

**NEW ISSUE****Full-Book-Entry**

(See "Book-Entry Only System" under The Bonds)

In the opinion of Bond Counsel, subject to compliance with certain tax covenants, interest on the Bonds is not includable in gross income for federal income tax purposes under existing statutes, regulations, rulings and court decisions. However, see Tax Exemption for a description of the alternative minimum tax on corporations and certain other federal tax consequences of ownership of the Bonds. Bond Counsel is further of the opinion that the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation.

**\$503,963,264.10**  
**COMMONWEALTH OF PUERTO RICO**  
 Public Improvement Refunding Bonds, Series 1998  
 (General Obligation Bonds)

Dated: January 15, 1998†

Due: July 1, as shown below

The Bonds are issuable as registered bonds without coupons in denominations of \$5,000 and any multiple thereof (\$5,000 maturity amount and any multiple thereof in the case of the Capital Appreciation Bonds). Interest on the Bonds will be payable July 1, 1998 (representing five and one half months' interest) and each January 1 and July 1 thereafter, except that interest on the Capital Appreciation Bonds will be compounded on January 1 and July 1 of each year, commencing July 1, 1998, and will be payable only at maturity. The term Bonds are subject to redemption prior to maturity as set forth herein, the earliest possible date of redemption being July 1, 2008.

The Bonds are general obligations of the Commonwealth of Puerto Rico. The good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds. The Constitution of Puerto Rico provides that public debt of the Commonwealth, including the Bonds, constitutes a first claim on available Commonwealth revenues.

**\$203,540,000 Serial Bonds**

<u>Amount</u>	<u>Maturity</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>Amount</u>	<u>Maturity</u>	<u>Interest Rate</u>	<u>Yield</u>
\$3,665,000	2000	4.50%	3.80%	\$ 9,255,000	2007	5.00%	4.40%
7,005,000	2001	4.50	3.90	9,715,000	2009	5.50	4.45
7,320,000	2002	4.50	4.00	30,760,000	2010	5.50	4.55
7,650,000	2003	4.50	3.95	32,475,000	2011	5.50	4.59
7,995,000	2004	5.00	4.20	34,290,000	2012	5.50	4.64
8,390,000	2005	5.00	4.30	36,210,000	2013	5.50	4.66
8,810,000	2006	5.00	4.35				

\$ 6,159,601.45 Capital Appreciation Bonds due July 1, 2008 - Yield - 4.42%

\$17,407,612.80 Capital Appreciation Bonds due July 1, 2014 - Yield - 4.85%

\$16,469,587.20 Capital Appreciation Bonds due July 1, 2015 - Yield - 4.90%

\$15,625,102.50 Capital Appreciation Bonds due July 1, 2016 - Yield - 4.98%

\$14,841,500.25 Capital Appreciation Bonds due July 1, 2017 - Yield - 4.95%

\$14,149,859.90 Capital Appreciation Bonds due July 1, 2018 - Yield - 4.95%

\$187,530,000 4.50% Term Bonds due July 1, 2023 - Yield - 5.03%

\$28,240,000 5.00% Term Bonds due July 1, 2026 - Yield - 5.05%

(plus accrued interest)

The Bonds are offered for delivery when, as and if issued and accepted by the Underwriters subject to the approval of legality by Brown & Wood LLP, New York, New York, Bond Counsel and certain other conditions. Certain legal matters will be passed upon for the Underwriters by Pietrantonio Méndez & Alvarez, San Juan, Puerto Rico. It is expected that settlement for the Bonds will occur in New York, New York on or about January 29, 1998.

MORGAN STANLEY DEAN WITTER

BEAR, STEARNS &amp; CO. INC.

GOLDMAN, SACHS &amp; CO.

MERRILL LYNCH &amp; CO.

PAINWEBBER INCORPORATED

RAYMOND JAMES &amp; ASSOCIATES INC.

JP MORGAN &amp; CO.

PRUDENTIAL SECURITIES INCORPORATED

SAMUEL A. RAMIREZ CO., INC.

SALOMON SMITH BARNEY

January 15, 1998

†Capital Appreciation Bonds dated their date of delivery.



# Commonwealth of Puerto Rico

## Governor

PEDRO ROSSELLÓ

## Members of the Cabinet

ANGEL MOREY  
*Chief of Staff*

NORMA E. BURGOS ANDÚJAR  
*Secretary of State*

JOSÉ A. FUENTES AGOSTINI  
*Secretary of Justice*

XENIA VÉLEZ SILVA  
*Secretary of the Treasury*

VÍCTOR FAJARDO  
*Secretary of Education*

CÉSAR ALMODÓVAR MARCHANY  
*Secretary of Labor and  
Human Resources*

CARMEN FELICIANO DE MELECIO  
*Secretary of Health*

MIGUEL A. MUÑOZ MUÑOZ  
*Secretary of Agriculture*

CARLOS I. PESQUERA MORALES  
*Secretary of Transportation  
and Public Works*

CARLOS J. VIVONI  
*Secretary of Economic  
Development and Commerce*

CARMEN L. RODRÍGUEZ RODRÍGUEZ  
*Secretary of Family Affairs*

ANA CARMEN ALEMAÑY  
*Secretary of Housing*

DANIEL PAGÁN ROSA  
*Secretary of Natural and  
Environmental Resources*

JOSÉ A. ALICEA  
*Secretary of Consumer Affairs*

ERIC R. LABRADOR ROSA  
*Secretary of Sports and Recreation*

NYDIA COTTO VIVES  
*Secretary of Corrections  
and Rehabilitation*

PEDRO TOLEDO  
*Commissioner of  
Protection and Public Safety*

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### *Legislative Officers*

CHARLIE RODRÍGUEZ  
President, Senate

### *Fiscal Officers*

JORGE E. APONTE HERNÁNDEZ  
Director, Office of Management  
and Budget

EDISON MISLA ALDARONDO  
Speaker, House of  
Representatives

MARCOS RODRÍGUEZ-EMA  
President, Government Development  
Bank for Puerto Rico

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### *Others*

NORMA E. BURGOS ANDÚJAR  
*President, Planning Board*

XAVIER ROMEU  
*Director, Federal Affairs Office*

No dealer, broker, sales representative or other person has been authorized by the Commonwealth or the Underwriters to give any information or to make any representations other than those contained herein and, if given or made, such other information or representations must not be relied upon as having been authorized by the Commonwealth or any Underwriter. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Bonds, by any person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. The information set forth herein has been obtained from the Commonwealth and other official sources that are believed to be reliable, but is not guaranteed as to accuracy or completeness and is not to be construed as a representation by any Underwriter. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Commonwealth since the date hereof.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS OFFERED HEREBY AND THE COMMONWEALTH'S OUTSTANDING GENERAL OBLIGATION BONDS AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

## TABLE OF CONTENTS

	<u>Page</u>		<u>Page</u>
INTRODUCTORY STATEMENT .....	1	Economic Development Program - New	
OVERVIEW .....	1	Economic Model .....	I-5
Economic Trends .....	1	Employment and Unemployment .....	I-6
Fiscal Management .....	3	Economic Performance by Sector .....	I-6
Debt Management .....	3	Higher Education .....	I-14
PLAN OF FINANCING .....	4	Tax Incentives .....	I-15
Sources and Uses of Funds .....	5	Debt .....	I-19
THE BONDS .....	5	Public Sector Debt .....	I-19
General .....	5	Debt Service Requirements for Commonwealth	
Book-Entry Only System .....	5	General Obligation Bonds and Certain	
Payments and Transfers .....	7	Guaranteed Debt .....	I-20
Discontinuance of the Book-Entry Only System .....	7	Commonwealth Guaranteed Debt .....	I-21
Authorization .....	7	Trends of Public Sector Debt .....	I-21
Redemption .....	7	Public Corporations .....	I-23
Notice and Effect of Redemption of Bonds .....	8	Government Development Bank for Puerto Rico .....	I-24
Security .....	9	Other Public Corporations .....	I-25
Payment Record .....	10	Insurance Matters .....	I-30
Debt Limitation .....	10	Retirement Systems .....	I-30
Maturity Limitation .....	11	Summary of Commonwealth Financial Statements .....	I-33
PUBLIC SECTOR DEBT OF THE		Puerto Rico Taxes, Other Revenues and	
COMMONWEALTH .....	11	Expenditures .....	I-33
Pro Forma Public Sector Debt .....	11	Summary and Management Discussion of	
Debt Service Requirements for Commonwealth		General Fund Results .....	I-33
General Obligation Bonds and Certain		Major Sources of General Fund Revenues .....	I-35
Guaranteed Debt .....	11	Collections of Income and Excise Taxes .....	I-37
TAX EXEMPTION .....	13	Transfers to General Obligation	
Capital Appreciation Bonds and		Redemption Fund .....	I-37
Original Issue Discount .....	13	Components of General Fund Expenditures .....	I-38
Premium Bonds .....	14	Federal Grants .....	I-38
UNDERWRITING .....	14	Budget of the Government of Puerto Rico .....	I-39
LEGAL MATTERS .....	14	Office of Management and Budget .....	I-39
LEGAL INVESTMENT .....	14	Budgetary Process .....	I-39
VERIFICATION OF MATHEMATICAL		Financial Control and Adjustment	
COMPUTATIONS .....	15	Procedures .....	I-40
GOVERNMENT DEVELOPMENT BANK		Appropriations .....	I-40
FOR PUERTO RICO .....	15	Fiscal 1997 Budget .....	I-42
RATINGS .....	15	Fiscal 1998 Budget .....	I-44
CONTINUING DISCLOSURE .....	15	Differences between Budget and General	
MISCELLANEOUS .....	17	Purpose Financial Statements .....	I-45
Appendix I - Commonwealth of Puerto Rico .....	I-1	Appendix II - Comprehensive Annual Financial	
Geographic Location and Demography .....	I-1	Report of the Commonwealth of	
Relationship with the United States .....	I-1	Puerto Rico for the fiscal year ended	
Governmental Structure .....	I-2	June 30, 1997 .....	II-1
Political Trends .....	I-2	Appendix III- Form of Opinion of Bond Counsel .....	III-1
The Economy .....	I-3	Appendix IV - Table of Accreted Values .....	IV-1
General .....	I-3		

**\$503,963,264.10**

**Commonwealth of Puerto Rico**

**Public Improvement Refunding Bonds, Series 1998**

**(General Obligation Bonds)**

**INTRODUCTORY STATEMENT**

This Official Statement of the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico"), which includes the cover page and the appendices, provides certain information in connection with the sale of \$503,963,264.10 Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 1998 (the "Bonds"). The Bonds maturing on July 1, 2008 and July 1, 2014 through July 1, 2018 are being issued as capital appreciation bonds (the "Capital Appreciation Bonds").

The Bonds are being issued under the provisions of Act No. 2 of the Legislature of Puerto Rico, approved October 10, 1985, and Joint Resolution No. 57 of the Legislature of Puerto Rico, approved July 12, 1993 (collectively, the "Act"), and pursuant to a resolution authorizing the issuance of the Bonds (the "Bond Resolution") adopted by the Secretary of the Treasury and approved by the Governor of Puerto Rico on January 15, 1998.

Under the Act, the good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds. The Constitution of Puerto Rico provides that public debt of the Commonwealth, including the Bonds, constitutes a first claim on available Commonwealth revenues.

**OVERVIEW**

The following is a summary of certain information regarding the Commonwealth contained in *Appendix I* and does not purport to be complete. This summary is qualified in its entirety by reference to more detailed information appearing in *Appendix I*, which should be read in its entirety.

Puerto Rico is located approximately 1,600 miles southeast of New York City. Its population was estimated to be 3,726,000 in fiscal 1996. Puerto Rico's constitutional status is that of an unincorporated territory of the United States and the ultimate source of power over Puerto Rico, pursuant to the territorial clause of the Federal Constitution, is the United States Congress. The Government of Puerto Rico exercises virtually the same control over its internal affairs as do the fifty states, with similar separation of powers among the executive, legislative and judicial branches. The official languages of Puerto Rico are Spanish and English.

**Economic Trends**

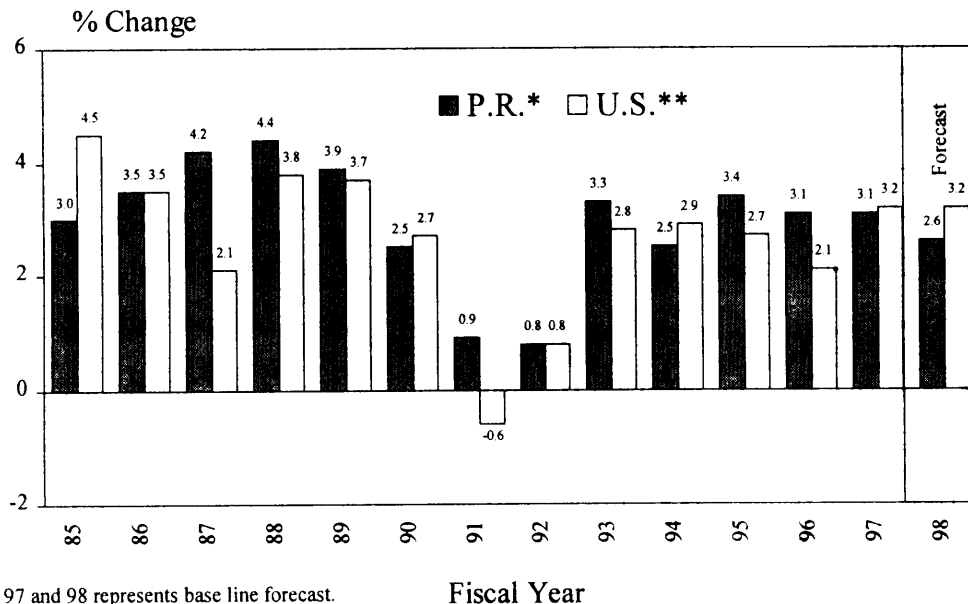
Puerto Rico's more than decade-long economic expansion continued throughout the five-year period from fiscal 1993 through fiscal 1997. Almost every sector of the economy participated and record levels of employment were achieved. Factors behind this expansion included government-sponsored economic development programs, periodic declines in the exchange value of the United States dollar, increases in the level of federal transfers, and the relatively low cost of borrowing.

Gross product in fiscal 1993 was \$25.1 billion (\$24.5 billion in 1992 prices) and gross product in fiscal 1997 was \$32.0 billion (\$27.6 billion in 1992 prices). This represents an increase in gross product of 27.5% from fiscal 1993 to 1997 (12.6% in 1992 prices). Since fiscal 1985, personal income, both aggregate and per capita, has increased consistently each fiscal year. In fiscal 1996, aggregate personal income was \$29.4 billion (\$27.8 billion in 1992 prices) and personal income per capita was \$7,882 (\$7,459 in 1992 prices).

Average employment increased from 999,000 in fiscal 1993, to 1,128,300 in fiscal 1997. Average unemployment decreased from 16.8% in fiscal 1993, to 13.1% in fiscal 1997. According to the Labor Department's Household Employment Survey, during fiscal 1997, total employment increased 3.3% over fiscal 1996. Total employment averaged 1,128,300 in fiscal 1997, compared to 1,092,300 in fiscal 1996. The seasonally adjusted unemployment rate for November 1997 was 14.0%.

According to the Planning Board's preliminary data released on November 5, 1997, the gross product growth for fiscal 1997 was 3.1%. The Planning Board's gross product forecast for fiscal 1998 projects an increase of 2.6% over fiscal 1997.

## Real Rates of Growth of GNP



\* 97 and 98 represents base line forecast.

\*\* DRI Forecast.

Puerto Rico has a diversified economy with the manufacturing and service sectors comprising the principal sectors. Manufacturing is the largest sector in terms of gross domestic product. According to the Planning Board's preliminary figures, in fiscal 1996 manufacturing generated \$18.9 billion, or 41.4% of gross domestic product and accounted for 15.3% of total employment; as compared with fiscal 1995, when it generated \$17.9 billion, or 41.9%, of gross domestic product and accounted for 16.4% of total employment. See "Economic Performance by Sector" under *The Economy in Appendix I*. Manufacturing in Puerto Rico is now more diversified than during the earlier phases of its industrial development. In the last two decades, industrial development has tended to be more capital intensive and more dependent on skilled labor. This gradual shift in emphasis is best exemplified by the heavy investment in the pharmaceutical, scientific instruments, computer, microprocessor, medical product and electrical product industries over the last decade. One of the factors assisting the development of the manufacturing sector has been the tax incentives offered by the federal and Puerto Rico governments. Recently enacted federal legislation amending Internal Revenue Code Section 936, however, phases out the federal tax incentives during a ten-year period. See "Tax Incentives—Sections 30A and 936 of the Code" under *The Economy in Appendix I*.

The services sector, which includes hotel and related services and which, during fiscal 1997, accounted for approximately 48.8% of total employment, accounted for \$17.1 billion, or 37.6%, of Puerto Rico's gross domestic product in fiscal 1996, as compared with \$16.2 billion, or 38.1%, of gross domestic product in fiscal 1995. The services sector, particularly wholesale and retail trade and finance, insurance and real estate, has experienced significant growth partly in response to the expansion of the manufacturing sector.

Growth in construction and tourism has also contributed to increased economic activity in fiscal 1997. The growth in the construction industry has been evidenced by a nominal increase of 14.7 % in construction investment for fiscal 1997 over fiscal 1996. Tourism has grown in each fiscal year since fiscal 1985. More than 4.3 million visitors spent over \$2.0 billion in Puerto Rico in fiscal 1997. San Juan has become the largest home port for cruise ships in the Caribbean and the second largest home port for cruise ships in the world. Twenty-four U.S. and international airlines offer scheduled service to and from San Juan, and a major U.S. airline uses San Juan as a hub for its intra-Caribbean operations. This reflects the importance of Puerto Rico as a tourist destination and as a transportation hub in the Caribbean.

### **Fiscal Management**

Fiscal responsibility for the Commonwealth is shared among the Department of the Treasury, the Office of Management and Budget and Government Development Bank for Puerto Rico ("Government Development Bank"). The Department of the Treasury is responsible for collecting most of the Commonwealth's revenues, overseeing preparation of its financial statements and contributing to the preparation of the budget. The Office of Management and Budget prepares the Commonwealth's budget and has the responsibility for monitoring expenditures. Government Development Bank is the fiscal agent and financial advisor to the Commonwealth and its agencies, public corporations and municipalities and coordinates the management of public finances.

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 revenues, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."

Since fiscal 1990 the complete financial statements of the Commonwealth have been audited. The financial statements for the Commonwealth for fiscal 1997 have been audited by Deloitte & Touche LLP whose report thereon is set forth in *Appendix II*. For a summary of the Commonwealth's significant accounting policies, see Note 1 to *Appendix II*. Preparation of the audited financial statements of the Commonwealth involves the collection and combination of audited financial statements from 48 separate reporting entities.

### **Debt Management**

The Constitution of Puerto Rico provides a limitation on the amount of general obligation debt that can be issued. The Commonwealth's policy has been and continues to be to maintain the level of such debt within a prudent range below the constitutional limitation. See "Debt Limitation" under *The Bonds*.

Historically, the Commonwealth has maintained a fiscal policy which provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. The Commonwealth also has sought opportunities to realize debt service savings by refunding outstanding debt with obligations bearing lower interest rates.

During the period from fiscal 1992 to 1996, public sector debt and gross product increased 27.5% and 27.7%, respectively. During the period from fiscal 1993 to 1997, however, public sector debt increased 37.0% while gross product increased 27.5%. This higher level of growth of public sector debt over that of gross product is due to the increase during fiscal 1996 and 1997 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. This trend of higher levels of public sector debt relative to the growth in gross product is expected to continue during the next few fiscal years as the level of public sector capital investment remains high. See "Trends of Public Sector Debt" under *Debt* and "Economic Performance by Sector - Construction" under *The Economy* in *Appendix I*.

Short-term debt outstanding relative to total debt was 10.1% as of December 31, 1997. Short-term debt outstanding includes \$600,000,000 in tax and revenue anticipation notes issued on December 3, 1997 and maturing on July 30, 1998. Excluding said tax and revenue anticipation notes, short term debt outstanding relative to total debt outstanding as of December 31, 1997 was 7.4%.

## PLAN OF FINANCING

The Bonds will be issued under the provisions of the Act for the purpose of refunding the following Commonwealth of Puerto Rico Public Improvement Bonds (the "Refunded Bonds"), such Refunded Bonds maturing or being redeemed on the dates, and at the prices, set forth below:

Refunded Bonds	Amount to be Refunded	Interest Rate	Maturity Date July 1,	Redemption Date July 1,	Redemption Price (% of Par)
Public Improvement Bonds of 1988, Series A	\$ 4,851,415.95*	—	1998	—	—
Public Improvement Bonds of 1989, Series A	7,450,000.00	7.10%	1998	—	—
Public Improvement Bonds of 1990	7,630,000.00	6.70	1998	—	—
Public Improvement Bonds of 1991	3,910,000.00	6.70	1998	—	—
Public Improvement Bonds of 1993	5,515,000.00	5.00	1998	—	—
Public Improvement Bonds of 1993	10,725,000.00	5.850	2010	2002	101.50%
Public Improvement Bonds of 1993	11,380,000.00	5.850	2011	2002	101.50
Public Improvement Bonds of 1993	52,925,000.00	5.850	2015	2002	101.50
Public Improvement Bonds of 1993	48,855,000.00	5.875	2018	2002	101.50
Public Improvement Bonds of 1993	80,460,000.00	6.00	2022	2002	101.50
Public Improvement Bonds of 1994	4,900,000.00	5.05	1998	—	—
Public Improvement Bonds of 1994	9,785,000.00	6.35	2010	2004	101.50
Public Improvement Bonds of 1994	10,405,000.00	6.40	2011	2004	101.50
Public Improvement Bonds of 1994	78,105,000.00	6.45	2017	2004	101.50
Public Improvement Bonds of 1994	113,790,000.00	6.50	2023	2004	101.50
Public Improvement Bonds of 1997	<u>27,500,000.00</u>	6.00	2026	2007	101.50
<b>Total</b>	<b><u>\$478,186,415.95</u></b>				

\*Capital Appreciation Bonds. Stated amount reflects initial principal amount.

The refunding will permit the Commonwealth to realize savings on the aggregate debt service requirements on its general obligation bonds. The Secretary of the Treasury will deposit the net proceeds of the Refunding Bonds and certain other available moneys with State Street Bank and Trust Company, N.A., as Escrow Agent. A portion of the net proceeds and such other available moneys will be invested in noncallable direct obligations of the United States, the principal of and interest on which, with any remaining net proceeds not so invested, will be sufficient to pay the principal of and premium, if any, on the Refunded Bonds on the respective maturity or redemption dates set forth above, and to pay interest accrued thereon to such dates. None of such dates will be changed by the Secretary of the Treasury. The sufficiency of the amount so deposited, with the investment earnings thereon, to accomplish the refunding of the Refunded Bonds will be verified by Deloitte & Touche LLP, the verification agent. Upon the deposit with the Escrow Agent referred to above, the Refunded Bonds will cease to be outstanding under the terms of their respective authorizing resolutions. Under the Act, once the above deposit of cash and noncallable direct obligations of the United States has been made, all the Refunded Bonds will be deemed not to be outstanding for the purpose of applying the debt limitation under Section 2 of Article VI of the Commonwealth's Constitution.



## Sources and Uses of Funds

### Sources:

Principal amount of the Bonds .....	\$503,963,264.10
Net original issue premium .....	680,817.05
Other available moneys .....	<u>19,605,000.00</u>
Total sources .....	<u>\$524,249,081.15</u>

### Uses:

Deposit to Escrow Fund .....	\$520,063,182.34
Underwriting discount and legal, printing, and other financing expenses .....	<u>4,185,898.81</u>
Total uses .....	<u>\$524,249,081.15</u>

## THE BONDS

### General

The Bonds will be dated, will bear interest at such rates (or have such yields in the case of the Capital Appreciation Bonds), payable at such times, and will mature on the dates and in the principal amounts (except with respect to the Capital Appreciation Bonds) set forth on the cover page of this Official Statement. The Bonds are subject to redemption at the times and at the prices set forth below in "Redemption."

The Capital Appreciation Bonds will be payable at maturity in amounts (the "Accreted Values") equal to the original principal amounts of such Bonds plus interest from their dated dates, compounded semi-annually. The Accreted Value per \$5,000 maturity amount of each Capital Appreciation Bond, on the date of delivery of the Bonds and on each January 1 and July 1, commencing July 1, 1998, is shown in Appendix IV hereto. The Accreted Value of the Capital Appreciation Bonds on any other date is calculated on the assumption that such Accreted Value increases in equal daily amounts up to the Accreted Value on the next January 1 or July 1, as appropriate. Interest on the Capital Appreciation Bonds will be payable only at maturity.

### Book-Entry Only System

The following information concerning The Depository Trust Company ("DTC"), New York, New York and DTC's book-entry system has been obtained from DTC; and neither the Commonwealth nor the Underwriters take any responsibility for the accuracy thereof.

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully registered Bonds in the name of Cede & Co. (DTC's partnership nominee). One fully registered Bond will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants (the "Participants") deposit with DTC. DTC also facilitates the settlement among Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations (the "Direct Participants"). DTC is owned by a number of its Direct

Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a DTC Participant, either directly or indirectly (the "Indirect Participants"). The Rules applicable to DTC and its Participants are on file with the Securities and Exchange Commission.

Purchases of the Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of a Bond (a "Beneficial Owner") will in turn be recorded in the Direct or Indirect Participants' records. Beneficial Owners will not receive written confirmations from DTC of their purchases, but Beneficial Owners are expected to receive written confirmation providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds will be accomplished by entries made on the books of Participants acting on behalf of the Beneficial Owners. Beneficial Owners will not receive definitive Bonds representing their ownership interests in Bonds except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers all Bonds deposited by Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. The deposit of Bonds with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices will be sent to Cede & Co. If less than all of the Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in the Bonds to be redeemed. Neither DTC nor Cede & Co. will consent or vote with respect to the Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the Commonwealth as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, redemption premium, if any, and interest payments on the Bonds will be made to DTC. DTC's practice is to credit Direct Participants' accounts on the payable date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on the payable date. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC, the Commonwealth, or Banco Popular de Puerto Rico as paying agent and registrar (the "Registrar"), subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, redemption premium, if any, and interest to DTC is the responsibility of the Commonwealth or the Registrar, disbursement of such payments to Direct Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners shall be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the Commonwealth or the Registrar. Under such circumstances, in the event that a successor securities depository is not obtained, definitive Bonds are required to be printed and delivered.

The Commonwealth may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, definitive Bonds will also be printed and delivered.

**Payments and Transfers**

No assurance can be given by the Commonwealth that DTC will make prompt transfer of payments to the Participants or that Participants will make prompt transfer of payments to Beneficial Owners. The Commonwealth is not responsible or liable for payment by DTC or Participants or for sending transaction statements or for maintaining, supervising or reviewing records maintained by DTC or Participants.

For every transfer and exchange of the Bonds, the Beneficial Owners may be charged a sum sufficient to cover any tax, fee or other charge that may be imposed in relation thereto.

**Discontinuance of the Book-Entry Only System**

In the event that such book-entry only system is discontinued, the following provisions will apply: principal of and redemption premium, if any, on the Bonds shall be payable in lawful money of the United States of America at the principal office of the Registrar in San Juan, Puerto Rico. Interest on the Bonds (except for the interest on the Capital Appreciation Bonds, which interest is payable at maturity of such Bonds) will be payable by check mailed to the respective addresses of the registered owners determined as of the applicable record date thereof provided in the Bond Resolution as shown on the registration books of the Commonwealth maintained by the Registrar. The Bonds will be issued only as registered Bonds without coupons in denominations of \$5,000 and any multiple thereof (except for the Capital Appreciation Bonds, which will be issued as fully registered bonds in denominations of \$5,000 maturity amounts and multiples thereof). The transfer of the Bonds will be registrable and they may be exchanged at the corporate trust office of the Registrar in San Juan, Puerto Rico, upon the payment of any taxes or other governmental charges required to be paid with respect to such transfer or exchange.

**Authorization**

Section 2 of Article VI of the Constitution of the Commonwealth provides that the power of the Commonwealth to contract and to authorize the contracting of debts shall be exercised as determined by the Legislature. Pursuant to this power, the Legislature enacted the Act, which authorizes the issuance of the Bonds.

**Redemption**

*Optional Redemption.* At the option of the Secretary of the Treasury and upon at least 30 days' notice, the term Bonds maturing July 1, 2023 and July 1, 2026 are subject to redemption, from any moneys that may be available for that purpose (other than from moneys set aside in respect of an amortization requirement), prior to maturity, on or after July 1, 2008, either in whole or in part, on any date, as directed by the Secretary of the Treasury, at the redemption prices (expressed as a percentage of principal amount) set forth in the table below, together with accrued interest to the date fixed for redemption:

<u>Period During Which Redeemed</u>	<u>Redemption Price</u>
July 1, 2008 through June 30, 2009 .....	101 %
July 1, 2009 through June 30, 2010 .....	100½
July 1, 2010 and thereafter .....	100

The Bonds maturing prior to July 1, 2023 are not subject to redemption prior to maturity.

*Mandatory Redemption.* The term Bonds maturing July 1, 2023 and July 1, 2026 are subject to redemption to the extent of the respective amortization requirements therefor set forth below (less the amount applied to the purchase of any such Bonds and otherwise subject to adjustment as described below), upon at least 30 days' notice, on July 1, 2019 and on July 1 in each year thereafter at a redemption price of par plus accrued interest to the dates fixed for redemption:

<u>July 1</u>	<u>Amortization Requirements for Bonds due July 1</u>	
	<u>2023</u>	<u>2026</u>
	(dollars in thousands)	
2019 .....	\$38,470,000	
2020 .....	40,235,000	
2021 .....	42,085,000	
2022 .....	44,020,000	
2023 .....	22,720,000*	
2024 .....		\$ 235,000
2025 .....		245,000
2026 .....		27,760,000*
 <b>Average life (years)</b> .....	 23.3	 28.4

\*Maturity.

If the amount of the Bonds purchased or redeemed pursuant to an amortization requirement during any fiscal year exceeds the amount of the amortization requirement for such Bonds for such fiscal year, the amortization requirement for such Bonds may be decreased for such subsequent fiscal years and in such amounts aggregating the amount of such excess as the Secretary of the Treasury shall determine.

#### **Notice and Effect of Redemption of Bonds**

Any redemption of the Bonds, either in whole or in part, shall be made upon at least thirty (30) days' prior notice by mail to DTC or, if the book-entry only system as described above has been discontinued, by first class mail, postage prepaid, to all registered owners in the manner and under the terms and conditions provided in the Bond Resolution. On the date designated for redemption, notice having been given as provided in the Bond Resolution and moneys for payment of the principal of and redemption premium, if any, and accrued interest on the Bonds or portions thereof so called for redemption being held by the Registrar, interest on the Bonds or portions thereof so called for redemption shall cease to accrue. Subject to certain provisions of the Bond Resolution, Bonds and portions of Bonds which have been duly called for redemption under the provisions of the Bond Resolution, or with respect to which irrevocable instructions to call for redemption or to pay at maturity have been given, and for the payment of the principal of and redemption premium, if any, and the accrued interest on which sufficient moneys or investments permitted by law shall be held in separate trust for the owners of the Bonds or portions thereof to be paid or redeemed, shall not be deemed to be outstanding under the Bond Resolution, and the registered owners thereof shall have no rights in respect thereof except to receive payment of the principal thereof and the redemption premium, if any, and the accrued interest thereon from said separate trust.

Each notice of redemption shall contain, among other things, the CUSIP identification number of the Bonds (or portion thereof) being called for redemption, the redemption date and price and the address at which such Bonds are to be surrendered for payment of the redemption price. Any defect in such notice or the failure so to mail any such notice to DTC in respect of, or the registered owner of, any Bond will not affect the validity of the proceedings for the redemption of any other Bond.

If less than all the Bonds of any maturity are called for redemption, the particular Bonds so called for redemption shall be selected by the Registrar by such method as it deems fair and appropriate, except that so long

as the book-entry only system shall remain in effect, in the event of any such partial redemption, DTC shall reduce the credit balances of the applicable DTC Participants in respect of the Bonds and such DTC Participants shall in turn select those Beneficial Owners whose ownership interests are to be extinguished by such partial redemption each by such method as DTC or such DTC Participant, as the case may be, in its sole discretion, deems fair and appropriate.

## **Security**

### *Provision for Payment of Public Debt*

The Act provides that the good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds issued under the provisions of the Act. The Secretary of the Treasury is authorized and directed under the Act to pay the principal of and interest on the Bonds as the same become due and payable from any funds available for such purpose with the Department of the Treasury in the fiscal year in which such payment is due. The provisions contained in the Act regarding the payment of the principal of and interest on the Bonds are considered to be a continuous appropriation for the Secretary of the Treasury to make such payments, even though no specific appropriations are made for such purposes. Such payments are required to be made pursuant to the provisions of the laws of the Commonwealth that regulate the disbursement of public funds.

The Constitution of Puerto Rico provides that public debt of the Commonwealth will constitute a first claim on available Commonwealth revenues. Public debt includes general obligation bonds and notes of the Commonwealth and any payments required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public instrumentalities.

The Commonwealth has allocated certain motor vehicle fuel taxes, crude oil and derivative products excise taxes and license fees to Puerto Rico Highway and Transportation Authority (the "Highway Authority"). The amounts so allocated, however, are subject to first being applied to payment of the principal of and interest on the Commonwealth public debt, but only if and to the extent that all other available revenues of the Commonwealth are insufficient for that purpose. The Commonwealth has never applied such amounts to the payment of its public debt.

Since fiscal 1989, the Commonwealth has pledged to Puerto Rico Infrastructure Financing Authority certain federal excise taxes imposed on alcoholic beverages and tobacco products produced in Puerto Rico and sold in the United States, which taxes are returned to the Commonwealth. The amounts so pledged, however, are subject to first being applied to payment of the principal of and interest on the Commonwealth public debt, but only if and to the extent that all other available revenues of the Commonwealth are insufficient for that purpose. The Commonwealth has never applied such amounts to the payment of its public debt.

The Constitution expressly empowers a holder of bonds and notes evidencing public debt to bring suit against the Secretary of the Treasury to require application of available revenues, including surplus, to the payment of principal of and interest on public debt when due.

### *Special Fund for General Obligation Debt Service*

Act No. 83, approved 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 exempt from taxation. The proceeds of said tax are credited to the Special Fund for the Amortization and Redemption of General Obligations Evidenced by Bonds and Promissory Notes (the "Redemption Fund"), for application to the payment of general obligation bonds and notes of the Commonwealth.

Act No. 39, approved May 13, 1976, as amended ("Act No. 39"), requires the Secretary of the Treasury to transfer each month from available funds of the Commonwealth to the Redemption Fund such amounts which together with certain funds otherwise deposited therein will be equal to the sum of one-sixth of the interest to be

paid in the next six months and one-twelfth of the principal to be paid or required to be amortized within the next twelve months on all bonds and notes of the Commonwealth for which its full faith and credit are pledged as the same become due and for which the guaranty of the Commonwealth has been exercised. Moneys in the Redemption Fund are held in trust by Government Development Bank. Act No. 39 provides that the obligation of the Secretary of the Treasury to make the above transfers is cumulative, and the amount of any deficiency in any month shall be added to the amount of transfers required in future months until such deficiency has been fully paid. On December 31, 1997, the amount on deposit in the Redemption Fund was \$179,969,909, which was the required amount.

Act No. 39 expressly relates to direct obligations of the Commonwealth. It may also apply to the payment of Commonwealth guaranteed obligations of public corporations outstanding prior to the date of its adoption but not to the payment of bonds and other obligations of such public corporations guaranteed by the Commonwealth issued after the date of its adoption.

Pursuant to Commonwealth legislation, the Secretary of the Treasury is authorized to issue up to \$500,000,000 in general obligation debt of the Commonwealth with a maturity of not more than 30 years for long-term capital projects. The Commonwealth may issue such debt during fiscal 1998, although the Commonwealth is not obligated to issue all or any of such debt during fiscal 1998, and no assurance can be given as to when such debt will be issued or its aggregate amount.

### **Payment Record**

The Commonwealth has never defaulted on the payment of principal of or interest on any of its debt.

### **Debt Limitation**

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 account of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenues raised under the provisions of Commonwealth legislation and covered into the Treasury of Puerto Rico (hereinafter "internal revenues") in the two fiscal years preceding the then 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. Internal revenues consist principally of income taxes, property taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco products and customs duties, which are collected by the United States Government and returned to the Treasury of Puerto Rico, and motor vehicle fuel taxes and license fees, which are allocated to the Highway Authority, are not included as internal revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service.

On December 21, 1995, Puerto Rico Aqueduct and Sewer Authority issued \$400,340,000 Puerto Rico Aqueduct and Sewer Authority Refunding Bonds, guaranteed by the Commonwealth of Puerto Rico (the "PRASA Guaranteed Bonds"). On January 1, 1997, the Commonwealth began to make payments of debt service on the PRASA Guaranteed Bonds under the full faith and credit guarantee of the Commonwealth. The amount paid by the Commonwealth will be taken into account as an additional amount of debt service on the Commonwealth's general obligation debt for purposes of computing the above described 15% constitutional debt limitation.

After giving effect to the issuance of the Bonds and the refunding of the Refunded Bonds, future maximum annual debt service for the Commonwealth's outstanding general obligation debt will be \$434,567,000 in the fiscal year ending June 30, 2000. See "Debt Service Requirements for Commonwealth General Obligation Bonds and Certain Guaranteed Debt," under *Public Sector Debt of the Commonwealth*, below. Debt service for the PRASA Guaranteed Bonds paid during fiscal 1997 (including for this purpose debt service payments due July 1, 1997) was \$20,794,919. The sum of those amounts (\$455,362,000) is equal to 8.83% of \$5,155,398,500, which is the average of the adjusted internal revenues for the prior two fiscal years ended June 30, 1997.

## Maturity Limitation

The Constitution provides that no bonds or notes of the Commonwealth shall mature later than 30 years from their date of issue, except bonds or notes for housing facilities, which shall mature in no more than 40 years.

## PUBLIC SECTOR DEBT OF THE COMMONWEALTH

### Pro Forma Public Sector Debt

The following table presents a summary of the public sector debt of the Commonwealth as of December 31, 1997 and as adjusted for the issuance of the Bonds and the refunding of the Refunded Bonds. The table should be read in conjunction with the information set forth in *Debt in Appendix I*.

	December 31, 1997	As Adjusted
Puerto Rico direct debt . . . . .	\$ 4,893,891	\$4,919,668
Municipal debt . . . . .	885,105	885,105
Public corporations debt . . . . .		
Puerto Rico guaranteed debt . . . . .	446,420	446,420
Debt supported by Puerto Rico appropriations or taxes . . . .	8,195,945	8,195,945
Other non-guaranteed debt . . . . .	<u>5,933,395</u>	<u>5,933,395</u>
Total public corporations debt . . . . .	<u>14,575,760</u>	<u>14,575,760</u>
Total public sector debt . . . . .	<u>\$20,354,756</u>	<u>\$20,380,533</u>

\* For a complete recital of all notes to this table, see "Public Sector Debt" under *Debt in Appendix I*.

Source: Government Development Bank.

### Debt Service Requirements for Commonwealth General Obligation Bonds and Certain Guaranteed Debt

The following table presents debt service requirements for: (i) general obligation bonds of the Commonwealth outstanding on December 31, 1997, excluding the Refunded Bonds; (ii) the Bonds; (iii) all general obligation bonds of the Commonwealth, adjusted to include the issuance of the Bonds and the refunding of the Refunded Bonds; and (iv) bonds of Aqueduct and Sewer Authority for which debt service payments are being made under the Commonwealth guaranty. See "Commonwealth Guaranteed Debt" in *Appendix I*. With respect to other debt of Aqueduct and Sewer Authority, see *Public Corporations in Appendix I*. Debt service requirements for each fiscal year, as shown in the following table, include principal and interest due on July 1 immediately following the close of such fiscal year.

**Puerto Rico  
Debt Service Requirements\*  
(in thousands)**

Fiscal Year Ending June 30	Total Debt Service Prior to Issuance of Bonds(1)	Debt Service on Bonds(2)	Adjusted Debt Service(3)			Aqueduct and Sewer Authority Bonds Debt Service	Grand Total
			Principal	Interest	Total		
1998	\$ 391,692	\$ 9,507	\$ 177,375	\$ 223,824	\$ 401,199	\$ 33,473	\$ 434,672
1999	400,696	20,617	200,276	221,037	421,312	33,530	454,843
2000	410,285	24,282	227,855	206,712	434,567	33,509	468,075
2001	400,917	27,457	233,881	194,493	428,374	33,473	461,847
2002	391,339	27,457	234,864	183,932	418,796	33,542	452,338
2003	391,456	27,457	168,189	250,724	418,913	32,745	451,658
2004	356,097	27,458	139,245	244,310	383,555	30,125	413,681
2005	352,535	27,453	214,402	165,587	379,989	30,127	410,116
2006	327,620	27,454	176,028	179,046	355,074	30,121	385,195
2007	307,358	27,458	150,054	184,763	334,816	30,126	364,943
2008	245,606	27,456	123,878	149,184	273,062	30,131	303,193
2009	227,350	27,456	132,970	121,836	254,806	30,123	284,929
2010	206,379	47,966	142,525	111,820	254,345	29,984	284,329
2011	205,863	47,989	149,822	104,030	253,852	29,928	283,781
2012	198,787	48,018	158,195	88,610	246,805	30,127	276,932
2013	181,085	48,052	148,740	80,397	229,137	30,128	259,264
2014	160,381	48,091	117,068	91,405	208,472	30,125	238,597
2015	160,525	48,131	121,955	86,701	208,656	30,126	238,782
2016	160,411	48,176	126,335	82,252	208,587	30,121	238,707
2017	160,544	48,216	132,512	76,249	208,760	30,122	238,882
2018	160,403	48,261	137,870	70,794	208,664	30,126	238,790
2019	139,417	48,321	148,200	39,538	187,738	30,125	217,863
2020	140,520	48,355	156,825	32,049	188,874	0	188,874
2021	97,228	48,394	121,760	23,862	145,622	0	145,622
2022	75,144	48,435	105,820	17,759	123,579	0	123,579
2023	75,142	25,154	87,845	12,452	100,297	0	100,297
2024	75,149	1,647	68,950	7,846	76,796	0	76,796
2025	51,892	1,645	49,485	4,053	53,538	0	53,538
2026	0	29,148	27,760	1,388	29,148	0	29,148
<b>Total</b>	<b><u>\$6,451,822</u></b>	<b><u>\$985,512</u></b>	<b><u>\$4,180,681</u></b>	<b><u>\$3,256,652</u></b>	<b><u>\$7,437,333</u></b>	<b><u>\$681,937</u></b>	<b><u>\$8,119,270</u></b>

\* Totals may not add due to rounding.

