be terminated at any time by the consent of the holders representing 100% of the Units of such Trust then outstanding. Each Trust in Investors' Quality Tax-Exempt Trust, 6th Multi-State, 7th Multi-State, 8th Multi-Series and subsequent series may be terminated at any time by consent of the holders representing 51% of the Units of such Trust then outstanding. The Trust Agreement provides that each Trust shall terminate upon the redemption, sale or other disposition of the last Security held in such Trust, but in no event shall it continue beyond the end of the year preceding the fiftieth anniversary of the Trust Agreement. In the event of termination of the Fund or any Trust, written notice thereof will be sent by the Trustee to each Unitholder of such Trust at his address appearing on the registration books of the Fund maintained by the Trustee. Within a reasonable time thereafter, the Trustee shall liquidate any Securities then held in such Trust and shall

deduct from the funds of such Trust any accrued costs, expenses or indemnities provided by the Trust Agreement, including estimated compensation of the Trustee and costs of liquidation and any amounts required as a reserve to provide for payment of any applicable taxes or other governmental charges. The sale of Securities in the Trust upon termination may result in a lower amount than might otherwise be realized if such sale were not required at such time. For this reason, among others, the amount realized by a Unitholder upon termination may be less than the principal amount of Securities represented by the Units held by such Unitholder. The Trustee shall then distribute to each Unitholder his share of the balance of the Interest and Principal Accounts. With such distribution, the Unitholder shall be furnished a final distribution statement of the amount distributable. At such time as the Trustee in its sole discretion shall determine that any amounts held in reserve are no longer necessary, it shall make distribution thereof to Unitholders in the same manner.

#### LIMITATION ON LIABILITIES

The Sponsor, the Evaluator and the Trustee shall be under no liability to Unitholders for taking any action or for refraining from taking any action in good faith pursuant to the Trust Agreement, or for errors in judgment, but shall be liable only for their own willful misfeasance, bad faith or gross negligence in the performance of their duties or by reason of their reckless disregard of their obligations and duties hereunder. The Trustee shall not be liable for depreciation or loss incurred by reason of the sale by the Trustee of any of the Securities. In the event of the failure of the Sponsor to act under the Trust Agreement, the Trustee may act thereunder and shall not be liable for any action taken by it in good faith under the Trust Agreement.

The Trustee shall not be liable for any taxes or other governmental charges imposed upon or in respect of the Securities or upon the interest thereon or upon it as Trustee under the Trust Agreement or upon or in respect of a Trust which the Trustee may be required to pay under any present or future law of the United States of America or of any other taxing authority having jurisdiction. In addition, the Trust Agreement contains other customary provisions limiting the liability of the Trustee.

The Trustee, Sponsor and Unitholders may rely on any evaluation furnished by the Evaluator and shall have no responsibility for the accuracy thereof. Determinations by the Evaluator under the Trust Agreement shall be made in good faith upon the basis of the best information available to it; provided, however, that the Evaluator shall be under no liability to the Trustee, Sponsor or Unitholders for errors in judgment. This provision shall not protect the Evaluator in any case of willful misfeasance, bad faith, gross negligence or reckless disregard of its obligations and duties.

#### UNIT DISTRIBUTION

Units repurchased in the secondary market, if any, may be offered by this Prospectus at the secondary Public Offering Price (which includes Purchased Interest in those Trusts which contain Purchased Interest) plus accrued undistributed interest to the settlement date. Broker-dealers or others will be allowed a concession or agency commission in connection with secondary market transactions in the amount of 70% of the applicable sales charge as determined using the table found in "Public Offering". Certain commercial banks are making Units of the Trust available to their customers on an agency basis. A portion of the sale charge (equal to the agency commission referred to above) is retained by or remitted to the banks. Under the Glass-Steagall Act, banks are prohibited from underwriting Trust Units; however, the Glass-Steagall Act does permit certain agency transactions and the banking regulators have not indicated that these particular agency transactions are not permitted under such Act. In addition, state securities laws on this issue may differ from the interpretations of federal law expressed herein and banks and financial institutions may be required to register as dealers pursuant to state law. The minimum purchase in the secondary market will be one Unit.

Broker-dealers of the Trust may be eligible to participate in a program in which such firms receive from the Sponsor a nominal award for each of their registered representatives who have sold a minimum number of units of unit investment trusts created by the Sponsor during a specified time period. In addition, at various times the Sponsor may implement other programs under which the sales force of a broker or dealer may be eligible to win other nominal awards for certain sales efforts, or under which the Sponsor will reallocate to any such broker or dealer that sponsors sales contests or recognition programs conforming to criteria established by the Sponsor, or participates in sales programs sponsored by the Sponsor, an amount not exceeding the total applicable sales charges on the sales generated by such person at the public offering price during such programs. Also, the Sponsor in its discretion may from time to time pursuant to objective criteria established by the Sponsor pay fees to qualifying brokers or dealers for certain services or activities which are primarily intended to result in sales of Units of the Trust. Such payments are made by the Sponsor out of its own assets, and not out of the assets of the Trust. These programs will not change the price Unitholders pay for their Units or the amount that the Trust will

receive from the Units sold.

