

**COMMONWEALTH OF PUERTO RICO**

Comprehensive Annual Financial Report

Fiscal Year Ended June 30, 2004

# **COMPREHENSIVE ANNUAL FINANCIAL REPORT**

*Fiscal Year Ended June 30, 2004*



***Commonwealth of Puerto Rico***

***Honorable Aníbal Acevedo Vilá***  
***Governor***

*Prepared by:*

***Puerto Rico Department of the Treasury***

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*This document is available on the Puerto Rico Department of the Treasury homepage  
On the World Wide Web: <http://www.hacienda.gobierno.pr>*

# COMMONWEALTH OF PUERTO RICO

## Comprehensive Annual Financial Report

Year ended June 30, 2004

### Table of Contents

	<b>Page</b>
<b>Introductory Section</b>	
Letter of Transmittal	1
Principal Officials	13
Organization Chart	14
Certificate of Achievement for Excellence in Financial Reporting	15
<b>Financial Section</b>	
Independent Auditors' Report	1
Management's Discussion and Analysis	3
Basic Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Assets	20
Statement of Activities	22
Fund Financial Statements:	
Balance Sheet – Governmental Funds	23
Reconciliation of the Balance Sheet to the Statement of Net Assets – Governmental Funds	25
Statement of Revenue, Expenditures, and Changes in Fund Balances – Governmental Funds	26
Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balances to the Statement of Activities – Governmental Funds	27
Statement of Revenue and Expenditures – Budget and Actual – Budget Basis – General Fund	28
Statement of Net Assets – Proprietary Funds	29
Statement of Revenue, Expenses, and Changes in Net Assets – Proprietary Funds	30
Statement of Cash Flows – Proprietary Funds	31

# COMMONWEALTH OF PUERTO RICO

## Comprehensive Annual Financial Report

Year ended June 30, 2004

### Table of Contents

	<b>Page</b>
Statement of Fiduciary Net Assets	32
Statement of Changes in Fiduciary Net Assets – Pension Trust Funds	33
Combining Statement of Net Assets – Major Component Units	34
Combining Statement of Activities – Major Component Units	36
Notes to Basic Financial Statements	37
<b>Combining, Individual Fund Financial Statements and Schedules</b>	
General Fund:	
Supplemental Schedule of Expenditures by Agency – Budget and Actual – Statutory Basis – General Fund	147
Nonmajor Governmental Funds:	
Combining Balance Sheet – Nonmajor Governmental Funds	152
Combining Statement of Revenue, Expenditures, and Changes in Fund Balances – Nonmajor Governmental Funds	153
Nonmajor Proprietary Funds:	
Combining Statement of Net Assets – Nonmajor Proprietary Funds	155
Combining Statement of Revenue, Expenditures, and Changes in Net Assets – Nonmajor Proprietary Funds	156
Combining Statement of Cash Flows – Nonmajor Proprietary Funds	157
Fiduciary Funds:	
Combining Statement of Fiduciary Net Assets – Pension Trust Funds	159
Combining Statement of Changes in Fiduciary Net Assets – Pension Trust Funds	160
Combining Statement of Changes in Assets and Liabilities – Agency Fund	161

# COMMONWEALTH OF PUERTO RICO

## Comprehensive Annual Financial Report

Year ended June 30, 2004

### Table of Contents

	<b>Page</b>
Nonmajor Component Units:	
Nonmajor Discretely Presented Component Units – Statement of Net Assets	163
Nonmajor Discretely Presented Component Units – Statement of Activities	174
<b>Statistical Section</b>	
Changes in Net Assets for the Last Three Fiscal Years	1
Net Assets by Component for the Last Three Fiscal Years	2
General Governmental Expenditures by Function	
All Governmental Fund Types for the Last Ten Fiscal Years	3
General Governmental Revenue by Source	
All Governmental Fund Types for the Last Ten Fiscal Years	4
Fund Balances of Governmental Funds for the Last Three Fiscal Years	5
Computation of the Legal Debt Margin at June 30, 2004	6
Ratio of Annual Debt Service for General Bonded Debt to Total General Expenditures for the Last Ten Fiscal Years	7
Demographic Statistics for the Last Ten Fiscal Years	8
Construction and Bank Deposits for the Last Ten Fiscal Years	9
Miscellaneous Statistics at June 30, 2004	10
General Fund Net Revenue for the Last Ten Fiscal Years	11
General Fund Net Revenue for the Fiscal Year 2004 (Chart)	12
General Fund Net Revenue for the Last Ten Fiscal Years (Chart)	13
Income Tax Receipts for the Fiscal Year 2004 (Chart)	14
Gross Product for the Last Ten Fiscal Years	15
Real Gross Product Growth for the Last Ten Fiscal Years (Chart)	16

# COMMONWEALTH OF PUERTO RICO

## Comprehensive Annual Financial Report

Year ended June 30, 2004

### Table of Contents

	<b>Page</b>
Employment and Unemployment for the Last Ten Fiscal Years	17
Average Employment by Sector for the Last Ten Fiscal Years	18
Employment for the Last Ten Fiscal Years (Chart)	19
Tourism Indicators for the Last Ten Fiscal Years	20

## **INTRODUCTORY SECTION**



Juan C. Méndez Torres, Esq., CPA  
Secretary

April 8, 2005

To the Honorable Governor of Puerto Rico,  
Members of the Legislature, and People of Puerto Rico:

It is a pleasure to submit, for your information, the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Puerto Rico (the Commonwealth) as of and for the fiscal year ended June 30, 2004. This report, presented in three sections, Introductory, Financial, and Statistical, is the primary means of reporting the Commonwealth's financial activities.

The introductory section, which is not audited, includes this letter of transmittal, general information about the Commonwealth, a list of the Commonwealth's principal elected and appointed officials at the balance sheet date, an organizational chart, and a reproduction of the Certificate of Achievement for Excellence in Financial Reporting that the Commonwealth received for its June 30, 2002 CAFR. The Financial Section contains the independent auditors' report, management's discussion and analysis (MD&A), and the basic financial statements as listed in the table of contents. The financial section also includes the notes to the basic financial statements, required supplementary information, and other supplementary information. The statistical section, which is not audited, includes selected financial and demographic information, generally presented on a multi-year basis.

### **PROFILE OF THE COMMONWEALTH**

The Puerto Rico Department of the Treasury is responsible for the preparation of this report. The responsibility for the accuracy of presented data and the completeness and fairness of the presentation, including all of the disclosures, rests on the Commonwealth's management. To the best of our knowledge and belief, the following data, as presented, is accurate in all material respects, and is presented in a manner designed to set forth the financial position and the results of operations of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth as of June 30, 2004 and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America. We have included all the necessary disclosures to enable the reader to gain a thorough understanding of the Commonwealth's activities.

Page 2

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

The financial reporting entity includes all funds of the Commonwealth, which is the primary government, as well as all its component units. In accordance with Governmental Accounting Standards Board Statement No. 14, the Commonwealth's financial reporting entity includes 50 component units; 6 are blended component units including 3 fiduciary component units, 7 major discretely presented component units, and 37 nonmajor discretely presented component units. Component units are legally separate entities for which the primary government is financially accountable, or other organizations, the nature and significance of whose relationship with the Commonwealth are such that exclusion would cause the Commonwealth's basic financial statements to be misleading and incomplete. Blended component units, although legally separate entities, are, in substance, part of the primary government's operations and are included as part of the primary government. Discretely presented component units, both major and nonmajor, are reported in a separate column in the government-wide financial statements to emphasize that they are not part of the primary government and to differentiate their financial position and results of operations from those of the primary government.

Generally, each component unit issues audited financial statements, which can be obtained from the component unit's administrative offices. The basic financial statements included in the financial section of this CAFR provide descriptions of the operations of each of the following component units of the Commonwealth:

*Blended Component Units:*

Public Buildings Authority  
Puerto Rico Maritime Shipping Authority  
The Children's Trust

*Discretely Presented Component Units:*

Agricultural Services and Development Administration  
Automobile Accident Compensation Administration  
Cardiovascular Center Corporation of Puerto Rico and the Caribbean  
Caribbean Basin Projects Financing Authority  
Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico  
Economic Development Bank for Puerto Rico  
Employment and Training Enterprises Corporation  
Farm Insurance Corporation of Puerto Rico  
Fine Arts Center Corporation  
Governing Board of the 9-1-1 Service  
Government Development Bank for Puerto Rico  
Institutional Trust of the National Guard of Puerto Rico  
Musical Arts Corporation  
National Parks Company of Puerto Rico  
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives  
Puerto Rico Aqueduct and Sewer Authority

Page 3

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

Puerto Rico Land Authority  
Puerto Rico Conservatory of Music Corporation  
Puerto Rico Convention Center District Authority  
Puerto Rico Council on Higher Education  
Puerto Rico Electric Power Authority  
Puerto Rico Exports Development Corporation  
Puerto Rico Government Investment Trust Fund  
Puerto Rico Health Insurance Administration  
Puerto Rico Highway and Transportation Authority  
Puerto Rico Industrial Development Company  
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities  
Financing Authority  
Puerto Rico Infrastructure Financing Authority  
Puerto Rico Land Administration  
Puerto Rico Maritime Transportation Authority  
Puerto Rico Medical Services Administration  
Puerto Rico Metropolitan Bus Authority  
Puerto Rico Municipal Finance Agency  
Puerto Rico Ports Authority  
Puerto Rico Public Broadcasting Corporation  
Puerto Rico School of Plastic Arts  
Puerto Rico Solid Waste Authority  
Puerto Rico Telephone Authority  
Puerto Rico Trade and Export Company  
Right to Employment Administration  
Special Communities Perpetual Trust  
State Insurance Fund Corporation  
Tourism Company of Puerto Rico  
University of Puerto Rico

*Fiduciary Component Units:*

Employees Retirement System of the Government of Puerto Rico and its Instrumentalities  
Puerto Rico Judiciary Retirement System  
Puerto Rico System of Annuities and Pensions for Teachers

**Change in Administration**

As a result of general elections, which took place in November 2004, a new administration took office in January 2005. The list of Commonwealth's elected and appointed officials included within the introductory section corresponds to those officials who held office as of June 30, 2004.



SECRETARY OF THE TREASURY

Page 4

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

### **Independent Auditors**

Commonwealth statutes require an annual audit by independent certified public accountants. The firm of KPMG LLP was selected by the Commonwealth to perform the audit of the basic financial statements in accordance with auditing standards generally accepted in the United States of America for the fiscal year 2003-2004. The goal of the independent audit was to provide reasonable assurance that the financial statements of the Commonwealth for the fiscal year ended June 30, 2004, are free of material misstatements. The independent auditor's report on the basic financial statements is included in the financial section of this report.

### **Internal Controls**

The management of the Commonwealth is responsible for establishing and maintaining internal controls to ensure that assets of the Commonwealth are protected from loss, theft, or misuse, and that adequate accounting data is compiled for the preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. The internal controls are designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

As a recipient of federal assistance, the Commonwealth is also responsible for ensuring that internal controls are in place to ensure that documents and processes are in compliance with applicable laws and regulations related to such federal financial assistance programs.

Certain departments, agencies, and political subdivisions are subject to the requirements of the U.S. Office of Management and Budget Circular A-133. As a result, these entities are audited for compliance with the requirements of the federal financial assistance programs. These audits are performed at the department or agency level. The Commonwealth has provided for the possible cost disallowance that may arise from these audits, as well as from other audits that may be performed by federal grantors.

### **Budget and Fiscal Policy**

The fiscal year of the Commonwealth begins each July 1. The Governor is constitutionally required to submit to the Legislature an annual balanced budget of capital improvements and operating expenses of the Central Government for the ensuing fiscal year.

The annual budget is prepared by the Puerto Rico Office of Management and Budget, working with the Puerto Rico Planning Board, the Puerto Rico Department of the Treasury, and other government offices and agencies. Section 7 of Article 6 of the Constitution provides that *"The appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."*



SECRETARY OF THE TREASURY

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

The Commonwealth maintains extensive budgetary controls. The objective of these controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the Legislature. Activities of the general fund are included in the annual appropriated budget. Budgetary control resides at the department level. The Commonwealth also maintains an encumbrance accounting system as one method of maintaining budgetary control.

The annual budget, which is developed using elements of performance-based program budgeting and zero-based budgeting, includes an estimate of revenue and other resources for the ensuing fiscal year under laws existing at the time the budget is submitted and legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in her judgment are necessary, convenient and in conformity with the four-year investment plan prepared by the Puerto Rico Planning Board.

The Legislature may amend the budget submitted by the Governor, but may not increase items that would cause a deficit without imposing additional taxes to cover such deficit. Once approved by the Legislature, the budget is referred to the Governor, who may decrease or eliminate any item, but may not increase or insert new items in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature with his objections. The Legislature, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, as originally approved by the Legislature and the Governor, it is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This allows the Commonwealth to continue to pay operating and other expenses until a new budget is approved.

### **Governmental Activities**

General governmental activities of the Commonwealth are accounted for in four governmental funds. These funds are: general, special revenue, debt service, and capital project. The general fund is the primary operating fund of the Commonwealth. The general fund is used to account for resources traditionally associated with government, which are not required legally or by sound financial management to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, education, and economic development. Other major funds are the debt service fund, which accounts for the accumulation of resources predominantly for, and the payment of the Commonwealth general long-term bonds' principal, interest and related costs, the Public Buildings Authority capital project fund, which accounts for the financial resources used for the acquisition and construction of major capital facilities, and The Children's Trust special revenue fund which accounts for the moneys received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The financial resources received by this fund are used to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico. Nonmajor governmental funds are combined in a single column in the governmental fund financial statements, and individually identified in the supplementary combining nonmajor governmental funds financial statements of this report.



Page 6  
Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

### **Business-Type Activities**

Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the government is that the costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or where the government has decided that periodic determination of net income is appropriate for accountability purposes.

The Commonwealth's proprietary operations comprise the following activities: the unemployment insurance trust fund, and the Lottery of Puerto Rico and the Additional Lottery System (the Lotteries Fund), both major funds. The Puerto Rico Water Pollution Control Revolving Fund, the Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund, the Disability Insurance Fund, and the Drivers' Insurance Fund are all nonmajor proprietary funds combined in a single column in the proprietary fund financial statements, and individually identified in the supplementary combining nonmajor proprietary funds financial statements of this report.

### **Fiduciary Operations**

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity or as an agent for individuals, private organizations, and other governmental units. These include the pension trust and agency funds. Pension trust funds are established through trust agreements specifying how the fund will operate. Agency funds are custodial in nature and do not report fund balances. The pension trust funds include the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities, the Puerto Rico Judiciary Retirement System, and the Puerto Rico System of Annuities and Pensions for Teachers.

Agency funds consist of the Special Deposits Fund. This agency fund includes deposits under the custody of the Courts of Justice for alimony payments, deposits under the custody of the Commissioner of Insurance of the Commonwealth for escheated property, and for insurance companies under bankruptcy.

### **Cash Management Policies and Practices**

The Commonwealth maintains a cash pool for its cash and cash equivalents. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing accounts in the Government Development Bank for Puerto Rico (GDB), a discretely presented component unit. In addition, the Puerto Rico Government Investment Trust Fund (PRGITF), was created by the Commonwealth pursuant to Act No. 176 of August 11, 1995, and began operations on December 4, 1995. PRGITF is a no-load diversified collective investment trust that was created for the purpose of providing eligible investors with a convenient and economical way to invest in a professionally managed money market portfolio. The deposits on hand and the investments purchased are not collateralized, secured, or guaranteed by the Commonwealth or any of its agencies, instrumentalities, or political subdivisions.

The Commonwealth's investment policy is to minimize credit and market risk while maintaining a competitive yield on its portfolio. The cash temporarily idle during this year was invested mainly in U.S.



SECRETARY OF THE TREASURY

Page 7

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

government securities, stocks, corporate bonds, repurchase agreements, Commonwealth securities, trading securities, and short-term investments. These are primary government investments that are restricted and unrestricted.

### **Capital Assets**

These basic financial statements include the capital assets of the Commonwealth. A discussion of capital assets accounting is included in the Management's Discussion and Analysis that is part of the basic financial statements. More detailed information about capital assets can be found in the notes to the basic financial statements.

### **Debt Administration**

As of June 30, 2004, the Commonwealth had a number of debt issues outstanding. The Commonwealth has maintained an A- credit rating from Standard and Poor's Corporation and a Baa1 from Moody's Investor Service on general obligation bond issues. We are focusing our efforts to maintain or improve this classification.

Section 2 of Article VI of the Constitution of Puerto Rico provides that direct obligations of the Commonwealth evidenced by full faith and credit bonds or notes shall not be issued if the amount of the principal of and interest on such bonds and notes and on all such bonds and notes theretofore issued which is payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on accounts of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenues raised under the provisions of the Commonwealth Legislation and covered into Treasury of Puerto Rico in the two fiscal year preceding the current fiscal year. Section 2 of Article VI does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded. See the computation of the Legal Debt Margin on page 3 in the Statistical Section. More detailed information about long-term debt can be found in the notes to the basic financial statements.

### **Risk Financing**

The Commonwealth purchases commercial insurance to cover casualty, theft, tort claims, and other losses. The current insurance policies have not been canceled or terminated. As it relates to worker's compensation, the Commonwealth's discretely presented component unit, the State Insurance Fund Corporation, provides workers' compensation to both public and private employees.

### **Financial Advisor and Fiscal Agent**

The principal functions of GDB are to act as financial advisor to and fiscal agent for the Commonwealth, its municipalities, and public corporations, in connection with the issuance of bonds and notes, and to make loans to private enterprises to aid the economic development of Puerto Rico. GDB was the first governmental entity in Puerto Rico to obtain a Certificate of Achievement for Excellence in Financial Reporting for its



SECRETARY OF THE TREASURY

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

CAFR. It has received the award for the years ended June 30, 1994 through 2002. GDB is presented as a major discretely presented component unit.

## ECONOMIC CONDITIONS AND OUTLOOK

Puerto Rico enjoyed almost two decades of economic expansion through fiscal year 2001. Almost every sector of the economy participated, and record levels of employment were achieved. Factors behind this expansion included government-sponsored economic development programs, periodic declines in the value of the U.S. dollar, which is the currency used in the Commonwealth, increases in the level of federal transfers, a significant expansion in construction investment driven by infrastructure projects and private investment, primarily in housing, and the relatively low cost of borrowing.

Puerto Rico has a diversified economy with manufacturing and services comprising its principal sectors. The economy of Puerto Rico is closely linked to the United States economy. The following exogenous variables are affected by the United States economy: exports, direct investment, transfer payments, interest rates, inflation, and tourist expenditures. During fiscal year 2004 (July 2003 through June 2004), approximately 83% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 45% of Puerto Rico's imports. In fiscal year 2004, Puerto Rico experienced a \$16.1 billion positive merchandise trade balance.

Puerto Rico has a diversified economy with manufacturing and services comprising its principal sectors. Manufacturing is the largest sector in terms of gross domestic product. The Puerto Rico Planning Board estimates that in fiscal year 2004 manufacturing generated \$34.0 billion, or 43.0%, of gross domestic product, as compared with fiscal year 2003 when it generated \$31.3 billion, or 42.0%, of gross domestic product. Manufacturing in Puerto Rico is now more diversified than during the earlier phases of its industrial development and includes several industries less prone to business cycles. In the last three decades, industrial development has tended to be more capital intensive and more dependent on skilled labor.

The services sector, which includes finance, insurance, real estate, wholesale and retail trade, tourism, and other services generated \$30.5 billion, or 38.69%, of Puerto Rico's gross domestic product in fiscal year 2004, as compared with \$28.7 billion, or 38.63%, of gross domestic product in fiscal year 2003. The development of the services sector has shown a strong interaction with manufacturing, tourism, construction, and agriculture.

Tourism makes a significant contribution to economic activity. Total visitors' expenditures accounted for 3.8% of the island's gross domestic product in fiscal year 2004. An estimated 4.8 million visitors spent \$3.0 billion in Puerto Rico in fiscal year 2004. San Juan has become the largest home port for cruise ships in the Caribbean and the fourth largest home port for cruise ships in the world. During the year 2004, the number of persons registered in tourist hotels increased 5.5% in comparison with fiscal year 2003, when tourism was adversely affected by 9/11. The construction sector contributed to the economic activity from fiscal year 1999 through fiscal year 2004. During that period, construction investment increased 1.1%. Puerto Rico is heavily dependent on oil imports for the production of electricity. As a result of the construction of two cogeneration plants, however, one of which is fueled by liquefied natural gas and the other by coal, Puerto Rico's dependence on oil imports for the production of electricity has been reduced from 99% to 72%.



Page 9

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

The Puerto Rico Planning Board's preliminary reports of the performance of the Puerto Rico economy during fiscal year 2004 indicate that the economy registered a nominal increase of 5.2% in total gross product. Gross product in fiscal year 1999 was \$38.3 billion and gross product in fiscal year 2004 was \$50.3 billion. This represents an increase in gross product of 31.3% from fiscal year 1999 to fiscal year 2004.

In terms of personal income, in fiscal year 2004, aggregate personal income was \$46.7 billion and personal income per capita was \$12,031.

According to the Department of Labor and Human Resources Household Employment Survey, during fiscal year 2004, total monthly employment averaged 1,234,200 compared to 1,210,000 in fiscal year 2003. Unemployment, although at relative low historical levels, remains above the United States average. The average unemployment rate decreased from 12.1% during fiscal year 2003 to 11.4% in fiscal year 2004.

## **Major Initiatives**

### ***Individual Income Taxes***

Resident individuals are subject to tax on their taxable income from all sources. As a result of legislation enacted in 1999 and 2000, there are several changes in income tax brackets applicable to future taxable years. However, due to significant limitation of available resources, the Commonwealth has deferred further reduction in income tax rates, in an effort to maintain revenue levels, and avoid budgetary shortfalls. On April 11, 2001, the Commonwealth approved legislation to reduce capital gain tax rate from 20% to 10%.

### ***Industrial Incentives Program***

#### ***U.S. Internal Revenue Code***

For many years, U.S. companies operating in Puerto Rico enjoyed a special tax credit that was available under Section 936 of the U.S. Internal Revenue Code. Originally, the credit provided an effective 100% federal income tax exemption for most operating income, as well as qualifying investment income from Puerto Rico sources. Amendments to Section 936 made in 1993 (the 1993 Amendments) instituted certain methods for calculating the tax credit and limited the amount of the credit that a qualifying company can claim. As a result of amendments incorporated in the Small Business Job Protection Act of 1996, (the 1996 Amendments), the tax credit is now being phased-out over a 10-year period for existing 936 credit claimants and is no longer available for corporations that established operations in Puerto Rico after October 13, 1995 (including existing 936 Corporations, if they establish new product lines in Puerto Rico). The 1996 Amendments also moved the credit based on the economic activity limitation to Section 30A of the Code and phased it out over 10 years. In addition, the 1996 Amendments eliminated the credit previously available for income derived from certain qualified investments in Puerto Rico.

Because of the credit limitations and impending phase-out of Sections 30A and 936, a large number of entities previously operating under the provisions of those sections have restructured their operations in Puerto Rico, in whole or in part, to become controlled foreign corporations (CFC). The Puerto Rico Office of Tax



SECRETARY OF THE TREASURY

Page 10  
Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

Exemption has received notification of over 60 corporations that have converted part or all of their operations under Puerto Rico tax incentives laws to CFCs. These include most major pharmaceutical, instrument, and electronics manufacturing companies in Puerto Rico. CFCs operate under transfer pricing rules for intangible income that are different from those corporations operating under Sections 30A and 936. In many cases, they are allowed to attribute a larger share of this income to their Puerto Rico operations, but must make a royalty payment “commensurate with income” to their U.S. affiliates. Section 936 companies were exempted from Puerto Rico withholding taxes on any cost-sharing payments they might have opted to make, but CFCs are subject to a 10% Puerto Rico withholding tax on royalty payments.

Also, due to the phase-out of Sections 30A and 936 of the Code, the U.S. Senate designated a special commission through the General Accounting Office to study the economic impact of said phase-out and to present recommendations on alternative tax incentives for U.S.-based companies operating in Puerto Rico. In the meantime, most U.S.-based companies operating under Sections 30A and 936 of the Code have converted from U.S. corporations to Puerto Rico or a foreign corporation, which has lessened the impact of the phase-out of those sections.

#### *Public Sector Debt*

Historically, the Commonwealth has maintained, as a matter of fiscal policy, a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. During certain fiscal years, however, public sector debt increased at a greater rate than the rate of gross product primarily due to an increase in the amount of debt incurred to finance certain key infrastructure projects, which are important to the development of the economy and are expected to produce long-term economic benefits, and debt incurred to refinance outstanding debt to enable Puerto Rico to benefit from the historically low levels of interest rates and realize debt service savings. During fiscal year 2004, public sector debt increased 14.3%.

#### *Prospects for the Future*

The Commonwealth is committed to research and pursue solutions to improve the Commonwealth’s competitive economic performance and the quality of life for its citizens. The Governor of Puerto Rico has established three long-range priorities which he expressed in his March 2005 state of the Commonwealth message. Those priorities, named “El Triángulo del Éxito”, are: (1) to provide a new economy which generates new employments providing its citizens with the best quality of life; (2) to provide a safe society; and (3) to establish an excellent educational system for the benefit of the children.

The Commonwealth’s economic development program is based on the fundamental, interrelated changes in technology, demographics, and institutions, which are transforming the global economy. These changes provide the challenges and opportunities that encompass the economic development strategy.



SECRETARY OF THE TREASURY

Page 11

Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

The economic program is based on: (1) re-focus the economy on bio-technology, telecommunications, technology information and related sectors; (2) "Apoyo al de aqui" to create new Puerto Rican enterprises; and (3) infrastructure economic planning.

Initiatives to achieve the economic development program objectives have begun in the following five areas: (1) legislation towards economic development through tax and fiscal reform; (2) consolidation and reductions of governmental entities; (3) refocused strategic projects towards excise taxes; (4) reduction on subsidies provided to governmental entities; and (5) refocused strategic projects related to the citizen's health.

### **Financial Condition**

The MD&A, which can be found immediately following the independent auditor's report, provides an overview of the Commonwealth's financial activities addressing both governmental and business-type activities reported in the government-wide financial statements. In addition, the MD&A focuses on the Commonwealth's major funds. Component units and fiduciary activities are excluded from the MD&A.

### ***Estimated Fiscal Year 2005 Compared to Actual Fiscal Year 2004***

It is projected that the general fund total revenue for fiscal year 2005 will be \$8,304 million, representing an increase of \$319 million, or 4%, from preliminary fiscal year 2004 revenue. The major changes from fiscal year 2004 are expected to be: (1) increases in income taxes of \$259 million; (2) increases in excise taxes of \$86 million; and (3) decreases in non-tax revenues of \$26 million.

### **Other Information**

#### ***Certificate of Achievement***

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a ***Certificate of Achievement for Excellence in Financial Reporting*** to the Commonwealth for its CAFR for the fiscal years ended from June 1996 through 2002. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for the preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only.

We believe the Comprehensive Annual Financial Report of the Commonwealth of Puerto Rico as of and for the fiscal year ended June 30, 2004 continues to conform to GFOA standards and we are submitting it to the GFOA to determine its eligibility for a Certificate of Achievement for Excellence in Financial Reporting.



SECRETARY OF THE TREASURY

Page 12  
Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
April 8, 2005

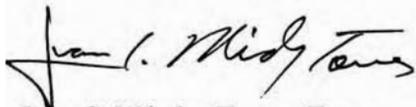
***Acknowledgements***

The preparation of this report requires the collective efforts of numerous finance personnel throughout the Commonwealth and is made possible only with the cooperation and support of the Executive, Legislative, and Judicial branch agencies, universities, and component units of the Commonwealth. We sincerely appreciate the dedicated efforts of all these individuals.

The report could not have been accomplished without the professionalism and dedication of CPA Miguel Rivera Rivera from our accounting team as well as the rest of the personnel of the central government accounting area. Also, we would like to give special thanks to our independent auditors, KPMG LLP, for their advice and commitment.

This report continues our commitment to the citizens of the Commonwealth of Puerto Rico, the Governor, the Legislature, and the financial community, to maintain our general purpose financial statements in conformance with the highest standards of financial accountability.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Juan C. Méndez Torres". The signature is written in a cursive style with a large initial 'J'.

Juan C. Méndez Torres, Esq.  
Secretary of the Treasury

## COMMONWEALTH OF PUERTO RICO

### PRINCIPAL OFFICIALS

As of June 30, 2004

**Sila M. Calderón**  
Governor

### Members of the Cabinet

**César Miranda**  
Chief of Staff

**José M. Izquierdo**  
Secretary of State

**Anabelle Rodríguez**  
Secretary of Justice

**Juan A. Flores Galarza**  
Secretary of the Treasury

**César A. Rey Hernández**  
Secretary of Education

**Frank Zorrilla Maldonado**  
Secretary of Labor and  
Human Resources

**Johnny V. Rullán**  
Secretary of Health

**Luis Rivero Cubano**  
Secretary of Agriculture

**Fernando E. Fagundo**  
Secretary of Transportation and  
Public Works

**Milton Segarra**  
Secretary of Economic  
Development and Commerce

**Yolanda Zayas Santana**  
Secretary of Family Affairs

**Ileana Echegoyen**  
Secretary of Housing

**Luis E. Rodríguez**  
Secretary of Natural and  
Environmental Resources

**Fernando Torres Ramírez**  
Interim Secretary of  
Consumer Affairs

**Jorge L. Rosario**  
Secretary of Sports and  
Recreation

**Miguel A. Pereira**  
Secretary of Corrections and  
Rehabilitation

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### LEGISLATIVE OFFICERS

As of June 30, 2004

**Antonio Fas Alzamora**  
President, Senate

**Carlos Vizcarrondo**  
Speaker, House of  
Representatives

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### FISCAL OFFICERS

As of June 30, 2004

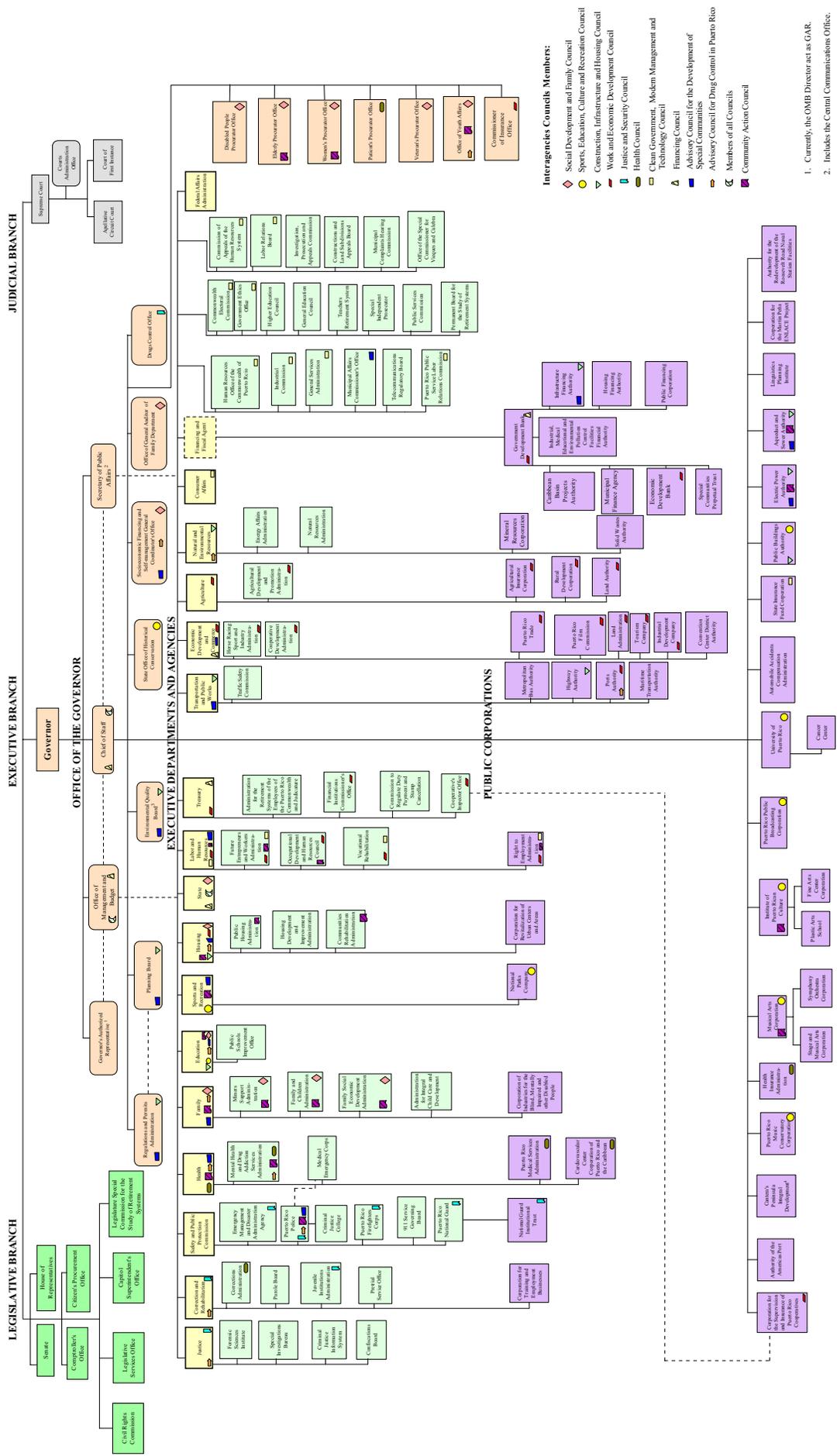
**Melba Acosta**  
Director, Office of Management  
and Budget

**Antonio Faria**  
President, Government  
Development Bank for  
Puerto Rico

## ORGANIZATIONAL CHART



# COMMONWEALTH OF PUERTO RICO



- Intergovernmental Councils Members:**
- Social Development and Family Council
  - Sports, Education, Culture and Recreation Council
  - Construction, Infrastructure and Housing Council
  - Work and Economic Development Council
  - Health Council
  - Clean Government, Modern Management and Technology Council
  - Financing Council
  - Advisory Council for the Development of Special Communities
  - Advisory Council for Drug Control in Puerto Rico
  - Members of all Councils
  - Community Action Council

1. Currently, the OMB Director acts as GAR.
2. Includes the Central Communications Office.
3. Includes the Commission for the Sustainable Development of Puerto Rico.
4. Is valid until July 10, 2007, renewable for an additional 15 years or until the debts are cancelled.

Reviewed April 2005

## FINANCIAL SECTION



**KPMG LLP**  
American International Plaza  
Suite 1100  
250 Muñoz Rivera Avenue  
San Juan, PR 00918-1819

## **Independent Auditors' Report**

The Honorable Governor and Legislature of the  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Puerto Rico (the Commonwealth) as of and for the year ended June 30, 2004, which collectively comprise the Commonwealth's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Commonwealth's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Public Buildings Authority capital project fund (a major fund) which represents 4% and 0%, respectively, of the assets and revenue of the governmental activities. We also did not audit the financial statements of the following activities, funds, and component units:

- Puerto Rico Public Housing Administration, the Office for the Improvements of Public Schools, Human Resources and Occupational Development Council, and the Office for the Administration of the Assets of CRUV Attached to the Puerto Rico Department of Housing which collectively represent 27% and 4%, respectively, of the assets and revenue of the general fund and 8% and 6%, respectively, of the assets and revenue of the governmental activities,
- The Additional Lottery System, which represents 77% and 39%, respectively, of the assets and revenue of the lotteries fund and 23% and 30%, respectively, of the assets and revenue of the business-type activities,
- Public Buildings Authority special revenue and debt service funds, which collectively represent 4% and 1%, respectively, of the assets and revenue of the aggregate remaining fund information and 2% and 0%, respectively, of the assets and revenue of the governmental activities,
- The pension trust funds, which represent 73% and 94%, respectively, of the assets and revenue of the aggregate remaining fund information, and
- Entities identified in note 2, that are presented as discretely presented component units, which collectively represent 65% and 85%, respectively, of the assets and revenue of the aggregate discretely presented component units.



These financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Puerto Rico, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 through 19 and the schedule of funding progress on page 141 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's basic financial statements. The combining and individual fund financial statements and schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. These financial statements and combining schedules have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and in our opinion, based on our audit and the report of the other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections of this report listed in the table of contents have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

KPMG LLP

April 8, 2005

Stamp No. 1995399 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

Management of the Commonwealth of Puerto Rico (the Commonwealth) provides this Management's Discussion and Analysis for the readers of the Commonwealth's basic financial statements. This narrative overview and analysis of the financial activities of the Commonwealth is for the fiscal year ended June 30, 2004, and is intended to provide an easily readable explanation of the information provided in the attached basic financial statements. We encourage readers to consider this information with the Commonwealth's basic financial statements that follow.

### FINANCIAL HIGHLIGHTS – PRIMARY GOVERNMENT

#### Government-wide Highlights

- The Commonwealth reported a deficit of \$12.8 billion as of June 30, 2004, a deterioration in financial position of \$2.7 billion from last year's balances. The accumulated deficit is principally the result of the Commonwealth's practice of issuing debt and transferring such funds to its discretely presented component units in order for them to carry out the corresponding construction programs.
- The Commonwealth's total deficit increased by \$2.7 billion (a 26% increase) as a result of this year's operations. The governmental activities deficit increased by \$2.8 billion (a 25% increase), while net assets of the business-type activities showed an increase of \$116 thousand (a 16% increase).
- The Commonwealth's governmental activities had total revenue of \$12.2 billion, which were exceeded by total expenses of \$15.2 billion, excluding transfers received from business-type activities amounting to \$203 million and a special item arising from the transfer of certain properties to municipalities amounting to \$36 million.
- The Commonwealth's business-type activities had total revenue of \$1.2 billion, which exceeded total expenses of \$901 million, excluding transfers made to the governmental activities amounting to \$203 million.

#### Fund Highlights

- As of June 30, 2004, the Commonwealth's governmental funds reported a combined ending fund balance of \$1 billion, an increase of \$164 million in comparison with the prior year.
- The general fund reported a deficit of \$366 million as of June 30, 2004.

#### Long-Term Debt

- Total long-term obligations as of June 30, 2004 were \$23 billion, from which \$2.5 billion are due within one year.
- The Commonwealth's total long-term obligations increased by \$4 billion (21%) during the current fiscal year.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Commonwealth's basic financial statements. The Commonwealth's basic financial statements include three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains additional required supplementary information in addition to the basic financial statements themselves. These components are described below:

#### **Basic Financial Statements**

The basic financial statements include two kinds of financial statements that present different views of the Commonwealth—the government-wide financial statements and the fund financial statements and combining major component units financial statements. These financial statements also include the notes to the basic financial statements that explain some of the information in the financial statements and provide more detail.

#### ***Government-wide Financial Statements***

The government-wide financial statements provide a broad view of the Commonwealth's operations in a manner similar to a private sector business. The statements provide both short- and long-term information about the Commonwealth's financial position, which assists in assessing the Commonwealth's economic condition at the end of the fiscal year. These are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most businesses. They take into account all revenue and expenses connected with the fiscal year even if cash involved has not been received or paid. The government-wide financial statements include two statements:

- ***Statement of Net Assets*** – This presents all of the government's assets and liabilities with the difference between the two reported as net assets (deficit). Over time, increases or decreases in the Commonwealth's net assets (deficit) may serve as a useful indicator of whether the financial position of the Commonwealth is improving or deteriorating.
- ***Statement of Activities*** – This presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenue for each function of the Commonwealth.

Both of the above financial statements have separate sections for three different types of Commonwealth programs or activities. These three types of activities are as follows:

- ***Governmental Activities*** – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with Commonwealth government fall into this category, including general government, public safety, health, public housing and welfare, education, and economic development.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

- ***Business-Type Activities*** – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Commonwealth include the operations of the following major funds: unemployment insurance trust fund (by the Commonwealth Employment Security Bureau) and the lotteries.
- ***Component Units*** – These are organizations that are legally separate from the Commonwealth, but the Commonwealth is either financially accountable for them, or the nature and significance of their relationship with the Commonwealth is such that their exclusion would cause the Commonwealth's financial statements to be misleading or incomplete. The Commonwealth has both blended and discretely presented component units.
  - ***Blended Component Units*** – Although legally separate entities, these are in substance part of the primary government's operations. Therefore, data from blended component units are integrated into the appropriate funds for reporting purposes.

The Commonwealth's three blended component units are:

- Public Buildings Authority
- Puerto Rico Maritime Shipping Authority
- The Children's Trust
- ***Discretely Presented Component Units*** – These are operations for which the Commonwealth has financial accountability but they have certain independent qualities as well. For the most part, these entities operate similar to private sector businesses and the business-type activities described above. The Commonwealth's discretely presented component units are presented in two categories, major and nonmajor. This separation is determined by the relative size of the entities' assets, liabilities, revenue and expenses in relation to the total of all component units.

The Commonwealth's 37 discretely presented nonmajor component units are combined into a single column for reporting in the fund financial statements. Complete financial statements of the individual component units can be obtained from their respective administrative offices. Addresses and other additional information about the Commonwealth's component units are presented in note 1 to the basic financial statements.

The Commonwealth's seven discretely presented major component units are:

- Government Development Bank
- Puerto Rico Highway and Transportation Authority
- Puerto Rico Electric Power Authority
- Puerto Rico Aqueduct and Sewer Authority
- Puerto Rico Infrastructure Financing Authority
- Puerto Rico Health Insurance Administration
- University of Puerto Rico

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

The government-wide financial statements can be found immediately following this discussion and analysis.

### ***Fund Financial Statements***

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Commonwealth, like other states and local governments, uses fund accounting to help ensure and demonstrate compliance with finance-related legal requirements. The fund financial statements focus on individual parts of the Commonwealth government, reporting the Commonwealth's operations in more detail than the government-wide statements. All of the funds of the Commonwealth can be divided into three categories. It is important to note that these fund categories use different accounting approaches and should be interpreted differently. The three categories of funds are the following:

- ***Governmental Funds Financial Statements*** – Most of the basic services provided by the Commonwealth are financed through governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, the governmental fund financial statements focus on near-term inflows and outflows of expendable resources. They also focus on the balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating the government's near-term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Commonwealth's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Commonwealth. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenue, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the governmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The Commonwealth has four major governmental funds. That is, each major fund is presented in a separate column in the governmental fund balance sheet and in the governmental fund statement of revenue, expenditures, and changes in fund balances. The Commonwealth's four major governmental funds are the general fund, The Children's Trust special revenue fund, the debt service fund, and the Public Buildings Authority capital projects fund. The remaining nonmajor governmental funds are grouped and presented in a single column in the governmental fund financial statements. The basic governmental funds financial statements can be found immediately following the government-wide financial statements.

- ***Proprietary Funds Financial Statements*** – These funds are used to show activities that operate more like those of commercial enterprises. Because these funds charge fees for services provided to outside customers including local governments, they are known as enterprise funds. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. Like the government-wide financial statements, proprietary fund financial statements use the accrual basis of accounting. There is no reconciliation needed between the government-wide financial statements for business-type activities and the

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

proprietary fund financial statements. The Commonwealth has two major enterprise funds. As previously mentioned, they are the operations of the unemployment insurance trust fund (administered by the Commonwealth's Employment Security Bureau) and the lotteries. Other nonmajor proprietary funds are grouped and presented in a separate column in the enterprise fund financial statements. The basic proprietary funds financial statements can be found immediately following the governmental fund financial statements.

- ***Fiduciary Funds and Similar Component Units Financial Statements*** – These funds are used to account for resources held for the benefit of parties outside the Commonwealth government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of these funds are not available to support the Commonwealth's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. They use the accrual basis of accounting. The Commonwealth's fiduciary funds are the pension trust funds (three separate retirement systems for employees, which are fiduciary component units of the Commonwealth), and the agency funds (which account for the assets held for distribution by the Commonwealth as an agent for other governmental units, other organizations, or individuals). The basic fiduciary funds and similar component units' financial statements can be found immediately following the proprietary fund financial statements.

### ***Component Units Financial Statements***

As mentioned above, these are operations for which the Commonwealth has financial accountability but they have certain independent qualities as well, and they operate similar to private-sector businesses. The government-wide financial statements present information for the component units in a single column of the statement of net assets. Also, some information on the statement of changes in net assets is aggregated for component units. The combining statements of net assets and the combining statement of activities provide detail for each major component unit and the nonmajor component units in aggregate. The basic combining financial statements for major component units can be found immediately following the fiduciary funds financial statements.

### ***Notes to the Financial Statements***

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and the fund financial statements. The notes to the financial statements can be found immediately following component units' financial statements.

### **Required Supplementary Information**

The basic financial statements include within its notes a section of required supplementary information. This section includes information of funding progress for the Commonwealth's three separate retirement systems.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### GOVERNMENT-WIDE FINANCIAL ANALYSIS

#### Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. Total assets and total liabilities of the Commonwealth's primary government at June 30, 2004 amounted to \$12.9 billion and \$25.7 billion, respectively, for a net deficit of \$12.8 billion, compared to \$10.1 billion net deficit at the beginning of the current year, as restated.

A portion of the Commonwealth's net assets (deficit) reflects its investment in capital assets such as land, buildings, and equipment, less any related debt used to acquire those assets that are still outstanding. The Commonwealth uses these capital assets to provide services to its residents; consequentially, these assets are not available for future spending. Although the Commonwealth's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Commonwealth's net assets (deficit) represents resources that are subject to external restrictions on how they may be used. An otherwise positive remaining balance would be used to meet the Commonwealth's ongoing obligations to its residents and creditors. Internally imposed designations of resources are not presented as restricted net assets. At the end of the current fiscal year, the Commonwealth is able to report positive balances in two categories of net assets, and a deficit, both for the government as a whole, as well as for its separate governmental and business-type activities.

As explained earlier, the net deficit of the primary government primarily results from the Commonwealth's practice of issuing debt and transferring such funds to the component units so that they can carry out the construction projects. The primary government retains the debt while the component units report the corresponding asset financed by such debt.

Total assets increased by \$1 billion during the fiscal year 2004 when compared to prior fiscal year. The key elements for this increase are as follows:

- Restricted cash increased by \$1 billion when compared to the prior year. This increase is primarily the result of unused proceeds from the issuance of facilities revenue bonds by the Public Buildings Authority amounting to \$490 million and from unused proceeds from capital fund program bonds amounting to \$734 million.
- Additions of capital assets and depreciation expense of \$491 million and \$188 million, respectively.

Total liabilities increased \$2.7 billion during the current fiscal year when compared to the prior fiscal year. The key elements for this increase are mostly due to net increase in debt issued or refunded by \$4.5 billion consisting of issuances during fiscal year 2004 of Commonwealth general obligation bonds, Commonwealth appropriation bonds and notes payable amounting to \$3.6 billion, \$888 million and \$5.5 billion, respectively, partially offset by repayments and defeasances of such debt in the amount of approximately \$7 billion.

**COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis

June 30, 2004

**Commonwealth's Net Assets – Primary Government  
June 30, 2004**

(expressed in thousands)

	<b>Governmental activities</b>	<b>Business-type activities</b>	<b>Total</b>
Current assets	\$ 2,989,468	884,062	3,873,530
Capital assets	6,099,129	1,672	6,100,801
Other assets	2,568,723	396,838	2,965,561
Total assets	11,657,320	1,282,572	12,939,892
Current liabilities	5,070,859	146,233	5,217,092
Noncurrent liabilities	20,242,807	284,510	20,527,317
Total liabilities	25,313,666	430,743	25,744,409
Invested in capital assets, net of related debt	3,133,230	1,672	3,134,902
Restricted	—	853,194	853,194
Unrestricted	(16,789,576)	(3,037)	(16,792,613)
Total net assets (deficit)	\$ (13,656,346)	851,829	(12,804,517)

**Commonwealth's Net Assets – Primary Government  
June 30, 2003**

(expressed in thousands)

	<b>Governmental activities</b>	<b>Business-type activities</b>	<b>Total</b>
Current assets	\$ 3,260,960	796,676	4,057,636
Capital assets	5,841,089	1,895	5,842,984
Other assets	1,432,203	431,650	1,863,853
Total assets	10,534,252	1,230,221	11,764,473
Current liabilities	5,411,156	274,402	5,685,558
Noncurrent liabilities	17,075,880	220,237	17,296,117
Total liabilities	22,487,036	494,639	22,981,675
Invested in capital assets, net of related debt	1,969,864	1,895	1,971,759
Restricted	19,749	736,947	756,696
Unrestricted	(13,942,397)	(3,260)	(13,945,657)
Total net assets (deficit)	\$ (11,952,784)	735,582	(11,217,202)

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### Changes in Net Assets

The Commonwealth's net deficit increased by \$2.7 billion or 26% from last year's total net deficit. Approximately 58% of the Commonwealth's total revenue came from taxes, while 28% resulted from grants and contributions (primarily federal financial assistance). Charges for various goods and services provided 14% of the total revenue. The Commonwealth's expenses cover a range of services. The largest expenses were for education, public housing and welfare, and health. In 2004, governmental activities' expenses exceeded program revenue, resulting in the use of \$8 billion in general revenue (mostly taxes). On the other hand, program revenue from business-type activities in 2004 exceeded expenses by approximately \$296 million, resulting in the use of \$24 million in other general revenue.

Governmental activities decreased the Commonwealth's net assets by \$2.8 billion, compared with a decrease of \$1.7 billion in the prior year. Key elements of this variance are as follows:

- Reduction of federal grant revenue by \$400 million.
- Increase of expenses of the Department of Education by \$189 million in 2004.
- Decrease in the transfer of land and recreational facilities to municipalities by \$168 million.

Business-type activities increased the Commonwealth's net assets by \$116 million. The key elements of this variance is the decrease in unemployment insurance benefits by \$201 million primarily caused by a reduction in the number of weeks for extended benefit payments as establish in the Job Creation and Worker Assistance Act of 2002 partially offset by an increase in lottery prizes expense of \$35 million.

**COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis

June 30, 2004

**Commonwealth of Puerto Rico's Changes in Net Assets – Primary Government  
Year ended June 30, 2004**  
(expressed in thousands)

	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
Revenue:			
Program revenue:			
Charges for services	\$ 769,207	1,136,705	1,905,912
Operating grants and contributions	3,462,924	59,728	1,098,504
Capital grants and contributions	167,907	-	2,592,055
	<u>4,400,038</u>	<u>1,196,433</u>	<u>5,596,471</u>
General revenue:			
Income taxes	5,191,080	-	5,191,080
Property taxes	121,815	-	121,815
Excise taxes	1,924,610	-	1,924,610
Other taxes	19,211	-	19,211
Revenue from component units	175,729	-	175,729
Other	399,615	23,831	423,446
	<u>7,832,060</u>	<u>23,831</u>	<u>7,855,891</u>
Total revenue	<u>12,232,098</u>	<u>1,220,264</u>	<u>13,452,362</u>
Expenses:			
General government	1,963,879	-	1,963,879
Public safety	1,950,635	-	1,950,635
Health	2,386,735	-	2,386,735
Public housing and welfare	2,919,315	-	2,919,315
Education	3,684,331	-	3,684,331
Economic development	896,925	-	896,925
Intergovernmental	591,237	-	591,237
Interest and other	778,700	26,763	805,463
Lotteries	-	731,344	731,344
Unemployment	-	142,652	142,652
Total expenses	<u>15,171,757</u>	<u>900,759</u>	<u>16,072,516</u>
(Decrease) increase in net assets before transfers and special item	(2,939,659)	319,505	(2,620,154)
Transfers	203,258	(203,258)	-
Special item – land and recreational facilities transferred to municipalities	<u>(35,646)</u>	-	<u>(35,646)</u>
Increase (decrease) in net assets	(2,772,047)	116,247	(2,655,800)
Net assets (deficit), beginning of year	(11,952,784)	735,582	(11,217,202)
Restatement to beginning net assets (deficit)	1,068,485	-	1,068,485
Net assets (deficit), end of year	<u>\$ (13,656,346)</u>	<u>851,829</u>	<u>(12,804,517)</u>

**COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis

June 30, 2004

**Commonwealth of Puerto Rico's Changes in Net Assets – Primary Government**  
**Year ended June 30, 2003**  
(expressed in thousands)

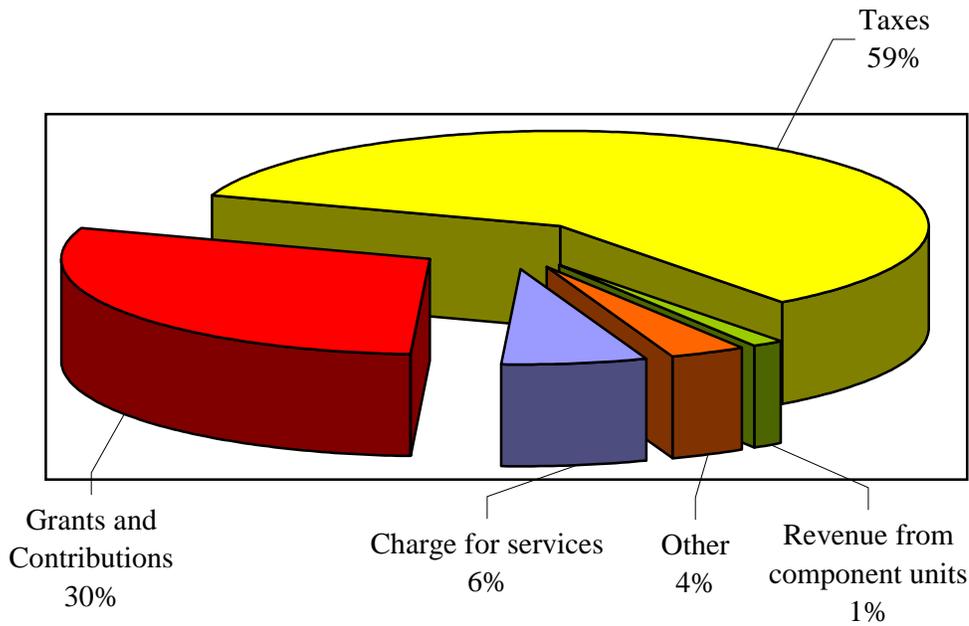
	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
Revenue:			
Program revenue:			
Charges for services	\$ 757,116	1,132,285	1,889,401
Operating grants and contributions	3,830,639	97,033	3,927,672
Capital grants and contributions	173,644	—	173,644
	<u>4,761,399</u>	<u>1,229,318</u>	<u>5,990,717</u>
General revenue:			
Income taxes	4,941,128	—	4,941,128
Property taxes	122,666	—	122,666
Excise taxes	1,894,729	—	1,894,729
Other taxes	3,055	—	3,055
Revenue from component units	111,752	1,038	112,790
Other	382,552	77,362	459,914
	<u>7,455,882</u>	<u>78,400</u>	<u>7,534,282</u>
Total revenue	<u>12,217,281</u>	<u>1,307,718</u>	<u>13,524,999</u>
Expenses:			
General government	2,324,715	—	2,324,715
Public safety	1,606,272	—	1,606,272
Health	1,903,811	—	1,903,811
Public housing and welfare	3,239,366	—	3,239,366
Education	3,375,815	—	3,375,815
Economic development	451,945	—	451,945
Intergovernmental	466,762	—	466,762
Interest and other	671,228	22,385	693,613
Lotteries	—	695,888	695,888
Unemployment	—	343,243	343,243
Total expenses	<u>14,039,914</u>	<u>1,061,516</u>	<u>15,101,430</u>
(Decrease) increase in net assets before transfers	(1,822,633)	246,202	(1,576,431)
Transfers	279,060	(279,060)	—
Special item – land and recreational facilities transferred to municipalities	(203,514)	—	(203,514)
Decrease in net assets	(1,747,087)	(32,858)	(1,779,945)
Net assets (deficit), beginning of year	(10,171,632)	768,440	(9,403,192)
Restatement to beginning net assets (deficit)	(34,065)	—	(34,065)
Net assets (deficit), end of year	\$ <u>(11,952,784)</u>	<u>735,582</u>	<u>(11,217,202)</u>

**COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis

June 30, 2004

**Revenue – Governmental Activities  
Year ended June 30, 2004**



**Expenses – Governmental Activities  
Year ended June 30, 2004  
(expressed in thousands)**

<u>Functions</u>	<u>Expenses</u>
<b>Primary government:</b>	
<b>Governmental activities:</b>	
General government	\$ 1,963,879
Public safety	1,950,635
Health	2,386,735
Public housing and welfare	2,919,315
Education	3,684,331
Economic development	896,925
Intergovernmental	591,237
Interest and other	<u>778,700</u>
<b>Total governmental activities</b>	<b>\$ <u><u>15,171,757</u></u></b>

**COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis

June 30, 2004

**Governmental Activities**

Governmental activities increased the Commonwealth's net deficit to \$13.7 billion. The decrease in net assets by the business-type activities is explained below. A comparison of the cost of services by function for the Commonwealth's governmental activities is shown below, along with the revenue used to cover the net expenses of the governmental activities (expressed in thousands).

**Governmental Activities – Expenses Net of Program Revenue**  
**Year ended June 30, 2004**  
(expressed in thousands)

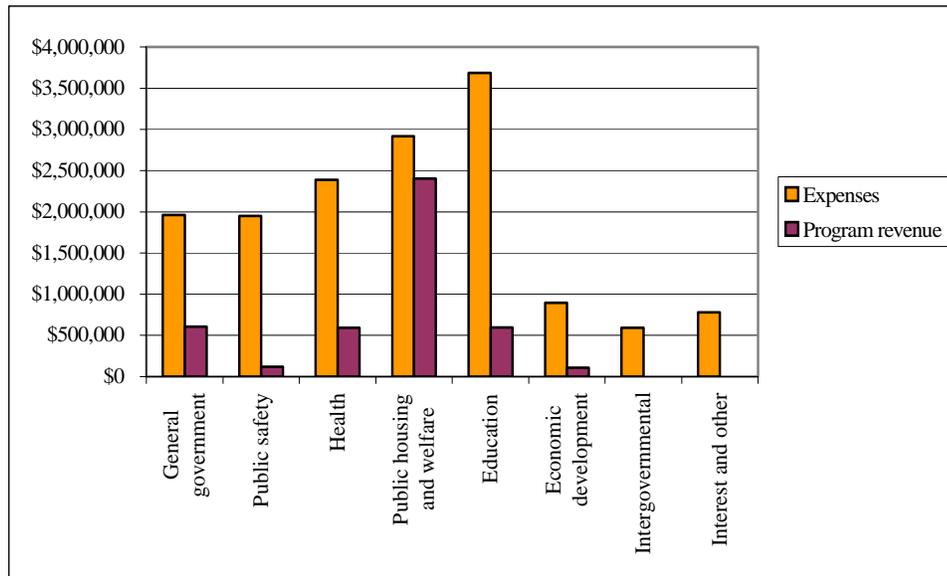
Expenses:		
General government	\$	(1,359,430)
Public safety		(1,831,726)
Health		(1,791,725)
Public housing and welfare		(516,338)
Education		(3,114,810)
Economic development		(787,753)
Intergovernmental		(591,237)
Interest and other		<u>(778,700)</u>
Total governmental activities expenses, net program revenue		(10,771,719)
General revenue:		
Taxes		7,256,716
Revenue from component units		175,729
Special item – land and recreational facilities transferred to the municipalities		(35,646)
Transfers from business type activities		203,258
Other revenue		<u>399,615</u>
Increase in governmental activities net deficit	\$	<u><u>(2,772,047)</u></u>

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### Expenses and Program Revenue – Governmental Activities Year ended June 30, 2004 (expressed in thousands)



### Business-Type Activities

The business-type activities increased the Commonwealth's net assets by \$116 million. This resulted predominantly from a \$19.8 million increase in net assets by the Commonwealth's loan revolving funds (nonmajor funds) and a \$104 million increase in the net assets of the unemployment insurance trust fund. The Commonwealth's revolving funds represent loan funds which receive operating and capitalization grants from the U.S. Environmental Protection Agency and generate interest income through its lending activities. The net assets presented in this fund primarily represent the accumulation of interest earnings since the fund's inception.

### FINANCIAL ANALYSIS OF THE COMMONWEALTH'S INDIVIDUAL FUNDS

As noted earlier, the Commonwealth uses fund accounting to help ensure and demonstrate compliance with finance-related legal requirements.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### Governmental Funds

The focus of the Commonwealth's governmental funds is to provide information on near-term inflows, outflows, and balances of expendable resources. Such information is useful in assessing the Commonwealth's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of the end of fiscal year 2004, the Commonwealth's governmental funds reported combined ending fund balance of \$1 billion, an increase of \$164 million or 19% in comparison with the prior year. The increase in the governmental fund balance is principally the result of unspent proceeds from the issuance of facilities revenue and capital program bonds, as discussed in the government-wide financial analysis section above, partially offset by a reduction in federal grant revenue of \$400 million and increases in public safety, educational and health expenditures in the aggregate amount of approximately \$780 million (see Budgetary Highlights section). There is \$1.2 billion of fund balance reserved to indicate that it is not available for new spending because it has already been committed (1) to liquidate contracts and purchase orders of the prior fiscal year, (2) to pay debt service, or (3) for a variety of other restricted purposes.

The general fund is the chief operating fund of the Commonwealth. At the end of the current fiscal year, unreserved fund deficit of the general fund was \$1.5 billion, while the total fund balance has a total deficit of \$366 million. The fund balance of the Commonwealth's general fund decreased by \$286 million as a result of the current fiscal year's change in financial position. This is a 356% decrease when compared to total fund balance reported in fiscal year 2003. Also, see additional related comments in the following section titled General Fund Budgetary Highlights.

### Proprietary Funds

The Commonwealth's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. As discussed in the business-type activities above, the Commonwealth's net assets increased by \$116 million as a result of operations in the proprietary funds. This resulted from a \$104 million increase (228% from prior year) in net assets by the unemployment insurance trust fund and an increase of net assets of \$12 million (45% from prior year) by the Commonwealth's other nonmajor enterprise funds.

### GENERAL FUND BUDGETARY HIGHLIGHTS

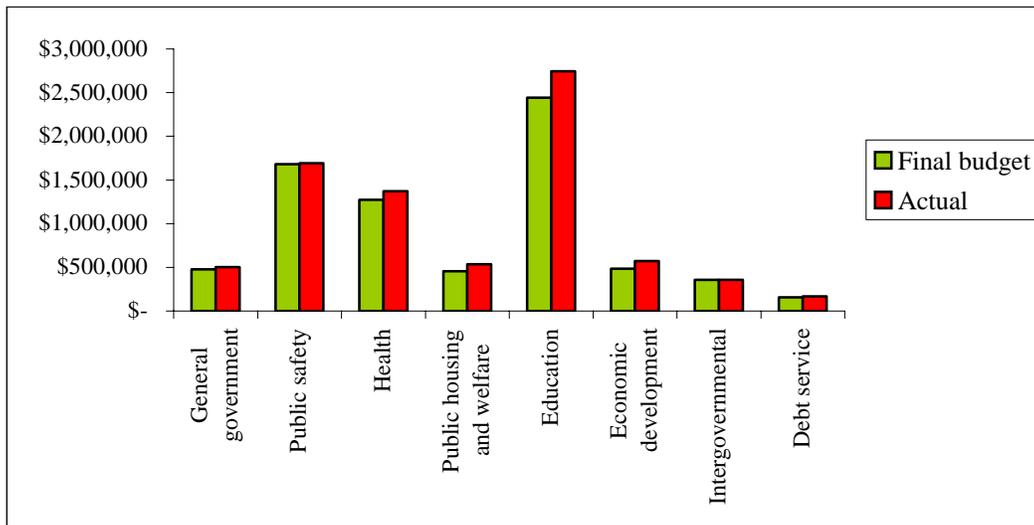
Actual revenues exceeded final budgeted revenue by \$62.8 million. The net increase was primarily attributed to revenue derived by a tax incentive plan designed to attract tax debtors, contributions made by component units to the general fund in excess of anticipated amounts and a decrease in excise tax revenue. Other revenue primarily comprised of fines, penalties, registration fees and custom duties also experienced an increase during 2004. The actual expenditures reflected an increase of \$613 million when compared to the final budgeted amounts. The variance in expenditures was predominantly caused by the Department of Education with \$302 million, the Department of Transportation and Public Works with \$80 million, the Department of Health with \$89 million, and the Department of Social Economic Development Administration with \$34 million. Most of these variances were financed through the use of borrowings which provided resources of \$695 million. The proceeds of these borrowings are presented separately in the statement of revenue and expenditures – budget and actual – budget basis – general fund. Transfers to other funds exceeded the final budget by \$15 million in addition to the shortfall in the transfers from other funds of \$237 million.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2004

### Expenditures – General Fund Budget vs. Actual Year ended June 30, 2004 (expressed in thousands)



As of June 30, 2004, there was an excess of expenditures and other uses over revenue and other sources of \$108 million.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

The Commonwealth's investment in capital assets for its governmental and business-type activities as of June 30, 2004, amounts to \$8.2 billion, an accumulated depreciation of \$2.1 billion, leaving a book value of \$6.1 billion. This investment in capital assets includes land, buildings, building improvements, equipment, and construction in progress.

The net book value of capital assets at June 30, 2004 is distributed by function/activity in the following proportions: general government, 17%; public safety, 14%; health, 4%; public housing and welfare, 35%; and education, 29%; and economic development 1%. Actual expenditures to purchase or construct capital assets were approximately \$1 billion for the year. Depreciation charges for the year totaled \$189 million.

The infrastructure assets representing items that are normally immovable and of value only to the Commonwealth as roads, highways, bridges, toll facilities, water and sewer systems, lighting production, transmission and distribution systems, and similar items are principally owned by the component units of the

**COMMONWEALTH OF PUERTO RICO**

Management’s Discussion and Analysis

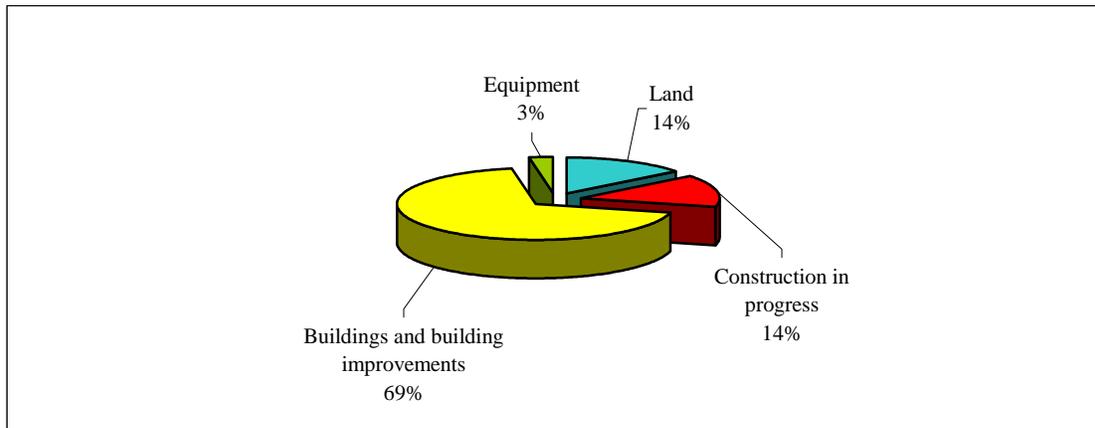
June 30, 2004

Commonwealth. Therefore, the infrastructure assets are reported within depreciable capital assets under the discretely presented component units’ column. Additional information on the Commonwealth’s capital assets can be found in note 12 to the basic financial statements that accompany this report.

**Commonwealth’s Capital Assets – Primary Government  
June 30, 2004**

(expressed in thousands)

	<u>Governmental activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Land	\$ 880,510	—	880,510
Construction in progress	881,482	—	881,482
Buildings and building improvements	4,172,434	—	4,172,434
Equipment	164,703	1,672	166,375
<b>Total capital assets</b>	<b>\$ 6,099,129</b>	<b>1,672</b>	<b>6,100,801</b>



**Debt Administration**

General obligation bonds are backed by the full faith and credit of the Commonwealth, including the Commonwealth’s power to levy additional taxes to help ensure repayment of the debt.

The Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth, are not to be issued if the amount of the principal of, and interest on, such bonds and notes and on all such bonds and notes issued thereafter which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenue raised under the provisions of Commonwealth legislation and conveyed into the Treasury in the two fiscal years preceding the then current fiscal year. Section 2, Article VI of the Constitution of the Commonwealth does not limit the amount of debt that the Commonwealth may guarantee so long as the 15%

## **COMMONWEALTH OF PUERTO RICO**

### **Management's Discussion and Analysis**

June 30, 2004

limitation is not exceeded. At June 30, 2004, the Commonwealth is in compliance with the debt limitation requirement.

Moody's and Standard & Poor's have given the Commonwealth's bonds ratings of "Baa1" and "A-", respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained only from the respective rating agency.

The Commonwealth's total long-term obligations increased by \$4 billion during the current fiscal year, representing a 21% increase. Additional information on the Commonwealth's long-term obligations can be found in note 14 to the basic financial statements of this report.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The unemployment rate for the Commonwealth of Puerto Rico is currently 11.4%, which is a decrease from a rate of 12.1% a year ago.

Based on the projections of the Puerto Rico Planning Board, the Puerto Rico economy is expected to reflect a real growth of 2.8% for the fiscal year 2005. In nominal terms, the projection of the Puerto Rico Planning Board anticipates an increase of 4.6% for the next fiscal year.

The consolidated budget for the fiscal year 2004-05 amounts to \$21.8 billion. From this amount, \$15.9 billion is assigned to operating expenses, \$3.3 billion to a permanent capital improvements program, and \$2.7 billion for the debt service.

### **REQUESTS FOR INFORMATION**

This financial report is designed to provide a general overview of the Commonwealth's finances for all of the Commonwealth's residents, taxpayers, customers, investors and creditors. This financial report seeks to demonstrate the Commonwealth's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to: Department of the Treasury of the Commonwealth of Puerto Rico, Área de Contabilidad Central, P.O. Box 9024140, San Juan, Puerto Rico 00902-4140.

COMMONWEALTH OF PUERTO RICO

Statement of Net Assets

June 30, 2004  
(In thousands)

Assets	Primary government			Component units
	Governmental activities	Business-type activities	Totals primary government	
Cash and cash equivalents	\$ 73,258	498,429	571,687	1,608,535
Cash and cash equivalents in governmental banks	810,945	296,144	1,107,089	497,476
Investments	409,175	34,141	443,316	3,766,716
Receivables, net of allowance for uncollectibles:				
Taxes	1,091,457	—	1,091,457	—
Unemployment insurance premiums	—	50,126	50,126	—
Intergovernmental	253,937	—	253,937	60,466
Accounts	133,046	—	133,046	627,022
Loans	944	—	944	3,193,797
Accrued interest	2,092	5,882	7,974	185,979
Other	7,598	8,684	16,282	115,635
Due from:				
Primary government	—	—	—	35,675
Component units	95,747	9,670	105,417	1,083,880
Other governmental entities	3,189	—	3,189	356,682
Internal balances	19,014	(19,014)	—	—
Inventories	26,714	—	26,714	261,354
Prepaid expenses	5,501	—	5,501	73,818
Other assets	56,851	—	56,851	—
Restricted assets:				
Cash and cash equivalents	1,244,948	—	1,244,948	611,200
Cash and cash equivalents in governmental banks	1,055,667	215,213	1,270,880	178,752
Other restricted assets	—	—	—	5,526,401
Long-term investments	—	—	—	1,160,156
Long-term receivables from:				
Intergovernmental	—	1,962	1,962	—
Loans	—	—	—	151,512
Long-term amounts due from:				
Primary government	—	—	—	81,470
Component units	—	142,880	142,880	32,364
Other governmental entities	—	—	—	12,830
Real estate held for sale or future development	64,114	—	64,114	258,057
Deferred expenses and other assets	203,994	36,783	240,777	450,055
Capital assets (net of accumulated depreciation):				
Land and other nondepreciable assets	1,761,992	—	1,761,992	12,155,011
Depreciable assets	4,337,137	1,672	4,338,809	14,411,308
Total assets	\$ 11,657,320	1,282,572	12,939,892	46,896,151

COMMONWEALTH OF PUERTO RICO

Statement of Net Assets, continued

June 30, 2004  
(In thousands)

Liabilities	Primary government			Component units
	Governmental activities	Business-type activities	Totals primary government	
Accounts payable and accrued liabilities	\$ 1,119,407	16,050	1,135,457	1,918,266
Deposits and escrow liabilities	—	—	—	4,634,882
Tax refunds payable	221,262	—	221,262	—
Due to:				
Primary government	—	—	—	65,696
Component units	37,940	—	37,940	895,660
Other governmental entities	—	—	—	18,560
Securities lending transactions and reverse repurchase agreements	—	—	—	382,637
Interest payable	296,937	—	296,937	399,261
Deferred revenue	137,960	18,966	156,926	122,842
Other current liabilities	104,794	—	104,794	114,010
Tax revenue anticipation notes	800,000	—	800,000	—
Liability for automobile accident insurance and workmen compensation claims	—	—	—	882,672
Liabilities payable within one year:				
Commonwealth appropriation bonds	53,442	—	53,442	9,194
Bonds	214,175	—	214,175	619,613
Notes	797,784	148	797,932	1,184,486
Capital leases	6,866	—	6,866	—
Compensated absences	915,449	2,890	918,339	187,304
Lottery prizes	—	37,071	37,071	—
Unemployment insurance payable	—	71,108	71,108	—
Other long-term liabilities	364,843	—	364,843	—
Due to primary government - long-term portion	—	—	—	182,601
Due to component units - long-term portion	—	—	—	226,119
Deferred revenue - long-term portion	43,034	—	43,034	10,477
Liabilities payable after one year:				
Commonwealth appropriation bonds	2,704,624	—	2,704,624	1,020,449
Bonds	11,605,361	—	11,605,361	16,781,454
Notes	1,038,237	1,028	1,039,265	418,446
Capital leases	146,348	—	146,348	—
Net pension obligation	4,177,387	—	4,177,387	—
Compensated absences	471,424	2,082	473,506	282,769
Lottery prizes	—	281,400	281,400	—
Other long-term liabilities	56,392	—	56,392	355,906
Total liabilities	25,313,666	430,743	25,744,409	30,713,304
Net assets:				
Invested in capital assets, net of related debt	3,133,230	1,672	3,134,902	11,693,544
Restricted for:				
Trust - nonexpendable	—	—	—	1,287,506
Capital projects	—	—	—	184,301
Debt service	—	—	—	1,039,924
Payment of unemployment and related benefits	—	853,194	853,194	—
Affordable housing and related loan insurance programs	—	—	—	340,230
Student loans and other educational purposes	—	—	—	48,136
Other	—	—	—	2,249,951
Unrestricted deficit	(16,789,576)	(3,037)	(16,792,613)	(660,745)
Total net assets (deficit)	\$ (13,656,346)	851,829	(12,804,517)	16,182,847

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO

Statement of Activities

Year ended June 30, 2004

(In thousands)

Functions	Program revenue			Net (expense) revenue and changes in net assets			Component units
	Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Primary government Business-type activities	Total	
<b>Primary government:</b>							
<b>Governmental activities:</b>							
General government	\$ 1,963,879	80,527	—	(1,359,430)	—	(1,359,430)	—
Public safety	1,950,635	70,243	3,030	(1,831,726)	—	(1,831,726)	—
Health	2,386,735	494,265	—	(1,791,725)	—	(1,791,725)	—
Public housing and welfare	2,919,315	2,230,928	162,146	(516,338)	—	(516,338)	—
Education	3,684,331	2,387	2,667	(3,114,810)	—	(3,114,810)	—
Economic development	896,925	22,494	64	(787,753)	—	(787,753)	—
Intergovernmental	591,237	—	—	(591,237)	—	(591,237)	—
Interest and other	778,700	—	—	(778,700)	—	(778,700)	—
<b>Total governmental activities</b>	<b>15,171,757</b>	<b>3,462,924</b>	<b>167,907</b>	<b>(10,771,719)</b>	<b>—</b>	<b>(10,771,719)</b>	<b>—</b>
<b>Business-type activities:</b>							
Lotteries	731,344	—	—	—	158,106	158,106	—
Unemployment insurance	142,652	—	—	—	82,042	82,042	—
Other	26,763	59,728	—	—	55,526	55,526	—
<b>Total business-type activities</b>	<b>900,759</b>	<b>59,728</b>	<b>—</b>	<b>—</b>	<b>295,674</b>	<b>295,674</b>	<b>—</b>
<b>Total primary government</b>	<b>\$ 16,072,516</b>	<b>\$ 3,522,652</b>	<b>\$ 167,907</b>	<b>\$ (10,771,719)</b>	<b>\$ 295,674</b>	<b>\$ (10,476,045)</b>	<b>\$ —</b>
<b>Component units:</b>							
Government Development Bank for Puerto Rico	\$ 511,067	113,743	21,493	—	—	—	50,498
Puerto Rico Highway and Transportation Authority	638,916	—	74,091	—	—	—	(379,377)
Puerto Rico Electric Power Authority	2,684,825	—	38,857	—	—	—	(40,204)
Puerto Rico Aqueduct and Sewer Authority	747,606	21,846	—	—	—	—	(403,167)
Puerto Rico Infrastructure Financing Authority	132,601	—	—	—	—	—	(132,601)
Puerto Rico Health Insurance Administration	1,369,714	—	—	—	—	—	(989,683)
University of Puerto Rico	1,173,252	249,844	5,000	—	—	—	(755,393)
Other component units	2,173,487	30,726	35,981	—	—	—	(565,750)
<b>Total component units</b>	<b>\$ 9,431,468</b>	<b>\$ 416,159</b>	<b>\$ 175,422</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ (3,215,677)</b>
<b>General revenue:</b>							
<b>Taxes:</b>							
Income taxes				\$ 5,191,080	—	5,191,080	—
Property taxes				121,815	—	121,815	—
Excise taxes				1,924,610	—	1,924,610	391,829
Other taxes				19,211	—	19,211	—
Revenue from global settlement agreement				70,420	—	70,420	—
Revenue from Tourism Company of Puerto Rico				77,475	—	77,475	—
Revenue from Government Development Bank for Puerto Rico				18,397	—	18,397	—
Revenue from Caribbean Basin Projects Financing Authority				5,082	—	5,082	—
Revenue from Puerto Rico Telephone Authority				13,500	—	13,500	—
Revenue from State Insurance Fund Corporation				61,275	—	61,275	—
Grants and contributions not restricted to specific programs				5,706	—	5,706	8,744
Payment from primary government				—	23,831	23,831	2,697,181
Unrestricted investment earnings				60,585	—	60,585	71,732
Gain on sale of assets				—	—	—	13,558
Other				262,904	—	262,904	12,750
Special item				(35,646)	—	(35,646)	—
Transfers				203,258	(203,258)	—	—
Total general revenue, transfers, and special item				7,999,672	(179,427)	7,820,245	3,195,794
Change in net (deficit) assets				(2,772,047)	116,247	(2,655,800)	(19,883)
Net (deficit) assets, beginning of year (as restated)				(10,884,299)	735,582	(10,148,717)	16,202,730
Net (deficit) assets, end of year				\$ (13,656,346)	\$ 851,829	\$ (12,804,517)	\$ 16,182,847

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Balance Sheet – Governmental Funds

June 30, 2004  
(In thousands)

Assets	General	The Children's Trust special revenue	Debt service	PBA capital projects	Other governmental funds	Totals governmental funds
Cash and cash equivalents	\$ 1,346	—	—	—	71,912	73,258
Cash and cash equivalents in governmental banks	58,078	46,265	271,358	—	435,244	810,945
Investments	—	286,899	—	—	122,276	409,175
Receivables, net of allowance for uncollectibles:						
Taxes	1,075,126	—	16,331	—	—	1,091,457
Intergovernmental	253,937	—	—	—	—	253,937
Accounts	117,954	—	—	—	15,092	133,046
Loans	908	—	—	—	36	944
Accrued interest	324	737	1,030	—	1	2,092
Other	7,598	—	—	—	—	7,598
Due from:						
Other funds	70,249	—	—	25,757	75,429	171,435
Component units	63,134	—	—	—	32,613	95,747
Other governmental entities	3,189	—	—	—	—	3,189
Inventories	270	—	—	—	—	270
Restricted assets:						
Cash, cash equivalents, and investments	832,330	—	—	403,567	9,051	1,244,948
Cash and cash equivalents in governmental banks	904,985	—	19,185	45,800	85,697	1,055,667
Other assets	56,851	—	—	—	—	56,851
Real estate held for sale or disposition	64,114	—	—	—	—	64,114
Total assets	\$ <u>3,510,393</u>	<u>333,901</u>	<u>307,904</u>	<u>475,124</u>	<u>847,351</u>	<u>5,474,673</u>

**COMMONWEALTH OF PUERTO RICO**  
 Balance Sheet – Governmental Funds, continued  
 June 30, 2004  
 (In thousands)

Liabilities and Fund Balances	General	The Children's Trust special revenue	Debt service	PBA capital projects	Other governmental funds	Totals governmental funds
<b>Liabilities:</b>						
Accounts payable and accrued liabilities	\$ 947,542	1,738	—	126,158	43,969	1,119,407
Tax refunds payable	221,262	—	—	—	—	221,262
Due to:						
Other funds	152,421	—	—	—	—	152,421
Component units	1,778	—	—	—	20,000	21,778
Notes payable	658,329	—	—	—	—	658,329
Bonds payable	—	—	168,150	—	35,910	204,060
Interest payable	15,820	—	135,172	—	31,891	182,883
Deferred revenue	966,979	—	—	—	—	966,979
Tax revenue anticipation notes	800,000	—	—	—	—	800,000
Other liabilities	112,212	—	8,343	—	6,632	127,187
Total liabilities	<u>3,876,343</u>	<u>1,738</u>	<u>311,665</u>	<u>126,158</u>	<u>138,402</u>	<u>4,454,306</u>
<b>Fund balances:</b>						
Reserved for:						
Encumbrances	317,066	—	—	—	72,455	389,521
Debt service	679,354	—	—	—	—	679,354
Capital projects	14,210	—	—	—	—	14,210
Assets in liquidation	76,824	—	—	—	—	76,824
Inventories	270	—	—	—	—	270
Low income housing assistance	14,508	—	—	—	—	14,508
Unreserved (deficit), reported in:						
General fund	(1,468,182)	—	—	—	—	(1,468,182)
Debt service funds	—	—	(3,761)	—	123,591	119,830
Special revenue funds	—	332,163	—	—	117,292	449,455
Capital project funds	—	—	—	348,966	395,611	744,577
Total fund balances (deficit)	<u>(365,950)</u>	<u>332,163</u>	<u>(3,761)</u>	<u>348,966</u>	<u>708,949</u>	<u>1,020,367</u>
Total liabilities and fund balances	<u>\$ 3,510,393</u>	<u>333,901</u>	<u>307,904</u>	<u>475,124</u>	<u>847,351</u>	<u>5,474,673</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Reconciliation of the Balance Sheet to the Statement of Net Assets  
Governmental Funds

Year ended June 30, 2004  
(In thousands)

Amounts reported for governmental activities in the statement of net assets are different because:

Total fund balances of governmental funds	\$ 1,020,367
Inventories and prepaid expenses that are not available to pay for current period expenditures, and therefore are not recognized in the funds	31,945
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds	6,099,129
The difference between the proceeds of Qualified Zone Academic Bonds (QZAB) issued and the amounts paid to escrow agent to "early defease" such bonds is deferred in the statement of net assets and amortized over the life of the QZAB. Since such difference did not provide current financial resources, it is not reported in the funds	(43,034)
Deferred revenue in governmental funds that are recognized as revenue in the governmental activities	829,019
Debt issued by the Commonwealth have associated costs that are paid from current available resources in the funds. However, these costs are deferred on the statement of net assets	191,973
Net pension asset of the Puerto Rico Judiciary Retirement System recognized in governmental activities is not a financial resource and therefore is not reported in the funds	12,021
Liabilities, including Commonwealth appropriation bonds (\$2,758,066), bonds payable (\$11,615,476), notes payable (\$1,177,691), capital leases payable (\$153,214), long-term portion of compensated absences (\$1,373,677), net pension obligation (\$4,177,387) and other long-term liabilities (\$412,039) are not due and payable in the current period and therefore are not reported in the funds	(21,667,550)
Liability to component unit not due and payable in the current period and therefore is not reported in the funds.	(16,162)
Interest liabilities are not due and payable in the current period and therefore are not reported in the funds	(114,054)
Deficit of governmental activities	\$ <u><u>(13,656,346)</u></u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Statement of Revenue, Expenditures, and Changes in Fund Balances  
Governmental Funds  
Year ended June 30, 2004  
(In thousands)

	General	The Children's Trust special revenue	Debt service	PBA capital projects	Other governmental funds	Totals governmental funds
Revenue:						
Taxes:						
Income taxes	\$ 5,061,761	—	—	—	—	5,061,761
Property taxes	4,222	—	117,591	—	—	121,813
Excise taxes	1,924,610	—	—	—	—	1,924,610
Other taxes	19,211	—	—	—	—	19,211
Charges for services	750,978	—	—	—	—	750,978
Revenue from global settlement agreement	—	—	—	—	70,409	70,409
Revenue from component units:						
Tourism Company of Puerto Rico	77,475	—	—	—	—	77,475
Government Development Bank for Puerto Rico	18,397	—	—	—	—	18,397
Caribbean Basin Projects Financing Authority	5,082	—	—	—	—	5,082
Puerto Rico Telephone Authority	13,500	—	—	—	—	13,500
State Insurance Fund Corporation	61,275	—	—	—	—	61,275
Intergovernmental	3,654,766	—	—	—	—	3,654,766
Interest and investment earnings	45,127	4,512	1,287	—	7,988	58,914
Other	255,109	—	—	—	6,366	261,475
<b>Total revenue</b>	<b>11,891,513</b>	<b>4,512</b>	<b>118,878</b>	<b>—</b>	<b>84,763</b>	<b>12,099,666</b>
Expenditures:						
Current:						
General government	1,480,090	—	—	—	297,275	1,777,365
Public safety	1,751,489	—	—	—	13,710	1,765,199
Health	2,159,982	5,340	—	—	11,419	2,176,741
Public housing and welfare	2,643,557	—	—	—	94,459	2,738,016
Education	3,454,464	15,440	—	—	4,109	3,474,013
Economic development	589,593	60,000	—	—	219,333	868,926
Intergovernmental	446,648	—	—	—	82,181	528,829
Capital outlays	263,431	—	—	274,666	43,691	581,788
Debt service:						
Principal	307,368	—	168,150	—	51,054	526,572
Interest and other	207,764	240	291,186	—	146,645	645,835
Debt issuance costs	26,007	—	23,762	15,549	26,349	91,667
<b>Total expenditures</b>	<b>13,330,393</b>	<b>81,020</b>	<b>483,098</b>	<b>290,215</b>	<b>990,225</b>	<b>15,174,951</b>
Excess of expenditures over revenue	(1,438,880)	(76,508)	(364,220)	(290,215)	(905,462)	(3,075,285)
Other financing sources (uses):						
Transfers in	366,692	398	342,538	—	324,462	1,034,090
Transfers out	(587,328)	(63,075)	—	(38,849)	(141,580)	(830,832)
Long-term debt issued	1,356,912	—	—	842,748	801,456	3,001,116
Discount on bonds issued	(135)	—	—	(21,875)	(1,051)	(23,061)
Capital leases	2,300	—	—	—	—	2,300
Refunding bonds issued	578,769	—	743,210	—	1,050,710	2,372,689
Payment to refunded bond escrow agent	(564,098)	—	(731,969)	—	(1,020,843)	(2,316,910)
<b>Total other financing sources (uses)</b>	<b>1,153,112</b>	<b>(62,677)</b>	<b>353,779</b>	<b>782,024</b>	<b>1,013,154</b>	<b>3,239,392</b>
Net change in fund balances (deficit)	(285,768)	(139,185)	(10,441)	491,809	107,692	164,107
Fund balances (deficit), beginning of year	(80,182)	471,348	6,680	(142,843)	601,257	856,260
Fund balances (deficit), end of year	\$ (365,950)	332,163	(3,761)	348,966	708,949	1,020,367

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balances  
to the Statement of Activities - Governmental Funds

Year ended June 30, 2004  
(In thousands)

Amounts reported for governmental activities in the statement of activities are different because:

Net change in fund balances - total governmental funds	\$ 164,107
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays (\$581,788) exceeded depreciation (\$188,582) in the current period.	393,206
In the statement of activities, only the losses on the sale of capital assets is reported, whereas in the governmental funds, the proceeds from the sale increase financial resources. Therefore, the change in the net assets differs from the change in fund balance by the cost of the asset sold.	(45,122)
Revenue in the statement of activities that do not provide current financial resources are not reported as revenue in the governmental funds.	2,700
Debt proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets. This is the amount by which net proceeds (\$5,353,044) exceeded repayments (\$2,843,482).	(2,509,562)
Repayments of advances from a component unit provided current financial resources to governmental funds, but reduced the liability to component units in the statement of net assets.	2,878
Income tax revenue that are not currently available are deferred in the governmental funds, but are accruable as revenue in the statement of activities. This is the amount by which deferred revenue increased during the year.	129,319
Governmental funds do not report transfers of long-term assets or liabilities because such transfers do not represent financial resources, however they are recorded in the statement of activities. This amount represents the transfer of property by the Commonwealth to certain municipalities (see note 12)	(35,646)
Generally, inventory and prepayments are recorded as expenditures in the governmental funds when purchased rather than capitalized as an asset. However, these assets are capitalized in the statement of net assets. This amount represents the increase in inventory for the year.	13,212
Debt issuance costs are expenditures to governmental funds, but are deferred assets in the statement of net assets. This is the amount of debt issue costs for the year.	91,667
Certain interest and other costs reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount equivalent to the increase in interest payable (\$70,585), combined with the amortization of debt issue costs (\$6,147), and the net accretion and amortization of debt issue discount and deferred losses (\$93,413).	(170,145)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount by which the net increases in net pension obligation (\$375,574), Christmas bonus liability (\$1,197), liability in federal cost disallowances (\$47,143), liability for legal claims and judgments (\$152,606), and accrued compensated absences (\$234,723) exceeded the net decreases in other liabilities (\$2,582).	(808,661)
Change in deficit of governmental activities	\$ (2,772,047)

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Statement of Revenue and Expenditures – Budget and Actual –  
Budget Basis – General Fund  
Year ended June 30, 2004  
(In thousands)

	<u>Original budget</u>	<u>Amended budget</u>	<u>Actual</u>	<u>Variance</u>
Revenue:				
Income taxes	\$ 5,286,000	5,286,000	5,297,831	11,831
Excise taxes	1,997,000	1,997,000	1,945,300	(51,700)
Other taxes	90,000	90,000	99,922	9,922
Charges for services	171,000	171,000	228,724	57,724
Intergovernmental	20,000	20,000	34,266	14,266
Revenue from component units	96,000	96,000	100,466	4,466
Other	111,000	111,000	127,277	16,277
Total revenue	<u>7,771,000</u>	<u>7,771,000</u>	<u>7,833,786</u>	<u>62,786</u>
Expenditures:				
Current:				
General government	497,302	477,407	504,190	(26,783)
Public safety	1,733,303	1,682,073	1,689,666	(7,593)
Health	1,289,202	1,272,106	1,368,936	(96,830)
Public housing and welfare	451,064	455,470	536,448	(80,978)
Education	2,566,909	2,442,692	2,745,083	(302,391)
Economic development	484,244	483,608	571,772	(88,164)
Intergovernmental	356,567	357,604	357,609	(5)
Debt service:				
Principal	51,477	51,477	51,477	–
Interest and other	106,704	106,704	116,734	(10,030)
Total expenditures	<u>7,536,772</u>	<u>7,329,141</u>	<u>7,941,915</u>	<u>(612,774)</u>
Excess (deficiency) of revenue over (under) expenditures	<u>234,228</u>	<u>441,859</u>	<u>(108,129)</u>	<u>(549,988)</u>
Other financing sources (uses):				
Notes payable issued	–	–	695,131	(695,131)
Transfer in	523,375	523,375	285,961	237,414
Transfer out	(757,603)	(965,234)	(980,681)	15,447
Total other financing sources (uses)	<u>(234,228)</u>	<u>(441,859)</u>	<u>411</u>	<u>(442,270)</u>
Excess of expenditures and other uses over revenue and other sources	<u>\$ –</u>	<u>–</u>	<u>(107,718)</u>	<u>(107,718)</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Statement of Net Assets – Proprietary Funds  
June 30, 2004  
(In thousands)

Assets	<b>Business-type activities – enterprise funds</b>			
	<b>Unemployment Insurance Trust</b>	<b>Lotteries</b>	<b>Other funds</b>	<b>Totals</b>
<b>Current assets:</b>				
Cash and cash equivalents	\$ 485,083	3,908	9,438	498,429
Cash and cash equivalents in governmental banks	71,458	86,590	138,096	296,144
Accounts and loans receivable, net:				
Insurance premiums, net	46,642	–	3,484	50,126
Component units	–	–	9,670	9,670
General fund	–	51,235	–	51,235
Accrued interest	–	2,682	3,200	5,882
Other	8,293	–	391	8,684
Unrestricted investments	–	–	34,141	34,141
Total current assets	<u>611,476</u>	<u>144,415</u>	<u>198,420</u>	<u>954,311</u>
<b>Noncurrent assets:</b>				
Component units	–	–	142,880	142,880
Intergovernmental	–	–	1,962	1,962
Capital assets, net	–	1,672	–	1,672
Restricted cash	–	215,213	–	215,213
Other	–	36,783	–	36,783
Total assets	<u>611,476</u>	<u>398,083</u>	<u>343,262</u>	<u>1,352,821</u>
<b>Liabilities and Net Assets</b>				
<b>Current liabilities:</b>				
Accounts payable and accrued liabilities	–	9,097	6,953	16,050
Due to other funds	14,677	55,572	–	70,249
Deferred revenue	7,153	11,751	62	18,966
Compensated absences	–	1,957	933	2,890
Lottery awards	–	37,071	–	37,071
Insurance benefits payable	69,833	–	1,275	71,108
Notes payable	–	148	–	148
Total current liabilities	<u>91,663</u>	<u>115,596</u>	<u>9,223</u>	<u>216,482</u>
<b>Noncurrent liabilities:</b>				
Compensated absences	–	1,424	658	2,082
Lottery awards	–	281,400	–	281,400
Notes payable	–	1,028	–	1,028
Total liabilities	<u>91,663</u>	<u>399,448</u>	<u>9,881</u>	<u>500,992</u>
<b>Net assets:</b>				
Invested in capital assets	–	1,672	–	1,672
Restricted for:				
Payment of insurance benefits	519,813	–	130,900	650,713
Capital projects	–	–	202,481	202,481
Unrestricted	–	(3,037)	–	(3,037)
Total net assets (deficit)	<u>\$ 519,813</u>	<u>(1,365)</u>	<u>333,381</u>	<u>851,829</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Statement of Revenue, Expenses, and Changes in Net Assets  
Proprietary Funds  
Year ended June 30, 2004  
(In thousands)

	<b>Business-type activities - enterprise funds</b>			
	<b>Unemployment Insurance Trust</b>	<b>Lotteries</b>	<b>Other funds</b>	<b>Totals</b>
Operating revenue:				
Lottery ticket sales	\$ —	888,997	—	888,997
Insurance premiums	224,623	—	17,721	242,344
Interest	—	—	4,840	4,840
Other	71	453	—	524
Total operating revenue	<u>224,694</u>	<u>889,450</u>	<u>22,561</u>	<u>1,136,705</u>
Operating expenses:				
Lottery awards	—	598,517	—	598,517
Unemployment, disability, and drivers insurance benefits	142,652	—	4,918	147,570
General, administrative, and other operating expenses	—	132,436	21,845	154,281
Depreciation and amortization	—	391	—	391
Total operating expenses	<u>142,652</u>	<u>731,344</u>	<u>26,763</u>	<u>900,759</u>
Operating income (loss)	<u>82,042</u>	<u>158,106</u>	<u>(4,202)</u>	<u>235,946</u>
Nonoperating revenue (expenses):				
Contributions from U.S. government	46,531	—	15,074	61,605
Interest and investment earnings	23,831	—	(1,877)	21,954
Total nonoperating revenue (expenses)	<u>70,362</u>	<u>—</u>	<u>13,197</u>	<u>83,559</u>
Income before transfers	152,404	158,106	8,995	319,505
Transfers from general fund	—	—	2,960	2,960
Transfers to general fund	(48,112)	(158,106)	—	(206,218)
Net change in net assets (deficit)	104,292	—	11,955	116,247
Net assets (deficit), beginning of year	415,521	(1,365)	321,426	735,582
Net assets (deficit), end of year	<u>\$ 519,813</u>	<u>(1,365)</u>	<u>333,381</u>	<u>851,829</u>

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO

Statement of Cash Flows  
Proprietary Funds

Year ended June 30, 2004  
(In thousands)

	Business-type activities - enterprise funds			
	Unemployment Insurance Trust	Lotteries	Other funds	Totals
Cash flows from operating activities:				
Receipts from customers and users	\$ 236,288	891,658	20,275	1,148,221
Other receipts	110	453	—	563
Payments to suppliers and employees	(204)	(296,974)	(15,215)	(312,393)
Payment of lottery prizes	—	(360,101)	—	(360,101)
Payments of disability and insurance benefits	(251,773)	—	(4,758)	(256,531)
Net cash provided by (used in) operating activities	(15,579)	235,036	302	219,759
Cash flows from noncapital financing activities:				
Intergovernmental grants and contributions	46,531	—	14,878	61,409
Transfers out to general fund	(48,112)	(212,383)	—	(260,495)
Principal payments of notes payable	—	(280)	—	(280)
Transfers to general fund	(2,021)	—	2,960	939
Net cash provided by (used in) noncapital financing activities	(3,602)	(212,663)	17,838	(198,427)
Cash flows from capital and related financing activities:				
Capital expenditures	—	(168)	—	(168)
Principal payments of notes payable	—	(929)	—	(929)
Net cash used in capital and related financing activities	—	(1,097)	—	(1,097)
Cash flows from investing activities:				
Interest received on deposits and investments	23,856	—	1,950	25,806
Principal collected on loans	—	—	3,064	3,064
Loans originated	—	—	(17,166)	(17,166)
Net cash provided by (used in) investing activities	23,856	—	(12,152)	11,704
Net increase in cash and cash equivalents	4,675	21,276	5,988	31,939
Cash and cash equivalents, beginning of year	551,866	284,435	141,546	977,847
Cash and cash equivalents, end of year	\$ 556,541	305,711	147,534	1,009,786
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:				
Operating income (loss)	\$ 82,042	158,106	(4,202)	235,946
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization	—	391	—	391
Increase (decrease) in accounts and loans receivable	11,704	2,678	(13,043)	1,339
Interests earned on deposits loans and investments	—	—	10,903	10,903
Changes in operating assets and liabilities:				
Decrease in other assets	—	3,805	200	4,005
Increase in obligation for unpaid lottery awards	—	43,695	—	43,695
Increase in due to other funds	—	30,012	—	30,012
(Decrease) increase in deferred revenue	(204)	(1,954)	32	(2,126)
Increase in compensated absences	—	768	495	1,263
(Decrease) increase in liability for insurance benefits payable	(109,121)	—	160	(108,961)
(Decrease) increase in accounts payable and accrued liabilities	—	(2,465)	5,757	3,292
Total adjustments	(97,621)	76,930	4,504	(16,187)
Net cash provided by (used in) operating activities	\$ (15,579)	235,036	302	219,759

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Statement of Fiduciary Net Assets

June 30, 2004  
(In thousands)

<b>Assets</b>	<b>Pension trust funds</b>	<b>Special deposits agency fund</b>
Cash and cash equivalents:		
Unrestricted	\$ 80,815	454,754
Restricted	2,396	—
Cash and cash equivalents in governmental banks:		
Unrestricted	32,076	97,769
Restricted	4,857	—
Investments:		
Debt and equity securities, at fair value	3,298,355	22,999
Investment in PRTA Holdings, at appraised value	404,390	—
Other	85,292	—
Receivables, net:		
Accounts	47,748	23,435
Loans and advances	714,198	—
Accrued interest and dividends	7,973	—
Other	46,769	—
Capital assets, net	32,662	—
Other assets	8,444	532
Total assets	4,765,975	599,489
<b>Liabilities</b>		
Accounts payable and accrued liabilities	36,978	599,489
Liability for securities lending transactions	94,379	—
Bonds payable	22,090	—
Notes payable to component unit	240	—
Total liabilities	153,687	599,489
<b>Net Assets</b>		
Net assets held in trust for pension and other benefits	\$ 4,612,288	—

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Statement of Changes in Fiduciary Net Assets – Pension Trust Funds

Year ended June 30, 2004  
(In thousands)

Additions:	
Contributions:	
Sponsor	\$ 446,440
Participants	415,334
Special	54,962
Total contributions	<u>916,736</u>
Interest	100,897
Dividends	24,116
Net change in fair value of investments, including realized losses on sale and maturities of investments	507,527
Investment expenses	(8,222)
Net interest and investment income	<u>624,318</u>
Other income	39,210
Total additions	<u>1,580,264</u>
Deductions:	
Pension and other benefits	1,032,768
Refunds of contributions	23,421
General and administrative	63,632
Total deductions	<u>1,119,821</u>
Net change in net assets held in trust for pension and other benefits	460,443
Net assets held in trust for pension and other benefits:	
Beginning of year	<u>4,151,845</u>
End of year	<u>\$ 4,612,288</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Combining Statement of Net Assets – Major Component Units  
June 30, 2004  
(In thousands)

Assets	Government Development Bank for Puerto Rico	Puerto Rico Highway and Transportation Authority	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Infrastructure Financing Authority	Puerto Rico Health Insurance Administration	University of Puerto Rico	Nonmajor component units	Total component units
Current assets:									
Cash and cash equivalents	1,184,967	34,171	17,606	39,200	58,736	10,288	56,243	207,324	1,608,535
Cash and cash equivalents in governmental banks	—	—	—	34,623	74,208	338	—	388,007	497,476
Investments, including collateral from securities lending transactions	1,996,710	—	—	—	324,959	—	42,380	1,402,667	3,766,716
Receivables, net:									
Intergovernmental	15,595	6,965	—	—	—	4,138	31,410	2,358	60,466
Accounts	—	5,237	360,683	29,525	—	—	10,879	220,698	627,022
Loans and advances	3,139,377	—	—	—	—	—	—	54,420	3,193,797
Accrued interest	136,801	3,235	2,229	—	20,017	1	—	23,696	185,979
Other governmental entities	—	—	158,902	30,953	370	10,591	21,524	134,342	356,682
Other	—	—	—	—	—	7,639	73,622	34,374	115,635
Due from:									
Primary government	—	—	6,327	—	—	—	7,570	21,778	35,675
Component units	1,016,844	—	14,089	—	—	—	12,955	39,992	1,083,880
Inventories	—	—	201,270	15,037	—	—	8,991	36,056	261,354
Prepays	—	4,031	31,878	2,047	1,419	—	22,606	11,837	73,818
Total current assets	7,490,294	53,639	792,984	151,385	480,009	32,995	288,180	2,577,549	11,867,035
Noncurrent assets:									
Restricted assets:									
Cash and cash equivalents	29,370	38,060	373,832	—	—	—	33,829	136,109	611,200
Cash and cash equivalents in governmental banks	—	5,247	—	36,702	—	—	—	136,803	178,752
Investments and other restricted assets	1,467,089	821,375	402,297	—	1,270,277	—	76,443	1,488,920	5,526,401
Investments	—	—	—	—	—	—	—	1,160,156	1,160,156
Receivables:									
Loans, interest, and other	—	—	—	—	—	—	2,523	148,989	151,512
Other governmental entities	—	—	12,830	—	—	—	—	—	12,830
Due from:									
Primary government	16,162	—	49,408	—	—	—	15,900	—	81,470
Component units	51,529	—	38,867	—	—	—	—	32,364	32,364
Property held for sale and future development	2,955	7,679,165	1,621,804	479,196	837,296	—	221,115	1,313,480	258,057
Capital assets, not being depreciated	12,249	5,086,055	3,182,731	4,079,954	190	390	443,735	1,606,004	14,411,308
Capital assets, depreciable, net	132,849	120,736	88,355	31,590	19,927	—	—	56,598	450,055
Deferred expenses and other assets	—	—	—	—	—	—	—	—	—
Total noncurrent assets	1,712,203	13,750,638	5,770,124	4,627,442	2,127,690	390	793,545	6,247,084	35,029,116
Total assets	9,202,497	13,804,277	6,563,108	4,778,827	2,607,699	33,385	1,081,725	8,824,633	46,896,151

**COMMONWEALTH OF PUERTO RICO**  
Combining Statement of Net Assets - Major Component Units, continued

June 30, 2004  
(in thousands)

	Government Development Bank for Puerto Rico	Puerto Rico Highway and Transportation Authority	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Infrastructure Financing Authority	Puerto Rico Health Insurance Administration	University of Puerto Rico	Nonmajor component units	Total component units
<b>Liabilities</b>									
Current liabilities:									
Accounts payable and accrued liabilities	\$ 109,738	169,092	468,096	260,091	77,878	32,325	107,637	693,409	1,918,266
Deposits and escrow liabilities	4,044,475	—	130,643	6,833	—	—	—	432,931	4,634,882
Due to:									
Primary government	8,397	—	61,452	9,670	—	—	—	47,629	65,696
Other governmental entities	—	—	—	—	—	—	29,644	804,564	895,660
Securities lending transactions and reverse repurchase agreements	160,000	—	—	—	—	—	—	18,560	18,560
Interest payable	11,766	135,924	132,517	9,874	38,800	—	3,026	67,354	399,261
Deferred revenue	933,327	—	130,000	920	—	—	14,671	107,251	1,228,842
Notes payable, current portion	—	—	—	—	—	—	—	121,159	1,184,486
Commonwealth appropriation bonds	—	—	6,797	—	1,177	—	—	1,220	9,194
Bonds payable, current portion	87,596	29,135	331,806	23,142	26,955	—	18,550	102,429	619,613
Accrued compensated absences	4,598	—	62,739	27,139	132	418	19,146	73,132	187,304
Reserves for automobile accident benefit payments	—	—	—	—	—	—	—	882,672	882,672
Current portion of other long-term liabilities	—	30,216	—	—	—	—	3,838	79,956	114,010
Total current liabilities	5,359,897	364,367	1,337,253	343,546	145,862	32,743	196,512	3,654,903	11,435,083
Noncurrent liabilities:									
Due to:									
Primary government	—	—	—	142,880	—	—	—	39,721	182,601
Component units	—	—	—	64,546	8,647	—	3,538	149,388	226,119
Deferred revenue	—	—	3,673	—	—	—	—	6,804	10,477
Notes payable	1,758	—	—	—	—	—	—	416,688	418,446
Commonwealth appropriation bonds	10,339	—	—	708,585	9,475	—	—	292,050	1,020,449
Bonds payable	1,514,365	5,842,874	4,572,721	820,729	1,933,722	—	480,976	1,616,067	16,781,454
Accrued compensated absences	—	16,022	128,954	22,828	130	400	96,279	18,156	282,769
Other long-term liabilities	—	18,000	—	57,201	6,000	—	49,776	224,929	355,906
Total noncurrent liabilities	1,526,462	5,876,896	4,705,348	1,816,769	1,957,974	400	630,569	2,763,803	19,278,221
Total liabilities	6,886,359	6,241,263	6,042,601	2,160,315	2,103,836	33,143	827,081	6,418,706	30,713,304
Net assets:									
Invested in capital assets, net of related debt	15,204	6,985,080	—	2,768,877	115,268	390	164,189	1,644,536	11,693,544
Restricted for:									
Trust - nonexpendable	—	—	—	—	1,287,506	—	—	—	1,287,506
Capital projects	—	28,124	115,983	—	—	—	6,680	33,514	184,301
Debt service	57,406	507,188	389,724	—	19,962	—	39,838	25,806	1,039,924
Affordable housing and related loan insurance programs	340,230	—	—	—	—	—	—	—	340,230
Student loans and other educational purposes	—	—	—	—	—	—	—	9,233	48,136
Other specified purposes	1,903,298	—	—	36,701	13,181	—	38,903	251,345	2,249,951
Unrestricted	—	42,622	14,800	(187,066)	(932,054)	(148)	(40,392)	441,493	(660,745)
Total net assets	2,316,138	7,563,014	5,205,507	2,618,512	503,863	242	254,644	2,405,927	16,182,847
Total liabilities and net assets	\$ 9,202,497	\$ 13,804,277	\$ 6,563,108	\$ 4,778,827	\$ 2,607,699	\$ 33,385	\$ 1,081,725	\$ 8,824,633	\$ 46,896,151

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO

Combining Statement of Activities—Major Component Units

Year ended June 30, 2004  
(In thousands)

Component units	Expenses	Program revenue		Capital grants and contributions	Net revenue (expenses) and changes in net assets	Payments from primary government	Payments from other component units	General revenue and transfers					Change in net assets	Net assets, beginning of year	Net assets, end of year
		Operating grants and contributions	Charges for services					Grants and contributions not restricted to specific programs	Taxes	Interest and investment earnings	Gain in sale of assets	Other			
Government															
Development Bank for Puerto Rico	\$ 511,067	426,329	113,743	21,493	50,498	112,721	(3,886)	—	—	1,026	—	—	160,359	2,155,779	2,316,138
Rico Rico Highway and Transportation Authority	638,916	185,448	—	74,091	(379,377)	—	—	318,380	—	14,391	—	—	(46,606)	7,609,620	7,563,014
Puerto Rico Electric Power Authority	2,684,825	2,605,764	—	38,857	(40,204)	—	—	—	—	9,875	—	6,057	(24,272)	544,779	520,507
Puerto Rico Aqueduct and Sewer Authority	747,606	322,593	21,846	—	(403,167)	266,575	126,005	—	—	—	—	(25,429)	(36,016)	2,654,528	2,618,512
Infrastructure Financing Authority	132,601	—	—	—	(132,601)	80,258	(126,005)	—	—	(77,136)	—	—	(255,484)	759,347	503,863
Puerto Rico Health Insurance Administration	1,369,714	380,031	—	—	(989,683)	969,804	—	—	—	20,459	—	—	580	(338)	242
University of Puerto Rico	1,173,252	163,015	249,844	5,000	(755,393)	745,875	—	6,010	—	3,023	—	839	354	254,290	254,644
Nonmajor component units	2,173,487	1,541,030	30,726	35,981	(565,750)	521,948	3,886	2,734	73,449	100,094	13,558	31,283	181,202	2,224,725	2,405,927
Total component units	\$ 9,431,468	5,624,210	416,159	175,422	(3,215,677)	2,697,181	—	8,744	391,829	71,732	13,558	12,750	(19,883)	16,202,730	16,182,847

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### (1) Summary of Significant Accounting Policies

The Commonwealth of Puerto Rico (the Commonwealth) was constituted on July 25, 1952, under the provisions of its Constitution as approved by the people of Puerto Rico and the U.S. Congress. The Commonwealth's Constitution provides for the separation of powers of the executive, legislative, and judicial branches of the government. The Commonwealth assumes responsibility for public safety, health, public housing and welfare, education, and economic development.