(1) Debt service requirements on all general obligation bonds outstanding on December 31, 1997, excluding the Refunded Bonds.

(2) Debt service requirements on the Bonds.

(3) Debt service requirements on all general obligation bonds outstanding, adjusted to include the issuance of the Bonds and the refunding of the Refunded Bonds.

Sources: GDB and Department of the Treasury.



## TAX EXEMPTION

The Internal Revenue Code of 1986, as amended (the "Code"), includes requirements which the Commonwealth must continue to meet after the issuance of the Bonds in order that interest on the Bonds not be included in gross income for federal income tax purposes. The Commonwealth's failure to meet these requirements may cause interest on the Bonds to be included in gross income for federal income tax purposes retroactive to their date of issuance. The Commonwealth has covenanted in the Bond Resolution to comply, to the extent permitted by the Constitution and the laws of the Commonwealth, with the requirements of the Code in order to maintain the exclusion from gross income for federal income tax purposes of interest on the Bonds. Bond Counsel is not aware of any provision of the Constitution or laws of the Commonwealth which would prevent the Commonwealth from complying with the requirements of the Code.

In the opinion of Bond Counsel, subject to continuing compliance by the Commonwealth with the tax covenant referred to above, under the provisions of the Acts of Congress now in force and under existing regulations, rulings and court decisions, interest on the Bonds is not includable in gross income for federal income tax purposes. Interest on the Bonds is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, interest on the Bonds will be includable in the computation of the alternative minimum tax on corporations imposed by the Code. Bond Counsel is further of the opinion that the Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Ownership of tax-exempt obligations may result in collateral federal income tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations, certain corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations.

Ownership of tax-exempt obligations may also result in collateral income tax consequences under Puerto Rico law to financial institutions doing business in Puerto Rico.

Prospective purchasers of the Bonds should consult their tax advisors as to the applicability and impact of any collateral consequences.

Legislation affecting municipal securities is constantly being considered by the United States Congress. There can be no assurance that legislation enacted after the date of issuance of the Bonds will not have an adverse effect on the tax-exempt status of the Bonds. Legislative or regulatory actions and proposals may also affect the economic value of tax exemption or the market prices of the Bonds.

### **Capital Appreciation Bonds and Original Issue Discount**

Under the Code, the difference between the respective Accreted Values at maturity of the Capital Appreciation Bonds or the principal amounts of the Bonds maturing July 1 of the years 2023 and 2026 and the corresponding initial offering prices to the public (excluding bond houses and brokers) at each of which prices a substantial amount of such Bonds were sold (collectively, the "Discount Bonds"), is original issue discount. Original issue discount on the Discount Bonds represents interest which is not includable in federal gross income. A portion of such interest that accrues to the Beneficial Owner of such Discount Bonds in each year, as described below, is, however, included in the calculation for determining a corporate taxpayer's alternative minimum tax and the distribution requirements of certain regulated investment companies and may result in some of the collateral federal income tax consequences described above under the caption "*Tax Exemption*" in the year of accrual. Consequently, Beneficial Owners of Discount Bonds should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, additional distribution requirements or other collateral federal income tax consequences although the Beneficial Owner may not have received cash in such year. Original issue discount on Discount Bonds will accrue over the terms of such Bonds at a constant interest rate compounded in a manner similar to that used in computing the accreted values on the Capital Appreciation Bonds.

Interest not includable in federal gross income equal to the original issue discount accruing during the period a Beneficial Owner holds such Discount Bond will increase the adjusted basis in such Discount Bond by the amount of such accruing discount for purposes of determining taxable gain or loss on the sale, redemption or other disposition of such Discount Bond. The accrual of original issue discount and its effect on the redemption, sale or other disposition of Discount Bonds which are not purchased in the initial offering at the initial offering price may be determined according to rules which differ from those described above. Beneficial Owners of Discount Bonds should consult their tax advisors with respect to the precise determination for federal income tax purposes of interest accrued upon sale, redemption or other disposition of Discount Bonds and with respect to the state and local tax consequences of owning and disposing of Discount Bonds.

### **Premium Bonds**

The difference between the amount payable at maturity of the Bonds maturing July 1 of the years 2000 through 2007 and the years 2009 through 2013 and the tax basis of such Bonds to a purchaser (other than a purchaser who holds such Bonds as inventory, stock in trade or for sale to customers in the ordinary course of business) is "bond premium". Bond premium is amortized over the term of such Bonds for federal income tax purposes. Beneficial Owners of such Bonds are required to decrease their adjusted basis in such Bonds by the amount of amortizable bond premium attributable to each taxable year such Bonds are held. The amortizable bond premium on such Bonds attributable to a taxable year is not deductible for federal income tax purposes. Beneficial Owners of such Bonds should consult their tax advisors with respect to the precise determination for federal income tax purposes of the treatment of bond premium upon sale or other disposition of such Bonds and with respect to the state and local tax consequences of owning and disposing of such Bonds.

## **UNDERWRITING**

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the Bonds from the Commonwealth at an aggregate discount of \$3,654,061.70 from the initial public offering prices of the Bonds set forth or derived from information set forth on the cover page hereof. The obligations of the Underwriters are subject to certain conditions precedent, and the Underwriters will be obligated to purchase all the Bonds, if any Bonds are purchased. The Underwriters may offer to sell the Bonds to certain dealers and others at prices lower than the initial public offering prices, and such offering prices may be changed, from time to time, by the Underwriters.

Morgan Stanley & Co. Incorporated ("Morgan Stanley"), a managing underwriter, has entered into a written agreement with Popular Securities, Inc. ("Popular Securities"), a subsidiary of Popular Inc. and an affiliate of Banco Popular de Puerto Rico, Registrar for the Bonds, pursuant to which Popular Securities has agreed to cooperate in connection with Morgan Stanley's provision of underwriting and investment banking services to the Commonwealth with respect to the Bonds. Pursuant to these arrangements, the existence of which has been disclosed to the Commonwealth and Government Development Bank, Popular Securities will be entitled to receive a portion of Morgan Stanley's actual net profits, if any, in connection with the underwriting of the Bonds.

## **LEGAL MATTERS**

The proposed form of opinion of Brown & Wood LLP, New York, New York, Bond Counsel, is set forth in *Appendix III* to this Official Statement. Certain legal matters will be passed upon for the Underwriters by Pietrantoní Méndez & Alvarez, San Juan, Puerto Rico.

## **LEGAL INVESTMENT**

The Bonds will be eligible for deposit by banks in Puerto Rico to secure public funds and will be approved investments for insurance companies to qualify them to do business in Puerto Rico, as required by law.

## VERIFICATION OF MATHEMATICAL COMPUTATIONS

Deloitte & Touche LLP will verify from the information provided to them the mathematical accuracy as of the date of the closing on the Bonds of the computations contained in the schedules provided to Deloitte & Touche LLP to determine that the anticipated receipts from the securities and cash deposits listed in such schedules, to be held in escrow, will be sufficient to pay, when due, the principal, interest and call premium payment requirements, if any, of the Refunded Bonds (see *Plan of Financing*). Deloitte & Touche LLP will express no opinion on the assumptions provided to them, nor as to the exclusion from gross income for federal income tax purposes of the interest on the Bonds.

## GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

As required by Act No. 272 of the Legislature of Puerto Rico, approved May 15, 1945, as amended, Government Development Bank has acted as financial advisor to the Commonwealth in connection with the Bonds offered hereby. As financial advisor, Government Development Bank participated in the selection of the Underwriters of the Bonds. Certain of the Underwriters have been selected by Government Development Bank to serve from time to time as underwriters of its obligations and the obligations of the Commonwealth, its instrumentalities and public corporations. Certain of the Underwriters or their affiliates participate in other financial transactions with Government Development Bank.

## RATINGS

Moody's Investors Service and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc., have given the 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.

Such rating agencies were provided with materials relating to the Commonwealth and the Bonds and other relevant information, and no application has been made to any other rating agency for the purpose of obtaining a rating on the Bonds.

There is no assurance that such ratings will remain in effect for any given period of time or that they will not be revised downward or withdrawn entirely by either or both of such rating agencies, if in the judgment of either or both, circumstances so warrant. Any such downward revision or withdrawal of such ratings, or either of them, may have an adverse effect on the market prices of the Bonds.

## CONTINUING DISCLOSURE

In accordance with the requirements of Rule 15c2-12, as amended (the "Rule"), promulgated by the Securities and Exchange Commission (the "SEC"), the Commonwealth has covenanted in the Bond Resolution for the benefit of the Beneficial Owners (as defined in such Bond Resolution and generally the tax owners of the Bonds):

1. to file within 305 days after the end of each fiscal year commencing with the fiscal year ending June 30, 1998, with each nationally recognized municipal securities information repository ("NRMSIR") and with any Commonwealth state information depository ("SID"), core financial information and operating data for the prior fiscal year, including (i) the Commonwealth's audited financial statements, prepared in accordance with generally accepted accounting principles in effect from time to time, and (ii) material historical quantitative data (including financial information and operating data) on the

Commonwealth and revenues, expenditures, financial operations and indebtedness generally found in this Official Statement; and

2. to file, in a timely manner, with each NRMSIR or with the Municipal Securities Rulemaking Board (the “MSRB”) and with any Commonwealth SID, notice of any failure of the Commonwealth to comply with paragraph 1 above and of the occurrence of any of the following events with respect to the Bonds if material:
  - a. principal and interest payment delinquencies;
  - b. non-payment related defaults;
  - c. unscheduled draws on debt service reserves reflecting financial difficulties;
  - d. unscheduled draws on credit enhancements reflecting financial difficulties;
  - e. substitution of credit or liquidity providers, or their failure to perform;
  - f. adverse opinions or events affecting the tax-exempt status of the Bonds;
  - g. modifications to rights of the holders (including Beneficial Owners) of the Bonds;
  - h. bond calls;
  - i. defeasances;
  - j. release, substitution, or sale of property securing repayment of the Bonds; and
  - k. rating changes.

Events (c), (d) and (e) are included pursuant to a letter from the SEC staff to the National Association of Bond Lawyers, dated September 19, 1995. However, events (c), (d) and (e) may not be applicable, since the terms of the Bonds do not provide for “debt service reserves” or “credit or liquidity providers”. For a description of the Bonds, see *The Bonds*. In addition, with respect to the following events:

Events (d) and (e). The Commonwealth does not undertake to provide any notice with respect to credit enhancement added after the primary offering of the Bonds, unless the Commonwealth applies for or participates in obtaining the enhancement.

Event (f). For information on the tax status of the Bonds, see *Tax Exemption*.

Event (h). The Commonwealth does not undertake to provide the above-described event notice of a mandatory scheduled redemption, not otherwise contingent upon the occurrence of an event, if the terms, dates and amounts of redemption are set forth in detail in this Official Statement under “*The Bonds — Redemption*”, the only open issue is which Bonds will be redeemed in the case of a partial redemption, notice of redemption is given to the Bondholders as required under the terms of the Bonds, and public notice of the redemption is given pursuant to Securities Exchange Act of 1934 Release No. 34-23856 of the SEC, even if the originally scheduled amounts are reduced by prior optional redemptions or Bond purchases.

The Commonwealth expects to provide the information described in paragraph 1 above by delivering its first bond official statement that includes its financial statements for the preceding fiscal year or, if no such official statement is issued by the 305-day deadline, by delivering its Comprehensive Annual Financial Report and a supplemental report containing other information to the extent necessary to provide the information described in paragraph 1 above by such deadline.

As of January 15, 1998, there is no Commonwealth SID, and the nationally recognized municipal securities information repositories are: Bloomberg Municipal Repository, P.O. Box 840, Princeton, New Jersey 08542-0840; Kenny Information Systems, Inc., Attn: Kenny Repository Service, 65 Broadway, New York, New York 10006; Thompson NRMSIR, 395 Hudson Street, New York, New York 10004, Attn: Municipal Disclosure; and DPC Data Inc., One Executive Drive, Fort Lee, New Jersey 07024.

The Commonwealth may from time to time choose to provide notice of the occurrence of certain other events in addition to those listed above if, in the judgment of the Commonwealth, such other events are material with

respect to the Bonds, but the Commonwealth does not undertake to provide any such notice of the occurrence of any material event except those events listed above.

The Commonwealth acknowledges that its undertaking pursuant to the Rule described above is intended to be for the benefit of the Beneficial Owners of the Bonds, and shall be enforceable by any such Beneficial Owners; provided that the right to enforce the provisions of its undertaking shall be limited to a right to obtain specific enforcement of the Commonwealth's obligations hereunder.

No Beneficial Owner may institute any suit, action or proceeding at law or in equity ("Proceeding") for the enforcement of the foregoing covenants (the "Covenants") or for any remedy for breach thereof, unless such Beneficial Owner shall have filed with the Commonwealth written notice of any request to cure such breach, and the Commonwealth shall have refused to comply within a reasonable time. All Proceedings shall be instituted only in a Commonwealth court located in the Municipality of San Juan, Puerto Rico for the equal benefit of all Beneficial Owners of the outstanding Bonds benefitted by the Covenants, and no remedy shall be sought or granted other than specific performance of any of the Covenants at issue. Moreover, Proceedings filed by Beneficial Owners against the Commonwealth may be subject to the sovereign immunity provisions of Section 2 of Act No. 104, approved June 29, 1955, as amended (32 L.P.R.A. §3077 and §3077a), which governs the scope of legal actions against the Commonwealth, substantially limits the amount of monetary damages that may be awarded against the Commonwealth and provides certain notice provisions, the failure to comply with which may further limit any recovery.

The Covenants may only be amended if:

(1) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of the Commonwealth, or type of business conducted; the Covenants, as amended, would have complied with the requirements of the Rule at the time of award of the Bonds, after taking into account any amendments or change in circumstances; and the amendment does not materially impair the interest of Beneficial Owners, as determined by persons unaffiliated with the Commonwealth; or

(2) all or any part of the Rule, as interpreted by the staff of the SEC at the date of the adoption of such Rule, ceases to be in effect for any reason, and the Commonwealth elects that the Covenants shall be deemed amended accordingly.

The Commonwealth has further agreed that the annual financial information containing any amended operating data or financial information will explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

Any assertion of beneficial ownership must be filed, with full documentary support, as part of the written request described above.

The Covenants have been made in order to assist the Underwriters in complying with the Rule.

## MISCELLANEOUS

The foregoing summaries of or references to the various acts, the Bonds, the Bond Resolution and the summaries of or references to the various acts contained in *Appendix I*, are made subject to all the detailed provisions thereof to which reference is hereby made for further information and do not purport to be complete statements of any or all of such provisions.

Appended to and constituting a part of this Official Statement is certain information concerning the Commonwealth (*Appendix I*), the Comprehensive Annual Financial Report of the Commonwealth for the fiscal year ended June 30, 1997 prepared by the Department of the Treasury, which includes the general purpose

financial statements of the Commonwealth for the fiscal year ended June 30, 1997, together with the independent auditor's report thereon, dated December 15, 1997, of Deloitte & Touche LLP, San Juan, Puerto Rico, certified public accountants (*Appendix II*), the proposed form of opinion of Bond Counsel (*Appendix III*) and the table of Accreted Values (*Appendix IV*).

The information set forth in this Official Statement, except for information pertaining to DTC, was supplied by certain officials of the Commonwealth or certain of its agencies or instrumentalities, in their respective official capacities, or was obtained from publications of the Commonwealth or certain of its agencies or instrumentalities, and is included in this Official Statement on the authority of such officials or the authority of such publications as public official documents. The information pertaining to DTC was supplied by DTC.

This Official Statement will be filed with each NRMSIR and with the MSRB.

**COMMONWEALTH OF PUERTO RICO**

By:                   /s/ Xenia Vélez Silva                    
*Secretary of the Treasury*

## COMMONWEALTH OF PUERTO RICO

**Geographic Location and Demography**

Puerto Rico, the fourth largest of the Caribbean islands, is located approximately 1,600 miles southeast of New York City. It is approximately 100 miles long and 35 miles wide.

According to the United States Census Bureau, the population of Puerto Rico was approximately 3,522,000 in 1990, compared to 3,196,520 in 1980. According to estimates of the Planning Board, the population of Puerto Rico increased to 3,726,000 in fiscal 1996. As of 1990, the population of San Juan, the island's capital and largest city, was approximately 437,000.

**Relationship with the United States**

Puerto Rico was discovered by Columbus in 1493 and shortly thereafter the island was conquered and settled by the Spaniards. It remained a Spanish possession for four centuries.

Puerto Rico came under United States sovereignty pursuant to the Treaty of Paris, signed on December 10, 1898, which ended the Spanish-American War. Puerto Ricans became citizens of the United States in 1917, with the approval of the Jones Act by the United States Congress. In 1950, after a long evolution toward greater self-government, Congress enacted Public Law 600 which provided that the existing political, economic, and fiscal relationship between Puerto Rico and the United States would remain the same, but Puerto Rico would be authorized to draft and approve its own Constitution, guaranteeing a republican form of government. The Constitution was drafted by a popularly elected constitutional convention, approved in a special referendum by the people of Puerto Rico, amended and ratified by the United States Congress, and subsequently approved by the President of the United States. Puerto Rico's constitutional status is that of a territory of the United States, and pursuant to the territorial clause of the Federal Constitution, the ultimate source of power over Puerto Rico is the United States Congress. The relationship between the United States and Puerto Rico is referred to herein as commonwealth status.

Puerto Rico exercises virtually the same control over its internal affairs as do the fifty states; however, it differs from the states in its relationship with the federal government. The people of Puerto Rico are citizens of the United States but do not vote in national elections. They are represented in Congress by a Resident Commissioner who has a voice in the House of Representatives and limited voting power. Most federal taxes, except those such as Social Security taxes, are not levied in Puerto Rico. No federal income tax is collected from Puerto Rico residents on income earned in Puerto Rico, except for certain federal employees who are subject to taxes on their salaries. Income earned by Puerto Rico residents from sources outside of Puerto Rico, however, is subject to federal income tax. Federal excise taxes on shipments of alcoholic beverages from Puerto Rico and other rum producing countries (which are at \$11.30 per gallon through October 1, 1998, and thereafter at \$10.50 per gallon) and other taxes on shipments of tobacco products from Puerto Rico to the mainland are returned to the Treasury of Puerto Rico.

The official languages of Puerto Rico are Spanish and English. Although the culture of Puerto Rico is mostly Hispanic, a considerable intermingling of Hispanic and United States cultures has occurred.

On February 26, 1997 legislation was introduced in the U.S. House of Representatives (the "Political Status Act") proposing a mechanism to settle permanently the political relationship between Puerto Rico and the United States, either through full self-government (e.g., statehood or independence, including, as an alternative, free association via a bilateral treaty) or continued commonwealth status. Under the proposed legislation, failure to settle on full self-government after completion of the referenda process provided therein would result in retention of the current commonwealth status. On March 19, 1997, similar legislation was introduced in the U.S. Senate. The House Resources Committee held hearings and voted in favor of the Political Status Act. The Political Status Act must be voted on by the House Rules Committee

before reaching the House floor. It is not possible at this time to predict when the Political Status Act will be voted on by the full House of Representatives, what course the legislation will follow in the Senate, and whether it will be subsequently enacted into law.

### **Governmental Structure**

The Constitution of the Commonwealth of Puerto Rico (the “Commonwealth” or “Puerto Rico”) provides for the separation of powers of the executive, legislative, and judicial branches of government. The Governor is elected every four years. The Legislature consists of a Senate and a House of Representatives, the members of which are elected for four-year terms. The highest court within the local jurisdiction is the Supreme Court of Puerto Rico. Decisions of the Supreme Court of Puerto Rico may be appealed to the Supreme Court of the United States under the same terms and conditions as decisions from state courts. Puerto Rico constitutes a District in the Federal Judiciary and has its own United States District Court. Decisions of this court may be appealed to the United States Court of Appeals for the First Circuit and from there to the Supreme Court of the United States.

Governmental responsibilities assumed by the central government of Puerto Rico are similar in nature to those of the various state governments. In addition, the central government assumes responsibility for local police and fire protection, education, public health and welfare programs, and economic development.

Pedro Rosselló was sworn in as Governor of Puerto Rico on January 2, 1993. He was re-elected for a second four year term in the November 1996 elections and sworn in again as Governor of Puerto Rico on January 2, 1997. He obtained a medical degree from Yale University in 1970, after completing his undergraduate studies at Notre Dame University in 1966. He specialized in General and Pediatric Surgery at Harvard University. In 1985, he was appointed Director of San Juan’s Health Department, a position which he held for three years. As a member of the New Progressive Party, he was the party’s candidate for Resident Commissioner to the United States Congress in 1988. In 1991, he was elected President of the New Progressive Party.

Xenia Vélez Silva, Secretary of the Treasury, took office on November 20, 1997. She is a graduate of the University of Puerto Rico, where she obtained a bachelor's degree in Business Administration and a Juris Doctor degree. Prior to her appointment, she was a partner in a San Juan law firm specializing in tax law.

Jorge E. Aponte Hernández, Director of the Office of Management and Budget, took office in January 1993. In November 1996, he was re-appointed by the Governor to continue in his position. He is a certified public accountant and a graduate of the University of Puerto Rico, where he obtained a bachelor's degree in Business Administration and Accounting. Prior to his appointment, he worked for twenty years as an accountant and auditor for various accounting firms.

Marcos Rodríguez-Ema, President of Government Development Bank for Puerto Rico (“Government Development Bank” or “GDB”), took office in January 1993. In November 1996, he was re-appointed by the Governor to continue in his position. He is a lawyer and a graduate of Georgetown University, where he obtained a Juris Doctor degree after completing his bachelor of science degree in foreign service. Prior to his appointment, he worked for five years as a lawyer in a San Juan law firm and for six years as an investment banker for two major securities firms.

### **Political Trends**

For many years there have been two major views in Puerto Rico with respect to the island’s relationship with the United States: one favoring statehood, represented by the New Progressive Party, and the other favoring the existing commonwealth status, represented by the Popular Democratic Party. The following table shows the percentages of the total vote received by the gubernatorial candidates of the various parties in the last five elections by voter preference with respect to statehood, commonwealth status, and independence. While the electoral choices of Puerto Rico’s voters are not based solely on preferences regarding the island’s relationship with the United States, candidates who support a continuing relationship between Puerto Rico and the United States have prevailed in elections for many years.



	<u>1980</u>	<u>1984</u>	<u>1988</u>	<u>1992</u>	<u>1996</u>
New Progressive Party . . . . .	47.3%	45.5%	45.8%	49.9%	51.1%
Popular Democratic Party . . . . .	47.0	48.5	48.7	45.9	44.5
Puerto Rico Independence Party . . . . .	5.4	3.9	5.4	4.2	3.8
Others . . . . .	0.3	2.1	0.1	--	0.6

With the results of the 1996 election, control of the executive and legislative branches continued under the New Progressive Party. The composition of the Senate and House by the several political parties is as follows:

	<u>Senate</u>	<u>House</u>
New Progressive Party . . . . .	19	37
Popular Democratic Party . . . . .	8	16
Puerto Rico Independence Party . . . . .	<u>1</u>	<u>1</u>
	28	54

The next general election (gubernatorial, municipal, and legislative) in Puerto Rico will be held in November 2000. Voter participation in Puerto Rico is substantially higher than in the United States, averaging 85% since 1972.

## THE ECONOMY

### General

The Government of Puerto Rico has established policies and programs directed at developing the manufacturing and service sectors (with emphasis on the tourism industry) of the economy and expanding and modernizing the island's infrastructure. Domestic and foreign investment has been stimulated by selective tax exemption, development loans, and other financial and tax incentives. Infrastructure expansion and modernization have been to a large extent financed by bonds and notes issued by the Commonwealth, its public corporations and municipalities. Economic progress has been aided by significant increases in the levels of education and occupational skills of the island's population.

The economy of Puerto Rico is fully integrated with that of the United States mainland. During fiscal 1996, approximately 88% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 62% of Puerto Rico's imports. In fiscal 1996, Puerto Rico experienced a \$3.2 billion positive adjusted merchandise trade balance.

The dominant sectors of the Puerto Rico economy are manufacturing and services. The manufacturing sector has experienced a basic change over the years as a result of increased emphasis on higher wage, high technology industries, such as pharmaceuticals, electronics, computers, microprocessors, professional and scientific instruments, and certain high technology machinery and equipment. The services sector, including finance, insurance, real estate, wholesale and retail trade, and hotel and related services, also plays a major role in the economy. It ranks second only to manufacturing in contribution to the gross domestic product and leads all sectors in providing employment. In recent years, the services sector has experienced significant growth in response to the expansion of the manufacturing sector.

### *Fiscal 1993 to 1997*

Puerto Rico's more than decade-long economic expansion continued throughout the five-year period from fiscal 1993 through fiscal 1997. 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 exchange value of the United States dollar, increases in the level of federal transfers, and the relatively low cost of borrowing.

Gross product in fiscal 1993 was \$25.1 billion (\$24.5 billion in 1992 prices) and gross product in fiscal 1997 was \$32.0 billion (\$27.6 billion in 1992 prices). This represents an increase in gross product of 27.5% from fiscal 1993 to 1997 (12.6% in 1992 prices).

Since fiscal 1985, personal income, both aggregate and per capita, has increased consistently each fiscal year. In fiscal 1996, aggregate personal income was \$29.4 billion (\$27.8 billion in 1992 prices) and personal income per capita was \$7,882 (\$7,459 in 1992 prices).

Personal income includes transfer payments to individuals in Puerto Rico under various social programs. Total federal payments to Puerto Rico, which include transfers to local government entities and expenditures of federal agencies in Puerto Rico, in addition to federal transfer payments to individuals, are lower on a per capita basis in Puerto Rico than in any state. Transfer payments to individuals in fiscal 1996 were \$6.6 billion, of which \$4.8 billion, or 72.2%, represented entitlements to individuals who had previously performed services or made contributions under programs such as Social Security, Veterans' Benefits, Medicare and U.S. Civil Service retirement pensions.

Average employment increased from 999,000 in fiscal 1993, to 1,128,300 in fiscal 1997. Average unemployment decreased from 16.8% in fiscal 1993, to 13.1% in fiscal 1997.

The following table shows the gross product for the five fiscal years ended June 30, 1997.

<b>Puerto Rico</b>	
<b>Gross Product</b>	
	Fiscal Year Ended June 30,
	<u>1993</u> <u>1994</u> <u>1995</u> <u>1996(p)</u> <u>1997(p)</u>
Gross product — \$ millions . . . . .	\$25,133      \$26,641      \$28,413      \$30,254      \$32,032
Real gross product — \$ millions (1992 prices) . . . . .	24,483      25,103      25,945      26,742      27,567
Annual percentage increase in real gross product (1992 prices) . . . . .	3.3%      2.5%      3.4%      3.1%      3.1%
U.S. annual percentage increase in real gross product (1992 prices)(1) . . . . .	2.8%      2.9%      2.7%      2.1%      3.2%

(p) Preliminary.  
(1) Restated to correspond to Puerto Rico's fiscal year ending June 30.

Sources: Planning Board and Data Resources Inc.

Since the 1950's the Planning Board has prepared a complete set of macroeconomic measures like those prepared for the United States by the Bureau of Economic Analysis ("BEA") of the Department of Commerce. In contrast with the BEA, which computes the economic accounts on a quarterly basis, the Planning Board computes the economic accounts on an annual basis. Like the BEA, the Planning Board revises the macroeconomic numbers on a regular basis. The Planning Board has always classified the latest annual numbers as preliminary until they are revised in conjunction with the release of the new data each year. At present, all macroeconomic accounts for fiscal 1996 are preliminary until the revised figures are released. The release of the 1997 data is expected to occur within the next few months.

*Fiscal 1998*

According to the Labor Department's Household Employment Survey, during the first five months of fiscal 1998, total employment increased 1.9% over fiscal 1997. Total employment averaged 1,137,200 during the first five months of fiscal 1998, compared to 1,115,600 in the same period of fiscal 1997. The seasonally adjusted unemployment rate for November 1997 was 14.0%.

The Planning Board's gross product forecast for fiscal 1998, made in February 1997, projected an increase of 2.6% over fiscal 1997.

## **Economic Development Program - New Economic Model**

Governor Rosselló's administration has developed and is implementing a new economic development program which is based on the premise that the private sector should provide the primary impetus for economic development and growth. This new program, referred to as the New Economic Model, promotes changing the role of the government from one of a provider of most basic services, to that of a facilitator for private sector initiatives, and encourages private sector investment by reducing government-imposed regulatory constraints.

The New Economic Model contemplates the development of initiatives that will foster private investment in, and private management of, sectors that are served more efficiently and effectively by private enterprise. One of the initiatives that has already been implemented is the adoption of a new tax code intended to expand the tax base, reduce top personal and corporate tax rates and simplify the tax system. Another initiative consists of improving and expanding Puerto Rico's infrastructure to facilitate private sector development and growth, such as the construction of the water pipeline and cogeneration facilities described below and the construction of a light rail system for the San Juan metropolitan area.

The New Economic Model seeks to identify and promote those areas in which Puerto Rico can compete more effectively in the global markets. In this regard, tourism has been targeted as a priority because of its potential for job creation and increased contribution to the gross product stemming from Puerto Rico's natural competitive advantage. As part of the initiatives directed at promoting the tourism sector, in 1993 a new Tourism Incentives Act was enacted providing special tax incentives for the development of new hotel projects. See "Tax Incentives" below. Also, in November 1993, the Tourism Development Fund was created for the purpose of promoting capital investments in and providing financing to entities that contribute to the development of the tourism industry. As a result of these initiatives, several new hotels have been constructed or are in the process of being constructed, increasing the number of total rooms on the island from 8,415 at the end of fiscal 1992 to 10,877 at the end of fiscal 1997 and to a projected 11,972 by the end of fiscal 1998. Similar tax incentives have been enacted in other areas targeted by the New Economic Model as areas of opportunity for the promotion of local and foreign investment in Puerto Rico, such as agriculture, solid waste management and venture capital.

The New Economic Model also seeks to reduce the size of government's direct contribution to gross domestic product. As part of this goal, the Government has transferred certain governmental operations and sold a number of its assets to private parties. On March 3, 1995, the Government completed the sale of the assets of the Maritime Shipping Authority to a private purchaser. On May 26, 1995, the Aqueduct and Sewer Authority executed a five-year agreement pursuant to which the management, operation, repair, and maintenance of the Authority's water and waste water treatment systems is being provided by a private company. On January 31, 1996, the Aqueduct and Sewer Authority executed a construction and operating agreement with a private consortium for the design, construction, and operation of an approximately 75 million gallon per day pipeline to deliver water to the San Juan metropolitan area from Dos Bocas reservoir in Utuado. The Electric Power Authority has entered into power purchase agreements with private power producers under which two cogenerating plants (with a total capacity of approximately 800 megawatts) using fuels other than oil will be constructed, operated and owned by these producers. The Administration of Corrections has entered into operating agreements with two private companies whereby three new correctional facilities are being operated by these companies. In 1995, the Government entered into a definitive agreement to sell to private companies certain assets of the pineapple juice processing business formerly operated by the Land Authority and sold certain government owned mango growing operations. The Government is currently in the process of transferring to local sugar cane growers the sugar processing facilities operated by the Sugar Corporation. The Government has also sold two hotel properties formerly owned by a subsidiary of the Tourism Company and is currently negotiating the sale of a complex consisting of two hotels and a convention center to a Florida-based corporation. On April 7, 1997, Governor Rosselló announced the Government's intention to sell the Puerto Rico Telephone Company ("PRTC"), a subsidiary of the Telephone Authority. Legislation authorizing the Government to negotiate the sale of PRTC has been approved and the Government is currently conducting the sale process.

One of the goals of the Rosselló administration is to change Puerto Rico's public health care system from one in which the government provides free health services to low income individuals through public health facilities owned and administered by the government to one in which all medical services are provided by the private sector and the government provides comprehensive health insurance coverage for qualifying (generally low income) Puerto Rico residents. Under this new system, the Government selects, through a bidding system, one private health insurance company in each of several designated regions of the island and pays such insurance company the insurance premium

for each eligible beneficiary within such region. This new health insurance system is now covering 61 municipalities out of a total of 78 on the island. It is expected that 11 municipalities will be added by the end of fiscal 1998 and 5 more by the end of fiscal 1999. The total cost of this program will depend on the number of municipalities included in the program, the number of participants receiving coverage, and the date coverage commences. As of June 30, 1997, over 1,090,592 persons were participating in the program at an estimated annual cost to the General Fund of Puerto Rico for fiscal 1997 of approximately \$521 million. In conjunction with this program, the operation of certain public health facilities has been transferred to private entities. The Government's current privatization plan for health facilities provides for the transfer of ownership of all health facilities to private entities. The Government has announced that it has selected various private companies with which it is commencing negotiations expected to culminate in the sale of ten health facilities to such companies.

**Employment and Unemployment**

The number of persons employed in Puerto Rico during fiscal 1997 averaged 1,128,300. Unemployment, although at relatively low historical levels, remains above the average for the United States.

The following table presents annual statistics of employment and unemployment from fiscal 1993 through fiscal 1997 and monthly statistics for July to November 1997.

**Puerto Rico  
Employment and Unemployment**

<u>Fiscal Years Ended June 30</u>	<u>Labor Force(1)</u>	<u>Employed(1)</u>	<u>Unemployed(1)</u> <u>(Annual Average)</u>	<u>Unemployment</u> <u>Rate(2)</u>
1993 .....	1,201	999	202	16.8%
1994 .....	1,204	1,011	193	15.9
1995 .....	1,219	1,051	168	13.8
1996 .....	1,268	1,092	175	13.8
1997 .....	1,298	1,128	170	13.1
<u>Fiscal 1998</u>		<u>(Seasonally Adjusted)</u>		
July .....	1,309	1,125	184	14.1%
August .....	1,314	1,141	173	13.2
September .....	1,337	1,162	175	13.1
October .....	1,303	1,126	177	13.6
November .....	1,316	1,132	184	14.0

(1) Thousands of persons age 16 years and over. Totals may not add due to rounding.  
 (2) Unemployed as percentage of labor force.

Source: Department of Labor and Human Resources — Household Survey.

**Economic Performance by Sector**

Puerto Rico has a diversified economy. During fiscal years 1992-1996, the manufacturing and services sectors generated the largest portion of gross domestic product. Three sectors of the economy provide the most employment: manufacturing, services and government.

The following table presents annual statistics of gross domestic product by sector and gross product for the five fiscal years ended June 30, 1996.

**Puerto Rico**

**Gross Domestic Product by Sector and Gross Product  
(in millions at current prices)**

	<b>Fiscal Year Ended June 30</b>				
	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996(p)</u>
Manufacturing	\$14,183	\$15,428	\$16,748	\$17,863	\$18,861
Services(1)	13,168	14,109	15,214	16,248	17,093
Government(2)	3,672	3,881	3,987	4,440	4,871
Transportation, communication and public utilities	2,828	3,009	3,134	3,284	3,487
Agriculture, forestry and fisheries	420	411	369	317	307
Construction (3)	798	874	928	955	1,003
Statistical discrepancy	<u>(439)</u>	<u>(789)</u>	<u>(689)</u>	<u>(501)</u>	<u>(117)</u>
Total gross domestic product(4)	34,630	36,923	39,691	42,607	45,505
Less: net payment abroad	<u>10,934</u>	<u>11,790</u>	<u>13,050</u>	<u>14,194</u>	<u>15,251</u>
Total gross product(4)	<u>\$23,696</u>	<u>\$25,133</u>	<u>\$26,641</u>	<u>\$28,413</u>	<u>\$30,254</u>

(p) Preliminary.

(1) Includes wholesale and retail trade, finance, insurance and real estate, hotel and related services, and other services.

(2) Includes the Government of Puerto Rico, its municipalities and the federal government; excludes public corporations.

(3) Includes mining.

(4) Totals may not add due to rounding.

Source: Planning Board

The following table presents annual statistics of average employment by sector for the five fiscal years ended June 30, 1997.

**Puerto Rico**

**Average Employment by Sector  
(thousands of persons age 16 and over)**

	<b>Fiscal Year ended June 30</b>				
	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>
Manufacturing . . . . .	168	166	172	167	162
Services(1) . . . . .	467	478	496	527	550
Government(2) . . . . .	217	224	232	246	261
Transportation, communication and public utilities . . . . .	54	55	60	61	59
Construction(3) . . . . .	59	54	57	59	65
Agriculture, forestry and fisheries . . . . .	<u>34</u>	<u>34</u>	<u>34</u>	<u>32</u>	<u>31</u>
Total(4) . . . . .	<u>999</u>	<u>1,011</u>	<u>1,051</u>	<u>1,092</u>	<u>1,128</u>

(1) Includes wholesale and retail trade, finance, insurance, real estate, hotels and related services and other services.

(2) Includes the Government of Puerto Rico, its municipalities and federal government; excludes public corporations.

(3) Includes mining.

(4) Totals may not add due to rounding.

Source: Department of Labor and Human Resources — Household Survey.

## Manufacturing

Manufacturing is the largest sector in the economy of Puerto Rico, in terms of gross domestic product. The Planning Board estimates that in fiscal 1996 manufacturing generated \$18.9 billion, or 41.4% of gross domestic product. The manufacturing sector employed 152,489 workers as of March 1997 (as reported in the Department of Labor and Human Resources — Monthly Survey on Employment Hours and Earnings). Most of the island's manufacturing output is shipped to the United States mainland, which is also the principal source of semifinished manufactured articles on which further manufacturing operations are performed in Puerto Rico. The United States minimum wage laws are applicable in Puerto Rico. As of March 1997 the average hourly manufacturing wage rate in Puerto Rico was 61% of the average mainland United States rate.

Manufacturing in Puerto Rico is now more diversified than during the earlier phases of the industrial development program. In the last two decades, industrial development has tended to be more capital intensive and more dependent on skilled labor. This gradual shift in emphasis is best exemplified by the heavy investment in pharmaceuticals, scientific instruments, computers, microprocessors, medical products, and electrical products industries over the last decade.

The following table sets forth gross domestic product by manufacturing sector for the five fiscal years ended June 30, 1996.

**Puerto Rico**  
**Gross Domestic Product by Manufacturing Sector**  
**(in millions at current prices)**

	Fiscal Year Ended June 30				
	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996(p)</u>
Pharmaceuticals . . . . .	\$6,460	\$7,249	\$8,229	\$8,905	\$9,214
Machinery and metal products . . . . .	2,935	3,226	3,310	3,449	4,046
Food products . . . . .	2,413	2,456	2,694	2,742	2,775
Apparel . . . . .	536	548	504	603	607
Other(1) . . . . .	<u>1,840</u>	<u>1,949</u>	<u>2,010</u>	<u>2,164</u>	<u>2,219</u>
Total gross domestic product of manufacturing sector(2) . . . . .	<u>\$14,183</u>	<u>\$15,428</u>	<u>\$16,748</u>	<u>\$17,863</u>	<u>\$18,861</u>

(p) Preliminary.

(1) Includes petroleum products; petrochemicals and other chemical products; tobacco products; stone, clay and glass products; textiles and others.

(2) Totals may not add due to rounding.

Source: Planning Board.

The following table sets forth manufacturing employment by industry group as of March for the last five years.

**Puerto Rico**

**Manufacturing Employment by Industry Group  
(persons age 16 years and over)**

<u>Industry Group</u>	<u>As of March 31,</u>				
	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>
Apparel and related products .....	29,018	25,213	26,034	23,918	22,592
Food and related products .....	20,608	20,471	20,882	20,343	20,021
Electrical machinery, equipment and supplies .....	17,721	19,676	22,928	23,464	23,798
Chemicals and related products (includes pharmaceuticals) .....	26,141	27,174	28,104	28,047	26,855
Professional and scientific instruments .....	16,437	15,495	14,390	15,131	14,943
Machinery, except electrical equipment .....	4,241	4,262	2,612	3,824	4,083
Petroleum refining and related industries; rubber and miscellaneous plastic products .....	5,294	5,593	4,983	5,268	5,470
Leather and leather products .....	7,196	7,260	7,282	6,636	6,397
Paper and related products; printing, publishing and related industries .....	5,944	6,118	6,628	7,184	7,258
Metal products .....	4,632	4,648	4,740	5,157	5,674
Stone, clay and glass products .....	4,465	4,716	4,708	4,825	4,907
Lumber and wood products; furniture and fixtures .....	2,882	2,927	2,894	3,183	3,323
Textile mill products .....	3,876	3,503	3,403	3,841	3,641
Tobacco products .....	850	763	953	989	1,190
Miscellaneous manufacturing industries .....	<u>2,223</u>	<u>2,443</u>	<u>3,069</u>	<u>2,134</u>	<u>2,337</u>
Total .....	<u>151,528</u>	<u>150,262</u>	<u>153,610</u>	<u>153,944</u>	<u>152,489</u>

Sources: Department of Labor and Human Resources — Census of Manufacturing, except for the March 1995 to 1997 which were derived from the "Monthly Survey on Employment, Hours and Earnings."