The Sponsor reserves the right to reject, in whole or in part, any order for the purchase of Units and to change the amount of the concession or agency commission to dealers and others from time to time.

#### SPONSOR AND DEALER COMPENSATION

Dealers will receive the gross sales commission as described under "Public Offering Price".

As stated under "Market for Units", the Sponsor intends to, and certain of the dealers may, maintain a secondary market for the Units of the Trust. In so maintaining a market, such person or persons will realize profits or sustain losses in the amount of any difference between the price at which Units are purchased and the price at which Units are resold (which price is based on the bid prices of the Securities in such Trust and includes a sales charge). In addition, such person or persons will also realize profits or sustain losses resulting from a redemption of such repurchased Units at a price above or below the purchase price for such Units, respectively.

#### LEGAL OPINIONS

The legality of the Units offered hereby has been passed upon by Chapman and Cutler, 111 West Monroe Street, Chicago, Illinois 60603, as counsel for the Sponsor. The counsel which has provided a state tax opinion to the respective State Trust under "Description and State Tax Status of State Trusts" has acted as special counsel to the Fund for the tax matters of such State. Various Counsel have acted as counsel for the Trustee and as special counsel for the Fund for New York tax matters. None of the special counsel for the Fund has expressed any opinion regarding the completeness or materiality of any matters contained in this Prospectus other than the tax opinion set forth by such special counsel.

#### AUDITORS

The statements of condition and the related securities portfolio for each Trust included in Part One of this Prospectus have been audited at the date indicated therein by Grant Thornton, independent certified public accountants, as set forth in their report in Part One of this Prospectus, and are included herein in reliance upon the authority of said firm as experts in accounting and auditing.

#### DESCRIPTION OF SECURITIES RATINGS\*

\*As published by the rating companies.

Standard & Poor's Corporation. A Standard & Poor's Corporation ("Standard & Poor's") corporate or municipal bond rating is a current assessment of the creditworthiness of an obligor with respect to a specific debt obligation. This assessment of creditworthiness may take into consideration obligors such as guarantors, insurers or lessees.

The bond rating is not a recommendation to purchase or sell a security, inasmuch as it does not comment as to market price.

The ratings are based on current information furnished to Standard & Poor's by the issuer and obtained by Standard & Poor's from other sources it considers reliable. The ratings may be changed, suspended or withdrawn as a result of changes in, or unavailability of, such information.

The ratings are based, in varying degrees, on the following considerations:

I. Likelihood of default capacity and willingness of the obligor as to the timely payment of interest and repayment of principal in accordance with the terms of the obligation.

II. Nature of and provisions of the obligation.

III. Protection afforded by, and relative position of, the obligation in the event of bankruptcy, reorganization or other arrangements under the laws of bankruptcy and other laws affecting creditors' rights.

#### AAA

This is the highest rating assigned by Standard & Poor's to a debt obligation and indicates an extremely strong capacity to pay principal and interest.

#### AA

Bonds rated AA also qualify as high-quality debt obligations. Capacity to pay principal and interest is very strong, and in the majority of instances they differ from AAA issues only in small degree.



## A

Bonds rated A have a strong capacity to pay principal and interest, although they are somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions.

## BBB

Bonds rated BBB are regarded as having an adequate capacity to pay interest and repay principal. Whereas they normally exhibit adequate protection parameters, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity to pay interest and repay principal for bonds in this category than for bonds in higher rated categories.

Plus (+) or Minus (-): To provide more detailed indications of credit quality, the ratings from "AA" to "BBB" may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

Provisional Ratings: A provisional rating "p" assumes the successful completion of the project being financed by the issuance of the bonds being rated and indicates that payment of debt service requirements is largely or entirely dependent upon the successful and timely completion of the project. This rating, however, while addressing credit quality subsequent to completion, makes no comment on the likelihood of, or the risk of default upon failure of, such completion. Accordingly, the investor should exercise his own judgment with respect to such likelihood and risk. Moody's Investors Service, Inc. A brief description of the applicable Moody's Investors Service, Inc. ("Moody's") rating symbols and their meanings follow:

## Aaa

Bonds which are rated Aaa are judged to be the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt edge". Interest payments are protected by a large, or by an exceptionally stable, margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues. With the occasional exception of oversupply in a few specific instances, the safety of obligations of this class is so absolute that their market value is affected solely by money market fluctuations.