The accompanying basic financial statements of the Commonwealth have been prepared in conformity with accounting principles generally accepted (GAAP) in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

The accompanying basic financial statements present the financial position of the Commonwealth and its various funds, the results of operations of the Commonwealth and its various funds and fund types, and the cash flows of the proprietary funds. The basic financial statements are presented as of June 30, 2004, and for the year then ended. The basic financial statements include the various departments, agencies, boards, commissions, public trusts and public corporations, and any other organizational units governed by the Puerto Rico Legislature and/or officers of the Commonwealth.

#### (a) *The Financial Reporting Entity*

The accompanying basic financial statements include all departments, agencies, and governmental entities whose funds are under the custody and control of the Secretary of the Treasury of the Commonwealth and the Commonwealth's component units pursuant to Act No. 230 of July 23, 1974, as amended, known as Commonwealth of Puerto Rico Accounting Law. The Commonwealth has considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth's basic financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Commonwealth to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Commonwealth.

As required by GAAP, these basic financial statements present the Commonwealth and its component units.

#### (b) *Component Units*

Component units are entities that are legally separate organizations for which the Commonwealth's elected officials are financially accountable or other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth's basic financial statements to be misleading and incomplete. GAAP details two methods of presentation: blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Commonwealth's balances and

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

transactions; or discrete presentation of the component units' financial data in columns separate from the Commonwealth's balances and transactions. The Commonwealth can impose its will on each of the component units through appointment of the members of their governing authorities. The financial statements of the component units discussed below have been included in the financial reporting entity either as blended component units or as discretely presented component units in accordance with GASB Statement No. 14, *The Financial Reporting Entity* (GASB No. 14), as amended.

### **Blended Component Units**

The following entities, while legally separate from the Commonwealth, meet the criteria to be reported as part of the primary government because they provide services entirely or almost entirely to the Commonwealth.

***Public Buildings Authority (PBA)*** – PBA is governed by a five-member board comprised by the Governor, the Secretary of the Department of Transportation and the Public Works (DTPW), the Secretary of Education of the Commonwealth, the President of the Government Development Bank for Puerto Rico (GDB), and one member appointed by the Governor of Puerto Rico with the advice and consent of the Senate. It is a legally separate entity, whose activities are blended within the primary government because it exists to construct, purchase, or lease office, school, health, correctional, social welfare, and other facilities for lease to the Commonwealth's departments, component units, and instrumentalities. Bonds issued by PBA to finance such facilities are payable from lease collections, which are largely derived from Commonwealth appropriations and are further secured by the Commonwealth's guaranty.

***Puerto Rico Maritime Shipping Authority (PRMSA)*** – PRMSA is governed by the President of GDB. The operations of PRMSA consist of servicing the long-term liability to third parties that resulted from the sale of certain maritime operations formerly owned and operated by PRMSA. The Commonwealth is required to annually appropriate funds in its general operating budget to provide for the payment of principal and interest on such debt [see note 14 d].

***The Children's Trust (the Trust)*** – The Trust is governed by a seven-member board comprised by the Governor, who designated the president of the board, the President of GDB, the Director of the Office of Management and Budget (OMB) of the Commonwealth, the Secretary of Justice of the Commonwealth, and three private citizens appointed by the Governor with the consent of the Senate. The Trust's sole operation consists of providing financial assistance principally to the Commonwealth's departments to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico, especially in the areas of education, recreation, and health. The operation of the Trust is financed with the moneys being received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The agreement calls for annual payments through the year 2025 which will vary due to inflationary and volume adjustments. After 2025, the tobacco companies shall continue making contributions in perpetuity.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Complete financial statements of the blended component units can be obtained directly by contacting their respective administrative offices at:

Public Buildings Authority  
P.O. Box 41029 Minillas Station  
San Juan, PR 00940-1029

The Children's Trust  
P.O. Box 42001  
San Juan, PR 00940-2001

Puerto Rico Maritime Shipping Authority  
P.O. Box 42001  
San Juan, PR 00940-2001

### ***Discretely Presented Component Units***

The following component units, consistent with GASB No. 14, are discretely presented in the basic financial statements because of the nature of the services they provide and the Commonwealth's ability to impose its will, principally through the appointment of their governing authorities. These have been classified by management between major and nonmajor component units.

### **Major Component Units**

***Government Development Bank for Puerto Rico (GDB)*** – is governed by a seven-member board appointed by the Governor. GDB acts as fiscal agent, depository of funds, disbursing agent, and financial advisor for the Commonwealth, its public corporations, and municipalities in connection with the issuance of bonds and notes; and it also makes loans and advances funds predominantly to the Commonwealth's departments, component units, and municipalities.

***Puerto Rico Aqueduct and Sewer Authority (PRASA)*** – PRASA is governed by a nine-member board comprised of five members appointed by the Governor, the Secretary of DTPW, the President of GDB, and two members elected in a referendum carried out by the Puerto Rico Consumer Affairs Department. PRASA owns and operates the system of public water supply and sanitary sewer facilities. PRASA is authorized, among other things, to borrow money and issue revenue bonds for any of its corporate purposes. Through the approval of Act No. 328 of 1998, as discussed in note 15 (a), the Commonwealth guarantees the principal and interest payments of certain outstanding bonds and of all future bonds issued to refinance those outstanding bonds, and other loans under the State Revolving Fund Program. PRASA maintained privatization contracts for the administration of its operations from 1985 to January 2004. The operation, management, repair, and maintenance of PRASA systems returned to PRASA after the cancellation of the privatization contract in January 2004.

***Puerto Rico Electric Power Authority (PREPA)*** – PREPA is governed by a nine-member board comprised of the Secretary of DTPW, six members appointed by the Governor with the advice and consent of the Senate, and two members representing the consumers' interest elected in a referendum carried out by the Puerto Rico Consumer Affairs Department. Board members are appointed or elected for a period of four years. PREPA is responsible for conserving, developing, and utilizing the

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

power resources of Puerto Rico and owns and operates the Commonwealth's electrical power generation, transmission, and distribution system.

***Puerto Rico Health Insurance Administration (PRHIA)*** – PRHIA is governed by a seven-member board comprised by the Secretary of Health of the Commonwealth, the Secretary of the Treasury of the Commonwealth, the Insurance Commissioner of Puerto Rico, and four additional members appointed by the Governor, with the consent of the Senate, including two professionals with competence in the insurance industry and health services, and two representing the public interest. PRHIA was created for implementing, administering, and negotiating a health insurance system through contracts with insurance underwriters to provide quality medical and hospital care to low-income individuals, employees of the Commonwealth, and policeman who voluntarily subscribe to the Puerto Rico health insurance medical plan.

***Puerto Rico Highway and Transportation Authority (PRHTA)*** – PRHTA is governed by the Secretary of DTPW. PRHTA has broad powers to carry out its responsibilities in accordance with DTPW's overall transportation policies. These powers include, among other things, the complete control and supervision of any highway facilities constructed, owned, or operated by PRHTA, the ability to set tolls for the use of the highway facilities, and the power to issue bonds, notes, or other obligations. PRHTA plans and manages the construction of all major projects relating to the Commonwealth toll highway system, undertakes major repairs, and maintains the toll ways.

***Puerto Rico Infrastructure Financing Authority (PRIFA)*** – PRIFA is governed by the board of directors of GDB and the Secretary of the Treasury of the Commonwealth. Its responsibilities are to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other component units and governmental instrumentalities of the Commonwealth, which are authorized to develop infrastructure facilities and to establish alternate means for financing them.

***University of Puerto Rico (UPR)*** – UPR is governed by a thirteen-member board of trustees comprised of one full-time student, two permanent professors, and ten community citizens of the private sector of which, at least one must be graduated from the institution. Community citizens are designated by the Governor with the advice and consent of the Senate. Members designated by the Governor are appointed for a period of four to eight years. The terms for the student and professors are of one year.

#### **Nonmajor Component Units**

***Agricultural Services and Development Administration (ASDA)*** – ASDA is governed by the Secretary of Agriculture of the Commonwealth. The purpose of ASDA is to provide a wide variety of services and incentives to the agricultural sector.

***Automobile Accidents Compensations Administration (AACA)*** – AACA is governed by a four-member board appointed by the Governor with the advice and consent of the Senate. AACA operates a system of compulsory insurance coverage for all registered motor vehicles and compensates citizens for injuries arising from motor vehicle accidents.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

***Cardiovascular Center Corporation of Puerto Rico and the Caribbean (CCCPRC)*** – CCCPRC is governed by a five-member board comprised of the Secretary of Health of the Commonwealth, the Director of the Medical Sciences Campus of the UPR, the Executive Director of the Puerto Rico Medical Services Administration, and two additional members appointed by the Governor with the consent of the Senate, one of which should be from the Cardiology Society of Puerto Rico and another a member of a cardiology foundation properly registered in the Department of State of the Commonwealth. The purpose of the CCCPRC is to provide special treatment to patients suffering from cardiovascular diseases.

***Caribbean Basin Projects Financing Authority (CBPFA)*** – CBPFA is governed by a seven-member board comprised by the Secretary of State of the Commonwealth, the Executive Director of the Puerto Rico Industrial Development Company (PRIDCO), the President of GDB, the President of Economic Development Bank for Puerto Rico, and three citizens, including at least two from the private sector, appointed by the Governor with the advice and consent of the Senate. CBPFA is authorized to issue revenue bonds and to loan the proceeds thereof to finance projects for the development of the Caribbean Basin countries that were authorized to receive investments of funds under the provisions of Section 936 of the U.S. Internal Revenue Code.

***Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico (CDASFIPR)*** – CDASFIPR is governed by a seven-member board of directors comprised by the Secretary of Economic Development and Commerce of the Commonwealth, the Chairman of the Board of the Puerto Rico Public Broadcasting Corporation, the Secretary of the Treasury of the Commonwealth, the Executive Director of the Institute of Puerto Rican Culture (IPRC), and three private citizens, appointed by the Governor with the advice and consent of the Senate. At least two of these private citizens must have proven interest, knowledge, and experience in arts, sciences, and the film industry. CDASFIR was created with the purpose of developing the production of local films in Puerto Rico.

***Economic Development Bank for Puerto Rico (EDB)*** – EDB is governed by a nine-member board comprised by the President of GDB, who is the Chairman, the Secretary of Agriculture of the Commonwealth, the Secretary of the Department of Economic Development and Commerce of the Commonwealth, the Executive Director of PRIDCO, the Executive Director of the Tourism Company of Puerto Rico, and four other members representing the private sector and appointed by the Governor with the consent of the Senate. Private sector members are appointed for a period of three years. EDB is responsible for the promotion and development of the private sector economy of the Commonwealth. This purpose is to be met by granting direct loans, loan guarantees, and or direct investments to any person or business organization devoted to manufacturing, agriculture, trade, tourism, or other service enterprises with preference but not limited to economic activities that may have the effect of substituting imports.

***Employment and Training Enterprises Corporation (ETEC)*** – ETEC is governed by a ten-member board comprised of the Puerto Rico Corrections Administrator, the Administrator of Youth Correctional Institutions, the Secretary of Justice of the Commonwealth, the Secretary of Education of the Commonwealth, the Executive Director of the Right to Employment Administration, the Administrator of the Administration of Mental Health and Anti-Addiction Services, the Sub-

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

Administrator for the Promotion of Puerto Rico Industries of the Economic Development Administration, the Director of the Volunteer Corps, and two private citizens appointed by the Governor with the consent of the Senate. The purpose of ETEC is to provide training, management, development, and employment for inmates of the correctional institutions of the Commonwealth.

***Farm Insurance Corporation of Puerto Rico (FICPR)*** – FICPR is governed by a five-member board comprised by the Secretary of Agriculture of the Commonwealth, the Dean of the Agricultural Sciences Faculty of the UPR Mayagüez Campus, a representative of GDB, and two bona fide farmers appointed by the Governor with the consent of the Senate. The purpose of the FICPR is to provide insurance to farmers against losses in their farms caused by natural disasters.

***Fine Arts Center Corporation (FACC)*** – FACC is governed by the board of directors of the Institute of Puerto Rican Culture (IPRC). FACC was created with the purpose of administering the Fine Arts Center.

***Governing Board of the 9-1-1 Service (911 Service)*** – The Governing Board of 9-1-1 Service (the Board) is comprised by the Commissioner of Security and Public Protection, the Executive Director of the Medical Emergency Services, the Director of the State Emergency Management Agency, the Chief of the Puerto Rico Firefighters Corps, and one member appointed by consensus of the four ex-official members to represent the public interest. The 911 Service is responsible for providing an efficient service of fast response to emergency calls through the 9-1-1 number and transferring these to the appropriate response agencies using technological and human resources to safeguard lives and properties.

***Institutional Trust of the National Guard of Puerto Rico (ITNGPR)*** – ITNGPR is governed by a seven-member board comprised by the National Guard Special Assistant, the President of GDB, the Secretary of Justice of the Commonwealth, three militaries from the Puerto Rico National Guard, and one representative from the community recommended by the National Guard Special Assistant and appointed by the Governor. ITNGPR's purpose is to provide life insurance, retirement benefits, and economic assistance to the active members of the Puerto Rico National Guard and their families.

***Musical Arts Corporation (MAC)*** – MAC is governed by a seven-member board appointed by the Governor with the consent of the Senate including the president of the board of IPRC. MAC was created to promote the development of the arts and cultural programs of the Commonwealth.

***National Parks Company of Puerto Rico (NPCPR)*** – NPCPR is governed by a nine-member board comprised by the Secretary of Recreation and Sports of the Commonwealth (the Secretary), who is the chairman, the Secretary of Education of the Commonwealth, the Executive Director of the Tourism Company of Puerto Rico (TCPR), the Secretary of Natural and Environmental Resources of the Commonwealth, and five members appointed by the Governor with the recommendation from the Secretary and with known interest in the development and preservation of parks in the private sector. NPCPR is responsible for the operation of all national parks and the protection, conservation, and use of parks, beaches, forests, natural, and historical monuments for the optimum enjoyment of present and future generations.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

***Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives (PCSDIPRC)*** – PCSDIPRC is governed by a nine-member board comprised by the Administrator of the Cooperative Development Administration, the Commissioner of Financial Institutions of Puerto Rico (the Commissioner of Financial Institutions), the Insurance Commissioner of Puerto Rico, the Secretary of the Treasury of the Commonwealth, the Inspector of Cooperatives, four citizens representing the cooperative movement, and one private citizen representing the public interest. PCSDIPRC has the responsibility of providing to all the cooperatives and the Federation of Cooperatives of Puerto Rico, insurance coverage over the stocks and deposits, for monitoring the financial condition of the insured cooperatives, and of uninsured cooperatives when requested by the Commissioner of Financial Institutions.

***Puerto Rico Conservatory of Music Corporation (PRCMC)*** – PRCMC is governed by a seven-member board appointed by the Governor. PRCMC is responsible for providing the Puerto Rican community and especially its youths with the required facilities to educate and perfect their musical skills, including secondary education programs for developing musical arts. It prepares the artistic element that nourishes the Puerto Rico Symphony Orchestra and other musical organizations, and coordinates the governmental efforts to interested industries, private enterprises, and particular citizens.

***Puerto Rico Convention Center District Authority (PRCCDA)*** – PRCCDA is governed by a board comprised of nine members, three of which shall be from the public sector and six of which shall be from the private sector. The public sector members are comprised of the Secretary of Economic Development and Commerce of the Commonwealth, who is the Chairman, the Executive Director of the Tourism Company of Puerto Rico, and the Mayor of the Municipality of San Juan. The private sector members are individuals having experience in the areas of hospitality, tourism, real estate, or convention centers who are appointed by the Governor with the advice and consent of the Senate. PRCCDA was created to develop, own, finance, plan, design, construct, operate, manage, and promote the new Puerto Rico Convention Center, currently under development.

***Puerto Rico Council on Higher Education (PRCHE)*** – PRCHE is governed by a board comprised of eight members appointed by the Governor with the advice and consent of the Senate and the Secretary of Education of the Commonwealth as an ex-officio member. Its purpose is to develop higher education, to administer the licensing and certification of institutions of higher education, and to administer scholarship funds.

***Puerto Rico Exports Development Corporation (PREDC)*** – PREDC is governed by the board of GDB. PREDC's purpose is to encourage the economic development of Puerto Rico by promoting the export of products and services of Puerto Rico to other countries and maintaining commercial facilities for lease to the public and private sector.

***Puerto Rico Government Investment Trust Fund (PRGITF)*** – PRGITF is governed by the Secretary of the Treasury of the Commonwealth. GDB is its trustee, custodian, and administrator. PRGITF's main objective is to provide investment opportunities in a professionally managed money market portfolio by investing, in high quality securities, with minimal credit risk. Qualified investors include the Commonwealth's central government, its public corporations, instrumentalities and

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

agencies, and the municipalities of Puerto Rico. In conformity with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investments Pools*, the financial statements of the PRGITF are not included in the accompanying basic financial statements because the primary government and each component unit investor is already presenting as cash or investment their corresponding share of the assets of the PRGITF (See note 5).

***Puerto Rico Industrial Development Company (PRIDCO)*** – PRIDCO is governed by a seven-member board comprised by the Secretary of Economic Development and Commerce of the Commonwealth, who is the Chairman, the Secretary of the Treasury of the Commonwealth, the President of GDB, the President of the Planning Board of Puerto Rico, and three members from the private sector appointed by the Governor with the advice and consent of the Senate. The private sector members are appointed for a period of four years. PRIDCO administers the Commonwealth-sponsored economic development program by providing facilities, general assistance, and special incentive grants to manufacturing companies operating in Puerto Rico. PRIDCO has issued interim notes and revenue bonds to finance manufacturing plants and other facilities. Rentals derived from the leasing of specified facilities of PRIDCO are pledged for the payment of PRIDCO's revenue bonds.

***Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority (known as AFICA by its Spanish acronym)*** – AFICA is governed by a seven-member board consisting of the Secretary of Economic Development and Commerce, the President of GDB, the Executive Director of PRIFA, the Executive Director of the Tourism Company of Puerto Rico, the President of the Environmental Quality Board, and two private citizens appointed by the Governor. AFICA is authorized to issue revenue bonds to finance industrial, tourist, environmental control, medical, and educational facilities in Puerto Rico and the United States for use by private companies, nonprofit entities, or governmental agencies. The bonds are payable solely from collections from such private companies, nonprofit entities, or governmental agencies, and do not constitute debt of the Commonwealth or any of its other component units.

***Puerto Rico Land Administration (PRLA)*** – PRLA is governed by an eleven-member board comprised by the Secretary of Economic Development and Commerce of the Commonwealth, who serves as president, the Secretary of the Treasury of the Commonwealth, the Secretary of Agriculture of the Commonwealth, the Secretary of DTPW of the Commonwealth, the Secretary of Housing of the Commonwealth, the Executive Director of PRIDCO, the President of the Planning Board of Puerto Rico, and four other members appointed by the Governor with the advice and consent of the Senate. PRLA acquires parcels of land on behalf of government instrumentalities through negotiation or expropriation.

***Puerto Rico Land Authority (PRLA)*** – PRLA is governed by a five-member board comprised by the Secretary of Agriculture of the Commonwealth and four members appointed by the Governor. PRLA was created to carry out the provisions of the Land Law of Puerto Rico.

***Puerto Rico Maritime Transportation Authority (PRMTA)*** – PRMTA is under the control of the Secretary of DTPW of the Commonwealth. Its purpose is to administer and operate the maritime transportation services (ferries operations).

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

***Puerto Rico Medical Services Administration (PRMSA)*** – PRMSA is governed by a ten-member board comprised of the Secretary of Health of the Commonwealth, who is the Chairman, the Dean of the Medical Sciences Faculty of the UPR, the President of the Board of the Puerto Rican Cancer Society, the Mayor of the Municipality San Juan, the Administrator of the State Insurance Fund Corporation (SIFC), the Secretary of the Department of Family Affairs of the Commonwealth, the Administrator of the Administration of Mental Health and Anti-Addiction Services, the President of the Medical Policy and Administration Committee, and two consumers appointed by the Secretary of Health of the Commonwealth. Its purpose is to plan, organize, operate, and administer the centralized health services, provided in support of the hospital and other functions offered by the member institutions and users of the medical complex known as the Puerto Rico Medical Center.

***Puerto Rico Metropolitan Bus Authority (PRMBA)*** – PRMBA is governed by the Secretary of DTPW of the Commonwealth. PRMBA provides bus transportation to passengers within the San Juan Metropolitan Area.

***Puerto Rico Municipal Finance Agency (PRMFA)*** – PRMFA is governed by a five-member board comprised by the President of GDB, who is the Chairman, the Commissioner of Municipal Affairs, and three additional members appointed by the Governor, one of whom shall be either the mayor or chief financial officer of a municipality. PRMFA was organized to create a capital market to assist the municipalities of Puerto Rico in financing their public improvement programs.

***Puerto Rico Ports Authority (PRPA)*** – PRPA is governed by a five-member board comprised by the Secretary of DTPW of the Commonwealth, who is the Chairman, the Secretary of Economic Development and Commerce of the Commonwealth, the Economic Development Administrator, the Executive Director of the Tourism Company of Puerto Rico, and one private citizen appointed for a period of four years by the Governor with the advice and consent of the Senate. The purpose of PRPA is to administer all ports and aviation transportation facilities of the Commonwealth and to render other related services.

***Puerto Rico Public Broadcasting Corporation (PRPBC)*** – PRPBC is governed by an eleven-member board of directors comprised by the Secretary of Education of the Commonwealth, the President of the UPR, the Executive Director of IPRC, and eight private citizens, appointed by the Governor with the advice and consent of the Senate. At least three of these private citizens must have proven interest, knowledge, and experience in education, culture, art, science, or radio and television. PRPBC was created for the purpose of integrating, developing, and operating the radio, television, and electronic communication facilities that belong to the Commonwealth.

***Puerto Rico School of Plastic Arts (PRSPA)*** – PRSPA is governed by a seven-member board. Four members are appointed by the board of directors of IPRC, representing the public educational and cultural interests. Board members may not be employees of the PRSPA. The remaining three members are elected from among the members of the board of directors of IPRC, one of whom will serve as president. PRSPA was created to develop, promote, plan, and coordinate programs of study in higher education oriented to the plastic arts, teaching, artistic techniques, and to help students to develop humanistic values.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

***Puerto Rico Solid Waste Authority (PRSWA)*** – PRSWA is governed by a four-member board comprised by the Secretary of the Department of Natural and Environmental Resources (DNER) of the Commonwealth, the Executive Director of PRSWA, the Special Assistant to the Secretary of DNER and one other board member appointed by the Governor with the advice and consent of the Senate. PRSWA provides alternatives for processing of solid waste and encourages recycling, reuse, and recovery of resources from waste.

***Puerto Rico Telephone Authority (PRTA)*** – PRTA is governed by a five-member board comprised by the President of GDB and four members that are appointed by the board of directors of GDB. PRTA is the legal entity responsible to account for the equity interest in Telecomunicaciones de Puerto Rico, Inc. for the benefit of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities.

***Puerto Rico Trade and Export Company (PRTEC)*** – PRTEC is governed by the Secretary of Economic Development and Commerce of the Commonwealth. The operations and assets of the Puerto Rico Exports Development Corporation and those of the Commercial Development Administration (CDA) were transferred to the Puerto Rico Trade and Export Company, which are ascribed to the Department of Economic Development and Commerce. PRTEC has the responsibility to promote the highest efficiency in the services provided to the commercial sector, with emphasis on small and medium sized enterprises while promoting the export of products and services from Puerto Rico to other countries.

***Right to Employment Administration (REA)*** – REA is governed by an administrator appointed by the Governor with the consent of the Senate. In addition, a consultative board comprised by the Secretary of Labor and Human Resources of the Commonwealth, the Secretary of Agriculture of the Commonwealth, the Secretary of the DTPW of the Commonwealth, the Secretary of Education of the Commonwealth, and five additional members appointed by the Governor, with the consent of the Senate, will advise the administrator on the implementation of the Right to Employment Act.

***Special Communities Perpetual Trust (SCPT)*** – SCPT is governed by a board of directors comprised of seven members: the Secretary of Housing of the Commonwealth, the Secretary of the DTPW of the Commonwealth, the Coordinator for the Social and Economic Financing of the Special Communities, one mayor of a municipality of Puerto Rico, one community leader resident in one special community and two private citizens representing the public interest. All members of the board of directors are appointed by the Governor. SCPT's principal purpose is to fund development projects which address the infrastructure and housing needs of underprivileged communities.

***State Insurance Fund Corporation (SIFC)*** – SIFC is governed by a seven-member board appointed by the Governor with the advice and consent of the Senate. The board is comprised by the Commissioner of Insurance of Puerto Rico, an officer from the Department of Labor and Human Resources of the Commonwealth, an officer from the Department of Health of the Commonwealth, a representative of the employer's interest, a representative of the employees' interest, and two members without any of these interests. One of these members is appointed by the Governor as president of the board for a period of six years. The three public officials are appointed for a period

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

of five years, and the rest of the members for four, three, two, and one year, respectively. SIFC provides workers' compensation and disability insurance to public and private employees.

***Tourism Company of Puerto Rico (TCPR)*** – TCPR is governed by a seven-member board comprised of representatives of different tourist-related sectors appointed by the Governor with the consent of the Senate. At least one member must represent internal tourism and two must not be residents of the metropolitan area. Its purpose is to promote the tourism industry of Puerto Rico.

Complete financial statements of the discretely presented component units can be obtained directly by contacting their administrative offices:

Government Development Bank for Puerto Rico  
P.O. Box 42001  
San Juan, PR 00940-2001

Puerto Rico Electric Power Authority  
P.O. Box 364267  
San Juan, PR 00936-4267

Puerto Rico Highway and Transportation Authority  
P.O. Box 42007  
San Juan, PR 00940-2007

University of Puerto Rico  
Jardín Botánico Sur 1187  
Calle Flamboyán  
San Juan, PR 00926-1117

Automobile Accident Compensation Administration  
P.O. Box 364847  
San Juan, PR 00936-4847

Caribbean Basin Projects Financing Authority  
P.O. Box 42001  
San Juan, PR 00940-2001

Economic Development Bank for Puerto Rico  
P.O. Box 2134  
San Juan, PR 00922-2134

Farm Insurance Corporation of Puerto Rico  
P.O. Box 9200  
San Juan, PR 00908

Puerto Rico Aqueduct and Sewer Authority  
P.O. Box 7066  
San Juan, PR 00916-7066

Puerto Rico Health Insurance Administration  
P.O. Box 195661  
San Juan PR 00919-5661

Puerto Rico Infrastructure Financing Authority  
Capital Center 235  
Ave. Arterial Hostos, Suite 1601  
San Juan, PR 00918-433

Agricultural Services and Development Administration  
P.O. Box 9200  
San Juan, PR 00908-0202

Cardiovascular Center Corporation of Puerto Rico and the Caribbean  
P.O. Box 366528  
San Juan, PR 00936-6528

Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico  
P.O. Box 362350  
San Juan, PR 00936-2350

Employment and Training Enterprises Corporation  
P.O. Box 366505  
San Juan, PR 00936-6505

Fine Arts Center Corporation  
P.O. Box 41287 – Minillas Station  
Santurce, PR 00940-1287

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Governing Board of the 9-1-1 Service  
P.O. Box 270200  
San Juan, PR 00927-0200

Institutional Trust of the National Guard of Puerto Rico  
P.O. Box 9023786  
San Juan, PR 00902-3786

Musical Arts Corporation  
P.O. Box 41227 – Minillas Station  
San Juan, PR 00940-1227

National Parks Company of Puerto Rico  
P.O. Box 9022089  
San Juan, PR 00902-2089

Public Corporation for the Supervision and  
Deposit Insurance of Puerto Rico Cooperatives  
P.O. Box 195449  
San Juan, PR 00919-5449

Puerto Rico Conservatory of Music Corporation  
350 Lamar Street and Roosevelt Avenue  
San Juan, PR 00918-2199

Puerto Rico Convention Center District Authority  
P.O. Box 19269  
San Juan, P.R 00910-1269

Puerto Rico Council on Higher Education  
P.O. Box 19900  
San Juan, PR 00910-1900

Puerto Rico Exports Development Corporation  
P.O. Box 195009  
San Juan , PR 00919-5009

Puerto Rico Government Investment Trust Fund  
P.O. Box 42001 – Minillas Station  
San Juan, PR 00940-2001

Puerto Rico Industrial Development  
Company  
P.O. Box 362350  
San Juan, PR 00936-2350

Puerto Rico Industrial, Tourist, Educational,  
Medical, and Environmental Control Facilities  
Financing Authority  
P.O. Box 42001 – Minillas Station  
San Juan, PR 00940-2001

Puerto Rico Land Administration  
P.O. Box 363767  
San Juan, PR 00936-3767

Puerto Rico Land Authority  
P.O. Box 9745  
San Juan, PR 00908-9745

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Puerto Rico Maritime Transportation Authority  
P.O. Box 362829  
San Juan, PR 00936-2829

Puerto Rico Medical Services  
Administration  
P.O. Box 2129  
San Juan, PR 00922-2129

Puerto Rico Metropolitan Bus Authority  
P.O. Box 195349  
San Juan, PR 00919-5349

Puerto Rico Municipal Finance Agency  
235 Arterial Hostos Avenue  
Suite 1601, Capital Center II  
San Juan, PR 00918-1433

Puerto Rico Ports Authority  
P.O. Box 362829  
San Juan, PR 00936-2829

Puerto Rico Public Broadcasting Corporation  
P.O. Box 19-0909  
San Juan, PR 00919-0909

Puerto Rico School of Plastic Arts  
P.O. Box 9021112  
San Juan, PR 00902-1112

Puerto Rico Solid Waste Authority  
P.O. Box 40285 – Minillas Station  
San Juan, PR 00940-0285

Puerto Rico Telephone Authority  
P.O. Box 42001  
San Juan, PR 00940-2001

Puerto Rico Trade and Export Company  
P.O. Box 195009  
San Juan, PR 00919-5009

Right to Employment Administration  
P.O. Box 364452  
San Juan, PR 00936-4452

Special Communities Perpetual Trust  
635 Fernandez Juncos Avenue,  
San Juan, PR 00907

State Insurance Fund Corporation  
P.O. Box 365028  
San Juan, PR 00936-5028

Tourism Company of Puerto Rico  
P.O. Box 902-3960  
Old San Juan Station  
San Juan, PR 00902-3960

The financial statements of the discretely presented component units have a year-end of June 30, 2004, except for the Puerto Rico Telephone Authority, which has a year-end of December 31, 2003.

### **Fiduciary Component Units**

The three employee retirement systems administer pension funds for the Commonwealth and its political subdivisions. The three systems are subject to legislative and executive controls, and the administrative expenses are subject to legislative budget controls. These component units, while meeting the definition of a component unit and are legally separate, are presented in the fund financial statements along with other fiduciary funds of the Commonwealth. They have been omitted from the government-wide financial statements.

***Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS)***  
– ERS is governed by a board of trustees, which is comprised by the Secretary of the Treasury of the Commonwealth, who is the President, the President of GDB, the Commissioner for Municipal Affairs, the Director of the Puerto Rico Central Office of Personnel Administration, two

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

participating employees, and one retiree, who are appointed by the Governor. The Commonwealth reports ERS as a single-employer pension plan. ERS is the administrator of a defined-benefit pension plan, which covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and component units not covered by their own retirement systems. On September 24, 1999, an amendment to the law that created ERS was enacted with the purpose of establishing a new defined-contribution plan (System 2000) for employees hired by the government on or after January 1, 2000.

***Puerto Rico Judiciary Retirement System (JRS)*** – JRS is governed by the same board of trustees as ERS. JRS is a single-employer defined-benefit plan, administered by ERS, which covers all individuals holding a position as Justice of the Supreme Court, Judge of the Superior Court or the District Court, or Municipal Judges of the Commonwealth.

***Puerto Rico System of Annuities and Pensions for Teachers (TRS)*** – TRS is governed by a five-member board comprised by the Secretary of Education of the Commonwealth, the Secretary of the Treasury of the Commonwealth, the President of GDB, and two participating members (one of whom is a retiree and the other the president of one of the teachers' organizations) appointed by the Governor with the advice and consent of the Senate for four years. The Commonwealth reports TRS as a single-employer pension plan. TRS provides retirement benefits to all teachers of the Department of Education of the Commonwealth, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education of the Commonwealth, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education of the Commonwealth. TRS provides retirement, death, and disability benefits.

Complete financial statements of these component units can be obtained directly by contacting their respective administrative offices at:

Employees' Retirement System of the  
Government of Puerto Rico and its  
Instrumentalities  
P.O. Box 42003 – Minillas Station  
Santurce, PR 00940

Puerto Rico Judiciary Retirement System  
P.O. Box 42003 – Minillas Station  
Santurce, PR 00940

Puerto Rico System of Annuities and Pensions for  
Teachers  
P.O. Box 191879  
San Juan, PR 00919-1879

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### (c) *Government-wide Financial Statements*

The government-wide financial statements (the statement of net assets and the statement of activities) report information of all of the nonfiduciary activities of the Commonwealth and its component units. For the most part, the effect of interfund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable. The statement of net assets presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- ***Invested in Capital Assets, Net of Related Debt*** – These consist of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- ***Restricted Net Assets*** – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- ***Unrestricted Net Assets*** – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

When both restricted and unrestricted resources are available for use, generally it is the Commonwealth's policy to use restricted resources first, then the unrestricted resources as they are needed.

The statement of activities demonstrates the degree to which the direct expenses of a given function, segment, or component unit are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function, segment, or component unit. Program revenue includes charges to customers who purchase, use, or directly benefit from goods or services provided by a given function, segment, or component unit. Program revenue also includes grants and contributions that are restricted to meeting the operational or capital requirements of a particular function, segment, or component unit. Taxes and other items not properly included among program revenue are reported instead as general revenue. Resources that are dedicated internally are reported as general revenue rather than as program revenue. The Commonwealth does not allocate general government (indirect) expenses to other functions.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

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

***Government-wide Financial Statements*** – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

***Governmental Fund Financial Statements*** – The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Commonwealth considers most revenue to be available if collected within 120 days after the end of the current fiscal year-end. Principal revenue sources considered susceptible to accrual include tax revenue, net of estimated overpayments (refunds) and amounts considered not collectible, which are recorded as taxpayers earn income (income taxes), as sales are made (consumption and use taxes), and as cash is received (miscellaneous taxes). In applying the susceptible to accrual concept to federal grants, there are essentially two types of revenue. For the majority of grants, moneys must be expended by the Commonwealth on the specific purpose or project before any amounts will be reimbursed. Revenue is, therefore, recognized as expenditures are incurred to the extent available. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the susceptible to accrual criteria is met. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- Employees' vested annual vacation and sick leave is recorded as an expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2004 has been reported only in the government-wide financial statements.
- Interest and principal on general long-term obligations are recorded when due, except for interest and principal due in July 1 of the following fiscal year.
- Executory purchase orders and contracts are recorded as a reservation of fund balance.
- Debt service expenditures, federal funds cost disallowances, other long-term obligations, and amounts subject to judgments under litigation are recorded only when payment is due.

***Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements*** – The financial statements of the proprietary funds, fiduciary funds and discretely presented component units are reported using the economic measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Each proprietary fund has the option under GASB Statement No. 20 to elect and apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless these conflict with a GASB pronouncement. The primary government's major enterprise funds have elected not to apply FASB pronouncements issued after November 30, 1989 and two nonmajor enterprise funds elected to adopt the FASB's pronouncements issued after November 30, 1989. Also, certain discretely presented component units have disclosed their election in their separately issued financial statements. The component units follow GAAP as issued by GASB and FASB as applicable to each component unit based on the nature of their operations. In addition, the Puerto Rico Government Investment Trust Fund adopted GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investments Pools*; however, such financial statements are not included in the accompanying basic financial statements because the primary government and each component units, investor already present their corresponding share of the assets of the PRGITF as cash or investments.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses. The major operating revenue of the Commonwealth enterprise funds is as follows:

- ***Unemployment Insurance Trust Fund*** – Amounts requisitioned for the Puerto Rico Unemployment Insurance Trust Fund held by the U.S. Treasury for payment of unemployment benefits and charges made to individual employers.
- ***Lotteries Fund*** – Amounts collected from the sale of traditional lottery tickets and electronic lotto games.

(e) ***Fund Accounting***

The Commonwealth reports its financial position and results of operations in funds, which are considered separate accounting entities and discrete presentations of those component units which are not required to be blended. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions. Major funds are determined using a predefined percentage of the assets, liabilities, revenue, or expenditures/expenses of either the fund category or the governmental and enterprise funds combined. The nonmajor funds are combined in a single column in the fund financial statements. The Commonwealth reports the following major funds:

### **Governmental Funds**

***General Fund*** – The general fund is the primary operating fund of the Commonwealth. It is used to account for all financial transactions, except those required to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, and education.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

***Debt Service Fund*** – The debt service fund accounts for the accumulation of resources predominantly for, and the payment of, general long-term bonds' principal, interest and related costs other than bonds payable from the operations of proprietary fund types, pension trust funds, and discretely presented component units. Long-term debt and interest due on July 1 of the following fiscal year are accounted for as a fund liability if resources are available as of June 30 for its payment.

***Public Buildings Authority Capital Projects Fund*** – The Public Buildings Authority's capital projects fund is used to account for the financial resources used for the acquisition or construction of major capital facilities not financed by proprietary fund types, pension trust funds, and discretely presented component units.

***The Children's Trust Special Revenue Fund*** – The Children's Trust special revenue fund is used to account for the moneys received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The financial resources received by this fund are used to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico.

### **Proprietary Funds**

These funds account for those activities for which the intent of management is to recover, primarily through user charges, the cost of providing goods or services to the general public.

***Unemployment Insurance Trust Fund*** – This fund accounts for amounts requisitioned for the Puerto Rico Unemployment Insurance Trust Fund held by the U.S. Treasury for payment of unemployment benefits and charges made to individual employers.

***Lotteries Fund*** – This fund accounts for the assets and operations of two lottery systems administered by the Commonwealth.

### **Fiduciary Funds**

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity, or as an agent for individuals, private organizations, and other governmental units. The following are the Commonwealth's fiduciary funds:

***Pension Trust Funds*** – are used to account for the assets, liabilities, and net assets available for pension benefits held in trust for the public employees' retirement systems.

***Agency Funds*** – are custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### **Discretely Presented Component Units**

Discrete presentation of component units is used to present the financial information of entities that do not qualify to be blended, in accordance with GASB No. 14, with the funds of the primary government. The component units column in the government-wide financial statements is used to report the financial activities of the Commonwealth's discretely presented component units. The financial statements of these component units are presented following the accrual basis of accounting. Under the accrual basis, revenue is recognized when earned and expenses are recorded as liabilities when incurred, without regard to receipt or payment of cash.

#### **(f) *Statutory (Budgetary) Accounting***

The Commonwealth's budget is adopted in accordance with a statutory basis of accounting, which is not in accordance with GAAP. Revenue is generally recognized when cash is received, net of tax refunds claimed by taxpayers as of year-end. Short- and long-term borrowings may be used to finance budgetary excess of expenditures over revenue. Expenditures are generally recorded when the related expenditure is incurred or encumbered. Encumbrances lapse the year following the end of the fiscal year when the encumbrance was established, as established by Act No. 123 of August 17, 2001, which amended the then existing appropriations and encumbrances lapsing provisions of Act No. 230 of July 23, 1974. Unencumbered appropriations lapse at year-end. Amounts required for settling claims and judgments against the Commonwealth, and certain other liabilities are not recognized until they are encumbered or otherwise processed for payment.

Under the statutory basis of accounting, the Commonwealth uses encumbrance accounting to record the full amount of purchase orders, contracts, and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control.

The statement of revenue and expenditures – budget and actual – budget basis – general fund, only presents the information for the general fund for which there is a legally adopted budget, as required by GAAP. See note 3 for a reconciliation of the statement of revenue and expenditures – budget and actual – budget basis – general fund with the statement of revenue, expenditures, and changes in fund balance (deficit) for the general fund.

#### **(g) *Cash and Short-Term Investments***

The Commonwealth follows the practice of pooling cash. The balance in the pooled cash accounts is available to meet current operating requirements, and any excess is invested in various interest-bearing accounts with GDB and with the PRGITF. At June 30, 2004, excess of checks drawn over the pooled bank balance amounted to \$230 million and is reported within accounts payable and accrued liabilities of the governmental activities.

Cash and cash equivalents include investments with original maturities of 90 days or less for the purpose of reporting enterprise fund cash flows.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The Commissioner of Financial Institutions requires that private financial institutions deposit collateral securities to secure the deposits of the Commonwealth and all other governmental entities in each of these institutions. The amount of collateral securities to be pledged for the security of public deposits shall be established by rules and regulations promulgated by the Commissioner of Financial Institutions.

The Puerto Rico Unemployment Insurance Trust Fund is maintained to account for the collection of unemployment insurance contributions from employers and the payment of unemployment benefits to eligible claimants. As required by federal law, all resources not necessary for current benefit payments are placed on deposit with the U.S. Treasury. Interest from these resources is retained in the fund.

Cash and short-term investments and cash equivalents of the component units are maintained in separate bank accounts, from those of the primary government, in their own names.

**(h) *Securities Purchased Under Agreements to Resell***

Certain component units of the Commonwealth enter into purchases of securities with simultaneous agreements to resell. The amounts advanced under these agreements generally represent short-term loans and are reflected as an asset. The securities underlying these agreements mainly consist of U.S. government obligations, mortgage-backed securities, and interest-bearing deposits with other banks.

**(i) *Securities Lending Transactions***

Certain component units of the Commonwealth enter into securities lending transactions in which governmental entities (lenders) transfer their securities to broker-dealers and other entities (borrowers) for collateral with a simultaneous agreement to return the collateral for the same securities in the future. Securities received as collateral are generally reflected as investments with a corresponding liability resulting from the obligation to return such collateral.

**(j) *Investments***

Investments include U.S. government and agencies obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, investment contracts, and corporate debt and equity obligations. Investment securities, including investments in limited partnership, are presented at fair value, except for money market investments and participating investment contracts with a remaining maturity at the time of purchase of one year or less and nonparticipating investment contracts, which are presented at cost. Changes in the fair value of investments are presented as investment earnings in the statement of activities, the statement of revenue, expenditures, and changes in fund balance – governmental funds, and the statement of revenue, expenses, and changes in fund net assets – proprietary funds. Fair value is determined based on quoted market prices. When securities are not listed on national exchanges, quotations are obtained from brokerage firms.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The PRGITF is considered a 2a7-like external investment pool, and as such, reports its investments at amortized cost.

The reverse repurchase agreements reported by certain discretely presented component units are authorized transactions under their respective enabling legislation and authorized by GDB.

**(k) Receivables**

Tax receivables in the general fund include predominantly amounts owed by taxpayers for individual and corporate income taxes, net of estimated uncollectible amounts. A portion of these income tax receivables is recognized as revenue when they become measurable and available based on actual collections during the 120 days following the fiscal year-end related to tax returns due before year-end. Tax receivables also include amounts owed by taxpayers on income earned in periods prior to June 30, 2004, estimated to be collectible but not currently available, and thus are reported as deferred revenue. Unemployment, disability, and driver's insurance receivable in the enterprise funds are stated net of estimated allowances for uncollectible accounts.

Taxes receivable also includes taxes that the Municipal Revenue Collection Center (CRIM, as per its Spanish acronym), a municipal corporation, is required to remit to the Commonwealth to be used by the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth. The amount to be remitted is based on the special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation, which is levied by the Commonwealth but collected by CRIM on the Commonwealth's behalf [see note 14(c)].

Accounts receivable are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables primarily represent amounts owed to the Commonwealth for reimbursement of expenditures incurred pursuant to federally funded programs.

The accounts receivable from nongovernmental customers of the component units are net of estimated uncollectible amounts. These receivables arise primarily from service charges to users. Accounts receivable from the primary government and other component units that arise from service charges do not have allowances for uncollectible accounts, as these are deemed fully collectible.

Loans of the general fund represent predominantly amounts owed by public corporations and municipalities for public insurance and rent paid by the general fund on their behalf.

The loans of the pension trust funds do not have allowances for uncollectible amounts since such loans are secured by mortgage deeds, plan members' contributions, and any unrestricted amounts remaining in escrow. Loans of the component units consist predominantly of loans to the primary government, other component units and municipalities, and do not have allowances for uncollectible accounts as those are deemed fully collectible. The remaining loans of the component units are to small and medium businesses, agricultural, and low-income housing loans from nongovernmental customers, and are presented net of estimated losses on such portfolios.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

**(l) Inventories**

Generally, inventories are valued at cost and predominantly on the first-in, first-out basis. Governmental fund inventories are recorded as expenditures when purchased rather than capitalized as an asset. Only significant amounts of inventory at the end of the year are capitalized in the governmental funds. However, inventories are always capitalized in the statement of net assets of governmental activities.

**(m) Restricted Assets**

Funds set aside for the payment and guarantee of notes and interest payable and for other specified purposes are classified as restricted assets since their use is limited for this purpose by applicable agreements or required by law. Restricted assets in the proprietary funds mainly include amounts set aside for the payment of lottery prizes.

**(n) Real Estate Held for Sale**

Real estate held for sale is stated at their estimated net realizable value determined by management based on previous units sales, commitments, or appraisal values.

**(o) Capital Assets**

Capital assets, which include land, buildings, building improvements, equipment, vehicles, construction in process, and infrastructure assets are reported in the applicable governmental, business-type activities and component unit columns in the government-wide financial statements. The Commonwealth's primary government defines capital assets as assets, which have an initial, individual cost of \$25,000 or more at the date of acquisition and have a useful life of five or more years. Capital assets are recorded at historical cost or at estimated historical cost if actual historical cost is not available.

The method to deflate the current cost of the same or a similar asset using an approximate price index was used to estimate the historical cost of certain land, buildings, and building improvements because invoices and similar documentation was no longer available in certain instances. Donated capital assets are recorded at fair market value at the time of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest costs are capitalized during construction period only for business-type activities and most component units. The costs of normal maintenance and repairs that do not add value to the assets or materially extend asset lives are not capitalized.

GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, provides transition standards that make available an extended period of deferral (fiscal year 2006) before the requirement to record and depreciate general infrastructure assets acquired before the implementation date (July 1, 2001) becomes

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

effective. General infrastructure assets (such as, dams, intake facilities, and similar items) acquired prior to July 1, 2001 have not been recorded because capitalization information is not available. No new infrastructure expenditures have been made by governmental activities after implementation year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the primary government are depreciated on the straight-line method over the assets' estimated useful life. There is no depreciation recorded for land and construction in progress. The estimated useful lives of capital assets are as follows:

	<u>Years</u>
Buildings and buildings improvements	20-50
Equipment, furniture, fixtures, and vehicles	5-15

The capital assets of the component units are recorded in accordance with the applicable standards of the component units and under their own individual capitalization thresholds. Depreciation has been recorded when required by these standards based on the types of assets, use and estimated useful lives of the respective assets, and on the nature of each of the component unit's operations.

The estimated useful lives of capital assets reported by the component units are as follows:

	<u>Years</u>
Buildings and buildings improvements	3-50
Equipment, furniture, fixtures, and vehicles	3-20
Infrastructure	10-50

**(p) Tax Refunds Payable**

During the calendar year, the Commonwealth collects individual income taxes through withholdings and payments from taxpayers. At June 30, the Commonwealth estimates the amount owed to taxpayers for overpayments during the first half of the calendar year. These estimated amounts and the actual tax refunds claimed for prior years but not paid at year-end are recorded as tax refunds payable and as a reduction of tax revenue.

**(q) Deferred Revenue**

Deferred revenue at the governmental fund level arises when potential revenue does not meet both the "measurable" and "available" criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Commonwealth has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Commonwealth has a legal claim

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized. Deferred revenue at the government-wide and proprietary fund levels arises only when the Commonwealth receives resources before it has a legal claim to them.

(r) ***Long-Term Debt***

The liabilities reported in the government-wide financial statements include Commonwealth general obligation bonds and long-term notes, obligations under lease/purchase agreements, and long-term liabilities including vacation, sick leave, long-term liabilities to other governmental entities, net pension obligation, legal claims, and noncurrent federal fund cost disallowances related to expenditures of federal grants. Long-term obligations financed by proprietary fund types and component units are recorded as liabilities in those funds and in the discretely presented component unit's column.

***Premiums, Discounts, and Issuance Costs*** – In the government-wide financial statements, long-term debt and other long-term obligations are presented in the columns for governmental and business-type activities. The same is presented in the proprietary fund financial statements. Bond and note premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt. Bonds and notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges in other assets and are amortized over the term of the related debt. In the governmental fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

(s) ***Reservations of Fund Balance – Governmental Funds***

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. The reserves for related assets such as inventories and prepayments are examples of the former. Reserves for encumbrances, debt service, and other specific purposes are examples of the latter.

(t) ***Accounting for Pension Costs***

For the purpose of applying the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* (GASB No. 27), the Commonwealth's financial reporting entity is considered to be a sponsor of three single-employer defined-benefit pension plans: ERS, JRS, and the TRS. This is because substantially all the participants in the three pension trust funds are part of the financial reporting entity of the Commonwealth. For the purpose of the basic financial statements, and as disclosed in note 19, the Commonwealth's annual pension cost, measured on the accrual basis of accounting, for the year ended June 30, 2004 amounted to approximately \$880 million. However, the amount recognized as pension expenditure in the governmental funds was recorded under the modified accrual basis, and amounted to approximately \$501 million. The excess

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

of the annual required contribution over the statutorily required contributions increased the net pension obligation at June 30, 2004 to approximately \$4.2 billion. This amount is presented in the statement of net assets of the governmental activities as of June 30, 2004.

For purposes of the stand-alone financial statements of each of the blended and discretely presented component units, the entities accounted for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized are equal to the statutorily or contractually required contributions, with a liability recorded for any unpaid required contributions. The basis of accounting used by the component units was either modified accrual basis or accrual basis, depending upon individual fund structure and type of entity. Most component units did not have pension-related assets or liabilities at transition because they have contributed the statutorily required contributions.

**(u) *Postemployment Benefits***

In addition to the pension benefits described in note 19, the Commonwealth provides postemployment healthcare benefits and a Christmas bonus for its retired employees in accordance with local law. Substantially all of the employees may become eligible for these benefits if they reach normal retirement age while working for the Commonwealth. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree with the Commonwealth providing a matching share of not more than \$100 per month for each retiree. During the year ended June 30, 2004, the cost of providing healthcare benefits amounted to approximately \$100 million for approximately 92,000 retirees. The Christmas bonus paid to the retired employees during the year ended June 30, 2004 was \$400 per retiree and the total amount was approximately \$36.7 million for approximately 91,830 retirees. These benefits are recorded as expenditures when paid in the general fund.

**(v) *Compensated Absences***

The vacation policy of the Commonwealth generally provides for the accumulation of 2.5 days per month, except for the teachers who accrue 4 days per month. Vacation time accumulated is fully vested to the employees from the first day of work up to a maximum of 60 days. Employees accumulate sick leave generally at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid leave at the current rate, if the employee has at least 10 years of service with the Commonwealth. Accrued compensated absences of the primary government at June 30, 2004 amounting to approximately \$1.4 billion are presented in the statement of net assets. Compensated absence accumulation policies for the blended component units and component units vary from entity to entity based on negotiated agreements and other factors agreed upon between the management of these entities and their employees.

The Public Service Personnel Law requires certain component units and the primary government of the Commonwealth to annually pay the employees the accumulated vacation and sick leave earned in excess of the limits mentioned above.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

(w) ***Interfund and Intraentity Transactions***

The Commonwealth has the following types of transactions among funds:

***Interfund Transfers*** – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds. Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivable and payable are considered internal balances and activities that have been eliminated in the government-wide financial statements.

***Intraentity Transactions*** – There are two types of intraentity transactions. First are resource flows between the primary government and its component units and among the component units. These resource flows and related outstanding balances are reported as if they were external transactions. However, resource flows between the primary government and blended component units are classified as interfund transactions, as described above.

Second are intraentity balances between the primary government funds and discretely presented component units that are tantamount to long-term debt financing. The primary government's liability is reported in the statement of net assets, the proceeds in the primary government's funds, and the asset in the discretely presented component units' statement of net assets.

(x) ***Lottery Revenue and Prizes***

The revenue, expenses, and prizes awarded by the Lottery of Puerto Rico and the Additional Lottery System, reported within the lotteries enterprise fund, are recognized as drawings are held. Moneys collected prior to June 30 for tickets related to drawings to be conducted subsequent to June 30 are reported as deferred revenue. Unpaid prizes awarded as of June 30 are reported as a fund liability. The Commonwealth maintains cash deposited in GDB for the payment of prizes payable in installments. The cash is reported as restricted assets and the prizes installments payable are reported as lottery prizes payable.

(y) ***Risk Management***

The Commonwealth purchases commercial insurance covering casualty, theft, tort claims, and other losses for the primary government, most component units, and the municipalities. The Commonwealth is reimbursed for premium payments made on behalf of the component units and the municipalities. The current insurance policies have not been canceled or terminated. For workers' compensation, the Commonwealth has a discretely presented component unit, the SIFC, which provides workers' compensation to both public and private employees. In the past three years, the Commonwealth has not settled claims that exceed insurance coverage.

Certain component units combine commercial insurance with internal self-insurance funds covering specific risks related to their specialized operations.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

**(z) *Reclassifications***

Certain reclassifications have been made to the information presented in the separately issued financial statements of certain blended component units and agencies included within the special revenue, debt service, capital projects, and enterprise funds; and discretely presented component units to conform to the accounting classifications used by the Commonwealth in the basic financial statements.

**(aa) *Use of Estimates***

The preparation of the basic financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**(bb) *Future Adoption of Accounting Pronouncements***

The GASB has issued the following accounting standards that have effective dates after June 30, 2004:

- GASB Statement No. 40, *Deposit and Investment Risk Disclosures, an amendment of GASB Statement No. 3*, which is effective for fiscal years beginning after June 15, 2004.
- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which is effective for fiscal years beginning after December 15, 2004.
- GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is effective for fiscal years beginning after December 15, 2004.
- GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section—an amendment of NCGA Statement 1*, which is effective for statistical sections prepared for periods beginning after June 15, 2005.
- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which is effective for fiscal years beginning after December 15, 2006.
- GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation*, which is effective for fiscal years, beginning after June 15, 2005.
- GASB Technical Bulletin No. 2004-2, *Recognition of Pensions and Other Postemployment Benefit Expenditures/Expense and Liability by Cost-Sharing Employers*, which is effective for fiscal years ending after December 15, 2004.

The impact of these statements on the Commonwealth's basic financial statements has not yet been determined.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### (2) Component Units

The Commonwealth follows the provisions of GASB No. 14. The basic financial statements of the Commonwealth include the financial statements of the following component units that were audited by other auditors:

#### Blended component units:

- Public Buildings Authority
- Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities
- Puerto Rico Judiciary Retirement System
- Puerto Rico System of Annuities and Pensions for Teachers

#### Discretely presented component units:

- Agricultural Services and Development Administration
- Automobile Accident Compensation Administration
- Cardiovascular Center Corporation of Puerto Rico and the Caribbean
- Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico
- Employment and Training Enterprises Corporation
- Farm Insurance Corporation of Puerto Rico
- Fine Arts Center Corporation
- Governing Board of the 9-1-1 Service
- Institutional Trust of the National Guard
- Musical Arts Corporation
- National Parks Company of Puerto Rico
- Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives
- Puerto Rico Aqueduct and Sewer Authority
- Puerto Rico Conservatory of Music Corporation
- Puerto Rico Convention Center District Authority
- Puerto Rico Council on Higher Education
- Puerto Rico Electric Power Authority
- Puerto Rico Exports Development Corporation
- Puerto Rico Health Insurance Administration
- Puerto Rico Highway and Transportation Authority
- Puerto Rico Land Administration
- Puerto Rico Land Authority
- Puerto Rico Maritime Transportation Authority
- Puerto Rico Medical Services Administration
- Puerto Rico Metropolitan Bus Authority
- Puerto Rico Ports Authority
- Puerto Rico Public Broadcasting Corporation

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Puerto Rico Trade and Export Company  
Puerto Rico School of Plastic Arts  
Puerto Rico Solid Waste Authority  
Right to Employment Administration  
Special Communities Perpetual Trust  
State Insurance Fund Corporation  
University of Puerto Rico

### (3) Stewardship, Compliance, and Accountability

#### (a) *Budgetary Control*

The Governor is constitutionally required to submit to the Legislature an annual balanced budget of the Commonwealth for the ensuing fiscal year. The annual budget is prepared by the Commonwealth's OMB and takes into consideration the advice provided by the Puerto Rico Planning Board (annual economic growth forecasts; four-year capital improvements plan), the Department of the Treasury of the Commonwealth (revenue estimates, accounting records, and the comprehensive annual financial report), GDB (fiscal agent), and other governmental offices and agencies. Section 7 of Article VI of the Constitution of Puerto Rico provides that "The appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year, unless the imposition of taxes sufficient to cover said appropriations is provided by law."

The annual budget, which is developed utilizing elements of performance-based program budgeting and zero-based budgeting, includes an estimate of revenue and other resources for the ensuing fiscal year under: (1) laws existing at the time the budget is submitted; and (2) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in her judgment are necessary, convenient, and in conformity with the four-year capital improvements plan adopted by the Puerto Rico Planning Board.

The Legislature may amend the budget submitted by the Governor but may not increase any items so as to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. Upon approval by the Legislature, the budget is referred to the Governor who may decrease or eliminate any line item but may not increase or insert any new line item in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature with her objections. The Legislature, by two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Legislature and the Governor, is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This permits the Commonwealth to continue making payments for its operating and other expenses until the new budget is approved. The appropriated annual budget for fiscal year 2004 amounted to approximately \$5.1 billion. The Legislature also made several special budgetary appropriations to the general fund throughout the year, which amounted to approximately \$3.2 billion.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The OMB has authority to amend the budget within a department, agency, or government unit without legislative approval.

For budgetary purposes, encumbrance accounting is used. The encumbrances (that is, purchase orders, contracts) are considered expenditures when a commitment is made. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of budgetary appropriations and GAAP fund balances and do not constitute expenditures or liabilities on a GAAP basis because the commitments will be honored during the subsequent year. The unencumbered balance of any appropriation of the general fund at the end of the fiscal year lapses immediately. Appropriations, other than in the general fund, are continuing accounts for which the Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

In addition, the Legislature may direct that certain revenue be retained and made available for spending within a specific appropriation account. Generally, expenditures may not exceed the level of spending authorized for an individual department. However, the Commonwealth is statutorily required to pay debt service, regardless of whether such amounts are appropriated. Appropriations are enacted for certain departments, agencies, and government units included in the balance sheet of the general fund. For these funds, a statement of revenue and expenditures – budget and actual – budget basis – general fund is included. Appropriations for capital projects are made for each bond issue and the authorization continues for the expected construction period.

The Commonwealth's Department of the Treasury and OMB has the responsibility to ensure that budgetary spending control is maintained on an individual department basis. OMB may transfer part or all of any unencumbered balance within a department to another department subject to legislative approval. Budgetary control is exercised through the Puerto Rico Integrated Financial Accounting System (PRIFAS). PRIFAS ensures that encumbrances or expenditures are not processed if they exceed the department's total available spending authorization, which is considered its budget. The legal level of budgetary control is at the individual department level for general fund expenditures, principal and interest due for the year for the debt service fund, and by bond authorization for capital expenditures.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

**(b) Budget/GAAP Reconciliation**

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity, timing, and basis differences in the excess (deficiency) of revenue and other sources of financial resources over expenditures and other uses of financial resources for the year ended June 30, 2004 is presented below for the general fund (expressed in thousands):

Excess of expenditures and other financing uses over revenue and other sources – budget basis	\$ (107,718)
Entity differences:	
Excess (deficiency) of revenue and other sources over expenditures and other uses for:	
Nonbudgeted funds	(589,773)
Inclusion of agencies with independent treasuries	658,101
Timing differences:	
Adjustment for encumbrances	37,927
Current year expenditure against prior year encumbrances	(38,909)
Basis of accounting differences:	
Net increase in taxes receivable (net of tax refunds)	(96,336)
Net decrease in other receivables	65,409
Net increase in deferred revenue	(122,405)
Proceeds from short-term line of credit reported as other financing source on a budgetary basis but as a fund liability on a GAAP basis	(140,000)
Qualified Zone Academic Bonds (QZAB) reported as an other financing source on a GAAP basis, not on a budgetary basis	47,936
Excess of expenditures and other financing uses over revenue and other financing sources (GAAP basis)	\$ (285,768)

**(c) Deficit Net Assets**

The following activities, funds, and discretely presented component units reflect deficit fund balance/net assets at June 30, 2004 (expressed in thousands):

Primary government:	
Governmental activities	\$ <u>13,656,346</u>
General fund	\$ <u>365,950</u>
Debt service fund	\$ <u>3,761</u>
Enterprise fund – lotteries	\$ <u>1,365</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### Component units:

Puerto Rico Land Authority	\$ <u>151,723</u>
Special Communities Perpetual Trust	\$ <u>81,326</u>
Cardiovascular Center Corporation of Puerto Rico and the Caribbean	\$ <u>40,575</u>
Tourism Company of Puerto Rico	\$ <u>11,123</u>
Agricultural Services and Development Administration	\$ <u>8,350</u>
Employment and Training Enterprises Corporation	\$ <u>5,376</u>

The Commonwealth's governmental activities show a deficit of approximately \$13.7 billion, mostly attributed to long-term obligations amounting to approximately \$23 billion, which is recognized in the statement of net assets.

In order to improve the financial situation of the Commonwealth, management is evaluating various strategic initiatives. Among these strategic initiatives is a fiscal reform lead by the implementation of a new consumption-based tax system. While the fiscal reform is implemented, management has identified temporary measures including proposed legislation, which affects the existing tax system. These measures should lead to an increase in the Commonwealth's recurring annual revenues. Other temporary initiatives being evaluated include spending reduction measures. To stimulate economic growth, the Commonwealth intends to invest in several strategic development/infrastructure projects, promote economically feasible Puerto Rican products/services, promote foreign direct investment, and diversify the portfolio of industries operating in Puerto Rico by attracting additional investments in the services industry. It is management's belief that these initiatives will improve the financial situation of the Commonwealth in future fiscal years.

On the other hand, the discretely presented component units report net assets of approximately \$16 billion. This inverse relationship between the governmental activities and component units' net assets reveal the operational structure of the Commonwealth where the primary government issues debt, the proceeds of which are predominantly transferred to the component units and to other governments as well, to finance their capital projects and other operational needs. The Commonwealth includes within the annual budgetary appropriation process the necessary funds to cover the annual debt service requirements of the aforementioned debt.

In the past, the Commonwealth has also provided financial resources to finance the deficit of component units. In addition, certain loans and obligations of TCPR and PRLA with GDB were restructured pursuant to Act No. 164, of December 17, 2001, described in note 14 (d).

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### (4) Changes in Reporting Entity and Restatement

The following table illustrates the change to net assets at the beginning of the year as previously reported in the governmental activities' statement of net assets. The change resulted from the effect of an incorrect inclusion in prior years of a capital asset that had been previously sold by a government agency and the elimination of certain bonds and notes payable to the United States Department of Housing and Urban Development (HUD) in the aggregate amount of approximately \$1.1 billion, for which HUD had agreed to pay through secured annual contributions prior to July 1, 2003. These notes were removed because they do not constitute a debt of the government agency. The beginning net assets have been restated as follows (expressed in thousands):

Beginning net assets, as previously reported	\$ 11,952,784
Restatements	<u>(1,068,485)</u>
Beginning net asset, as restated	<u>\$ 10,884,299</u>

The following table summarizes changes to net assets at the beginning of the year as previously reported in the statement of net assets by certain discretely presented component units. The changes resulted primarily from exclusions of nonmajor component units in current years' presentation, and restatements to correct errors in the prior year's financial statements of certain nonmajor component units (expressed in thousands):

Beginning net assets, as previously reported	\$ 16,181,807
Nonmajor component units excluded in fiscal year 2004, but included in fiscal year 2003	33,056
Restatements of nonmajor component units	<u>(12,133)</u>
Beginning net assets, as restated	<u>\$ 16,202,730</u>

### (5) Puerto Rico Government Investment Trust Fund (PRGITF)

PRGITF was created by Act No. 176, of August 11, 1995, and began operations on December 4, 1995. PRGITF is a no-load diversified collective investment trust administered by GDB that was created for the purpose of providing eligible governmental investors of Puerto Rico with a convenient and economical way to invest in a professionally managed money market portfolio. PRGITF is not an investment company or a mutual fund and is not subject to regulation or registration under the investment company Act of 1940. Units issued by PRGITF are not subject to regulation or registration under the Securities and Exchange Act of 1933, as amended, because the units are issued by a government entity. The deposits on hand and the investments purchased are not collateralized, secured, or guaranteed by the Commonwealth or any of its agencies, instrumentalities, or political subdivisions.

PRGITF is considered a 2a7-like external investment pool, and as such, reports its investment at amortized cost.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The investment securities on hand at June 30, 2004, consisted of certificates of deposit, bank notes, corporate obligations, commercial paper, and U.S. government and agencies obligations, all of which may be considered highly liquid. However, the participants' investments are subject to the ability of PRGITF to receive payment from the securities' issuer when due. The liquidity of certain investments and changes in interest rates may affect PRGITF's yield and the fair value of its investments.

The dollar amount of the deposits on hand at June 30, 2004, at \$1.00 per unit of participation, was reported in the individual financial statements of each of the participants, and combined in the basic financial statements as follows (expressed in thousands):

	<b><u>Balance outstanding</u></b>	<b><u>Percentage of total</u></b>
Primary government:		
Commonwealth	\$ 360,451	65.76%
The Children's Trust	147,737	26.95%
Public Buildings Authority	210	0.04%
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	2	0.00%
Total for primary government	508,400	92.75%
Discretely presented component units:		
Government Development Bank for Puerto Rico	12,760	2.33%
Puerto Rico Aqueduct and Sewer Authority	11,350	2.07%
Tourism Company of Puerto Rico	5,218	0.95%
Puerto Rico Institutional Trust of National Guard	3,308	0.60%
Puerto Rico Solid Waste Authority	1,508	0.28%
Puerto Rico Land Administration	616	0.11%
Puerto Rico Infrastructure Financing Authority	600	0.11%
State Insurance Fund Corporation	390	0.07%
Puerto Rico Highway and Transportation Authority	273	0.05%
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico	229	0.05%
National Parks Company of Puerto Rico	40	0.01%
Total for discretely presented component units	36,292	6.63%
Other governmental entities	3,436	0.62%
Total for all participants	\$ 548,128	100%

The deposits at June 30, 2004 were invested in securities with a cost which approximates fair value, plus accrued interest, for approximately \$548 million. The external portion of PRGITF was not considered significant for separate reporting in the accompanying basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### (6) Deposits and Investments

Under Commonwealth statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury's agents in the Commonwealth's name. In addition, the Commonwealth maintains deposits with GDB and EDB, two discretely presented component units, and the U.S. government (for unemployment insurance).

The Commonwealth's bank balance of deposits with financial institutions are categorized to provide an indication of the level of custodial credit risk assumed by the Commonwealth at year-end. Risk categories are described as follows:

**Category 1:** Insured or collateralized with securities held by the Secretary of the Treasury's agents in the Commonwealth's name.

**Category 2:** Collateralized with securities held by the pledging financial institution's trust department or agent in the Commonwealth's name.

**Category 3:** Uncollateralized (this includes any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the Commonwealth's name).

The Commonwealth's investments are categorized to provide an indication of the level of custodial credit risk assumed by the Commonwealth at year-end. Risk categories are described as follows:

**Category 1:** Insured or registered, or securities held by the Commonwealth or its agents in the Commonwealth's name.

**Category 2:** Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the Commonwealth's name.

**Category 3:** Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent, but not in the Commonwealth's name.

Pursuant to the Statement of Investment Guidelines for the Government of Puerto Rico, the agencies and public corporations may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, among other types of investments.

The public employees' retirement systems may invest in stocks, corporate bonds, U.S. mortgage loan obligations, private equity, and others.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### *Primary Government*

The carrying amount of deposits with financial institutions of the primary government at June 30, 2004 consists of the following (expressed in thousands):

Unrestricted:		
Carrying amount of deposits in commercial banks	\$	86,604
Carrying amount of deposits in governmental banks		1,107,089
Carrying amount of deposits with the U.S. government		<u>485,083</u>
Subtotal		<u>1,678,776</u>
Restricted:		
Carrying amount of deposits in commercial banks		1,202,935
Carrying amount of deposits in governmental banks		1,270,880
Carrying amount of deposits with the U.S. government		<u>42,013</u>
Subtotal		<u>2,515,828</u>
Total carrying amount of deposits as reported on the primary government statement of net assets	\$	<u>4,194,604</u>

At year end, the government's bank balance of deposits in commercial banks of \$1.3 billion was covered by Federal depository insurance of by collateral held by the government's agent in the government's name. The bank balance of deposits in governmental banks, which as of June 30, 2004, is uninsured and uncollateralized, is approximately \$3.1 billion. These deposits are maintained with GDB and EDB. Deposits of approximately \$485 million with the U.S. government represent unemployment insurance taxes collected from employers that are transferred to the Federal Unemployment Insurance Trust Fund in the U.S. Treasury.

Unrestricted deposits include approximately \$361 million of deposits from the Commonwealth that are invested in PRGITF (See note 5). Such amount has been included as cash and cash equivalents in the primary government's statement of net assets.

Deposits in governmental banks represent the balance of interest and noninterest-bearing accounts in GDB and EDB. The deposit liability at GDB and EDB is substantially related to deposits from other component units and of the Commonwealth. The deposit liability does not agree with the governmental cash balances

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

shown because of reconciling items such as outstanding checks and deposits in transit. The bank balance of GDB's and EDB's deposits at June 30, 2004 is broken down as follows (expressed in thousands):

Primary government	\$ 2,095,291
Discretely presented components units	<u>960,178</u>
Total reporting entity	3,055,469
Municipalities of Puerto Rico	494,813
Other nongovernmental entities	328,906
Certificates of indebtedness	251,798
Escrow accounts	<u>189,706</u>
Total deposits per GDB and EDB	<u>\$ 4,320,692</u>

Custodial credit risk classification for short-term investments and investments of the primary government are as follows (expressed in thousands):

	Category			Carrying amount
	1	2	3	
Unrestricted:				
Mortgage notes	\$ 14	—	—	14
U.S. government and agencies securities	<u>34,127</u>	—	—	<u>34,127</u>
Subtotal	<u>34,141</u>	—	—	<u>34,141</u>
Investments not subject to categorization:				
Puerto Rico Government Investment Trust Fund	—	—	—	147,737
External investment pool	—	—	—	84,133
Guaranteed investment contracts	<u>—</u>	—	—	<u>177,305</u>
Subtotal	—	—	—	<u>409,175</u>
Total – unrestricted	<u>\$ 34,141</u>	<u>—</u>	<u>—</u>	<u>443,316</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

***Component Units***

Cash, cash equivalents, and investments of the component units at June 30, 2004 consist of (expressed in thousands):

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Cash and cash equivalents	\$ 2,106,011	789,952	2,895,963
Investments	4,926,872	5,498,957	10,425,829
Total	<u>\$ 7,032,883</u>	<u>6,288,909</u>	<u>13,321,792</u>

Cash and cash equivalents consist of demand deposits, interest-bearing accounts, certificates of deposit, and bank investment contracts.

Information of carrying amounts and bank balances for deposits with financial institutions and bank investment contracts is as follows (expressed in thousands):

	<u>Carrying amount</u>	<u>Bank balance</u>
Deposits in commercial banks	\$ 2,219,735	2,204,140
Deposits in governmental banks	676,228	692,487
Total	<u>\$ 2,895,963</u>	<u>2,896,627</u>
Bank balances of deposits in banks:		
Category 1		\$ 1,219,313
Category 2		1,456
Category 3		<u>1,675,858</u>
Total bank balance of deposits in banks		<u>\$ 2,896,627</u>

The bank balance of deposits in governmental banks is uninsured and uncollateralized. Such deposits are maintained with GDB and EDB.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Custodial credit risk classification for short-term investments and investments of component units are as follows (expressed in thousands):

	<b>Category</b>			<b>Carrying Amount</b>
	<b>1</b>	<b>2</b>	<b>3</b>	
<b>Unrestricted:</b>				
Mortgage-backed securities	\$ 168,368	27,611	21,003	216,982
U.S. government and agencies securities	1,918,390	89,932	185,801	2,194,123
Negotiable certificates of deposit	188,874	—	99,099	287,973
Stocks	577,159	—	22,572	599,731
Corporate bonds	400,904	26,987	10,005	437,896
Repurchase agreements	35,000	—	56,167	91,167
Short-term investment	—	—	5,744	5,744
Foreign and municipal bonds	1,517	—	—	1,517
Money market funds	27,234	—	14,900	42,134
Other investments	—	—	340	340
Subtotal	<u>3,317,446</u>	<u>144,530</u>	<u>415,631</u>	<u>3,877,607</u>
<b>Investments not subject to categorization:</b>				
Guaranteed investment contracts	—	—	—	877,627
Puerto Rico Government Investment Trust Fund	—	—	—	1,655
Investment pool	—	—	—	132,906
Securities lending transactions underlying securities	—	—	—	33,838
Investment in equity securities	—	—	—	3,239
Total – unrestricted	<u>3,317,446</u>	<u>144,530</u>	<u>415,631</u>	<u>4,926,872</u>
<b>Restricted:</b>				
U.S. government and agencies securities	2,531,116	55,157	39,948	2,626,221
Foreign and municipal bonds	—	1,316,021	—	1,316,021
Mortgage-backed securities	350	657,491	—	657,841
Repurchase agreements	160,000	—	—	160,000
Negotiable certificates of deposit	5,048	—	21,083	26,131
Corporate bonds	12,621	1,857	—	14,478
Stocks	24,618	—	—	24,618
Subtotal	<u>\$ 2,733,753</u>	<u>2,030,526</u>	<u>61,031</u>	<u>4,825,310</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

	<u>Category</u>			<u>Carrying amount</u>
	<u>1</u>	<u>2</u>	<u>3</u>	
Subtotals brought forward	\$ 2,733,753	2,030,526	61,031	4,825,310
Investments not subject to categorization:				
Guaranteed investment contracts	—	—	—	668,384
Investment pool	—	—	—	4,717
Money market funds/mutual funds	—	—	—	546
Total – restricted	<u>2,733,753</u>	<u>2,030,526</u>	<u>61,031</u>	<u>5,498,957</u>
Total	<u>\$ 6,051,199</u>	<u>2,175,056</u>	<u>476,662</u>	<u>10,425,829</u>

Unrestricted repurchase agreements of approximately \$35 million and \$56 million belong to EDB and SIFC, respectively. As of June 30, 2004, the fair value of the collateral for the repurchase agreements amounted to approximately \$35 million for EDB, which consisted primarily of investment securities held in custody by EDB's agent, and \$56 million for SIFC, which consisted primarily of investment securities held by SIFC's agent but not in SIFC's name.

Certain discretely presented component units classified approximately \$25 million of investments in PRGITF as cash and cash equivalents.

***Fiduciary Funds***

The carrying amount of deposits with financial institutions of the fiduciary funds at June 30, 2004 consists of (expressed in thousands):

Unrestricted:		
Carrying amount of deposits in commercial banks	\$	535,569
Carrying amount of deposits in governmental banks		<u>129,845</u>
Subtotal		<u>665,414</u>
Restricted:		
Carrying amount of deposits in commercial banks		2,396
Carrying amount of deposits in governmental banks		<u>4,857</u>
Subtotal		<u>7,253</u>
Total carrying amount of deposits as reported on the statement of fiduciary net assets	\$	<u>672,667</u>
Bank balance of deposits in commercial banks:		
Category 1	\$	<u>537,965</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The bank balance of deposits in governmental banks, amounting to \$135 million at June 30, 2004, is uninsured and uncollateralized.

Custodial credit risk classification for short-term investments and investments of the fiduciary funds are as follows (expressed in thousands):

	<b>Category</b>			<b>Carrying amount</b>
	<b>1</b>	<b>2</b>	<b>3</b>	
Investment in preferred stock of PRTA				
Holdings	\$ —	—	404,390	404,390
Stocks	—	—	2,890,385	2,890,385
U.S. government and agencies securities	2,281	—	39,204	41,485
Mortgage bank securities	762	—	—	762
Corporate bonds	—	—	368,766	368,766
Short-term investments	15,008	—	—	15,008
State and local government bonds	4,948	—	—	4,948
	<u>22,999</u>	<u>—</u>	<u>3,702,745</u>	<u>3,725,744</u>
Subtotal				
Investments not subject to categorization:				
Limited partnership/private equity	—	—	85,292	85,292
	<u>—</u>	<u>—</u>	<u>85,292</u>	<u>85,292</u>
Total	<u>\$ 22,999</u>	<u>—</u>	<u>3,788,037</u>	<u>3,811,036</u>

Uninsured or unregistered investments at June 30, 2004 shown above belong mainly to the ERS.

ERS classified approximately \$2 thousand of investments in PRGITF as cash and cash equivalents. (See note 5)

**(7) Securities Lending Transactions**

***Primary Government***

During the year, the ERS and the JRS, included within the fiduciary funds, SIFC and AACA, two discretely presented component units, entered into securities lending transactions. These transactions amounting to \$92 million, pertaining to the retirement systems, and \$155 million, pertaining to the discretely presented component units, at June 30, 2004, are included within investments and the corresponding securities lending liability in the statement of fiduciary net assets and the statement of net assets, respectively.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### **Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities and Puerto Rico Judiciary Retirement System (the Retirement Systems)**

The Retirement Systems' securities custodian, as agent for the Retirement Systems, manages the securities lending program and receives liquid collateral. The collateral requirement amounted to approximately \$94.5 million of the fair value of the securities lent. The collateral securities cannot be pledged or sold unless the borrower defaults. Securities lending obligations for which collateral was received as of June 30, 2004 consist of the following (expressed in thousands):

<u>Securities lent</u>	<u>Fair value of underlying securities</u>
Corporate bonds	\$ 10,802
Equity securities	<u>80,839</u>
	<u>\$ 91,641</u>

Collateral received amounted to \$94.4 million and it was invested as follows: \$15 million in commercial paper, \$69.5 million in reverse report government delivered, and \$10 million in time and master note. The relationship between the investment maturities and the Retirement Systems' loans cannot be determined.

At year-end, the Retirement Systems have no credit risk exposure to borrowers because the amounts the Retirement Systems owe the borrowers exceed the amounts the borrowers owe to the Retirement Systems. The Retirement Systems' rights to collateral are defined in the contractual agreements. The borrower's creditworthiness is also proactively reviewed by the lending agent.

### ***Component Units***

#### **SIFC**

The Commonwealth statutes and the SIFC's board of directors' policies permit SIFC to use its investments to enter into securities lending transactions. The SIFC's securities custodian, as agent of SIFC, manages the securities lending program and receives cash, securities, or irrevocable bank letters of credit as collateral. The collateral securities cannot be pledged or sold by SIFC unless the borrower defaults. The collateral requirement is equal to 102% for securities issued in the United States and 105% for securities issued outside of the United States of the fair value of the securities lent. Additional collateral has to be provided by the next business day if its value falls to less than 100% of the fair value of the securities lent. At year-end, SIFC has no credit risk exposure to borrowers because the amounts SIFC owes the borrowers exceed the amounts the borrowers owe SIFC. Contracts with the lending agents require them to indemnify SIFC if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay SIFC for income distributions by the securities' issuers while the securities are on loan.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

All security loans can be terminated on demand by either SIFC or the borrower, although the average term of the loans is two weeks. In lending securities, the term to maturity of the securities loans is matched with the term to maturity of the investment of the cash collateral. Such matching existed at year-end. Securities lending obligations for which cash was received as collateral as of June 30, 2004 consist of the following (expressed in thousands):

<b>Securities lent</b>	<b>Fair value of underlying securities</b>
Equity securities	\$ 21,316
U.S. government, agencies, and instrumentalities obligations	45,598
Corporate bonds and notes	51,243
	\$ 118,157

Cash collateral received amounted to \$119 million and it was invested as follows: \$56 million in repurchase agreements, \$10 million in corporate bonds and notes, \$17 million in interest-bearing deposits, \$15 million in money market fund, and \$21 million in asset-backed securities.

In addition, SIFC had the following securities lending obligations collateralized by securities as of June 30, 2004 (expressed in thousands):

<b>Securities lent</b>	<b>Fair value of underlying securities</b>	<b>Securities collateral received</b>
U.S. government and agencies obligations	\$ 88,960	90,692

Securities lending transactions collateralized by securities that cannot be pledged or sold unless the borrower defaults are not reported as assets and liabilities in the accompanying balance sheets.

**AACA**

AACA lends securities to broker/dealers and other entities (borrowers) for collateral that will be returned in the future for the same securities. The custodial bank manages the securities lending program and receives cash, government securities, and letters of credit as collateral. The program provides for an initial minimum collateralization of 102% of the market value of the securities lent plus accrued income. Additional collateral has to be provided by the close of the next business day if its value falls to less than 100%. The contract with the custodial bank requires that should a collateral deficiency occur beyond the custodian's responsibilities, the deficiency should be allocated pro rata among all client lenders within the program.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Either the custodian bank or the borrower can terminate all security loans at any time. Cash collateral is invested in the program's agent short-term investment pools, which at fiscal year-end had a weighted average maturity of approximately 30 days. The relationship between securities of the investment pool and AACA loans cannot be determined.

The following represents the balances relating to the securities lending transactions as of June 30, 2004 (expressed in thousands):

<b>Securities lent</b>	<b>Fair value of underlying securities</b>	<b>Securities collateral received</b>
U.S. Treasury bills, bonds, and notes	\$ 15,889	14,839
Common stocks and preferred stocks	13,624	13,444
Corporate bonds	2,076	2,114
U.S. agencies	4,761	3,442
Totals	\$ 36,350	33,839

Securities lending transactions collateralized by securities that cannot be pledged or sold unless the borrower defaults do not have to be reported as assets and liabilities in the statement of net assets.

At year-end, AACA has no credit risk exposure to borrowers because the amounts AACA owes the borrowers exceed the amounts the borrowers owe AACA.

**(8) Investments in Limited Partnerships**

Pursuant to the Statement of Investment Guidelines for the Government of Puerto Rico, the pension trust funds and a component unit invested approximately \$12.7 million in limited partnerships during the fiscal year ended June 30, 2004. The investments were as follows:

- \$500,000 was invested in Guayacán Funds of Funds, L.P., a Delaware limited partnership, organized by Grupo Guayacán, Inc. as general partner, that has total commitments of \$56 million of which \$45 million are from pension trust funds and the remaining balance from the private corporate investors. This fund invests in United States and international private equity partnerships that in turn invest in private companies.
- \$5.2 million were invested in Guayacán Fund of Funds II, L.P., a Delaware limited partnership, organized by Grupo Guayacán as general partner, that has total commitments of \$62 million of which \$50 million are from the pension trust funds and the remaining balance from the private corporate investors in Puerto Rico. The fund invests in a broad range of United States and international private equity investment partnerships that, in turn, will make equity and equity-related investments primarily in private businesses.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

- There were no contributions made during fiscal year 2004 in Guayacán Private Equity Fund, L.P., a Delaware limited partnership, organized by Advent/Morro Partners as general partner, that has total commitments of \$42 million of which \$10 million are from the pension trust funds, \$20 million are from a component unit and the remaining balance from the private corporate investors in Puerto Rico. This fund invests in Puerto Rico private equity.
- \$460,000 was invested in Invesco Venture Partnership Fund III, L.P. a Delaware limited partnership, organized by IPC Partnership Associates III, LLC as General Partner in which the System has a total commitment of \$6 million. The Partnership was organized to invest in other collective investments funds investing in alternative assets, including primarily United States and international funds that focus on both early-and later-stage venture capital investments.
- \$1.4 million were invested in Invesco Non-U.S. Partnership Fund III, L.P. a Delaware limited partnership, organized by IPC Partnership Associates III, LLC as General Partner, in which the System has a total commitment of \$4.5 million. The Partnership was organized to invest in other collective investments funds investing in alternative assets, including primarily investments focusing on non-U.S. buyouts, expansion capital, turnaround, mezzanine, and distressed investment partnership.
- \$556,000 was invested in Invesco U.S. Buyout & Expansion Capital Partnership Fund III, L.P., a Delaware limited partnership, organized by IPC Partnership Associates III, LLC as General Partner in which the System has a total commitment of \$4.5 million. The Partnership was organized to invest in other collective funds investing in alternative assets, including primarily investments focusing on small, mid-size and large domestic buyout transactions.
- \$4.6 million was invested in Chase Capital Partners Private Equity Fund of Funds II, LTD, a limited partnership, organized by Chase as General Partner in which the System has a total commitment of \$35 million. The Fund's investment strategy is to capitalize on a globally diversified portfolio of private equity investments opportunities across various sectors, including buyouts, growth equity, venture capital and other special situations through partnership, investments, and direct investments.

The carrying value of these investments at June 30, 2004 amounted to \$86.3 million and is presented within investments in the statement of net assets. The allocations of net gain and net loss to the limited partners are based on certain percentages, as established in the limited partnership agreements.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

As of June 30, 2004, the pension trust funds and a discretely presented component unit had capital commitments and contributions as follows (expressed in thousands):

<u>Guayacán Funds of Funds, L.P.</u>	<u>Public sector commitments</u>	<u>Fiscal year contributions</u>	<u>Cumulative contributions</u>
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	\$ 25,000	500	23,279
Puerto Rico System of Annuities and Pensions for Teachers	20,000	—	18,623
Subtotal	<u>45,000</u>	<u>500</u>	<u>41,902</u>
<b>Guayacán Fund of Funds II, L.P.</b>			
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	25,000	2,460	17,664
Puerto Rico System of Annuities and Pensions for Teachers	25,000	2,710	17,664
Subtotal	<u>50,000</u>	<u>5,170</u>	<u>35,328</u>
<b>Guayacán Private Equity Fund, L.P.</b>			
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	5,000	—	3,930
Puerto Rico System of Annuities and Pensions for Teachers	5,000	—	3,930
Component unit – GDB	20,000	—	15,718
Subtotal	<u>30,000</u>	<u>—</u>	<u>23,578</u>
<b>Other Funds</b>			
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	20,000	2,889	12,429
Puerto Rico System of Annuities and Pensions for Teachers	30,000	4,153	18,219
Subtotal	<u>50,000</u>	<u>7,042</u>	<u>30,648</u>
Total	<u>\$ 175,000</u>	<u>12,712</u>	<u>131,456</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

**(9) Receivables and Payables**

Receivables in the general fund include approximately \$1 billion of accrued income and excise taxes and \$254 million receivable from the federal government. In addition, the enterprise funds include \$50 million of unemployment, disability, and drivers' insurance premium receivable.

Payables in the general fund include approximately \$1.1 billion of trade accounts due to suppliers for purchase of merchandise and services rendered and \$221 million of tax refunds liability.

**(10) Interfund and Intraentity Transactions**

Interfund receivables and payables at June 30, 2004 are summarized as follows (expressed in thousands):

Due from/to other funds:

Receivable fund	Payable fund	Amount
General fund	Enterprise fund – lotteries	\$ 55,572
General fund	Enterprise fund – unemployment insurance	14,677
Nonmajor governmental funds	General fund	75,429
PBA capital project fund	General fund	25,757
Enterprise fund-lotteries	General fund	51,235
		\$ 222,670

Transfers from/to other funds:

Transferee fund	Transferor fund	Amount
Nonmajor governmental funds	General fund	\$ 241,830
Debt service fund	General fund	342,538
General fund	Nonmajor governmental funds	97,399
General fund	Enterprise fund – lotteries	158,106
Nonmajor enterprise funds	General fund	2,960
General fund	Enterprise fund – unemployment insurance	48,112
Nonmajor governmental funds	PBA – capital project fund	38,849
General fund	The Children's Trust - special revenue fund	63,075
The Children's Trust special revenue fund	Nonmajor governmental funds	398
		\$ 993,267

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The principal purposes of the interfund transfers are to:

- Distribute the increase in net assets of the lotteries fund for the use of the general fund, as required by the lotteries enabling legislation.
- Make funds available for debt service payments in both the debt service fund and the general fund.
- Unemployment insurance trust fund's distribution of surplus cash belonging to the general fund for the payment of administrative expenses.
- Recognize as transfers the rental payments made by the Commonwealth's agencies on properties leased by the nonmajor funds of the PBA, a blended component unit of the Commonwealth.

Interfund receivables and payables represent the pending settlements of the aforementioned transfers.

Due from/to primary government and component units are as follows (expressed in thousands):

<u>Receivable entity/fund</u>	<u>Amount</u>	<u>Payable entity/fund</u>	<u>Amount</u>
Business-type activities		Puerto Rico Aqueduct and Sewer Authority	
	\$ 152,550		\$ 152,550
		Cardiovascular Center Corporation of Puerto Rico and the Caribbean	32,613
		State Insurance Fund Corporation	30,000
		Government Development Bank for Puerto Rico	8,397
		Tourism Company of Puerto Rico	7,917
		Employment and Training Enterprises Corporation	7,108
		Caribbean Basin Projects Financing Authority	5,082
Governmental activities	95,747	Governing Board of the 9-1-1 Service	4,630
	<u>\$ 248,297</u>		<u>\$ 248,297</u>
Puerto Rico Electric Power Authority	\$ 55,735	Governmental activities	\$ 117,145
University of Puerto Rico	23,470		
Special Communities Perpetual Trust	20,000		
Government Development Bank of Puerto Rico	16,162		
Puerto Rico Maritime Transportation Authority	1,778		
	<u>\$ 117,145</u>		<u>\$ 117,145</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The amount owed by PRASA of \$153 million represents construction loans granted by the Puerto Rico Water Pollution Control Revolving Fund, a nonmajor enterprise fund, to finance the construction of capital assets for PRASA.

The amount receivable by PREPA from the primary government includes approximately \$32 million representing an agreement with the Commonwealth by which the Commonwealth will pay the outstanding fuel adjustment subsidy receivable, which amounted originally to \$94 million, and an approximately \$24 million refinancing of other accumulated debt of the Commonwealth. This amount owed by the Commonwealth is presented within notes payable in the statement of net assets of the governmental activities.

The amount receivable by the UPR from the primary government includes a resolution approved by the Legislature of the Commonwealth to pay \$48.4 million to the UPR on behalf of the Department of Health of the Commonwealth over eight years. The related outstanding balance of \$23.5 million is presented by the Commonwealth within notes payable in the statement of net assets of the governmental activities.

Due from/to component units are as follows (expressed in thousands):

<b>Receivable entity</b>	<b>Amount</b>	<b>Payable entity</b>	<b>Amount</b>
University of Puerto Rico	\$ 12,955	Puerto Rico Medical Services Administration	\$ 27,044
Puerto Rico Electric Power Authority	14,089		
Economic Development Bank for Puerto Rico	9,178	Puerto Rico Trade and Export Company	9,178
Puerto Rico Ports Authority	23,645	Puerto Rico Maritime Transportation Authority	23,645
Farm Insurance Corporation of Puerto Rico	6,462	Agricultural Services and Development Administration	36,033
Puerto Rico Land Authority	29,571		
State Insurance Fund Corporation	3,500	Puerto Rico Solid Waste Authority	3,500
Balance carried forward	\$ 99,400		\$ 99,440

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

<u>Receivable entity</u>	<u>Amount</u>	<u>Payable entity</u>	<u>Amount</u>
Balance brought forward	\$ 99,400		\$ 99,400
Government Development Bank for Puerto Rico	1,016,844	Puerto Rico Ports Authority	250,493
		Puerto Rico Convention Center District Authority	205,473
		Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	140,911
		Special Communities Perpetual Trust	90,918
		Puerto Rico Aqueduct and Sewer Authority	64,546
		Puerto Rico Electric and Power Authority	61,452
		Puerto Rico Solid Waste Authority	60,818
		Puerto Rico Land Authority	40,617
		University of Puerto Rico	33,182
		Puerto Rico Metropolitan Bus Authority	26,334
		Agricultural Services and Development Administration	24,703
		Economic Development Bank for Puerto Rico	12,815
		Puerto Rico Infrastructure Financing Authority	8,647
		Employment and Training Enterprises Corporation	1,414
		Puerto Rico Industrial Development Company	<u>56</u>
			<u>1,022,379</u>
	<u>\$ 1,116,244</u>		<u>\$ 1,121,779</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The immaterial difference between due from/to component units resulted from the time lag between the dates that transactions are recorded by each discretely presented component unit and other reconciling items.

The balances due to GDB amounting to approximately \$1 billion represent loans payable to GDB at June 30, 2004.

The rest of the loans receivable reported by GDB consists of the following (expressed in thousands):

Primary government:		
Governmental activities	\$	1,754,945
Business-type activities		1,028
Pension trust funds		240
		<u>1,756,213</u>
Other governmental entities and municipalities		888,037
Private sector (net of \$27,444 presented within restricted assets)		<u>495,127</u>
Total loans receivable	\$	<u><u>3,139,377</u></u>

The loans to the primary government are presented by the Commonwealth within notes payable in the statement of net assets and in the statement of fiduciary net assets. A difference of \$1.8 million resulted from the time lag between the dates that transactions are recorded by GDB and the primary government.

Expenses of the primary government include approximately \$2.7 billion in capital and operational contributions to the component units, comprised as follows (expressed in thousands):

Puerto Rico Health Insurance Administration	\$	969,804
University of Puerto Rico		745,875
Puerto Rico Aqueduct and Sewer Authority		266,575
Government Development Bank of Puerto Rico		112,721
Puerto Rico Infrastructure Finance Authority		80,258
Nonmajor component units		<u>521,948</u>
Total contributions made by primary government to component units	\$	<u><u>2,697,181</u></u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

**(11) Restricted Assets**

Restricted assets of the primary government included in the basic financial statements at June 30, 2004 consist of cash, investments, and other assets to be used for the following purposes (expressed in thousands):

Primary government:		
Construction fund	\$	1,057,275
Debt service and sinking fund requirements		963,969
Payment of lottery prizes		215,213
Emergency fund		100,000
Assets held in trust for repayment of Qualified Zone Academic Bonds		62,224
Administrative costs for unemployment insurance		42,013
Other restricted assets of the Public Housing Administration		31,486
Residual receipts from sale of properties		22,618
Construction of governmental agencies		15,440
Other		<u>5,590</u>
Total for primary government	\$	<u><u>2,515,828</u></u>

Liabilities of the primary government payable from restricted assets consist of the following (expressed in thousands):

Governmental activities:		
Tax revenue anticipation notes payable	\$	800,000
Bonds payable		758,767
Qualified Zone Academic Bonds		47,936
Deferred revenue		42,013
Interest payable		<u>15,820</u>
Liabilities payable from restricted assets – governmental activities	\$	<u><u>1,664,536</u></u>
Business-type activities:		
Lottery prizes payable within one year	\$	20,475
Lottery prizes payable after one year		<u>194,738</u>
Liabilities payable from restricted assets – business-type activities	\$	<u><u>215,213</u></u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Restricted assets of the component units included in the basic financial statements at June 30, 2004 are to be used for the following purposes (expressed in thousands):

Component units:	
Debt service and sinking fund requirements	\$ 5,191,692
Financial assistance programs	500,715
Construction and betterments funds	272,921
Self-insurance fund	80,770
Maintenance reserve fund	59,684
Industrial incentives	46,202
Escrow	41,931
Contingency reserve	22,140
Development of infrastructure projects	15,941
Severance payment	4,036
Renewal and replacement fund	3,399
General reserve fund	3,065
Other uses	<u>73,857</u>
Total for components units	\$ <u>6,316,353</u>

**(12) Capital Assets**

Capital assets activity for the year ended June 30, 2004 is as follows (expressed in thousands):

***Primary Government***

	<b>Beginning balance (as restated)</b>	<b>Increases</b>	<b>Decreases</b>	<b>Ending balance</b>
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 894,320	17,456	31,266	880,510
Construction in progress	<u>910,210</u>	<u>424,758</u>	<u>453,486</u>	<u>881,482</u>
Total capital assets, not being depreciated	<u>1,804,530</u>	<u>442,214</u>	<u>484,752</u>	<u>1,761,992</u>
Capital assets, being depreciated:				
Buildings and building improvements	5,617,043	521,689	19,956	6,118,776
Equipment	<u>324,211</u>	<u>40,278</u>	<u>8,373</u>	<u>356,116</u>
Total capital assets, being depreciated	\$ <u>5,941,254</u>	<u>561,967</u>	<u>28,329</u>	<u>6,474,892</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

	<b>Beginning balance (as restated)</b>	<b>Increases</b>	<b>Decreases</b>	<b>Ending balance</b>
Less accumulated depreciation for:				
Buildings and building improvements	\$ 1,791,778	158,325	3,761	1,946,342
Equipment	<u>167,315</u>	<u>30,257</u>	<u>6,159</u>	<u>191,413</u>
Total accumulated depreciation	<u>1,959,093</u>	<u>188,582</u>	<u>9,920</u>	<u>2,137,755</u>
Total capital assets, being depreciated, net	<u>3,982,161</u>	<u>373,385</u>	<u>18,409</u>	<u>4,337,137</u>
Governmental activities capital assets, net	\$ <u>5,786,691</u>	<u>815,599</u>	<u>503,161</u>	<u>6,099,129</u>
Business-type activities:				
Total capital assets, being depreciated – equipment	\$ 4,819	167	—	4,986
Less accumulated depreciation of equipment	<u>2,924</u>	<u>390</u>	<u>—</u>	<u>3,314</u>
Total business-type activities capital assets, being depreciated, net	\$ <u>1,895</u>	<u>(223)</u>	<u>—</u>	<u>1,672</u>

Depreciation expense was charged to functions/programs of the primary government for the year ended June 30, 2004 as follows (expressed in thousands):

Governmental activities:	
General government	\$ 55,492
Public safety	21,225
Health	4,378
Public housing and welfare	79,946
Education	24,277
Economic development	<u>3,264</u>
Total depreciation expense – governmental activities	\$ <u>188,582</u>
Total depreciation business-type activities – lotteries	\$ <u>390</u>

The capital assets of the primary government were decreased as of the beginning of the year by approximately \$54 million to correct an overstatement in the balance of construction in progress erroneously capitalized in prior years by the Puerto Rico Public Housing Administration, a Commonwealth agency reported within the general fund (see note 4).

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

On August 17, 2001, the Legislature of the Commonwealth approved Act 120, which requires the conditional transfer of the ownership of certain real properties under the name of the Department of Recreation and Sports (DRS) of the Commonwealth to the municipalities of Commonwealth. The property consisted of certain recreational and sport facilities located throughout Puerto Rico. The land and the facilities were transferred at no cost to the municipalities. During fiscal year ended June 30, 2004, land, buildings, and building improvements with a cost of \$35.6 million were transferred to several municipalities and recorded as a special item in the accompanying statement of activities for the year ended June 30, 2004 to give effect to these transactions.