## Leading United States and Foreign Companies with Manufacturing Operations in Puerto Rico

### Employment 2,500 and over

	<u>Product</u>
American Home Products .....	Pharmaceuticals
Baxter International .....	Pharmaceuticals
Eaton Corp. ....	Electronic Instruments
General Electric Co. ....	Electrical Instruments
H. J. Heinz Co. ....	Food
Johnson and Johnson .....	Pharmaceuticals
Sara Lee Corp. ....	Apparel

### Employment 1,500 to 2,499

Abbott Laboratories, Inc. ....	Pharmaceuticals
Bristol-Myers Squibb .....	Pharmaceuticals
Hewlett-Packard .....	Computers
Intel .....	Computers
Merck & Co. ....	Chemicals
Unicord Co. LTD .....	Food
Warner-Lambert Co. ....	Pharmaceuticals

### Employment 1,000 to 1,499

Dexter Shoe .....	Footwear
Hampshire Designers Group ....	Textiles
Hubbell Incorporated .....	Electrical Instruments
Motorola, Inc. ....	Electronic Components
P.L. Industries, Inc. ....	Apparel
Pfizer .....	Pharmaceuticals
Schering-Plough Corp. ....	Pharmaceuticals
Sensormatic Electronics .....	Electronic Instruments

### Employment 500 to 999

Allergan .....	Pharmaceuticals
Angles Dairy Management .....	Dairy Products
Aramark .....	Apparel
Atlantron, Inc. ....	Communications
Avon Products Inc. ....	Costume Jewelry
B. Braun Medical Systems .....	Medical Equipment
Becton-Dickinson & Co. ....	Scientific Instruments
Checkpoint Systems, Inc. ....	Electronic
Coachman Inc. ....	Apparel
Coleman Co. ....	Luggage
Conagra .....	Food
DSC Communication Corp. ....	Communication Equipments
Dooney & Bourke .....	Leather
DuPont (E.I.) de Nemours .....	Chemicals
Echlin Mfg. ....	Motor Vehicles Parts
Eli Lilly and Co. ....	Pharmaceuticals
General Instruments Corp. ....	Communications
H.H. Brown Shoes Co., Inc. ....	Footwear
Ingersoll-Rand Co. ....	Electrical Instruments
Insilco Corporation .....	Office Equipment
Isla Verde Investment .....	Apparel
MacAndrews & Forbes Holdings .	Tobacco Products
Maidenform .....	Apparel
Medtronics .....	Surgical and Medical Instruments
Monsanto .....	Pharmaceuticals

Nycomed ASA .....	Pharmaceuticals
Owens Illinois .....	Glass and Plastics
Penn-State Coats & Aprons .....	Apparel
Pharmacia Up-John Co. ....	Pharmaceuticals
Phillips Van-Heusen .....	Apparel and Footwear
Propper International .....	Apparel
R.J.R. Nabisco .....	Food and Cigarettes
Seaboard Fluor Corp. ....	Food
SmithKline Beecham .....	Pharmaceuticals
Storage Technology .....	Electronics
Thomas & Betts .....	Electrical Instruments
Timberland Company (The) .....	Leather
U.S. Surgical .....	Scientific Instruments
Wolverine World Wide .....	Footwear

### Employment 300 to 499

AMP Incorporated .....	Electronic Connectors
Amgen Manufacturing Co. ....	Pharmaceuticals
Block Drug Co. ....	Consumers Products
Carnival Creations .....	Apparel
Carolina Underwear Co. ....	Apparel
Centennial .....	Communications
Coca-Cola Company (The) .....	Food
Colgate-Palmolive Co. ....	Consumers Products
Collin & Aikman Group, Inc. ....	Stockings
Eagle Work Clothes .....	Apparel
Eastern Canvas Products .....	Leather
Emerson Electric .....	Electronic and Scientific Instruments
Esco Manufacturing Co. ....	Structural Steel
Goya Foods .....	Food
Granada Sales .....	Apparel
Lawson Mardon Wheaton .....	Glass and Plastics
Loctite Corp. ....	Chemicals
Millipore Corp. ....	Scientific Instruments
Nestle S.A. ....	Pharmaceuticals
Nypro .....	Medical Devices
Ocular Science-American Hydron .....	Ophthalmic Products
Packaging Coordinators Inc. ....	Packaging Products
Pall Corp. ....	Filters
Phillips Petroleum Co. ....	Petroleum Products
Procter & Gamble Co. ....	Pharmaceuticals
Productos del Trópico .....	Food
R.E. Phelon & Co. ....	Electronics
Randa Corporation .....	Textiles
Siecor Corp. ....	Optic Fibers
Siemens AG .....	Electrical Instruments
Standard Motor Products .....	Motor Vehicles Parts
Stryker Corp. ....	Surgical and Medical Instruments
Sundstrand Corp. ....	Electrical Instruments
Syntex Corp. ....	Pharmaceuticals
Unifirst Corp. ....	Work Garment
Unilever PLC .....	Consumers & Medicals
Wesley Jessen Corp. ....	Ophthalmic Products
Zeneca Group PLC .....	Pharmaceuticals

Source: Economic Development Administration, Office of Economic Research (as of January 1998).



## Services

Puerto Rico has experienced significant growth in the services sector in terms of both income and employment over the past decade, showing a favorable trend as compared with certain other industrialized economies. During the period between fiscal 1992 and 1996, the gross domestic product in the services sector increased at an annual average rate of 6.7%. Employment in this sector (including finance, insurance, real estate, wholesale and retail trade, hotels and related services and other services) increased at an annual average rate of 4.2% during the period between fiscal 1993 and 1997. The development of the services sector in the local economy has shown a strong interaction among the following important sectors: manufacturing, tourism, construction, and agriculture. The services sector in Puerto Rico has a diversified base.

The high degree of knowledge, skills, and expertise in professional and technical services available in Puerto Rico places the island in a favorable competitive position with respect to Latin America and other trading countries throughout the world. A major element in the economic program of the present administration is the further development of the local services sector which has the capacity to increase its export potential and to generate more income and jobs during the coming years.

The services sector ranks second to manufacturing in its contribution to gross domestic product, and it is the sector with the greatest employment. In fiscal 1996, services generated \$17.1 billion of gross domestic product, or 37.6% of the total. Service employment grew from 467,000 in fiscal 1993 to 551,000 in fiscal 1997, a cumulative increase of 17.8%, which increase was greater than the 12.9% cumulative growth in total employment over the same period. Wholesale and retail trade and finance, insurance and real estate have experienced significant growth in the fiscal 1992 to 1996 period, as measured by gross domestic product. Gross domestic product in the wholesale and retail trade increased from \$5.0 billion in fiscal 1992 to \$6.2 billion in fiscal 1996. In finance, insurance and real estate, gross domestic product increased from \$4.6 billion in fiscal 1992 to \$5.9 billion in fiscal 1996. There are 20 commercial banks and trust companies currently operating in Puerto Rico of which two are U.S. major money center banks, four are foreign banks and fifteen are local banks and trust companies. Total assets of these institutions as of June 30, 1997 were \$34.7 billion. In addition, two federal thrift institutions and six major securities firms operate on the island.

The following tables set forth gross domestic product for the five fiscal years ended June 30, 1996 and services sector employment for the five fiscal years ended June 30, 1997.

### Puerto Rico

#### Gross Domestic Product by Services Sector (in millions at current prices)

	Fiscal Year Ended June 30				
	1992	1993	1994	1995	1996(p)
Wholesale and retail trade . . . . .	\$4,990	\$5,303	\$5,635	\$5,959	\$6,224
Finance, insurance and real estate . . . . .	4,596	4,897	5,246	5,596	5,878
Hotels . . . . .	351	373	432	475	502
Other services . . . . .	3,231	3,536	3,901	4,218	4,489
Total(1) . . . . .	<u>\$13,168</u>	<u>\$14,109</u>	<u>\$15,214</u>	<u>\$16,248</u>	<u>\$17,093</u>

(p) Preliminary.

(1) Totals may not add due to rounding.

Source: Planning Board.

**Puerto Rico**

**Average Employment by Services Sector  
(thousands of persons age 16 and over)**

	Fiscal Year Ended June 30				
	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>
Wholesale and retail trade . . . . .	201	201	211	218	228
Finance, insurance and real estate . . . . .	32	33	36	39	37
Other services(1) . . . . .	<u>234</u>	<u>244</u>	<u>249</u>	<u>270</u>	<u>285</u>
Total(2) . . . . .	<u>467</u>	<u>478</u>	<u>496</u>	<u>527</u>	<u>550</u>

(1) Includes hotels and related services.

(2) Totals may not add due to rounding.

Source: Department of Labor and Human Resources — Household Survey.

*Hotels and Related Services - Tourism*

Total visitors' expenditures accounted for 6.4% of the island's gross product in fiscal 1997. Visitors' expenditures and the number of visitors to the island have grown consistently since 1985, reaching \$2.0 billion, and more than \$4.3 million, respectively, in fiscal 1997. During fiscal 1997, the number of persons which registered in tourist hotels was 1,260,616, a 4.3% increase compared with fiscal 1996. The average occupancy rate in tourist hotels was 73.2% in fiscal 1997. The average number of rooms rented in tourist hotels increased 6.2% in fiscal 1997, compared with fiscal 1996. These increases are due in part to the increased marketing by the Government of Puerto Rico, the trends in the U.S. economy and increased hotel usage by Puerto Rico residents. Since fiscal 1992, a number of major hotels have undergone substantial renovation and more than 3,073 new rooms have been added with the opening of several major hotels. Various international hotel corporations have recently made substantial capital investments to develop additional tourist facilities. At June 30, 1997, the number of total rooms was 10,877 and is expected to increase to 11,972 during fiscal 1998 with the completion of several new hotels. A major reason for this increase in rooms has been the initiatives of the New Economic Model that encourage private development in tourism projects. See "Economic Development Program—New Economic Model" above and "Tax Incentives" below. During the first four months of fiscal 1998, the number of persons registered in tourist hotels totaled 432,087, a 10.8% increase compared with the same period in fiscal 1997. In the first four months of fiscal 1998, the average occupancy rate in tourist hotels was 67.3%. The average number of tourist hotel rooms available in October was 7,847.

San Juan has become the largest home port for cruise ships in the Caribbean and the second largest home port for cruise ships in the world.

The following table presents data relating to visitors to Puerto Rico and tourist expenditures for the five fiscal years ended June 30, 1997.

**Puerto Rico**

**Tourism Data**

<u>Fiscal Year Ended June 30</u>	<u>Number of Visitors</u>				<u>Total Visitors' Expenditures (in millions)</u>
	<u>Tourist Hotel(1)</u>	<u>Cruise Ship</u>	<u>Other(2)</u>	<u>Total</u>	
1993 .....	688,509	1,014,490	2,165,959	3,868,958	\$1,628.1
1994 .....	702,310	980,220	2,340,065	4,022,595	1,728.3
1995 .....	774,040	955,917	2,356,622	4,086,579	1,827.1
1996(p) .....	828,251	1,045,104	2,336,805	4,110,160	1,896.3
1997(p) .....	906,706	1,107,913	2,335,068	4,349,687	2,046.3

(p) Preliminary.

(1) Includes visitors in guest houses.

(2) Including visitors in homes of relatives, friends, and in hotel apartments.

Sources: Puerto Rico Tourism Company and the Planning Board.

*Government*

The government sector of Puerto Rico plays an important role in the economy. In fiscal 1996, government accounted for \$4.9 billion of Puerto Rico's gross domestic product, or 10.7% of the total. The government is also a significant employer, providing jobs for 261,000 workers, or 23.1% of total employment in fiscal 1997. The government sector employment does not include data relating to public corporations which are included in other sectors. These public corporations include significant employers such as the Electric Power Authority, the Telephone Authority, and the Aqueduct and Sewer Authority.

In May 1997, Governor Rosselló created a commission to study a proposal to permit the unionization of government employees. The commission adopted a resolution on October 14, 1997 proposing that legislation be enacted permitting the unionization of government employees. Such legislation is presently being considered by the Legislature.

*Transportation*

Thirty-four shipping lines offer regular ocean freight service to eighty United States and foreign ports. San Juan is the island's leading seaport, but there are also seaport facilities at other locations on the island including Arecibo, Culebra, Fajardo, Guayama, Guayanilla, Mayagüez, Ponce, Vieques, and Yabucoa.

The Luis Muñoz Marín International Airport is currently served by 24 United States and international airlines. At present, there is daily direct service between San Juan and New York, Chicago, Dallas, Los Angeles, Miami, Atlanta, Boston, and numerous other destinations within the United States. There is also regularly scheduled service between Puerto Rico and other Caribbean islands and major Latin American and European cities. A major United States airline uses San Juan as a hub for its intra-Caribbean service. Several smaller airports serve intra-island traffic.

The island's major cities are connected by a modern highway system which, as of December 31, 1997, totaled approximately 4,600 miles.

## *Construction*

The construction industry has experienced substantial real growth since fiscal 1987. In fiscal 1997, investment in construction rose to an unprecedented level of \$4.7 billion, a nominal increase of 14.7%, as compared to \$4.1 billion for fiscal 1996. The strong growth in the construction industry resulted from increased public and private investment in the past few years. Nominal public investment in key infrastructure projects increased 19.4% in fiscal 1997 and 33.0% in fiscal 1996. Private construction investment, particularly in housing and hotels, increased 8.8% in fiscal 1997 and 17.9% in fiscal 1996. During fiscal 1997, the total value of construction permits increased 19.0% and local cement consumption increased 7.2% in comparison with fiscal 1996. The Planning Board's construction investment forecast for fiscal 1998, made in July 1997, projected a nominal increase of 21.1%. In fiscal 1997, the average employment in the construction sector was 64,401, an increase of 9.4% over fiscal 1996. During the first quarter of fiscal 1998, cement sales increased 14.0% in comparison with the same period in fiscal 1997. In the first quarter of fiscal 1998, the average employment in the construction sector was 66,000.

## *Agriculture*

The Department of Agriculture and related agencies have directed their efforts at increasing and improving local agricultural production, increasing efficiency and quality of produce, and stimulating import substitution where economically feasible. During fiscal 1996, gross income from agriculture was \$662.6 million, a decrease of \$24.5 million in comparison with fiscal 1995. Agriculture gross income consists of the total value of production in the principal agricultural sectors, which include traditional crops, cattle products, farinaceous, vegetables, fruits, and other products. Recently, cattle products, non-traditional crops, and livestock products have contributed a higher percentage of the sector's income.

The Government of Puerto Rico supports agricultural activities through incentives, subsidies, and technical and support services, in addition to income tax exemptions for qualified income derived by bona fide farmers. Act No. 225, approved on December 1, 1995, increased the tax benefits available to bona fide farmers. The Act provides a 90% income tax exemption for income derived from agricultural operations, an investment tax credit equal to 50% of the investment in qualified agricultural projects, and a 100% exemption from excise taxes, real and personal property taxes, municipal license taxes and tariff payments. It also provides full income tax exemption for interest income from bonds, notes and other debt instruments to be issued by financial institutions to provide financing to agricultural businesses. Recent legislation imposes an aggregate annual limitation of \$15 million on the investment tax credits available under Act No. 225.

As part of the programs embodied in the New Economic Model, the Government of Puerto Rico has sold or has entered into a definitive agreement to sell to private entities various agricultural operations previously conducted by governmental entities. These include certain assets of the pineapple processing operation and a mango growing facility. Currently, the Government is in the process of transferring the sugar processing facilities of the Sugar Corporation to local private sugar cane growers.

## **Higher Education**

During the four decades from 1950 to 1990, Puerto Rico made significant advances in the field of education, particularly at the college and graduate school level. The transformation of Puerto Rico during the 1950's and 1960's from an agricultural economy to an industrial economy brought about an increased demand for educational services at all levels. During the 1970's and 1980's, certain higher wage, higher technology industries became more prominent in Puerto Rico. More recently, employment in the services sector has increased significantly. This has resulted in an increased demand for workers having a higher level of education, in general, and, in particular, greater expertise in various technical fields. During the same time period, enrollments in institutions of higher learning rose very rapidly due to growth in the college-age population, and the increasing proportion of college attendance by such population. After the 1980's, college attendance has remained relatively stable as a percentage of the college age population, generally following the trend in the United States.

The University of Puerto Rico, the only public university in Puerto Rico, includes eleven campuses located throughout the island. Total enrollment of the University was 68,020 students during academic year 1997-1998. The government of Puerto Rico is legally bound to appropriate annually to the University an amount equal to 9.60% of the

average annual revenue from internal sources for each of the two fiscal years immediately preceding the current fiscal year.

The following table presents comparative trend data for Puerto Rico and the United States with respect to college age population and percentage of such population attending institutions of higher learning.

### Trend in College Enrollment

Academic Year	Puerto Rico			Mainland United States		
	Population 18-24 Years of Age	Higher Education Enrollment	Percent(1)	Population 18-24 Years of Age	Higher Education Enrollment	Percent(1)
1970 .....	341,448	57,340	16.8%	23,714,000	8,580,887	36.2%
1980 .....	397,839	130,105	32.7	30,022,000	12,096,895	40.3
1990 .....	417,636	156,147	37.4	26,950,000	13,820,000	51.3
1994 .....	444,252	161,689	36.4	25,289,000	14,279,000	56.5
1995 .....	453,476	167,172	36.9	24,932,000	14,209,000	57.0
1996 .....	454,055	171,548	37.8	24,616,000	14,399,000	58.5

(1) Number of persons of all ages enrolled in institutions of higher education as percent of population 18-24 years of age.

Sources: Planning Board, U.S. Bureau of the Census, U.S. National Center for Education Statistics and Council on Higher Education of Puerto Rico.

In addition to the University of Puerto Rico, there are 37 private institutions of higher education located in Puerto Rico. Such institutions have current enrollment in excess of 109,180 students and provide programs of study in liberal arts, education, business, natural sciences, technology, secretarial and computer sciences, nursing, medicine, and law. Degrees are offered by these institutions at the associate, bachelor, master, and doctoral levels.

### Tax Incentives

One of the factors assisting the development of the manufacturing sector in Puerto Rico has been the various local and federal tax incentives available, particularly those under Puerto Rico's Industrial Incentives Program and Sections 30A and 936 of the Internal Revenue Code of 1986, as amended (the "Code"). New tax and other incentives have been established to promote the development of the tourism industry. These incentives are summarized below.

#### *Industrial Incentives Program*

Since 1948, Puerto Rico has had various industrial incentives laws designed to stimulate industrial investment in the island. Under these laws, companies engaged in manufacturing and certain other designated activities were eligible to receive full or partial exemption from income, property, and other local taxes. The most recent of these industrial incentives laws is Act No. 8 of January 24, 1987, known as the Puerto Rico Tax Incentives Act (the "1987 Act"). The activities eligible for exemption under the 1987 Act include manufacturing, certain designated services performed for markets outside Puerto Rico, the production of energy from local renewable sources for consumption in Puerto Rico, and laboratories for scientific and industrial research.

The 1987 Act provides a fixed 90% exemption from income and property taxes, and a 60% exemption from municipal license taxes during a 10, 15, 20 or 25 year period, depending on the region where the operations are located. This initial exemption period may be extended for an additional 10 years at lower exemption rates. The 1987 Act also provides for a special deduction equal to 15% of the production payroll for companies whose net income from operations is less than \$30,000 per production job. This special benefit is designed to attract and maintain labor intensive operations in Puerto Rico. The income from certain qualified investments in Puerto Rico ("passive income") and the instruments evidencing such investments are fully exempt from income, property and other local taxes. In addition, companies making qualifying investments for fixed periods of not less than five years are eligible to reduce the withholding tax (also known as the "tollgate tax") imposed on dividend and liquidating distributions from a maximum rate of 10% to a minimum rate of 5%, depending on the amount and term of their qualifying investments.

The 1987 Act imposes a special surtax based on sales volume, designed to raise revenues to fund a special government program of scientific and technical research for the development of new products and industrial processes, and the creation of special training programs for the chronically unemployed.

In 1993, the 1987 Act was amended to require the prepayment of a portion of the tollgate tax payable on dividend and liquidating distributions and to impose a minimum tollgate tax of 5% (previously the tollgate tax could be reduced to zero) on dividend and liquidating distributions. The amount of tollgate tax required to be prepaid is 5% of the company's annual income after the payment of income taxes. As a result of these amendments, the Department of the Treasury has increased its annual collections of tollgate taxes and is now able to predict with greater accuracy the annual tollgate tax revenues expected to be generated. The 1993 amendments also contained an option for companies to pay an upfront flat tax of 14% on annual net income, which would allow companies electing this option to repatriate their profits free of tollgate taxes. Under this option, if a company were to invest 25% or 50% of its profits in qualified investments, the 14% rate would drop to 11% or 9%, respectively.

Under the 1987 Act, as amended, applications for grants of tax exemption could be filed until December 31, 1996. On September 12, 1996 the Governor of Puerto Rico signed into law Act No. 212 which postponed the deadline for filing applications until December 31, 1997.

On December 2, 1997 the Governor of Puerto Rico signed into law Act No. 135 (the "1998 Tax Incentives Law"), a new industrial incentives law aimed at attracting and retaining foreign investment in Puerto Rico.

The benefits provided by the 1998 Tax Incentives Law are available to new companies as well as companies currently conducting tax exempt operations in Puerto Rico which choose to renegotiate their existing tax exemption grant. The activities eligible for tax exemption include manufacturing, certain designated services performed for markets outside Puerto Rico, the production of energy from local renewable sources for consumption in Puerto Rico and laboratories for scientific and industrial research. For companies qualifying thereunder, the 1998 Tax Incentives Law would impose income tax rates ranging from 2% to 7%. In addition, it would grant 90% exemption from property taxes, 100% exemption from municipal license taxes during the first eighteen months of operation and between 80% and 60% thereafter, and 100% exemption from municipal excise taxes. The 1998 Tax Incentives Law also provides various special deductions designed to stimulate employment and productivity, research and development and capital investment in Puerto Rico.

Under the 1998 Tax Incentives Law, companies can repatriate or distribute their profits free of tollgate taxes. In addition, passive income derived from the investment of eligible funds in Puerto Rico financial institutions, obligations of the Government of Puerto Rico and other designated investments continue to be fully exempt from income and municipal license taxes. Individual shareholders of an exempted business are allowed a credit against their Puerto Rico income taxes equal to 30% of their proportionate share in the exempted business' income tax liability. Gain from the sale or exchange of shares of an exempted business by its shareholders during the exemption period is subject to a 4% income tax rate.

#### *Tourism Incentives Program*

For many years Puerto Rico has also had incentives laws designed to stimulate investment in hotel operations on the island. The most recent of these laws, the Tourism Incentives Act of 1993, provides exemptions from income, property, and municipal license taxes for a period of up to 10 years. In addition, it provides certain tax credits for qualifying investments in hotel development projects.

As part of the incentives to promote the tourism industry, the Government of Puerto Rico established the Tourism Development Fund as a subsidiary of GDB with the authority to make investments in or provide financing to entities that contribute to the development of the tourism industry. The Fund was initially capitalized with \$50,000,000 and was authorized to provide financial guarantees for financing hotel development projects. To date the Fund has provided financial guarantees to private entities issuing bonds or borrowing funds to finance the development of five hotel projects which provided approximately 1,350 new hotel rooms.

## *Sections 30A and 936 of the Code*

For many years, United States companies operating in Puerto Rico enjoyed a special tax credit that was available under Section 936 of the Code. Originally, the credit provided an effective 100% federal tax exemption for operating and qualifying investment income from Puerto Rico sources. Amendments to Section 936 made in 1993 (the “1993 Amendments”) instituted two alternative methods for calculating the tax credit and limited the amount of the credit that a qualifying company could claim. These limitations are based on a percentage of qualifying income (the “percentage of income limitation”) and on qualifying expenditures on wages, other wage related benefits and other qualifying expenditures (the “economic activity limitation”, also known as the “wage credit limitation”). As a result of amendments incorporated in the Small Business Job Protection Act of 1996 enacted by the United States Congress and signed into law by President Clinton on August 20, 1996 (the “1996 Amendments”), as described below, the tax credit is now being phased out over a ten-year period for existing claimants and is no longer available for corporations that establish operations in Puerto Rico after October 13, 1995 (including existing Section 936 Corporations (as defined below) to the extent substantially new operations are established 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. The Section 30A Credit and the remaining Section 936 credit are discussed below.

Section 30A. The 1996 Amendments added a new Section 30A to the Code. Section 30A permits a “qualifying domestic corporation” (“QDC”) that meets certain gross income tests (which are similar to the 80% and 75% gross income tests of Section 936 of the Code discussed below) to claim a credit (the “Section 30A Credit”) against the federal income tax imposed on taxable income derived from sources outside the United States from the active conduct of a trade or business in Puerto Rico or from the sale of substantially all the assets used in such business (“possession income”).

A QDC is a United States corporation which (i) was actively conducting a trade or business in Puerto Rico on October 13, 1995, (ii) had a Section 936 election in effect for its taxable year that included October 13, 1995, (iii) does not have in effect an election to use the percentage limitation of Section 936(a)(4)(B) of the Code, and (iv) does not add a “substantial new line of business.”

The Section 30A Credit is limited to the sum of (i) 60% of qualified possession wages as defined in the Code, which includes wages up to 85% of the maximum earnings subject to the OASDI portion of Social Security taxes plus an allowance for fringe benefits of 15% of qualified possession wages, (ii) a specified percentage of depreciation deductions ranging between 15% and 65%, based on the class life of tangible property, and (iii) a portion of Puerto Rico income taxes paid by the QDC, up to a 9% effective tax rate (but only if the QDC does not elect the profit-split method for allocating income from intangible property).

A QDC electing Section 30A of the Code may compute the amount of its active business income, eligible for the Section 30A Credit, by using either the cost sharing formula, the profit-split formula or the cost-plus formula, under the same rules and guidelines prescribed for such formulas as provided under Section 936 (see discussion below). To be eligible for the first two formulas, the QDC must have a significant presence in Puerto Rico.

In the case of taxable years beginning after December 31, 2001, the amount of possession income that would qualify for the Section 30A Credit would be subject to a cap based on the QDC’s possession income for an average adjusted base period ending before October 14, 1995 (the “income cap”).

Section 30A applies only to taxable years beginning after December 31, 1995 and before January 1, 2006.

Section 936. Under Section 936 of the Code, as amended by the 1996 Amendments, United States corporations that meet certain requirements and elect its application (“Section 936 Corporations”) are entitled to credit against their United States corporate income tax, the portion of such tax attributable to income derived from the active conduct of a trade or business within Puerto Rico (“active business income”) and from the sale or exchange of substantially all assets used in the active conduct of such trade or business. To qualify under Section 936 in any given taxable year, a corporation must derive for the three-year period immediately preceding the end of such taxable year, (i) 80% or more of its gross income from sources within Puerto Rico, and (ii) 75% or more of its gross income from the active conduct of a trade or business in Puerto Rico.

Under Section 936, a Section 936 Corporation may elect to compute its active business income, eligible for the Section 936 credit, under one of three formulas: (i) a cost-sharing formula, whereby it is allowed to claim all profits attributable to manufacturing intangibles and other functions carried out in Puerto Rico provided it makes a cost sharing payment in the amount required under Section 936; (ii) a profit-split formula, whereby it is allowed to claim 50% of the combined net income of its affiliated group from the sale of products manufactured in Puerto Rico; or (iii) a cost-plus formula, whereby it is allowed to claim a reasonable profit on the manufacturing costs incurred in Puerto Rico. To be eligible for the first two formulas, the Section 936 Corporation must have a significant business presence in Puerto Rico for purposes of the Section 936 rules.

As a result of the 1993 Amendments and the 1996 Amendments, the Section 936 credit is only available to companies that were operating in Puerto Rico on October 13, 1995 and had elected the percentage of income limitation, and is limited in amount to 40% of the credit allowable prior to the 1993 Amendments, subject to a five-year phase-in period from 1994 to 1998 during which period the percentage of the allowable credit is reduced from 60% to 40%.

In the case of taxable years beginning on or after 1998, the possession income subject to the 936 credit will be subject to a cap based on the Section 936 Corporation's possession income for an average adjusted base period ending on October 14, 1995. The 936 credit is eliminated for taxable years beginning in 2006.

Proposal to Extend the Phaseout of Section 30A. During 1997, Governor Rosselló proposed to Congress the enactment of a new permanent federal incentive program similar to what is now provided under Section 30A. Such program would provide U.S. companies a tax credit based on qualifying wages paid and other wage related expenses, such as fringe benefits, as well as depreciation expenses for certain tangible assets and research and development expenses. Under the Governor's proposal, the credit granted to qualifying companies would continue in effect until Puerto Rico shows, among other things, substantial economic improvements in terms of certain economic parameters. The fiscal 1998 budget submitted by President Clinton to Congress in February 1997 included a proposal to modify Section 30A to (i) extend the availability of the Section 30A Credit indefinitely, (ii) make it available to companies establishing operations in Puerto Rico after October 13, 1995, and (iii) eliminate the income cap. President Clinton's proposal, however, was not included in the fiscal 1998 federal budget. While the Government of Puerto Rico plans to continue lobbying for this proposal, it is not possible at this time to predict whether the Section 30A Credit will be so modified.

Outlook. It is not possible at this time to determine the long-term effect on the Puerto Rico economy of the enactment of the 1996 Amendments. The Government of Puerto Rico does not believe there will be short-term or medium-term material adverse effects on Puerto Rico's economy as a result of the enactment of the 1996 Amendments. The Government of Puerto Rico further believes that during the phase-out period sufficient time exists to implement additional incentive programs to safeguard Puerto Rico's competitive position.



## DEBT

### Public Sector Debt

Public sector debt comprises bonds and notes of the Commonwealth, its municipalities, and public corporations ("notes" as used in this section refers to certain types of non-bond debt regardless of maturity), subject to the exclusions described in the following paragraph. Direct debt of the Commonwealth is supported by Commonwealth taxes. Debt of municipalities, other than bond anticipation notes, is supported by real and personal property taxes, and municipal license taxes. Debt of public corporations, other than bond anticipation notes, is generally supported by the revenues of such corporations from rates charged for services or products. See *Public Corporations*. However, certain debt of public corporations is supported, in whole or in part, directly or indirectly, by Commonwealth appropriations or taxes.

The following table presents a summary of public sector debt as of December 31, 1997, as adjusted for the expected issuance on January 29, 1998 of the Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 1998, in the principal amount of \$503,963,264.10 (the "Series 1998 Refunding Bonds") and the refunding of certain general obligation bonds of the Commonwealth (the "Refunded Bonds") by the Series 1998 Refunding Bonds. Excluded from this table is debt not primarily payable from either Commonwealth or municipal taxes, Commonwealth appropriations or rates charged by public corporations for services or products. Also excluded from the following table is debt the inclusion of which would reflect double counting, including, but not limited to, \$602,985,000 of bonds issued by the Municipal Finance Agency to finance its purchase of bonds of Puerto Rico municipalities, and \$1,653,762,000 of obligations of GDB issued to purchase certain Commonwealth public sector debt and for other purposes, of which \$267,000,000 is guaranteed by the Commonwealth.

### Puerto Rico

#### Public Sector Debt (in thousands)

	December 31, 1997
Puerto Rico direct debt(1) .....	\$ 4,919,668
Municipal debt.....	885,105
Public corporations debt .....	
Puerto Rico guaranteed debt(2) .....	446,420
Debt supported by Puerto Rico appropriations or taxes(3).....	8,195,945
Other non-guaranteed debt.....	5,933,395
Total public corporations debt.....	14,575,760
Total public sector debt .....	\$20,380,533

- 
- (1) Includes a \$21,415,921 loan from GDB to the Department of the Treasury to settle certain property tax claims of the municipalities (the "GDB Tax Claims Loan") and \$117,571,000 of certain indebtedness originally issued by Urban Renewal and Housing Corporation that was transferred to the Commonwealth by virtue of Act No. 134 of the Legislature of Puerto Rico, approved on December 13, 1994 ("Act No. 134 of 1994") (such indebtedness referred to as "Transferred CRUV Debt").
  - (2) Excludes \$1,814,511,000 of Public Buildings Authority bonds and notes which are primarily payable from Commonwealth appropriations and \$267,000,000 of GDB bonds payable from available moneys of GDB. Consists of bonds issued by Housing Bank and Finance Agency and Aqueduct and Sewer Authority.
  - (3) Represents, among others, bonds and notes issued by Aqueduct and Sewer Authority, Highway and Transportation Authority, Public Buildings Authority, Public Finance Corporation, Infrastructure Financing Authority, Economic Development Bank (and its affiliate, the Agriculture and Commercial Development Corporation), Health Facilities and Services Administration, and Housing Bank and Finance Agency.

Source: GDB.

No deductions have been made in the above table for debt service funds and debt service reserve funds. The table above and the amounts shown throughout this section as representing outstanding debt include outstanding capital appreciation bonds at their respective original principal amounts and do not include any accretion thereon.

## Debt Service Requirements for Commonwealth General Obligation Bonds and Certain Guaranteed Debt

The following table presents debt service requirements for general obligation bonds and bonds of Aqueduct and Sewer Authority for which debt service payments are being made under the Commonwealth guaranty, in each case outstanding on December 31, 1997, as adjusted for the issuance of the Series 1998 Refunding Bonds and the refunding of the Refunded Bonds. See "Commonwealth Guaranteed Debt" below. With respect to other debt of Aqueduct and Sewer Authority, see *Public Corporations*. Debt service requirements for each fiscal year, as shown in the following table, include principal and interest due on July 1 immediately following the close of such fiscal year.

### Puerto Rico Debt Service Requirements\* (in thousands)

Fiscal Year Ending <u>June 30</u>	Outstanding Bonds			Aqueduct and Sewer Authority Bonds Debt	Adjusted
	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Service</u>	<u>Total</u>
1998 .....	\$ 177,375	\$ 223,824	\$ 401,199	\$ 33,473	\$ 434,672
1999 .....	200,276	221,037	421,312	33,530	454,843
2000 .....	227,855	206,712	434,567	33,509	468,075
2001 .....	233,881	194,493	428,374	33,473	461,847
2002 .....	234,864	183,932	418,796	33,542	452,338
2003 .....	168,189	250,724	418,913	32,745	451,658
2004 .....	139,245	244,310	383,555	30,125	413,681
2005 .....	214,402	165,587	379,989	30,127	410,116
2006 .....	176,028	179,046	355,074	30,121	385,195
2007 .....	150,054	184,763	334,816	30,126	364,943
2008 .....	123,878	149,184	273,062	30,131	303,193
2009 .....	132,970	121,836	254,806	30,123	284,929
2010 .....	142,525	111,820	254,345	29,984	284,329
2011 .....	149,822	104,030	253,852	29,928	283,781
2012 .....	158,195	88,610	246,805	30,127	276,932
2013 .....	148,740	80,397	229,137	30,128	259,264
2014 .....	117,068	91,405	208,472	30,125	238,597
2015 .....	121,955	86,701	208,656	30,126	238,782
2016 .....	126,335	82,252	208,587	30,121	238,707
2017 .....	132,512	76,249	208,760	30,122	238,882
2018 .....	137,870	70,794	208,664	30,126	238,790
2019 .....	148,200	39,538	187,738	30,125	217,863
2020 .....	156,825	32,049	188,874	0	188,874
2021 .....	121,760	23,862	145,622	0	145,622
2022 .....	105,820	17,759	123,579	0	123,579
2023 .....	87,845	12,452	100,297	0	100,297
2024 .....	68,950	7,846	76,796	0	76,796
2025 .....	49,485	4,053	53,538	0	53,538
2026 .....	27,760	1,388	29,148	0	29,148
<b>Total</b>	<b><u>\$4,180,681</u></b>	<b><u>\$3,256,652</u></b>	<b><u>\$7,437,333</u></b>	<b><u>\$681,937</u></b>	<b><u>\$8,119,270</u></b>

\* Totals may not add due to rounding.

Sources: GDB and Department of the Treasury.

## **Commonwealth Guaranteed Debt**

As of December 31, 1997, \$46,080,000 of Commonwealth guaranteed bonds of Housing Bank and Finance Agency were outstanding. These bonds were originally issued by Urban Renewal and Housing Corporation and refinanced in fiscal 1992 by Housing Bank and Finance Agency. Annual debt service on these bonds is \$13,252,788 in fiscal 1999, which constitutes their maximum annual debt service. Their final maturity is October 1, 2001.

As of December 31, 1997, \$1,814,511,000 of Commonwealth guaranteed bonds of Public Buildings Authority were outstanding. Annual debt service on these bonds is \$150,008,064 in fiscal year ending June 30, 1998, with their final maturity being July 1, 2027.

No payments under the Commonwealth guaranty have been required to date for bonds of Housing Bank and Finance Agency or Public Buildings Authority.

As of December 31, 1997, \$267,000,000 of Commonwealth guaranteed obligations of GDB were outstanding. No payments under the Commonwealth guaranty have been required for any obligations of GDB to date.

As of December 31, 1997, the Commonwealth had guaranteed certain outstanding revenue bonds of the Aqueduct and Sewer Authority in the aggregate principal amount of \$400,340,000. On January 1, 1997, the Commonwealth began to make debt service payments under the Commonwealth guaranty and expects to make all debt service payments required on these revenue bonds.

The Farm Credit Corporation ("Farm Credit"), created pursuant to Act No. 68, approved on June 8, 1960, as amended, assumed responsibility in 1971 for the administration of the Farm Credit Security Fund (the "Security Fund") from the Department of Agriculture. The Security Fund has guaranteed, under the good faith and credit of the Commonwealth, certain loans made by financial institutions and Farm Credit to farmers. The Security Fund is authorized to guarantee loans, of which approximately \$11,393,053 has been committed as of December 31, 1997. As of December 31, 1997, \$3,066,798 was available in the Security Fund to cover loan payment defaults by farmers.

The functions of Farm Credit and the administration of the Security Fund were transferred to Commercial and Agricultural Credit and Development Corporation, a new public corporation (which is an affiliate of Economic Development Bank) created to provide, among other things, loans to the commercial and agricultural sectors. Simultaneously with the creation of this new corporation, the amount of guarantees was limited to the outstanding loans which carry such guaranty. A joint resolution adopted by the Legislature on August 19, 1990, appropriated \$8,000,000 per year beginning in fiscal 1993, to provide funds for the Security Fund. The proceeds of these appropriations were used to pay a \$40,000,000 loan made by GDB to the Security Fund used to cover payment on loans guaranteed by the Security Fund. The GDB loan was fully repaid on November 4, 1996.

## **Trends of Public Sector Debt**

Historically, Puerto Rico has maintained a fiscal policy which provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. The Government of Puerto Rico has also sought opportunities to realize debt service savings by refunding outstanding debt with obligations bearing lower interest rates.

During fiscal 1992 to 1996, public sector debt and gross product increased 27.5% and 27.7%, respectively. During fiscal 1993 to 1997, however, public sector debt increased 37.0% while gross product increased 27.7%. This higher level of growth of public sector debt over the growth of gross product is due to the increase during fiscal 1996 and 1997 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. This trend of higher levels of public sector debt relative to the growth in gross product is expected to continue during the next few fiscal years as the level of public sector capital investment remains high.

As of December 31, 1997, outstanding short-term debt, relative to total debt, was 10.1%, including \$600 million tax and revenue anticipation notes of the Commonwealth issued on December 3, 1997 and payable on July 30, 1998.

The following table shows the trends in gross product (in current dollars) and public sector debt for the five fiscal years ended June 30, 1997 and the first six months of fiscal 1998.

**Puerto Rico  
Public Sector Debt and Gross Product  
(dollars in millions)**

June 30	Public Sector Debt					Gross Product(1)	
	Long Term	Short Term(2)	Short Term as % of		Rate of Increase	Amount	Rate of Increase
			Total	Total*			
1993 .....	\$13,257	\$985(3)	6.9%	\$14,242	3.0%	\$25,133	6.1%
1994 .....	14,077	1,181(3)	7.7	15,258	7.1	26,641	6.0
1995 .....	14,688	1,305	8.2	15,993	4.8	28,413	6.7
1996 .....	16,316	1,310	7.4	17,626	10.2	30,254(p)	6.5
1997 .....	17,865	1,642(3)	8.4	19,507	10.7	32,032(p)	5.9
December 31, 1997 .....	18,322(5)	2,059(4)	10.1	20,381	4.5	-	-

\* Totals may not add due to rounding.

(p) Preliminary.

(1) In current dollars.

(2) Obligations issued with a maturity of three years or less are considered short term debt.

(3) Does not include the tax and revenue anticipation notes which were outstanding at the close of the indicated fiscal years because sufficient funds had been set aside for the payment of such notes in full prior to the end of said fiscal years.

(4) Includes \$600,000,000 Tax and Revenue Anticipation Notes, Series 1998A, maturing July 30, 1998.

(5) As adjusted for the expected issuance on January 29, 1998 of the Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 1998, and the refunding of certain general obligation bonds of the Commonwealth.

Source: GDB.

The following table shows the trend of public sector debt by major category for the five fiscal years ended June 30, 1997 and the first six months of fiscal 1998.

**Puerto Rico  
Public Sector Debt by Major Category  
(dollars in millions)**

June 30	Commonwealth			Municipalities			Public Corporations(1)			Total*		Grand Total*
	Long Term	Short Term(2)	Total*	Long Term	Short Term(2)	Total*	Long Term	Short Term(2)	Total*	Long Term	Short Term(2)	
1994 .....	3,713	120(3)	3,833	571	47	618	9,792	1,014	10,807	14,077	1,181(3)	15,257
1995 .....	4,236	30	4,266(4)	679	53	732	9,773	1,222	10,995	14,688	1,305	15,993
1996 .....	4,203	0	4,203(4)	706	58	765	11,405	1,251	12,657	16,316	1,310	17,625
1997 .....	4,512	0(3)	4,512	843	51	894	12,509	1,590	14,000	17,865	1,642(3)	19,507
Dec. 31, 1997 .....	4,320(6)	600(5)	4,920	843	42	885	13,159	1,417	14,576	18,322	2,059	20,381

\* Totals may not add due to rounding.

(1) Includes Commonwealth guaranteed debt.

(2) Obligations with a maturity of three years or less are considered short term debt.

(3) Does not include the tax and revenue anticipation notes which were outstanding at the close of the indicated fiscal years because prior to the end of said fiscal years sufficient funds had been set aside for the payment of such notes in full.

(4) Includes the GDB Tax Claims Loan and the Transferred CRUV Debt.

(5) Includes \$600,000,000 Tax and Revenue Anticipation Notes, Series 1998A, maturing July 30, 1998.

(6) As adjusted for the expected issuance on January 29, 1998 of the Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 1998, and the refunding of certain general obligation bonds of the Commonwealth.

Source: GDB.

## PUBLIC CORPORATIONS

In Puerto Rico, many governmental or quasi-governmental functions are performed by public corporations. These are governmental entities created by the Legislature with varying degrees of independence from the central government. Public corporations are generally created to perform a single function or a limited number of related functions. Most public corporations obtain revenues from rates charged for services or products, but many are subsidized to some extent by the central government. Most public corporations are governed by boards appointed by the Governor with the advice and consent of the Senate, but some public corporations are subsidiaries of departments of the central government. Capital improvements of most of the larger public corporations are financed by revenue bonds under trust agreements or bond resolutions or notes under loan agreements. The following table presents the outstanding bonds and notes of certain of the public corporations as of December 31, 1997 ("notes" as used in this section refers primarily to certain types of non-bonded debt regardless of maturity). Debt of certain other public corporations is excluded from this table because such debt is payable primarily from the Federal government or is payable from sources other than Commonwealth appropriations or taxes, or revenues of public corporations, or is payable from revenues derived from services or products, such as industrial development bonds. Also excluded from this table is debt of certain public corporations the inclusion of which would reflect double counting. No deductions have been made in the table for debt service funds and debt service reserve funds. More detailed information about the major public corporations is presented in the following sections.