## Aa

Bonds which are rated Aa are judged to be of high quality by all standards. Together with the Aaa group they comprise what are generally known as high grade bonds. They are rated lower than the best bonds because margins of protection may not be as large as in Aaa securities or fluctuations of protective elements may be of greater amplitude or there may be other elements present which make the long-term risks appear somewhat larger than in Aaa securities. These Aa bonds are high grade, their market value virtually immune to all but money market influences, with the occasional exception of oversupply in a few specific instances.

## A

Bonds which are rated A possess many favorable investment attributes and are to be considered as higher medium grade obligations. Factors giving security to principal and interest are considered adequate, but elements may be present which suggest a susceptibility to impairment sometime in the future. The market value of A-rated bonds may be influenced to some degree by credit circumstances during a sustained period of depressed business conditions. During periods of normalcy, bonds of this quality frequently move in parallel with Aaa and Aa obligations, with the occasional exception of oversupply in a few specific instances.

## Baa

Bonds which are rated Baa are considered as medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

Moody's bond rating symbols may contain numerical modifiers of a generic rating classification. The modifier 1 indicates that the bond ranks at the high end of its category; the modifier 2 indicates a mid-range ranking; and the modifier 3 indicates that the issue ranks in the lower end of its generic rating category.

## Con

Bonds for which the security depends upon the completion of some act or the fulfillment of some condition are rated conditionally. These are bonds secured

by (a) earnings of projects under construction, (b) earnings of projects unseasoned in operating experience, (c) rentals which begin when facilities are completed, or (d) payments to which some other limiting condition attaches. Parenthetical rating denotes probable credit stature upon completion of construction or elimination of basis of condition.

No person is authorized to give any information or to make any representations not contained in this Prospectus, and any information or representation not contained herein must not be relied upon as having been authorized by the Fund, the Sponsor or any dealer. This Prospectus does not constitute an offer to sell, or a solicitation of an offer to buy, securities in any state to any person to whom it is not lawful to make such offer in such state.

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This Prospectus contains information concerning the Fund and the Sponsor, but does not contain all of the information set forth in the registration statements and exhibits relating thereto, which the Fund has filed with the Securities and Exchange Commission, Washington, D.C., under the Securities Act of 1933 and the Investment Company Act of 1940, and to which reference is hereby made.

National and State Quality Trusts  
INVESTORS' QUALITY  
TAX-EXEMPT TRUST

Note: This Prospectus May Be Used Only When Accompanied by Part One.  
Both Parts of this Prospectus should be retained for future reference.

Dated as of the date of the Prospectus Part I accompanying this Prospectus  
Part II.

Sponsor: Van Kampen Merritt  
One Parkview Plaza  
Oakbrook Terrace, Illinois 60181  
and  
Mellon Bank Center  
1735 Market Street Suite 1300  
Philadelphia, Pennsylvania 19103

Please retain this Prospectus for future reference.

Contents of Post-Effective Amendment  
to Registration Statement

This Post-Effective Amendment to the Registration Statement  
comprises the following papers and documents:

The facing sheet

The prospectus

The signatures

The Consent of Independent Accountants

Signatures

Pursuant to the requirements of the Securities Act of 1933, the  
Registrant, Investors' Quality Tax-Exempt Trust, 35th Multi-Series,  
certifies that it meets all of the requirements for effectiveness of this  
Registration Statement pursuant to Rule 485(b) under the Securities Act  
of 1933 and has duly caused this Post-Effective Amendment to its  
Registration Statement to be signed on its behalf by the undersigned  
thereunto duly authorized, and its seal to be hereunto affixed and  
attested, all in the City of Chicago and State of Illinois on the  
22nd day of February, 1995.

Investors' Quality Tax-Exempt Trust, 35th Multi-  
Series  
(Registrant)

By Van Kampen American Capital Distributors,  
Inc.  
(Depositor)

By: Sandra A. Waterworth  
Vice President

(Seal)

Pursuant to the requirements of the Securities Act of 1933, this  
Post Effective Amendment to the Registration Statement has been signed  
below by the following persons in the capacities on February 22, 1995:

| Signature        | Title   |
|------------------|---|
| Don G. Powell    | Chairman, Chief Executive )<br>Officer and Director )<br>)    |
| William R. Rybak | Senior Vice President and )<br>Chief Financial Officer )<br>) |



Consent of Independent Certified Public Accountants

We have issued our report dated December 2, 1994 accompanying the financial statements of Investors' Quality Tax-Exempt Trust, 35th Multi-Series as of October 31, 1994, and for the period then ended, contained in this Post-Effective Amendment No. 10 to Form S-6.

We consent to the use of the aforementioned report in the Post-Effective Amendment and to the use of our name as it appears under the caption "Auditors".

Grant Thornton LLP

Chicago, Illinois  
February 22, 1995

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