***Discretely Presented Component Units***

	<b>Beginning balance (as restated)</b>	<b>Increases</b>	<b>Decreases</b>	<b>Ending balance</b>
Capital assets, not being depreciated:				
Land	\$ 2,337,969	103,544	21,193	2,420,320
Art works	2,475	—	—	2,475
Construction in progress	8,711,463	2,064,709	1,043,956	9,732,216
Total capital assets, not being depreciated	<u>\$ 11,051,907</u>	<u>2,168,253</u>	<u>1,065,149</u>	<u>12,155,011</u>
Capital assets, being depreciated:				
Buildings and building improvements	\$ 7,374,231	1,466,019	898,487	7,941,763
Equipment	980,569	132,129	44,277	1,068,421
Infrastructure	17,945,401	517,265	326,663	18,136,003
Total capital assets, being depreciated	<u>26,300,201</u>	<u>2,115,413</u>	<u>1,269,427</u>	<u>27,146,187</u>
Less accumulated depreciation for:				
Buildings and building improvements	4,145,472	347,244	80,263	4,412,453
Equipment	561,360	73,349	14,750	619,959
Infrastructure	7,314,919	396,469	8,921	7,702,467
Total accumulated depreciation	<u>\$ 12,021,751</u>	<u>817,062</u>	<u>103,934</u>	<u>12,734,879</u>
Total capital assets, being depreciated, net	<u>\$ 14,278,450</u>	<u>1,298,351</u>	<u>1,165,493</u>	<u>14,411,308</u>
Capital assets, net	<u>\$ 25,330,357</u>	<u>3,466,604</u>	<u>2,230,642</u>	<u>26,566,319</u>

The capital assets of the discretely presented component units were changed as of the beginning of the year primarily as a result of the inclusion of a component unit from the UPR in the current year (see note 4).

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

**(13) Tax Revenue Anticipation Notes Payable**

Tax revenue anticipation notes (TRANS) reported in the general fund were issued on October 3, 2003, at an interest rate ranging from 2% to 3.5% and were paid on July 30, 2004. The TRANS amounted to \$800 million at June 30, 2004 plus accrued interest of approximately \$16 million. The proceeds of the TRANS were used to cover a temporary cash deficiency resulting from the timing differences between tax collections and the payments of current expenditures.

**(14) Short-and Long-Term Obligations**

*Primary Government*

*(a) Summary of Short-and Long-Term Obligations*

Short-and long-term obligations at June 30, 2004 and changes for the fiscal year then ended are as follows (expressed in thousands):

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

	Balance at June 30, 2003 (as restated)	Debt/ refunding debt issued	Capitalized interest	Debt paid or defeased	Notes payable refunded	Net original issue (discounts) premiums	Other net increases (decreases)	Balance at June 30, 2004	Due within one year
Governmental activities:									
Bonds payable	\$ 9,573,772	3,603,330	70,904	(1,469,165)	—	65,388	(72,629)	11,771,600	214,175
Commonwealth appropriation bonds	2,797,431	888,203	—	(59,408)	(755,734)	32,530	(144,956)	2,758,066	53,442
Qualified Zone Academy Bonds	—	47,936	—	—	—	—	—	47,936	—
Notes payable:									
Component units:									
GDB	701,604	5,513,343	—	(4,458,131)	—	—	—	1,756,816	783,887
Other	62,637	24,138	—	(7,570)	—	—	—	79,205	13,897
Compensated absences	1,150,441	—	—	(857,285)	—	—	1,093,717	1,386,873	915,449
Net pension obligation	3,801,813	—	—	—	—	—	375,574	4,177,387	—
Obligation under capital leases	162,971	2,300	—	(12,057)	—	—	—	153,214	6,866
Other liabilities:									
Employees' Christmas bonus	101,623	—	—	(184,190)	—	—	185,387	102,820	102,820
Liability for federal cost	—	—	—	—	—	—	—	—	—
Disallowances	52,089	—	—	(876)	—	—	48,019	99,232	99,232
Liability for legal claims and	—	—	—	—	—	—	—	—	—
judgments	68,702	—	—	(42,791)	—	—	193,272	219,183	162,791
Other	2,582	—	—	(2,582)	—	—	—	—	—
Total governmental activities	18,475,665	10,079,250	70,904	(7,094,055)	(755,734)	97,918	1,678,384	22,552,332	2,352,559
Business-type activities:									
Debts payable to component units	1,308	326	—	(606)	—	—	—	1,028	—
Notes payable to third parties	1,077	—	—	(929)	—	—	—	148	148
Compensated absences	3,709	—	—	(2,388)	—	—	3,651	4,972	2,890
Obligation for unpaid lottery prizes	274,776	—	—	(46,911)	—	—	90,606	318,471	37,071
Liability for insurance benefits, including IBNR	180,069	—	—	(256,692)	—	—	147,731	71,108	71,108
Other	351	—	—	(351)	—	—	—	—	—
Total business-type activities	461,290	326	—	(307,877)	—	—	241,988	395,727	111,217
Total governmental and business-type	\$ 18,936,955	10,079,576	70,904	(7,401,932)	(755,734)	97,918	1,920,372	22,948,059	2,463,776

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The beginning balance of bonds and notes payable to third parties (all payable to HUD) by the Puerto Rico Public Housing Administration and reported in the governmental activities, was decreased by approximately \$81.6 million and \$1 billion, respectively, to eliminate such balances, erroneously reported as a liability. HUD had requested that this debt be eliminated prior to July 1, 2003 (see note 4).

The other net increases in bonds and notes payable consist of deferred losses on refunding, net of amortization, and amortization of premiums on bonds. These adjustments did not require any source or use of cash.

Compensated absences, net pension obligation, obligation for unpaid lottery awards, liability for insurance benefits, and other long-term liabilities reflect other net increases (decreases) resulting from adjustments and changes to agree these obligations to their estimated balances at June 30, 2004.

### **(b) Debt Limitation**

The Constitution of the Commonwealth authorizes the contracting of debts as determined by the Legislature. Nevertheless, the Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth are not to be issued if the amounts of the principal of, and interest on, such bonds and notes and on all such bonds and notes issued thereafter which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenue raised under the provisions of Commonwealth legislation and conveyed into the Treasury (hereinafter internal revenue) in the two fiscal years preceding the then current fiscal year. Section 2, Article VI of the Constitution does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded. Internal revenue consists principally of income taxes and excise taxes. Certain revenue, such as federal excise taxes on offshore shipments of alcoholic beverages, tobacco products, and customs duties, which are collected by the U.S. government and returned to the Commonwealth, and motor vehicle fuel taxes and license fees, which are allocated to the PRHTA, a discrete component unit, are not included as revenue for the purpose of calculating the debt limit, although they may be available for the payment of debt service. At June 30, 2004, the Commonwealth is in compliance with the debt limitation requirement.

### **(c) Bonds Payable**

The Constitution of the Commonwealth provides that public debt will constitute a first claim on the available revenue of the Commonwealth. Public debt includes general obligations and notes of the Commonwealth and any payment required to be made by the Commonwealth under its guarantees of bonds issued by blended or discretely presented component units. The good faith, credit, and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal and interest of the general obligation bonds.

Act No. 83 of August 30, 1991, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. The levy is made by CRIM, a municipal corporation, not a component unit of the Commonwealth. CRIM is

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

required to remit the 1.03% of property tax collected to the Commonwealth to be used by the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth. During the year ended June 30, 2004, the total revenue and receivable reported by the Commonwealth amounted to approximately \$118 million and \$16 million, respectively, which are included in the debt service fund.

For financial reporting purposes, the outstanding amount of bonds represents the total principal to be repaid, net of unamortized premiums, discount, and deferred refunding losses; for capital appreciation bonds, it represents total principal and accreted interest to be repaid.

Bonds payable outstanding at June 30, 2004 are as follows (expressed in thousands):

	<b>General obligation</b>	<b>Revenue bonds</b>	<b>Total</b>
Term bonds payable through 2036; interest payable semiannually at rates varying from 3% to 8%.	\$ 2,547,640	1,588,655	4,136,295
Serial bonds payable through 2024; interest payable semiannually at rates varying from 3.75% to 7.5%.	4,002,450	1,149,245	5,151,695
Capital appreciation bonds payable through 2031; no interest rate, yield ranging from 4.42% to 7.8%. Net of accreted discount of \$190 million.	313,332	178,232	491,564
The Children's Trust Fund tobacco settlement asset-backed bonds payable through 2026; interest payable annually at rates varying from 4.625% to 6%.	—	1,145,515	1,145,515
Capital Fund Program Bonds, maturing in various dates payable through 2024; interest payable at rates varying from 2% to 5%.	—	663,060	663,060
Appropriation refunding bonds for low-income housing payable through 2005; interest payable at rates varying from 6.9% to 8%.	10,115	—	10,115
Bond payment obligation payable through 2008; interest payable at rates varying from 3.5% to 5.5%.	33,450	—	33,450
Balance carried forward	\$ 6,906,987	4,724,707	11,631,694

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

	<b>General obligation</b>	<b>Revenue bonds</b>	<b>Total</b>
Balance brought forward	\$ 6,906,987	4,724,707	11,631,694
Bond payment obligation payable through 2009; interest payable at rates varying from 3.5% to 5.5%.	44,240	—	44,240
Bond payment obligation payable through 2010; interest payable at rates varying from 1.5% to 5.5%.	48,220	—	48,220
Yield curve bonds payable from 2009 through 2011; no interest rate, yield of 8.914%.	15,000	—	15,000
Yield retail bonds payable from 2009 through 2011; interest payable at rates varying from 2.875% to 5%.	26,000	—	26,000
Tax-exempt components maturing through 2007 and 2008; interest payable at rates ranging from 5.5% to 5.6%.	—	72,160	72,160
Inverse rate bonds payable from 2009 through 2011, interest payable at a rate of 6%.	15,000	—	15,000
Total	7,055,447	4,796,867	11,852,314
Unamortized premium (discount)	239,033	30,818	269,851
Deferred charges arising from debt refunding	(187,807)	(162,989)	(350,796)
Savings bonds	231	—	231
Total bonds payable	\$ 7,106,904	4,664,696	11,771,600

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

During the year ended June 30, 2004, the following changes occurred in the bonds payable (expressed in thousands):

	<u>Outstanding at June 30, 2003 (as restated)</u>	<u>Issued</u>	<u>Premiums/ discount (redemptions)</u>	<u>Outstanding at June 30, 2004</u>
Term bonds	\$ 3,460,105	1,875,265	(1,199,075)	4,136,295
Serial bonds	4,330,990	1,039,005	(218,300)	5,151,695
Capital appreciation bonds	436,065	—	55,499	491,564
The Children's Trust Fund tobacco settlement asset-backed bonds	1,157,240	—	(11,725)	1,145,515
New housing authority bonds	—	663,060	—	663,060
Appropriation refunding bonds	34,775	—	(24,660)	10,115
Bond payment obligations	125,910	—	—	125,910
Yield curve bonds	15,000	—	—	15,000
Yield retail bonds	—	26,000	—	26,000
Tax-exempt components	72,160	—	—	72,160
Inverse rate bonds	15,000	—	—	15,000
Subtotal	9,647,245	3,603,330	(1,398,261)	11,852,314
Unamortized premium	200,173	65,388	4,290	269,851
Deferred charges arising from debt refunding	(273,877)	(118,888)	41,969	(350,796)
Savings bonds	231	—	—	231
Total	<u>\$ 9,573,772</u>	<u>3,549,830</u>	<u>(1,352,002)</u>	<u>11,771,600</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Maturities of general obligations and of revenue bonds payable, including accrued interest of capital appreciation bonds, are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 214,175	511,551	725,726
2006	183,413	576,248	759,661
2007	244,234	599,517	843,751
2008	259,459	592,819	852,278
2009	306,366	546,958	853,324
2010-2014	1,908,334	2,362,134	4,270,468
2015-2019	2,489,939	1,968,172	4,458,111
2020-2024	2,023,496	1,210,749	3,234,245
2025-2029	1,564,005	824,823	2,388,828
2030-2034	1,521,759	473,084	1,994,843
2035-2039	704,535	161,572	866,107
2040-2044	181,850	43,064	224,914
Total	11,601,565	\$ 9,870,691	<u>21,472,256</u>
Plus: accreted discount	250,980		
Plus: unamortized premium	269,851		
Less: deferred charges arising from debt refunding	<u>(350,796)</u>		
Total	\$ <u>11,771,600</u>		

**(d) Commonwealth Appropriation Bonds**

Over the years, GDB, as fiscal agent and bank for the Commonwealth, had extended lines of credit, advances, and loans to several agencies and component units in order to finance their capital improvement projects and to cover their operational deficits at the time. At different points in time, these loans were refunded through the issuance of Commonwealth appropriation bonds issued by the Puerto Rico Public Finance Corporation (PFC), a blended component unit of GDB. PFC is the financing arm of GDB, which serves only as a conduit for the issuance of the bonds.

During June 2004, PFC advance refunded through the PFC 2004 Series A and B and PFC 2003 Series A through C Refunding Commonwealth Appropriation Bonds, a portion of certain of its outstanding Commonwealth Appropriation Bonds issued on prior years (except for the Health Facilities and Services Administration bonds described below, where no portion was refunded). The Commonwealth recognizes a mirror effect of this advance refunding by PFC in its own debt in proportion to the portion of the Commonwealth's notes included in the PFC refunding. As a result, the Commonwealth considered defeased and therefore removed from the balance sheet the portion refunded of \$775.7 million. Refunding proceeds and bond issue costs of \$888.2 million and \$21.9 million, respectively, were allocated to the Commonwealth and a resulting refunding loss of

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

approximately \$145 million was recognized and capitalized within the new refunding debt and deferred through the notes' terms. The repayment source for these bonds (both the refunding and unrefunded portions) consists of Commonwealth appropriations submitted for approval of the Legislature annually during the budget preparation process of the Commonwealth. The Legislature is not legally bound to appropriate funds for such repayments.

The outstanding balance of the Commonwealth appropriation bonds (both the refunding and unrefunded portion combined) is comprised of the following obligations (expressed in thousands):

Act No. 164 Restructuring	\$ 1,510,695
Health Facilities and Services Administration	514,851
Office for the Improvement of Public Schools	336,955
Puerto Rico Maritime Shipping Authority	273,991
Property tax settlement	<u>121,574</u>
Total Commonwealth appropriation bonds	\$ <u>2,758,066</u>

On December 17, 2001, Act No. 164 was approved, which authorized certain government agencies and discretely presented component units to refund approximately \$2.4 billion of their outstanding obligations with GDB, for which no repayment source existed, over a period not exceeding 30 years, and to be repaid with annual Commonwealth appropriations not to exceed \$225 million. This refunding was done with Commonwealth appropriation bonds through several series issued by PFC during the period between December 2001 and June 2002.

Approximately \$1.5 billion of the aforementioned outstanding obligations belonged to the primary government, predominantly the Department of Health of the Commonwealth (health reform financing and other costs for approximately \$1.1 billion) and the Department of the Treasury of the Commonwealth (the fiscal year 2001 deficit financing of \$268 million and the obligation assumed for defective tax liens in the amount of approximately \$132 million). The new bonds' balance of the Act No. 164 restructurings bears interest at rates ranging from 1.25% to 5.80%. The new combined bonds balance of the Act No. 164 restructuring bears interest at rates ranging from 1.25% to 5.80%. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 8,342	60,661	69,003
2006	21,425	84,838	106,263
2007	23,355	83,725	107,080
2008	35,076	81,944	117,020
2009	37,031	79,997	117,028
2010-2014	198,176	376,241	574,417
2015-2019	<u>274,270</u>	<u>301,689</u>	<u>575,959</u>
Balance carried forward	\$ <u>597,675</u>	<u>1,069,095</u>	<u>1,666,770</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Balance brought forward	\$ 597,675	1,069,095	1,666,770
2020-2024	384,529	187,455	571,984
2025-2029	360,745	80,438	441,183
2030-2034	<u>187,937</u>	<u>7,262</u>	<u>195,198</u>
Total	1,530,886	<u>\$ 1,344,250</u>	<u>2,875,135</u>
Plus: unamortized premium	26,054		
Less: deferred charges arising from debt refunding	<u>(46,245)</u>		
Total	<u>\$ 1,510,695</u>		

As of July 1, 1999, approximately \$595 million (including unpaid interest) of a promissory note of the Health Facilities and Services Administration (HFSA) due to GDB was transferred to the Department of Health of the Commonwealth and restructured through Commonwealth appropriation bonds. The bonds bear interest at rates ranging between 5.90% to 6.20%. Principal and interest on the bonds are payable solely from legislative appropriations to be made pursuant to Act No. 223 of August 9, 1998. The act provides that OMB shall include in the annual budget of the Commonwealth an amount equal to \$56.5 million for the fiscal year 1998-99, and for the next succeeding 15 fiscal years the amount necessary to pay the principal of and interest on the bonds, up to a maximum annual amount of \$57.7 million. As of June 30, 2004, approximately \$515 million were still outstanding.

Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 32,530	25,203	57,733
2006	34,540	23,191	57,731
2007	37,080	20,652	57,732
2008	39,600	18,133	57,733
2009	42,125	15,607	57,732
2010-2014	181,775	105,931	287,706
2015-2019	<u>147,201</u>	<u>81,571</u>	<u>228,772</u>
Total	<u>\$ 514,851</u>	<u>290,288</u>	<u>805,139</u>

Previous public schools infrastructure improvement loans provided additional funds for major repairs and improvements to the public schools in Puerto Rico. This activity is administered by the Office for the Improvement of the Public Schools of Puerto Rico (OIPS), included as part of the general fund of the primary government. These loans were refunded originally through the issuance of

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Commonwealth appropriation bonds pursuant to Act No. 85 of June 13, 1998 (Act 85). The new combined bonds bear interest at rates ranging from 5.0% to 5.85%. As of June 30, 2004, approximately \$336.7 million were outstanding. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ —	3,015	3,015
2006	9,090	18,503	27,593
2007	9,470	18,121	27,591
2008	9,945	17,647	27,592
2009	10,465	17,125	27,590
2010-2014	67,275	73,936	141,211
2015-2019	79,475	50,654	130,129
2020-2024	96,015	28,308	124,323
2025-2026	63,510	3,568	67,078
Total	345,245	\$ 230,877	576,122
Plus: unamortized premium	7,172		
Less: deferred charges arising from debt refunding	(15,462)		
Total	\$ 336,955		

A promissory note payable owed by PRMSA to GDB was assumed by the Commonwealth in connection with the sale of the maritime operations of PRMSA. Commonwealth appropriation bonds were issued to refund this liability. The new combined bonds balance bears interest at a variable rate ranging from 3.00% to 7.30%. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 155	4,091	4,246
2006	—	16,907	16,907
2007	—	16,907	16,907
2008	—	16,907	16,907
2009	—	16,907	16,907
2010-2014	45,390	79,980	125,370
2015-2019	73,905	64,297	138,202
2020-2024	94,415	42,411	136,826
2025-2029	106,205	14,587	120,792
2030	8,580	42	8,622
Total, balance carried forward	\$ 328,650	273,036	601,686

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

<b>Year ending June 30,</b>	<b>Principal</b>
Balance brought forward	\$ 328,650
Plus: Unamortized Discount	(696)
Less: deferred charges arising from debt refunding	(53,963)
Total	\$ 273,991

During fiscal year 1996, the Commonwealth refinanced the liability for the settlement of the property taxes owed to the municipalities of Puerto Rico. Commonwealth appropriation bonds were issued to refund this liability. The new combined bonds balance bears interest at rates ranging from 5.87% to 7.25%. Debt service requirements in future years are as follows (expressed in thousands):

<b>Year ending June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2005	\$ 12,415	5,991	18,406
2006	13,310	5,083	18,393
2007	14,285	4,103	18,388
2008	15,350	3,040	18,390
2009	16,505	1,885	18,390
2010-2014	68,216	23,747	91,963
2015-2016	10,779	7,631	18,410
Total	150,860	\$ 51,480	202,340
Less: deferred charges arising from debt refunding	(29,286)		
Total	\$ 121,574		

**(e) Qualified Zone Academy Bonds**

During November 2001, the Department of Education of the Commonwealth issued a certification whereby certain Commonwealth public schools were designated as a “qualified zone academy” pursuant to Section 1397E of the U.S. Internal Revenue Code of 1986, as amended. On May 18, 2004, PFC, a blended component unit of GDB, issued \$47.9 million of Qualified Zone Academic Bonds (QZAB) to finance expenditures of the Department of Education of the Commonwealth under the aforementioned program, including rehabilitation and repairs of school buildings and other facilities, the development and implementation of academic curricula, technology training for some schools, and the costs of issuance of the bonds. These May 2004 QZAB are payable upon its maturity on May 2020, since the U.S. government grants tax exemptions to bond holders in lieu of an interest rate. Beginning in August 2004, annual appropriations from the general fund on the

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

amount of approximately \$2.2 million will be made over the next 16 years and deposited in an escrow account, which along with accumulated earned interest will be sufficient to repay these bonds upon its maturity on 2020.

**(f) Notes Payable to Third Parties**

The outstanding balance of notes payable by the Commonwealth to third parties is comprised of notes payable to a computer vendor within the business-type activity in the amount of \$148,000.

The notes payable are represented by an installment sales contract agreement entered into with the Lottery of Puerto Rico for the purchase of certain computer equipment. The sales contract agreement is payable in monthly installments of \$74,000, including interest at the rate of 5.62%, through July 2004.

**(g) Notes Payable to Component Units**

The Commonwealth financed certain short- and long-term liabilities through GDB and other component units. The outstanding balance on the financing provided by GDB at June 30, 2004 is comprised of the following (expressed in thousands):

**Government activities:**

Department of the Treasury	\$ 1,525,958
Department of Agriculture	46,532
Puerto Rico Court Administration Office	42,817
Department of Justice	32,402
Department of Health	30,000
Department of Natural and Environmental Resources	18,328
Office of the Superintendent of the Capitol	17,943
Department of Recreation and Sports	15,938
Department of Transportation and Public Works	10,272
Department of Education	8,466
State Office for the Historic Conservation	4,500
Correction Administration	<u>3,660</u>
Total debt due to GDB	\$ <u>1,756,816</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The remaining outstanding balance on the financing provided by other component units at June 30, 2004 is comprised of the following (expressed in thousands):

Health facilities agreement payable to the Medical Science Campus of the UPR	\$ 23,470
Note payable to PREPA	<u>55,735</u>
Total debt due to other component units	<u>\$ 79,205</u>
<b><i>Business-type activities:</i></b>	
Line-of-credit agreement with GDB for the Traditional Lottery – business-type activities	<u>\$ 1,028</u>

The Department of Treasury of the Commonwealth has entered into an interim line-of-credit agreement with GDB, from which approximately \$3.9 billion were drawn and repaid within the same year. These drawings and repayments related to advances in anticipation of the issuance of the 2004 TRANS and to cover temporary cash deficiencies between tax collection and payments of current expenditures, which were later repaid upon the actual tax collection and replenishment of the aforementioned deficiency.

During fiscal year 2003, the PBA capital project fund had entered into an interim construction line of credit with GDB, which outstanding balance at June 30, 2003 amounted to \$85 million. During fiscal year 2004, an additional \$311 million was drawn under this line of credit but all advances were repaid prior to the end of the fiscal year.

The Department of the Treasury of the Commonwealth has entered into various line-of-credit agreements with GDB amounting to approximately \$1.5 billion at June 30, 2004, for different purposes as presented in the following table. The borrowings under these line-of-credit agreements bear interest predominantly at variable interest rates, payable annually until the maturity of such lines, which ranges from June 30, 2005 to June 30, 2019. The purpose, interest rate, maturity date,

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

and amount outstanding under each individual agreement at June 30, 2004 consist of the following (expressed in thousands):

<u>Purpose</u>	<u>Interest rate</u>	<u>Maturity</u>	<u>Line of credit</u>	<u>Outstanding balance</u>
Resources to meet appropriations in annual budget of Commonwealth and federal program expenditures	125 bp over three-month LIBOR	June 30, 2005	\$ 640,000	640,000
Replenishment of income tax refund liability	125 bp over three-month LIBOR	June 30, 2008	250,000	250,000
Resources to meet appropriations in annual budget of Commonwealth and partial repayments of TRANS	125 bp over three-month LIBOR	July 31, 2009	233,000	233,000
Capital improvement projects of agencies and municipalities	150 bp over GDB's commercial paper rate	June 30, 2019	130,000	96,278
Resources for repayment of agencies' old debts	125 bp over three-month LIBOR	September 30, 2012	<u>100,000</u>	<u>91,808</u>
Balance carried forward			\$ <u>1,353,000</u>	<u>1,311,086</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

<b>Purpose</b>	<b>Interest rate</b>	<b>Maturity</b>	<b>Line of credit</b>	<b>Outstanding balance</b>
Balance brought forward			\$ 1,353,000	1,311,086
Capital improvement projects of certain Commonwealth agencies	150 bp over GDB's commercial paper rate	September 30, 2007	105,000	89,095
Resources for repayment of various agencies' old outstanding debt with PBA	125 bp over three-month LIBOR	September 30, 2008	40,000	30,285
Information technology projects	150 bp over GDB's commercial paper rate	September 30, 2008	44,868	29,673
Resources to cover deficit in certain elderly and childcare programs of the Department of the Family	125 bp over three-month LIBOR	September 30, 2011	19,000	19,000
Resources to meet program initiatives of the Department of Health, Health Insurance Administration, and the Department of the Family	125 bp over three-month LIBOR	September 30, 2015	79,930	18,005
Resources to meet program expenditures of the Department of Transportation and Public works	2.5%	September 30, 2008	44,000	15,262
Acquisition of correctional facilities	125 bp over three month LIBOR	September 30, 2012	<u>15,000</u>	<u>13,552</u>
			\$ <u>1,700,798</u>	<u>1,525,958</u>

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

On August 9, 1999, the Department of Agriculture of the Commonwealth entered into a \$125 million nonrevolving line-of-credit agreement with GDB to provide economic assistance to the agricultural sector, which sustained severe damages caused by Hurricane Georges in 1998. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on September 30, 2004. As of June 30, 2004, \$46.5 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On May 7, 2001, the Puerto Rico Court Administration Office (the Office) entered into a \$49.4 million nonrevolving line-of-credit agreement with GDB for operating purposes. Borrowings under this line-of-credit agreement bear interest at a variable rate of three-month London Interbank Offered Rate (LIBOR) plus 1%, not to exceed 8%. The Office must deposit \$6 million a year, from the total fees collected on the filing of civil cases, in a special fund created by the Department of the Treasury of the Commonwealth, which will be pledged for repayment until July 31, 2012. As of June 30, 2004, approximately \$42.8 million remain outstanding.

On October 2, 2002, the Department of Justice of the Commonwealth entered into a \$90 million line-of-credit agreement with GDB for the financing of 12 public improvements projects for the Municipality of Ponce pursuant to a court order. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line-of-credit on September 30, 2013. As of June 30, 2004, \$32.4 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On August 2003, the Department of Health of the Commonwealth entered into a \$30 million line-of-credit agreement with GDB in order to repay certain outstanding debts that the Puerto Rico Medical Services Administration had with other agencies and suppliers. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon maturity of the line of credit on June 30, 2012.

On August 21, 2002, the Department of Natural and Environmental Resources of the Commonwealth entered into a \$22.7 million line-of-credit agreement with GDB for the canalization of the Bucaná River. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line-of-credit on June 30, 2005. As of June 30, 2004, \$18.3 million were outstanding. The line-of-credit will be repaid from future legislative appropriations.

On June 21, 2001, the Office of the Superintendent of the Capitol (Superintendent) entered into a \$10 million line-of-credit agreement with GDB for the construction of a parking lot. Borrowings under this line-of-credit agreement bear interest at a fixed rate of 8% and are payable from future legislative appropriations commencing in fiscal year 2003 through fiscal year 2006. As of June 30, 2004, \$12.2 million were outstanding. On February 15, 2002, the Superintendent entered into an additional \$10 million line-of-credit agreement with GDB for the acquisition and remodeling of several buildings under its jurisdiction. Borrowings under this line-of-credit agreement bear interest at a fixed rate of 8% and are payable from future legislative appropriations commencing in fiscal year 2003 through fiscal year 2008. As of June 30, 2004, \$5.7 million remained outstanding from the line-of-credit agreement. Although the amount drawn through June 30, 2004 is expected to be repaid

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

within one year, this line of credit is nevertheless classified as long-term since the maximum amount of \$10 million, when drawn completely, will be repaid in various installments through fiscal year 2008.

On October 23, 2002, the Department of Recreation and Sports (DRS) of the Commonwealth entered into a \$17.5 million line-of-credit agreement for the development of a recreational complex and other facilities in San Juan, which will eventually become the DRS' principal office headquarters. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on September 30, 2008. At June 30, 2004, \$7.9 million had been drawn under this line-of-credit without any repayments. The line of credit will be repaid from future legislative appropriations. On October 23, 2002, DRS also entered into a \$16 million line-of-credit agreement with GDB for the development of a series of recreational projects at different municipalities. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on June 30, 2005, therefore considered a short-term fund liability. As of June 30, 2004, approximately \$8 million remained outstanding. This line of credit will be repaid from future legislature appropriations.

On October 31, 2003, the Department of Transportation and Public Works entered into a \$15 million line-of-credit agreement with GDB for the construction and repavement of roads around the island. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon maturity of the line of credit on June 30, 2005, therefore considered a short-term fund liability. As of June 30, 2004, \$10.3 million remained outstanding. This line of credit will be repaid from future legislative appropriations.

On February 6, 2003, the Department of Education of the Commonwealth entered into a \$25 million line-of-credit agreement with GDB for the purchase of equipment and for school improvements. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on June 30, 2008. As of June 30, 2004, \$8.5 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On August 1, 2001, the State Office for the Historic Conservation entered into a \$4.5 million line-of-credit agreement with GDB for the construction and conservation of the Santa Catalina Palace and the Real Audiencia building. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on December 31, 2008. As of June 30, 2004, \$4.5 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On August 28, 2000, GDB approved an amendment to the terms of two line-of-credit agreements of the Correction Administration by which such debts would be repaid between fiscal years 2000 and 2004. The two agreements were issued by GDB in August 1998 to partially fund permanent improvements to correctional facilities. The agreements have variable interest rates and limits of \$60 million and \$15 million, respectively. Their outstanding balance as of June 30, 2004 is \$3.7 million, which is expected to be repaid during fiscal year 2005.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

As of July 1, 1999, debts of approximately \$102 million from various agreements payable to UPR, a discretely presented component unit, in relation to outstanding noninterest-bearing debt accumulated in prior years by HFSA were transferred to the Commonwealth. As of June 30, 2004, approximately \$23.5 million remains outstanding. Future amounts required to pay principal balances at June 30, 2004 are as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2005	\$ 7,570
2006	—
2007	7,570
2008	8,330
	<u>\$ 23,470</u>

The noninterest-bearing note payable to PREPA, a discretely presented component unit, consists of approximately \$31.6 million of a fuel adjustment subsidy due by the Commonwealth and the refinancing during 2004 of \$24.1 million of other accumulated debt by Commonwealth's agencies with PREPA. Future amounts required to pay principal balances at June 30, 2004 are as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2005	\$ 6,327
2006	6,327
2007	6,327
2008	6,327
2009	6,327
2010-2013	24,100
Total	<u>\$ 55,735</u>

The Department of the Treasury of the Commonwealth entered into a line-of-credit agreement with GDB for the purpose of financing the costs of a new series of lottery tickets for the Lottery of Puerto Rico. The note establishes a line-of-credit limit of \$2.5 million, maturing on July 1, 2007 and accruing interest at a rate of 6.5%. Annual interest payment commitments through 2007 are estimated at \$68,000. The amount outstanding as of June 30, 2004, is approximately \$1 million.

**(h) *Compensated Absences***

Long-term debt includes approximately \$1,392 million accrued vacation and sick leave benefits at June 30, 2004. The total liability of compensated absences recorded as governmental and business-type activities amounted to \$1,387 million and \$5 million, respectively.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

**(i) Net Pension Obligation**

The amount reported as net pension obligation of approximately \$4.2 billion represents the cumulative amount owed by the Commonwealth for the unfunded prior years' actuarially required pension contributions to the ERS and the TRS (collectively known as the pension plans) (see note 19). The net pension obligation has been recorded as a liability in the governmental activity in the accompanying government-wide statement of net assets.

**(j) Unpaid Lottery Prizes**

The amount reported as unpaid lottery prizes represents the lottery prizes payable of the Lottery of Puerto Rico (commonly known as Traditional Lottery) and the additional lottery system (commonly known as Lotto) jointly known as the Lottery Systems at June 30, 2004. The minimum annual payments related to unpaid awards of both lotteries are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 37,071	—	37,071
2006	31,043	618	31,661
2007	30,006	1,655	31,661
2008	28,818	2,810	31,628
2009	27,541	4,087	31,628
2010-2014	108,148	36,889	145,037
2015-2019	46,271	36,985	83,256
2020-2024	9,573	13,302	22,875
Total	<u>\$ 318,471</u>	<u>96,346</u>	<u>414,817</u>

The liability for unpaid lottery prizes is reported in the accompanying government-wide statement of net assets and the statement of net assets – business-type activities – enterprise funds.

**(k) Liability for Insurance Benefit Claims**

The Commonwealth provides unemployment compensation, nonoccupational disability, and drivers' insurance coverage to public and private employees through various insurance programs administered by the Department of Labor and Human Resources of the Commonwealth. These insurance programs cover workers against unemployment, temporary disability, or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment.

The Commonwealth establishes liabilities for incurred but unpaid benefits and benefit adjustment expenses based on the ultimate cost of settling the benefits. Insurance benefit claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. The liability for insurance benefits claims is reported as a

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

current liability in the accompanying government-wide statement of net assets and the statement of net assets – business-type activities – enterprise funds.

*(l) Obligations Under Capital Lease Arrangements*

The Commonwealth is obligated under capital leases with third parties that expire through 2034 for land, buildings, and equipment. At June 30, 2004, the capitalized cost of the land, buildings, and equipment amounted to approximately \$186 million and is included in the accompanying government-wide statement of net assets within capital assets.

The present value of future minimum capital lease payments at June 30, 2004 reported in the accompanying government-wide statement of net assets is as follows (expressed in thousands):

Year ending June 30,		
2005	\$	18,912
2006		17,599
2007		14,696
2008		14,308
2009		13,586
2010-2014		66,529
2015-2019		63,579
2020-2024		56,934
2025-2029		56,934
2030-2034		25,213
Total future minimum lease payments		348,290
Less: amount representing interest costs		(195,076)
Present value of minimum lease payments	\$	153,214

Leased land, buildings, and equipment under capital leases in capital assets at June 30, 2004, include the following (expressed in thousands):

Land	\$	7,960
Buildings		146,202
Equipment		31,385
Subtotal		185,547
Less: accumulated amortization		(36,480)
Total	\$	149,067

Amortization charge applicable to capital leases and included within depreciation expense of capital assets amounted to approximately \$8 million in 2004.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The Commonwealth is also committed under numerous operating leases, covering land, office facilities, and equipment. Rental expenditures within the governmental funds for the year ended June 30, 2004, under such operating leases were approximately \$135 million.

The future minimum lease payments for these leases are as follows (expressed in thousands):

<b>Year ending June 30,</b>		
2005	\$	87,981
2006		68,322
2007		45,804
2008		30,948
2009		19,242
2010-2014		30,212
2015-2019		4,999
2020-2024		5,040
Total future minimum lease payments	\$	292,548

**(m) Other Long-Term Liabilities**

The remaining long-term liabilities of governmental activities at June 30, 2004 include (expressed in thousands):

Employees' Christmas bonus	\$	102,820
Liability for federal cost disallowances		99,232
Liability for legal claims and judgments		219,183
Total	\$	421,235

**(n) Advance Refunding, Defeased Bonds, and Refunding of Special Promissory Notes**

The Commonwealth advance refunded certain general obligation bonds through the issuance of approximately \$727 million of general obligation public improvements refunding bonds during the year ended June 30, 2004. The Commonwealth used approximately \$732 million from the net proceeds of the issued bonds plus additional moneys provided by the Commonwealth to purchase U.S. government securities, which were deposited in an irrevocable trust fund with an escrow agent to provide for all future debt service payments of the refunded bonds. As a result, the refunded bonds are considered to be defeased, and the liabilities have therefore been removed from the statement of net assets. As a result of this advance refunding, the Commonwealth decreased current year debt service payments and has taken advantage of lower interest rates, and it has increased its aggregate debt service payments by approximately \$62.8 million over the next 27 years and obtained an economic gain (the difference between the present values of the debt service payments of the refunded and refunding bonds) of approximately \$60.2 million. At June 30, 2004, approximately

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

\$691 million of the bonds refunded during the year ended June 30, 2004 remain outstanding and are considered defeased.

In prior years, the Commonwealth also defeased certain general obligation and other bonds by placing the proceeds of bonds in an irrevocable trust to provide for all future debt service payments on the refunded bonds. Accordingly, the trusts' account assets and liabilities for the defeased bonds are not included in the basic financial statements. At June 30, 2004, approximately \$2.46 billion of bonds outstanding from prior years advance refunding are considered defeased.

As a result of the advance refunding of the Commonwealth appropriation bonds referred in note 14(i) the Commonwealth has decreased its aggregate debt service payments by approximately \$127.8 million over the next 27 years and obtained an economic gain (the difference between the present values of the debt service payments of the refunded and refunding bonds) of approximately \$119.9 million.

In addition, PBA, a blended component unit, defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old debts. Accordingly, the trust account's assets and liabilities for the defeased bonds are not included in the statement of net assets. As of June 30, 2004, approximately \$2.4 billion of PBA bonds are considered defeased.

On December 12, 2001, PFC, a blended component unit of GDB, issued \$96.8 million of QZAB to finance expenditures of the Department of Education of the Commonwealth under the QZAB program described in note 14(e), including rehabilitation and repairs of school buildings and other facilities, the development and implementation of academic curricula, technology training for some schools, and the costs of issuance of the bonds. These QZAB are payable upon its maturity on December 11, 2015. Simultaneous with the QZAB issuance, The Children's Trust, a blended component unit of the Commonwealth, granted \$47.2 million to the Department of Education of the Commonwealth, which in turn deposited the moneys to the credit of an escrow trust account invested in guaranteed investment contracts that will be used solely for the repayment in 2015 of these QZAB. These November 2001 QZAB are considered defeased and the difference between the bond amount and the amount deposited in the escrow account has been deferred and is amortized into income over the term of the bonds.

### **Fiduciary Funds**

On August 1, 1996, the TRS entered into a loan agreement with AFICA, a discretely presented component unit, to secure AFICA's issuance of \$26.9 million of industrial revenue term bonds. The bonds were issued under a trust agreement and are secured by a pledge of certain marketable securities of the TRS.

The proceeds from the sale of the bonds were lent by AFICA to TRS to finance the acquisition of certain buildings and related facilities and to pay certain expenses incurred in connection with the issuance and sale of the bonds.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Bonds payable outstanding at June 30, 2004, are as follows (expressed in thousands):

Term Bonds Series A payable through 2012, interest payable on a monthly basis at rates varying from 6.50% to 6.65%	\$ 6,880
Term Bonds Series B payable through 2022, interest payable semiannually at 5.50%	<u>15,210</u>
Total	<u>\$ 22,090</u>

Maturities of the term bonds are as follows (expressed in thousands):

Year ending June 30,	Principal	Interest	Total
2005	\$ 805	1,292	2,097
2006	855	1,239	2,094
2007	915	1,184	2,099
2008	975	1,123	2,098
2009	1,040	1,058	2,098
2010-2014	6,015	4,216	10,231
2015-2019	7,745	2,352	10,097
2020-2022	<u>3,740</u>	<u>311</u>	<u>4,051</u>
Total	<u>\$ 22,090</u>	<u>12,775</u>	<u>34,865</u>

The Series A and Series B Bonds are subject to redemption, at the option of the TRS, in whole or in part on July 1, 2006, or any date thereafter at the determined redemption prices plus accrued interest to the redemption date as follows:

July 1, 2006 through June 30, 2007	102%
July 1, 2007 through June 30, 2008	101%
July 1, 2008 and thereafter	100%

The TRS has also entered into a \$15 million line of credit with GDB, due on October 31, 2010 and guaranteed by a pool of investments of the TRS. At June 30, 2004, the outstanding balance of the line of credit was \$240,000 bearing interest at an annual interest rate of 5%.

**Discretely Presented Component Units**

Notes and bonds payable are those liabilities that are paid out of resources pledged by the other component units. These notes and bonds do not constitute a liability or debt of the Commonwealth.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Notes payable outstanding at June 30, 2004 are as follows (expressed in thousands):

<u>Component unit</u>	<u>Interest rate</u>	<u>Maturity through</u>	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Amounts due within one year</u>
Government Development Bank for Puerto Rico	1.46%	2003	\$ 761,167	3,699,480	3,525,562	935,085	933,327
Puerto Rico Electric Power Authority	LIBOR minus 3%	2004	5,000	—	—	5,000	5,000
State Insurance Fund Corporation	Discounted notes	2019	57,773	—	1,135	56,638	1,386
Economic Development Bank	.08%-5.4%	2023	160,551	200,000	5,317	355,234	55,234
Puerto Rico Industrial Development Company	6.625% – 6.8125%	2012	58,972	4,825	1,122	62,675	1,239
Puerto Rico Ports Authority	Variable	2005	47,062	21,400	5,162	63,300	63,300
Total notes payable – component units			\$ 1,090,525	3,925,705	3,538,298	1,477,932	1,059,486

Notes payable of \$125 million of PREPA, not included in the table above, have no fixed maturity date and variable interest rates. For financial reporting purposes, these notes have been classified as due within one year. These had no additions or reductions during 2004.

Debt service requirements on component units' notes payable with fixed maturities at June 30, 2004, were as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 1,059,486	1,016,828	2,076,314
2006	4,696	21,619	26,315
2007	3,575	19,664	23,239
2008	4,184	19,428	23,612
2009	4,659	19,144	23,803
2010-2014	130,026	77,437	207,463
2015-2019	176,300	56,704	233,004
2020-2024	90,523	18,071	108,594
2025-2029	4,483	8	4,491
Total	\$ 1,477,932	1,248,903	2,726,835

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Commonwealth appropriation bonds payable outstanding at June 30, 2004 are as follows (expressed in thousands):

<b>Component unit</b>	<b>Interest rate</b>	<b>Maturity through</b>	<b>Beginning balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending balance</b>	<b>Amounts due within one year</b>
Puerto Rico Aqueduct and Sewer Authority	5.50%	2031	\$ 712,130	343,641	340,389	715,382	6,797
Tourism Company of Puerto Rico	4%-6.15%	2031	127,308	54,206	53,944	127,570	1,217
Land Authority of Puerto Rico	4%-6.15%	2031	111,061	47,932	-	158,993	-
Government Development Bank for Puerto Rico	4%-6.15%	2031	10,029	4,541	4,231	10,339	-
Puerto Rico Infrastructure Financing Authority	7.50%	2031	10,331	321	-	10,652	1,177
Puerto Rico Solid Waste Authority	1.25%-5.75%	2029	21,992	16,265	31,550	6,707	3
Total appropriation bonds – component units			\$ 992,851	466,906	430,114	1,029,643	9,194

Debt service requirements on component units' appropriation bonds payable with fixed maturities at June 30, 2004, were as follows (expressed in thousands):

<b>Year ending June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2005	\$ 9,194	28,170	37,364
2006	4,460	56,516	60,976
2007	3,811	56,371	60,182
2008	14,930	55,665	70,595
2009	15,749	54,837	70,586
2010-2014	87,991	252,877	340,868
2015-2019	137,846	204,774	342,620
2020-2024	184,924	153,181	338,105
2025-2029	351,063	91,118	442,181
2030-2034	242,127	8,253	250,380
	1,052,095	961,762	2,013,857
Less: discounts, net	(22,452)	—	(22,452)
Total	\$ 1,029,643	961,762	1,991,405

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Bonds payable outstanding at June 30, 2004 are as follows (expressed in thousands):

<u>Component unit</u>	<u>Interest rate</u>	<u>Maturity through</u>	<u>Beginning balance (as restated)</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Amounts due within one year</u>
Government							
Development Bank for Puerto Rico	5%-6.25%	2006	\$ 1,771,670	—	169,709	1,601,961	87,596
Puerto Rico Infrastructure Financing Authority	Variable	2028	1,984,891	—	24,214	1,960,677	26,955
University of Puerto Rico	3% – 5.75%	2030	518,598	2,097	21,169	499,526	18,550
Puerto Rico Municipal Finance Authority	5% – 8.62%	2023	1,424,110	—	85,749	1,338,361	89,480
Puerto Rico Ports Authority	5% – 7.30%	2021	82,257	171	8,380	74,048	3,970
Puerto Rico Aqueduct and Sewer Authority	3.5%-8.22%	2040	818,750	370,525	345,404	843,871	23,142
Puerto Rico Highway and Transportation Authority	Variable	2041	5,314,394	643,447	85,832	5,872,009	29,135
Puerto Rico Industrial Development Company	5.375% – 7.75%	2021	177,245	163,183	34,341	306,087	8,979
Puerto Rico Electric Power Authority	3.8% – 7%	2031	4,506,718	399,288	1,479	4,904,527	331,806
Total bonds – component units			\$ 16,598,633	1,578,711	776,277	17,401,067	619,613

Debt service requirements on component units' bonds payable with fixed maturities at June 30, 2004, were as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 619,613	1,000,245	1,619,858
2006	554,105	879,425	1,433,530
2007	574,196	851,496	1,425,692
2008	512,465	823,496	1,335,961
2009	566,310	810,276	1,376,586
2010-2014	7,469,602	7,083,316	14,552,918
2015-2019	2,171,048	1,726,694	3,897,742
2020-2024	1,936,754	1,233,070	3,169,824
2025-2029	2,110,243	656,472	2,766,715
2030-2034	803,818	260,675	1,064,493
2035-2039	458,116	86,143	544,259
2040-2044	152,972	8,484	161,456
Total	17,929,242	15,419,792	33,349,034
Less: discounts, net	(528,175)	—	(528,175)
	\$ 17,401,067	15,419,792	32,820,859

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The bonds payable of discretely presented component units were changed as of the beginning of the year primarily as a result of the inclusion of a component unit from the UPR in the current year (see note 4).

Several component units have defeased certain revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old debts. Accordingly, the trust accounts' assets and liabilities for the defeased bonds are not included in the statement of net assets. As of June 30, 2004, the following bonds are considered defeased which pertain to major component units:

	<b>Amount outstanding at June 30, 2004 (in millions)</b>
Puerto Rico Highway and Transportation Authority	\$ 587
Puerto Rico Electric Power Authority	614

**(15) Guaranteed and Appropriation Debt**

*(a) Guaranteed Debt*

The Commonwealth may provide guarantees for the repayment of certain borrowings of component units to carry out designated projects. At June 30, 2004, the following component unit debts are guaranteed by the Commonwealth (expressed in thousands):

	<b>Maximum guarantee</b>	<b>Outstanding balance</b>
Blended component unit:		
Public Buildings Authority	\$ 3,325	2,914
Discretely presented component units:		
Puerto Rico Aqueduct and Sewer Authority	732	637
Government Development Bank for Puerto Rico	625	267
Total	\$ 4,682	3,818

The Commonwealth has guaranteed the payments of rentals of its departments, agencies, and component units to PBA, a blended component unit, under various lease agreements executed pursuant to the law that created PBA. Such rental payments include the amounts required by PBA for

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

the payment of principal and interest on the guaranteed debt as authorized by law. The rental commitment to cover principal and interest on the guaranteed debt (excluding premiums and deferred refunding losses) as of June 30, 2004 and for the next five years and thereafter follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 26,276	107,583	133,859
2006	35,840	146,737	182,577
2007	56,855	152,464	209,319
2008	73,057	138,934	211,991
2009	80,684	134,992	215,676
2010-2014	418,297	625,256	1,043,553
2015-2019	405,150	509,415	914,565
2020-2024	378,180	411,802	789,982
2025-2029	472,655	310,765	783,420
2030-2034	563,069	218,855	781,924
2035-2038	436,540	31,828	468,368
	<u>2,946,603</u>	<u>2,788,631</u>	<u>\$ 5,735,234</u>
Add (deduct) accreted discount	<u>41,689</u>	<u>(41,689)</u>	
Total	<u>\$ 2,988,292</u>	<u>2,746,942</u>	

Rental income of PBA funds amounted to approximately \$226 million during the year ended June 30, 2004, of which \$105 million was used to cover debt service obligations.

Act No. 45 of July 28, 1994, states that the Commonwealth guarantees the payment of principal and interest of all outstanding bonds at the date the law was enacted and of all future bond issues to refinance those outstanding bonds of PRASA. During December 1995, PRASA issued refunding bonds to refinance all outstanding bonds amounting to approximately \$400.3 million. The outstanding balance of these refunding bonds at June 30, 2004, amounted to \$305 million. Act No. 140 of August 3, 2000, amended Act No. 45 to extend the Commonwealth guarantee to include the principal and interest payments of the Rural Development Serial Bonds and the loans under the State Revolving Fund Program (SRFP) outstanding at the effective date of Act No. 140, and of all future bonds and SRFP loans that may be issued until June 30, 2005. Act No. 386 of September 21, 2004, extended the Commonwealth guarantee to June 30, 2010. The outstanding balance of the Rural Development Serial Bonds and SRFP loans at June 30, 2004, amounted to \$179 million and \$153 million, respectively.

The Commonwealth guarantees the Adjustable Refunding Bonds, Series 1985, issued by GDB, a discretely presented component unit. The outstanding balance of these bonds amounts to \$267 million at June 30, 2004.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

The Puerto Public Housing Administration, a former component unit of the Commonwealth, which merged with and into GDB during 2002, insured mortgages granted to low- and moderate-income families through its mortgage loan insurance program. The Commonwealth guarantees up to \$75 million of such mortgage loans. As of June 30, 2004, the mortgage loan insurance program was insuring loans aggregating \$497 million. Currently, the Commonwealth has not been called to make any direct payments pursuant to these guarantees.

### (b) *Appropriation Debt*

At June 30, 2004, the outstanding balances of debt payable by government appropriations and which are included in the individual financial statements of these entities are as follows (expressed in thousands):

Discretely presented component units:

Puerto Rico Aqueduct and Sewer Authority	\$ 734,928
Puerto Rico Convention Center District Authority	205,474
Puerto Rico Land Authority	158,993
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	140,911
Tourism Company of Puerto Rico	127,570
Government Development Bank for Puerto Rico	124,514
Special Communities Perpetual Trust	90,918
Puerto Rico Solid Waste Authority	83,789
Puerto Rico Infrastructure Financing Authority	80,652
National Parks Company of Puerto Rico	13,035
University of Puerto Rico	1,905
Employment and Training Enterprises Corporation	1,414
Puerto Rico Electric Power Authority	19
Other governmental entities	40,115
	<u>\$ 1,804,237</u>

### (16) **Conduit Debt Obligations**

To provide for the development and modernization of low-rent housing units, PHA has issued New Housing Authority bonds, permanent notes and federal financial bank notes. These bonds and notes are payable by HUD and secured by annual contributions. The bonds and notes do not constitute a debt by PHA and accordingly have not been reported in the accompanying financial statements. The following consists of the composition of the conduit debt referred to above at June 30, 2004 (expressed in thousands):

Permanent notes	\$ 1,048,015
New Housing Authority bonds	70,620
Federal Financial Bank notes	9,638
	<u>\$ 1,128,273</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

From time to time, certain of the Commonwealth's component units issue revenue bonds to provide financial assistance to private-sector entities for the acquisition and construction of transportation, environmental, industrial, tourism, educational, commercial facilities, and Caribbean Basin projects deemed to be in the public interest and that are expected to provide benefits to Puerto Rico. These bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities is retained by the private-sector entity served by the bond issuance. Neither the Commonwealth nor any political subdivision or component unit thereof is obligated in any manner for the repayment of the bonds.