### Outstanding Debt December 31, 1997 (in thousands)

	Bonds			Notes			Total Bonds and Notes		
	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total
Agricultural Services Administration	\$ 0	\$ 0	\$ 0	\$ 0	\$ 44,126	\$ 44,126	\$ 0	\$ 44,126	\$ 44,126
Aqueduct and Sewer Authority	400,340	67,216(1)	467,556	0	244,820	244,820	400,340	312,036	712,376
Agricultural and Commercial Credit and Development Corporation	0	0	0	0	21,176	21,176	0	21,176	21,176
Electric Power Authority(2)	0	3,516,040	3,516,040	0	160,000	160,000	0	3,676,040	3,676,040
Health Facilities and Services Administration	0	0	0	0	848,145(3)	848,145(3)	0	848,145	848,145
Highway and Transportation Authority	0	2,411,955	2,411,955	0	160,185	160,185	0	2,572,140	2,572,140
Housing Bank	46,080	783,495	829,575	0	245,554	245,554	46,080	1,029,049	1,075,129
Industrial Development Company(2)	0	202,488	202,488	0	25,104	25,104	0	227,592	227,592
Infrastructure Financing Authority	0	1,017,045	1,017,045	0	0	0	0	1,017,045	1,017,045
Public Finance Corporation	0	464,173(3)	464,173	0	0	0	0	464,173	464,173
Office for the Improvement of Public Schools	0	0	0	0	229,313	229,313	0	229,313	229,313
Ports Authority	0	122,455	122,455	0	142,613	142,613	0	265,068	265,068
Public Buildings Authority(2)	1,814,511	0	1,814,511	0	74,627	74,627	1,814,511	74,627	1,889,138
Sugar Corporation	0	0	0	0	27,419(3)	27,419(3)	0	27,419	27,419
Telephone Authority	0	894,365	894,365	0	0	0	0	894,365	894,365
University of Puerto Rico	0	330,330	330,330	0	185	185	0	330,515	330,515
Others	0	10,998	10,998	0	421,002	421,002	0	432,000	432,000
<b>Total</b>	<b>\$2,260,931(4)</b>	<b>\$9,820,560</b>	<b>\$12,081,491</b>	<b>\$ 0</b>	<b>\$2,644,269</b>	<b>\$2,644,269</b>	<b>\$2,260,931(4)</b>	<b>\$12,464,829</b>	<b>\$14,725,760</b>

- (1) Principal of and interest on this debt is reimbursed from Commonwealth appropriations.
- (2) Does not include accretion of interest from the respective issuance dates on capital appreciation bonds as follows: Electric Power Authority \$107,265,418 as of December 31, 1997; Industrial Development Company \$7,875,256, as of December 31, 1997; and Public Buildings Authority \$43,859,023, as of December 31, 1997.
- (3) Payable primarily from Commonwealth appropriations.
- (4) Authorization for Commonwealth guarantee of debt as of December 31, 1997, was \$3,483,000,000. Excludes \$11,393,053 of loans from lending institutions to farmers guaranteed by the Security Fund as of December 31, 1997.

Source: GDB.

## Government Development Bank for Puerto Rico

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, to make loans and advances to public corporations and municipalities, and to make loans to private enterprises to aid in the economic development of Puerto Rico.

As of November 30, 1997, \$1,118,882,000 of bonds and notes of GDB were outstanding. GDB has \$2,983,096,000 in loans to local public corporations and municipalities. Act No. 12 of May 9, 1975, as amended, provides that the payment of principal of and interest on specified notes and other obligations of GDB, not exceeding \$550,000,000, may be guaranteed by the Commonwealth, of which \$267,000,000 were outstanding as of December 31, 1997.

GDB has the following principal subsidiaries:

*Higher Education Assistance Corporation* was established in May 1981 for the purpose of guaranteeing loans made to post-secondary school students under federal insurance programs. The operations of this Corporation were transferred to the Great Lakes Higher Education Corporation, a guarantee agency based in Wisconsin, and the Corporation is in the process of liquidation.

*Housing Finance Corporation* was created in November 1977 to provide needed rental housing units and stimulate the construction industry under federally subsidized programs. The Corporation has issued tax-exempt revenue bonds and notes to finance the construction of housing units approved for federal rental subsidies, which bonds and notes are limited obligations of the Corporation payable solely from revenues collected in respect of such housing units. The Federal Housing Administration has insured mortgages on certain of the housing units. As of December 31, 1997, \$1,044,403,622 of bonds of Housing Finance Corporation were outstanding.

*Tourism Development Fund* was created in November 1993 to promote the hotel and tourism industry of Puerto Rico, primarily by making available guarantees to secure the payment of private financing used for new hotel development projects. The Tourism Development Fund is also authorized to make capital investments and provide direct financing to tourism related projects. As of December 31, 1997, the Tourism Development Fund had issued guarantees totaling \$225,949,987.

*Development Fund* was created in 1977 to provide an alternate source of financing to private enterprises in Puerto Rico that have difficulties in obtaining financing from traditional sources. The Development Fund may also guarantee obligations of these enterprises and invest in their equity securities.

*Capital Fund* was created in November 1993 for trading in debt obligations and publicly traded shares of domestic and foreign corporations.

*Public Finance Corporation* was established in December 1984 to provide agencies and instrumentalities of Puerto Rico with alternate means of meeting their financing requirements. On June 30, 1995, the Corporation issued \$296,393,974 of bonds to purchase from GDB certain debt issued by Maritime Shipping Authority, a portion of which bonds was subsequently refunded. On April 23, 1996, the Corporation issued \$192,108,735 of bonds to purchase from GDB a portion of a debt of the Secretary of the Treasury relating to advances made to the municipalities to settle certain property tax claims. As of December 31, 1997, the Corporation had \$464,173,000 aggregate principal amount of bonds outstanding.

A description of certain other affiliates of GDB is provided in "Other Public Corporations."

## Other Public Corporations

*Aqueduct and Sewer Authority* owns and operates a system of public water supply and sanitary sewer facilities. Capital expenditures are financed by revenues of the system, debt issuances, and federal and Puerto Rico grants. Debt service on revenue bonds is payable from net revenues of the system after payment of current expenses.

Facilities and operations of the Authority's system are subject to regulation under numerous federal and Puerto Rico environmental laws, including the federal Clean Water Act administered by the United States Environmental Protection Agency ("EPA"). The Authority has embarked on an extensive capital improvement program for the five-year period ending June 30, 2002, that is estimated to cost approximately \$1.7 billion. A portion of the capital improvement program is designed to enable the Authority to comply with federal and Commonwealth laws and regulations.

The Authority needs to make a substantial investment in infrastructure and a major overhaul of its operations to maintain the viability of the existing system and to finance its expansion for new users. Funds for this investment are expected to be provided through a combination of bond issues, legislative appropriations and federal grants. Due to the Authority's financial difficulties (discussed below) and its inability to access the bond market, Act No. 45 was enacted in July 1994 to provide a Commonwealth guaranty of the principal and interest payments to the bondholders of all outstanding debt previously issued by the Authority which, at that time, amounted to \$388 million, and to also guarantee all future bonds or any other similar obligations incurred by the Authority to refinance such debt. In December 1995, the Authority issued \$400,340,000 of its Refunding Bonds, Series 1995 (the "Series 1995 Bonds") to refund all of the Authority's outstanding revenue and revenue refunding bonds. The Series 1995 Bonds are guaranteed by the Commonwealth pursuant to Act No. 45. On January 2, 1997, the Commonwealth began making all debt service payments under said guaranty in respect of the Series 1995 Bonds.

Legislation was approved in July 1994 providing for annual Commonwealth appropriations to the Authority to pay a portion of the principal of and interest on the Authority's indebtedness and/or to defray a portion of the Authority's operating and maintenance expenses, as follows: \$20 million for fiscal 1995, \$25 million for fiscal 1996, \$30 million for fiscal 1997, and \$35 million for fiscal 1998. Additional legislation was approved in August 1997 providing for annual Commonwealth appropriations of \$35 million annually through fiscal 2008.

On May 26, 1995, the Authority and Professional Services Group, Inc. ("PSG") entered into a five-year agreement (the "Agreement") for the operation, management, repair and maintenance of the Authority's public water supply and sanitary sewer facilities (including its customer services systems) (the "Authority System"). PSG, which is headquartered in Houston, Texas, is a subsidiary of Compagnie Generale des Eaux, a French based international waste and wastewater utility and operations service company. The Agreement includes terms and conditions that are expected to result in improved efficiency of the Authority System. Fees and other amounts payable to PSG under the Agreement for fiscal years 1998 to 2001 will be approximately \$360.1 million. The Agreement includes incentives to encourage PSG to improve collections from the Authority's customers, as well as penalties in the event PSG fails to operate the Authority System within specified employment parameters. The annual fees may be adjusted to provide for certain unforeseen events and circumstances, such as excessive overtime. The Agreement gives the Authority the right, without penalty, to terminate the contract at the end of the third year. PSG began its management and operations at the Authority on September 1, 1995.

The Authority has also entered into an agreement with Thames-Dick Superaqueduct Partners, Inc. for the planning, design, construction, operation and maintenance of the North Coast Superaqueduct Project (the "Project") to supply additional potable water to certain municipalities, mainly in the San Juan Metropolitan Area. The total estimated cost for the Project is approximately \$345 million. GDB is providing interim financing for this Project, which is being paid over time from the proceeds of Commonwealth general obligation bonds or from Commonwealth General Fund appropriations. On May 20, 1997, in a suit brought by a local environmental group challenging the validity of the permits issued for the Project, the Puerto Rico Circuit Court of Appeals issued an order revoking the land use permit granted by the Planning Board and staying the construction of the Project. This decision was affirmed by the Puerto Rico Supreme Court. Construction of the Project resumed in June, 1997, however, after approval of legislation authorizing, among other things, a special permitting process for the Project. The Project is now approximately 50% complete and is expected to be completed by late 1998, as originally scheduled.

Included in the Authority's strategic projects is a major dredging program of the Carraizo Reservoir with an estimated cost of \$60 million. The Carraizo Reservoir is the main water supply source for the San Juan Metropolitan

Area. This dredging project is directed at recovering reservoir storage capacity by removing approximately 6 million cubic meters of sediment. Under the agreement signed on October 7, 1996 with Weeks Marine Corporation, with headquarters in New Jersey, the Authority entered into a multi-year dredging program to remove sediment from the Carraizo Reservoir which includes the construction, operation, and maintenance of the areas that will be used to dispose of the dredged materials. GDB approved a \$50 million line of credit to the Authority to provide partial interim financing to pay for the dredging and related costs. This financing will be paid from the proceeds of Commonwealth general obligation bonds or from Commonwealth General Fund appropriations. The dredging commenced on August, 1997.

Notwithstanding the issuance of the Series 1995 Bonds, the execution of the Agreement with PSG discussed above, and the legislative appropriations previously discussed, it is likely that additional substantial legislative appropriations to the Authority may be needed for several years in order to support the financial and operational viability of the Authority, and to allow the Authority to finance its capital improvement program. The Authority has reported net losses during the past three fiscal years ended June 30, 1997 of approximately \$60.5 million, \$91.0 million and \$55 million, respectively. These losses reflect the continuing financial and operating difficulties that the Authority has experienced in recent years, and were further aggravated in fiscal 1996 by extraordinary items, including the required adoption of new government accounting requirements relating to required expense reserves, the posting of previous years' non-registered entries and adjustments, employees' salary increases and early retirement bonuses, and non-budgeted or underestimated expenses relating to the PSG Agreement.

*Economic Development Bank* was created in July 1985 to engage primarily in granting small direct loans, providing loan guarantees to private enterprises, and making equity investments in such enterprises. Its initial capital was provided by a transfer of loans in the principal amount of \$15,000,000 previously administered by a now inactive subsidiary of GDB. As of June 30, 1997, the Economic Development Bank had outstanding \$42,000,000 of collateralized Promissory Notes.

*Electric Power Authority* owns and operates the island's electric system. Capital improvements are financed primarily by borrowed funds, supplemented by internally generated funds. The Authority's bonded debt consists of Power Revenue Bonds, secured by a lien on net revenues of the electric system. As of December 31, 1997, the Authority had \$3,516,040,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). The Authority has entered into power purchase contracts relating to the construction of certain cogeneration plants that will use fuels other than oil. See "Economic Development Program—New Economic Model" under *The Economy* above.

*Health Facilities and Services Administration* ("AFASS") was created by Act No. 26 of November 13, 1975, as amended, for the purpose of carrying out the following functions: planning, evaluation and development of health services, alleviation of environmental contamination, operation of public hospitals and other health facilities, prevention and treatment of mental illness and administration of family planning programs and maternal and child care activities. The operations of AFASS are funded substantially by appropriations from the Commonwealth. AFASS' outstanding indebtedness to GDB as of December 31, 1997 was \$848,145,000 payable primarily from Commonwealth appropriations. Such indebtedness is expected to be paid also from the proceeds of the sale of certain health facilities.

*Highway and Transportation Authority* is responsible for highway construction in Puerto Rico. Such construction is financed by debt (interim notes and revenue bonds), revenues of the Authority, and federal and Puerto Rico grants. Debt service on the Authority's revenue bonds constitutes a first lien on its gross revenues, which consist currently of all the proceeds of the gasoline tax, one-half of the proceeds of the tax on gas oil or diesel oil, highway toll revenues, and the gross receipts of \$15.00 per vehicle per year from certain motor vehicle license fees. Such revenues (except for toll revenues) may be applied first to the payment of debt service on general obligation bonds and notes of the Commonwealth and payments required to be made by the Commonwealth under its guarantees of bonds and notes to the extent that no other revenues are available for such purpose. The Government of Puerto Rico has never applied such revenues for such payment. As of December 31, 1997, the Highway and Transportation Authority had \$2,411,955,000 in bonds outstanding.

The Authority is a party to a concession agreement under which a private company designed, constructed and currently is operating a toll bridge spanning the San José Lagoon. The toll bridge was financed with special facility revenue bonds of the Authority payable by the private company principally from toll revenues. The concession is for a term of 35 years, subject to earlier termination or extension. The bridge opened for traffic in February 1994. In certain circumstances as described in the concession agreement, including where toll revenues are insufficient to generate certain



rates of return to the private operator, the private company may require the Authority, among other things, to assume the private company's obligations with respect to the special facility revenue bonds. Some of those circumstances, including low toll revenues, exist at this time, but the Authority does not currently anticipate that the private company will exercise its remedy against the Authority.

The Authority has contracted with various qualified firms for the planning, design, construction, and operation of certain segments of a light-rail mass transit system to serve a portion of the San Juan metropolitan area.

On July 16, 1997, legislation was approved providing to the Authority up to \$120 million annually from proceeds of an excise tax on crude oil, unfinished oil and derivative products imposed by the Commonwealth. This additional source of income will enable the Authority to improve its capacity to finance its capital improvement program.

*Housing Bank and Finance Agency* is engaged in insuring mortgages and servicing mortgages originated by Urban Renewal and Housing Corporation and issues bonds and notes to provide interim and permanent financing for low-income housing projects and single-family home ownership programs. The Agency obtains funds from legislative appropriations, sales of mortgages, mortgage repayments and other sources.

As of December 31, 1997, the Agency had outstanding \$829,575,000 of bonds (of which \$46,080,000, originally issued by the Urban Renewal and Housing Corporation, are guaranteed by the Commonwealth) issued to pay obligations of the Commonwealth under law, otherwise payable from Commonwealth appropriations, to fund certain payments of the Commonwealth under its mortgage subsidy program for low and moderate income families, to guarantee certain insurance obligations of the Agency under certain programs, and to refund bonds originally issued by Urban Renewal and Housing Corporation to carry out activities related to the provision of low-cost housing for moderate income families, federally aided public housing for low income families, and urban renewal, housing and related activities. These bonds are payable principally from appropriations in substantially the amount that the Commonwealth would otherwise have been bound to appropriate for such purposes.

*Industrial Development Company* participates in the Commonwealth-sponsored economic development program by providing physical facilities, general assistance, and special incentive grants to manufacturers. The Company was merged into the Economic Development Administration on January 1998. Rentals derived from the leasing of specified facilities of the Company are pledged to the payment of the Company's revenue bonds. As of December 31, 1997, the Company had \$202,488,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds).

*Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority* was created in June 1977. The Authority has issued revenue bonds to finance industrial, tourist, pollution control, medical, and educational facilities in Puerto Rico for the use of private companies, non-profit entities, or government agencies. The bonds are payable solely from payments to be made to the Authority by such private companies, non-profit entities, or government agencies, and do not constitute a debt of the Commonwealth or any of its other public corporations or municipalities. As of December 31, 1997, \$2,182,950,181 of the Authority's bonds were outstanding.

*Infrastructure Financing Authority* was created in June 1988 by virtue of Act No. 44 of June 21, 1988, as amended ("Act No. 44") to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other public corporations and governmental instrumentalities of Puerto Rico authorized to develop infrastructure facilities and to establish alternate means for financing infrastructure facilities. Act No. 44 also established the Puerto Rico Infrastructure Fund, funded in the amount of \$30 million during fiscal 1989 and \$40 million for the following twenty-nine fiscal years with the first proceeds of federal excise taxes imposed on rum and other articles produced in Puerto Rico and sold in the United States which are transferred to Puerto Rico pursuant to the Internal Revenue Code of 1986, as amended. On July 7, 1997, Act No. 44 was amended to increase to \$60 million for fiscal year 1998 and \$70 million for each subsequent year until fiscal year 2028 the amount of federal excise taxes transferred to the Authority. The increased level of appropriations will be used by the Authority to provide additional financial support to Aqueduct and Sewer Authority.

In November 1988, the Authority issued \$327,740,000 of Special Tax Revenue Bonds, Series 1988A to refund in advance certain outstanding revenue bonds and other debt of the Aqueduct and Sewer Authority. As of December 31, 1997, \$209,285,000 of such bonds were outstanding. The Authority's Special Tax Revenue Bonds, Series 1988A are

secured by a pledge of a portion of such federal excise taxes, subject to the prior application of such taxes to the payment of Puerto Rico's general obligation bonds and notes and certain other obligations guaranteed by Puerto Rico.

In December 1997, the Authority issued \$801,760,000 Special Tax Revenue Bonds, Series 1997A and 1997B, to finance certain capital projects and working capital needs of Aqueduct and Sewer Authority. The Authority is expected to issue \$134,660,000 Special Tax Revenue Refunding Bonds, Series 1998A, on or about April 2, 1998, to refund certain of its outstanding revenue bonds. The Authority had \$1,011,045,000 in Bonds outstanding as of December 31, 1997.

*Maritime Shipping Authority* commenced operations in 1974 upon the acquisition of three shipping lines serving Puerto Rico and the United States mainland. The Authority acquired vessels and other equipment financed by the issuance of notes on a secured basis to the previous owners. As of the date of the sale of the Authority's assets referred to below, the Authority carried approximately 30% of the total cargo shipped between Puerto Rico and the United States mainland.

On March 3, 1995, the assets and operations of Maritime Shipping Authority were acquired by an investor group headed by BTIP, a subsidiary of Bankers Trust New York Corporation, under the terms and conditions approved by the Legislature of Puerto Rico and signed by the Governor on September 27, 1994.

Act No. 112 of September 27, 1994, restructured the operations and administration of the Authority by creating the Maritime Shipping Authority as a public corporation affiliated with GDB, subject to the control of the President of GDB, but as a separate legal entity, apart from GDB and any of its other affiliates and subsidiaries. The remaining debt of the Authority was refinanced, as allowed under Act No. 113 of September 27, 1994, by the issuance of bonds by Public Finance Corporation, a subsidiary of GDB. The aggregate principal amount of such bonds as of December 31, 1997, was \$374,135,000. The bonds are payable from funds to be appropriated annually by the Legislature of Puerto Rico. Public Finance Corporation purchased a note of the Authority from GDB with the proceeds of the bonds issued.

*Municipal Finance Agency* was created in 1972 as a municipal "bond bank" for Puerto Rico. The Agency is authorized to issue bonds to purchase general obligation bonds and notes of Puerto Rico municipalities and to fund a debt service reserve. Debt service on the Agency's bonds is payable from debt service payments on municipal bonds held by the Agency and from the reserve, including investment income thereon. The Government of Puerto Rico has agreed to pay such amounts to the reserve as may be necessary to maintain it at its required level, subject to appropriation by the Legislature, which appropriation is not legally required to be made. To date no such payments have been required.

*Ports Authority* owns and operates the major airport and seaport facilities in Puerto Rico. The Authority derives revenues from a variety of sources, including charges on airplane fuel sales, air terminal space rentals, landing fees, wharfage, dockage and harbor fees, and rentals for the lease of seaport equipment and property. The Authority has a \$126.3 million line of credit from GDB for capital improvements, of which approximately \$99.3 million was outstanding as of December 31, 1997. This line of credit has been increased to \$144.2 million to partially finance the dredging of San Juan Bay. In addition, GDB has approved a \$32.9 million line of credit for the Authority to finance the construction of a new multi-level parking facility at the Luis Muñoz Marín International Airport. The Authority had total net losses of approximately \$70 million during fiscal years 1993 and 1994, and, as a result, was not in compliance with its rate covenant with bondholders. After eliminating its operating losses through a comprehensive rate revision process including the implementation of annual (instead of triennial) rate revision analyses, the Authority is currently in compliance with its rate covenant. The Authority is implementing a plan to restructure its operations which, among other things, encompasses revisions to its capital improvement program, measures to increase collections from certain users of its facilities and proposals to improve the efficiency of its operations. As of December 31, 1997, the Authority had \$122,455,000 in bonds outstanding.

*Public Buildings Authority* is authorized to construct, purchase or lease office, school, health, and social welfare facilities for lease to departments, public corporations, and instrumentalities of the Government of Puerto Rico. Bonds that have been issued by the Authority to finance such facilities (through retirement of interim notes or otherwise) are payable from lease payments, which are largely derived from legislative appropriations, and are further secured by the Commonwealth's guaranty. The Authority is authorized by Act No. 17 of 1968, as amended, to have outstanding at any one time up to \$2,100,000,000 of bonds guaranteed by the Commonwealth. As of December 31, 1997, \$1,814,511,000 of such bonds of the Authority were outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). The Authority has four lines of credit for its capital improvement program totaling \$694,457,805 of which \$74,627,000 was outstanding as of December 31, 1997.

The Authority is undertaking a program to construct additional correctional facilities to be completed by the end of fiscal 2001 at an estimated cost of \$187,000,000. The Authority has previously issued \$126,972,552 in bonds to finance the construction of three correctional facilities, which will be operated by private companies.

At present, the Government of Puerto Rico is a defendant in a lawsuit filed in United States District Court in which it is charged with violating the constitutional rights of correctional system inmates as a result of severe overcrowding in the island's correctional system. Fines to assure compliance with minimum space standards have been assessed in the past against the Government of Puerto Rico. Most of these fines have been earmarked for improving the conditions of inmates but not for construction of additional correctional facilities to alleviate prison overcrowding. In April 1995, the District Court judge overseeing the above lawsuit imposed an additional series of fines against the Government of Puerto Rico for noncompliance with the minimum space standards, which fines may exceed \$30 million. The Government of Puerto Rico can give no assurance that additional fines will not be levied in connection with the above mentioned lawsuit. The Authority is not responsible for the payments of these fines.

*Sugar Corporation* was created in 1973 to consolidate ownership and management of the Government of Puerto Rico's interests in Puerto Rico's sugar industry. Sugar Corporation owns or leases and operates virtually all the sugar production facilities on the island. Sugar Corporation buys all cane grown by private growers, processes the cane, and sells crude and refined sugar and molasses. For many years, its operations produced substantial operating deficits. For fiscal 1998 appropriations of approximately \$8,543,086 were made to cover the operating deficit. As of December 31, 1997, the total debt of the Corporation was \$27,419,000 payable primarily from Commonwealth appropriations.

At present, the Government of Puerto Rico is in the process of transferring the operations of the Corporation to certain entities to be formed by sugar cane growers. On September 5, 1996, the Governor of Puerto Rico signed into law Act No. 189, which authorizes the transfer, for a nominal sum, of certain assets and liabilities of the Corporation to entities to be created by the sugar cane growers. The Corporation will retain substantially all its liabilities. The transfer is subject to a definitive agreement to be negotiated between the sugar cane growers and the Corporation and is subject to the approval of the Legislature of Puerto Rico.

*Telephone Authority* was created in July 1974 when the Government of Puerto Rico purchased Puerto Rico Telephone Company ("PRTC") from International Telephone and Telegraph Corporation. Puerto Rico Telephone Company operates the principal telephone system in Puerto Rico. The Telephone Authority acquired the assets of the Puerto Rico Communications Authority on May 30, 1990. Capital improvements at present are financed by internally generated funds, although in the past they have also been financed with revenue bonds. The Authority's revenue bonds are payable from net revenues, which consist primarily of moneys received after payment of the Company's operating expenses. As of December 31, 1997, the Authority had \$894,365,000 of bonds and other obligations outstanding, none of which was supported by the guaranty of the Commonwealth.

On April 7, 1997, Governor Rosselló announced the Government's intention to sell PRTC. The sale is expected to be completed during 1998, although no assurance can be given that the sale will be completed by that time. The proceeds of the sale are expected to be used primarily to mitigate the unfunded pension benefit obligation of the Employees Retirement System of the Government of Puerto Rico and its Instrumentalities, to create a trust fund for infrastructure, to assist in the solution of the problems associated with the supply and distribution of water resources, and to pay certain benefits to PRTC employees.

*University of Puerto Rico*, with 68,020 students during academic year 1997-1998, is by far the largest institution of higher education on the island. Government appropriations are the principal source of University revenues, but additional revenues are derived from tuition, student fees, auxiliary enterprises, interest income, federal grants, and other sources. University capital improvements have been financed mainly by revenue bonds of which \$330,330,000 were outstanding as of December 31, 1997.

*Public corporations*, in addition to those mentioned above, have outstanding debt in the aggregate amount of \$684,615,000 as of December 31, 1997. Debt service on \$255,424,000 of such outstanding debt is being paid from legislative appropriations. However, the Government of Puerto Rico is not obligated to make any such appropriations. Additional legislative appropriations are made to enable certain of such corporations to pay their operating expenses.

## INSURANCE MATTERS

Government-owned property is insured through policies obtained by the Secretary of the Treasury and through self-insurance, except for property owned by the Electric Power Authority, the Aqueduct and Sewer Authority, and the Telephone Authority, which are insured through arrangements and policies obtained by the respective Authorities. Personal injury awards against the Government of Puerto Rico are limited by law to \$150,000 per occurrence.

## RETIREMENT SYSTEMS

Public employees of the Government of Puerto Rico and its instrumentalities are covered by five retirement systems: the Employees Retirement System of the Government of Puerto Rico and its Instrumentalities (the "Employees Retirement System"), the Annuity and Pension System for the Teachers of Puerto Rico (the "Teachers Retirement System"), the Commonwealth of Puerto Rico Judiciary Retirement System (the "Judiciary Retirement System"), the Retirement System of the University of Puerto Rico (the "University Retirement System"), and the Employees Retirement System of Puerto Rico Electric Power Authority (the "Electric Power Authority Retirement System").

The University Retirement System and the Electric Power Authority Retirement System apply to employees of the University of Puerto Rico and Electric Power Authority, respectively. The Government of Puerto Rico is not required to contribute directly to those two systems, although a large portion of University revenues are derived from legislative appropriations.

The Teachers Retirement System covers primarily public school teachers, the Judiciary Retirement System covers judges, and the Employees Retirement System covers all other employees of the Government of Puerto Rico, its municipalities and instrumentalities. As of June 30, 1997, the preliminary total number of active members of the three systems was as follows: Employees Retirement System, 159,680; Teachers Retirement System, 61,134 and Judiciary Retirement System, 346. The three systems are financed by contributions made by employers (the Government of Puerto Rico, public corporations, or municipalities), employees, and investment income. The government is responsible for approximately 66% of total employer contributions to the Employees Retirement System and 100% and 99% of total employer contributions to the Judiciary and Teachers Retirement Systems, respectively. Retirement and related benefits provided by the systems and required contributions to the systems by employees are determined by statute. Required contributions to the systems by employers are determined by statute with respect to the Teachers Retirement System and, with respect to the Employees and Judiciary Retirement Systems, by the Administrators of the Systems. In fiscal 1998, the Government of Puerto Rico has budgeted approximately \$275,206,000 as its contribution to the Employees Retirement System, \$4,323,000 as the contribution to the Judiciary Retirement System and \$85,309,760 as its contribution to the Teachers Retirement System.

According to the most recent actuarial valuation of the Employees Retirement System and Judiciary Retirement System submitted by a firm of independent consulting actuaries, as of June 30, 1997, the total pension benefit obligation for the Employees Retirement System and Judiciary Retirement System was \$6,913,900,000 and \$76,500,000, respectively. The unfunded pension benefit obligation of the Employees Retirement System and Judiciary Retirement System for the same period was \$5,469,429,000 and \$19,245,000, respectively. The actuarial valuation was completed in accordance with the "Projected Unit Credit" method. An investment return of 8.5% per year, a salary increase of 5% per year and a post-retirement benefit increase for the Employees Retirement System of 3% every third year were assumed. This benefit increase was provided by the Legislature of Puerto Rico by Act No. 10 of May 10, 1992. The first 3% increase was granted to retirees who have been receiving their annuities for three or more years as of that date. The second 3% increase was granted to retirees who have been receiving their annuities for three or more years as of January 1, 1995. This increase is being financed by additional contributions from the employers. Subsequent increases will depend upon the explicit approval of the System's Board of Trustees and the Legislature, based on a favorable recommendation from the System's independent consulting actuary and given a minimum of 24 months of benefit payment reserves.

On February 1, 1990, the Legislature of Puerto Rico enacted Act No. 1 which is directed at ensuring the solvency of the Employees Retirement System for the next fifty years. Among other provisions, the legislation increases the level of contribution to the System and limits benefits for new employees by increasing the length of time for the vesting of

certain benefits and reducing the level of benefits in the case of early retirement. The legislation also reduces the level of occupational injury and death benefits received by new employees.

The most recent actuarial valuation of the Teachers Retirement System was submitted by a firm of independent consulting actuaries in December 1996. As of June 30, 1996, the actuarial accrued liability of the system was \$2,615,833,862, the actuarial value of assets amounted to \$1,652,819,537, and the resulting unfunded actuarial accrued liability was \$963,014,325, a decrease of \$163,357,932 from the valuation as of June 30, 1995. It is recognized that it will be necessary to further strengthen the finances of the Teachers Retirement System in order to assure that combined contributions and investment income continue to exceed benefit payments, avoiding the possible future drawdown of assets.

The following table presents in summary form, income and expenses of the retirement systems for the fiscal year ended June 30, 1996, preliminary numbers for the fiscal year ended June 30, 1997 and estimates for the fiscal year ending 1998.

**Retirement Systems  
Income and Expenses  
(in thousands)**

	Employees Retirement System	Judiciary Retirement System	Teachers Retirement System
<u>Fiscal Year Ended June 30, 1996</u>			
	<u>Actual</u>	<u>Actual</u>	<u>Actual</u>
Income:			
Employers contributions	\$224,942	\$ 3,890	\$ 79,324
Employee contributions	177,250	1,618	62,991
Investment income	<u>178,616</u>	<u>9,348</u>	<u>127,841</u>
Total	<u>580,808</u>	<u>14,856</u>	<u>270,156</u>
Expenses:			
Benefit payments	399,665	5,846	153,493
Administrative and other expenses	<u>26,907</u>	<u>1,072</u>	<u>14,369</u>
Total	<u>426,572</u>	<u>6,918</u>	<u>167,862</u>
Net Income	<u>\$154,236</u>	<u>\$ 7,938</u>	<u>\$102,294</u>
<u>Fiscal Year Ended June 30, 1997</u>			
	<u>Actual</u>	<u>Actual</u>	<u>Actual</u>
Income:			
Employers contributions	\$248,523	\$4,102	\$ 82,431
Employee contributions	206,094	1,763	68,777
Investment income	<u>230,412</u>	<u>9,290</u>	<u>268,167</u>
Total	<u>685,029</u>	<u>15,155</u>	<u>419,375</u>
Expenses:			
Benefit payments	437,069	6,080	168,643
Administrative and other expenses	<u>33,001</u>	<u>1,815</u>	21,480
Total	<u>470,070</u>	<u>7,895</u>	<u>190,123</u>
Net Income	<u>\$214,959</u>	<u>\$7,260</u>	<u>\$229,252</u>
<u>Fiscal Year Ending June 30, 1998</u>			
	<u>Estimated</u>	<u>Estimated</u>	<u>Estimated</u>
Income:			
Employers contributions	\$270,000	\$4,326	\$ 87,250
Employee contributions	239,000	2,100	71,400
Investment income	<u>250,000</u>	<u>9,000</u>	<u>294,984</u>
Total	<u>759,000</u>	<u>15,426</u>	<u>453,634</u>
Expenses:			
Benefit payments	463,000	6,300	186,200
Administrative and other expenses	28,000	1,100	21,300
Total	<u>491,000</u>	<u>7,400</u>	<u>207,500</u>
Net Income	<u>\$268,000</u>	<u>\$8,026</u>	<u>\$246,134</u>

Sources: Employees Retirement System, Judiciary Retirement System and Teachers Retirement System.

## **SUMMARY OF COMMONWEALTH FINANCIAL STATEMENTS**

Since fiscal 1990, the complete financial statements of the Commonwealth are audited. For fiscal 1997, such financial statements were audited by Deloitte & Touche LLP, whose report thereon is dated December 15, 1997. Preparation of the audited financial statements of the Commonwealth involves the collection and combination of audited financial statements from 48 separate reporting entities.

### **PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES**

The Secretary of the Treasury has custody of the funds of the central government and is responsible for the accounting, disbursement and investment of such funds. Central government funds are grouped into three major categories or "types" of funds, as follows: (i) Governmental Fund Types, which include the General, Special Revenue, Debt Service (also referred to herein as Redemption), and Capital Project Funds; (ii) Proprietary Fund Types, which include the Enterprise and Internal Service Funds; and (iii) Fiduciary Fund Types, which include the Trust and Agency Funds. These funds do not include funds of the municipalities, because the municipalities are governmental entities with independent treasuries. The Special Revenue Fund was incorporated into the General Fund commencing in fiscal 1993.

The General Fund is the primary operating fund of the Government of Puerto Rico. General Fund revenues are broadly based and include revenues raised internally as well as those from non-Puerto Rico sources. Internal revenues consist principally of income taxes and excise taxes. Revenues from non-Puerto Rico sources are derived from federal excise taxes and customs duties returned to the Government of Puerto Rico. The primary expenditures of the Government of Puerto Rico through the General Fund are for grants and subsidies, and personal and other services.

#### **Summary and Management Discussion of General Fund Results**

The following table presents revenues and expenditures of the General Fund on a cash basis for fiscal 1994 through fiscal 1998. Insofar as the information relates to fiscal 1998, it is based on estimates provided by the Secretary of the Treasury as of October 30, 1997. The information for fiscal 1994 through fiscal 1997 is based on actual fiscal year end results. General Fund revenues, expenditures, and transfers as presented in the table, differ from the General Fund revenues, expenditures, and transfers as presented in the financial statements, as the latter statements reflect an expanded General Fund entity in accordance with generally accepted accounting principles.

**Puerto Rico**  
**General Fund Revenues, Expenditures, and Changes in Cash Balance**  
(in thousands)

	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998(1)</u>
Beginning cash balance .....	\$(116,501)	\$ 309,055	\$ 534,929	\$ 147,066	\$127,477
Revenues from internal sources:					
Income Taxes:					
Individuals .....	1,409,824	1,578,269	1,709,116	1,825,337	1,995,000
Corporations .....	1,107,265	1,304,612	1,348,160	1,440,691	1,402,000
Partnerships .....	1,802	3,391	3,323	2,120	3,000
Withheld from non-residents .....	73,626	79,072	78,235	88,603	90,000
Tollgate taxes .....	224,356	220,873	179,454	210,245	199,000
Interest .....	5,293	6,070	6,662	7,582	9,000
Dividends .....	<u>33,968</u>	<u>28,650</u>	<u>43,225</u>	<u>35,438</u>	<u>33,000</u>
Total income taxes .....	<u>2,856,134</u>	<u>3,220,937</u>	<u>3,368,175</u>	<u>3,610,016</u>	<u>3,731,000</u>
Commonwealth excise taxes .....					
Alcoholic beverages .....	220,882	222,187	237,915	229,043	238,000
Cigarettes .....	115,453	107,943	107,177	120,287	108,000
Motor vehicles .....	275,654	319,676	307,931	365,820	387,000
Other excise taxes .....	<u>588,411</u>	<u>602,521</u>	<u>651,001</u>	<u>704,203</u>	<u>637,000</u>
Total Commonwealth excise taxes .....	<u>1,200,400</u>	<u>1,252,327</u>	<u>1,304,024</u>	<u>1,419,353</u>	<u>1,370,000</u>
Property taxes .....	4,568	7,889	5,107	8,286	0
Inheritance and gift taxes .....	934	1,535	1,547	4,028	2,000
Licenses .....	49,084	49,100	50,467	53,535	113,000
Other:					
Lottery .....	62,348	63,317	60,856	52,829	58,000
Electronic Lottery .....	52,193	59,414	57,008	47,994	83,000
Miscellaneous non-tax revenues .....	<u>131,909</u>	<u>125,973</u>	<u>127,734</u>	<u>139,838</u>	<u>138,000</u>
Total other .....	<u>246,450</u>	<u>248,704</u>	<u>245,598</u>	<u>240,661</u>	<u>279,000</u>
Total revenues from internal sources .....	<u>4,357,570</u>	<u>4,780,492</u>	<u>4,974,918</u>	<u>5,335,879</u>	<u>5,495,000</u>
Revenues from non-Commonwealth sources:					
Federal excise taxes .....	185,285	187,494	194,917	203,755	210,000
Customs .....	<u>122,477</u>	<u>112,153</u>	<u>77,781</u>	<u>61,114</u>	<u>50,000</u>
Total revenues from non-Commonwealth sources .....	<u>307,762</u>	<u>299,647</u>	<u>272,698</u>	<u>264,869</u>	<u>260,000</u>
Sub-total revenues .....	4,665,332	5,080,139	5,247,616	5,600,748	5,755,000
Proceeds from special funds .....	<u>55,564</u>	<u>14,155</u>	<u>20,716</u>	<u>23,217</u>	<u>37,000</u>
Total Revenues .....	<u>4,720,896</u>	<u>5,094,294</u>	<u>5,268,332</u>	<u>5,623,965</u>	<u>5,792,000</u>
Other Income .....	<u>558,069</u>	<u>307,931</u>	<u>113,515</u>	<u>80,388</u>	<u>384,627</u>
Transfers to redemption fund (2) .....	(284,346)	(316,766)	(359,638)	(375,000)	(393,950)
Note proceeds (3) .....	700,963	0	0	551,186	601,892
Repayment of notes (4) .....	<u>(717,850)</u>	<u>0</u>	<u>0</u>	<u>(563,628)</u>	<u>(617,775)</u>
Adjusted revenues .....	<u>4,977,732</u>	<u>5,085,459</u>	<u>5,022,209</u>	<u>5,316,911</u>	<u>5,766,794</u>
Expenditures:					
Grants and subsidies .....	1,251,879	1,308,511	1,620,347	1,676,929	1,728,505
Personal services .....	1,559,152	1,805,996	1,993,176	2,164,007	2,690,821
Other services .....	492,653	579,568	602,460	666,004	664,028
Materials and supplies .....	64,945	82,701	86,370	84,789	103,223
Equipment purchases .....	41,885	54,288	54,685	37,507	64,702
Other debt service and capital outlays .....	128,396	0.00	116,863	47,269	217,588
Transfers to agencies .....	565,696	537,649	564,360	355,213	244,383
Other expenditures .....	<u>447,570</u>	<u>436,181</u>	<u>371,811</u>	<u>304,782</u>	<u>157,000</u>
Total expenditures .....	<u>4,552,176</u>	<u>4,859,585</u>	<u>5,410,072</u>	<u>5,336,500</u>	<u>5,870,230</u>
Adjusted revenues less expenditures .....	<u>425,556</u>	<u>225,874</u>	<u>(387,863)</u>	<u>(34,667)</u>	<u>(103,436)</u>
Ending cash balance .....	<u>\$ 309,055</u>	<u>\$ 534,929</u>	<u>\$ 147,066</u>	<u>\$ 127,477</u>	<u>\$ 24,041</u>

- (1) Budget, as adopted.
- (2) Consists of amounts to pay principal of and interest on general obligation bonds and notes of the Commonwealth. Does not include amounts deposited directly to the redemption fund from non-General Fund revenues.
- (3) Consists of proceeds from Commonwealth tax and revenue anticipation notes issued in each such fiscal year.
- (4) Consists of repayment of Commonwealth tax and revenue anticipation notes in each such fiscal year.

Source: Department of the Treasury



### *Estimated Fiscal 1998 Compared to Fiscal 1997*

General Fund estimated total revenues for fiscal 1998 are forecast at \$5,755 million, an increase of \$154.3 million (2.75%) over fiscal 1997. Major projected changes are: an increase in income taxes of individuals of \$121 million; an increase in license fees of \$59.5 million and an increase in electronic lottery collection of \$35 million.

Total projected expenditures for fiscal 1998 are estimated at \$5,870 million, an increase of \$533.7 million (10%) from fiscal 1997. The ending cash balance for the General Fund for fiscal 1998 is estimated to be \$24 million, a decrease of \$103.4 million from fiscal 1997.

### *Fiscal 1997 Compared to Fiscal 1996*

General Fund total revenues for fiscal 1997 were \$5,601 million, an increase of \$353.1 million (6.73%) over fiscal 1996. Major changes were: an increase in income taxes of \$241.8 million and an increase in excise taxes of \$115.3 million.

Total expenditures for fiscal 1997 decreased by \$73.6 million, when compared to fiscal 1996. The ending cash balance for the General Fund for fiscal 1997 was \$127,477 million, a decrease of \$19.6 million from fiscal 1996.

### *Fiscal 1996 Compared to Fiscal 1995*

General Fund total revenues for fiscal 1996 were \$5,247 million, an increase of \$167.5 million (3.3%) over fiscal 1995. Major changes were: an increase in income taxes of \$147.2 million; an increase in excise taxes of \$51.7 million; and a decrease in customs of \$34.4 million.

Total expenditures for fiscal 1996 increased by \$550.5 million, when compared to fiscal 1995. The ending cash balance for the General Fund for fiscal 1996 decreased by \$387.9 million.

### *Fiscal 1995 Compared to Fiscal 1994*

General Fund total revenues for fiscal 1995 were \$5,080 million, an increase of \$414.8 million (8.9%) over fiscal 1994. Major changes were the following: total income taxes and excise taxes increased by \$364.8 million and \$51.9 million, respectively.

Total expenditures for fiscal 1995 increased by \$307.4 million (6.8%), when compared to fiscal 1994. The ending cash balance for the General Fund for fiscal 1995 increased by \$225.8 million.

## **Major Sources of General Fund Revenues**

### *Income Taxes*

Puerto Rico's Internal Revenue Code of 1994 (the "P.R. Code"), adopted on October 31, 1994, imposes a tax on the income of individual residents of Puerto Rico, trusts, estates, and domestic and foreign (if engaged in a trade or business in Puerto Rico) corporations and partnerships. The P.R. Code represented a major revision to the prior income tax structure. The purpose of the P.R. Code was to establish a more equitable tax structure that lowered tax rates and simplified and enhanced compliance.

*Individuals.* Resident individuals are subject to tax on their taxable income from all sources. The P.R. Code has five tax brackets with tax rates of 8%, 12%, 18%, 31% and 33%. Dividend income from Puerto Rico sources is taxed at a rate of 10%. Gains realized from the sale or exchange of a capital asset, if held for more than 6 months, are taxed at a rate of 20%.

Interest income in excess of \$2,000 on deposits with Puerto Rico financial institutions is taxed at a rate of 17%; the first \$2,000 of interest income is exempt from taxation.

*Corporations and Partnerships.* Puerto Rico corporations and partnerships are subject to tax on income from whatever source; foreign corporations and partnerships that are engaged in a trade or business in Puerto Rico are subject

to tax on their income from Puerto Rico sources and on income from sources outside Puerto Rico that is effectively connected with the conduct of a trade or business in Puerto Rico. Unless a corporation or partnership qualifies for partial exemption from corporate income and other taxes under the industrial incentives program (see "Tax Incentives" under *The Economy*), it is subject to tax at graduated rates.

The P.R. Code provides six income tax brackets for corporations and partnerships, with the highest rate (39%) applicable to taxable income in excess of \$275,000. Certain corporations and partnerships covered by the tax incentives act continue to be subject to a maximum tax rate of 45% on their taxable income. Corporations and partnerships covered by the Puerto Rico Tourism Incentives Acts are subject to a maximum tax rate of 42% on their taxable income. The P.R. Code maintains the alternative minimum tax at 22%.

The P.R. Code imposes a branch profits tax on resident foreign corporations. The tax is 10% of an annual dividend equivalent amount and it applies without regard to the Puerto Rico source of income rules.

Interest from Puerto Rico sources paid to non-resident non-affiliated recipients is no longer subject to withholding tax. Interest paid to certain related non-resident recipients is subject to a withholding tax of 29%. Dividends paid to non-resident corporate recipients is subject to a withholding tax of 10%. Gains realized from the sale or exchange of a capital asset, if held for more than six months, is taxed at a maximum rate of 25%. Payments in excess of \$1,000 made by the Government of Puerto Rico and persons engaged in a trade or business in consideration of the receipt of services are now subject to a 7% withholding tax.

In July 1997 the P.R. Code was amended to include certain provisions designed to promote investments in local capital market instruments. The amendments include (i) reducing to 7% the long term capital gains rate applicable to gains from the conversion prior to the year 2001 of any privately owned Puerto Rico corporation or partnership to a publicly owned corporation or partnership; (ii) reducing to 17% the tax rate applicable to interest received by non-corporate taxpayers on certain debt instruments of Puerto Rico corporations or partnerships; and (iii) eliminating the special tax exemption for interest on GNMA Certificates issued after July 31, 1997 (other than those issued in connection with the initial conveyance of newly constructed low and moderate residential property in Puerto Rico).

#### *Excise Taxes*

The P.R. Code imposes a tax on articles and commodities that are imported into or manufactured in Puerto Rico for consumption in Puerto Rico and a tax on certain transactions, such as hotel occupancy, public shows, and horse racing. The excise tax on certain articles and commodities, such as cigarettes and petroleum products, is based upon the quantity of goods imported. The excise tax on motor vehicles is based on the suggested retail prices. The P.R. Code imposes a tax at an effective rate of 6.6% of the F.O.B. factory price for imported goods and 3.6% of the sales price of goods manufactured in Puerto Rico, except sugar, cement, cigarettes, motor vehicles and certain petroleum products which are taxed at different rates. Goods to be used by the government, except for motor vehicles and construction equipment, are not exempt. Exemptions apply to certain articles, such as food and medicines, and to articles designated for certain users.

#### *Other Taxes and Revenues*

Motor vehicle license plate and registration fees comprise the major portion of license tax receipts.

Non-tax revenues consist principally of lottery proceeds, documentary stamps, permits, fees and forfeits, proceeds of land sales, and receipts from certain public corporations in lieu of taxes.

Revenues from non-Puerto Rico sources include customs duties collected in Puerto Rico and excise taxes on shipments of alcoholic beverages from the island to the mainland United States. The customs duties and excise taxes on shipments are imposed and collected by the United States and returned to the Government of Puerto Rico.

#### *Property Taxes*

Personal property, which accounts for approximately 55% of total collections of taxable property, is self-assessed. Real property taxes are currently assessed at 1958 values. No real property reassessment has been made since 1958, and construction taking place after that year has been assessed on the basis of what the value of the property would have been

in 1958. Accordingly, the overall assessed valuation of real property for taxation purposes is substantially lower than the actual market value. Also, an exemption on the first \$15,000 of assessed valuation in owner-occupied residences is available.

On August 30, 1991, legislation was adopted in Puerto Rico providing a municipal reform program which also involved the creation of the Municipal Revenues Collection Center to collect property taxes. The program transferred the previous functions of the Department of the Treasury with respect to real and personal property tax assessment, notification, determination, and collection to the Municipal Revenues Collection Center, as of July 1, 1993. The special 1.03% tax on the assessed value of all property (other than exempted property) imposed by the Commonwealth for purposes of paying the Commonwealth's general obligation debt continues to be deposited in the Commonwealth's Redemption Fund.

### Puerto Rico

#### Assessed Valuations and Real and Personal Property Taxes (Commonwealth and Municipalities Combined) (in thousands)

<u>Fiscal Year Ended June 30</u>	<u>Assessed Valuations(1)</u>	<u>Taxes Levied</u>	<u>Collections of Current Year</u>	<u>Collections of Previous Years</u>	<u>Total</u>
1993 .....	\$11,337,421	\$378,750	\$267,220	\$21,579	288,799
1994 .....	11,735,626	443,448	329,058	32,654	361,712
1995 .....	12,508,656	508,275	370,029	54,241	424,270
1996 .....	17,499,974	533,362	400,207	70,571	470,778
1997(2) .....	19,272,428	619,344	471,445(p)	50,418(p)	521,863(p)

- (p) Preliminary.  
 (1) Valuation set as of July 1 of fiscal year.  
 (2) Municipal Revenues Collection Center Distribution Report August 1997.

Source: Municipal Revenues Collection Center.

During 1997, legislation was enacted authorizing the Center to sell tax liens on residential and commercial properties to persons who, after payment of the purchase price to the Center, would then be responsible for collecting from the delinquent property tax payers.

#### Collections of Income and Excise Taxes

The Department of the Treasury has continued its program for improving tax collections which began in fiscal 1986. The program has consisted, in part, of taking the initiative in sponsoring and implementing tax reform, particularly in the areas of excise taxes and income taxes, in order to decrease the incidences of nonpayment of taxes, and to expand the taxpayer base. The program has also included (a) improving the methods by which delinquent taxpayers are identified, primarily through the use of computer analyses, (b) computerizing the processing of tax returns, and (c) identifying and eliminating taxpayer abuses of the existing tax laws.

#### Transfers to General Obligation Redemption Fund

These consist of transfers from the General Fund to the Redemption Fund for the amortization of the principal of and interest on general obligation bonds and notes of the Commonwealth.

## **Components of General Fund Expenditures**

### *Grants and Subsidies*

This category includes grants and contributions to municipalities, public corporations with independent treasuries, and contributions to charitable institutions. It also includes items for or included in court awards, damage awards for personal injury or property damage, as well as payment of taxes and payment in lieu of taxes.

### *Personal Services*

This category includes compensation paid for personal services rendered to the Government of Puerto Rico and its public instrumentalities by individuals or firms in the form of salaries, wages, *per diems*, fees, commissions, or other forms of compensation.

### *Other Services*

This category includes the payment of services other than the services referred to above, including advertising, printing, communication services, legal expenses, utility services, building and equipment rental and maintenance expenses, insurance premiums and miscellaneous services.

### *Materials and Supplies*

This category includes all articles which ordinarily have short life and durability, lose their characteristic identity in the process of use, have only nominal value (\$25 or less), or are not otherwise chargeable as equipment.

### *Equipment Purchases*

The category includes items which have three special characteristics which distinguish them from materials; durability, long useful life, and high unit cost. In addition, these items are subject to centralized inventory control as fixed assets.

### *Other Debt Service and Capital Outlays*

Includes payments on notes held by GDB to be paid from the balance in the General Fund and payments for the amortization of the principal of and interest on non-general obligations payable from Commonwealth appropriations. Capital outlays are made primarily for land acquisition or interests in land, construction of buildings, roads, bridges and other structures, as well as permanent improvements and additions.

### *Transfers to Agencies*

Includes repayment of loans and advances to other funds, certain refunds, advances from other funds and other receipts, repayment of advances from other funds, grants and contributions to other funds under the custody of the Secretary of the Treasury and other items. The major portion of grants and contributions in recent fiscal years consists of transfers to the Health Facilities and Services Administration and advances to the municipalities.

### *Other Expenditures*

This category represents recurring General Fund expenditures not appropriately attributable to other expenditures line items, such as advances to government agencies and municipalities which advances are to be reimbursed to the General Fund by law.

## **Federal Grants**

Puerto Rico receives federal grants under numerous programs. The following table presents revenues from federal grants by broad program areas which are accounted in the central accounting system of the Department of the Treasury.

**Puerto Rico**

**Federal Grants  
(in thousands)**

	Fiscal Year Ending June 30				
	1994	1995	1996	1997(p)	1998(e)
Education .....	\$ 427,407	\$ 472,409	\$ 529,084	\$ 518,254	\$ 513,709
Social Services .....	1,329,671	1,440,351	1,463,802	1,508,969	1,524,318
Health .....	399,056	392,076	382,497	329,469	322,502
Labor and Human Resources (1) .....	196,736	150,857	136,508	107,800	116,286
Public Works and Transportation(2) ...	45	306	136	39	0
Crime .....	11,161	15,569	20,876	27,198	25,726
Housing(3) .....	201,695	222,312	239,586	224,965	224,787
Drug and Justice .....	6,417	5,148	5,613	9,209	9,714
Agriculture and Natural Resources ....	6,764	12,558	11,546	14,516	6,771
Contributions to Municipalities .....	61,801	65,993	66,389	64,911	64,911
Other .....	16,755	4,687	4,495	5,929	5,629
Total	<u>\$2,657,508</u>	<u>\$2,782,266</u>	<u>\$2,860,812</u>	<u>\$2,811,259</u>	<u>\$2,814,254</u>

(p) Preliminary

(e) Estimated

(1) Amounts include grants to Right to Work Administration and the Occupational Development and Human Resources Council.

(2) Amounts of federal grants to the Highway and Transportation Authority are not included in the Public Works and Transportation area. For fiscal 1994, 1995, 1996 and 1997 the federal grants to this agency are \$75.9 million, \$90.8 million, \$101.9 million and \$128.2 million, respectively.

(3) Amounts include grants to the Public Housing Administration.

**BUDGET OF THE GOVERNMENT OF PUERTO RICO**

**Office of Management and Budget**

The fundamental objective of the Office of Management and Budget (“OMB”) is to improve and strengthen the relationship between policy formulation and budgetary and fiscal management. The law creating OMB also strengthened budgetary controls and created an Operational Audit Division with the primary function of evaluating government operations and programs.

**Budgetary Process**

The fiscal year of the Government of Puerto Rico 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 OMB, working with the Planning Board, the Department of the Treasury, and other government offices and agencies. Section 7 of Article VI of the Constitution provides that “The appropriations made for any fiscal year shall not exceed the total revenues, 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 program budgeting and zero-base budgeting, includes an estimate of revenues and other resources for the ensuing fiscal year under (i) laws existing at the time the budget is submitted, and (ii) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor’s recommendations as to appropriations that in his judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the 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 to cover such deficit. Upon passage by the Legislature, the budget is referred to the Governor who may decrease or eliminate any item but may not increase or insert any new item 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, the annual budget for the preceding fiscal year as originally 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 Government of Puerto Rico to continue to make payments of its operating and other expenses until a new budget is approved.

### **Financial Control and Adjustment Procedures**

Revenue estimates for budgetary purposes are prepared by the Department of the Treasury, except for estimates of federal grants, which are prepared by OMB and various departments and other recipients of such grants. Revenue and federal grant estimates are under continuous review and, if necessary, are revised at least quarterly during the fiscal year. Fiscal control over expenditures is exercised severally by the Governor, through the Director of OMB, and the Secretary of the Treasury. Quarterly reviews and expenditure cut-off procedures are designed to prevent expenditures in excess of appropriations.

During any fiscal year in which the resources available to the Commonwealth are insufficient to cover the appropriations approved for such year, the Governor may take administrative measures to reduce expenses and submit to both houses of the Legislature a detailed report of any adjustment necessary to balance the budget, or make recommendations to the Legislature for new taxes or authorize borrowings under provisions of existing legislation or take any other necessary action to meet the estimated deficiency. Any such proposed adjustments shall give effect to the "priority norms" established by law for the disbursement of public funds in the following order of priority: first, the payment of the interest on and amortization requirements for public debt (Commonwealth general obligations and guaranteed debt for which the Commonwealth's guarantee has been exercised); second, the fulfillment of obligations arising out of legally binding contracts, court decisions on eminent domain, and certain commitments to protect the name, credit and good faith of the Commonwealth; third, current expenditures in the areas of health, protection of persons and property, education, welfare and retirement systems; and fourth, all other purposes.

A Budgetary Fund was created by Act No. 147 of June 18, 1980, as amended (the "Budgetary Fund Act"), to cover the appropriations approved in any fiscal year in which the revenues available for such fiscal year are insufficient, honor the public debt, and provide for unforeseen circumstances in the provision of public services. The Budgetary Fund Act was amended in 1994 to require that an annual legislative appropriation equal to one third of one percent (.33%) of the total budgeted appropriations for each fiscal year be deposited in the Budgetary Fund. In 1997, the Budgetary Fund Act was further amended to increase the annual legislative appropriation required to be deposited in the Budgetary Fund to one percent (1%) of the net revenues of the preceding fiscal year, beginning in fiscal year 2000. In addition, other income (non-tax revenue) that is not assigned by law to a specific purpose is also required to be deposited in the Budgetary Fund. The maximum balance of the Budgetary Fund may not exceed six percent (6%) of the total appropriations included in the budget for the preceding fiscal year.

### **Appropriations**

Appropriations in the central government budget of Puerto Rico consist of the following:

- (i) General Fund appropriations for recurring ordinary operating expenses of the central government and for contributions to public corporations, municipalities, and private organizations. Such appropriations are made by a single annual law known as the Joint Resolution of the General Budget
- (ii) General Fund appropriations for special operating expenses and for capital expenditures. Such appropriations are authorized by separate laws for one or more years for special programs or activities, which may be permanent or transitory.
- (iii) Disbursements of Special Funds for operating purposes and for capital improvements. For the most part, such disbursements do not require annual legislative authorization, because they are authorized by previous legislation or by the United States Congress. Federal grants constitute the major part of the resources of the Special Funds.

(iv) Bond Fund appropriations for capital expenditures financed by bonds. Such expenditures may occur in one or more years.

In Puerto Rico, the central government has many functions which in the fifty states are the responsibility of local government, such as providing public education and police and fire protection. The central government also makes large annual grants to the University of Puerto Rico and to the municipalities. In the summaries of the budgets of the central government presented below, grants to the University of Puerto Rico are included in current expenses for education and debt service on general obligation bonds is included in current expenses for debt service. Debt service on Sugar Corporation notes paid by the Government of Puerto Rico is included in current expenses for economic development, and debt service on Urban Renewal and Housing Corporation bonds and notes and on Housing Bank and Finance Agency mortgage subsidy bonds paid by the Government of Puerto Rico is included in current expenses for housing.

Approximately 24.9% of the General Fund is committed, including debt service on direct debt of the Commonwealth and on the debt of the Sugar Corporation, municipal subsidies, grants to the University of Puerto Rico, contributions to Aqueduct and Sewer Authority, and rental payments to Public Buildings Authority, among others.

**Fiscal 1997 Budget**

The following table presents a summary of the Commonwealth budget for the fiscal year ended June 30, 1997.

**Puerto Rico  
Summary of Central Government Annual Budget  
Fiscal Year Ended June 30, 1997  
(in thousands)**

	<u>General Fund</u>	<u>Bond Fund</u>	<u>Special Funds</u>	<u>Total</u>
Resources:				
Revenues from internal sources:				
Property taxes	\$ 8,286	\$ 0	\$ 65,000	\$ 73,286
Personal income taxes	1,825,337	0	0	1,825,337
Income tax withheld from non-residents	88,603	0	0	88,603
Corporation income taxes	1,440,691	0	0	1,440,691
Partnership income taxes	2,120	0	0	2,120
Tollgate taxes	210,245	0	0	210,245
17% withholding tax on interest	7,582	0	0	7,582
10% withholding tax on dividends	35,438	0	0	35,438
Inheritance and gift taxes	4,028	0	0	4,028
Excise taxes:				
Alcoholic beverages	229,043	0	0	229,043
Motor vehicles and accessories	365,820	0	200	366,020
Cigarettes	120,287	0	0	120,287
Special excise tax on certain petroleum products	158,739	0	0	158,739
General 5% excise tax	446,500	0	0	446,500
Other	98,964	0	67,310	166,274
Licenses	53,535	0	0	53,535
Miscellaneous non-tax revenues:				
Contributions from lottery fund	52,829	0	0	52,829
Electronic lottery	47,994	0	0	47,994
Registration and document certification fees	95,869	0	0	95,869
Other	<u>43,969</u>	<u>0</u>	<u>151,208</u>	<u>195,177</u>
Total revenues from internal sources	5,335,879	0	283,718	5,619,597
Revenues from non-Puerto Rico sources:				
Federal excise taxes on off-shore shipments	203,755	0	16,000	219,755
Federal grants <sup>(1)</sup>	0	0	2,811,259	2,811,259
Customs	<u>61,114</u>	<u>0</u>	<u>0</u>	<u>61,114</u>
Total revenues from non-Puerto Rico sources	<u>264,869</u>	<u>0</u>	<u>2,827,259</u>	<u>3,092,128</u>
Total revenues	<u>5,600,748</u>	<u>0</u>	<u>3,110,977</u>	<u>8,711,725</u>
Other:				
Miscellaneous income	<u>51,175</u>	<u>0</u>	<u>0</u>	<u>51,175</u>
Total other income	51,175	0	0	51,175
Payment in lieu of taxes PRTC	33,000	0	0	33,000
Balance from previous year	16,877	0	336,058	352,935
Bonds authorized	<u>0</u>	<u>369,000</u>	<u>0</u>	<u>369,000</u>
Total other sources	<u>101,052</u>	<u>369,000</u>	<u>336,058</u>	<u>806,110</u>
Total resources	<u>\$5,701,800</u>	<u>\$369,000</u>	<u>\$3,447,035</u>	<u>\$9,517,835</u>



	<u>General Fund</u>	<u>Bond Fund</u>	<u>Special Funds</u>	<u>Total</u>
Appropriations:				
Current expenses:				
General government	\$ 534,527	\$ 0	\$ 26,740	\$ 561,267
Education	1,804,283	0	591,360	2,395,643
Health	787,438	0	354,090	1,141,528
Welfare	319,599	0	1,734,248	2,053,847
Economic development	219,972	0	33,145	253,117
Public safety and protection	922,758	0	67,672	990,430
Transportation and communications	78,746	0	5,345	84,091
Housing	22,570	0	144,148	166,718
Contributions to municipalities	262,241	0	2,013	264,254
Special pension contributions	28,087	0	0	28,087
Debt service	375,000	0	65,000	440,000
Other debt service	<u>300,824</u>	<u>0</u>	<u>0</u>	<u>300,824</u>
Total appropriations-current expenses	<u>5,656,045</u>	<u>0</u>	<u>3,023,761</u>	<u>8,679,806</u>
Capital improvements	14,873	369,000	175,775	559,648
Total appropriations	<u>5,670,918</u>	<u>369,000</u>	<u>3,199,536</u>	<u>9,239,454</u>
Year end balance	<u>30,882</u>	<u>0</u>	<u>247,499</u>	<u>278,381</u>
Total appropriations and year-end balance	<u>\$5,701,800</u>	<u>\$369,000</u>	<u>\$3,447,035</u>	<u>\$9,517,835</u>

(1) Does not include grants received by agencies whose accounting systems are not centralized in the Department of the Treasury.

Sources: Department of the Treasury resources and Office of Management and Budget as reported on October 9, 1997.

In the fiscal 1997 budget proposal revenues and other resources of all budgetary funds total \$8,795,900,000 excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated net increase in General Fund revenues from fiscal 1996 are accounted for by increases in personal income taxes (up \$116,221,000), corporation income taxes (up \$92,531,000), motor vehicles and accessories (up \$57,889,000), 5% excise taxes (up \$49,811,000), tollgate taxes (up \$30,791,000), excise taxes on cigarettes (up \$13,110,000), withholding taxes (up \$10,368,000), federal excise taxes on off-shore shipments (up \$8,838,000), registration and document certification fees (up \$6,864,000), property taxes (up \$3,179,000), and decrease in alcoholic beverages (down \$8,872,000), contributions from lottery fund (down \$8,027,000), electronic lottery (down \$9,014,000), 10% withholding tax on dividends (down \$7,787,000), and customs (down \$16,667,000).

Current expenses and capital improvements of all budgetary funds total \$9,239,454,000, an increase of \$63,797,000 from fiscal 1996. The major changes in General Fund expenditures by program in fiscal 1997 are: public safety and protection (up \$91,767,000), education (up \$98,572,000), general government (up \$43,926,000), debt service (up \$27,096,000), contributions to municipalities (up \$20,973,000), other debts (up \$14,493,000), special pension contributions (up \$5,449,000), transportation and communications (up \$2,146,000), housing (up \$1,388,000), welfare (down \$4,773,000), economic development (down \$27,118,000), reserve to reimburse the General Fund (down \$30,000,000), and health (down \$82,931,000).

The general obligation bond authorization for the fiscal 1997 budget was \$369,000,000.

## Fiscal 1998 Budget

The following table presents a summary of the Commonwealth budget for the fiscal year ended June 30, 1998.

### Puerto Rico Summary of Central Government Annual Budget Fiscal Year Ending June 30, 1998 (in thousands)

	<u>General Fund</u>	<u>Bond Fund</u>	<u>Special Funds</u>	<u>Total</u>
Resources:				
Revenues from internal sources:				
Property taxes	\$ 0	\$ 0	\$ 65,000	\$ 65,000
Personal income taxes	1,995,000	0	0	1,995,000
Income tax withheld from non-residents	90,000	0	0	90,000
Corporation income taxes	1,402,000	0	0	1,402,000
Partnership income taxes	3,000	0	0	3,000
Tollgate taxes	199,000	0	0	199,000
17% withholding tax on interest	9,000	0	0	9,000
10% withholding tax on dividends	33,000	0	0	33,000
Inheritance and gift taxes	2,000	0	0	2,000
Excise taxes:				
Alcoholic beverages	238,000	0	0	238,000
Motor vehicles and accessories	387,000	0	200	387,200
Cigarettes	108,000	0	0	108,000
Special excise tax on certain petroleum products	48,000	0	0	48,000
General 5% excise tax	469,000	0	0	469,000
Slot machines and machines for entertainment	30,000	0	0	90,000
Other	90,000	0	69,040	159,040
Licenses	113,000	0	0	53,000
Miscellaneous non-tax revenues:				
Contributions from lottery fund	58,000	0	0	58,000
Electronic lottery	83,000	0	0	83,000
Registration and document certification fees	95,000	0	0	95,000
Other	<u>43,000</u>	<u>0</u>	<u>142,978</u>	<u>185,978</u>
Total revenues from internal sources	<u>5,495,000</u>	<u>0</u>	<u>277,218</u>	<u>5,772,218</u>
Revenues from non-Commonwealth sources:				
Federal excise taxes on off-shore shipments	210,000	0	16,500	226,500
Federal grants <sup>(1)</sup>	0	0	2,814,353	2,814,353
Customs	<u>50,000</u>	<u>0</u>	<u>0</u>	<u>50,000</u>
Total revenues from non-Commonwealth sources	<u>260,000</u>	<u>0</u>	<u>2,830,853</u>	<u>3,090,853</u>
Total revenues	<u>5,755,000</u>	<u>0</u>	<u>3,108,071</u>	<u>8,863,071</u>
Other:				
Miscellaneous income	<u>60,075</u>	<u>0</u>	<u>0</u>	<u>60,075</u>
Total other income	60,075	0	0	60,075
Payment in lieu of taxes PRTC	58,550	0	0	58,550
Assets sales	65,000	0	0	65,000
Others income	140,000	0	0	140,000
Balance from previous year	30,882	0	247,499	278,381
Bonds authorized	<u>0</u>	<u>500,000</u>	<u>0</u>	<u>500,000</u>
Total other sources	<u>354,507</u>	<u>500,000</u>	<u>247,499</u>	<u>1,102,006</u>
Total resources	<u>\$6,109,507</u>	<u>\$500,000</u>	<u>\$3,355,570</u>	<u>\$9,965,077</u>

	<u>General Fund</u>	<u>Bond Fund</u>	<u>Special Funds</u>	<u>Total</u>
<b>Appropriations:</b>				
<b>Current expenses:</b>				
General government	\$ 528,318	\$ 0	\$ 26,205	\$ 554,523
Education	1,921,995	0	593,321	2,515,316
Health	928,491	0	337,493	1,265,984
Welfare	307,166	0	1,726,924	2,034,090
Economic development	224,061	0	29,083	253,144
Public safety and protection	1,017,718	0	62,249	1,079,967
Transportation and communications	62,150	0	5,283	67,433
Housing	18,851	0	145,629	164,480
Contributions to municipalities	264,518	0	2,209	266,727
Special pension contributions	29,595	0	0	29,595
Debt service	393,950	0	65,000	458,950
Other debt service	<u>410,094</u>	<u>0</u>	<u>0</u>	<u>410,094</u>
Total appropriations—current expenses	6,106,907	0	2,993,396	9,100,303
Capital improvements	<u>230</u>	<u>500,000</u>	<u>167,251</u>	<u>667,481</u>
Total appropriations	6,107,137	500,000	3,160,647	9,767,784
Year-end balance	<u>2,370</u>	<u>0</u>	<u>194,923</u>	<u>197,293</u>
Total appropriations and year-end balance	<u>\$6,109,507</u>	<u>\$500,000</u>	<u>\$3,355,570</u>	<u>\$9,965,077</u>

(1) Does not include grants received by agencies whose accounting systems are not centralized in the Department of Treasury.

Sources: Department of the Treasury and Office of Management and Budget.

In the fiscal 1998 budget proposal revenues and other resources of all budgetary funds total \$9,186,696,000 excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated net increase in General Fund revenues from fiscal 1997 is accounted for by increases in personal income taxes (up \$169,663,000), slot machines and machines for entertainment (up \$90,000,000), electronic lottery (up \$35,006,000), 5% excise taxes (up \$22,500,000), motor vehicles and accessories (up \$21,180,000), alcoholic beverages (up \$8,957,000), and decrease in property taxes (down \$8,286,000), customs (down \$11,114,000), tollgate taxes (down \$11,245,000), cigarettes (down \$12,287,000), corporation income taxes (down \$38,691,000), and special excise tax on certain petroleum products (down \$110,739,000).

Current expenses and capital improvements of all budgetary funds total \$9,767,784,000, an increase of \$528,330,000 from fiscal 1997. The major changes in General Fund expenditures by program in fiscal 1998 are: health (up \$141,053,000), education (up \$117,712,000), public safety and protection (up \$94,960,000), other debts (up \$109,270,000), debt service (up \$18,950,000), economic development (up \$4,089,000), contributions to municipalities (up \$2,277,000), special pension contributions (up \$1,508,000), housing (down \$3,719,000), general government (down \$6,209,000), transportation and communications (down \$16,596,000), and welfare (down \$12,433,000).

The general obligation bond authorization for the fiscal 1998 budget is \$500,000,000.

### **Differences between Budget and General Purpose Financial Statements**

Revenues and expenditures, as reported by the Department of the Treasury in its General Purpose Financial Statements, may differ substantially from resources and appropriations in the annual budget for a number of reasons, including the following:

(i) The budgetary accounts are on a cash basis, while the financial statements prepared by the Department of the Treasury include accruals and other adjustments as required by government accounting standards.

(ii) Expenditures for current purposes in a particular fiscal year may include amounts appropriated for earlier periods but not previously expended and, conversely, may exclude amounts appropriated for such fiscal year but not expended until later periods.

(iii) Bonds are authorized by the Commonwealth in accordance with a four-year capital improvement program. Since bond sales are determined by bond market conditions and other factors, the amount of bonds sold in any year does not necessarily equal the amount of bonds authorized in the budget for that year. Expenditures for capital improvements are financed by advances from the General Fund to the Capital Projects Fund, which are later reimbursed from proceeds of bond or note sales.

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**COMMONWEALTH OF PUERTO RICO**

**COMPREHENSIVE ANNUAL FINANCIAL REPORT**

**FISCAL YEAR ENDED JUNE 30, 1997**

Prepared by the Puerto Rico Department of the Treasury

**Xenia Veléz Silva, Esq., CPA**  
**Secretary of the Treasury**

**Haydée Ortiz Ramos, CPA**  
**Assistant Secretary of Central Accounting**

**Regina Miranda Palacio**  
**Deputy Assistant Secretary of Central Accounting**

**DECEMBER 24, 1997**



# **COMMONWEALTH OF PUERTO RICO TREASURY DEPARTMENT**

## **MISSION OF THE ORGANIZATION**

Establish and carry out the fiscal policies of the Commonwealth of Puerto Rico by enacting a fair and equitable tax system; broaden and balance the taxpayers base; achieve an effective collection of the tax levied and maintain an adequate oversight of the public disbursements, thus promoting: the social and economic development of Puerto Rico, and the trust of the people on its government.

## **ORGANIZATIONAL VALUES**

Our organizational values are focused in our commitment to honesty, integrity, loyalty, justice, sensibility, efficiency, responsibility, accessibility, innovation, professional management, quality and excellence in our functions and services.

## **PURSUIT OF EXCELLENCE**

The products and services of the Department of Treasury shall be considered by our clients as the best. In order to achieve this, we will continuously improve them. Our leaders and fellow workers will be highly admired and respected. Together with other governmental entities and component units of our economy, we will position Puerto Rico as a symbol of excellence.





# COMMONWEALTH OF PUERTO RICO

## COMPREHENSIVE ANNUAL FINANCIAL REPORT FOR THE YEAR ENDED JUNE 30, 1997

### TABLE OF CONTENTS

INTRODUCTORY SECTION	PAGE
Letter of Transmittal	1
General Information of the Commonwealth of Puerto Rico	15
Principal Officials	18
Organization Chart	19
Certificate of Achievement for Excellence in Financial Reporting	20
FINANCIAL SECTION	
Independent Auditors' Report	1
General Purpose Financial Statements:	
Combined Balance Sheet - All Fund Types, Account Groups and Discretely Presented Component Units	3
Combined Statement of Revenues, Expenditures and Changes in Fund Balances - All Governmental Fund Types and Expendable Trust Funds	5
Combined Statement of Revenues and Expenditures - Budget and Actual - Budget Basis - General and Debt Service Funds	6
Combined Statement of Revenues, Expenses and Changes in Retained Earnings (Deficit)/Fund Balances - Proprietary Fund Type, and Similar Discretely Presented Component Units	7
Combined Statement of Cash Flows - Proprietary Fund Type and Similar Discretely Presented Component Units	8
Combined Statement of Changes in Plan Net Assets Available for Pension Benefits - Pension Trust Fund Types and Similar Discretely Presented Component Units	11
Combined Statement of Changes in Fund Balances - Public University Funds - University of Puerto Rico	12
Combined Statement of Current Funds Revenues, Expenditures and Other Changes - Public University Funds - University of Puerto Rico	13
Combined Statement of Changes in Net Assets in Liquidation - Office for the Liquidation of the Accounts of Puerto Rico Urban Renewal and Housing Corporation	14
Notes to General Purpose Financial Statements	15

Combining, Individual Fund Financial Statements and Schedules	
General Fund:	
Schedule of Expenditures by Agency- Budget and Actual - Budget Basis	113
Debt Service Funds:	
Combining Balance Sheet	122
Combining Statement of Revenues, Expenditures and Changes in Fund Balances	123
Capital Projects Funds:	
Combining Balance Sheet	124
Combining Statement of Revenues, Expenditures and Changes in Fund Balance	126
Schedule of Commonwealth Capital Project Expenditures and Authorizations	128
Enterprise Funds:	
Combining Balance Sheet	129
Combining Statement of Revenues, Expenses and Changes in Retained Earnings (Deficit)	130
Combining Statement of Cash Flows	131
Trust and Agency Funds:	
Combining Balance Sheet	132
Combining Statement of Plan Net Assets Available for Pension Benefits - Pension Trust Funds	133
Combining Statement of Changes in Plan Net Assets Available for Pension Benefits - Pension Trust Funds	134
Combining Balance Sheet - Expendable Trust Funds	135
Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Expendable Trust Funds	136
Combining Balance Sheet - Agency Funds	137
Statement of Changes in Assets and Liabilities - Agency Funds	138
Public University Funds:	
Combining Balance Sheet	139
Component Units - Other:	
Combining Balance Sheet	140
Combining Statement of Revenues, Expenses and Changes in Retained Earnings (Deficit)/Fund Balance	144
Combining Statement of Cash Flows	146
General Fixed Assets Account Group:	
Schedule of General Fixed Assets - By Source	150
Schedule of General Fixed Assets - By Function and Activity	151
Combining Statement of Primary Government General Fixed Assets Account Group	153
General Long-Term Debt Account Group:	
Combining Statement of Primary Government General Long-Term Debt Account Group	154

## STATISTICAL SECTION

General Governmental Expenditures by Function All Governmental Fund Types - Last Eight Fiscal Years	1
General Governmental Revenues by Source - All Governmental Fund Types - Last Eight Fiscal Years	2
Computation of the Legal Debt Margin at July 1, 1997	3
Ratio of Annual Debt Service for General Bonded Debt to Total General Expenditures - Last Eight Fiscal Years	4
Demographic Statistics - Last Ten Fiscal Years	5
Construction and Bank Deposits - Last Ten Fiscal Years	6
Miscellaneous Statistics	7
General Fund Net Revenues - For the Fiscal Years 1988-1997	8
General Fund Net Revenues - For the Fiscal Year 1997	9
Four Year Term Growth in General Fund Net Revenues	10
Income Tax Receipts - For Fiscal Year 1997	11
Gross Product - For the Last Seven Fiscal Years	12
Real Gross Product Growth - For the Last Seven Fiscal Years	13
Employment and Unemployment - For the Last Eight Fiscal Years	14
Average Employment by Sector - For the Last Eight Fiscal Years	15
Employment - For the Last Eight Fiscal Years	16
Tourism Indicators - For the Last Eight Fiscal Years	17



# **INTRODUCTORY SECTION**





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WINNER: TOTAL EXCELLENCE - GOVERNOR'S AWARD FOR QUALITY IN THE PUBLIC SECTOR 1995-1996

Xenia Vélez Silva  
Secretary

December 24, 1997

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 of the Commonwealth of Puerto Rico for the fiscal year ended June 30, 1997. The Puerto Rico Treasury Department has prepared the report. The responsibility for both the accuracy of presented data and the completeness and fairness of presentation, including all of the disclosures, rests on the Commonwealth's management. To the best of our knowledge and belief, the enclosed 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 various funds, account groups and component units of the Commonwealth. We have included all the necessary disclosures to enable the reader to gain a thorough understanding of the Commonwealth's activities.

The Comprehensive Annual Financial Report is presented in three sections: Introductory, Financial and Statistical. 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, the Commonwealth's organization chart, and a reproduction of the Certificate of Achievement for Excellence in Financial Reporting that the Commonwealth received for its fiscal year 1996 report. The Financial section includes the general purpose financial statements, the combining and individual fund and account group financial statements and schedules, as well as the independent auditors' report on the general-purpose financial statements. The Statistical section, which is not audited, includes selected financial and demographic information, generally presented on a multi-year basis.

The financial reporting entity includes all funds and account groups of the Commonwealth of Puerto Rico, which is the primary government, as well as of all its 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 general purpose 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 are reported in separate columns in the combined financial statements to emphasize that they are not part of the primary government and to differentiate their financial position, results of operations and cash flows 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 general purpose financial statements included in the financial section of this Comprehensive Annual Financial Report provide descriptions of the operations of each of the following component units of the Commonwealth:

#### Blended Component Units

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

#### Discretely Presented Component Units

- University of Puerto Rico
- University of Puerto Rico Retirement System
- Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation
- Government Development Bank for Puerto Rico and Subsidiaries
- Puerto Rico Electric Power Authority
- Puerto Rico Aqueduct and Sewer Authority
- Puerto Rico Telephone Authority and Subsidiary, and Puerto Rico Telephone Company
- Puerto Rico Government Investment Trust Fund
- Puerto Rico Housing Bank and Finance Agency
- State Insurance Fund Corporation
- Economic Development Bank for Puerto Rico
- Puerto Rico Industrial Development Company
- Puerto Rico Ports Authority
- Puerto Rico Municipal Financial Agency
- Puerto Rico Infrastructure Financing Authority
- Sugar Corporation of Puerto Rico
- Puerto Rico School of Plastic Arts
- Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority
- Caribbean Basin Projects Financing Authority
- Automobile Accident Compensation Administration
- Puerto Rico Metropolitan Bus Authority
- Puerto Rico Public Broadcasting Corporation
- Puerto Rico Solid Waste Authority
- Tourism Company of Puerto Rico





- Employment and Training Enterprises Corporation and Subsidiary
- Industries for the Blind, Mentally Retarded and Other Disabled Persons of Puerto Rico
- Institutional Trust of the National Guard of Puerto Rico
- Musical Arts Corporation and Subsidiaries
- Puerto Rico Conservatory of Music Corporation
- Corporation of Stocks and Deposits Insurance for the Savings and Loans Cooperatives
- Puerto Rico Land Administration
- Puerto Rico Health Insurance Administration
- Land Authority of Puerto Rico
- Fine Arts Center Corporation
- Right to Employment Administration
- Farm Insurance Corporation of Puerto Rico
- Puerto Rico Medical Services Administration
- Puerto Rico and Caribbean Cardiovascular Center Corporation
- Commercial and Farm Credit and Development Corporation for Puerto Rico
- Recreational Development Company of Puerto Rico
- Farm Credit Guarantee Fund and Guarantee Loan Fund for Eligible Businesses of Puerto Rico
- Agricultural Services and Development Administration
- Trust for the Development, Operation and Conservation of National Parks of Puerto Rico

### **Local Economic Condition and Outlook**

The Government of Puerto Rico has established policies and programs directed at developing the manufacturing and service sectors of the economy (with emphasis on the tourism industry) and expanding and modernizing the Island's infrastructure. Selective tax exemption, development loans, and other financial and tax incentives have stimulated domestic and foreign investment. Infrastructure expansion and modernization have been to a large extent financed by bonds and notes issued by the Commonwealth, its public corporations and municipalities. Economic progress has been aided by significant increases in the levels of education and occupational skills of the Island's population.

The dominant sectors of the Puerto Rico economy are manufacturing and services. The manufacturing sector has experienced a fundamental change over the years as a result of increased emphasis on higher-wage and high technology industries, such as pharmaceuticals, electronics, computers, microprocessors, professional and scientific instruments, and certain high technology machinery and equipment. The services sector, including finance, insurance, real estate, wholesale and retail trade, and hotel and related services, also plays a major role in the economy. It ranks second only to manufacturing in contribution to the gross domestic product and leads all sectors in providing employment. In recent years, the services sector has experienced significant growth in response to the expansion of the manufacturing sector.

The economy of Puerto Rico is fully integrated with that of the United States mainland. During fiscal 1996, approximately 88% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 62% of Puerto Rico's imports. In fiscal 1996, Puerto Rico experienced a \$3.2 billion positive adjusted merchandise trade balance.



Gross product in fiscal 1993 was \$25.1 billion; gross product in fiscal 1997 was \$32.3 billion. This represents an increase of 27.5% from fiscal 1993 to 1997. Since fiscal 1985, personal income, both aggregate and per capita, has increased consistently each fiscal year. In fiscal 1996, aggregate personal income was \$29.4 billion and personal income per capita was \$7,882.

Average employment increased from 999,000 in fiscal 1993 to 1,128,300 in fiscal 1997. Average unemployment decreased from 16.8% in fiscal 1993 to 13.1% in fiscal 1997. According to the Labor Department's Household Employment Survey, during fiscal 1997, total employment increased 3.3% over fiscal 1996. Total employment averaged 1,128,300 in fiscal 1997, compared to 1,092,300 in fiscal 1996.

The Planning Board uses a composite index of thirteen economic indicators, known as the Economic Activity Index (the "Index"), as an indicator of short-term economic activity. These thirteen indicators consist of: total employment, manufacturing employment, manufacturing payroll, electric energy consumption, external trade, tourist hotel registrations, retail sales, excise taxes, electric energy production, new housing unit permits, hours worked, cement production, and new motor vehicle registrations.

The Index does not necessarily change at the same percentage rate as the gross product of Puerto Rico. In fact, notwithstanding the expected growth in gross product for fiscal year 1997, the Index decreased 0.2% for fiscal 1997 compared to fiscal 1996. One of the factors that may explain this discrepancy between the projected growth in gross product and the Index is the negative impact of Hurricane Hortense, which struck the Island on September 9, 1996. The week of the hurricane coincided with the week in which the Department of Labor collects the information for the payroll survey. This survey provides information on three variables that are part of the Index: manufacturing employment, manufacturing payroll and manufacturing weekly hours worked. As a result of the hurricane, there was a sharp decline in these components and this decline has affected the Index for the entire year.

### **Sections 30A and 936 of the Internal Revenue Code**

For many years, United States companies operating in Puerto Rico enjoyed a special tax credit that was available under Section 936 of the 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 two alternative methods for calculating the tax credit and limited the amount of the credit that a qualifying company can claim. These limitations are based on a percentage of qualifying income (the "percentage of income limitation") and on qualifying expenditures for wages, other wage related benefits and other qualifying costs and expenses (the "economic activity limitation", also known as the "wage credit limitation").

As a result of amendments incorporated in the Small Business Job Protection Act of 1996, enacted by the United States Congress and signed into law by President Clinton on August 20, 1996 (the "1996 Amendments"), the tax credit is now being phased out over a ten-year period for existing 936 credit claimants and is no longer available for corporations that establish operations in Puerto Rico after October 13, 1995 (including existing Section 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.