Accordingly, the bonds are not reported as liabilities in the basic financial statements of the issuing entities. As of June 30, 2004, conduit debt obligations consisted of the following bonds issued by component units (expressed in thousands):

<b>Issuing entity</b>	<b>Issued since inception to date</b>	<b>Amount outstanding</b>
Discretely presented component units:		
Caribbean Basin Projects Financing Authority	\$ <u>676,000</u>	<u>22,000</u>
Puerto Rico Ports Authority	\$ <u>155,410</u>	<u>155,410</u>
Puerto Rico Highway and Transportation Authority	\$ <u>270,000</u>	<u>153,856</u>
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	\$ <u>5,844,000</u>	<u>2,153,000</u>

**(a) Caribbean Basin Projects Financing Authority (CBPFA)**

Pursuant to the loan agreements covering the issuance of these bonds, the proceeds from the sales were borrowed from CBPFA by corporations and partnerships operating in qualified Caribbean Basin countries. The revenue bonds are special and limited obligations of CBPFA and, except to the extent payable from bond proceeds and investments thereof, will be payable solely from and secured by a pledge and assignment of the amounts payable under the loan agreements between CBPFA and the borrowers. Furthermore, payment of the principal and interest on the revenue bonds is unconditionally guaranteed by the borrowers, their parent companies, and/or letters of credit from major U.S. banks or U.S. branches of international banks. The revenue bonds do not constitute a debt or a pledge of the good faith and credit of CBPFA or the Commonwealth or any political subdivision thereof.

**(b) Puerto Rico Ports Authority**

PRPA has issued Special Facilities Revenue Bonds under the provisions of two trust agreements between PRPA and a private bank. The proceeds from the sale of the bonds were used to finance the construction, acquisition of equipment, and improvement of certain facilities at Luis Muñoz Marín

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

International Airport, for the benefit of a major private airline. The property is owned by PRPA and leased to the private company. Pursuant to the agreements between PRPA and the private company, the bonds will be paid from the rent collected from the airline in amounts sufficient to pay principal, premium (if any), and interest on the bonds. The airline has guaranteed these payments.

(c) ***Puerto Rico Highway and Transportation Authority (PRHTA)***

In March 1992, PRHTA issued Special Facility Revenue Bonds for approximately \$117 million for the construction of a toll bridge. The proceeds from the sale of these bonds were transferred by PRHTA to a private entity, pursuant to a signed agreement for the construction, transfer, and operation of the bridge. The bonds shall be paid from the proceeds received by the private entity from the operation of the bridge. However, under certain circumstances, the private entity may have the right of terminating the agreement and PRHTA will assume the obligation to pay the bonds. The outstanding balance of these bonds at June 30, 2004 included accreted interest.

(d) ***AFICA***

The revenue bonds of AFICA are used to finance facilities for environmental control, development of industrial and commercial companies, tourism projects, hospitals, and educational facilities. Pursuant to the loan agreements, the proceeds from the sales were borrowed by corporations and partnerships operating in Puerto Rico. The bonds are limited obligations of AFICA and, except to the extent payable from bond proceeds and investment thereof, will be payable solely from and secured by a pledge and assignment of the amounts payable under the loan agreements between AFICA and each borrower. Furthermore, payment of the principal and interest on the revenue bonds is unconditionally guaranteed by each of the borrowers, their parent companies, or letters of credit from major U.S. banks or U.S. branches of international banks.

**(17) Risk Management**

The risk management program of the Commonwealth and most of its discretely component units are described in note 1(y). The following describes the risk management programs separately administered by certain discretely presented component units.

(a) ***UPR***

The UPR is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The UPR carries commercial insurance for these risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Under Act No. 98 of August 24, 1994, the responsibility of UPR on medical malpractice claims is limited to a maximum amount of \$75,000 per person, or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Self-insured risks liabilities are reported when it is probable that a loss has occurred and the amount of the

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

Changes in the claim liabilities amount for the current fiscal year was as follows (expressed in thousands):

Claims payable at beginning of year	\$	13,358
Incurred claims and changes in estimates		3,311
Net payments for claims and adjustment expenses		<u>(2,871)</u>
Claims payable at end of year	\$	<u>13,798</u>

Claims payable are reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

**(b) PREPA**

PREPA is exposed to various risks of losses related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. PREPA obtains insurance policies covering all-risk property (excluding transmission and distribution lines), boiler and machinery, and public liability. The all-risk property and boiler and machinery policies have a combined coverage of \$650 million per occurrence. The policies' self-retention in case of earthquake and windstorm losses is \$25 million, \$2 million for all other covered risks, except boiler and machinery losses, which carry a \$2 million retention. The public general liability policy covers property damage and bodily injury to third parties with a \$75 million aggregate limit in excess of the self-retention limit of a \$1 million occurrence.

In addition, PREPA is self-insured for damage to its transmission and distribution lines. Transmission and distribution lines amounted to approximately \$3.1 billion at June 30, 2004. PREPA's self-insurance fund provides for its self-insurance risk. This fund represents principally net assets and restricted assets set-aside for self-insurance amounting to approximately \$80.8 million as of June 30, 2004.

PREPA has a cost plus health insurance program covering substantially all its employees. PREPA contracted an administrator for the processing, approval, and payment of claims at cost plus an administrative fee. The accrual includes claims processed and an estimate for claims incurred but not reported.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

Changes in the balances of the health insurance program and other self-insurance risks for the current fiscal year were as follows (expressed in thousands):

Claims payable at beginning of year	\$	50,891
Incurred claims		92,822
Claims payment		<u>(112,073)</u>
Claims payable at end of year	\$	<u>31,640</u>

Claims payable is reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

(c) **PRASA**

PRASA is exposed to various risks of losses related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Under the property insurance program, PRASA has a \$300 million blanket insurance on all real and personal property. The deductible for windstorm and flood is 2% and 5% for earthquake with a maximum amount of \$7.5 million, and \$3 million for flood. For property in transit, the deductible is \$150,000 per occurrence. This policy has a general limit of \$10 million per occurrence..

The comprehensive general liability and automobile liability have basic limits of \$3 million and the umbrella is \$25 million in excess of \$3 million, per occurrence. Also, there is an excess liability of \$45 million in excess of \$28 million.

The boiler and machinery policy was included under the property insurance policy as an additional coverage; the directors and officers policy was modified as follows: primary policy limits are \$12 million with a self-retention of \$150,000 per claim; the travel/accident policy has a \$2 million in aggregate coverage, and a limit of \$500,000 per person.

(d) **SIFC**

SIFC provides workers' compensation insurance to public and private employees. This insurance covers workers against injuries, disability, or death because of work or employment-related accidents, or because illness is suffered as a consequence of their employment. SIFC establishes liabilities for estimated incurred but unpaid benefits and benefit adjustment expenses based on the

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

ultimate cost of settling the benefits. The following table provides a reconciliation of the beginning and ending liability for incurred but unpaid benefits and benefit adjustment expenses for the year ended June 30, 2004 (expressed in thousands):

Liability for incurred but unpaid benefits and benefit adjustment expenses at beginning of year	\$ 865,352
Total incurred benefits	285,314
Total benefit payments	<u>(377,838)</u>
Liability for incurred but unpaid benefits and benefit adjustment expenses at end of year	<u>\$ 772,828</u>

The liability for incurred but unpaid benefits and benefit adjustment expenses is reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

The liability for compensation benefits is based on historical claims experience data, assumptions and projections as to future events, including claims frequency, severity, persistency, and inflationary trends determined by an independent actuary. The actuarial study also included estimates for medical benefits, benefit adjustment expenses, and reimbursement of premiums. The assumptions used in estimating and establishing the liabilities are reviewed annually based on current circumstances and any adjustments resulting thereof are reflected in operations in the current period.

(e) **AACA**

AACA operates a system of compulsory insurance for vehicles licensed to be used on public roads and highways in Puerto Rico. This insurance covers death and bodily injuries caused by automobile accidents. The annual premium is \$35 per motor vehicle.

The following table provides a reconciliation of the beginning and ending liability for future benefits for the year ended June 30, 2004 (expressed in thousands):

Liability for future benefits at beginning of year	\$ 113,562
Total incurred benefits	60,358
Total benefit payments	<u>(64,075)</u>
Liability for future benefits at end of year	<u>\$ 109,845</u>

The liability for future benefits is reported as account payable and accrued liabilities in the accompanying statement of net assets. AACA has recorded this liability, including administrative expenses for claim processing, based on the results of actuarial reports prepared by independent

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

actuaries, determined under two different methods. Death, funeral, disability, dismemberment, and the basic medical hospitalization liabilities were determined using a triangulation method. The extended benefits medical hospitalization reserve uses a regression methodology to predict the ultimate incurred claims for each incurred calendar quarter. Additionally, assumptions are made about the mortality rates of the extended benefit claimants, recognizing the impact of their traumatic injuries on life span.

Changes in the ultimate liabilities for benefit payments may be required as information develops which varies from experience, provides additional data, or, in some cases, augments data, which previously were not considered sufficient for use in determining the claim liabilities.

### **(18) Commitments and Contingencies**

#### ***Primary Government***

The Commonwealth is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are authorized to sue the Commonwealth only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Commonwealth may provide its officers and employees with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the payment of such judgments.

With respect to pending and threatened litigation, excluding the litigation mentioned in the following paragraph, the Commonwealth reported approximately \$99 million as an amount to cover for awarded and anticipated unfavorable judgments at June 30, 2004. This amount was included as other long-term liabilities in the accompanying statement of net assets, and represents the amount estimated as a probable liability or a liability with a fixed or expected due date that will require future available financial resources for its payment. Management believes that the ultimate liability in excess of amounts provided, if any, would not be significant.

The Commonwealth is a defendant in a lawsuit filed in a local district court by an association of primary care health centers seeking to recover from the Commonwealth \$120 million of Medicaid funds retained by the Department of Health of the Commonwealth since 1997. In June 2004, the First Circuit Court of San Juan determined that the Commonwealth must return these funds. The Commonwealth appealed this decision. As of June 30, 2004, the Commonwealth accrued \$120 million for this legal contingency.

The Commonwealth and various component units are defendants in other lawsuits alleging violations of civil rights and other damages. Preliminary hearings and discovery proceedings are in progress. The amounts claimed exceed \$7.8 billion; however, the ultimate liability cannot be presently determined. It is the opinion of management that the claims are excessive and exaggerated. No provisions for any liability that may result upon adjudication of these lawsuits have been recognized in the basic financial statements

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

by the Commonwealth. Management believes that the ultimate liability in excess of amounts provided, if any, would not be significant.

Additionally on April 13, 2004, in anticipation of the issuance of the Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 2004 B Bonds, GDB entered into interest rate exchange agreements (the Interest Rate Agreements) with three counterparties. At the same time, GDB entered into several mirror swap agreements (mirror swaps) with the Commonwealth in the notional amount of \$448 million. The purpose of the Interest Rate Agreements was to hedge the Commonwealth's variable rate debt exposure and the interest rate risks associated therewith in relation to the Series 2004 B Bonds. The mirror swaps transfer the exposures and risks to the Commonwealth. On November 18, 2004, upon enactment of legislation that expressly authorizes the Commonwealth to enter into agreements of the nature of the Interest Rate Agreements and, among other things, to pledge the full faith, credit, and taxing power of the Commonwealth to all payments to be made under the Agreements, the interest Rate Agreements were transferred to the Commonwealth in exchange for the cancellation of the mirror swaps.

The Commonwealth receives financial assistance from the federal government in the form of grants and entitlements. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal law and regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under Circular A-133 of the OMB of the United States of America (OMB Circular A-133), all of which are performed at the individual agency level. Disallowance as a result of these audits may become liabilities of the Commonwealth. At June 30, 2004, based on an evaluation of pending federal disallowances, the Commonwealth has recorded approximately \$99.2 million as other long-term liabilities in the accompanying statement of net assets.

Construction commitments at June 30, 2004, entered by PBA amounted to approximately \$286 million. In addition, the Commonwealth's construction commitments for public housing facilities amounted to approximately \$312 million at June 30, 2004.

At June 30, 2004, The Children's Trust, a blended component unit of the Commonwealth, had approved commitments to provide assistance to several entities through 77 contracts with balances amounting to approximately \$311.6 million.

On November 23, 1998, a global settlement agreement (the Agreement) was entered into by and between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The Agreement calls for annual payments through the year 2025, which will vary due to inflationary and volume adjustments. After 2025, the tobacco companies are to continue making contributions in perpetuity. Pursuant to Act No. 173 of July 30, 1999, which created The Children's Trust, the Commonwealth assigned and transferred to The Children's Trust all payments that the Commonwealth is entitled to receive under the Agreement. Payments received under the Agreement and recognized as revenue during the year ended June 30, 2004, amounted to approximately \$70 million.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Following is a summary of estimated payments to be received by The Children's Trust through the year ending June 30, 2025 (expressed in thousands):

<u>Year ending June 30,</u>	
2005	\$ 73,642
2006	74,845
2007	75,990
2008	78,679
2009	79,854
Thereafter	<u>1,525,081</u>
Total	\$ <u>1,908,091</u>

### *Component Units*

In the normal course of their operations the various component units are subject to guarantees, actions brought by third parties seeking damages or entering into commitments. Such actions are disclosed in the separately issued reports of the component units some of which are summarized below:

### *General Commitments and Contingencies*

#### *(a) GDB*

At June 30, 2004, GDB has financial guarantees for public entities for approximately \$75 million and for private sector of approximately \$352 million. In addition, standby letters of credit to public entities were approximately \$115 million and to private sector were approximately \$20 million. Commitments to extend credit to public entities were approximately \$3.9 billion and to private sector were approximately \$27.3 million.

GDB enters into sales of securities under agreements to repurchase. These agreements generally represent short-term debts and are presented as a liability in the statement of net assets. The securities underlying these agreements are usually held by the broker, or its agent, with whom the agreement is transacted. As of June 30, 2004, there were agreements outstanding for \$160 million and during the year the average amount outstanding was approximately \$351 million, the maximum amount outstanding at any month-end was approximately \$179 million; and the weighted average interest rate for the year and at year-end was approximately 1.63% and 1.27%, respectively.

GDB issues commercial paper in the U.S. taxable and tax-exempt commercial paper markets, the Eurodollar commercial paper market, and to corporations that have tax exemption under the Commonwealth's Industrial Incentives Act and qualify for benefits provided by the U.S. Internal Revenue Code Section 936. Commercial paper represents unsecured obligations of GDB. The carrying amount of commercial paper at June 30, 2004 was approximately \$918 million; the maximum amount at any month-end was approximately \$1,114 million; the weighted average

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

amount outstanding during the year was approximately \$828 million and the weighted average interest rate for the year and at year-end was approximately 1.04% and 1.08%, respectively.

At June 30, 2004, GDB had outstanding interest rate swap agreements with other financial institutions in the aggregate notional amounts of \$1.5 billion, having a fair value (payable position) of approximately \$27 million. GDB also had an equity appreciation index embedded in a \$200 million certificate of indebtedness. Such embedded derivative has been recognized as a liability at its fair value of approximately \$13 million as of June 30, 2004. GDB is exposed to credit loss in the event of nonperformance by the other parties to swap agreements. However, GDB does not anticipate nonperformance by counterparties.

On November 21, 2002, the Legislature of the Commonwealth approved Joint Resolution No.1027, authorizing GDB to transfer \$500 million as a contribution to SCPT, a discretely presented component unit created for the purpose of financing a variety of initiatives, primarily housing and infrastructure, directed to the betterment of disadvantaged communities across the island. As approved in the Joint Resolution, the contribution will be disbursed following approved laws and regulations. The board of director of GDB approved a regulation (the regulation), which calls for the disbursement of contributions based on the compliance with certain reimbursement requirements. As of June 30, 2004, disbursements amounted to \$3.8 million.

In addition, the Legislature approved on November 21, 2002 Joint Resolution No. 1028, which authorized the Special Communities Trust to borrow up to \$500 million in order to carry out the initiatives with which it was entrusted. The Joint Resolution authorizes GDB to provide such financing and requires the Director of the OMB to include in the budget of the Commonwealth submitted annually to the Legislature, for a period of ten fiscal years starting with the budget of fiscal year 2003-2004, the sum of \$50 million plus accrued interest for the repayment of such borrowing. The appropriations shall be made from the product of the sale of public improvement bonds issued during each of said fiscal years. GDB approved a line of credit with aggregate borrowings of \$500 million. Disbursements under this line of credit will also be subject to the regulation. Consequently, as of June 30, 2004, the balance of the line of credit amounted to \$90,917,757.

On December 21, 2004, the Governor of the Commonwealth issued an executive order establishing the creation, through GDB, of an irrevocable trust to guarantee compliance with the abovementioned Joint Resolutions. As established by the order, GDB will fund into the trust the previously unfunded amounts authorized under the Joint Resolutions. The beneficiary of the trust will be SCPT.

**(b) PRASA**

PRASA was managed and operated by Ondeo de Puerto Rico (Ondeo), a subsidiary of Suez. The agreement for the management and operation commenced on July 1, 2002 for a period of 10 years. Under this agreement, PRASA would remain as owner of the property, with control of the rates, the revenues, and the planning of capital improvements and its respective financing. Within the performance of its responsibilities under the contract, Ondeo would supervise PRASA employees

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

and would honor the labor unions contracts with the respective unions. Future negotiations with the labor unions require ratification from the board of directors of PRASA.

As of January 13, 2004, PRASA and Ondeo entered into a Resolution Agreement pursuant to which the parties agreed, effective as of January 15, 2004 to settle certain outstanding and potential claims in connection with the Service Agreement and terminate and mutually release each other in respect of certain of their rights and obligations under the service agreement.

As established in the Resolution Agreement, PRASA and Ondeo entered in the Transition Service Agreement to provide for the operation and management of the Managed Assets on a transitional basis from January 15, 2004 to March 31, 2004. During the transition period, Ondeo should perform at all times: (1) the obligations under the Service Contract except to the extended terminated of modified by the Resolution Agreement; (2) cooperation with PRASA in the transfer of complete control over the Managed Assets by March 31, 2004, and (3) services required to bring certain Managed Assets into compliance with applicable laws.

As established in the Resolution Agreement, PRASA agreed to reimburse to Ondeo the amount of \$29.4 million associated with an early retirement program established by Ondeo during the period in which PRASA was operated by them. Such amount represents the estimated future savings to the early retirement of 540 employees of PRASA.

(c) **PRHTA**

During 2001, a number of contractors presented claims related to the PRHTA's Urban Train project. These contractors' claims, which are at various stages of analysis to reach a final resolution, amount to \$289 million. From this amount, \$166 million have been categorized as merited claims and recorded as accounts payable. The outstanding balance of these claims as of June 30, 2004 amounted to approximately \$49 million.

(d) **PREPA**

In June 2004, the Office of the Comptroller of the Commonwealth of Puerto Rico issued a report stating that PREPA overcharged its clients by approximately \$49.8 million and should reimburse this amount to such clients. After this report was made public, two lawsuits were filed by clients of PREPA against PREPA demanding the reimbursement of such alleged overcharges.

(e) **PRIFA**

The law that created PRIFA (as amended) requires that the first \$70 million up to fiscal year 2023 of federal excise taxes received by the Commonwealth be transferred to PRIFA for deposit to PRIFA's infrastructure fund (the Infrastructure Fund). Federal excise taxes consist of taxes received by the Commonwealth from the United States in connection with rum and other articles produced in Puerto Rico and sold in the United States that are subject to federal excise tax.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

A related trust agreement requires PRIFA to deposit to the credit of a sinking fund the federal excise taxes and other moneys deposited to the credit of the Infrastructure Fund in such amounts as are required to meet debt service requirements with respect to the bonds. Rum is the only article currently produced in Puerto Rico subject to federal excise tax, the proceeds of which are required to be transferred from the federal government to the Commonwealth.

The federal excise taxes securing the bonds are subject to a number of factors, including the continued imposition and remittance of such taxes to the Commonwealth and conditions affecting the Puerto Rico rum industry. If the federal excise taxes received by the Commonwealth in any fiscal year are insufficient to deposit the amount required by the act into the Infrastructure Fund, the act requires that PRIFA request and the director of the OMB include in the annual budget of the Commonwealth for the corresponding fiscal year an appropriation necessary to cover such deficiency. The Commonwealth's Legislature, however, is not legally obligated to make the necessary appropriation to cover such deficiency.

*(f) PRTA*

PRTA, through its subsidiary PRTA Holdings, holds shares of Telecomunicaciones de Puerto Rico, Inc. (TELPRI). TELPRI is the Puerto Rico corporation that was organized for the purpose of acquiring the stock of Puerto Rico Telephone Company (PRTC) and Celulares Telefónica (CT) from PRTA in connection with the sale transaction of March 2, 1999, where a subsidiary of Verizon, Popular, Inc., and TELPRI's employee stock ownership plan acquired 57% of TELPRI and completed the privatization of PRTC and CT. It is contemplated that all shares of TELPRI held by PRTA Holdings will be sold in public offerings and private placements, and all dividends and proceeds received from the sale of the shares will be distributed to the ERS.

Verizon delivered a notice of claim for indemnity to PRTA related to certain alleged actions of PRTA that occurred before the closing of the sale transaction described above. The amount of indemnity sought by Verizon is approximately \$105 million, related to several matters including PRTC's exposure to a potential reduction in tariffs or required rebate to clients as a result of an adverse decision by the Federal Communications Commission (FCC) on a regulatory matter. The FCC's decision has been appealed by PRTC and is awaiting a determination by the FCC. Additionally, in connection with the privatization, the PRTA agreed to indemnify, defend, and hold TELPRI harmless for specified litigation in excess of \$50 million in the aggregate.

On March 2, 1999, PRIFA received \$1.2 billion in connection with the sale of certain assets of PRTA, which were deposited in a corpus account, which principal may not be reduced for any reason, and that income received from the investment of moneys in a corpus account and other moneys received may be deposited in additional accounts. Moneys deposited in the additional accounts are to be used first to pay the principal and interest of any bonds outstanding or to be issued by PRIFA and then for the expansion, development, and modernization of infrastructure related to the aqueduct and sewer systems of Puerto Rico.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

**(g) UPR**

UPR participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-profit Organizations*, or to compliance audits by grantor agencies. The resolution of certain previously identified questioned costs has not occurred. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although UPR expects such amounts, if any, to be immaterial.

**(h) PCSDIPRC**

PCSDIPRC provides insurance coverage over the stocks and deposits of all the cooperatives and the Federation of Cooperatives of Puerto Rico. The deposit base of the cooperatives approximates \$5.8 billion at June 30, 2004.

**(i) PRLA**

At year-end, PRLA had approximately \$44.1 million in accruals to cover the estimated costs related to the liquidation of Sugar Corporation of Puerto Rico, a blended component unit of PRLA, including, among others: employee severance, pending legal cases, environmental clean up costs, refinery repair costs, and estimated future losses to be incurred. Management believes these accruals to be sufficient; however, given the many uncertainties involved, the ultimate outcome cannot be determined with certainty at this time and the actual liquidation costs could be higher or lower than the estimates made.

### ***Environmental Commitments and Contingencies***

The following component units' operations include activities that are subject to state and federal environmental regulations:

- **PREPA** – Facilities and operations of PREPA are subject to regulations under numerous federal and Commonwealth environmental laws, including the Clean Air Act, Clean Water Act, and the National Pollutant Discharge Elimination System (NPDES). In February 1992, the U.S. Environmental Protection Agency (EPA) performed an inspection of various facilities of PREPA and became aware of deficiencies in different areas, principally air opacity; water quality; spill prevention control and countermeasures; and underground storage tanks. As a result, PREPA agreed to, among other things, make certain capital improvements, undertake supplemental environmental projects (SEPs), and use fuel oil not exceeding certain predetermined levels of sulfur, vanadium, and asphalt in its content.
- **PRASA** – Facilities and operations of PRASA's water and sewer system are subject to regulation under numerous federal and Commonwealth environmental laws. Under agreements with the federal government, acting on behalf of EPA, PRASA, and the Commonwealth, are subject to consent decrees to enforce compliance with environmental laws. Accordingly, PRASA has assessed stipulated

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

noncompliance penalties. During the year ended June 30, 2004, such penalties amounted to \$1.5 million. In addition, PRASA has committed to perform environmental projects, in lieu of penalties, in the amount of \$2 million as of June 30, 2004.

- **PRSWA** – PRSWA is currently involved in the implementation and development of the Infrastructure Regional Plan for Recycling and Disposal of Solid Waste in Puerto Rico. As of June 30, 2004, PRSWA has no insurance coverage for environmental risks and management believes that, at this time, there is no sufficient information available to determine the potential amount of related losses, if any, and no provision for losses has been made in the PRSWA's financial statements. Nevertheless, preventive infrastructure has been constructed to minimize any possible impact or events that occur. In addition, operational plans have been developed to incorporate good maintenance practices.
- **PRLA** – PRLA was named a potential responsible party (PRPs) along with the Municipality of Juncos and other third parties for investigation and clean up costs under federal remediation laws for the contamination of the Juncos Landfill superfund site. On August 21, 2001, the U.S. Department of Justice (DOJ) proposed that the PRPs pay a total of \$5,500,000 in settlement of EPA past cost claims, through November 2000, land penalty and punitive damages claims relating to prior alleged noncompliance. A separate final agreement has been reached between PRLA and the Commonwealth of Puerto Rico Housing and Improvement Administration of which PRLA will disburse \$227,500 and the Commonwealth of Puerto Rico Housing and Improvement \$422,500 of the total agreed amount of the public sector PRP's amounting to \$650,000. EPA and DOJ signed settlement documents in August 2004. The execution of this settlement is pending to be performed. The separate agreement between the public sector PRP does not alter or modify the obligations assumed by both agencies with the U.S. government. Therefore, in the unlikely event of default by the Commonwealth of Puerto Rico Housing and Improvement Administration, PRLA would be liable for payments of \$650,000. Management, after consulting with its legal counsel is of the opinion that this will not occur.
- **PRIDCO** – Financial responsibility for clean up costs has been and/or is being undertaken by the industrial potential responsible parties (PRPs) at the two Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA) sites (Vega Alta and Guayama), where the federal government named PRIDCO as a PRP solely for being a part owner of both sites. PRIDCO's participation in the site remediation efforts to date has been limited to providing in-kind support to the industrial PRP's implementation of the clean up programs and, consequently, has not involved any cash disbursements to the federal government or the industrial PRP groups. Under CERCLA and its regulations, liability for the clean up costs and damage to natural resources and any assessment of health effects may be imposed on the present and past owners or operators of a facility from which there was a release of hazardous substances. In addition, any person who arranged for the disposal or treatment of hazardous substances at a site from which there was a release may also be liable.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### *Construction Commitments*

As of June 30, 2004, the following component units maintained various unspent construction agreements as follows (expressed in thousands):

Puerto Rico Highway and Transportation Authority	\$	896,315
Special Communities Perpetual Trust		357,557
Puerto Rico Electric Power Authority		212,200
Puerto Rico Aqueduct and Sewer Authority		209,065
Puerto Rico Solid Waste Authority		110,822
Puerto Rico Convention Center District Authority		108,067
University of Puerto Rico		87,033
Puerto Rico Ports Authority		86,416
Puerto Rico Industrial Development Company		46,000
Puerto Rico Public Broadcasting Corporation		9,573
Puerto Rico Exports Development Corporation		7,247
Cardiovascular Center Corporation of Puerto Rico and the Caribbean		2,753
Fine Arts Center Corporation		1,618
Puerto Rico Conservatory of Music Corporation		1,460
Institutional Trust of the National Guard of Puerto Rico		835
Puerto Rico Infrastructure Financing Authority		227
Total	\$	<u>2,137,188</u>

### **(19) Retirement Systems**

The Commonwealth sponsors three contributory pension plans (collectively known as the Retirement Systems), which are reported in the accompanying statement of fiduciary net assets:

- Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities
- The Puerto Rico Judiciary Retirement System
- Puerto Rico System of Annuities and Pensions for Teachers

Each system is independent; thus their assets or liabilities may not be transferred from one system to another or used for any purpose other than to benefit the participants of each system.

The Retirement Systems issue financial reports, which are publicly available and include the basic financial statements, the required trend information, and any other required supplementary information.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

These reports may be obtained by written request to the corresponding retirement system administrator at the addresses detailed in note 1 of each retirement system's basic financial statements.

(a) **ERS**

**Plan Description**

The ERS is the administrator of a single-employer (as related to the Commonwealth financial reporting entity) defined-benefit pension plan sponsored by the Commonwealth. ERS was created under Act No. 447 (the Act), approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers substantially all full-time employees of: (1) the Commonwealth's primary government and (2) certain municipalities of Puerto Rico and certain component units of the Commonwealth not having their own retirement systems. Appointed and temporary Commonwealth employees become plan members upon their date of employment. Plan members are eligible for a retirement annuity upon reaching the following age:

Police and Firemen	Other employees
50 with 25 years of credited services	55 with 25 years of credited services
58 with 10 years of credited services	58 with 10 years of credited services

Plan members are eligible for merit annuity with a minimum of 30 years or more of credited service.

On the coordinated plan, a participating employee contributes a 5.775% of the monthly salary for the first \$550 and 8.275% for the excess over \$550. By the time the employee reaches 65 years of age and begins to receive Social Security benefits, the pension benefits are reduced by the following:

- \$165 per month if retired with 55 years of age and 30 years of credited service
- \$110 per month if retired with less than 55 years of age and 30 years of credited service
- All other between \$82 and \$100 per month
- Disability annuities under the coordinated plan are also adjusted at age 65 and in some cases are reduced over \$165 per month.

On the noncoordinated plan, the participating employee contributes 8.275% of the monthly salary and does not have any change on the pension benefits upon receipt of Social Security benefits.

Death benefits are divided into occupational, nonoccupational and postretirement. Under the occupational benefits a surviving spouse may receive an annuity equal to 50% of the participating employee's salary at the date of death and each child may receive \$10 per month for minor, or student, up to a maximum benefit per family of 100% of the participating employee's salary at the date of death. Under the nonoccupational benefits, the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of death are paid. Under the postretirement benefit, the beneficiary with a surviving spouse age 60 or over and child 18

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

or under receive up to 30% of the retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$750.

On September 24, 1999, an amendment to the Act, which created ERS, was enacted to establish a defined contribution plan known as System 2000.

System 2000 became effective on January 1, 2000. Employees participating in the defined benefit plan system at December 31, 1999, had the option to either stay in the defined benefit plan or transfer to System 2000. Persons employed on or after January 1, 2000, are only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of plan assets, which will be invested by ERS, together with those of the defined benefit plan. Benefits at retirement age will not be guaranteed by the Commonwealth. The annuity will be based on a formula which assumes that each year the participants' contributions (with a minimum of 8.275% of the participants' salary up to a maximum of 10%) will be invested as instructed by the participant in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Notes; (2) earn a rate equal to 75% of the return of ERS's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The sponsors' contributions (9.275% of the participants' salary) will be used to fund the defined benefit plan.

System 2000 reduces the retirement age from 65 years to 60 for those employees who joined the original plan on or after January 1, 2000.

### **Funding Policy**

Contribution requirements, which are established by law and are not actuarially determined, are as follows:

Commonwealth and other sponsors	9.275% of applicable payroll
Participants:	
Hired on or before March 31, 1990	5.775% of monthly gross salary up to \$550
	8.275% of monthly gross salary in excess of \$550
Hired on or after April 1, 1990	8.275% of monthly gross salary

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

**(b) JRS**

**Plan Description**

The JRS is a single-employer defined benefit plan, which is also administered by the ERS. The system was created under Act No. 12, approved on October 19, 1954. Membership is made up of all judges of the Judicial Branch of the Commonwealth.

The system provides retirement as well as death and disability benefits. Benefits vest after 10 years of service and upon reaching 60 years of age.

Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the last month of compensation. The retirement annuity, for which the plan participant is eligible, is limited to a minimum of 25% and a maximum of 75% of the average compensation, except for judges of the Supreme Court for whom the annuity is limited to a minimum of 50% and a maximum of 100% of the average compensation.

Death benefits are divided into occupational, nonoccupational, and postretirement. Under the occupational benefits, a surviving spouse may receive an annuity equal to 50% of the participating employee's salary at the date of death and each child may receive \$10 per month for each child, minor, or student, up to a maximum benefit per family of 75% of the participating employee's salary at the date of death. Under the nonoccupational benefits, the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of death is paid. Under the postretirement benefit, the beneficiary with surviving spouse age 60 or over and child 21 or under receive up to 60% of the retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$500.

During 1997, JRS enacted Act No. 177 which provides, effective January 1, 1999, for increases of 3%, every three years, of the pension benefits paid by JRS to those plan participants with three or more years of retirement.

**Funding Policy**

All participants are required to make contributions to the plan equal to 8% of the applicable payroll. The Commonwealth, as sponsor, must contribute 20% of the applicable payroll. Contributions are established by law and are not actuarially determined.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

(c) **TRS**

**Plan Description**

The TRS is a single-employer defined plan sponsored by the Commonwealth. All active teachers of the Department of Education of the Commonwealth are covered by the system under the terms of Act No. 91 of March 29, 2004 that superseded Act No. 218 of 1951. Licensed teachers working in private schools may also participate in the system as long as the required employer and employee contributions are satisfied.

The plan provides retirement, death, and disability benefits. Benefits vest after completion of a given number of years of credited service based on age. Benefits are determined by the application of stipulated benefit ratios to the members' average compensation. Average compensation is computed based on the highest three years of compensation recognized by TRS.

The annuity for which a plan member is eligible is limited to a minimum of \$300 per month and a maximum of 75% of the average compensation.

**Funding Policy**

Effective January 27, 2000, participant contributions were increased to 9% of their compensation, as provided by Act No. 45 of 2000. The Commonwealth, as sponsor, matches the participants' contributions at a rate of 8.5% of the applicable payroll. Contribution rates are established by law and are not actuarially determined.

Other relevant information on the Commonwealth's Retirement Systems is presented below (as of July 1, 2003, latest valuation date):

**Membership**

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>	<u>Total</u>
Retirees and beneficiaries currently receiving benefits	88,518	338	28,046	116,902
Current employees	<u>161,947</u>	<u>336</u>	<u>50,723</u>	<u>213,006</u>
Total	<u>250,465</u>	<u>674</u>	<u>78,769</u>	<u>329,908</u>

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

***Annual Pension Cost and Net Pension Obligation (Asset)***

The Commonwealth's annual pension cost and net pension obligation (asset) of the three pension plans for the year ended June 30, 2004, were as follows (expressed in thousands):

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>	<u>Total</u>
Annual required contributions	\$ 578,387	8,707	217,002	804,096
Interest on net pension obligation (asset)	284,347	(1,262)	35,236	318,321
Adjustment to annual required sponsors' contributions	<u>(210,482)</u>	<u>935</u>	<u>(33,070)</u>	<u>(242,617)</u>
Annual pension cost	652,252	8,380	219,168	879,800
Statutory sponsors' contributions made	<u>(344,889)</u>	<u>(5,556)</u>	<u>(150,957)</u>	<u>(501,402)</u>
Increase in net pension obligation	307,363	2,824	68,211	378,398
Net pension obligation (asset) at beginning of year	<u>3,345,254</u>	<u>(14,845)</u>	<u>456,559</u>	<u>3,786,968</u>
Net pension obligation (asset) at end of year	<u>\$ 3,652,617</u>	<u>(12,021)</u>	<u>524,770</u>	<u>4,165,366</u>

The net pension obligation for ERS and TRS, and the net pension asset of JRS of \$4,177 million and \$12 million, respectively, are recorded in the accompanying statement of net assets.

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

The annual required contribution was determined by actuarial valuations for each of the pension plans as described below:

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>
Date of latest actuarial valuation	July 1, 2003	July 1, 2003	July 1, 2003
Actuarial-cost method	Projected unit credit cost	Projected unit credit cost	Entry age normal
Amortization method	Level percentage of pay	Level percentage of the projected payroll	Level percentage closed 5% payroll increase per year
Remaining amortization period	23 years	23 years	17 years
Amortization approach	Closed	Closed	Closed
	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>
Asset-valuation method	Market value	Market value	Market value
Actuarial assumptions:			
Inflation	3.5%	3.5%	3.5%
Investment rate of return	8.5%	8.5%	8.0%
Projected salary increases per annum	5.0%	5.0%	5.0%
Cost-of-living adjustments	None	None	None

***Three-Year Trend Information***

The three-year trend information is as follows (expressed in thousands):

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>
<b>Annual pension cost (APC)</b>			
Year ended June 30, 2004	\$ 652,252	8,380	219,168
Year ended June 30, 2003	860,082	6,464	176,237
Year ended June 30, 2002	860,082	6,464	176,237
<b>Percentage of APC contributed</b>			
Year ended June 30, 2004	52.9%	66.3%	68.9%
Year ended June 30, 2003	38.4%	85.6%	70.4%
Year ended June 30, 2002	35.8%	83.7%	70.4%
<b>Net pension obligation (asset)</b>			
Year ended June 30, 2004	\$ 3,652,617	(12,021)	524,770
Year ended June 30, 2003	2,815,576	(15,773)	404,474
Year ended June 30, 2002	2,263,722	(16,825)	352,388

**COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements

June 30, 2004

***Schedule of Funding Progress (Required Supplementary Information – Unaudited)***

Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (expressed in thousands):

<b>Actuarial valuation date</b>	<b>Actuarial value of assets</b>	<b>Actuarial accrued liability (AAL)</b>	<b>Unfunded AAL (UAAL)</b>	<b>Funded ratio</b>	<b>Covered Payroll</b>	<b>UAAL as a percentage of covered payroll</b>
July 1, 2003	\$ 1,947,000	11,191,000	9,244,000	17%	\$ 3,334,000	277%
July 1, 2001	2,429,000	9,881,000	7,452,000	25%	2,549,000	292%
July 1, 2000	2,042,000	9,459,000	7,418,000	22%	2,463,000	301%

The Puerto Rico Judiciary Retirement System (expressed in thousands):

<b>Actuarial valuation date</b>	<b>Actuarial value of assets</b>	<b>AAL</b>	<b>UAAL</b>	<b>Funded ratio</b>	<b>Covered Payroll</b>	<b>UAAL as a percentage of covered payroll</b>
July 1, 2003	\$ 67,800	166,700	105,000	37%	\$ 25,700	408%
July 1, 2001	70,100	162,200	92,100	43%	26,700	345%
July 1, 2000	82,800	135,800	53,000	61%	25,700	206%

Puerto Rico System of Annuities and Pensions for Teachers (expressed in thousands):

<b>Actuarial valuation date</b>	<b>Actuarial value of assets</b>	<b>AAL</b>	<b>UAAL</b>	<b>Funded ratio</b>	<b>Covered Payroll</b>	<b>UAAL as a percentage of covered payroll</b>
July 1, 2003	\$ 2,143,000	4,540,000	2,397,000	47%	\$ 1,195,000	201%
July 1, 2002	2,167,000	4,155,000	1,988,000	52%	991,000	201%
July 1, 2001	2,283,000	3,683,000	1,400,000	62%	871,000	161%

On August 12, 2000, Act No. 174 was approved to allow certain ERS participants to be eligible for early retirement upon attaining at least age 55 with 25 years of service, provided they made their election on or before April 1, 2001. Those who elected early retirement under this law will receive monthly benefits of 75% (if 25 or more years of service and age 55, or 30 or more years of service and age 50) or benefits of 65% (if 25 years of service by less than age 55) of their average compensation which is computed based on the highest 36 months of compensation recognized by ERS. In these cases, the sponsor is responsible for

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

contributing to ERS amounts to cover the benefit payments and the sponsor contribution with respect to the participants covered until the participants reach the normal retirement age.

### (20) Subsequent Events

#### *Primary Government*

The Additional Lottery receives ticket sales services, software, equipment, office space, and marketing and promotion services through an agreement with an outside service provider. This agreement provides for a weekly fee payment to the service provider based on a volume of retailer's ticker sales within a range of terminals in operations. Effective March 17, 2005, a new outside service provider was appointed for a term of seven (7) years.

On September 24, 2004, the Commonwealth issued \$535 million of General Obligation Bonds consisting of \$441 million of 2005 Series A Public Improvement Bonds and \$94 million of 2005 Series B Public Improvement Bonds. The proceeds from these bonds will be used to provide funds to carry out the capital improvement programs authorized by the Commonwealth Legislature. The 2005 Series A Public Improvement Bonds will bear interest rates ranging from 1.95% to 5%, payable each July 1 and January 1. The principal is payable each July 1 beginning on July 1, 2014 through July 1, 2025.

On September 24, 2004, the Commonwealth issued \$800 million tax and revenue anticipation notes for the purpose of funding a portion of the projected cash flow requirements of the general fund in fiscal year 2005, which requirements result from timing differences between expected disbursements and receipts of taxes and other revenue. The notes are due on June 30, 2005, and bear an annual interest rate of 3%.

Effective on July 29, 2004, the Additional Lottery transferred approximately \$200 million to the Department of the Treasury of the Commonwealth under Act No. 171 of July 29, 2004.

On July 28, 2004, PBA executed a credit facility with GDB for the interim financing of its capital improvement program in an amount not to exceed \$256 million, bearing interest at 1.50% over the cost of tax-exempt commercial paper issued by GDB. The loan is due on July 31, 2006 and will be payable from the proceeds of bonds to be issued by PBA pursuant to the provision of Section 208 of Resolution No.468.

On July 28, 2004, PBA entered into an agreement with the Puerto Rico Courts Administration, for the collection of rent due to PBA aggregating \$18.4 million, to be collected in 5 years plus interest payable at a rate of 2.5%.

On July 23, 2004, PBA entered into an agreement with the Department of Education of the Commonwealth (Institute of Technology in Ponce), for the collection of rent due to PBA aggregating \$12 million to be collected in 32 years plus interest payable at a rate of 2.81%. Subsequent to the signing of the agreement, PBA credited to the balance due \$4 million as agreed with OMB of the Commonwealth and reduced the payment period to 15 years.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

### *Component Units*

#### *(a) GDB*

On September 10, 2004, GDB, through its Tourism Development Fund, increased its guarantee on the Coco Beach Golf & Country Club to secure AFICA bonds in the amount of \$7.4 million to be used to finance certain cost overruns related to the construction of the golf course and the club house. These bonds will begin to amortize in 2008; until then, they will accrue \$1.9 million in interest where the total risk exposed by the Tourism Development Fund will amount to \$9.4 million.

On August 18, 2004, and September 30, 2004, GDB sold mortgage loans with an outstanding balance of approximately \$65 million. The net proceeds from the sale of such loans amounted to approximately \$69 million, resulting in a gain on sale of approximately \$4 million.

#### *(b) PRHTA*

On August 25, 2004, GDB approved a line-of-credit agreement to PRHTA amounting to \$70 million to finance a portion of PRHTA's construction improvement program. The line-of-credit agreement will expire on June 30, 2006 and the interest will be payable at a monthly variable interest rate plus 150 basis points.

#### *(c) PREPA*

On March 24, 2005, PREPA issued \$993 million Power Revenue Bonds to finance a portion of the cost of various projects under its capital improvement program.

On March 4, 2005, the PREPA started the process of issuing approximately \$500 million Power Revenue Bonds and \$475 million Power Refunding Bonds. The expected issuance date of these bonds is April 2005.

On August 12, 2004, PREPA issued approximately \$320 million Power Revenue Refunding Bonds. The refunding will permit PREPA to realize savings on its debt service requirements on bonds outstanding under the 1974 Agreement.

#### *(d) PRASA*

On November 10, 2004, the U.S. Environment Protection Agency (EPA) notified its intention to deny a request for a waiver from secondary wastewater treatment for PRASA's Ponce Regional Wastewater Treatment Plant. If the proposed waiver is finally denied, EPA will put PRASA on an enforceable schedule to upgrade the plant at a secondary waste water treatment level. The final determination of EPA has not been issued.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2004

Subsequent to June 30, 2004, labor union employees declared a strike, which extended for 84 days. At the conclusion of the strike, the labor union and the PRASA reached an agreement on a new labor contract.

Subsequent to June 30, 2004, GDB approved a line-of-credit agreement amounting to \$325 million to be used for the purchase of generators of electricity and/or alternative projects to address the situation of electricity failure in the filtration and pump plants. Such line of credit is guaranteed by the Commonwealth.

*(e) AFICA*

On August 3, 2004, Act 185 amended Act 351 of September 2, 2000, known as the Convention Center District Authority Act, to transfer the rights and title of the Coliseum of Puerto Rico Jose Miguel Agrelot to the Puerto Rico Convention Center District Authority (PRCCADA). Its current debt will be refinanced with a new bond issue and will be assumed by PRCCADA. On August 28, 2004, the Coliseum was completed and transferred to PRCCADA.

*(f) PRIFA*

On August 26, 2004, PRIFA entered into a loan agreement with GDB related to a nonrevolving line of credit in an amount not to exceed \$125 million for the acquisition, construction, equipping, installation, and development of various infrastructure projects for municipalities, public corporations, political subdivisions, and Commonwealth's instrumentalities included within the PRIFA's Capital Improvements Program for fiscal year 2004-2005. The principal amount of the loan is due and payable on June 30, 2005.

*(g) PRPA*

On December 16, 2004, PRPA obtained financing under a line-of-credit agreement with GDB for \$48.8 million with interest payable at a rate of 1.25% over LIBOR, due on December 16, 2006. Proceeds will be used for construction purposes.

In September 2004, PRPA refinanced all its debt with GDB with a \$317 million loan, payable in monthly installments of \$1.3 million plus interest payable at 1.25% over LIBOR and due on October 1, 2024.

In July 2004, PRPA transferred the Mayaguez port to "La Comision del Puerto de Mayaguez." The transfer includes property, utilities, and operations but excludes control over the navigation and maritime traffic of said port.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2004

**(h) PRLA**

On October 11, 2004, the Superior Court in San Juan resolved in behalf of the PRLA that all personal and real property are exempt from the payment of property taxes to the CRIM (Centro de Recaudaciones e Ingresos Municipales) since 1979, when the operations in the proportional benefits farms finalized and established the reimbursement of all property taxes paid to the CRIM since 1979.

**(i) PRTA**

On December 23, 2003, PRTA reached a settlement agreement with TI Holding and TISA by which the Authority agreed to withdraw and cancel the notice of the put option of its shares of TUPPR sent to TI Holding, and to cancel the put option set forth in Section 8 of the stockholders' agreement. Additionally, PRTA will retain the shares held by it representing its 85.1% interest in TUPR. The parties agree that the total consideration payable to PRTA by TISA in connection with the agreement is \$13.5 million and TI Holding will transfer to PRTA its 14.9% interest in TUPR. As of said date the stockholders' agreement dated December 22, 1992 by and between the Authority and TI Holding terminated and has no further force and effect.

In June 2004, subsequent to PRTA's fiscal year-end, PRTA transferred to the Commonwealth the proceeds of such transaction (\$13.5 million) pursuant to Act No. 132 approved on June 17, 1999.

**COMBINING, INDIVIDUAL FUND  
FINANCIAL STATEMENTS AND SCHEDULES**

## **GENERAL FUND**

The general fund is the primary operating fund of the Commonwealth. The general fund is used to account for resources traditionally associated with government, which are not required legally or by sound financial management to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, education, and economic development. Following is the supplemental schedule of expenditures – budget and actual – general fund.