During 1997, the Governor proposed to Congress the enactment of a new permanent federal incentive program similar to what is now provided under Section 30A. Such program would provide U.S. companies a tax credit based on qualifying wages paid and other wage related expenses, such as fringe benefits, as well as depreciation expenses for certain tangible assets and research and development expenses. Under the Governor's proposal, the credit granted to qualifying companies would continue in effect until Puerto Rico shows, among other things, substantial economic improvements in terms of certain economic parameters. The fiscal 1998 federal budget submitted by President Clinton to Congress in February 1997, included a proposal to modify Section 30A to extend the availability of the Section 30A credit indefinitely, make it available to companies establishing operations in Puerto Rico after October 13, 1995, and eliminate the income cap. However, President Clinton's proposal was not included in the fiscal 1998 federal budget. While the Government of Puerto Rico intends to continue lobbying for this proposal, it is not possible at this time to predict whether the Section 30A credit will be modified, nor to determine the long term effect on the Puerto Rico economy of the enactment of the 1996 Amendments. The Commonwealth of Puerto Rico does not believe there will be short-term or medium-term material adverse effects on Puerto Rico's economy as a result of the enactment of the 1996 Amendments. The Commonwealth of Puerto Rico further believes that the phase-out period allows sufficient time to implement additional incentive programs to safeguard Puerto Rico's competitive position.

## **Major Initiatives**

### *Income Tax Reform*

On October 31, 1994, the Commonwealth enacted Law No. 120, **Puerto Rico Internal Revenue Code of 1994** (the Code), which was amended in July 1997. Its main purpose was to compile in a single volume all laws and regulations governing the Commonwealth's internal revenues and to establish a more equitable tax structure that lowered tax rates and simplified and enhanced compliance. As part of this initiative, the Commonwealth approved the **Income Tax Reform of 1994**, included as Subtitle A of the Code, which substantially revised the Puerto Rico income tax laws. The Income Tax Reform of 1994 resulted in income tax relief to taxpayers of approximately \$400 for fiscal year 1996.

The Tax Reform is a vehicle to promote economic growth and regain the confidence of taxpayers, since it contains a series of measures to (1) provide tax relief to honest taxpayers, and tax incentives to work and invest, (2) simplify tax provisions and reduce compliance costs to taxpayers, (3) provide an alternative to eliminate double taxation with respect to earnings of local corporations, and (4) provide the Puerto Rico Treasury Department with new instruments to increase its efficiency and fight against tax evasion. The Tax Reform of 1994 returned \$400 million to taxpayers. Even with such massive tax relief, fiscal revenues increased by \$168 million, which is evidence of the increased taxpayer confidence, as well as of the success of the Puerto Rico Treasury Department's commitment to control tax evasion. From 1994 through 1997, fiscal revenues grew by \$1,575 million, for a 39 percent increase when compared to the previous four year period. The increase is three times larger than the increase in the previous four-year period, 1990 through 1993, when revenues grew by only \$461 million.



In July 1997, the Puerto Rico Code was amended to include certain provisions designed to promote investments in local capital market instruments.

The Puerto Rico Treasury Department has designed and implemented certain administrative programs, such as the Administrative Reform, that have transformed the organizational structure of the Department. This has entailed changing the management and reporting concept from bureaus that manage particular laws to bureaus that manage similar functional activities, as well as reorganizing the Island in five regions, and transferring the management of local collectors' offices to such regions. This Reform has had excellent results, reducing estimated individual tax evasion from 26 to 21 percent.

The Puerto Rico Treasury Department is in the process of installing the Puerto Rico Integrated Tax Administration System (PRITAS). This is a new computerized system which integrates the administration of Puerto Rico's tax base. It will improve taxpayer compliance and will increase productivity and efficiency, resulting in increased tax collections. Conversion to the new system has been completed for corporate income taxes, employer withholding taxes, excise taxes and internal revenue licenses.

#### *Improvements to Payroll and Accounting System*

The Puerto Rico Treasury Department is in the process of implementing two additional new systems:

##### *Human Resources and Payroll System*

This is a client server system that integrates and mechanizes the human resources and payroll functions. With the implementation of this system, the Puerto Rico Treasury Department will improve the processes and decentralize the functions of data entry and validation of information at the agencies. This system is year 2000 compliant.

##### *Puerto Rico Integrated Financial Accounting System (P.R.I.F.A.S)*

PRIFAS is a new integrated financial accounting system that will replace the current accounting system. It is a client server system; the modules being implemented include: General Ledger, Budget Checking, Federal Grants, Accounts Payable, Accounts Receivable, Purchasing and the Assets Management functions.

PRIFAS will be implemented in all the agencies of the Primary Government of Puerto Rico by the year 2000. In addition to the implementation of PRIFAS, the Puerto Rico Treasury Department is reengineering its existing processes and upgrading its technical infrastructure to support the new systems.

#### *Public Sector Debt*

Historically, Puerto Rico has maintained a fiscal policy which provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. The Commonwealth of Puerto Rico has also sought opportunities to realize debt



service savings by refunding outstanding debt with obligations bearing lower interest rates.

During the period from fiscal 1992 to 1996, public sector debt and gross product increased 27.5% and 27.7%, respectively. During the period from fiscal 1993 to 1997, however, public sector debt increased 37.0% while gross product increased 27.7%. This higher level of growth of public sector debt over the growth of gross product is due to increases in the amount of debt incurred during fiscal years 1996 and 1997 to finance certain key infrastructure projects. These projects are important to the development of the economy and are expected to produce long term economic benefits. This trend of higher levels of public sector debt relative to the growth in gross product is expected to continue during the next few fiscal years as the level of public sector capital investment remains high.

As of June 30, 1997, outstanding short-term debt, relative to total debt, was 8.4%, excluding \$550 million of tax and revenue anticipation notes of the Commonwealth issued on December 17, 1996 and paid on July 30, 1997.

### *Health Reform Program*

One of the goals of the Governor is to change Puerto Rico's public health care system from one in which the government provides free health services to low income individuals through public health facilities owned and administered by the government, to one in which all medical services are provided by the private sector and the government provides comprehensive health insurance coverage for qualifying (generally low income) Puerto Rico residents. Under this new system, the Government selects, through a bidding system, one private health insurance company in each of several designated regions of the Island and pays such insurance company the insurance premium for each eligible beneficiary within such region. This new health insurance system is now available in 61 municipalities out of a total of 78 on the Island. It is expected that 11 municipalities will be added by the end of fiscal 1998 and 5 more by the end of fiscal 1999. The total cost of this program will depend on the number of municipalities included in the program, the number of participants receiving coverage, and the date coverage commences. As of June 30, 1997, over 1,090,592 persons were participating in the program at an estimated annual cost to the General Fund of Puerto Rico for fiscal 1997 of approximately \$521 million. In conjunction with this program, the operation of certain public health facilities has been transferred to private entities.

The Government's current privatization plan for health facilities provides for the transfer of ownership of all health facilities to private entities. The Government has announced that it has selected various private companies with which it is commencing negotiations expected to culminate in the sale of ten health facilities.

Other highlights of fiscal year 1997 are:

- On September 5, 1996, the Governor signed Law No. 189 authorizing the Government of the Commonwealth of Puerto Rico to negotiate the transfer, for the nominal value of one dollar, of most of the assets and the operations of the Sugar Corporation to a group of private entities created and owned by the sugar cane growers. Negotiations with the growers is still in progress.
- The Government has also sold two hotel properties formerly owned by a subsidiary of the



Tourism Company of Puerto Rico (The Hostal El Convento and the Mayagüez Hilton), and is currently negotiating the sale to a Florida-based corporation of a complex consisting of two hotels and a convention center.

- On April 7, 1997, the Governor announced the Government's intention to sell the Puerto Rico Telephone Company ("PRTC"), a subsidiary of the Telephone Authority. Legislation authorizing the Government to negotiate the sale of PRTC has been approved and the Government is currently conducting the sale processes.
- The Corrections Administration has entered into operating agreements with two private companies whereby three new correctional facilities (Ponce and Guayama Correctional Facilities and Bayamón Institutional Facility for Youthful Offenders) are being operated by these companies. The private companies have experience in the area of privatized correction services in the United States mainland.
- The Employees Retirement System of the Government of Puerto Rico and its Instrumentalities is designing and implementing an investment strategy that will increase returns and ultimately should reduce the System's unfunded pension liability. This strategy involves two phases, namely, the transfer of ownership of certain government assets that have the potential to generate adequate returns to the pension plans, and the prospective conversion of the government's pension program from a defined benefit plan into a privately managed defined contribution program
- The Government has implemented an educational reform that seeks to give Puerto Rico access to the best available tools for learning. As part of this reform, the Government established the Community-Based School Program, following the principle that education is everyone's commitment. As of June 30, 1997, more than 1,000 public schools had been converted into community-based schools. Also, a voucher program was developed to give the families a free choice of schools. This allows parents to select schools that offer the best educational opportunities for their children, improving the quality of education. As of June 30, 1997, 26,041 students had benefited from these vouchers.

### *Prospects for the Future*

The Governor has developed and is implementing a new economic development program, based on the premise that the private sector should provide the primary impetus for economic development and growth. This new program, referred to as the New Economic Model, promotes changing the role of the government from one of provider of most basic services, to that of facilitator for private sector initiatives, and encourages private sector investment by reducing government-imposed regulatory constraints. The New Economic Model contemplates the development of initiatives that will foster private investment and private management of sectors that are served more efficiently and effectively by private enterprise. One of the initiatives that already has been implemented is the adoption of a new tax code intended to expand the tax base, reduce the personal and corporate marginal tax rates and simplify the tax system, as mentioned before.

Another initiative consists of improving and expanding Puerto Rico's infrastructure to facilitate private sector development and growth, such as the construction of a modern light rail system for



the San Juan metropolitan area that will connect five densely populated sectors of the metropolitan area. This project is a \$1.2 billion venture and has been recognized by the Federal Transit Administration as one of the most cost effective mass transit projects in the United States. Another example of initiatives to improve and expand Puerto Rico's infrastructure is the construction of a major water pipeline at a cost of \$305 million, the North Coast Superaqueduct, that will supply water to fifteen municipalities along the north coast of the Island. These municipalities are Arecibo, Barceloneta, Manatí, Vega Baja, Vega Alta, Dorado, Toa Alta, Toa Baja, Bayamón, Cataño, Guaynabo, San Juan, Carolina, Trujillo Alto and Caguas. These two projects will have significant social and economic impacts, including the creation of nearly 47,893 direct, indirect and induced jobs.

Also, this Model seeks to identify and promote those areas in which Puerto Rico can compete more effectively in the global markets. In this regard, tourism has been targeted as a priority because of its potential for job creation and increased contribution to the gross product, stemming from Puerto Rico's natural competitive advantage. As part of the initiatives directed at promoting the tourism sector, in 1993 a new Tourism Incentives Act was enacted to provide special tax incentives for the development of new hotel projects. Also, in November 1993, the Tourism Development Fund was created for the purpose of promoting capital investments in and providing financing to entities that contribute to the development of the tourism industry. As a result of these initiatives, several new hotels have been constructed or are in the process of being constructed, increasing the number of total rooms on the Island from 8,415 at the end of fiscal 1992 to 10,877 at the end of fiscal 1997 and to a projected 11,972 by the end of fiscal 1998. Similar tax incentives have been enacted in other areas targeted by the New Economic Model as areas of opportunity for the promotion of local and foreign investment in Puerto Rico, such as agriculture, solid waste management and venture capital.

The New Economic Model is designed to help reduce the size of the government's direct contribution to gross domestic product. As part of this goal, the Government has transferred certain governmental operations and sold a number of its assets to private parties:

- On March 3, 1995, the Government completed the sale of the assets of the Maritime Shipping Authority to a private purchaser.
- On May 26, 1995, the Aqueduct and Sewer Authority executed a five-year agreement pursuant to which the management, operation, repairs and maintenance of the Authority's water and waste water treatment systems is being provided by a private company. The agreement requires that the private company generate efficiencies and savings in such operations, while improving this vital service.
- On January 31, 1996, the Aqueduct and Sewer Authority executed a construction and operating agreement with a private consortium for the design, construction, and operation of an approximately 75 million gallon per day pipeline to deliver water from the Dos Bocas reservoir in Utuado to the San Juan metropolitan area.



## **Financial Information**

The management of the Commonwealth is responsible for establishing and maintaining an internal control structure that ensures that the 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 generally accepted accounting principles. The internal control structure is 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 an adequate internal control structure is 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 Single Audit Act of 1984, as amended. As a result, these 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.

## **Budgetary Controls**

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

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 and the debt service funds are included in the annual appropriated budget. Budgetary control resides at the departmental 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 revenues 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 his judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the Planning Board.





The Legislature may amend the budget submitted by the Governor, but may not increase any 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 any new item 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, the annual budget for the preceding fiscal year as originally 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 to pay its operating and other expenses until a new budget is approved.

### General Government Functions

General governmental activities are accounted for in three governmental fund types. These funds are: general, debt service and capital project.

As a result of the initiatives implemented by the Government, such as the approval of the Tax Reform, the Administrative Reform in the Puerto Rico Treasury Department, the aggressive identification of old debts and tax evaders, and the expansion of the taxpayer base, income tax revenues increased to \$3.623 billion in fiscal 1997, from \$3.397 in fiscal 1996, or 6.65%. The Commonwealth also experienced increases in revenues from excise taxes from \$1.523 in fiscal 1996 to \$1.633 billion in fiscal 1997, or 7.22%, as a result of overall economic growth.

Other increases in revenues are attributable to intergovernmental revenues, mainly composed of federal financial assistance programs. These revenues increased to \$2.930 billion in fiscal 1997 from \$2.379 in fiscal 1996, or 23.16%, showing an increase in the level of federal spending in Puerto Rico.

### Enterprise Operations

Comparative data for the Enterprise Funds for the past two fiscal years (expressed in thousands) follows:

	June 30, 1997	June 30, 1996	Increase (Decrease)
Operating Revenues	\$ 879,664	\$ 899,002	\$ (19,338)
Operating Expenditures	<u>1,260,876</u>	<u>1,362,567</u>	<u>(101,691)</u>
	<u>\$(381,212)</u>	<u>\$(463,565)</u>	<u>\$ (82,353)</u>

The Enterprise Funds realized a net loss of approximately \$381 million in 1997. The net loss for the fiscal year ended June 30, 1996 was approximately \$464 million. The overall decrease in operating losses of \$82 million can be attributed to a decrease in the operating expenses of the Health Facilities and Services Administration of Puerto Rico of \$109 million, net of a decrease in its operating revenues of approximately \$14 million. In addition, the operating revenues of the



Additional Lottery System decreased by \$11 million in fiscal year 1997.

### **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, other governmental units or other funds. These include the expendable trust, pension trust and agency funds. 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 Trust funds include the 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, Unemployment Trust Fund and the Health Facilities and Services Administration of Puerto Rico Trust Fund.

Agency Funds include 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 Insurance Commissioner for escheated property and for insurance companies under bankruptcy.

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

The principal functions of the Government Development Bank for Puerto Rico (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 Comprehensive Annual Financial Report. They have received the award for the years ended June 30, 1994, 1995 and 1996. The Government Development Bank for Puerto Rico and Subsidiaries is presented as a discrete component unit.

### **Debt Administration**

As of June 30, 1997, the Commonwealth had a number of debt issues outstanding. These issues included approximately \$4.4 billion in general obligation bonds and approximately \$4.3 billion in revenue bonds. 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, and we expect that these classifications will be maintained or improved in future years.

The Constitution of the Commonwealth limits the amount of debt service that can be incurred with respect to issued or guaranteed debt to 15% of internal revenues, as therein defined. As of June 30, 1997, the Commonwealth is in compliance with the debt limitation requirement. See the Computation of the Legal Debt Margin, Page No. 3 in the Statistical Section.

Revenue bonds include outstanding bonds issued by two blended component units: the Puerto Rico Highway and Transportation Authority (PRHTA) and the Public Buildings Authority (PBA). PRHTA's bonds are issued to finance the construction of certain infrastructure facilities; \$2.4 billion were outstanding as of June 30, 1997. PBA had \$1.9 billion of revenue bonds outstanding at June 30, 1997.



## **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 Workers' Compensation, the Commonwealth's presented component unit, the State Insurance Fund Corporation, provides workers' compensation to both public and private employees.

## **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 GDB, a discretely presented component unit. In addition, the Puerto Rico Government Investment Trust Fund (Trust Fund), was created by the Commonwealth pursuant to Act No. 176, of August 11, 1995, and began operations on December 4, 1995.

The Trust Fund is a no-load diversified collective investment trust that was created for the purpose of providing eligible investors (mainly component units and the municipalities of Puerto Rico) 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 US 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. The Statement of Investment Guidelines for the Government of Puerto Rico was approved by the GDB on February 22, 1996.

## **Other Information**

### *Independent Audit*

Commonwealth statutes require an annual audit by independent certified public accountants. The firm of Deloitte & Touche LLP was selected by the Commonwealth to perform the audit of the general purpose financial statements in accordance with generally accepted auditing standards for the fiscal years 1996-97 through 1999-2000. The independent auditors' report on the general purpose financial statements is included in the financial section of this report.

### *Improvements in Financial Reporting*

The Commonwealth has significantly improved its financial reporting practices and policies during the past five years. The general purpose financial statements, which used to take thirteen months to be released with several qualifications, are now prepared within six months after the close of the fiscal year. For fiscal year 1995-1996, the general purpose financial statements were issued on December 31, 1996 with an unqualified opinion in the Independent Auditors' Report.



## Awards

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 of Puerto Rico for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 1996. 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 comprehensive annual financial report, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

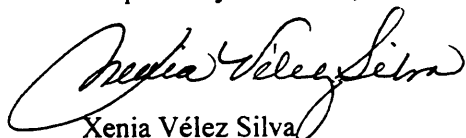
A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to the GFOA.

## Acknowledgments

The preparation of this report could not have been accomplished without the efficient and dedicated efforts of Manuel Díaz Saldaña, previous Secretary of the Puerto Rico Treasury Department, Juan Alvarado Zayas, Undersecretary, Haydeé Ortiz Ramos and Regina Miranda Palacio from our accounting staff, as well as the rest of the personnel of the central government accounting division. In addition, the executive and finance directors of the component units and agencies provided support and information on a timely basis for the completion of the general purpose financial statements and the sections of this report; their efforts are most appreciated. Due credit should also be given to the Honorable Pedro Rosselló for his continuous support to better and improved fiscal and administrative policies, to the President and staff of the Government Development Bank for Puerto Rico, and to the Director and staff of the Office of Management and Budget of Puerto Rico. We would like to give special thanks to our independent auditors, Deloitte & Touche LLP, specially to Gilberto Del Valle, Pat Hardiman, Luis Rivera, and Ivelisse Céspedes for their excellent advice and unwavering commitment.

And remember, **Hacienda...is at your service.**

Respectfully submitted,



Xenia Vélez Silva  
Secretary of Treasury



# GENERAL INFORMATION ABOUT PUERTO RICO

## Geography and Population

Puerto Rico, the fourth largest of the Caribbean islands, is located approximately 1,600 miles southeast of New York City. It is approximately 100 miles long and 35 miles wide.

According to the United States Census Bureau, the population of Puerto Rico was approximately 3,522,000 in 1990, compared to 3,196,520 in 1980. According to estimates of the Planning Board, the population of Puerto Rico increased to 3,805,915 in fiscal 1997. As of 1990, the population of San Juan, the island's capital and largest city, was approximately 437,000.

## History and Relationship with the United States

Columbus discovered Puerto Rico in 1493, and shortly thereafter the Island was conquered and settled by the Spaniards. It remained a Spanish possession for four centuries.

Puerto Rico came under United States sovereignty pursuant to the Treaty of Paris, signed on December 10, 1898, which ended the Spanish-American War. Puerto Ricans became citizens of the United States in 1917, with the approval of the Jones Act by the United States Congress. In 1950, after a long evolution toward greater self-government, Congress enacted Public Law 600 which provided that the existing political, economic and fiscal relationship between Puerto Rico and the United States would remain the same, but Puerto Rico would be authorized to draft and approve its own constitution, guaranteeing a republican form of government. The Constitution was drafted by a popularly elected constitutional convention, approved in a special referendum by the people of Puerto Rico, amended and ratified by the United States Congress, and subsequently approved by the President of the United States. Puerto Rico's constitutional status is that of a territory of the United States, and pursuant to the territorial clause of the Federal Constitution, the ultimate source of power over Puerto Rico is the United States Congress. The relationship between the United States and Puerto Rico is referred to herein as *Commonwealth* status.

Puerto Rico exercises virtually the same control over its internal affairs as do the fifty states; however, it differs from the states in its relationship with the federal government. The people of Puerto Rico are citizens of the United States but do not vote in national elections. They are represented in Congress by a Resident Commissioner who has a voice in the House of Representatives and limited voting power. Most federal taxes, except Social Security and other similar taxes, are not levied in Puerto Rico. No federal income tax is collected from Puerto Rico residents on income earned in Puerto Rico, except for certain federal employees who are subject to taxes on their salaries. Income earned by Puerto Rico residents from sources outside of Puerto Rico, however, is subject to federal income tax. Federal excise taxes on shipments of alcoholic beverages from Puerto Rico (which are \$11.30 per gallon through October 1, 1998 and \$10.50 per gallon thereafter) and other taxes on shipments of tobacco products from Puerto Rico to the mainland are returned to the Puerto Rico Treasury Department.

On February 26, 1997, legislation was introduced in the U.S. House of Representatives (the "Political Status Act") proposing a mechanism to settle permanently the political relationship between Puerto Rico and the United States, either through full self-government (e.g., statehood or independence, including, as an alternative, free association via a bilateral treaty) or continued Commonwealth status. Under the proposed legislation, failure to settle on full self-government

after completion of the referenda process therein would result in retention of the current Commonwealth status. On March 19, 1997, similar legislation was introduced in the U.S. Senate. The House Resources Committee held hearings and voted in favor of the Political Status Act. The Political Status Act must be voted on by the House Rules Committee before reaching the House floor. It is not possible at this time to predict when the Political Status Act will be voted on by the full House of Representatives, what course the legislation will follow in the Senate, and whether it will be subsequently enacted into law.

The official languages of Puerto Rico are Spanish and English. Although the culture of Puerto Rico is primarily Hispanic, a considerable intermingling of Hispanic and United States cultures have occurred.

### Governmental Structure

The Constitution of the Commonwealth of Puerto Rico provides for the separation of powers of the executive, legislative and judicial branches of government. The Governor is elected every four years. The Legislature consists of a Senate and a House of Representatives, the members of which are elected for four-year terms. The highest court within the local jurisdiction is the Supreme Court of Puerto Rico. Decisions of the Supreme Court of Puerto Rico may be appealed to the Supreme Court of the United States under the same terms and conditions as decisions from state courts. Puerto Rico constitutes a District in the Federal Judiciary System and has its own United States District Court. Decisions of this court may be appealed to the United States Court of Appeals for the First Circuit and from there to the Supreme Court of the United States.

Pedro Rosselló was sworn in as Governor of Puerto Rico on January 2, 1993. He was re-elected for a second four-year term in the November 1996 elections. He obtained a medical degree from Yale University in 1970, after completing his undergraduate studies at Notre Dame University in 1966. He made his specialization in General and Pediatric Surgery at Harvard University. In 1985, he was appointed Director of San Juan's Health Department, a position which he held for three years.

Xenia Vélez Silva was recently appointed by the Governor as Secretary of the Treasury and took office on November 20, 1997. She is a lawyer and certified public accountant. She is a graduate of the University of Puerto Rico, where she obtained a bachelor's degree in Business Administration as well as a Juris Doctor degree.

### Political Trends

For many years, there have been two major views in Puerto Rico with respect to the Island's relationship to the United States: one favoring statehood, represented by the New Progressive Party, and the other favoring the existing Commonwealth status, represented by the Popular Democratic Party. The following table shows the percentages of the total votes received by the gubernatorial candidates of the various parties in the last five elections by voter preference with respect to statehood, Commonwealth status and independence. While the electoral choices of Puerto Rico's voters are not based solely on preferences regarding the Island's relationship with the United States, candidates who support a continuing relationship between Puerto Rico and the United States have prevailed in elections for many years.

	<u>1980</u>	<u>1984</u>	<u>1988</u>	<u>1992</u>	<u>1996</u>
New Progressive Party	47.3%	45.5%	45.8%	49.9%	51.1%
Popular Democratic Party	47.0	48.5	48.7	45.9	44.5
Puerto Rico Independence Party	5.4	3.9	5.4	4.2	3.8
Others	0.3	2.1	0.1	-	0.6

After the 1996 elections, control of the executive and legislative branches continued under the New Progressive Party. The composition of the Senate and House of Representatives, by the several political parties, is as follows:

	<u>Senate</u>	<u>House</u>
New Progressive Party	19	37
Popular Democratic Party	8	16
Puerto Rico Independence Party	<u>1</u>	<u>1</u>
	<u>28</u>	<u>54</u>

The next general election (gubernatorial, municipal, and legislative) in Puerto Rico will be held in November 2000. Voter participation in Puerto Rico is substantially higher than in the United States, averaging 85% since 1972.





# COMMONWEALTH OF PUERTO RICO

## PRINCIPAL OFFICIALS

**Pedro J. Rosselló**  
*Governor*

### *Members of the Cabinet*

**Angel Morey**  
Chief of Staff

**Norma E. Burgos Andújar**  
Secretary of State

**José Fuentes Agostini**  
Secretary of Justice

**Xenia Vélez Silva**  
Secretary of the Treasury

**Víctor Fajardo**  
Secretary of Education

**César Almodóvar Marchany**  
Secretary of Labor and Human  
Resources

**Carmen Feliciano de Melecio**  
Secretary of Health

**Miguel A. Muñoz Muñoz**  
Secretary of Agriculture

**Carlos I. Pesquera Morales**  
Secretary of Transportation and  
Public Works

**Carlos Vivoni Nazario**  
Secretary of Economic  
Development and Commerce

**Carmen L. Rodríguez**  
Secretary of Family Affairs

**Ana Carmen Alemañy**  
Secretary of Housing

**Daniel Pagán Rosa**  
Secretary of Natural and  
Environmental Resources

**José A. Alicea**  
Secretary of Consumer Affairs

**Eric R. Labrador Rosa**  
Secretary of Sports and Recreation

**Nydia Cotto Vives**  
Secretary of Correction  
and Rehabilitation

**Pedro Toledo**  
Commissioner of Protection  
and Public Safety

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## LEGISLATIVE OFFICERS

**Charlie Rodríguez**  
President, Senate

**Edison Mislá Aldarondo**  
Speaker, House of Representatives

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## FISCAL OFFICERS

**Jorge E. Aponte Hernández**  
Director, Office of Management and  
Budget

**Marcos Rodríguez-Ema**  
President, Government Development  
Bank for Puerto Rico

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## OTHERS

**Norma E. Burgos Andújar**  
President, Planning Board

**Xavier Romeu**  
Director, Federal Affairs Office



# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Commonwealth of Puerto Rico

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 1996

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Linda N. Savitsky*  
President

*Jeffrey L. Esler*  
Executive Director



# FINANCIAL SECTION

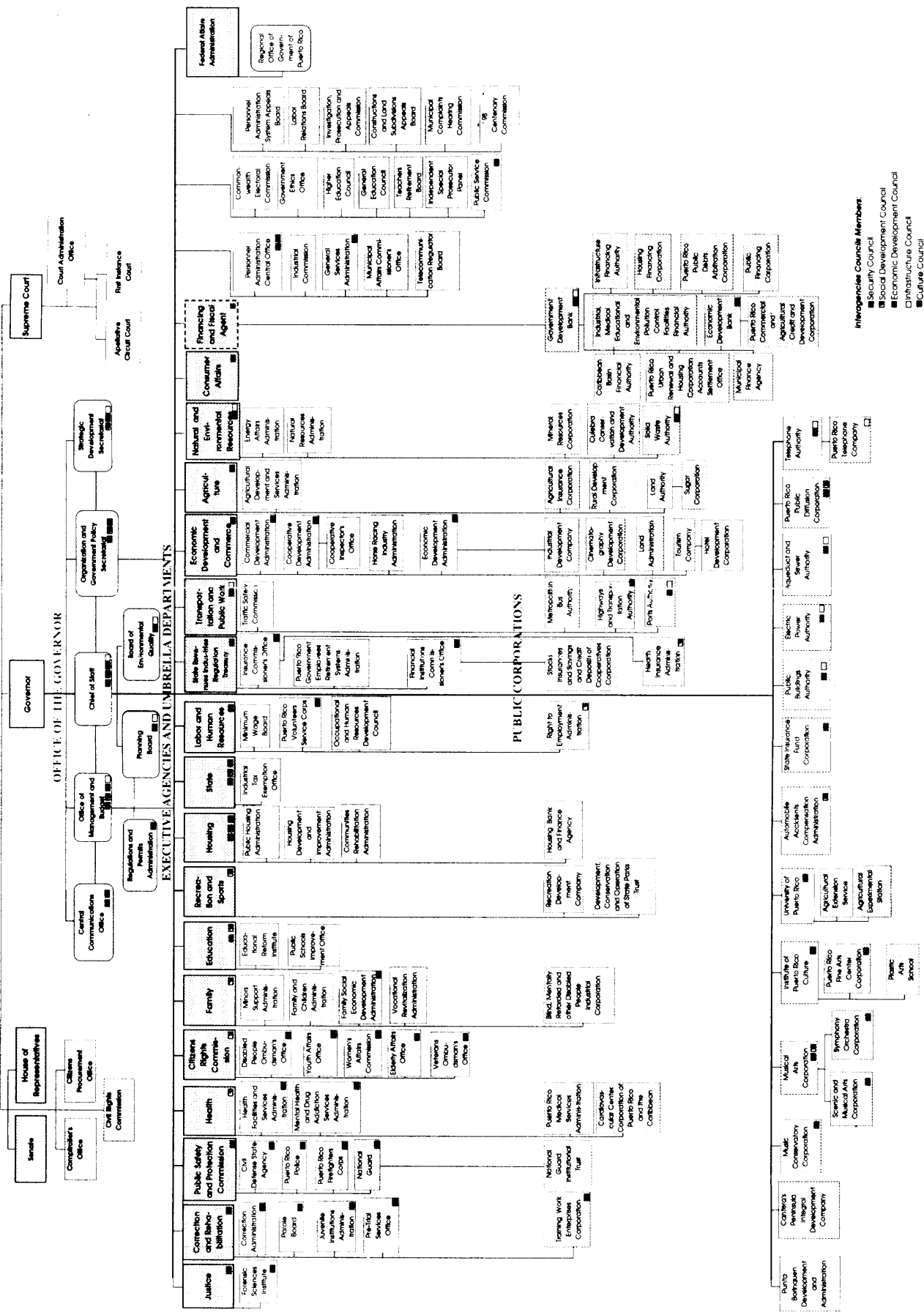


# GOVERNMENT OF PUERTO RICO ORGANIZATION OPERATION CHART



## LEGISLATIVE BRANCH

## EXECUTIVE BRANCH



- ### Interagency Council Members
- Security Council
  - Social Development Council
  - Economic Development Council
  - Infrastructure Council
  - Culture Council
- The last operation day of the Commission, by law will be at February 28, 2001.







## **INDEPENDENT AUDITORS' REPORT**

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

We have audited the accompanying general purpose financial statements of the Commonwealth of Puerto Rico (the Commonwealth) as of June 30, 1997, and for the year then ended, listed in the table of contents. These general purpose financial statements are the responsibility of the management of the Commonwealth. Our responsibility is to express an opinion on these general purpose financial statements based on our audit. We did not audit the financial statements of the Pension Trust funds, the Public University funds, the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, and the following activities and component units. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Pension Trust funds, Public University funds, the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, and the following activities and component units, is based solely on the reports of the other auditors:

- Puerto Rico Highway and Transportation Authority, a blended component unit, which represents the following indicated percentages of total assets and total revenues, respectively, of the debt service funds (43% and 52%), the capital projects funds (9% and 71%), the enterprise funds (20% and 1%); total assets of the general fixed assets account group (2%); and of total liabilities of the long-term debt account group (18%).
- Health Facilities and Services Administration of Puerto Rico, an enterprise fund, which represents 53% and 23%, respectively, of total assets and total revenues of the enterprise funds.
- The Additional Lottery System, an enterprise fund, which represents 21% and 24%, respectively, of total assets and total revenues of the enterprise funds.
- Entities identified in Note 2, that are presented as component units-other, which represent 44% and 52%, respectively, of the total assets and total revenues of the component units-other column.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose 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 reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and on the reports of the other auditors, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the Commonwealth of Puerto Rico as of June 30, 1997, and the results of its operations and the cash flows of its proprietary fund types, similar trust funds and discretely presented component units-other for the year then ended in conformity with generally accepted accounting principles.

As discussed in Note 19 certain accounting and financial reporting changes were made effective July 1, 1996:

- The Commonwealth changed its financial reporting policies to present the Office for the Improvement of Public Schools as a capital project fund
- The Commonwealth and certain component units made other accounting and financial reporting changes

Accordingly, beginning fund balances/retained earnings of the funds and component units-other have been restated.

Our audit was conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The combining and individual fund financial statements and schedules listed in the table of contents, are presented for the purpose of additional analysis and are not a required part of the general purpose financial statements of the Commonwealth. These financial statements and schedules are also the responsibility of the management of the Commonwealth. Such additional information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, based on our audit and the reports of other auditors referred to in the first paragraph, are fairly stated in all material respects when considered in relation to the general purpose financial statements taken as a whole.

The introductory and statistical sections of this report listed in the table of contents are presented for purposes of additional analysis and are not a required part of the general purpose financial statements of the Commonwealth. Such additional information has not been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, accordingly, we express no opinion on it.

*Deloitte & Touche LLP*

December 15, 1997

Stamp No. 1467140  
affixed to original.

**COMMONWEALTH OF PUERTO RICO**

**COMBINED BALANCE SHEET - ALL FUND TYPES, ACCOUNT GROUPS AND DISCRETELY PRESENTED COMPONENT UNITS  
JUNE 30, 1997 (Expressed in Thousands)**

ASSETS AND OTHER DEBITS	Governmental Fund Types			Fiduciary Fund Types	Account Groups		Totals Primary Government (Memorandum Only)	Component Units			Totals Reporting Entity (Memorandum Only)	
	Proprietary Fund Type		Trust and Agency		General Fixed Assets	General Long-Term Debt		Public University	Office for the Liquidation	Other		
	General	Debt Service										Capital Projects
<b>Assets:</b>												
Cash and cash equivalents	\$ 268,612	\$ 76,076	\$ 924,406	\$ 29,859	\$ 751,397	\$	\$ 2,050,350	\$ 63,841	\$ 1,233	\$ 262,767	\$ 2,378,191	
Cash and cash equivalents in governmental banks	30,103	306,035	114,185	24,358	750,339		1,225,020	72,522	5,505	97,099	1,400,146	
Investments	7,900	349,605	98,790		2,546,070		3,002,365	353,081		5,598,064	8,933,510	
Receivables, net:												
Taxes	78,014				67,514		145,528				145,528	
Intergovernmental	126,882		33,369	6,790			167,041		1,132	15,393	183,566	
Accounts	36,246	67,867	1,378	48,778	58,738		213,007	3,026	108	1,031,249	1,247,390	
Loans and advances	92,859	16,786	16,446		580,782		706,873	118,195	6,884	420,278	1,252,230	
Accrued interest	438	3,119	5,579		12,749		21,885	3,078		171,447	196,410	
Other	18,481		9,475	25,611	8,948		62,515	14,396	61	44,236	121,208	
Due from:												
Other funds	29,582		50,938	7,192	5,818		93,530	34,016		95,140	129,156	
Primary government												
Component units												
Other governmental entities	103,171						103,171			8,818	180,735	
Advances to:												
Primary government												
Component units		1,557					1,557					
Other governmental entities												
Inventories				15,346			15,346	5,810		388,643	409,799	
Restricted assets:												
Cash and cash equivalents	566,725			1,431	6,356		574,512	71,863	372	362,860	1,009,607	
Other restricted assets				180,523	36,354		216,877	102,597		3,618,723	3,938,197	
Housing units and land lots held for sale									132,986	132,433	265,419	
Fixed assets, net		6,429	15,763	557,840	24,454	2,590,195	3,172,489	625,634	63	10,366,971	14,165,157	
Other assets				1,480	32,470		56,142	74		259,843	316,059	
<b>Other Debits:</b>												
Amount available in debt service funds						256,958	256,958			60,854	317,812	
Amount to be provided for retirement of bonds and notes payable						8,719,444	8,719,444			369,990	9,089,434	
Amount to be provided for payment of accrued compensated absences, and other long-term liabilities						4,374,479	4,374,479			318,531	4,693,010	
<b>TOTAL ASSETS AND OTHER DEBITS</b>	<b>\$ 1,359,013</b>	<b>\$ 827,474</b>	<b>\$ 1,270,329</b>	<b>\$ 899,208</b>	<b>\$ 4,881,989</b>	<b>\$ 2,590,195</b>	<b>\$ 25,179,089</b>	<b>\$ 1,468,133</b>	<b>\$ 1,48,344</b>	<b>\$ 26,541,911</b>	<b>\$ 53,337,477</b>	

See notes to general purpose financial statements.

(Continued)

**COMMONWEALTH OF PUERTO RICO**

**COMBINED BALANCE SHEET - ALL FUND TYPES, ACCOUNT GROUPS AND DISCRETELY PRESENTED COMPONENT UNITS  
JUNE 30, 1997 (Expressed in Thousands)**

	Governmental Fund Types			Fiduciary Fund Types	Account Groups			Component Units			Totals Reporting Entity (Memorandum Only)
	Proprietary Fund Type		Trust and Agency		General		Public University	Office for the Liquidation	Other		
	General	Capital Projects			Fixed Assets	Long-Term Debt					
<b>LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS</b>											
Liabilities:											
Accounts payable and accrued liabilities	\$ 428,169	\$ 7,061	\$ 242,854	\$ 156,975	\$	\$	\$	\$ 86,979	\$ 4,199	\$ 2,358,920	\$ 3,384,927
Tax refunds payable	27,024							2,868		4,042,947	27,024
Deposits											4,045,815
Due to:											
Other funds	17,777	41,552		10,114							93,530
Primary government component units			24,087							39,374	39,374
Other governmental entities			45,879		64,973					21,238	132,090
Advances from:										1,444	1,444
Other funds											
Primary government component units	962	71,259	578,292		1,105,917				1,557	1,557	1,557
Securities lending transactions and reverse repurchases										1,207,673	2,964,103
Component units	11,856	218,333	36,923				1,510		946,875	946,875	946,875
Interest payable	213		14,362						193,186	193,186	461,808
Deferred revenues	553,683	299,565	193,824						202,234	202,234	216,809
Lottery prizes payable											193,824
Notes payable					21,416			324,974	55,996	1,636,336	2,267,431
Bonds payable					8,698,028			77,655	165	7,796,629	17,146,141
Accrued compensated absences	4,413	10,307	81,738		684,940					318,692	1,182,505
Deferred compensation payable	10,733	4,005	9,460							56,081	15,611
Other liabilities			328,919		940,278			15,611		298,325	543,535
Other long-term liabilities					1,835,329			31,273		34,263	1,900,865
Net pension obligation											
Total liabilities	1,054,830	570,516	339,604	642,262	13,350,881			545,309	60,360	19,155,774	37,132,790
<b>Equity (Deficit) and Other Credits:</b>											
Investment in general fixed assets					2,590,195			323,751		195,445	3,111,391
Contributed capital										4,830,618	5,006,468
Retained earnings (deficit)			175,850		(689,896)					1,468,101	778,205
Unrealized gain in value of debt and equity securities										61,583	61,583
Fund balances:											
Reserved for:											
Encumbrances	180,757			2,768							304,317
Debt service		256,958								68,221	330,546
Unemployment benefits				803,282							803,282
Employees' pension benefits				3,393,868							3,899,334
Advances and other specified purposes	17,197		840,065	8,767						93,841	983,677
Net assets available in the investment trust fund									3,110	624,199	624,199
Net assets in liquidation									84,874	39,945	84,874
Unreserved	106,229			31,042				16,595			193,811
Total equity (deficit) and other credits	304,183	256,958	930,725	4,239,727	2,590,195			922,824	87,984	7,386,137	16,204,687
<b>TOTAL LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS</b>	\$ 1,359,013	\$ 827,474	\$ 1,270,329	\$ 4,881,989	\$ 2,590,195	\$ 13,350,881	\$ 1,468,133	\$ 1,468,133	\$ 1,483,344	\$ 26,541,911	\$ 53,337,477

(Concluded)

See notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -  
ALL GOVERNMENTAL FUND TYPES AND EXPENDABLE TRUST FUNDS  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Governmental Fund Types			Fiduciary Fund Type	Totals (Memorandum Only)
	General	Debt Service	Capital Projects	Expendable Trust	
<b>REVENUES:</b>					
Taxes:					
Income	\$ 3,622,988	\$	\$	\$	\$ 3,622,988
Excise	1,632,613	194,692			1,827,305
Unemployment				236,171	236,171
Other	64,910				64,910
Charges for services	113,297	350,297	440	3,584	467,618
Intergovernmental	2,929,697	50,133	97,212	30,940	3,107,982
Interest	50,946	24,545	35,286	49,472	160,249
Other	128,874		5,945	4,118	138,937
<b>Total revenues</b>	<b>8,543,325</b>	<b>619,667</b>	<b>138,883</b>	<b>324,285</b>	<b>9,626,160</b>
<b>EXPENDITURES:</b>					
Current:					
General government	499,652			4,953	504,605
Public safety	1,188,814			1,431	1,190,245
Health	508,659			1,486	510,145
Public housing and welfare	2,086,828			321,161	2,407,989
Education	1,960,185				1,960,185
Economic development	333,290			9,219	342,509
Intergovernmental	496,844				496,844
Capital outlay	19,995		1,375,468	10,834	1,406,297
Debt service:					
Principal	58,521	301,330			359,851
Interest and other	69,099	487,736			556,835
<b>Total expenditures</b>	<b>7,221,887</b>	<b>789,066</b>	<b>1,375,468</b>	<b>349,084</b>	<b>9,735,505</b>
Excess (deficiency) of revenues over (under) expenditures	1,321,438	(169,399)	(1,236,585)	(24,799)	(109,345)
<b>OTHER FINANCING SOURCES (USES):</b>					
Proceeds from long-term debt issues	48,219		1,210,276		1,258,495
Proceeds from refunding bonds		335,155			335,155
Transfers-in from component units	100,635				100,635
Operating transfers-in from other funds	613,354	432,411	109,221	757	1,155,743
Operating transfers-out to other funds	(1,160,497)	(171,113)	(39,058)	(657)	(1,371,325)
Transfers-out to component units	(956,660)		(3,437)		(960,097)
Payment to refunded bond escrow agent		(333,111)			(333,111)
<b>Total other financing sources (uses)</b>	<b>(1,354,949)</b>	<b>263,342</b>	<b>1,277,002</b>	<b>100</b>	<b>185,495</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	(33,511)	93,943	40,417	(24,699)	76,150
FUND BALANCES AT BEGINNING OF YEAR (as restated)	337,694	251,800	890,308	870,558	2,350,360
RESIDUAL EQUITY TRANSFER		(88,785)			(88,785)
FUND BALANCES AT END OF YEAR	\$ 304,183	\$ 256,958	\$ 930,725	\$ 845,859	\$ 2,337,725

See notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

COMBINED STATEMENT OF REVENUES AND EXPENDITURES - BUDGET AND ACTUAL -  
BUDGET BASIS - BUDGETED GENERAL AND DEBT SERVICE FUNDS  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Budgeted General Fund			Budgeted Debt Service Fund		
	Budget	Actual	Variance	Budget	Actual	Variance
<b>REVENUES:</b>						
Income taxes	\$ 3,647,000	\$ 3,609,904	\$ (37,096)	\$	\$	\$
Intergovernmental taxes	3,000	8,286	5,286			
Excise taxes	1,603,000	1,623,108	20,108		14,560	14,560
Other taxes	58,000	57,563	(437)			
Charges for services	94,000	95,846	1,846			
Intergovernmental	58,000	61,114	3,114	65,000	28,026	(36,974)
Interest	600	4,275	3,675		1,192	1,192
Other	107,074	152,997	45,923			
Total revenues	5,570,674	5,613,093	42,419	65,000	43,778	(21,222)
<b>EXPENDITURES:</b>						
Current:						
General government	350,567	344,299	6,268			
Public safety	1,027,141	1,025,590	1,551			
Health	248,339	245,525	2,814			
Public housing and welfare	355,322	351,426	3,896			
Education	1,335,002	1,334,166	836			
Economic development	301,351	297,327	4,024			
Intergovernmental	263,998	263,307	691			
Debt service:						
Principal	54,933	55,174	(241)	208,005	208,005	
Interest and other	50,533	44,900	5,633	231,995	225,377	6,618
Total expenditures	3,987,186	3,961,714	25,472	440,000	433,382	6,618
Excess (deficiency) of revenues over (under) expenditures	1,583,488	1,651,379	67,891	(375,000)	(389,604)	(14,604)
<b>OTHER FINANCING SOURCES (USES):</b>						
Proceeds of refunding bonds						
Operating transfers-in from other funds	95,000	100,823	5,823			
Transfers-in from component units	28,033	28,033		375,000	375,000	
Operating transfers-out to other funds	(812,445)	(812,445)				
Transfers-out to component units	(878,970)	(842,970)	36,000			
Payment of refunded bond escrow agent						
Total other financing sources (uses)	(1,568,382)	(1,526,559)	41,823	375,000	364,211	(10,789)
Excess (deficiency) of revenues and other sources over (under) expenditures and other uses	\$ 15,106	\$ 124,820	\$ 109,714	\$	\$ (25,393)	\$ (25,393)

See notes to general purpose financial statements.

## COMMONWEALTH OF PUERTO RICO

### COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS (DEFICIT)/FUND BALANCES - PROPRIETARY FUND TYPE AND SIMILAR DISCRETELY PRESENTED COMPONENT UNITS YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Proprietary Fund Type	Other Discretely Presented Component Units
	Enterprise	
<b>OPERATING REVENUES:</b>		
Charges for services	\$ 879,664	\$ 4,301,004
Financing income		181,473
Investment earnings		444,984
Other		29,277
Total operating revenues	<u>879,664</u>	<u>4,956,738</u>
<b>OPERATING EXPENSES:</b>		
Cost of services	1,253,549	4,148,109
Interest		400,599
Depreciation and amortization	27,327	596,096
Other		8,678
Total operating expenses	<u>1,260,876</u>	<u>5,153,482</u>
<b>OPERATING LOSS</b>	<u>(381,212)</u>	<u>(196,744)</u>
<b>NON-OPERATING REVENUES (EXPENSES):</b>		
Intergovernmental	2,173	(25,929)
Interest income	881	193,386
Interest expense	(58,525)	(362,193)
Other, net	21,866	(15,380)
Total non-operating expenses	<u>(33,605)</u>	<u>(210,116)</u>
<b>LOSS BEFORE OPERATING TRANSFERS</b>	<u>(414,817)</u>	<u>(406,860)</u>
<b>TRANSFERS:</b>		
Operating transfers from other funds	381,620	
Operating transfers to other funds	(136,915)	
Transfers from component units - other		15,500
Transfers to component units - other		(37,015)
From primary government		648,777
Total transfers, net	<u>244,705</u>	<u>627,262</u>
<b>NET INCOME (LOSS)</b>	<u>(170,112)</u>	<u>220,402</u>
<b>EXCESS OF REVENUES OVER EXPENDITURES FROM GOVERNMENTAL OPERATIONS</b>		8,638
<b>WITHDRAWALS</b>		(689,819)
<b>DEPRECIATION ON FIXED ASSETS ACQUIRED THROUGH CAPITAL CONTRIBUTIONS</b>	<u>1,337</u>	<u>51,267</u>
<b>DECREASE IN RETAINED EARNINGS/ FUND BALANCES</b>	<u>(168,775)</u>	<u>(409,512)</u>
<b>RETAINED EARNINGS (DEFICIT)/ FUND BALANCES AT BEGINNING OF YEAR (as restated)</b>	<u>(520,454)</u>	<u>2,807,460</u>
<b>TRANSFERS TO CONTRIBUTED CAPITAL</b>	<u>(667)</u>	<u>(102,457)</u>
<b>RETAINED EARNINGS (DEFICIT)/ FUND BALANCES AT END OF YEAR</b>	<u>\$ (689,896)</u>	<u>\$ 2,295,491</u>

See notes to general purpose financial statements.

# COMMONWEALTH OF PUERTO RICO

## COMBINED STATEMENT OF CASH FLOWS - PROPRIETARY FUND TYPE AND SIMILAR DISCRETELY PRESENTED COMPONENT UNITS YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Proprietary Fund Type	Other Discretely Presented Component Units
	Enterprise	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Operating loss	\$ (381,212)	\$ (196,744)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	27,327	596,096
Provision for uncollectible accounts	23,793	68,641
Amortization of debt discount		1,174
Net gain on disposition of fixed assets		(4,533)
Net gain on sale of investments and fixed assets		(65,489)
Contribution in lieu of taxes		(162,941)
Net cash flow effect of noncapital financing, capital and related financing and investing activities included in operating loss		(141,215)
Other		46,944
Change in assets and liabilities:		
Increase in:		
Receivables	(19,599)	(179,120)
Due from other funds	(640)	
Inventories	(91)	(34,352)
Other assets		(16,357)
Accounts payable and accrued liabilities	9,110	198,103
Due to other funds	1,792	
Deposits		8,284
Interest payable		60
Deferred revenues	56	28,655
Lottery prizes payable	20,952	
Accrued compensated absences		21,227
Other liabilities		284
Decrease in:		
Receivables		21,182
Inventories	2,672	24,255
Other assets	70	6,847
Accounts payable and accrued liabilities	(962)	(25,005)
Deposits		(85)
Interest payable		(865)
Deferred revenues		(7,731)
Accrued compensated absences	(32)	
Other liabilities		(8,713)
Total adjustments	<u>64,448</u>	<u>375,346</u>
Net cash provided by (used in) operating activities, (carried forward)	\$ (316,764)	\$ 178,602

See notes to general purpose financial statements.

(Continued)



COMMONWEALTH OF PUERTO RICO

COMBINED STATEMENT OF CASH FLOWS -  
 PROPRIETARY FUND TYPE AND SIMILAR DISCRETELY PRESENTED COMPONENT UNITS  
 YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Proprietary Fund Type	Other Discretely Presented Component Units
	Enterprise	
Net cash provided by (used in) operating activities, (brought forward)	\$ (316,764)	\$ 178,602
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>		
Proceeds from notes and loans		2,710,137
Principal paid on notes and loans		(2,112,126)
Interest paid on notes and loans		(318,493)
Operating grants received	2,071	409,716
Operating transfers-in from other funds	523,202	
Operating transfers-out to other funds	(128,603)	
Transfers-in from primary government		15,919
Transfers-out to primary government		(65,377)
Transfers from component units		346,662
Transfers to component units		(17,200)
Capital contributions	115,890	22,236
Net increase in securities lending transactions		40,332
Net cash provided by noncapital financing activities	<u>512,560</u>	<u>1,031,806</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Acquisition and construction of capital assets	(129,797)	(1,505,206)
Proceeds from issuance of bonds and notes		1,134,552
Principal paid on bonds and notes	(357)	(564,026)
Interest paid on bonds and notes	(54,681)	(270,885)
Proceeds from sale of equipment		53,762
Capital contributions		17,219
Net cash used in capital and related financing activities	<u>(184,835)</u>	<u>(1,134,584)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of investment securities	(20,064)	(12,114,599)
Proceeds from sales and maturities of investments securities		12,459,783
Purchases of units in the Puerto Rico Government Investment Trust fund		(26,124)
Redemptions of units in the Puerto Rico Government Investment Trust fund		643
Interest and dividends on investments	8,344	482,322
Principal collected on loans to:		
Public entities of the Commonwealth of Puerto Rico		1,146,574
Private sector		58,805
Loans originated to:		
Public entities of the Commonwealth of Puerto Rico		(1,983,143)
Private sector		(157,106)
Net cash used in investing activities	<u>(11,720)</u>	<u>(132,845)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(759)	(57,021)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	56,407	668,762
CASH AND CASH EQUIVALENTS FROM GOVERNMENTAL OPERATIONS		<u>110,985</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 55,648</u>	<u>\$ 722,726</u>

See notes to general purpose financial statements.

(Continued)

COMMONWEALTH OF PUERTO RICO

COMBINED STATEMENT OF CASH FLOWS -  
 PROPRIETARY FUND TYPE AND SIMILAR DISCRETELY PRESENTED COMPONENT UNITS  
 YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	<u>Proprietary Fund Type</u>	<u>Other Discretely Presented Component Units</u>
	Enterprise	
<b>RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE COMBINED BALANCE SHEET:</b>		
Cash and cash equivalents	\$ 29,859	\$ 262,767
Cash and cash equivalents in governmental banks	24,358	97,099
Cash and cash equivalents - restricted assets	<u>1,431</u>	<u>362,860</u>
	<u>\$ 55,648</u>	<u>\$ 722,726</u>

**RECONCILIATION OF BEGINNING CASH AND CASH EQUIVALENTS:**

Cash and cash equivalents as of June 30, 1996, as previously reported	\$ 1,555,858
Investments considered cash equivalents under Governmental Accounting Standards Board No. 9, Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting (GASB No. 9)	191,410
Cash equivalents considered investments under GASB No. 9	(878,743)
Cash and cash equivalents from governmental operations	<u>(199,763)</u>
Cash and cash equivalents as of June 30, 1996, as adjusted	<u>\$ 668,762</u>

**SCHEDULE OF SUPPLEMENTAL CASH FLOWS INFORMATION  
AND NON-CASH TRANSACTIONS:**

Financing of property acquisition	\$ 76,767	\$ 827
Long-term debt proceeds deposited directly in the Puerto Rico Treasury Department	\$ 196,346	\$
Transfers of retained earnings to contributed capital	\$	\$ 100,000
Retirement of property	\$	\$ 13,363
Loans to foreclosed real estate	\$	\$ 27,200
Payments made by the Puerto Rico Treasury Department on behalf of the Health Facilities and Services Administration of Puerto Rico	\$ 23,581	\$
Deferred gain on sale of securities	\$	\$ 30,699

See notes to general purpose financial statements.

(Concluded)

# COMMONWEALTH OF PUERTO RICO

## COMBINED STATEMENT OF CHANGES IN PLAN NET ASSETS AVAILABLE FOR PENSION BENEFITS - PENSION TRUST FUND TYPES AND SIMILAR DISCRETELY PRESENTED COMPONENT UNITS YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Fidiciary Fund Type	Public University Fund
	Pension Trust Funds	University of Puerto Rico Retirement System
ADDITIONS:		
Contributions:		
Employer	\$ 319,207	\$ 50,231
Employees	276,634	18,025
Special	<u>25,920</u>	<u>          </u>
Total contributions	<u>621,761</u>	<u>68,256</u>
Investment income:		
Interest	106,920	19,714
Dividends	17,115	2,840
Net appreciation of investments	<u>378,405</u>	<u>46,348</u>
Total investment income	502,440	68,902
Other income	<u>5,429</u>	<u>          </u>
Total additions	<u>1,129,630</u>	<u>137,158</u>
DEDUCTIONS:		
Benefits	586,222	57,545
Refunds of contributions	25,570	
General and administrative	<u>56,296</u>	<u>1,583</u>
Total deductions	<u>668,088</u>	<u>59,128</u>
NET INCREASE	461,542	78,030
NET ASSETS AVAILABLE FOR PENSION BENEFITS AT BEGINNING OF YEAR	<u>2,932,326</u>	<u>427,436</u>
NET ASSETS AVAILABLE FOR PENSION BENEFITS AT END OF YEAR	<u>\$ 3,393,868</u>	<u>\$ 505,466</u>

See notes to general purpose financial statements.

**COMMONWEALTH OF PUERTO RICO**

**COMBINED STATEMENT OF CHANGES IN FUND BALANCES -  
PUBLIC UNIVERSITY FUNDS - UNIVERSITY OF PUERTO RICO  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

	Current Funds			Endowment and Similar Funds	Plant Funds			
	Unrestricted	Restricted	Loan Funds		Unexpended	Renewal and Replacement	Retirement of Indebtedness	Investment in Plant
<b>REVENUES AND OTHER ADDITIONS:</b>								
Unrestricted current fund revenues	\$ 573,335	\$	\$	\$	\$	\$	\$	\$
Commonwealth of Puerto Rico appropriations, grants and contracts		66,087		253				
Federal grants and contracts		144,781						
Private gifts, grants and contracts		8,892		297		246		
Investment income		138	153	550	3,438	1,696		
Interest on loans receivable							18,515	
Expended for plant facilities							12,801	
Retirement of indebtedness								
Other		16,982	42		183	92		
Total revenues and other additions	<u>573,335</u>	<u>236,880</u>	<u>195</u>	<u>847</u>	<u>4,646</u>	<u>1,942</u>	<u>31,316</u>	
<b>EXPENDITURES AND OTHER DEDUCTIONS:</b>								
Educational and general expenditures	512,412	253,036						
Auxiliary enterprises expenditures	9,068							
Refunded to grantors		497	5		5,000			
Loan cancellations and assignments			87					
Administrative and collection costs			30					
Expended for plant facilities						28	2,450	
Retirement of indebtedness								
Interest on indebtedness								
Disposal of plant facilities								3,969
Other					9		149	
Total expenditures and other deductions	<u>521,480</u>	<u>253,533</u>	<u>122</u>		<u>5,009</u>	<u>29,689</u>	<u>6,568</u>	
<b>TRANSFERS AMONG FUNDS-ADDITIONS (DEDUCTIONS):</b>								
Mandatory:								
Principal and interest	(29,057)							
Restricted current fund matching grants	(5,725)	5,575			150		29,057	
Other transfers:								
Unrestricted current funds	(15,286)	12,536		2,021	735	(7)		
Total transfers	<u>(50,068)</u>	<u>18,111</u>		<u>2,021</u>	<u>885</u>	<u>(7)</u>	<u>29,057</u>	
<b>NET INCREASE FOR THE YEAR</b>	<b>1,787</b>	<b>1,458</b>	<b>73</b>	<b>2,868</b>	<b>522</b>	<b>57</b>	<b>24,748</b>	
<b>FUND BALANCES AT BEGINNING OF YEAR</b>	<b>9,594</b>	<b>27,798</b>	<b>4,102</b>	<b>11,646</b>	<b>5,933</b>	<b>405</b>	<b>301,003</b>	
<b>FUND BALANCES AT END OF YEAR</b>	<b>\$ 11,381</b>	<b>\$ 29,256</b>	<b>\$ 4,175</b>	<b>\$ 14,514</b>	<b>\$ 6,455</b>	<b>\$ 462</b>	<b>\$ 325,751</b>	

See notes to general purpose financial statements.

# COMMONWEALTH OF PUERTO RICO

## COMBINED STATEMENT OF CURRENT FUNDS REVENUES, EXPENDITURES AND OTHER CHANGES - PUBLIC UNIVERSITY FUNDS - UNIVERSITY OF PUERTO RICO YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Unrestricted	Restricted	Total
<b>REVENUES:</b>			
Tuition and fees	\$ 64,189	\$ 4,979	\$ 69,168
Transfers from primary government	488,960	66,087	555,047
Federal grants and contracts		155,363	155,363
Private gifts, grants and contracts		8,892	8,892
Sales and services of educational departments	620	4,624	5,244
Sales and services of auxiliary enterprises	6,902		6,902
Investment income	7,212	138	7,350
Other sources	5,452	7,378	12,830
Total current revenues	<u>573,335</u>	<u>247,461</u>	<u>820,796</u>
<b>EXPENDITURES AND MANDATORY TRANSFERS:</b>			
Educational and general:			
Instruction	216,743	30,758	247,501
Research	18,477	49,881	68,358
Public service	11,380	38,100	49,480
Academic support	65,963	9,042	75,005
Student services	29,847	2,334	32,181
Institutional support	93,247	4,865	98,112
Operation and maintenance of plant	74,008	239	74,247
Scholarships and fellowships	1,675	100,993	102,668
Hospitals		13,168	13,168
Independent operations	3	930	933
Other	1,069	2,726	3,795
Total educational and general expenditures	<u>512,412</u>	<u>253,036</u>	<u>765,448</u>
Mandatory transfers for:			
Principal and interest	29,057		29,057
Restricted current fund matching grants	5,725	(5,575)	150
Total educational, general and mandatory transfers	<u>547,194</u>	<u>247,461</u>	<u>794,655</u>
Auxiliary enterprises - expenditures	<u>9,068</u>		<u>9,068</u>
Total expenditures and mandatory transfers	<u>556,262</u>	<u>247,461</u>	<u>803,723</u>
<b>TRANSFERS AND ADDITIONS (DEDUCTIONS):</b>			
Deficit of restricted receipts under transfers to revenues		(10,581)	(10,581)
Refunded to grantors		(497)	(497)
Nonmandatory transfers	(15,286)	12,536	(2,750)
Total other transfers and additions (deductions)	<u>(15,286)</u>	<u>1,458</u>	<u>(13,828)</u>
NET INCREASE IN FUND BALANCE	<u>\$ 1,787</u>	<u>\$ 1,458</u>	<u>\$ 3,245</u>

See notes to general purpose financial statements.

# COMMONWEALTH OF PUERTO RICO

## COMBINED STATEMENT OF CHANGES IN NET ASSETS IN LIQUIDATION OFFICE FOR THE LIQUIDATION OF THE ACCOUNTS OF THE PUERTO RICO URBAN RENEWAL AND HOUSING CORPORATION YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Operating	Housing Management	Combined
<b>ADDITIONS TO NET ASSETS IN LIQUIDATION:</b>			
Mortgage collections and other	\$ 815	\$	\$ 815
Gain on disposition of assets	826		826
Interest	<u>642</u>	<u></u>	<u>642</u>
Total additions	<u>2,283</u>	<u></u>	<u>2,283</u>
<b>DEDUCTIONS TO NET ASSETS IN LIQUIDATION:</b>			
General and administrative expenses	4,902		4,902
Bad debt expense	290		290
Other expenses	<u>239</u>	<u></u>	<u>239</u>
Total deductions	<u>5,431</u>	<u></u>	<u>5,431</u>
DEDUCTIONS TO NET ASSETS IN LIQUIDATION BEFORE ADJUSTMENTS	(3,148)		(3,148)
ADJUSTMENTS OF ESTIMATED VALUES	<u>(405)</u>	<u>3,375</u>	<u>2,970</u>
ADDITIONS (DEDUCTIONS) TO NET ASSETS IN LIQUIDATION	(3,553)	3,375	(178)
NET ASSETS IN LIQUIDATION AT BEGINNING OF YEAR	83,073	4,219	87,292
Transfer to the Puerto Rico Treasury Department	<u>(2,240)</u>	<u></u>	<u>(2,240)</u>
NET ASSETS IN LIQUIDATION AT END OF YEAR	<u>\$ 77,280</u>	<u>\$ 7,594</u>	<u>\$ 84,874</u>

See notes to general purpose financial statements.

# COMMONWEALTH OF PUERTO RICO

## NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 1997

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### 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 United States 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, public health, public housing, welfare, education and economic development.

#### A. The Financial Reporting Entity

The accompanying general purpose financial statements have been prepared in conformity with generally accepted accounting principles (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for governmental accounting and financial reporting. In addition, GAAP requires that the Commonwealth's proprietary activities apply GAAP as it is applied by similar business activities in the private sector. As a result, the financial statements of certain component units follow the specialized reporting practices for financial institutions, insurance companies, public utilities, colleges and universities, telecommunications, investment companies, and hospitals, as prescribed by the GASB and other authoritative sources, including pronouncements of the Financial Accounting Standards Board (FASB). The financial statements of the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, a discretely presented component unit, have been presented on the liquidation basis of accounting, as required by generally accepted accounting principles, for an entity under a liquidation process.

The accompanying general purpose financial statements include all departments, agencies and governmental entities whose funds are under the custody and control of the Secretary of Treasury, 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 component units discussed below are included as part of the Commonwealth's reporting entity because they are financially accountable to the Commonwealth pursuant with GASB Statement No. 14, *The Financial Reporting Entity*.

#### B. Component Units

GAAP defines component units as those entities which 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 general purpose 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 transactions; or discrete presentation of the component units' financial data in columns separate from the Commonwealth's balances and transactions.

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 GAAP.

1. **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.

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

The Puerto Rico Highway and Transportation Authority is governed by the Secretary of the Department of Transportation and Public Works (DTPW), who is appointed by the Governor with the consent of the Senate. PRHTA has broad powers to carry out its responsibilities in accordance with the 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 tollways.

**Public Buildings Authority (PBA)**

The Public Buildings Authority is governed by a seven-member board of which the Secretary of DTPW is a permanent member and the other six members are appointed by the Governor with the 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, jails, 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 generally secured by the Commonwealth's guarantee. (See Note 16).

**Puerto Rico Maritime Shipping Authority (PRMSA)**

The Puerto Rico Maritime Shipping Authority is governed by the President of the Government Development Bank for Puerto Rico. On March 3, 1995, the Commonwealth sold to private investors its maritime transportation business. The remaining operations of PRMSA are for the sole purpose of servicing the long term liability to third parties that resulted from the aforementioned sale. 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 15).



**Employees' Retirement System of the Government of Puerto Rico  
and its Instrumentalities (ERS)**

The Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities is governed by a Board of Trustees which is composed of the Secretary of the Treasury, who is the President, the president of the Government Development Bank for Puerto Rico, the Insurance Commissioner, the Director of the Puerto Rico Central Office of Personnel Administration, two participating employees and one pensioner, 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 system. (See Note 22).

**Puerto Rico Judiciary Retirement System (JRS)**

The Puerto Rico Judiciary Retirement System is governed by the same Board of Trustees as ERS. JRS is a single-employer defined benefit plan which is administered by the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities 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 of Puerto Rico. (See Note 22).

**Puerto Rico System of Annuities and Pensions for Teachers (TRS)**

The Puerto Rico System of Annuities and Pensions for Teachers is governed by a five-member board comprised of the Secretary of Education, the Secretary of the Treasury, the President of the Teachers' Association and two members named by the Governor with the advice and consent of the Senate for four years of which one must be a retiree and the other an active member. 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, those holding positions in the Retirement Board, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education. The Plan provides retirement, death and disability benefits. (See Note 22).

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

Administrative offices:

PR Highway and Transportation Authority  
PO Box 42007  
San Juan, PR 00940-2007

Public Buildings Authority  
PO Box 41029 Minillas Station  
San Juan, PR 00940-1029

PR Maritime Shipping Authority  
PO Box 41249  
San Juan, PR 00940-1249

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

Puerto Rico Judiciary Retirement System  
PO Box 42003 Minillas Station  
Santurce, PR 00940

Puerto Rico System of Annuities and  
Pensions for Teachers  
PO Box 1879  
Hato Rey, PR 00919-1879

## **2. Discretely Presented Component Units:**

The following component units, consistent with GASB Statement No. 14, are discretely presented in the general purpose financial statements because of the nature of the services they provide and the Commonwealth's ability to impose its will. The public university funds financial information is presented in a separate column due to its reporting model being different from that followed by the other component units. The Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation is presented in a separate column and separate statement of activity because it reports on a liquidation basis of accounting.

### **Public University Funds**

#### **University of Puerto Rico (UPR)**

The University of Puerto Rico is governed by a thirteen-member Board of Trustees of which ten are appointed by the Governor with the consent of the Senate, one full-time student and two term professors. Board members are appointed for a period from four to eight years. The terms for the student and professors are one year.

#### **University of Puerto Rico Retirement System (UPRRS)**

The University of Puerto Rico Retirement System is the administrator of a single employer pension plan for the employees of the University of Puerto Rico. It is governed by the Board of Trustees of the University, and is reported as a component unit of the UPR. (See Note 22).

#### **Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation (the Office)**

The Office was created for the purpose of carrying out the liquidation of the Puerto Rico Urban Renewal and Housing Corporation and is administered by a Trustee appointed by the Governor. The Trustee is responsible for obtaining the maximum realization from the sale of assets in order to meet outstanding obligations.

### **Component Units - Other**

#### **Government Development Bank for Puerto Rico and Subsidiaries (GDB)**

The Government Development Bank for Puerto Rico and Subsidiaries are governed by a seven-member board appointed by the Governor. The Secretary of Treasury was the Chairman until October 1997 when the Chief of Staff became the Chairman. GDB acts as the financial advisor and fiscal agent 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 to public corporations.

### **Puerto Rico Electric Power Authority (PREPA)**

The Puerto Rico Electric Power Authority is governed by a nine-member board. Seven members are appointed by the Governor with the consent of the Senate, and the remaining two members by the Puerto Rico Consumer Affairs Department. PREPA is responsible for conserving, developing and utilizing the power resources of Puerto Rico and owns and operates the Commonwealth's electric system. PREPA is authorized, among others, to borrow money and issue revenue bonds for any of its corporate purposes and is required, under the terms of a 1947 Indenture and a 1974 Agreement, to determine and collect reasonable rates for electrical power generation and distribution system in order to produce revenues sufficient to cover all operating and financing obligations.

### **Puerto Rico Aqueduct and Sewer Authority (PRASA)**

The Puerto Rico Aqueduct and Sewer Authority is governed by a seven-member board. Four members are appointed by the Governor and the remaining three members, one should be the Secretary of Transportation and Public Works and two members appointed 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 powers, to borrow money and issue revenue bonds for any of its corporate purposes. PRASA is required, under the terms of its Trust Agreements, to determine and collect reasonable rates for water services to produce revenues sufficient to cover all operating and financing obligations. PRASA's capital is generated by non-reimbursable legislative appropriations from the Commonwealth, grants from various agencies of the Federal government, donations in-kind or other operating cash transfers from various governmental agencies and instrumentalities of the Commonwealth, other customers of PRASA, and internally generated funds. As discussed in Note 16, the Commonwealth guarantees the principal and interest payments of certain outstanding bonds and of all future bonds issued to refinance these outstanding bonds.

### **Puerto Rico Telephone Authority and Subsidiary, and Puerto Rico Telephone Company (PRTA)**

The Puerto Rico Telephone Authority and Subsidiary, and Puerto Rico Telephone Company are governed by a five-member board appointed by the Governor with the consent of the Senate. PRTA is responsible for acquiring, developing and operating telephone, radio, cable or other communication systems. PRTA is authorized, among other powers, to borrow money and issue revenue bonds for any of its corporate purposes. PRTA is required, as defined in the Trust Agreement, to determine and collect reasonable rates for the use of its communication facilities in order to produce revenues sufficient to cover all operating and financing obligations.

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

The Puerto Rico Government Investment Trust Fund was created in fiscal 1996 and is governed by the Secretary of the Treasury of the Commonwealth, who is appointed by the Governor, with the consent of the Senate. The Government Development Bank for Puerto Rico is its trustee, custodian and administrator. PRGITF's main objective is to provide investment opportunities in a 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 agencies, and the municipalities of Puerto Rico. PRGITF is neither subject to regulation under the Investment Company Act of 1940, nor is it required to register under the Securities and Exchange Act of 1933. (See Note 4).

#### **Puerto Rico Housing Bank and Finance Agency (PRHBFA)**

The Puerto Rico Housing Bank and Finance Agency is governed by the Secretary of Housing who is appointed by the Governor with the consent of the Senate. PRHBFA issues bonds and notes to provide interim and permanent financing for low-income housing projects and single-family home ownership programs. It is also engaged in insuring and servicing mortgages originated by the former Puerto Rico Urban Renewal and Housing Corporation which ceased operations effective August 9, 1991. PRHBFA obtains funds from legislative appropriations, sale of mortgages, collection of mortgage repayments, and other sources.

#### **State Insurance Fund Corporation (SIFC)**

The State Insurance Fund Corporation is governed by five-member board appointed by the Governor with the consent of the Senate. SIFC provides worker's compensation and disability insurance to public and private employees who suffer accidents during the course, or as a consequence of functions which are inherent, to their work.

#### **Economic Development Bank for Puerto Rico (EDB)**

The Economic Development Bank for Puerto Rico is governed by a nine-member board comprised of the President of the Government Development Bank for Puerto Rico, who is the Chairman, the Secretary of Agriculture, the Secretary of Economic Development and Commerce, the Economic Development Administrator, the Executive Director of the Tourism Company of Puerto Rico and four other members appointed by the Governor with the consent of the Senate. 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, loan participation, and/or direct investments available to any person or business organization devoted to manufacturing, agriculture, trade, tourism or other service enterprises, whose economic activity may have the effect of substituting imports.

#### **Puerto Rico Industrial Development Company (PRIDCO)**

The Puerto Rico Industrial Development Company is governed by the Economic Development Administrator who is appointed by the Governor with the consent of the Senate. PRIDCO operates the Commonwealth-sponsored economic development program by providing facilities, general assistance, and special incentive grants to manufacturing companies in Puerto Rico. PRIDCO has issued interim notes and revenue bonds to finance factories 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 Ports Authority (PRPA)**

The Puerto Rico Ports Authority is governed by a five-member board consisting of the Secretary of Transportation and Public Works, as the Chairman, the Secretary of Economic Development and Commerce, the Economic Development Administrator, the Executive Director of the Tourism Company of Puerto Rico and one private citizen appointed by the Governor with the 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 Municipal Finance Agency (PRMFA)**

The Puerto Rico Municipal Finance Agency is governed by a five-member board comprised of the Secretary of the Treasury, the President of the Government Development Bank for Puerto Rico 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 Infrastructure Financing Authority (PRIFA)**

The Puerto Rico Infrastructure Financing Authority was created by the Commonwealth. PRIFA is governed by the Secretary of Treasury and six members of the board of the Government Development Bank for Puerto Rico. 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.

### **Sugar Corporation of Puerto Rico (SCPR)**

The Sugar Corporation of Puerto Rico is administered by the Governing Board of the Land Authority of Puerto Rico consisting of the Secretary of Agriculture as Chairman, and four other members appointed by the Governor with the consent of the Senate. SCPR was created to consolidate ownership and management of the Commonwealth's interests in Puerto Rico's sugar industry. SCPR owns or leases and operates all the sugar production facilities in Puerto Rico. SCPR buys all the cane grown by private farmers, processes the cane, and sells the raw and refined sugar and molasses. (See Note 26).

### **Puerto Rico School of Plastic Arts (SPA)**

The Puerto Rico School of Plastic Arts is governed by a seven-member board elected by the Board of Directors of the Institute of Puerto Rican Culture (the Institute). Board members may not be employees of the SPA. Of these, three are elected from among the members of the Board of Directors of the Institute, one of whom will serve as president. SPA 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.

### **Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority (AFICA)**

The Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority is governed by a seven-member board consisting of the Economic Development Administrator, the President of the Government Development Bank for Puerto Rico, the Executive Director of the Puerto Rico Aqueduct and Sewer Authority, the Director of the Tourism Company and the President of the Environmental Quality Board and two private citizens appointed by the Governor with the consent of the Senate. AFICA is authorized to issue revenue bonds to finance industrial, pollution control, medical, and educational facilities in Puerto Rico and the United States for the use by private companies, non-profit entities or governmental agencies. The bonds are payable solely from collections from such private companies, non-profit entities or governmental agencies, and do not constitute a debt of the Commonwealth or any of its other components units.

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

The Caribbean Basin Projects Financing Authority is governed by a five-member board consisting of the Economic Development Administrator, the President of the Government Development Bank for Puerto Rico, the President of the Economic Development Bank for Puerto Rico and two private citizens appointed by the Governor with the consent of the Senate. CBPFA is authorized to issue revenue bonds and to loan the proceeds thereof to finance the projects for the development of the Caribbean Basin countries that are authorized to receive investments of funds under the provisions of Section 936 of the US Internal Revenue Code.

### **Automobile Accident Compensation Administration (AACCA)**

The Automobile Accident Compensation Administration board is composed of one member of the Cabinet of the Governor and four members appointed by the Governor with the consent of the Senate. AACCA operates a system of compulsory insurance coverage for all registered motor vehicles and compensates citizens for injuries arising from motor vehicles accidents.

### **Puerto Rico Metropolitan Bus Authority (PRMBA)**

The Puerto Rico Metropolitan Bus Authority is governed by the Secretary of Transportation and Public Works, who is appointed by the Governor with the consent of the Senate. The PRMBA provides transportation to passengers within the San Juan Metropolitan Area. This service is principally financed by Commonwealth and Federal government appropriations, and passenger fares.

### **Puerto Rico Public Broadcasting Corporation (PRPBC)**

The Puerto Rico Public Broadcasting Corporation board of directors is comprised of four members of the public sector and five private citizens on behalf of the public interest, appointed by the Governor with the consent of the Senate. PRPBC was created with the purpose of integrating, developing and operating the radio, television and electronic communication facilities that belong to the Commonwealth. The PRPBC changed its fiscal year end from December 31, to June 30 effective for fiscal year 1996-97. The impact on the financial statements of the Commonwealth of Puerto Rico is immaterial.

### **Puerto Rico Solid Waste Authority (PRSWA)**

The Puerto Rico Solid Waste Authority is governed by the Secretary of Natural Resources, who is appointed by the Governor with the consent of the Senate. PRSWA provides alternatives for processing of solid waste and encourages recycling, reuse and recovery of resources from waste.

### **Tourism Company of Puerto Rico (TCPR)**

The Tourism Company of Puerto Rico is governed by an eleven-member board comprised of the Secretary of Economic Development and Commerce who serves as Chairman, the Secretary of Treasury, the Secretary of Agriculture, the Secretary of Transportation and Public Works, the Secretary of Housing, the Economic Development Administrator, the President of the Planning Board, and four other members appointed by the Governor with the consent of the Senate. Its purpose is to promote the tourism industry of Puerto Rico.

### **Employment and Training Enterprises Corporation and Subsidiary (ETEC)**

The Employment and Training Enterprises Corporation and Subsidiary is governed by a ten-member board comprised of the Administrator of Correction, the Administrator of Youth Correctional Institutions, the Secretary of Justice, the Secretary of Education, the Executive Director of the Right to Employment Administration, the Administrator of the Administration of Mental Health and Anti-Addiction, the Sub-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 in the correctional institutions of the Commonwealth.

### **Industries for the Blind, Mentally Retarded and Other Disabled Persons of Puerto Rico**

The Industries for the Blind, Mentally Retarded and Other Disabled Persons of Puerto Rico is governed by the Secretary of the Department of Family Affairs, who is its President. The purpose of the entity is to provide economic and social rehabilitation for the blind, mentally retarded and other disabled persons through job opportunities within the public and private industries.

### **Institutional Trust of the National Guard of Puerto Rico (ITNGPR)**

The Institutional Trust of the National Guard of Puerto Rico is administered by a seven-member board comprised of the General Adjutant of the Puerto Rico National Guard, the President of the Government Development Bank for Puerto Rico, the Secretary of Justice and four members of the Puerto Rico National Guard appointed by the Governor with the consent of the Senate. ITNGPR purpose is to provide life insurance and retirement benefits to the active members of the Puerto Rico National Guard and to provide economic assistance to the members of the Puerto Rico National Guard and their families.

### **Musical Arts Corporation and Subsidiaries (MAC)**

The Musical Arts Corporation and Subsidiaries are governed by a seven-member board appointed by the Governor with the consent of the Senate. MAC was created to promote the development of the arts and cultural programs of the Commonwealth.

### **Puerto Rico Conservatory of Music Corporation (PRCMC)**

The Puerto Rico Conservatory of Music Corporation is governed by the same board as the Musical Arts Corporation. PRCMC was created for the development, promotion, planning, coordination and operation of the Baccalaureate Program, the Children's Strings Program, the Artistic Varieties Program, and the Extension Program.

### **Corporation of Stocks and Deposits Insurance for the Savings and Loans Cooperatives (CSDISLC)**

The Corporation of Stock and Deposits Insurance for the Savings and Loans Cooperatives is governed by a nine-member board consisting of the Commissioner of Financial Institutions of Puerto Rico, the Insurance Commissioner of Puerto Rico, the Administrator of the Cooperative Development Administration, the Secretary of the Puerto Rico Treasury Department, the Director of the Office of Management and Budget, a representative of the Government Development Bank for Puerto Rico, two citizens representing the cooperative movement, and one private citizen. CSDISLC 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 of Puerto Rico.

### **Puerto Rico Land Administration (PRLA)**

The Puerto Rico Land Administration is governed by an eleven-member board comprised by the Secretary of Economic Development and Commerce, who serves as Chairman, the Secretary of Treasury, the Secretary of Agriculture, the Secretary of Transportation and Public Works, the Secretary of Housing, the Economic Development Administrator, the President of the Planning Board, and four other members appointed by the Governor with the consent of the Senate. PRLA acquires, through negotiation or expropriation, parcels of land, on behalf of government instrumentalities.

### **Puerto Rico Health Insurance Administration (PRHIA)**

The Puerto Rico Health Insurance Administration is governed by a board comprised of the Secretary of Health, the Secretary of Treasury, the Insurance Commissioner and four additional members appointed by the Governor, with the consent of Senate. 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.



### **Land Authority of Puerto Rico (LAPR)**

The Land Authority of Puerto Rico is governed by a five-member board consisting of the Secretary of Agriculture and four members appointed by the Governor with the consent of the Senate. LAPR was created to carry out the provisions of the Land Law of Puerto Rico.

### **Fine Arts Center Corporation (FACC)**

The Fine Arts Center Corporation is governed by a seven-member board of which five are appointed by the President of the Board of Directors of the Arts and Cultural Development Administration and two are appointed by the President of the Board of Directors of the Puerto Rico Culture Institute. FACC was created with the purpose of administering the Fine Arts Center.

### **Right to Employment Administration**

The Right to Employment Administration is governed by an Administrator appointed by the Governor with the consent of the Senate. In addition, a Consultative Board composed of the Secretary of Labor, the Secretary of Agriculture, the Secretary of Transportation and Public Works, the Secretary of Education and five additional members appointed by the Governor, with the consent of the Senate, will advise the Administrator in the implementation of the Right to Employment Act.

### **Farm Insurance Corporation of Puerto Rico (FICPR)**

The Farm Insurance Corporation of Puerto Rico is governed by a five-member board consisting of the Secretary of Agriculture, the Director of the Agriculture Sciences Faculty of the Mayagüez Campus of the University of Puerto Rico, a representative of the Government Development Bank for Puerto Rico 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.

### **Puerto Rico Medical Services Administration**

The Puerto Rico Medical Services Administration is governed by the Secretary of Health who is appointed by the Governor with the consent of the Senate. It was created 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 *Puerto Rico Medical Center*.

### **Puerto Rico and Caribbean Cardiovascular Center Corporation (PRCCCC)**

The Puerto Rico and Caribbean Cardiovascular Center Corporation is governed by a seven-member board comprised of the Secretary of Health, the Director of the Medical Sciences Campus of the University of Puerto Rico, the Executive Director of the Puerto Rico Medical Services Administration and four 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. The purpose of the PRCCCC is to provide special treatment to patients suffering cardiovascular diseases.

### **Commercial and Farm Credit and Development Corporation for Puerto Rico (CFDCPR)**

The Commercial and Farm Credit and Development Corporation for Puerto Rico is governed by the members of the Economic Development Bank for Puerto Rico board of directors. CFDCPR has as its purpose the promotion of the development of the productivity, competitiveness and profits of commercial, manufacturing, service and agro-industrial enterprises, including, without limitation, agriculture, livestock, fishing industries, aquatic and marine resources, as well as forestry and terrestrial. Such purpose is to be met by providing financing through diverse credit mechanisms. The CFDCPR is a subsidiary of the Economic Development Bank for Puerto Rico.

### **Recreational Development Company of Puerto Rico (RDCPR)**

The Recreational Development Company of Puerto Rico is governed by the Secretary of Sports and Recreation, who is appointed by the governor with the consent of the Senate. The purpose of RDCPR is to develop a program for the construction and operation of recreational facilities which shall contribute to the physical and mental development of the communities, family welfare and improvement in the quality of life.

### **Farm Credit Guarantee Fund and Guarantee Loan Fund for Eligible Businesses of Puerto Rico**

Pursuant to Act No. 1 of October 4, 1954, as amended, the Farm Credit Guarantee Fund was empowered to secure loans granted by financial institutions to farmers and agricultural entities for agricultural purposes up to a maximum of \$120 million under the guarantee of the good faith and credit of the Commonwealth of Puerto Rico. It is governed by the Secretary of Agriculture who is appointed by the Governor with the consent of the Senate. Pursuant to Act No. 87 of July 9, 1985, as amended, the Guarantee Loan Fund for Eligible Businesses of Puerto Rico was empowered to guarantee the payment of loans granted by legally established credit institutions to certain eligible business organizations. It is administered by an Executive Committee that consists of the President of the Commercial and Farm Credit and Development Corporation of Puerto Rico and the President of the Government Development Bank for Puerto Rico.

### **Agricultural Services and Development Administration**

The Agricultural Services and Development Administration was created by Law No. 5 of July 1, 1994 to provide a wide variety of services and incentives to the agricultural sector. It is governed by the Secretary of Agriculture who is appointed by the Governor with the consent of the Senate.

### **Trust for the Development, Operation and Conservation of National Parks of Puerto Rico**

The Trust for the Development, Operation and Conservation of National Parks of Puerto Rico is governed by the Secretary of Sports and Recreation, and four representatives from the government, the private sector, the advisory council and the trustees, all of which are appointed by the Governor with the consent of the Senate. The Trust shall develop, operate and provide maintenance to the national parks of Puerto Rico.