COMMONWEALTH OF PUERTO RICO

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2004  
(In thousands)

	Original budget	Final budget	Actual	Variance
Expenditures:				
Current:				
General government:				
Senate of Puerto Rico	\$ 36,713	32,835	32,835	–
House of Representatives of Puerto Rico	46,141	41,384	41,928	(544)
Commissions	850	850	850	–
Comptroller’s Office	40,061	38,611	37,136	1,475
Governor’s Office	5,589	3,378	5,650	(2,272)
Office of Management and Budget	35,925	40,427	47,384	(6,957)
Planning Board	11,740	11,282	11,282	–
Constructions and Land Subdivisions Appeals Board	1,531	1,372	1,375	(3)
Department of State	10,007	10,182	10,142	40
Department of the Treasury	166,769	159,570	178,416	(18,846)
Central Office of Personnel Administration	6,395	6,296	6,283	13
Commonwealth Elections Commission	46,741	45,796	46,102	(306)
Federal Affairs Administration	10,367	10,359	10,359	–
General Services Administration	2,579	3,027	2,696	331
Municipal Complaints Hearing Commission	4,940	4,536	4,370	166
Civil Rights Commission	1,204	1,175	869	306
Office of the Citizens Ombudsman	3,947	3,445	3,656	(211)
Rules and Permits Administration	2,000	1,898	1,986	(88)
Commonwealth’s Commission to Settle Municipal Complaints	262	250	250	–
Legislative Affairs Office	775	775	521	254
Commission for the Public Service Worker Relations	2,295	2,191	2,189	2
Government Ethics Board	9,505	9,208	9,208	–
Legislative Affairs Office	11,203	8,528	8,440	88
Office of the Superintendent of the Capitol	8,044	8,044	8,572	(528)
Comptroller’s Special Reports Joint Commission	684	670	680	(10)
Legislative Donation Commission	800	781	569	212
Coordination Office for Special Communities of Puerto Rico	9,302	9,145	9,062	83
Public Affairs	7,574	6,626	6,614	12
Governor’s Secretary Office	13,359	14,766	14,766	–
Total general government	497,302	477,407	504,190	(26,783)
Public safety :				
Puerto Rico General Court of Justice	243,666	243,666	241,386	2,280
State Civil Defense Agency	40	40	–	40
Commission of Investigation, Processing, and Appeals Board	754	718	715	3
Department of Justice	136,763	131,051	124,527	6,524
Puerto Rico Police Department	663,065	647,000	652,568	(5,568)
Puerto Rico Firefighters Corps	55,280	53,938	54,015	(77)
Puerto Rico National Guard	8,890	8,889	8,810	79
Public Service Commission	10,220	10,218	10,218	–
Consumer Affairs Department	13,433	13,015	12,906	109
Juvenile Institutions Administration	84,756	84,751	85,168	(417)
Corrections Administration	350,519	331,453	339,471	(8,018)
Department of Correction and Rehabilitation	4,515	4,240	4,233	7
Natural Resources Administration	30,841	30,851	30,849	2
Parole Board	3,389	3,351	3,363	(12)
Forensic Sciences Institute	12,058	10,588	10,588	–
Special Prosecutor Panel	2,017	1,970	1,970	–
Pre-Trial Services Office	4,971	4,756	4,717	39
Correctional Health	85,448	78,900	78,900	–
Medical Emergencies Service	22,678	22,678	25,262	(2,584)
Total public safety	\$ 1,733,303	1,682,073	1,689,666	(7,593)

COMMONWEALTH OF PUERTO RICO

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2004  
(In thousands)

	Original budget	Final budget	Actual	Variance
<b>Health:</b>				
Environmental Quality Board	\$ 8,426	10,287	10,287	–
Department of Health	175,078	148,329	237,157	(88,828)
Mental Health and Drug Addiction Services Administration	96,292	104,329	105,523	(1,194)
Drug Control	1,978	1,924	1,720	204
Cardiovascular Center Corporation of Puerto Rico and the Caribbean	30,000	30,000	30,000	–
Solid Waste Authority of Puerto Rico	6,533	6,533	6,533	–
Puerto Rico Health Insurance Administration	970,895	970,704	977,716	(7,012)
<b>Total health</b>	<b>1,289,202</b>	<b>1,272,106</b>	<b>1,368,936</b>	<b>(96,830)</b>
<b>Public housing and welfare:</b>				
Rural Housing Administration	8,464	8,617	8,617	–
Puerto Rico Volunteers Service Corps	11,980	11,979	11,977	2
Department of Labor and Human Resources	6,884	6,685	6,724	(39)
Labor Relations Board	1,409	1,347	1,347	–
Department of Housing	9,173	9,182	36,888	(27,706)
Department of Recreation and Sports	42,059	42,409	41,967	442
Administration for the Horse Racing Sport and Industry	3,253	3,252	3,252	–
Women’s Affairs Commission	5,482	5,283	3,700	1,583
Public Housing Administration	2,272	2,290	2,290	–
Office of the Veteran’s Ombudsman	1,444	1,367	1,358	9
Department of Family	38,889	47,671	47,463	208
Family and Children Administration	122,051	121,059	139,979	(18,920)
Child Support Administration	9,194	9,117	9,116	1
Vocational Rehabilitation Administration	18,804	17,989	17,989	–
Social Economic Development Administration	89,676	87,368	121,176	(33,808)
Office of the Disabled Persons Ombudsman	2,937	2,600	2,601	(1)
Office for Elderly Affairs	3,664	3,664	3,597	67
Communities Rehabilitation Administration	5,600	6,037	6,027	10
Patient Ombudsman	5,067	4,932	4,909	23
Office of the General Auditor-Department of Family	551	411	411	–
Institutional Trust of the National Guard of Puerto Rico	495	495	495	–
Right to Employment Administration	22,916	22,916	22,916	–
Cantera’s Península Integral Development Company	192	192	192	–
Puerto Rico Housing Finance Authority	5,668	5,668	5,668	–
Industries for the Blind, Mentally Retarded, and Other Disabled Persons of Puerto Rico	141	141	141	–
Puerto Rico Infrastructure Financing Authority	31,618	31,618	31,618	–
Administration for the Care and Development of the Childhood	1,181	1,181	4,030	(2,849)
<b>Total public housing and welfare</b>	<b>451,064</b>	<b>455,470</b>	<b>536,448</b>	<b>(80,978)</b>
<b>Education:</b>				
Department of Education	1,750,658	1,628,201	1,930,595	(302,394)
State Office for Historic Preservation	2,030	1,871	4,377	(2,506)
General Education Council	2,138	2,080	2,070	10
Athenaeum of Puerto Rico	560	560	560	–
Institute of Puerto Rico Culture	33,453	32,815	31,315	1,500
Plastic Arts School	2,885	2,585	2,586	(1)
University of Puerto Rico	710,784	710,344	710,344	–
Musical Arts Corporation	6,703	6,703	6,703	–
Fine Arts Center Corporation	3,077	3,077	3,077	–
Puerto Rico Public Broadcasting Corporation	21,438	21,438	21,438	–
Puerto Rico Conservatory of Music Corporation	4,052	3,887	3,887	–
Puerto Rico Higher Education Council	28,131	28,131	28,131	–
Institute of Linguistic Planification	1,000	1,000	–	1,000
<b>Total education</b>	<b>\$ 2,566,909</b>	<b>2,442,692</b>	<b>2,745,083</b>	<b>(302,391)</b>

**COMMONWEALTH OF PUERTO RICO**

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2004  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
<b>Economic development:</b>				
Department of Transportation and Public Works	\$ 63,286	61,851	141,824	(79,973)
Department of Natural and Environmental Resources	1,456	1,496	1,474	22
Department of Agriculture	22,286	22,127	33,175	(11,048)
Department of Economic Development and Commerce	9,411	9,352	6,612	2,740
Cooperative Enterprises Development Administration	3,703	3,492	3,490	2
Cooperative Enterprises Inspector's Office	841	768	768	–
Rural Development Corporation	2,815	2,810	2,768	42
Department of Economic Development and Commerce	3,277	4,734	4,723	11
Energy Affairs Administration	168	164	164	–
Culebra Conservation and Development Authority	491	449	449	–
Puerto Rico Infrastructure Financing Agency	70,576	70,576	70,576	–
Puerto Rico Aqueduct and Sewer Authority	148,952	148,952	148,926	26
Puerto Rico Industrial Development Company	15,333	15,333	15,333	–
Puerto Rico Electric Power Authority	3	15	3	12
Government Development Bank for Puerto Rico	1,005	1,005	1,005	–
Puerto Rico Metropolitan Bus Authority	479	479	479	–
Puerto Rico Maritime Transportation Authority	15,500	15,500	15,500	–
Tourism Company of Puerto Rico	10,794	10,820	10,820	–
Agricultural Services and Development Administration	83,400	83,400	83,400	–
National Parks Company of Puerto Rico	16,507	16,507	16,507	–
Puerto Rico Land Authority	56	56	56	–
Corporation for the Development of the Film Industry in Puerto Rico	1,619	1,436	1,434	2
Puerto Rico Land Administration	128	128	128	–
Port of the Americas Authority	3,700	3,700	3,700	–
Sugar Corporation	8,458	8,458	8,458	–
<b>Total economic development</b>	<u>484,244</u>	<u>483,608</u>	<u>571,772</u>	<u>(88,164)</u>
<b>Intergovernmental:</b>				
Vieques Commissioner's Office	1,254	1,117	1,138	(21)
Appellative Board of the Personnel System Administration	1,636	1,528	1,528	–
Municipal Service Administration	353,677	354,959	354,943	16
<b>Total intergovernmental</b>	<u>356,567</u>	<u>357,604</u>	<u>357,609</u>	<u>(5)</u>
<b>Debt service:</b>				
Principal	51,477	51,477	51,477	–
Interest and other	106,704	106,704	116,734	(10,030)
<b>Total expenditures</b>	<u>\$ 7,536,772</u>	<u>7,329,141</u>	<u>7,941,915</u>	<u>(612,774)</u>
<b>Transfer-out to other funds:</b>				
Senate of Puerto Rico	\$ –	2,662	2,662	–
House of Representatives of Puerto Rico	–	2,986	2,986	–
Comptroller's Office	–	2,280	2,280	–
Puerto Rico General Court of Justice	–	–	7,185	(7,185)
Office of Youth Affairs	3,610	3,464	3,374	90
Office of Management and Budget	146,205	146,229	146,229	–
Planning Board	–	704	704	–
Constructions and Land Subdivisions Appeals Board	–	56	56	–
Department of the Treasury	–	2,617	2,617	–
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	158,208	146,137	146,137	–
Civil Rights Commission	–	306	306	–
Department of Justice	–	3,107	3,107	–
Puerto Rico Police Department	–	13,700	13,700	–
<b>Balance carried forward</b>	<u>\$ 308,023</u>	<u>324,248</u>	<u>331,343</u>	<u>(7,095)</u>

**COMMONWEALTH OF PUERTO RICO**

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2004  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
Balance brought forward	\$ 308,023	324,248	331,343	(7,095)
Department of Transportation and Public Works	–	892	892	–
Department of Agriculture	–	159	159	–
Department of Economic Development and Commerce	–	38	38	–
Office of the Citizen’s Ombudsman	–	87	87	–
Cooperative Enterprises Development Administration	–	10	10	–
Department of Labor and Human Resources	–	165	165	–
Consumer Affairs Department	–	323	323	–
Department of Health	–	26,762	26,762	–
Department of Education	–	123,307	141,663	(18,356)
Teachers’ Pensions Board	28,958	40,409	40,409	–
Mental Health and Drug Addiction Services Administration	–	56	56	–
Corrections Administration	–	19,800	19,800	–
Department of Family	–	557	557	–
Family and Children Administration	–	929	929	–
Child Support Administration	–	30	30	–
Vocational Rehabilitation Administration	–	94	94	–
Social Economic Development Administration	–	1,444	1,444	–
Natural Resources Administration	–	21	21	–
Office of the Disabled Persons Ombudsman	–	9	9	–
Contributions to Political Parties	900	900	900	–
Correctional Health	–	2,973	2,973	–
Legislative Affairs Office	–	2,444	2,444	–
Comptroller’s Special Reports Joint Commission	–	13	13	–
Legislative Donation Commission	–	19	19	–
Administration for the Care and Development of the Childhood	–	123	123	–
Human Resources and Occupational Development Council	300	–	–	–
Office for the Improvements of Public Schools	26,250	26,250	24,722	1,528
Puerto Rico Urban Renewal and Housing Corporation	26,429	26,429	26,429	–
Puerto Rico Maritime Shipping Authority	24,205	24,205	15,729	8,476
Department of Treasury – Transfer to debt service	342,538	342,538	342,538	–
Total operating transfers-out to other funds	\$ <u>757,603</u>	<u>965,234</u>	<u>980,681</u>	<u>(15,447)</u>

## NONMAJOR GOVERNMENTAL FUNDS

### *Special Revenue Funds*

Special revenue funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditure for specific purposes.

**Public Buildings Authority Special Revenue Fund:** The operating fund of a blended component unit used to account for the operation, maintenance, equipment replacement and other extraordinary operation and maintenance costs of the buildings and facilities that, when constructed, are leased to the Commonwealth primary government agencies.

### *Debt Service Funds*

The debt service funds are used to account for the accumulation of resources predominantly for, and the payment of, general long-term bonds principal, interest and related costs other than bonds payable from operations of proprietary fund types, pension trust funds and discretely presented component units. Long term debt and interest due on July 1 of the following year are accounted as a fund liability if resources are available as of June 30 for its payment.

**Public Buildings Authority Debt Service Fund:** A blended component unit engaged in the construction and/or acquisition of building facilities for lease mainly to the Commonwealth's primary government agencies. Its debt service fund is used to account for the accumulation of resources for the payment of revenue bonds and other liabilities incurred to finance the construction of the buildings and facilities.

**Puerto Rico Maritime Shipping Authority Debt Service Fund:** This is the remainder of a former shipping company owned by the Commonwealth. Its debt service fund is used to account for the accumulation of resources for the payment of the long-term liability that resulted from the sale of its marine operations. This fund is mainly subsidized from appropriations and operating transfers from the general fund.

**The Children's Trust Debt Service Fund:** The debt service fund of The Children's Trust (a blended component unit) accounts for the accumulation of resources for payment of interest and principal on long term obligations financed with moneys to be received by the Commonwealth from the global settlement agreement signed by certain tobacco companies.

### *Capital Project Funds*

Capital project funds are used to account for the financial resources used for the acquisition or construction of major capital facilities not being financed by proprietary fund types, pension trust funds, and discretely presented component units.

**Commonwealth Public Improvements Funds and Other Funds:** These funds present the activities of the capital improvements program of the Commonwealth, financed with the proceeds of the general obligation bonds.

**COMMONWEALTH OF PUERTO RICO**

Combining Balance Sheet – Nonmajor Governmental Funds

June 30, 2004  
(In thousands)

	Special revenue			Debt service			Capital projects		Total nonmajor governmental funds
	Public Buildings Authority	The Children's Trust	Public Buildings Authority	Puerto Rico Maritime Shipping Authority	Total	Commonwealth of Puerto Rico			
<b>Assets</b>									
Cash and cash equivalents	\$ 34,846	—	—	2,364	2,364	34,702	71,912		
Cash and cash equivalents in governmental banks	7,700	—	—	—	—	427,544	435,244		
Investments	5,639	114,880	—	1,757	116,637	—	122,276		
Receivables, net of allowance for uncollectibles:									
Accounts	13,547	—	—	—	—	1,545	15,092		
Loans	—	—	—	—	—	36	36		
Accrued interest	—	—	—	1	1	—	1		
Due from:									
Other funds	45,536	—	—	—	—	29,893	75,429		
Primary government	—	—	—	—	—	—	—		
Component units	32,613	—	—	—	—	—	32,613		
Restricted assets:									
Cash and cash equivalents	1,000	—	8,051	—	8,051	—	9,051		
Cash and cash equivalents in governmental banks	20,030	—	65,667	—	65,667	—	85,697		
<b>Total assets</b>	<b>\$ 160,911</b>	<b>114,880</b>	<b>73,718</b>	<b>4,122</b>	<b>192,720</b>	<b>493,720</b>	<b>847,351</b>		
<b>Liabilities and Fund Balances</b>									
Liabilities:									
Accounts payable and accrued liabilities	\$ 43,619	—	—	350	350	—	43,969		
Bonds payable	—	—	35,910	—	35,910	—	35,910		
Due to component units	—	—	—	—	—	20,000	20,000		
Interest payable	—	—	31,891	—	31,891	—	31,891		
Other liabilities	—	—	—	978	978	5,654	6,632		
<b>Total liabilities</b>	<b>43,619</b>	<b>—</b>	<b>67,801</b>	<b>1,328</b>	<b>69,129</b>	<b>25,654</b>	<b>138,402</b>		
Fund balances:									
Reserved for:									
Encumbrances	—	—	—	—	—	72,455	72,455		
Unreserved reported in:									
Debt service funds	—	114,880	5,917	2,794	123,591	—	123,591		
Special revenue funds	117,292	—	—	—	—	—	117,292		
Capital projects funds	—	—	—	—	—	395,611	395,611		
<b>Total fund balances</b>	<b>117,292</b>	<b>114,880</b>	<b>5,917</b>	<b>2,794</b>	<b>123,591</b>	<b>468,066</b>	<b>708,949</b>		
<b>Total liabilities and fund balances</b>	<b>\$ 160,911</b>	<b>114,880</b>	<b>73,718</b>	<b>4,122</b>	<b>192,720</b>	<b>493,720</b>	<b>847,351</b>		

COMMONWEALTH OF PUERTO RICO

Combining Statement of Revenue, Expenditures, and Changes in Fund Balances - Nonmajor Governmental Funds

Year ended June 30, 2004  
(In thousands)

	Special revenue			Debt service			Capital projects		Total nonmajor governmental funds
	Public Buildings Authority	The Children's Trust	Public Buildings Authority	Puerto Rico Maritime Shipping Authority	Total	Commonwealth of Puerto Rico			
Revenue:									
Revenue from global settlement agreement	—	70,409	—	—	70,409	—	—	70,409	
Interest and investment earnings	4,403	3,551	—	34	3,585	—	—	7,988	
Other	4,695	—	—	—	—	1,671	—	6,366	
Total revenue	9,098	73,960	—	34	73,994	1,671	—	84,763	
Expenditures:									
Current:									
General government	130,055	—	—	—	—	167,220	—	297,275	
Public safety	—	—	—	—	—	13,710	—	13,710	
Health	—	—	—	—	—	11,419	—	11,419	
Public housing and welfare	—	—	—	—	—	94,459	—	94,459	
Education	—	—	—	—	—	4,109	—	4,109	
Economic development	—	—	—	—	—	219,290	—	219,333	
Intergovernmental	—	—	—	43	43	82,181	—	82,181	
Capital outlays	—	—	—	—	—	43,691	—	43,691	
Debt service:									
Principal	—	11,725	39,329	—	51,054	—	—	51,054	
Interest and other	—	62,294	69,977	14,613	146,884	(239)	—	146,645	
Debt issuance costs	—	—	16,931	3,845	20,776	5,573	—	26,349	
Total expenditures	130,055	74,019	126,237	18,501	218,757	641,413	—	990,225	
Excess of expenditures over revenue	(120,957)	(59)	(126,237)	(18,467)	(144,763)	(639,742)	—	(905,462)	
Other financing sources (uses):									
Transfers in	203,345	—	105,388	15,729	121,117	—	—	324,462	
Transfers out	—	(398)	(43,783)	—	(44,181)	(97,399)	—	(141,580)	
Long-term debt issued	—	—	—	—	—	801,456	—	801,456	
Discount on bonds issued	—	—	—	(697)	(697)	(354)	—	(1,051)	
Refunding bond issued	—	—	708,050	342,660	1,050,710	—	—	1,050,710	
Payment to refunded bond escrow agent	—	—	(682,725)	(338,118)	(1,020,843)	—	—	(1,020,843)	
Total other financing sources (uses)	203,345	(398)	86,930	19,574	106,106	703,703	—	1,013,154	
Net change in excess (deficiency) of revenue and other fund balances (deficit)	82,388	(457)	(39,307)	1,107	(38,657)	63,961	—	107,692	
Fund balances, beginning of year	34,904	115,337	45,224	1,687	162,248	404,105	—	601,257	
Fund balances, end of year	117,292	114,880	5,917	2,794	123,591	468,066	—	708,949	

## NONMAJOR PROPRIETARY FUNDS

Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent of the government is that the costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

**Puerto Rico Water Pollution Control Revolving Fund:** It was created by Act No. 44 on June 21, 1988, as amended. It is administered, pursuant to Act No. 9 of June 18, 1970, as amended, by the Puerto Rico Environmental Quality Board (EQB). Pursuant to such Act, EQB is authorized to enter into operating agreements and capitalization grant agreements with the U.S. Environmental Protection Agency (EPA) for lending activities.

**Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund:** It was created by Act No. 32. It is administered, pursuant to Act No. 9 of June 18, 1970, as amended, by the Puerto Rico Department of Health (DOH). Pursuant to such act, DOH, on behalf of the Commonwealth, is authorized to enter into operating and capitalization grant agreements with the U.S. Environmental Protection Agency (EPA) for lending activities.

**Disability Insurance:** It was created by Act 139 on June 26, 1968. It is used to account for disability benefits to remedy temporarily the loss of income as a consequence of disability caused by sickness or accident unrelated to the employment.

**Drivers' Insurance:** It was created by Act 428 on May 15, 1950. It is used to account for contributions made by the drivers and their employers to provide a social security plan for the benefit of the drivers in Puerto Rico. The plan also includes payment of benefits for health and life insurance.

COMMONWEALTH OF PUERTO RICO

Combining Statement of Net Assets –  
Nonmajor Proprietary Funds

June 30, 2004  
(In thousands)

	<b>Business-type activities – nonmajor enterprise funds</b>				
	<b>Disability insurance</b>	<b>Drivers’ insurance</b>	<b>Puerto Rico Water Control Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
<b>Assets</b>					
Current assets:					
Cash and cash equivalents	\$ –	9,438	–	–	9,438
Cash and cash equivalents in governmental banks	64,562	27,686	33,990	11,858	138,096
Accounts and loans receivable, net:					
Insurance premiums, net	2,414	1,070	–	–	3,484
Component units	–	–	9,192	478	9,670
Accrued interests	331	7	2,364	498	3,200
Other	277	23	91	–	391
Unrestricted investments	34,141	–	–	–	34,141
Total current assets	<u>101,725</u>	<u>38,224</u>	<u>45,637</u>	<u>12,834</u>	<u>198,420</u>
Noncurrent assets:					
Loans receivable, excluding current portion, net:					
Component units	–	–	115,559	27,321	142,880
Intergovernmental	–	–	1,962	–	1,962
Total assets	<u>101,725</u>	<u>38,224</u>	<u>163,158</u>	<u>40,155</u>	<u>343,262</u>
<b>Liabilities and Net Assets</b>					
Current liabilities:					
Accounts payable and accrued liabilities	5,697	424	595	237	6,953
Deferred revenue	–	62	–	–	62
Compensated absences	621	312	–	–	933
Insurance benefits payable	1,020	255	–	–	1,275
Total current liabilities	<u>7,338</u>	<u>1,053</u>	<u>595</u>	<u>237</u>	<u>9,223</u>
Noncurrent liabilities – compensated absences	399	259	–	–	658
Total liabilities	<u>7,737</u>	<u>1,312</u>	<u>595</u>	<u>237</u>	<u>9,881</u>
Net assets:					
Restricted for:					
Payment of insurance benefits	93,988	36,912	–	–	130,900
Capital projects	–	–	162,563	39,918	202,481
Total net assets	<u>\$ 93,988</u>	<u>36,912</u>	<u>162,563</u>	<u>39,918</u>	<u>333,381</u>

COMMONWEALTH OF PUERTO RICO

Combining Statement of Revenue, Expenditures and Changes in Net Assets  
Nonmajor Proprietary Funds

Year ended June 30, 2004  
(In thousands)

	<b>Business-type activities - nonmajor enterprise funds</b>				
	<b>Disability insurance</b>	<b>Drivers' insurance</b>	<b>Puerto Rico Water Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
Operating revenue:					
Insurance premiums	\$ 12,690	5,031	-	-	17,721
Intergovernmental	-	-	-	-	-
Interest	1,767	85	2,463	525	4,840
Total operating revenue	<u>14,457</u>	<u>5,116</u>	<u>2,463</u>	<u>525</u>	<u>22,561</u>
Operating expenses:					
Disability and drivers insurance benefits	3,713	1,205	-	-	4,918
General, administrative and other operating expenses	17,666	2,992	478	709	21,845
Total operating expenses	<u>21,379</u>	<u>4,197</u>	<u>478</u>	<u>709</u>	<u>26,763</u>
Operating income (loss)	<u>(6,922)</u>	<u>919</u>	<u>1,985</u>	<u>(184)</u>	<u>(4,202)</u>
Nonoperating revenue (expenses):					
Contributions from U.S. government	-	-	11,159	3,915	15,074
Interest and investment earnings	(1,877)	-	-	-	(1,877)
Total nonoperating revenue (expenses)	<u>(1,877)</u>	<u>-</u>	<u>11,159</u>	<u>3,915</u>	<u>13,197</u>
Income before transfers	<u>(8,799)</u>	<u>919</u>	<u>13,144</u>	<u>3,731</u>	<u>8,995</u>
Transfers from general fund	-	-	2,211	749	2,960
Net change in net assets (deficit)	<u>(8,799)</u>	<u>919</u>	<u>15,355</u>	<u>4,480</u>	<u>11,955</u>
Net assets, beginning of year	<u>102,787</u>	<u>35,993</u>	<u>147,208</u>	<u>35,438</u>	<u>321,426</u>
Net assets, end of year	<u>\$ 93,988</u>	<u>36,912</u>	<u>162,563</u>	<u>39,918</u>	<u>333,381</u>

COMMONWEALTH OF PUERTO RICO

Combining Statement of Cash Flows  
Nonmajor Proprietary Funds

Year ended June 30, 2004  
(In thousands)

	<b>Business-type activities - nonmajor enterprise funds</b>				
	<b>Disability insurance</b>	<b>Drivers' insurance</b>	<b>Puerto Rico Water Control Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
Cash flows from operating activities:					
Receipts from customers and users	\$ 13,754	5,025	1,241	255	20,275
Payments to suppliers and employees	(11,894)	(2,576)	(34)	(711)	(15,215)
Payments of insurance benefits	(3,605)	(1,153)	—	—	(4,758)
Net cash provided by (used in) operating activities	<u>(1,745)</u>	<u>1,296</u>	<u>1,207</u>	<u>(456)</u>	<u>302</u>
Cash flows from noncapital financing activities:					
Intergovernmental grants and contributions	—	—	10,797	4,081	14,878
Transfers from general fund	—	—	2,211	749	2,960
Net cash provided by noncapital financing	<u>—</u>	<u>—</u>	<u>13,008</u>	<u>4,830</u>	<u>17,838</u>
Cash flows from investing activities:					
Interests received on deposits and investments	1,862	88	—	—	1,950
Principal collected on loans	—	—	3,064	—	3,064
Loans originated	—	—	(13,048)	(4,118)	(17,166)
Net cash provided by (used in) investing activities	<u>1,862</u>	<u>88</u>	<u>(9,984)</u>	<u>(4,118)</u>	<u>(12,152)</u>
Net increase in cash and cash equivalents	117	1,384	4,231	256	5,988
Cash and equivalents, beginning of year	64,445	35,740	29,759	11,602	141,546
Cash and cash equivalents, end of year	<u>\$ 64,562</u>	<u>37,124</u>	<u>33,990</u>	<u>11,858</u>	<u>147,534</u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:					
Operating income (loss)	\$ (6,922)	919	1,985	(184)	(4,202)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
(Increase) decrease in accounts and loans receivable	1,064	(6)	(9,983)	(4,118)	(13,043)
Interests earned on deposits, loans and investments	(1,767)	(85)	8,907	3,848	10,903
Changes in operating assets and liabilities:					
Decrease in other assets	—	—	200	—	200
Increase in deferred revenue	—	32	—	—	32
Increase in compensated absences	399	96	—	—	495
Increase in liability for insurance benefits payable	108	52	—	—	160
Increase (decrease) in accounts payable and accrued liabilities	5,373	288	98	(2)	5,757
Total adjustments	<u>5,177</u>	<u>377</u>	<u>(778)</u>	<u>(272)</u>	<u>4,504</u>
Net cash provided by (used in) operating activities	<u>\$ (1,745)</u>	<u>1,296</u>	<u>1,207</u>	<u>(456)</u>	<u>302</u>

## **FIDUCIARY FUNDS**

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity, or as an agent for individuals, organizations, and other governmental units. Following are the Commonwealth's fiduciary funds:

### ***Pension Trust Funds***

The pension trust funds are used to account for the assets, liabilities, and net assets available for pension benefits held in trust for the public employees of the Commonwealth.

**Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS):** ERS is the administrator of a defined-benefit pension plan which covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and component units not covered by their retirement systems. On September 24, 1999, an amendment to the Law that created ERS was enacted with the purpose of establishing a new defined contribution pension plan (System 2000) for persons joining the government on or after January 1, 2000.

**Puerto Rico System of Annuities and Pensions for Teachers (TRS):** TRS provides retirement benefits to all teachers of the Department of Education of the Commonwealth, all pensioned teachers who work in teachers, who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education. TRS provides retirement, death, and disability benefits.

**Puerto Rico Judiciary Retirement System (JRS):** JRS is administered by the ERS and covers all individuals holding a position as Justice of the Supreme Court, Judge of the former Superior Court, Judge of District Court, or the Municipal Judges of the Commonwealth. The system provides retirement as well as death and disability benefits.

### ***Agency Fund***

Agency fund is used to account for assets held by the government as an agent for individuals, private organizations, and other governments. This fund is custodial in nature (assets equal liabilities) and does not involve measurement of the results of operations.

**Special Deposits:** This fund acts in a fiduciary capacity in order to account for moneys received with specified purposes for which the law does not address any other fund. It mainly includes deposits under the custody of the courts of justice for alimony payments.

COMMONWEALTH OF PUERTO RICO

Combining Statement of Fiduciary Net Assets – Pension Trust Funds

June 30, 2004  
(In thousands)

Assets	Pension Trust Funds			Totals
	Employees' Retirement System (ERS)	Teachers' Retirement System (TRS)	Judiciary Retirement System (JRS)	
Cash and cash equivalents:				
Unrestricted	\$ 12,673	67,113	1,029	80,815
Restricted	—	2,396	—	2,396
Cash and cash equivalents in governmental banks:				
Unrestricted	31,853	—	223	32,076
Restricted	1,140	3,717	—	4,857
Investments:				
Debt and equity securities	1,269,203	1,959,426	69,726	3,298,355
Investment in PRTA Holdings, at appraised value	404,390	—	—	404,390
Other	41,632	43,660	—	85,292
Receivables, net:				
Accounts	47,748	—	—	47,748
Loans and advances	369,203	344,783	212	714,198
Accrued interests and dividends	2,288	5,380	305	7,973
Other	38,662	8,035	72	46,769
Capital assets, net	8,330	24,332	—	32,662
Other assets	7,825	619	—	8,444
Total assets	<u>2,234,947</u>	<u>2,459,461</u>	<u>71,567</u>	<u>4,765,975</u>
<b>Liabilities</b>				
Accounts payable and accrued liabilities	2,842	34,136	—	36,978
Liability for securities lending transactions	90,663	—	3,716	94,379
Bonds payable	—	22,090	—	22,090
Notes payable to component unit	—	240	—	240
Total liabilities	<u>93,505</u>	<u>56,466</u>	<u>3,716</u>	<u>153,687</u>
<b>Net Assets</b>				
Net assets held in trust for pension and other benefits	\$ <u>2,141,442</u>	<u>2,402,995</u>	<u>67,851</u>	<u>4,612,288</u>

**COMMONWEALTH OF PUERTO RICO**

Combining Statement of Changes in Fiduciary Net Assets – Pension Trust Funds

Year ended June 30, 2004

(In thousands)

	Pension Trust Funds			Totals
	Employees' Retirement System (ERS)	Teachers' Retirement System (TRS)	Judiciary Retirement System (JRS)	
Additions:				
Contributions:				
Sponsor	\$ 330,336	110,548	5,556	446,440
Participants	294,013	118,743	2,578	415,334
Special	14,553	40,409	—	54,962
Total contributions	638,902	269,700	8,134	916,736
Interests	43,842	55,878	1,177	100,897
Dividends	6,693	17,264	159	24,116
Net change in fair value of investments, including realized losses on sale and maturities of investments	258,702	240,732	8,093	507,527
Investment expenses	(3,058)	(4,958)	(206)	(8,222)
Net interest and investment income	306,179	308,916	9,223	624,318
Other income	6,813	32,397	—	39,210
Total additions	951,894	611,013	17,357	1,580,264
Deductions:				
Pension and other benefits	698,230	324,611	9,927	1,032,768
Refunds of contribution	19,989	3,432	—	23,421
General and administrative	39,635	22,637	1,360	63,632
Total deductions	757,854	350,680	11,287	1,119,821
Net change in net assets held in trust for pension and other benefits	194,040	260,333	6,070	460,443
Net assets held in trust for pension and other benefits:				
Beginning of year	1,947,402	2,142,662	61,781	4,151,845
End of year	\$ 2,141,442	2,402,995	67,851	4,612,288

**COMMONWEALTH OF PUERTO RICO**

Combining Statement of Changes in Assets and Liabilities – Agency Fund

Year ended June 30, 2004  
(In thousands)

	<b>Balance June 30 0</b>	<b>Additions</b>	<b>Deletions</b>	<b>Balance June 30 0</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 506,200	—	51,446	454,754
Cash and cash equivalents in governmental banks	88,326	2,961,068	2,951,625	97,769
Investments	13,095	9,904	—	22,999
Accounts receivable, net	18,983	80,939	76,487	23,435
Other assets	532	—	—	532
Total assets	\$ 627,136	3,051,911	3,079,558	599,489
<b>Liabilities</b>				
Accounts payable and accrued liabilities	\$ 627,086	3,861,747	3,889,344	599,489
Total liabilities	\$ 627,086	3,861,747	3,889,344	599,489

## **NONMAJOR COMPONENT UNITS**

These entities are presented because the nature and significance of their relationship with the primary government are such that their exclusion would cause the basic financial statements to be misleading. These are discretely presented in a separate column in the general purpose financial statements due to nature of the services they provide. The accounting principles followed by each of the component units included herein may vary depending on the type of industries these are involved (that is, banking, construction, public utilities, and so forth). The detailed information for each of these entities may be obtained directly from the administrative offices of the corresponding entities, as described in note 1, of the basic financial statements included in the financial section of this report.

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Municipal Finance Agency	Puerto Rico Ports Authority	Puerto Rico Industrial Development Company	Automobile Accident Compensation Administration	Puerto Rico Land Administration	National Parks Company of Puerto Rico
Assets:								
Current assets:								
Cash and cash equivalents	2,534	2,570	—	169	39,515	3,077	2,919	359
Cash and cash equivalents in governmental banks	170,897	105	4,191	—	4,504	—	43,007	16,895
Investments, including collateral from securities lending transactions	554,105	247,611	240,573	—	—	230,484	23,826	5,744
Receivables, net:								
Intergovernmental	—	—	—	—	—	—	—	—
Accounts	71,377	—	—	62,952	8,705	3,437	4,598	2,525
Loans and advances	—	51,814	—	—	—	—	—	—
Accrued interest	10,130	5,112	—	—	5,119	1,163	1,433	—
Other governmental entities	—	—	—	—	—	—	—	23
Other	17,384	—	—	—	—	2,466	2,835	—
Due from:								
Primary government	—	—	—	—	—	—	—	—
Component units	3,500	459	—	—	—	—	—	—
Inventories	6,278	—	—	446	—	—	—	—
Prepays	—	—	—	7,107	—	—	—	755
Total current assets	836,205	307,671	244,764	70,674	57,843	240,627	78,618	26,301
Noncurrent assets:								
Restricted assets:								
Cash and cash equivalents	—	—	74	54,394	61,192	—	—	100
Cash and cash equivalents in governmental banks	—	—	—	12,865	29,040	—	—	36,503
Investments and other restricted assets	—	—	1,423,982	—	—	—	—	11,905
Investments	714,966	375,680	—	1,000	32,297	—	—	—
Loans, interest and other receivable	—	104,656	35,964	—	3,936	—	—	—
Due from component units	—	8,719	—	23,645	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—	—	—
Capital assets not being depreciated	13,010	—	—	294,928	252,659	901	167,661	—
Capital assets, depreciable, net	102,100	11,394	—	362,963	455,322	8,442	7,621	21,179
Deferred expenses and other assets	—	4,977	20,846	2,925	9,291	47	3,341	—
Total noncurrent assets	830,076	505,426	1,480,866	752,720	843,737	9,390	184,993	274,739
Total assets	1,666,281	813,097	1,725,630	823,394	901,580	250,017	263,611	301,040

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Puerto Rico Medical Services Administration	Puerto Rico Trade and Export Company	Tourism Company of Puerto Rico	Puerto Rico and Caribbean Cardiovascular Center Corporation	Agricultural Services and Development Corporation	Land Authority of Puerto Rico	Puerto Rico Metropolitan Bus Authority
	\$ 3,068	3,859	104,732	1,765	6	3,407	8,105
Cash and cash equivalents	—	8,476	262	—	—	19,968	632
Cash and cash equivalents in governmental banks	—	—	—	—	—	—	—
Investments, including collateral from securities lending transactions	—	15,887	—	—	—	—	—
Receivables, net:							
Intergovernmental	—	—	—	—	—	—	2,096
Accounts	15,400	994	4,376	14,754	6,762	10,220	—
Loans and advances	—	—	2,189	—	—	162	—
Accrued interest	—	39	—	—	—	—	—
Other governmental entities	55,585	—	—	—	74,450	—	—
Other	—	—	1,787	1,433	1,373	—	2,309
Due from:							
Primary government	—	—	—	—	—	—	—
Component units	—	—	—	—	—	29,571	—
Inventories	4,111	—	—	1,930	13,538	66	7,495
Prepays	—	101	—	540	374	—	—
Total current assets	78,164	29,356	113,346	20,422	96,503	63,394	20,637
Noncurrent assets:							
Restricted assets:							
Cash and cash equivalents	6,237	—	—	1,568	2,184	—	—
Cash and cash equivalents in governmental banks	—	—	—	4,600	391	1,036	3,104
Investments and other restricted assets	—	9,178	—	—	—	—	—
Investments	—	—	10,000	—	—	1,596	—
Loans, interest and other receivable	—	627	1,800	—	—	725	—
Due from component units	—	—	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—	—
Capital assets not being depreciated	7,322	61,523	11,976	1,387	6,359	76,736	2,569
Capital assets, depreciable, net	24,837	35,890	16,363	41,468	28,134	10,274	57,401
Deferred expenses and other assets	—	26	12,015	—	540	—	—
Total noncurrent assets	38,396	107,244	52,154	49,023	37,608	90,367	63,074
Total assets	116,560	136,600	165,500	69,445	134,111	153,761	83,711

**COMMONWEALTH OF PUERTO RICO**

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Puerto Rico Telephone Authority	Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental, Control Facilities Financing Authority	Puerto Rico Solid Waste Authority	Public Corporation for the Supervision and Deposit Insurance of Puerto Rico	Right to Employment Administration	Puerto Rico Public Broadcasting Corporation
<b>Assets:</b>						
<b>Current assets:</b>						
Cash and cash equivalents	—	—	1,795	—	—	2,614
Cash and cash equivalents in governmental banks	404	38,334	415	581	5,470	—
Investments, including collateral from securities lending transactions	—	—	—	82,430	—	—
Receivables, net:						
Intergovernmental	—	—	—	—	262	—
Accounts	—	—	1,505	—	100	443
Loans and advances	—	—	—	—	—	—
Accrued interest	—	14	—	637	—	—
Other governmental entities	—	—	—	—	1,377	485
Other	—	—	—	249	—	15
Due from:						
Primary government	—	—	—	—	—	—
Component units	—	—	—	—	—	—
Inventories	—	—	—	—	—	—
Prepaids	—	—	—	—	8	194
<b>Total current assets</b>	<b>404</b>	<b>38,348</b>	<b>3,715</b>	<b>83,897</b>	<b>7,217</b>	<b>3,751</b>
<b>Noncurrent assets:</b>						
<b>Restricted assets:</b>						
Cash and cash equivalents	—	—	—	—	—	5,108
Cash and cash equivalents in governmental banks	22,140	—	17,630	—	—	—
Investments and other restricted assets	41,798	—	721	—	—	—
Investments	—	—	950	23,667	—	—
Loans, interest and other receivable	57	—	—	—	—	—
Due from component units	—	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—
Capital assets not being depreciated	—	211,119	45,356	—	—	7,329
Capital assets, depreciable, net	—	—	1,407,704	207	462	13,125
Deferred expenses and other assets	—	5	—	—	—	526
<b>Total noncurrent assets</b>	<b>63,995</b>	<b>211,124</b>	<b>205,361</b>	<b>23,874</b>	<b>462</b>	<b>26,088</b>
<b>Total assets</b>	<b>64,399</b>	<b>249,472</b>	<b>209,076</b>	<b>107,771</b>	<b>7,679</b>	<b>29,839</b>

**COMMONWEALTH OF PUERTO RICO**

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Fine Arts Center Corporation	Puerto Rico Maritime Transportation Authority	Puerto Rico Council on Higher Education	Farm Insurance Corporation of Puerto Rico	Employment and Training Enterprise Corporation	Caribbean Basin Projects Financing Authority	Puerto Rico Conservatory of Music Corporation	Musical Arts Corporation
<b>Assets:</b>								
<b>Current assets:</b>								
Cash and cash equivalents	\$ 481	34	—	25	—	—	151	2,806
Cash and cash equivalents in governmental banks	—	—	2,175	—	380	5,189	—	—
Investments, including collateral from securities lending transactions	1,783	—	—	—	—	—	—	—
Receivables, net:								
Intergovernmental	—	—	—	—	—	—	—	—
Accounts	108	—	516	120	2,676	—	6,962	53
Loans and advances	—	—	—	—	—	—	—	—
Accrued interest	—	—	—	—	—	2	—	—
Other governmental entities	701	—	—	—	—	—	424	503
Other	—	—	—	—	—	—	55	2
Due from:								
Primary government	—	1,778	—	—	—	—	—	—
Component units	—	—	—	6,462	—	—	—	—
Inventories	—	499	—	—	1,634	—	—	—
Prepays	210	461	—	658	—	—	—	—
<b>Total current assets</b>	<b>3,283</b>	<b>2,772</b>	<b>2,691</b>	<b>7,265</b>	<b>4,690</b>	<b>5,191</b>	<b>7,640</b>	<b>3,364</b>
<b>Noncurrent assets:</b>								
<b>Restricted assets:</b>								
Cash and cash equivalents	—	—	—	1,775	2,812	—	664	1
Cash and cash equivalents in governmental banks	—	—	8,099	—	976	—	—	—
Investments and other restricted assets	790	—	—	—	—	—	—	—
Investments	—	—	—	—	—	—	—	—
Loans, interest and other receivable	—	—	—	—	—	—	—	—
Due from component units	—	—	—	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—	—	—
Capital assets not being depreciated	2,929	9,090	—	—	—	—	15,176	153
Capital assets, depreciable, net	15,534	46,439	623	233	550	—	1,854	267
Deferred expenses and other assets	—	—	—	—	—	—	—	—
<b>Total noncurrent assets</b>	<b>19,253</b>	<b>55,529</b>	<b>8,722</b>	<b>2,008</b>	<b>4,338</b>	<b>—</b>	<b>17,694</b>	<b>421</b>
<b>Total assets</b>	<b>\$ 22,536</b>	<b>\$ 58,301</b>	<b>\$ 11,413</b>	<b>\$ 9,273</b>	<b>\$ 9,028</b>	<b>\$ 5,191</b>	<b>\$ 25,334</b>	<b>\$ 3,785</b>

**COMMONWEALTH OF PUERTO RICO**

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Puerto Rico School of Plastic Arts	Corporation for the Development of the Arts, Sciences and Film Industry	Governing Board of the 911 Service	Institutional Trust of the National Guard of Puerto Rico	Special Communities Perpetual Trust	Puerto Rico Convention Center District Authority	Total
<b>Assets:</b>							
<b>Current assets:</b>							
Cash and cash equivalents	\$ 55	2,640	—	—	—	20,638	207,324
Cash and cash equivalents in governmental banks	1,884	7,937	23,014	33,126	161	—	388,007
Investments, including collateral from securities lending transactions	—	—	—	224	—	—	1,402,667
Receivables, net:							
Intergovernmental	—	—	—	—	—	—	2,358
Accounts	—	—	2,115	—	—	—	220,698
Loans and advances	—	—	255	—	—	—	54,420
Accrued interest	—	—	47	—	—	—	23,696
Other governmental entities	—	—	—	—	—	794	134,342
Other	—	—	—	3,052	1,414	—	34,374
Due from:							
Primary government	—	—	—	—	20,000	—	21,778
Component units	—	—	—	—	—	—	39,992
Inventories	—	—	59	—	—	—	36,056
Prepays	—	—	—	—	—	1,381	11,837
<b>Total current assets</b>	<b>1,939</b>	<b>10,577</b>	<b>25,490</b>	<b>36,402</b>	<b>21,575</b>	<b>22,813</b>	<b>2,577,549</b>
<b>Noncurrent assets:</b>							
<b>Restricted assets:</b>							
Cash and cash equivalents	—	—	—	—	—	—	136,109
Cash and cash equivalents in governmental banks	—	—	—	419	—	—	136,803
Investments and other restricted assets	546	—	—	—	—	—	1,488,920
Investments	—	586	638	—	—	—	1,160,156
Loans, interest and other receivable	—	—	—	—	—	—	148,989
Due from component units	—	—	—	—	—	—	32,364
Property held for sale and future development	—	—	—	1,483	—	—	167,661
Capital assets not being depreciated	—	—	—	4,147	—	262,675	1,313,480
Capital assets, depreciable, net	8,920	24	6,726	4,147	—	179	1,606,004
Deferred expenses and other assets	—	—	—	2,059	—	—	56,598
<b>Total noncurrent assets</b>	<b>9,466</b>	<b>610</b>	<b>7,364</b>	<b>8,108</b>	<b>—</b>	<b>262,854</b>	<b>6,247,084</b>
<b>Total assets</b>	<b>11,405</b>	<b>11,187</b>	<b>32,854</b>	<b>44,510</b>	<b>21,575</b>	<b>285,667</b>	<b>8,824,633</b>

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Municipal Finance Agency	Puerto Rico Ports Authority	Puerto Rico Industrial Development Company	Automobile Accident Compensation Administration	Puerto Rico Land Administration
<b>Liabilities and Net Assets</b>							
Current liabilities:							
Accounts payable and accrued liabilities	\$ 147,717	—	1,298	102,887	55,256	7,241	3,017
Deposits and escrow liabilities	—	256,000	158,447	1,224	6,716	—	1,617
Due to:							
Primary government	30,000	—	—	—	—	—	—
Component units	—	295	—	238,493	56	—	—
Other governmental entities	119,573	—	—	—	—	—	—
Securities lending transactions and reverse-repurchase agreements	—	69,226	—	—	—	33,838	—
Interest payable	60,011	4,080	29,625	2,586	4,762	—	—
Deferred revenue	1,386	—	260	589	—	36,868	—
Notes payable, current portion	—	55,234	—	63,300	1,239	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	—	—	—
Bonds payable, current portion	—	—	89,480	3,970	8,979	—	—
Accrued compensated absences	36,253	—	—	7,673	—	3,324	902
Reserves for automobile accident benefit payments	772,827	—	—	—	—	109,845	—
Current portion of other long-term liabilities	277	4,280	—	9,425	262	—	—
Total current liabilities	1,168,044	389,115	279,110	430,147	77,270	191,116	5,536
Noncurrent liabilities:							
Due to:							
Primary government	—	—	—	—	—	—	—
Component units	—	12,520	—	12,000	—	—	—
Deferred revenue	—	—	2,541	3,475	—	—	—
Notes payable	55,252	300,000	—	—	61,436	—	—
Commonwealth appropriation bonds	—	—	—	—	—	—	—
Bonds payable	—	—	1,248,881	70,078	297,108	—	—
Accrued compensated absences	—	1,804	—	—	—	—	—
Other long-term liabilities	46,331	580	86,723	304	—	—	—
Total noncurrent liabilities	101,583	314,904	1,338,145	85,857	358,544	—	38,939
Total liabilities	1,269,627	704,019	1,617,255	516,004	435,814	191,116	44,475
Invested in capital assets, net of related debt	24,630	(1,422)	—	322,436	369,176	—	6,476
Restricted for:							
Trust nonexpendable	—	—	—	—	—	—	—
Capital projects	—	—	—	27,669	—	—	—
Debt service	—	—	—	25,806	—	—	—
Student loans and other educational purposes	—	—	—	—	—	—	—
Other specified purposes	—	8,551	23,355	5,862	105,401	—	—
Unrestricted	372,024	101,949	85,020	(74,383)	(8,811)	58,901	212,660
Total net assets	396,654	109,078	108,375	307,390	465,766	58,901	219,136
Total liabilities and net assets	1,666,281	813,097	1,725,630	823,394	901,580	250,017	263,611

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	National Parks Company of Puerto Rico	Puerto Rico Medical Services Administration	Puerto Rico Trade and Export Company	Tourism Company of Puerto Rico	Puerto Rico and Caribbean Cardiovascular Center Corporation	Agricultural Services and Development Corporation
<b>Liabilities and Net Assets</b>						
Current liabilities:						
Accounts payable and accrued liabilities	\$ 11,077	39,188	3,981	34,297	32,246	68,890
Deposits and escrow liabilities	—	—	—	—	—	—
Due to:						
Primary government	—	—	—	7,917	—	—
Component units	—	27,044	459	—	—	60,736
Other governmental entities	1,178	15,637	—	—	—	476
Securities lending transactions and reverse-repurchase agreements	—	—	—	—	—	—
Interest payable	—	—	46	—	17,143	—
Deferred revenue	—	—	—	—	—	572
Notes payable, current portion	—	—	—	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	1,217	—	—
Bonds payable, current portion	—	—	—	—	—	—
Accrued compensated absences	337	7,097	—	1,662	—	9,232
Reserves for automobile accident benefit payments	—	—	—	—	—	—
Current portion of other long-term liabilities	—	8,257	—	104	9,035	—
Total current liabilities	12,592	97,223	4,486	45,197	58,424	141,801
Noncurrent liabilities:						
Due to:						
Primary government	—	—	—	—	32,613	—
Component units	—	—	8,719	—	—	—
Deferred revenue	—	—	—	—	—	—
Notes payable	—	—	—	—	—	—
Commonwealth appropriation bonds	—	—	—	126,353	—	—
Bonds payable	—	—	—	—	—	—
Accrued compensated absences	4,766	—	1,499	4,186	—	—
Other long-term liabilities	977	8,451	4,612	887	18,983	660
Total noncurrent liabilities	5,743	8,451	14,830	131,426	51,596	660
Total liabilities	18,335	105,674	19,316	176,623	110,020	142,461
Invested in capital assets, net of related debt	226,231	28,648	88,233	27,635	42,075	—
Restricted for:						
Trust nonexpendable	—	—	—	—	—	—
Capital projects	—	—	—	—	4,806	—
Debt service	—	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	—	—
Other specified purposes	—	4,123	9,295	—	—	—
Unrestricted	56,474	(21,885)	19,756	(38,758)	(87,456)	(12,445)
Total net assets	282,705	10,886	117,284	(11,123)	(40,575)	4,095
Total liabilities and net assets	301,040	116,560	136,600	165,500	69,445	(8,350)
						134,111

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Land Authority of Puerto Rico	Puerto Rico Metropolitan Bus Authority	Puerto Rico Telephone Authority	Industrial, Tourist, Educational, Medical, and Environmental, Control Facilities Financing Authority	Puerto Rico Solid Waste Authority	Public Corporation for the Supervision and Deposit Insurance of Puerto Rico
<b>Liabilities and Net Assets</b>						
Current liabilities:						
Accounts payable and accrued liabilities	70,142	23,540	277	7,996	11,116	8,721
Deposits and escrow liabilities	8,664	—	—	—	—	—
Due to:						
Primary government	—	—	—	—	—	—
Component units	40,617	—	—	140,911	19,687	—
Other governmental entities	—	—	—	—	—	—
Securities lending transactions and reverse-repurchase agreements	—	—	—	—	—	—
Interest payable	4,048	108	—	2,628	—	—
Deferred revenue	393	188	—	—	—	—
Notes payable, current portion	—	—	—	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	3	—
Bonds payable, current portion	—	—	—	—	—	—
Accrued compensated absences	1,451	—	—	—	432	1,030
Reserves for automobile accident benefit payments	—	—	—	—	—	—
Current portion of other long-term liabilities	6,332	—	39,675	2,268	19	—
Total current liabilities	131,647	23,836	39,952	153,803	31,257	9,751
Noncurrent liabilities:						
Due to:						
Primary government	—	—	—	—	—	—
Component units	—	26,334	—	—	44,631	—
Deferred revenue	—	—	—	—	—	—
Notes payable	—	—	—	—	—	—
Commonwealth appropriation bonds	158,993	—	—	—	6,704	—
Bonds payable	—	—	—	—	—	—
Accrued compensated absences	—	—	—	—	432	—
Other long-term liabilities	14,844	—	—	—	116	—
Total noncurrent liabilities	173,837	26,334	—	—	51,883	—
Total liabilities	305,484	50,170	39,952	153,803	83,140	9,751
Invested in capital assets, net of related debt	87,010	59,970	—	57,853	114,900	207
Restricted for:						
Trust nonexpendable	—	—	—	—	—	—
Capital projects	—	42	—	—	—	—
Debt service	—	—	—	—	—	—
Student loans and other educational purposes	—	—	24,319	—	—	—
Other specified purposes	—	—	128	—	—	—
Unrestricted	(238,733)	(26,471)	—	37,816	8,870	55,449
Total net assets	(151,723)	33,541	24,447	95,669	125,936	98,020
Total liabilities and net assets	153,761	83,711	64,399	249,472	209,076	107,771

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Right to Employment Administration	Puerto Rico Public Broadcasting Corporation	Fine Arts Center Corporation	Puerto Rico Maritime Transportation Authority	Puerto Rico Council on Higher Education	Farm Insurance Corporation of Puerto Rico
<b>Liabilities and Net Assets</b>						
Current liabilities:						
Accounts payable and accrued liabilities	\$ 1,830	2,987	526	11,534	1,424	1,306
Deposits and escrow liabilities	—	—	226	37	—	—
Due to:						
Primary government	—	—	—	—	—	—
Component units	—	—	—	—	—	—
Other governmental entities	1,017	—	3	—	—	249
Securities lending transactions and reverse-repurchase agreements	—	—	—	—	—	—
Interest payable	—	—	—	—	—	—
Deferred revenue	841	5,108	1,340	—	—	467
Notes payable, current portion	—	—	—	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	—	—
Bonds payable, current portion	—	—	—	—	—	—
Accrued compensated absences	1,208	725	59	—	—	361
Reserves for automobile accident benefit payments	—	—	—	—	—	—
Current portion of other long-term liabilities	—	—	22	—	—	—
Total current liabilities	4,896	8,820	2,176	11,571	1,424	2,383
Noncurrent liabilities:						
Due to:						
Primary government	—	—	—	—	—	—
Component units	—	—	—	23,645	—	—
Deferred revenue	—	—	—	—	—	—
Notes payable	—	—	—	—	—	—
Commonwealth appropriation bonds	—	—	—	—	—	—
Bonds payable	—	—	—	—	—	—
Accrued compensated absences	1,362	1,129	379	1,102	307	—
Other long-term liabilities	—	—	34	144	—	—
Total noncurrent liabilities	1,362	1,129	413	24,891	307	—
Total liabilities	6,258	9,949	2,589	36,462	1,731	2,383
Invested in capital assets, net of related debt	462	20,454	18,122	55,530	623	233
Restricted for:						
Trust nonexpendable	—	—	—	—	—	—
Capital projects	—	—	—	—	—	—
Debt service	—	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	8,687	—
Other specified purposes	—	—	790	—	—	1,775
Unrestricted	959	(564)	1,035	(33,691)	372	4,882
Total net assets	1,421	19,890	19,947	21,839	9,682	6,890
Total liabilities and net assets	7,679	29,839	22,536	58,301	11,413	9,273

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Employment and Training Enterprise Corporation	Caribbean Basin Projects Financing Authority	Puerto Rico Conservatory of Music Corporation	Musical Arts Corporation	Puerto Rico School of Plastic Arts	Corporation for the Development of the Arts, Sciences and Film Industry
<b>Liabilities and Net Assets</b>						
Current liabilities:						
Accounts payable and accrued liabilities	\$ 4,807	6	1,014	972	756	162
Deposits and escrow liabilities	—	—	—	—	—	—
Due to:						
Primary government	—	5,082	—	—	—	—
Component units	793	—	—	—	—	—
Other governmental entities	—	—	—	—	—	—
Securities lending transactions and reverse-repurchase agreements	—	—	—	—	—	—
Interest payable	90	—	—	—	—	—
Deferred revenue	—	—	216	290	108	—
Notes payable, current portion	—	—	—	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	—	—
Bonds payable, current portion	—	—	—	—	—	—
Accrued compensated absences	197	—	131	145	—	9
Reserves for automobile accident benefit payments	—	—	—	—	—	—
Current portion of other long-term liabilities	—	—	—	—	—	—
Total current liabilities	5,887	5,088	1,361	1,407	864	171
Noncurrent liabilities:						
Due to:						
Primary government	7,108	—	—	—	—	—
Component units	621	—	—	—	—	—
Deferred revenue	788	—	—	—	—	—
Notes payable	—	—	—	—	—	—
Commonwealth appropriation bonds	—	—	—	—	—	—
Bonds payable	—	—	—	—	—	—
Accrued compensated absences	—	—	808	73	219	90
Other long-term liabilities	—	—	137	2,207	—	—
Total noncurrent liabilities	8,517	—	945	2,280	219	90
Total liabilities	14,404	5,088	2,306	3,687	1,083	261
Invested in capital assets, net of related debt	550	—	16,814	420	8,920	24
Restricted for:						
Trust nonexpendable	—	—	—	—	—	—
Capital projects	—	—	—	—	997	—
Debt service	—	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	546	—
Other specified purposes	504	—	659	(62)	—	10,622
Unrestricted	(6,430)	103	5,555	(260)	(141)	280
Total net assets	(5,376)	103	23,028	98	10,322	10,926
Total liabilities and net assets	9,028	5,191	25,334	3,785	11,405	11,187

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2004  
(In thousands)

	Governing Board of the 911 Service	Institutional Trust of the National Guard of Puerto Rico	Special Communities Perpetual Trust	Puerto Rico Convention Center District Authority	Total
<b>Liabilities and Net Assets</b>					
<b>Current liabilities:</b>					
Accounts payable and accrued liabilities	\$ 3,101	929	11,640	21,528	693,409
Deposits and escrow liabilities	—	—	—	—	432,931
Due to:					
Primary government	4,630	—	—	—	47,629
Component units	—	—	70,000	205,473	804,564
Other governmental entities	—	—	—	—	18,560
Securities lending transactions and reverse-repurchase agreements	—	—	—	—	222,637
Interest payable	—	—	343	—	67,354
Deferred revenue	—	—	—	—	107,251
Notes payable, current portion	—	—	—	—	121,159
Commonwealth appropriation bonds, current portion	—	—	—	—	1,220
Bonds payable, current portion	—	—	—	—	102,429
Accrued compensated absences	685	—	—	147	73,060
Reserves for automobile accident benefit payments	—	—	—	—	882,672
Current portion of other long-term liabilities	—	—	—	—	79,956
Total current liabilities	8,416	929	81,983	227,148	3,654,831
<b>Noncurrent liabilities:</b>					
Due to:					
Primary government	—	—	—	—	39,721
Component units	—	—	20,918	—	149,388
Deferred revenue	—	—	—	—	6,804
Notes payable	—	—	—	—	416,688
Commonwealth appropriation bonds	—	—	—	—	292,050
Bonds payable	—	—	—	—	1,616,067
Accrued compensated absences	—	—	—	—	18,156
Other long-term liabilities	—	—	—	—	224,929
Total noncurrent liabilities	—	—	20,918	—	2,763,803
Total liabilities	8,416	929	102,901	227,148	6,418,634
Invested in capital assets, net of related debt	5,316	5,630	—	57,380	1,644,536
Restricted for:					
Trust nonexpendable	—	—	—	—	—
Capital projects	—	—	—	—	33,514
Debt service	—	—	—	—	25,806
Student loans and other educational purposes	—	—	—	—	9,233
Other specified purposes	7,981	3,000	—	—	251,345
Unrestricted	11,141	34,879	(81,326)	1,139	441,493
Total net assets	24,438	43,509	(81,326)	58,519	2,405,927
Total liabilities and net assets	32,854	44,438	21,575	285,667	8,824,561

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Activities

Year ended June 30, 2004  
(in thousands)

	Expenses	Program revenue			Net revenue (expenses) and changes in net assets	General revenue					Change in net assets	Net assets, beginning of year	Net assets, end of year	
		Charges for services	Operating grants and contributions	Capital grants and contributions		Payments from (to) primary government	Payments from other component units	Grants and contributions not restricted to specific programs	Taxes	Interest and investment earnings				Gain in sale of assets
Agricultural Services and Development Administration	\$ 199,736	59,038	-	-	(140,698)	161,087	-	-	-	-	6,822	27,211	(65,561)	(8,330)
Automobile Accident Compensation Administration	94,510	77,616	-	-	(16,894)	-	-	-	-	-	-	225	58,676	58,901
Cardiovascular Center Corporation of Puerto Rico and the Caribbean	64,952	54,335	-	-	(10,617)	2,000	-	-	-	-	-	(8,554)	(32,021)	(40,575)
Caribbean Basin Projects Financing Authority	5,086	-	-	-	(5,086)	-	-	-	-	-	-	(5,066)	5,169	103
Corporation for the Development of the Arts, Sciences and Film Industry of Puerto Rico	1,185	73	-	-	(1,112)	1,259	-	-	-	3,572	63	3,782	7,144	10,926
Economic Development Bank for Puerto Rico	33,069	31,459	-	-	(1,610)	-	-	-	-	-	-	1,316	107,762	109,078
Employment and Training Enterprise Corporation	6,542	6,652	146	-	256	906	-	-	-	-	54	1,310	(6,686)	(5,376)
Farm Insurance Corporation of Puerto Rico	6,794	5,622	-	-	(1,172)	-	-	-	-	-	881	(260)	7,150	6,890
Fine Arts Center Corporation	6,182	2,559	-	-	(3,623)	4,023	-	-	-	-	-	550	19,397	19,947
Governing Board of the 911 Service	7,140	11,471	-	-	4,331	-	-	-	-	-	70	4,609	19,829	24,438
Institutional Trust of the National Guard of Puerto Rico	6,628	16,127	-	-	9,499	495	-	-	-	-	-	10,453	33,056	43,509
Musical Arts Corporation and Subsidiaries	9,275	699	-	-	(7,461)	6,528	-	-	-	412	-	(147)	245	98
National Parks Company of Puerto Rico	44,954	10,811	-	-	(34,143)	23,062	-	-	-	-	3,186	(7,348)	290,053	282,705
Insurance of Puerto Rico	5,862	37,034	4,764	-	35,936	-	-	-	-	-	-	37,934	60,086	98,020
Puerto Rico Conservatory of Music Corporation	6,610	2,306	391	-	(3,913)	6,097	-	-	-	6	-	2,194	20,834	23,028
Puerto Rico Convention Center District Authority	7,804	-	-	-	(7,804)	-	-	-	-	-	-	3,828	62,322	58,519
Puerto Rico Council on Higher Education	29,370	80	1,474	-	(27,816)	28,131	-	-	-	(130)	-	272	9,410	9,682
Puerto Rico Exports Development Corporation	10,991	11,250	-	-	259	-	(108,401)	-	-	97	-	(107,597)	107,597	-
Puerto Rico Industrial Development Company	102,871	46,866	-	-	(55,797)	19,902	-	-	-	-	-	(18,675)	484,441	465,766
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	94	-	-	-	(94)	20,000	-	-	-	-	-	20,046	75,623	95,669
Puerto Rico Land Administration	9,150	9,689	-	-	539	-	-	-	-	-	-	1,619	217,517	219,136
Puerto Rico Land Authority	29,880	13,448	-	-	(16,432)	-	-	-	-	(4,068)	-	(6,160)	(145,563)	(151,723)
Puerto Rico Maritime Transportation Authority	32,925	3,985	2,981	-	(25,959)	15,500	-	-	-	-	-	(10,457)	32,296	21,839
Puerto Rico Medical Services Administration	128,648	102,229	-	-	(26,419)	48,392	-	-	-	-	-	22,245	(11,359)	10,886
Puerto Rico Metropolitan Bus Authority	67,683	24,267	14,007	-	(29,409)	18,731	-	-	-	-	-	(10,639)	44,180	33,541
Puerto Rico Municipal Finance Agency	73,803	-	-	-	(73,803)	-	-	-	-	-	-	(59,863)	168,238	108,375
Puerto Rico Ports Authority	155,450	124,553	9,511	-	(21,386)	2,500	-	-	-	22,440	-	4,001	303,389	307,390
Puerto Rico Public Broadcasting Corporation	31,316	1,577	-	-	(29,739)	33,756	-	-	-	137	-	7,453	12,437	19,890
Puerto Rico School of Plastic Arts	3,611	952	7,800	-	5,141	3,544	-	-	-	-	-	8,685	1,637	10,322
Puerto Rico Solid Waste Authority	12,783	907	215	-	(11,661)	26,339	-	-	-	(260)	-	14,646	111,290	125,936
Puerto Rico Telephone Authority	227	-	-	-	(227)	-	-	-	-	-	-	(2,040)	26,487	24,447
Puerto Rico Trade and Export Company	8,214	3,911	-	-	(4,303)	10,758	-	-	-	133	-	117,284	-	117,284
Right to Employment Administration	47,692	-	24,095	-	(23,597)	24,716	-	-	-	48	-	1,220	201	1,421
Special Communities Perpetual Trust	128,455	-	-	-	(128,455)	50,000	-	-	-	-	-	(74,569)	(6,757)	(81,326)
State Insurance Fund Corporation	514,701	625,433	-	-	110,732	-	-	-	-	-	-	177,117	219,537	396,654
Tourism Company of Puerto Rico	279,294	256,081	-	-	(23,213)	14,222	-	-	-	3,354	1,430	32,208	(43,331)	(11,123)
Total nonmajor component units	\$ 2,173,487	1,541,030	30,726	35,981	(565,750)	521,948	2,734	3,886	73,449	100,094	181,202	2,224,725	2,248,927	

**STATISTICAL SECTION**

COMMONWEALTH OF PUERTO RICO

Changes in Net Assets  
For the last three fiscal years

Accrual Basis of Accounting  
(In thousands)

	2004	2003	2002
<b>Expenses:</b>			
<b>Governmental activities:</b>			
General government	\$ 1,963,879	\$ 2,324,715	\$ 1,429,265
Public safety	1,950,635	1,606,272	1,883,061
Health	2,386,735	1,903,811	1,990,852
Public housing and welfare	2,919,315	3,239,366	2,803,742
Education	3,684,331	3,375,815	3,477,373
Economic development	896,925	451,945	632,083
Intergovernmental	591,237	466,792	467,957
Interest and other	778,700	671,228	646,120
Total governmental activities	<u>15,171,757</u>	<u>14,039,914</u>	<u>13,330,453</u>
<b>Business-type activities:</b>			
Lotteries	731,344	695,888	603,768
Unemployment	142,652	343,243	331,754
Other	26,763	22,385	16,902
Total business-type activities	<u>900,759</u>	<u>1,061,516</u>	<u>952,424</u>
Total primary government expenses	<u>\$ 16,072,516</u>	<u>\$ 15,101,430</u>	<u>\$ 14,282,877</u>
<b>Program revenue:</b>			
<b>Governmental activities:</b>			
Charges for services	\$ 789,207	\$ 757,116	\$ 535,423
Operating grants and contributions	1,038,776	3,830,639	3,400,729
Capital grants and contributions	2,592,055	173,644	187,512
Total governmental activities	<u>4,400,038</u>	<u>4,761,399</u>	<u>4,123,664</u>
<b>Business activities:</b>			
Charges for services	1,136,705	1,132,285	1,021,070
Operating grants and contributions	59,728	97,033	26,509
Total business-type activities	<u>1,196,433</u>	<u>1,229,318</u>	<u>1,047,579</u>
<b>Net (expense) revenue:</b>			
Governmental activities	(10,771,719)	(9,278,515)	(9,206,789)
Business-type activities	295,674	167,902	96,155
Total primary government net expense	<u>\$ (10,476,045)</u>	<u>\$ (9,110,713)</u>	<u>\$ (9,110,634)</u>
<b>General revenue:</b>			
<b>Governmental activities:</b>			
<b>Taxes:</b>			
Income	\$ 5,191,080	\$ 4,941,128	\$ 4,448,570
Property	121,815	122,660	102,554
Excise	1,924,610	1,994,729	1,713,098
Other	19,211	3,055	1,963
Revenue from global settlement agreement	70,420	101,849	37,153
Unrestricted investment earnings	60,585	85,565	90,940
Revenue from component units	175,729	111,752	228,118
Grants and contributions not restricted to specific programs	5,706	103,423	46,117
Payment from agency fund	—	—	129,000
Special item	(35,646)	(203,514)	123,785
Transfers	203,258	279,060	187,183
Other	262,904	91,715	472,642
Total governmental activities	<u>\$ 7,999,672</u>	<u>\$ 7,531,428</u>	<u>\$ 7,579,123</u>
<b>Business-type activities:</b>			
Unrestricted investments earnings	23,831	77,362	36,455
Revenue from component units	—	1,038	3,370
Grants and contributions not restricted to specific programs	—	—	44,320
Transfers	(203,258)	(279,060)	(187,183)
Total business-type activities	<u>(179,427)</u>	<u>(200,660)</u>	<u>(103,038)</u>
Total primary government	<u>\$ 7,820,245</u>	<u>\$ 7,330,768</u>	<u>\$ 7,476,085</u>
<b>Change in net assets:</b>			
<b>Governmental activities</b>			
Governmental activities	(2,772,047)	(1,747,087)	(1,627,666)
<b>Business-type activities</b>			
Business-type activities	118,247	(32,658)	(7,883)
Total primary government	<u>\$ (2,655,800)</u>	<u>\$ (1,779,745)</u>	<u>\$ (1,635,549)</u>

**COMMONWEALTH OF PUERTO RICO**

**Net Assets by Component  
For the last three fiscal years**

**Accrual Basis of Accounting  
(In thousands)**

	2004	2003	2002
<b>Governmental activities:</b>			
Invested in capital assets, net of related debt	\$ 3,133,230	1,969,864	1,909,137
Restricted	—	19,749	4,616
Unrestricted (deficit)	<u>(16,789,576)</u>	<u>(13,942,397)</u>	<u>(12,085,385)</u>
<b>Total governmental activities net assets</b>	<b><u>\$ (13,656,346)</u></b>	<b><u>\$ (11,952,784)</u></b>	<b><u>\$ (10,171,632)</u></b>
<b>Business-type activities:</b>			
Invested in capital assets, net of related debt	\$ 1,672	1,895	310
Restricted	853,194	736,947	769,804
Unrestricted (deficit)	<u>(3,037)</u>	<u>(3,260)</u>	<u>(1,675)</u>
<b>Total business-type activities net assets</b>	<b><u>\$ 851,829</u></b>	<b><u>\$ 735,582</u></b>	<b><u>\$ 768,439</u></b>
<b>Primary government:</b>			
Invested in capital assets, net of related debt	\$ 3,134,902	1,971,759	1,909,447
Restricted	853,194	756,696	774,420
Unrestricted (deficit)	<u>(16,790,091)</u>	<u>(13,945,657)</u>	<u>(12,087,060)</u>
<b>Total primary government net assets</b>	<b><u>\$ (12,801,995)</u></b>	<b><u>\$ (11,217,202)</u></b>	<b><u>\$ (9,403,193)</u></b>

**COMMONWEALTH OF PUERTO RICO**  
**General Governmental Expenditures by Function**  
**All Governmental Fund Types**

For the last ten fiscal years  
(In thousands)

Function:	2004	%	2003	2002*	2001	2000	1999	1998	1997	1996	1995
General government	\$ 1,777,365	11.7%	\$ 1,774,156	1,279,750	739,009	853,040	526,629	484,547	499,652	661,359	451,275
Public safety	1,765,199	11.6%	1,424,846	1,659,280	1,623,362	1,310,322	1,103,606	1,241,762	1,188,814	926,498	878,673
Health	2,176,741	14.3%	1,908,717	1,983,727	954,563	972,757	625,475	656,498	508,659	245,743	231,212
Public housing and welfare	2,738,016	18.0%	2,953,189	2,726,129	2,315,899	2,102,410	2,485,092	1,902,902	2,086,828	1,701,434	1,681,688
Education	3,474,013	22.9%	3,297,248	3,343,002	2,308,479	2,436,267	2,272,903	2,744,630	1,960,185	1,832,271	1,760,784
Economic development	868,926	5.7%	428,621	637,794	170,937	337,255	314,897	186,296	333,290	88,143	154,796
Intergovernmental	528,829	3.5%	465,699	466,169	222,721	373,016	318,664	55,739	496,844	306,226	207,389
Capital outlays	581,788	3.8%	1,184,976	507,634	1,020,344	833,597	642,016	1,515,230	1,395,463	1,255,430	848,801
Debt service:											
Principal	526,572	3.5%	330,346	2,062,059	466,467	416,369	351,722	620,866	359,851	367,198	660,133
Interest and other	737,502	4.9%	685,461	614,347	545,001	444,595	442,614	595,053	556,835	504,480	435,549
<b>Total expenditures - all governmental fund types</b>	<b>\$ 15,174,951</b>	<b>100.0%</b>	<b>\$ 14,453,259</b>	<b>15,279,891</b>	<b>10,366,782</b>	<b>10,079,628</b>	<b>9,083,618</b>	<b>10,003,523</b>	<b>9,386,421</b>	<b>7,888,782</b>	<b>7,310,300</b>

\*In 2002, the Commonwealth adopted GASB No. 34. This statement requires payments to component units to be included as expenditure by function. In prior years such payments were reported as operating transfers-out to component units.

**COMMONWEALTH OF PUERTO RICO**

**General Governmental Revenue by Source  
All Governmental Fund Types**

For the last ten fiscal years  
(In thousands)

Source:	2004	%	2003	2002*	2001	2000	1999	1998	1997	1996	1995
<b>Taxes:</b>											
Income	\$ 5,061,761	41.8%	\$ 4,874,795	4,843,852	4,536,840	4,967,138	4,413,860	3,989,239	3,622,988	3,396,724	3,242,876
Property	121,813	1.0%	122,666	102,554	—	—	—	—	—	—	—
Excise	1,924,610	15.9%	1,894,729	1,713,098	1,768,992	1,736,539	1,714,444	1,884,348	1,827,305	1,713,537	1,664,529
Other	19,211	0.2%	3,055	1,963	92,024	87,523	78,926	73,426	64,910	57,662	56,556
<b>Charges for services</b>	<b>750,978</b>	<b>6.2%</b>	<b>780,905</b>	<b>535,423</b>	<b>645,806</b>	<b>617,020</b>	<b>457,454</b>	<b>569,096</b>	<b>464,034</b>	<b>461,736</b>	<b>455,500</b>
Intergovernmental	3,654,766	30.2%	4,107,706	3,634,358	3,807,049	2,971,528	3,435,765	3,009,169	3,077,042	2,545,615	2,492,443
Interest	58,914	0.5%	85,565	90,940	67,020	91,525	97,880	116,030	110,777	59,788	—
Other	507,613	4.2%	314,002	736,686	270,711	383,548	162,228	189,476	134,819	186,591	170,025
<b>Total revenue - all governmental fund types</b>	<b>\$ 12,099,666</b>	<b>100.0%</b>	<b>\$ 12,183,423</b>	<b>11,658,674</b>	<b>11,208,442</b>	<b>10,854,821</b>	<b>10,360,557</b>	<b>9,830,784</b>	<b>9,301,875</b>	<b>8,421,653</b>	<b>8,081,929</b>

\*The annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation, collected by the Municipal Revenue Collection Center on the Commonwealth's behalf, is presented as property tax from 2002 henceforth but as intergovernmental revenue in prior years.

**COMMONWEALTH OF PUERTO RICO**

**Fund Balances of Governmental Funds  
For the last three fiscal years**

**Modified Accrual Basis of Accounting  
(In thousands)**

	2004	2003	2002
<b>General fund:</b>			
Reserved	\$ 1,102,232	\$ 262,758	\$ 366,558
Unreserved (deficit)	<u>(1,468,182)</u>	<u>(342,941)</u>	<u>(193,131)</u>
Total general fund	<u>\$ (365,950)</u>	<u>\$ (80,183)</u>	<u>\$ 173,427</u>
<b>All other governmental funds:</b>			
Reserved	\$ 72,455	\$ 33,047	\$ 72,455
Unreserved reported in:			
Debt service funds	119,830	168,928	120,216
Special revenue funds	449,455	506,252	378,852
Capital project funds	<u>744,577</u>	<u>228,215</u>	<u>356,201</u>
Total all other governmental funds	<u>\$ 1,386,317</u>	<u>\$ 936,442</u>	<u>\$ 927,724</u>

**COMMONWEALTH OF PUERTO RICO**

**Computation of the Legal Debt Margin**

**June 30, 2004**

**(In thousands)**

<b>Statutory Margin</b>	
<b>Section 2, Article VI of Constitution of Puerto Rico</b>	
<b>(Section 2, Article VI of Constitution of Puerto Rico)</b>	
<b>Internal revenue for the year ended June 30, 2002</b>	<b>\$ 6,865,454</b>
<b>Internal revenue for the year ended June 30, 2003</b>	<b>7,505,866</b>
	<hr/>
<b>Total internal revenue for the years ended June 30, 2003 and 2004</b>	<b>\$ 14,371,320</b>
	<hr/>
<b>Internal revenue average for the two years</b>	<b>\$ 7,185,660</b>
	<hr/>
<b>Legal debt limit – 15% of internal revenue average for the two years</b>	<b>\$ 1,077,849</b>
<b>Maximum debt service requirement – 8.330% on Commonwealth bonds maturing on 2020 and PRASA debt service paid during fiscal year 2004</b>	<b>598,547</b>
	<hr/>
<b>Additional legal debt service requirement margin</b>	<b>\$ 479,302</b>
	<hr/>

**Source: Government Development Bank for Puerto Rico**

**COMMONWEALTH OF PUERTO RICO**

**Ratio of Annual Debt Service for General  
Bonded Debt to Total General Expenditures**

**For the last ten fiscal years  
(In thousands)**

<b>Fiscal Year</b>	<b>Total Debt Service</b>	<b>General Governmental Expenditures</b>	<b>Ratio (%)</b>
2004	459,336	15,174,951	3.0%
2003	362,136	14,453,259	2.5
2002	608,674	15,279,891	4.0
2001	538,436	10,366,782	5.2
2000	507,336	10,079,628	5.0
1999	468,970	9,083,618	5.2
1998	435,894	10,003,523	4.4
1997	430,153	9,386,421	4.6
1996	424,753	7,888,782	5.4
1995	389,278	7,310,300	5.3

**COMMONWEALTH OF PUERTO RICO**

**Demographic Statistics**

**For the last ten fiscal years**

Fiscal year	Population*	Per capita income	Median age	School enrollment**	Unemployment rate (%)
2004 (p)	3,887	\$ 12,031	33.8	864,597	11.4
2003	3,869 r	11,566 r	33.3	875,831	12.1
2002	3,849 r	10,921 r	32.9	792,284	12.5 r
2001	3,828 r	10,732 r	32.6	799,933	10.5
2000	3,808 r	10,204	32.2	799,322	11.0
1999	3,791 r	9,659	31.8	753,705	12.5
1998	3,770 r	9,108	31.4	753,428	13.6
1997	3,742 r	8,729	31.0	749,938	13.1
1996	3,704 r	8,076	30.7	770,537	13.8
1995	3,666 r	7,468	30.3	709,559	13.8

\* Amounts expressed in thousands

\*\* The enrollment in private schools is an estimate

p Preliminary

r Revised

Source: Puerto Rico Planning Board, Department of Education, and the General Council of Education of the Commonwealth

**COMMONWEALTH OF PUERTO RICO**

**Construction and Bank Deposits**

**For the last ten fiscal years**

Fiscal year	Commercial construction (1)		Residential construction (1)		(2) Bank deposits *
	Number of permits	Value *	Number of permits	Value *	
2004	942	\$ 236,600	7,806	\$ 1,603,539	\$49,452,980
2003	892 r	269,001 r	7,286 r	1,249,126 r	45,895,052
2002	944 r	300,150 r	6,760 r	1,065,082 r	39,219,512
2001	839 r	299,214 r	6,580 r	1,149,380 r	37,788,557
2000	907 r	354,682 r	6,594 r	991,891 r	30,449,860
1999	828 r	180,694 r	6,504 r	694,891 r	28,423,313
1998	910 r	218,556 r	6,740 r	631,486 r	25,354,086
1997	858 r	273,696 r	6,135 r	632,791 r	23,191,572
1996	780 r	142,423 r	6,181 r	582,188 r	24,191,572
1995	346	126,021	6,678	674,797	22,876,069

r revised

\* Amounts expressed in thousands

(1) Source: Puerto Rico Planning Board.

(2) Source: Commissioner of Financial Institutions of the Commonwealth

COMMONWEALTH OF PUERTO RICO

Miscellaneous Statistics

June 30, 2004

Statistic	Quantity
Population (millions)	3.9 (p)
Life expectancy	76.8
Area in square miles	3,426
Fire protection:	
Number of stations	98
Number of fire personnel and officers	1,851
Calls answered	10,716
Building inspections conducted	56,093
Police protection:	
Number of stations	231
Police personnel and officers	21,185
Total police vehicles	6,907
Water system:	
Customers	1,256,988
Water consumption (millions of cubic meters)	359
Electric distribution system:	
Customers	1,419,602
Electricity consumption (millions of kilowatts)	20,260
Electricity production (millions of kilowatts)	24,100
Education:	
Enrollment in public schools:	
Kindergarten to sixth grade	321,653
Seventh to ninth grade	142,305
Tenth to twelfth grade	116,829
Enrollment in private schools:	
Kindergarten to sixth grade	172,479
Seventh to ninth grade	62,574
Tenth to twelfth grade	48,757
Enrollment in universities and colleges:	
Public	74,056
Private	132,735

(p) Preliminary

Source: Various Commonwealth agencies

COMMONWEALTH OF PUERTO RICO

General Fund Net Revenue

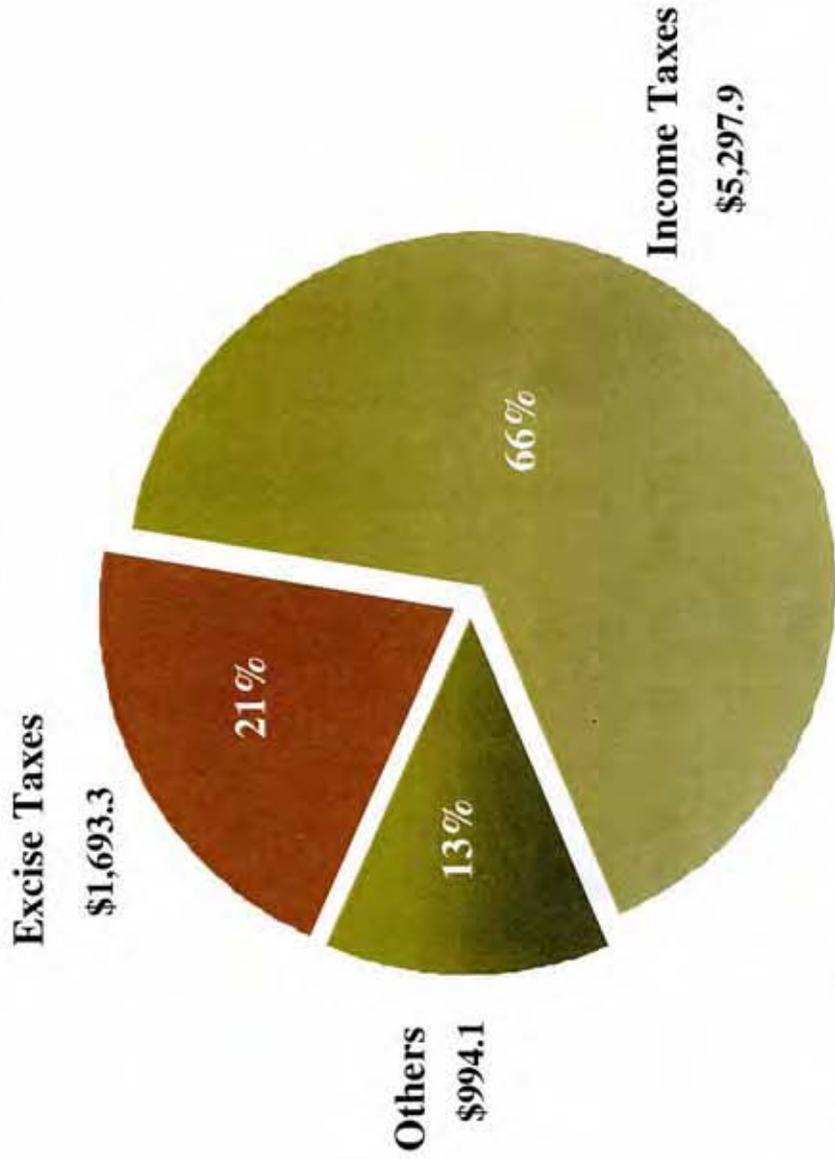
For the last ten fiscal years  
(In thousands)

	1992	1993	1996	1997	1998	1999	2000	2001	2002	2003	2004
<b>TOTAL</b>	\$ 3,861,136	5,080,139	5,247,616	5,600,748	5,002,506	6,550,043	6,043,613	6,962,134	7,454,399	7,841,742	7,985,388
<b>FROM INTERNAL REVENUE</b>	3,573,070	4,280,492	4,974,918	5,335,879	5,630,040	6,271,392	6,647,632	6,632,090	6,865,454	7,505,866	7,632,201
<b>TAX REVENUE</b>	3,356,945	4,531,788	4,729,520	5,095,218	5,358,805	5,982,504	6,344,398	6,204,639	6,428,083	6,910,345	7,091,198
<b>PROPERTY TAXES</b>	15,603	7,889	5,107	8,286	5,673	2,214	1,131	287	—	—	—
<b>INCOME TAXES, TOTAL</b>	2,335,631	3,220,937	3,368,175	3,610,016	3,972,869	4,433,804	4,856,011	4,778,590	4,878,418	5,170,294	5,297,931
INDIVIDUALS	1,122,335	1,578,269	1,709,116	1,823,337	2,026,612	2,244,376	2,352,066	2,259,090	2,449,982	2,767,678	2,720,920
CORPORATIONS	1,019,468	1,304,612	1,348,160	1,440,691	1,327,415	1,651,762	1,781,862	1,696,766	1,706,137	1,776,985	1,831,027
PARTNERSHIPS	1,167	3,391	3,323	2,120	4,404	2,087	2,339	3,026	2,670	2,101	3,005
WITHHOLDING TO NONRESIDENTS	62,066	79,072	78,235	88,603	192,463	369,384	557,276	696,835	583,256	517,141	631,100
TOLLGATE TAX (REGULAR)	98,502	110,945	78,554	83,640	65,285	49,249	57,203	23,664	44,213	35,576	24,411
TOLLGATE TAX (PREPAYMENT)	—	109,928	100,900	126,605	105,668	65,284	53,927	25,847	15,302	9,745	7,168
INTEREST SUBJECT TO 17%	8,505	6,070	6,662	7,582	11,406	10,666	11,674	14,782	14,310	11,278	10,108
TAXES ON DIVIDENDS	23,588	28,650	43,225	35,438	39,616	38,996	39,664	58,580	62,548	49,790	70,192
<b>INHERITANCE AND GIFT TAXES</b>	1,148	1,535	1,547	4,028	1,380	1,811	3,109	7,475	1,962	2,825	15,691
<b>EXCISE TAXES, TOTAL</b>	988,321	1,232,327	1,304,024	1,419,353	1,312,716	1,473,827	1,410,346	1,341,940	1,465,128	1,651,350	1,693,345
<b>ALCOHOLIC BEVERAGES, TOTAL</b>	216,890	222,187	237,915	229,043	238,118	243,464	236,374	237,512	249,705	299,582	296,302
DISTILLED SPIRITS	48,537	50,586	54,934	51,855	48,034	47,319	49,425	46,963	51,734	58,389	61,306
BEER	161,484	162,630	172,425	167,321	178,465	181,348	170,065	177,448	179,377	223,309	217,568
OTHER BEVERAGES	6,869	8,971	10,556	9,867	11,619	14,597	16,884	13,101	18,234	17,884	17,428
<b>GENERAL TAXES, TOTAL</b>	741,431	1,030,140	1,066,109	1,190,310	1,074,598	1,230,363	1,173,972	1,104,437	1,215,423	1,351,768	1,397,043
CIGARETTES	102,408	107,943	107,177	120,287	111,094	119,105	115,157	119,135	116,055	149,487	144,733
PETROLEUM PRODUCTS	8,742	16,706	20,006	22,095	6,172	5,562	4,689	7,046	5,095	5,860	4,934
MOTOR VEHICLE	178,329	319,676	307,931	365,820	350,004	411,573	389,995	406,252	418,024	499,252	551,181
HORSE RACES	17,062	30,828	29,535	29,138	27,401	21,405	26,351	18,893	22,033	28,872	28,865
INSURANCE PREMIUMS	16,570	20,942	20,748	19,430	19,364	20,368	21,564	22,845	24,290	26,771	27,217
CEMENT	1,563	1,849	1,901	2,234	1,702	2,431	2,707	3,426	3,279	3,432	—
SLOT MACHINES	—	—	—	—	12,230	26,330	30,869	—	36,953	90,018	76,966
CRUDE OIL AND DERIVED PRODUCTS	120,374	139,594	157,742	158,739	51,636	70,056	24,786	1,901	38,619	12,925	—
5% GENERAL EXCISE TAX	279,812	367,545	396,689	446,500	468,425	520,351	525,561	508,972	486,302	505,709	535,381
HOTEL ROOMS	7,189	10,800	11,237	12,139	13,299	15,923	17,275	—	—	9,056	—
OTHERS	9,390	14,287	13,143	13,928	13,271	17,473	15,194	16,686	64,636	20,539	24,334
<b>LICENSES</b>	46,842	49,100	50,467	53,535	66,167	70,848	73,801	76,338	82,575	85,876	84,231
<b>MOTOR VEHICLES</b>	36,964	38,530	39,667	42,354	46,268	46,781	49,133	49,834	54,896	58,426	55,638
<b>ENTERTAINMENT MACHINES</b>	—	—	—	—	7,327	9,235	10,545	11,322	12,874	13,932	14,393
<b>ALCOHOLIC BEVERAGES AND OTHERS</b>	9,878	10,570	10,800	11,181	12,572	14,832	14,123	15,182	14,805	13,518	14,200
<b>NON-TAX REVENUE</b>	216,125	248,704	245,598	240,661	271,235	288,888	303,234	427,451	437,371	595,521	531,003
TRADITIONAL LOTTERY	60,597	63,317	60,856	52,829	57,986	59,206	63,779	57,482	61,358	67,621	65,387
ELECTRONIC LOTTERY	59,091	59,414	57,068	47,994	54,683	53,013	70,209	70,211	57,897	89,443	86,115
TRANSFER IN FROM NON-BUDGETED FUNDS	—	—	—	—	—	—	—	—	—	89,093	80,000
MISCELLANEOUS	96,437	125,973	127,734	139,838	158,568	176,669	169,246	210,665	238,116	314,857	379,501
<b>FROM NON-INTERNAL REVENUE</b>	288,066	299,647	272,698	264,869	272,466	278,651	295,981	330,044	344,848	335,876	363,182
<b>CUSTOM DUTIES</b>	93,038	112,153	77,781	61,114	72,206	61,355	50,231	43,154	30,595	25,918	34,266
<b>EXPENSES ON OFF-SHORE SHIPMENTS</b>	195,028	187,494	194,917	203,755	200,260	245,750	286,890	314,253	309,958	328,921	328,921
<b>ADMINISTRATIVE MEASURES</b>	—	—	—	—	—	—	—	—	—	244,097	—

Note: The net revenue presented above include the actual revenue and the operating transfers in from other funds presented in the combined statement of revenue and expenditures - budget and actual - budget book.  
Source: Department of the Treasury of the Commonwealth

# Commonwealth of Puerto Rico General Fund Net Revenue

For the fiscal year 2004  
(In millions)

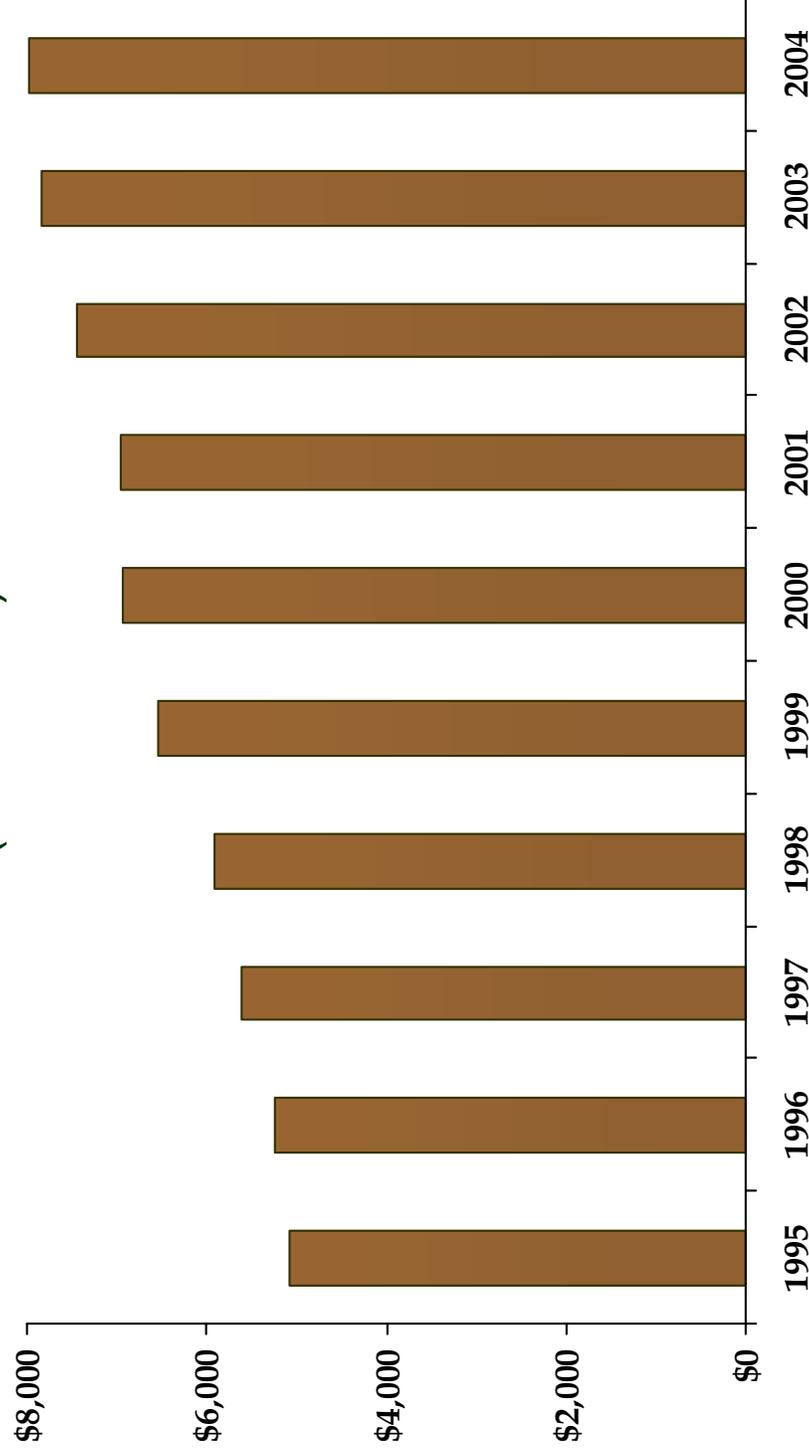


Note: The net revenue presented above include the actual revenue and the operating transfers-in from other funds presented in the combined statement of revenue and expenditures – budget and actual – budget basis.

Source: Department of the Treasury of the Commonwealth

# Commonwealth of Puerto Rico General Fund Net Revenue

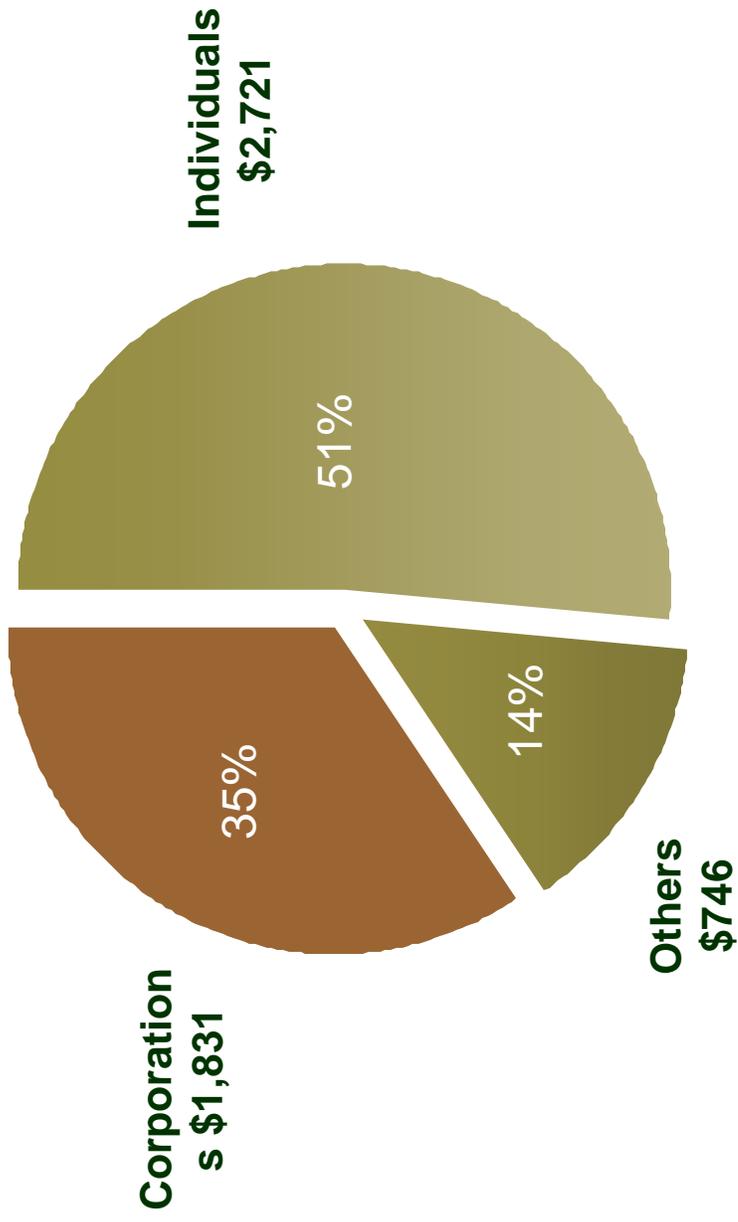
For the last ten fiscal years  
(In millions)



Note: The net revenue presented above, include the actual revenue and the operating transfers-in from other funds presented in the combined statement of revenue and expenditures – budget and actual – budget basis.

# Commonwealth of Puerto Rico Income Tax Receipts

For the fiscal year 2004  
(In millions)



Source: Department of the Treasury of the Commonwealth

COMMONWEALTH OF PUERTO RICO

Gross Product

For the last ten fiscal years  
(In millions)

	2004 (p)	2003 (r)	2002 (r)	2001	2000	1999	1998	1997	1996	1995
Gross product - (current prices)	\$ 50,320	\$ 47,354	\$ 45,071	\$ 44,047	\$ 41,419	\$ 38,281	\$ 35,111	\$ 32,343	\$ 30,357	\$ 28,452
Real gross product - (2000 prices)	\$ 41,418	\$ 42,690	\$ 41,909	\$ 42,049	\$ 41,419	\$ 40,228	\$ 38,659	\$ 37,445	\$ 36,210	\$ 35,064
Increase (decrease) in real gross product (%)										
Puerto Rico	2.8	2.0	(0.3)	1.5	3.0	4.1	3.2	3.4	3.3	3.4
United States (1)	4.6	2.3	0.7	1.4	4.6	4.1	4.3	4.3	2.7	3.5

(r) Revised

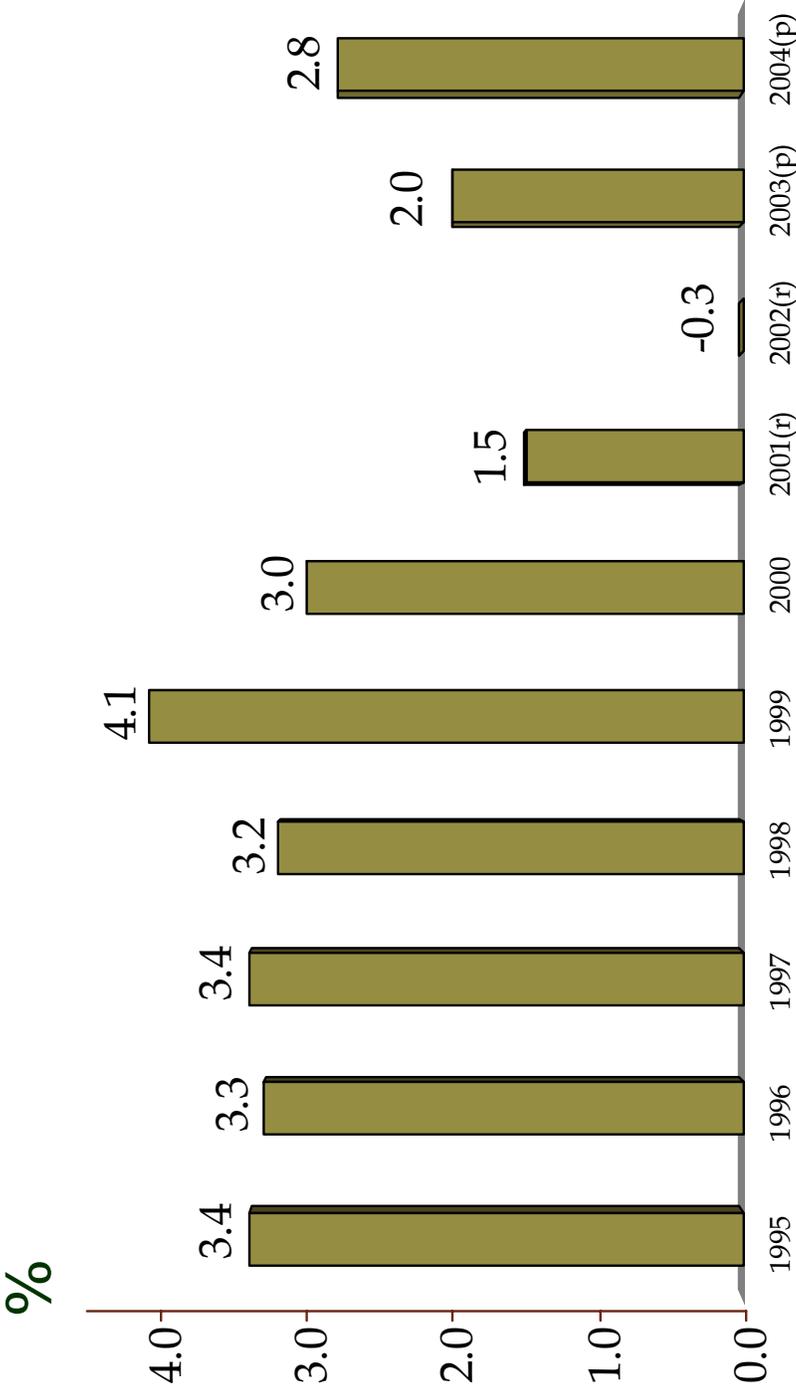
(p) Preliminary

Source: Puerto Rico Planning Board and the Government Development Bank for Puerto Rico

(1) Base in 2000 Chained Method

# Commonwealth of Puerto Rico Real Gross Product Growth

For the last ten fiscal years



(r) Revised  
(p) Preliminary  
Source: Puerto Rico Planning Board.

**COMMONWEALTH OF PUERTO RICO**

**Employment and Unemployment**

**For the last ten fiscal years  
(In thousands)**

Fiscal year	Labor force	Employed	Unemployed	Unemployment rate (%)
2004	1,392	1,234	158	11.4
2003	1,378	1,211	167	12.1
2002	1,330	1,170	160	12.0
2001	1,293	1,158	135	10.5
2000	1,303	1,160	143	11.0
1999	1,310	1,147	163	12.5
1998	1,316	1,137	179	13.6
1997	1,298	1,128	170	13.1
1996	1,267	1,092	175	13.8
1995	1,219	1,051	168	13.8

Source: Puerto Rico Department of Labor and Human Resources, Household Survey

COMMONWEALTH OF PUERTO RICO

Average Employment by Sector

For the last ten fiscal years  
(In thousands)

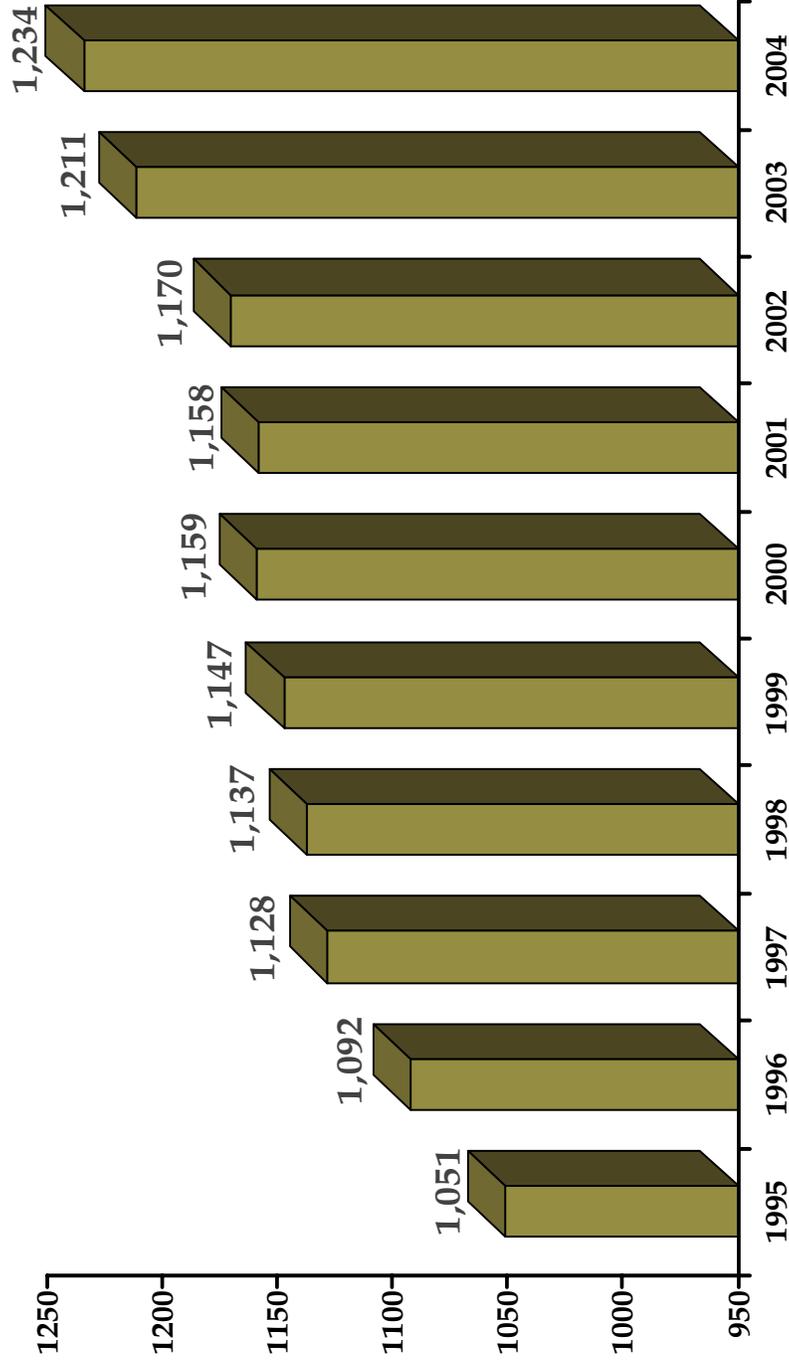
Sector	2004	2003	2002	2001	2000	1999	1998	1997	1996	1995
Agriculture	26	25	23	22	24	27	31	31	32	34
Manufacturing	139	136	139	159	159	159	161	161	167	172
Construction	90	83	86	85	85	78	69	64	59	57
Trade	259	257	240	242	239	229	236	228	218	211
Finance, insurance, and real estates	43	45	43	41	42	43	40	37	39	36
Transportation, communications, and public utilities	55	56	62	56	55	59	59	59	61	59
Services	347	335	316	302	307	306	297	285	270	249
Government (1)	275	274	261	251	249	246	244	263	246	233
Total	1,234	1,211	1,170	1,158	1,160	1,147	1,137	1,128	1,092	1,051

(1) Includes the Commonwealth, its municipalities and federal government, and excludes public corporations.

Sources: Puerto Rico Department of Labor and Human Resources, Household Survey

# Commonwealth of Puerto Rico Employment

For the last ten fiscal years  
(In thousands)



Source: Puerto Rico Department of Labor and Human Resources,  
Household Survey.

COMMONWEALTH OF PUERTO RICO

Tourism Indicators

For the last ten fiscal years

	2004 (p)	2003 (r)	2002	2001	2000	1999	1998	1997	1996	1995
All hotels and hostelry registration	2,012,574	1,964,963	1,821,274	1,836,377	1,674,092	1,637,620	1,570,683	1,461,567	1,400,815	1,302,387
Occupancy rates	68.9%	64.9%	61.8%	66.7%	70.7%	71.9%	67.3%	69.8%	69.0%	68.0%
Numbers of rooms	12,864	12,778	12,768	12,353	11,928	11,102	11,848	10,869	10,265	10,251
Visitors expenditures*	\$ 3,024	\$ 2,627	\$ 2,486	\$ 2,728	\$ 2,388	\$ 2,139	\$ 2,233	\$ 2,046	\$ 1,898	\$ 1,828

\*Amounts expressed in millions of dollars

(r) Revised

(p) Preliminary

Sources: Puerto Rico Tourism Company and Puerto Rico Planning Board