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

Administrative offices:

University of Puerto Rico  
PO Box 364984  
San Juan, PR 00936-4984

PR Housing Bank and Finance  
Agency  
PO Box 345  
San Juan, PR 00919-0345

University of Puerto Rico  
Retirement System  
PO Box 21769  
University Station  
San Juan, PR 00936-1769

State Insurance Fund Corporation  
PO Box 365028  
San Juan, PR 00936-5028

Office for the Liquidation of the  
Accounts of the PR Urban  
Renewal and Housing Corporation  
PO Box 11872  
San Juan, PR 00922-1365

Economic Development Bank for PR  
and Subsidiary  
PO Box 195009  
San Juan, PR 00919-5009

Government Development Bank for  
Puerto Rico and Subsidiaries  
PO Box 42001  
San Juan, PR 00940-2001

PR Industrial Development Co.  
PO Box 362350  
San Juan, PR 00936-2350

PR Electric Power Authority  
PO Box 364267  
San Juan, PR 00936-4267

Puerto Rico Ports Authority  
PO Box 362829  
San Juan, PR 00936-2829

PR Aqueduct and Sewer Authority  
PO Box 7066  
San Juan, PR 00916-7066

PR Municipal Finance Agency  
PO Box 42001  
San Juan, PR 00940-2001

Puerto Rico Telephone Authority  
PO Box 360998  
San Juan, PR 00936-0998

Puerto Rico Infrastructure Financing  
Authority  
PO Box 42001  
San Juan, PR 00940-2001

PR Government Investment  
Trust Fund  
PO Box 42001 Minillas Station  
San Juan, PR 00940

Sugar Corporation of Puerto Rico  
PO Box 9477  
San Juan, PR 00908-9477

Puerto Rico School of Plastic Arts  
PO Box 9021112  
San Juan, PR 00902-1112

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

Caribbean Basin Projects Financing  
Authority  
PO Box 3271  
San Juan, PR 00904-3271

Automobile Accident Compensation  
Administration  
PO Box 364847  
San Juan, PR 00936-4847

PR Metropolitan Bus Authority  
PO Box 195349  
San Juan, PR 00919-5349

Puerto Rico Public Broadcasting  
Corporation  
PO Box 190909  
San Juan, PR 00919-0909

PR Solid Waste Authority  
PO Box 40285  
San Juan, PR 00940-0285

Tourism Company of Puerto Rico  
PO Box 4435  
Old San Juan Station  
San Juan, PR 00905-4435

Employment and Training  
Enterprises Corporation  
PO Box 366505  
San Juan, PR 00936-6505

Industries for the Blind, Mentally  
Retarded and Other Disabled  
Persons of PR  
PO Box 13382  
San Juan, PR 00940-3382

Institutional Trust of the National  
Guard of PR  
PO Box 3786  
San Juan, PR 00908-3786

Musical Arts Corporation  
PO Box 41227 - Minillas Station  
San Juan, PR 00940-1227

PR Conservatory of Music  
Corporation  
350 Lamar Street & Roosevelt Ave.  
San Juan, PR

Corporation of Stocks and Deposits  
Insurance for the Savings and  
Loans Cooperatives  
PO Box 195449  
San Juan, PR 00919-5449

Puerto Rico Land Administration  
PO Box 3767  
San Juan, PR 00902-3767

Puerto Rico Health Insurance  
Administration  
PO Box 4264  
San Juan, PR 00902/4264

Land Authority of Puerto Rico  
PO Box 9745  
San Juan, PR 00908-9745

Fine Arts Center Corporation  
PO Box 41287 - Minillas Station  
Santurce, PR 00940-1287

Right to Employment Administration  
PO Box 364452  
San Juan, PR 00936-4452

Farm Insurance Corporation of  
Puerto Rico  
PO Box 9200  
Santurce, PR 00908-9200

Puerto Rico Medical Services  
Administration  
PO Box 2129  
San Juan, PR 00922-2129

Farm Credit Guarantee Fund and  
Guarantee Loan Fund for Eligible  
Business of PR  
PO Box-195009  
San Juan, PR 00919-5009

Puerto Rico and Caribbean  
Cardiovascular Center  
Corporation  
PO Box 366528  
San Juan, PR 00936-6528

Agricultural Services and  
Development Administration  
PO Box 9200  
San Juan, PR 00908-0202

Commercial and Farm Credit and  
Development Corporation for  
Puerto Rico  
PO Box 195009  
San Juan, PR 00936-5009

Trust for the Development,  
Operation and Conservation of  
National Parks of Puerto Rico  
PO Box 363332  
San Juan, PR 00936-3332

Recreational Development Company  
of Puerto Rico  
PO Box 3207  
San Juan PR 00904-3207

The financial statements of the discretely presented component units have a year end of June 30, 1997 except for Puerto Rico Telephone Authority and Sugar Corporation of Puerto Rico which have a year end of December 31, 1996.

**C. Basis of Presentation**

The Commonwealth reports its financial position and results of operations in funds and account groups, each of which is considered an independent fiscal entity, 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 that comprise its assets, liabilities, fund equity, revenues and expenditures/expenses. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds are maintained consistent with legal and managerial requirements. Account groups are a reporting device to account for certain assets and liabilities of the governmental funds not recorded directly in those funds. They are not considered funds because they do not report expendable available financial resources and related liabilities. For financial reporting purposes, the Commonwealth's reporting entity is divided into the primary government and its component units. Individual funds of the primary government are classified into three type categories: governmental funds, proprietary funds and fiduciary funds. Discretely presented component units are classified into public university funds, the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation (an entity reported on the liquidation basis) and component units - other.

The Commonwealth has established the following fund categories, fund types, account groups and discrete presentation of component units:

**1. Governmental Fund Types:**

Governmental funds are used to account for the general government functions of the Commonwealth. The following are the Commonwealth's governmental fund types:

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.

Debt Service Funds - The debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs other than bonds payable from the operations of proprietary fund types, nonexpendable 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.

Capital Projects Funds - Capital projects funds are used to account for the financial resources used for acquisition or construction of major capital facilities not financed by proprietary fund types, nonexpendable trust funds and discretely presented component units.

**2. Proprietary Fund Type:**

Proprietary funds are used to account for activities that are similar to those found in the private sector where net income and capital maintenance are measured. The enterprise fund is the Commonwealth's only proprietary fund, and is used to account for operations that are financed and operated in a manner similar to private business enterprises. Costs of providing goods and services to the general public on a continuing basis, including depreciation, are financed or recovered primarily through user charges.

**3. Fiduciary Fund Types:**

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

Expendable Trust Funds - are used to account for trusts which principal and income may be expended for their designated purpose.

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.

4. **Account Groups:**

Account groups establish control and accountability over the Commonwealth's general fixed assets and general long-term obligations.

**General Fixed Assets Account Group** - This account group is used to account for general fixed assets of the Commonwealth, and excludes the fixed assets held by the proprietary funds and discretely presented component units.

**General Long-Term Debt Account Group** - This account group is used to account for long-term obligations of the Commonwealth including bonds, appropriation and revenue bonds and long-term notes payable, obligations under lease/purchase agreements, net pension obligation, and other long-term liabilities excluding the liabilities of proprietary funds, public university funds and discretely presented component units.

5. **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 Governmental Accounting Standards Board Statement No. 14, *The Financial Reporting Entity*, with the funds and account groups of the primary government. The following are the Commonwealth's discrete presentation columns:

**Public University Funds** - are used to account for the activities of the University of Puerto Rico and the University of Puerto Rico Retirement System.

**Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation** - This discretely presented component unit is reported in a separate column and a separate statement of activity because its financial statements have been prepared in accordance with the liquidation basis of accounting, as required by generally accepted accounting principles.

**Component Units - Other** - are used to account for the financial activities of the Commonwealth's discretely presented component units, excluding public university funds and the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation. The financial statements of these component units are presented in accordance with the appropriate accounting methods as discussed below.

D. **Basis of Accounting**

The basis of accounting determines when the Commonwealth recognizes revenues and expenditures or expenses and related assets and liabilities.

The modified accrual basis of accounting is followed by governmental fund types, expendable trust funds and agency funds. Under the modified accrual basis of accounting, revenues are recorded when they become measurable and available to pay liabilities of the current period. Tax revenues, net of estimated overpayments (refunds), are recorded by the Commonwealth as taxpayers earn income (income and unemployment), as sales are made (consumption and use taxes) and as cash is received (miscellaneous taxes).

In applying the susceptible to accrual concept to intergovernmental revenues, there are essentially two types of revenues. For the majority of grants, monies must be expended by the Commonwealth on the specific purpose or project before any amounts will be reimbursed. Revenues are, therefore, recognized as expenditures are incurred. For the other revenues, monies are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria is met.

Expenditures and related liabilities are recorded in the accounting period in which the liability is incurred, except for (1) principal payment and interest on long-term obligations, which is recorded when due, except for principal and interest due during July of the following fiscal year which is recorded when resources are available in the debt service funds and (2) vacation, sick leave, federal funds cost disallowances and amounts subject to judgments under litigation which are recorded in the general long-term debt account group.

The Commonwealth reports deferred revenues on its combined balance sheet. Deferred revenues arise when a potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenues also arise when resources are received before the Commonwealth has a legal claim to them, as when grant monies 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 to the resources, the liability for deferred revenues is removed from the combined balance sheet and the revenue is recognized.

The accrual basis of accounting is used by proprietary fund types and pension trust funds. 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. The accrual basis is also used by the public university funds, except that depreciation of fixed assets is not required to be recorded.

The public university funds include the University of Puerto Rico, and the University of Puerto Rico Retirement System. The University reports using the AICPA Audit and Accounting Guide model defined by Governmental Accounting Standards Board Statement No. 15, *Governmental College and University Accounting and Financial Reporting Models*. Accordingly, the public university funds are an aggregate of the following funds: current funds - restricted and unrestricted; loan funds; endowment and similar funds; plant funds; agency funds; and the activities of the retirement system. The Retirement System is a defined benefit single employer retirement plan and, therefore, follows the accounting and reporting practices applicable to public employees' retirement system.

The financial statements of the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation have been prepared on the liquidation basis of accounting, as required by generally accepted accounting principles, for entities under a liquidation process. Under this basis, assets held for sale are accounted for at its net realizable value, and liabilities at its current values. When liquidation concludes, fixed assets not held for sale will be transferred to the Commonwealth's general fixed assets account group. An allowance has not been recognized to account for the estimated expenses to be incurred in the disposition of assets because these cannot be readily determined. Additions and deductions to net assets are accounted for under the accrual basis of accounting. Additions are recorded when earned, and deductions are recorded at the time liabilities are incurred.



The Commonwealth's primary government and the blended component units have elected not to follow Financial Accounting Standards Board (FASB) pronouncements issued subsequent to November 30, 1989 for its proprietary fund types, as allowed by Statement No. 20 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. However, certain discretely presented component units have disclosed their election in their separately issued financial statements.

The component units - other follow generally accepted accounting principles as issued by the Governmental Accounting Standards Board (GASB), and the Financial Accounting Standards Board (FASB) as applicable to each component unit based on the nature of their operations. Certain discretely presented component units also follow specialized accounting and financial reporting practices, such as banking, insurance, telecommunications, public utilities and higher education. In addition, the Puerto Rico Government Investment Trust Fund follows the specialized accounting and reporting practices for investment companies.

**E. Statutory (Budgetary) Accounting**

The Commonwealth's budget is adopted in accordance with a statutory basis of accounting which is not in accordance with GAAP. Revenues are generally recognized when cash is received. However, revenues receivable for federal grants and reimbursements are recognized when related expenditures are incurred. Amounts due from certain political subdivisions of the Commonwealth are recognized when considered measurable and available at year end.

Expenditures are generally recorded when the related cash disbursement occurs. At year end, payroll is accrued and payables are recognized, to the extent of approved encumbrances, provided that the goods or services have been received by June 30. Available appropriations and encumbrances lapse three years after the end of the fiscal year. Amounts required to settle 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 combined statement of revenues and expenditures-budget and actual - budget basis-general and debt service funds, only present the information for those funds for which there is a legally adopted budget, as required by generally accepted accounting principles. See Note 3 for a reconciliation of the combined statement of revenues and expenditures - budget and actual - budget basis-general and debt service funds with the combined statement of revenues, expenditures and changes in fund balance (deficit), for the general and debt service funds.

**F. Cash, Cash Equivalents and Short Term-Investments**

The Commonwealth follows the practice of pooling 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 with the Government Development Bank for Puerto Rico, and with the Puerto Rico Government Investment Trust Fund.

Cash and cash equivalents include investments with original maturities of ninety days or less.

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.

Short-term investments are stated at cost or amortized cost.

**G. 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 with a corresponding liability. The securities underlying these agreements mainly consist of US Government obligations, mortgage-backed securities, and interest-bearing deposits with other banks.

**H. 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.

**I. Investments**

As described in Note 5, investments include US Government and agencies obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. Investments are reported at cost or amortized cost, except for investments of the pension trust funds, the University of Puerto Rico and the University of Puerto Rico Retirement System deferred compensation funds, and investments of certain component units with trading securities and investments held for sale which are reported at fair value.

**J. Receivables**

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

The loan funds of the public university funds are stated net of uncollectible amounts.

The mortgage notes receivable of the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation are stated net of uncollectible amounts. Interest income on mortgage notes receivable is recorded on the cash basis of accounting due to the high delinquency rate of the related loans and the risk of possible losses in the collection of such interest.

The accounts receivable from nongovernmental customers of the component units - other 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.

**K. Contribution in Lieu of Taxes**

Certain component units are required, by local laws, to contribute a specific percentage of their revenues as payment in lieu of taxes to the Commonwealth and the municipalities of Puerto Rico. During the year ended June 30, 1997, the Commonwealth received payments in lieu of taxes of approximately \$56.7 million, which have been included as operating transfers-in from component units.

**L. Inventories**

The proprietary fund types, public university funds and component units - other recognize an asset when the inventory is purchased and an expense when it is consumed. Inventories in proprietary fund types are primarily valued at the lower of cost or market using the first-in, first-out method.

**M. Restricted Assets**

Funds set aside by the general fund for payment and guarantee of notes and interest payable are classified as restricted assets since their use is limited for this purpose by applicable debt agreements. Restricted assets in the proprietary fund types mainly include amounts set aside for the payment of lottery prizes. Restricted assets in the public university funds and in the component units - other column are set aside primarily for the payment of bonds, notes, construction funds, and other specific purposes. (See Note 10).

**N. Housing Units and Land Lots Held for Sale**

Housing units and land lots held for sale of the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation are stated at its estimated net realizable value determined by the Office's management based on previous housing units sales or appraisal values.

**O. Fixed Assets**

For governmental fund types, general fixed asset acquisitions are recorded as expenditures in the acquiring fund and capitalized in the general fixed assets account group in the year purchased. General fixed assets are recorded at historical cost, or at estimated historical cost if actual historical cost is not available. Donated fixed assets are recorded at fair market value at the time of donation. Interest costs are capitalized during the construction period. The costs of normal maintenance and repairs that do not add value to the asset or materially extend asset lives are not capitalized. Public domain general fixed assets (infrastructure) consisting of roads, bridges, streets, sidewalks, drainage and lighting systems are not capitalized as these assets are immovable and of value only to the government.

Fixed assets of the proprietary fund types and similar trust funds are stated at cost or estimated historical cost. Contributed fixed assets are recorded at estimated fair market value at the time received. Interest costs are capitalized on projects during the construction period. Depreciation is provided using the straight-line method over the estimated useful lives of the assets.

The estimated useful lives of fixed assets are as follows:

	Years
Buildings	25 - 50
Building improvements	10 - 20
Equipment, furniture, fixtures and vehicles	3 - 10

Fixed assets of the public university funds are stated at cost or fair value at the date of donation in the case of gifts. Interest costs are capitalized during the construction period. Depreciation on physical plant and equipment is not recorded, except for equipment of auxiliary enterprises and of the University Pediatric Hospital.

Fixed assets not held for sale of the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation (the Office) are stated at cost. Depreciation is provided over the estimated useful lives of the assets using the straight-line method. Housing units and land lots for sale is stated at its estimated realizable value determined by the Office management based on similar housing units sales, commitments, and appraisal values.

The fixed assets of the component units - other are recorded in accordance with the applicable standards. 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.

**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.

**Q. Long-Term Debt**

The liabilities reported in the general long-term debt account group include the Commonwealth's general obligation bonds and long-term notes, obligations under lease/purchase agreements and other long-term liabilities including vacation, sick leave, litigation, long-term liabilities to other governmental entities, net pension obligation, and non-current federal fund cost disallowances related to expenditures of federal grants. Long-term obligations financed by proprietary fund types, public university funds, Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, and component units - other are recorded as liabilities in those funds and discretely presented component unit columns.

**R. Reservations of Fund Balance**

Reservations of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriable for expenditure. The Commonwealth has the following reservations of fund balance:

Encumbrances - Represent future expenditures under purchase orders and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

Debt Service - Represents net assets available to finance future debt service payments.

Unemployment Benefits - Represent net assets available to fund future unemployment benefits payments.

Employee Pension Benefits - Represents the net assets available for pension benefits in the pension plans.

Advances and Other Specified Purposes - Represent the reservation of monies set aside for long-term receivables which are not considered current financing resources, the guarantee of notes payable, disability and drivers insurance, long-term assets, construction commitments, endowment and amounts available to fund various fiduciary arrangements.

Net Assets Available in the Investment Trust Fund - The net assets available in the investment trust fund represents the value of the investments held by the Puerto Rico Government Investment Trust Fund, a discretely presented component unit. (See Note 4).

Net Assets in Liquidation - The net assets in liquidation for the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation represent the dollar amount of the net assets available for sale or transfer, as required by generally accepted accounting principles applicable to entities under liquidation. As established by Law 181 of August 12, 1995, any surplus of funds that remain after the final sale and transfer of assets and after the payment of operational expenses, shall be transferred to the General Fund of the primary government.

**S. Unrealized Gain (Loss) in Value of Debt and Equity Securities**

Certain component units report an unrealized gain (loss) in value of debt and equity securities. This represents the cumulative effect of the accounting and reporting requirements of Financial Accounting Standards Board Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

**T. Bond Premiums, Discounts and Issuance Cost**

For governmental fund types, bond premiums and discounts, as well as issuance costs, are recognized during the current period. Bond proceeds are reported as other financing sources net of the applicable premium or discount. Issuance cost, whether or not withheld from the actual net proceeds received, are reported as debt service expenditures. For proprietary fund types, bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the interest method. Bonds payable are reported net of the applicable bond premium or discount. Issuance costs are reported as deferred charges. Public university funds present bond premiums and discounts in the net investment in plant fund and are amortized using the interest method. Component units - other follow appropriate statements.

**U. Accounting for Pension Costs**

For the purpose of applying the requirements of Governmental Accounting Standards Board Statement No. 27, (SGAS), *Accounting for Pensions by State and Local Government Employers* the Commonwealth's financial reporting entity is considered to be a participant in three single-employer defined benefits pension plans: Employees Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS); Puerto Rico Judiciary Retirement System (JRS); and the Puerto Rico System of Annuities and Pensions for Teachers (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 general purpose financial statements, and as disclosed in Note 22, the Commonwealth's annual pension cost, measured on the accrual basis of accounting, for the year ended June 30, 1997 amounted to approximately \$782 million. However, the amount recognized as pension expenditure in the governmental funds, (excluding blended component units)

was recorded under the modified accrual basis, and amounted to approximately \$543 million. The excess of the annual required contribution over the statutorily required contributions of approximately \$239 million increased the net pension obligation at June 30, 1997 to approximately \$1.8 billion. This amount is presented in the general long-term debt account group at June 30, 1997.

For purposes of the stand-alone financial statements of each of the blended and discretely presented component units - other, 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 contractually required contributions.

In addition, the University of Puerto Rico, which is reported in the public university funds, applied the provisions of SGAS 27 as it is applicable to an entity with a single-employer defined benefits pension plan.

#### **V. Deferred Compensation Plan**

The University of Puerto Rico, offers certain employees a non-qualified deferred compensation plan which was created pursuant to Certification No. 94 of the Council of Higher Education, dated February 13, 1984. The plan, managed by independent plan administrators, permits employees to defer a portion of their salary until future years. At the employee's election, such amounts may be invested in mutual funds which represent varying levels of risk and return. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency. All amount of compensation deferred under the plans, all property and rights purchased with those amounts, and all income attributable to these amounts, are (until paid or made available to the employee or other beneficiary) solely the property and rights of the University (without being restricted to the provisions of benefits under the plan), subject only to the claims of the University's general creditors. Participant's rights under the plan are equal to those of general creditors of the University in an amount equal to the fair market value of the deferred account for each participant. It is the opinion of the University's legal counsel that the University has no liability for the losses under the plan but does have the duty of care that would be required of an ordinary prudent investor. The University believes that it is unlikely that it will use the assets of the plan to satisfy the claims of general creditors in the future.

#### **W. Postemployment Benefits**

In addition to the pension benefits described in Note 22, the Commonwealth provides postemployment health care 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. Health care benefits are provided through insurance companies whose premiums are paid by the retiree with the Commonwealth providing a matching share of not more than \$40 per month for each retiree. During the year ended June 30, 1997, the cost of providing health care benefits amounted to approximately \$28.9 million for approximately 62,000 retirees. The Christmas bonus paid to the

retired employees during the year ended June 30, 1997 was \$150 per retiree and the total amount was approximately \$11.9 million for approximately 80,000 retirees. These benefits are recorded as expenditures when paid in the general fund.

#### X. 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 sick leave at the current rate, if the employee has at least ten years of service with the Commonwealth.

Compensated absence accumulation policies for the blended component units, the public university funds, the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, and component units - other vary from entity to entity based on negotiated agreements and other factors agreed upon between the management of these entities and its employees.

Subsequent to June 30, 1997, the Commonwealth amended the *Public Service Personnel Law* to allow certain component units and the executive agencies of the Commonwealth to annually pay the employees the accumulated vacation and sick leave earned in excess of the limits mentioned above.

#### Y. Interfund and Intra-Entity Transactions

The Commonwealth has the following types of transactions among funds:

Operating Transfers - Legally required transfers that are reported when incurred as "Operating transfers-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.

Interfund Payments (Quasi-external Transactions) - Charges or collections for services rendered by one fund to another that are recorded as revenues of the recipient fund and as expenditures or expenses of the disbursing fund.

Intra-Entity Transactions - There are three types of intra-entity transactions. First are transactions between the primary government and its component units, and among the component units. Transfers between the primary government and its other funds are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds. Balances and transfers between the primary government and discretely presented component units (and among those component units) are reported separately from balances with blended component units.

Second are intra-entity balances that do not represent available/demands on current financial resources of governmental funds and are generally of intermediate terms. These balances are reported as interfund advances.

Third are intra-entity balances between the primary government funds and component unit-other entities that are tantamount to long-term bond financing. The primary government's liability is reported in the long-term debt account group, the proceeds in the primary government's fund balances, and the asset in the component unit-other.

Residual Equity Transfers - These are nonrecurring or non routine transfers of equity between funds.

## **Z. Lottery Revenues and Prizes**

The revenues, expenses and prizes awarded by the Lottery of Puerto Rico, and the Additional Lottery System, are reported within the enterprise funds and are recognized as drawings are held. Monies collected prior to June 30 for tickets related to drawings to be conducted subsequent to June 30 are reported as deferred revenues. Unpaid prizes awarded as of June 30 are reported as a fund liability. For prizes payable in installments, the Commonwealth purchases annuities through the Government Development Bank for Puerto Rico, which are reported as restricted assets and lottery prizes payable.

## **AA. Public University Funds**

Financial activities of the University of Puerto Rico (the University) and the University of Puerto Rico Retirement System (the System) are reported in the public university funds. Such funds are discretely presented in a separate column in the general purpose financial statements and represent the combination of the following funds of the University:

Current Funds - Account for resources that may be used for any purpose in carrying out the primary objectives of the University.

Loan Funds - Account for resources available for loans to students, faculty, or staff of the University.

Endowment and Similar Funds - Account for endowment and quasi-endowment transactions. These funds are similar to trust funds and the University must comply with the terms of any applicable agreement.

Plant Funds - Account for transactions involving physical facilities of the University. The investment in plant accounts for funds expended and, thus, invested for property and any related outstanding debt.

Agency Funds - Account for resources held by the University as custodian or agent for others.

The combined statement of current funds revenues, expenditures and other changes - public university funds is a statement of financial activities related to the current reporting period. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

The public university funds measurement focus is based upon determination of resources received and used. Current funds used to finance plant assets are accounted for as (1) expenditures, for normal replacement of movable equipment and library books; (2) mandatory transfers, for required provisions for debt amortization/interest and equipment renewal and replacement; and (3) transfers of a nonmandatory nature for all other cases.

Public university funds record expenditures when they acquire fixed assets and capitalize those assets within the plant funds. These funds capitalize interest expenditures during construction but do not record depreciation.



**AB. Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**AC. Future Adoption of Accounting Pronouncements**

The Governmental Accounting Standards Board has issued the following statements which the Commonwealth, or its component units, have not yet adopted.

Statement No.		Adoption required in fiscal year
31	Accounting and Financial Reporting for Certain Investments and for External Investments Pools	1998

The impact of this statement has not yet been determined.

**AD. Risk Financing**

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

Most component units carry commercial insurance as part of their risk financing programs. Certain other component units combine commercial insurance with internal self-insurance funds covering specific risks related to their specialized operations.

**AE. Reclassifications**

Certain reclassifications have been made to the information presented in the separately issued financial statements of certain component units included within the debt service, capital projects, enterprise, expendable trust, pension trust, public university, the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation, and discretely presented component units to conform to the accounting classifications used by the Commonwealth in the general purpose financial statements.

**AF. Totals Columns (Memorandum Only)**

Total columns on the combined financial statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis. Data in these columns does not present consolidated financial position, results of operations, or cash flows in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation since interfund eliminations have not been made.

## 2. COMPONENT UNITS

The Commonwealth follows the provisions of Governmental Accounting Standards Board Statement No. 14, *The Financial Reporting Entity*. The general purpose financial statements include the financial statements of the following component units that were audited by other auditors:

Agricultural Services and Development Administration  
Automobile Accident Compensation Administration  
Employment and Training Enterprises Corporation and Subsidiary  
Farm Credit Guarantee Fund and Guarantee Loan Fund for Eligible  
Businesses of Puerto Rico  
Farm Insurance Corporation of Puerto Rico  
Fine Arts Center Corporation  
Industries for the Blind, Mentally Retarded and Other Disabled Persons  
of Puerto Rico  
Institutional Trust of the National Guard of Puerto Rico  
Land Authority of Puerto Rico  
Musical Arts Corporation and Subsidiaries  
Office for the Liquidation of the Accounts of the PR Urban Renewal  
and Housing Corporation  
Puerto Rico School of Plastic Arts  
Puerto Rico Aqueduct and Sewer Authority  
Puerto Rico and Caribbean Cardiovascular Center Corporation  
Puerto Rico Electric Power Authority  
Puerto Rico Housing Bank and Finance Agency  
Puerto Rico Industrial Development Company  
Puerto Rico Land Administration  
Puerto Rico Medical Services Administration  
Puerto Rico Metropolitan Bus Authority  
Puerto Rico Public Broadcasting Corporation  
Recreational Development Company of Puerto Rico  
Right to Employment Administration  
Puerto Rico Solid Waste Authority  
Sugar Corporation of Puerto Rico  
Tourism Company of Puerto Rico  
Trust for the Development, Operation and Conservation of National  
Parks of Puerto Rico  
University of Puerto Rico  
University of Puerto Rico Retirement System

Condensed financial information of the major discretely presented component units-other are presented on the following two pages (expressed in thousands).

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Government Investment Trust Fund	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
<b>Balance Sheet</b>											
<b>Assets and Other Debits</b>											
Current assets	\$ 421,965	\$ 684,273	\$ 103,392	\$ 440,366	\$ 3,104	\$ 99,683	\$ 98,571	\$ 155,811	\$ 29,146	\$ 654,644	\$ 2,690,955
Investments	2,974,741			96,649	621,859		1,041,234	517,829		345,752	5,598,064
Due from:		64,973									
Primary government										30,167	95,140
Component units								797		8,021	8,818
Other governmental entities										77,564	77,564
Advances to:											
Primary government	1,279,632										1,279,632
Component units	1,216,822	677									1,234,670
Other governmental entities	326,706										326,706
Restricted assets:											
Cash and cash equivalents	1,302,790	668,269	150	81,544		239,604				123,106	362,860
Other restricted assets			31,049			635,077			55,425	844,569	3,618,723
Housing units and land lots held for sale										132,433	132,433
Fixed assets, net		3,263,107	3,471,500	1,946,955		1,019	27,667	1,829	516,784	1,138,110	10,366,971
Amount available in debt						36,766				24,088	60,854
service funds											
Amount to be provided for										369,990	369,990
the retirement of bonds											
and notes payable											
Amount to be provided for											
payment of accrued											
compensated absences											
and other long-term debt											
<b>Total</b>	<b>\$ 7,522,656</b>	<b>\$ 4,681,299</b>	<b>\$ 3,606,091</b>	<b>\$ 2,565,514</b>	<b>\$ 624,963</b>	<b>\$ 1,318,331</b>	<b>\$ 1,167,472</b>	<b>\$ 693,437</b>	<b>\$ 601,355</b>	<b>\$ 3,760,793</b>	<b>\$ 26,541,911</b>
<b>Liabilities and Fund Equity</b>											
Current liabilities	\$ 4,015,466	\$ 661,617	\$ 332,546	\$ 380,284	\$ 764	\$ 271,298	\$ 1,041,854	\$ 576,222	\$ 43,614	\$ 739,189	\$ 8,062,854
Due to:											
Primary government											39,374
Component units											21,238
Other governmental entities											1,444
Advances from:											
Primary government											1,557
Component units	1,191,317	15,000	689,408			21,994			26,516	454,755	1,207,673
Notes payable	1,037,953	125,000	72,434	9,380				42,000	10,537	185,668	1,636,336
Bonds payable		3,511,102	438,349	901,268		755,873			158,394	993,690	7,796,629
Other liabilities						43,776				12,305	56,081
Other long-term liabilities		3,118		76,784		2,884				215,539	298,325
Net pension obligation		21,759		12,504							34,263
<b>Total liabilities</b>	<b>6,244,736</b>	<b>4,337,596</b>	<b>1,532,737</b>	<b>1,380,220</b>	<b>764</b>	<b>1,095,825</b>	<b>1,041,854</b>	<b>618,222</b>	<b>239,061</b>	<b>2,664,759</b>	<b>19,155,774</b>
<b>Fund equity</b>	<b>1,277,920</b>	<b>343,703</b>	<b>2,073,354</b>	<b>1,185,294</b>	<b>624,199</b>	<b>222,506</b>	<b>125,618</b>	<b>75,215</b>	<b>362,294</b>	<b>1,096,034</b>	<b>7,386,137</b>
<b>Total</b>	<b>\$ 7,522,656</b>	<b>\$ 4,681,299</b>	<b>\$ 3,606,091</b>	<b>\$ 2,565,514</b>	<b>\$ 624,963</b>	<b>\$ 1,318,331</b>	<b>\$ 1,167,472</b>	<b>\$ 693,437</b>	<b>\$ 601,355</b>	<b>\$ 3,760,793</b>	<b>\$ 26,541,911</b>

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Government Investment Trust Fund	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
Operating revenues	\$ 460,591	\$ 1,637,802	\$ 308,700	\$ 1,175,528	\$ 46,239	\$ 47,454	\$ 430,125	\$ 59,229	\$ 50,025	\$ 741,045	\$ 4,956,738
Operating expenses	334,941	1,365,863	395,629	964,160	1,954	45,788	474,527	68,080	37,279	1,465,261	5,153,482
Operating income (loss)	125,650	271,939	(86,929)	211,368	44,285	1,666	(44,402)	(8,851)	12,746	(724,216)	(196,744)
Non-operating revenues (expenses)		(279,304)	1,688	(50,398)		3,693	76,115	9,020	(8,171)	37,241	(210,116)
Income (loss) before operating transfers	125,650	(7,365)	(85,241)	160,970	44,285	5,359	31,713	169	4,575	(686,975)	(406,860)
Transfers from (to):											
Primary government			30,000	(41,873)			(22,347)			682,997	648,777
Component units				(15,500)						(6,015)	(21,515)
Transfers, net			30,000	(57,373)			(22,347)			676,982	627,262
Net income (loss)	125,650	(7,365)	(55,241)	103,597	44,285	5,359	9,366	169	4,575	(9,993)	220,402
Excess of revenues over expenditures from governmental operations											
Contributions						18,023				(9,385)	8,638
Withdrawals					(689,905)					86	86
Depreciation on fixed assets acquired through contributed capital			48,520							2,747	51,267
Increase (decrease) in retained earnings (deficit) fund balance	125,650	(7,365)	(6,721)	103,597	(645,620)	23,382	9,366	169	4,575	(16,545)	(409,512)
Retained earnings (deficit) fund balance at beginning of year, as restated	27,715	211,085	298,896	1,056,735	1,269,819	69,806	102,252	22,910	43,246	(295,004)	2,807,460
Transfer to contributed capital	(100,000)									(2,457)	(102,457)
Retained earnings (deficit) fund balance at end of year	\$ 53,365	\$ 203,720	\$ 292,175	\$ 1,160,332	\$ 624,199	\$ 93,188	\$ 111,618	\$ 23,079	\$ 47,821	\$ (314,006)	\$ 2,295,491

Condensed financial statements of the public university funds are as follows (expressed in thousands):

	University of Puerto Rico	Retirement System	Eliminations	Total
<b>ASSETS</b>				
Current assets	\$124,422	\$509,601	\$	\$ 634,023
Due from other funds		351	(351)	
Due from primary government	34,016			34,016
Restricted assets:				
Cash and cash equivalents	64,863	7,000		71,863
Other restricted assets	100,218	2,379		102,597
Fixed assets - net	<u>625,430</u>	<u>204</u>		<u>625,634</u>
 Total Assets	 <u>\$948,949</u>	 <u>\$519,535</u>	 <u>\$ (351)</u>	 <u>\$1,468,133</u>
<b>LIABILITIES AND FUND EQUITY</b>				
Current liabilities	\$ 77,489	\$ 13,868	\$	\$ 91,357
Due to other funds	351		(351)	
Bonds payable	324,974			324,974
Other liabilities	97,504	201		97,705
Net pension obligation	<u>31,273</u>			<u>31,273</u>
 Total Liabilities	 531,591	 14,069	 (351)	 545,309
 Fund Equity	 <u>417,358</u>	 <u>505,466</u>	 <u></u>	 <u>922,824</u>
 Total Liabilities and Fund Equity	 <u>\$948,949</u>	 <u>\$519,535</u>	 <u>\$ (351)</u>	 <u>\$1,468,133</u>

### 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 Office of Management and Budget, and takes into consideration the advice provided by the Planning Board (annual economic growth forecasts; four year capital improvements plan), the Department of the Treasury (revenue estimates; accounting and the comprehensive annual financial report), the Government Development Bank for Puerto Rico (fiscal agent) and the 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 revenues, 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-base budgeting, includes an estimate of revenues and other resources for the ensuing fiscal year under (i) laws existing at the time the budget is submitted and (ii) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in his judgment are necessary, convenient, and in conformity with the four-year investment plan adopted by the 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 to cover such deficit. Upon approval by the Legislature, the budget is referred to the Governor who may decrease or eliminate any line items 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 his 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 originally 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 Legislature made several supplemental budgetary appropriations to the general fund throughout the year, amounting to approximately \$1.9 billion.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse three years after the end of such fiscal year or at the date prescribed by the Secretary of the Treasury. Others 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 revenues 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 departmental appropriation account. However, the Commonwealth is statutorily required to pay debt service, regardless of whether such amounts are appropriated.

Appropriations are enacted for certain of the departmental accounts included in the combined balance sheet for the general fund, and debt service funds. For these funds, a Combined Statement of Revenues and Expenditures - Budget and Actual - Budget Basis - Budgeted General, and Debt Service Funds is included.

Appropriations for capital projects are made for each bond issue and the authorization continues for the expected construction period. The Commonwealth's Treasury Department and the Office of Management and Budget (OMB) have the responsibility to ensure that budgetary spending control is maintained on an individual departmental appropriation account basis. The OMB may transfer part or all of any unencumbered balance within a department or from one department to another subject to Legislature approval. Budgetary control is exercised through the Commonwealth Integrated Financial Accounting System (CIFAS). CIFAS ensures that encumbrances or expenditures are not processed if they exceed the appropriation account's total available spending authorization, which is considered its budget. The legal level of budgetary control is at individual department level for general fund expenditures and by bond authorization for capital expenditures.

**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 revenues and other sources of financial resources over expenditures and other uses of financial resources for the year ended June 30, 1997 is presented below for the general, and debt service funds (expressed in thousands):

	<b>General</b>	<b>Debt Service</b>
Excess of revenues and other sources over expenditures and other uses - budget basis	\$ 124,820	\$ (25,393)
Entity differences:		
Excess (deficiency) of revenues and other sources over expenditures and other uses for:		
Non-budgeted amounts	(54,116)	
Inclusion of blended component units		87,590
Timing differences:		
Adjustment to encumbrances	95,160	
Basis of accounting differences:		
Net decrease in taxes receivable	(5,497)	
Net increase in other receivables and other assets	11,579	28,518
Net (increase) decrease in accounts payable and other liabilities	<u>(205,457)</u>	<u>3,228</u>
Excess of revenues and other financing sources over expenditures and other financing uses (GAAP basis)	<u>\$ (33,511)</u>	<u>\$ 93,943</u>

**C. Deficit Fund Equity**

The following component units reflect a deficit fund balance or retained earnings at June 30, 1997 (expressed in thousands):

Enterprise Funds:

Health Facilities and Services Administration of Puerto Rico	\$ 688,571
Additional Lottery System	1,365

The Commonwealth has committed to continue providing financial support for the Health Facilities and Services Administration in the form of operational subsidies.

Component Units - Other:

Tourism Company of Puerto Rico	\$208,112
Sugar Corporation of Puerto Rico	153,717
Land Authority of Puerto Rico	146,804
Puerto Rico Ports Authority	53,454
Puerto Rico Metropolitan Bus Authority	49,942
Agricultural Services and Development Administration	20,883
Commercial and Farm Credit and Development Corporation of Puerto Rico	19,206
Corporation of Stocks and Deposits Insurance for the Savings and Loan Cooperatives	19,171
Recreational Development Company of Puerto Rico	18,159
Employment and Training Enterprises Corporation and Subsidiary	4,246
Farm Credit Guarantee Fund and Guarantee Loan Fund for Eligible Businesses of Puerto Rico	2,658
Puerto Rico and Caribbean Cardiovascular Center Corporation	1,502
Fine Arts Center Corporation	1,098
Puerto Rico Conservatory of Music Corporation	1,017

These entities are designing plans that will either increase revenues or decrease expenditures in order to cover these deficits.

**4. PUERTO RICO GOVERNMENT INVESTMENT TRUST FUND**

The Puerto Rico Government Investment Trust Fund (Trust Fund), a discretely presented component unit, was created by the Secretary of the Treasury of the Commonwealth pursuant to Act No. 176, of August 11, 1995, and began operations on December 4, 1995. The Trust Fund is a no-load diversified collective investment trust that was created for the purpose of providing eligible investors (mainly composed of component units and the municipalities of Puerto Rico) 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 investment securities on hand at June 30, 1997 consisted of bankers' acceptances, certificates of deposits, bank notes, corporate obligations, commercial paper and US Government and agencies obligations, all of which may be considered highly-liquid. However, the participants' investments are subject to the ability of the Trust Fund to receive payment for the securities' issuer when due. The liquidity of certain investments, and changes in interest rates, may affect the Trust Funds' yield and the fair value of its investments.

Following is key financial information for the year ended June 30, 1997 (expressed in thousands):

Deposits at June 30, 1996	\$1,269,819
Deposits received from participants	1,058,690
Net earnings reinvested	44,285
Withdrawals	<u>(1,748,595)</u>
Deposits at June 30, 1997	<u>\$ 624,199</u>



The deposits at June 30, 1997 and 1996 were invested in securities with a cost which approximates fair value, plus accrued interest, for approximately \$624 million and \$1.27 billion, respectively.

In addition to the Trust Fund being reported in the component units-other column, the dollar amount of deposits on hand at June 30, 1997, at \$1.00 per unit of participation, was reported in the individual component units financial statements of each of the participants, and combined in the general purpose financial statements as follows (expressed in thousands):

	Balance Outstanding	Percentage of Total
<b><u>Primary Government:</u></b>		
Commonwealth	\$ 323,385	51.81%
Public Buildings Authority	84,177	13.49%
Employees Retirement System of the Government of PR and Its Instrumentalities	<u>35,748</u>	<u>5.73%</u>
Total for primary government	<u>443,310</u>	<u>71.03%</u>
<b><u>Public University Funds:</u></b>		
University of Puerto Rico	<u>2,397</u>	<u>0.38%</u>
<b><u>Discretely Presented Component Units:</u></b>		
State Insurance Fund Corporation	54,177	8.68%
Puerto Rico Housing Bank and Finance Agency	43,776	7.01%
Recreational Development Company of Puerto Rico	38,377	6.15%
Puerto Rico Land Administration	26,002	4.17%
Government Development Bank for PR and Subsidiaries	7,449	1.19%
Corporation of Stocks and Deposits Insurance for the Savings and Loans Cooperatives	4,770	0.76%
Institutional Trust of the National Guard of PR	2,366	0.38%
Puerto Rico Ports Authority	487	0.08%
Puerto Rico Plastic Arts School	<u>111</u>	<u>0.02%</u>
Total for discretely presented component units	<u>177,515</u>	<u>28.44%</u>
<b>Other:</b>		
Municipalities	<u>977</u>	<u>0.15%</u>
Total for all participants	<u>\$ 624,199</u>	<u>100%</u>

## 5. 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, or an agent, in the Commonwealth's name. In addition, the Commonwealth maintains deposits with the Government Development Bank for Puerto Rico and the Economic Development Bank for Puerto Rico, two discretely presented component units, and the United States Government (for unemployment insurance).

Cash, cash equivalents and investments of the primary government at June 30, 1997 consist of (expressed in thousands):

### Primary Government

	Unrestricted	Included in Debt Service	Included in Capital Projects	Included in Trust and Agency	Included in Restricted Assets	Total
Cash and cash equivalents	\$ 298,471	\$ 76,076	\$ 924,406	\$ 751,397	\$	\$2,050,350
Cash and cash equivalents in governmental banks	54,461	306,035	114,185	750,339	574,512	1,799,532
Investments	<u>7,900</u>	<u>349,605</u>	<u>98,790</u>	<u>2,546,070</u>	<u>216,877</u>	<u>3,219,242</u>
Total	<u>\$ 360,832</u>	<u>\$ 731,716</u>	<u>\$1,137,381</u>	<u>\$4,047,806</u>	<u>\$ 791,389</u>	<u>\$7,069,124</u>

The Commonwealth's bank balance of deposits with financial institutions is categorized to provide an indication of the level of collateral 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 Treasury or by its agent 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 carrying amount of deposits with financial institutions of the primary government at June 30, 1997 consists of (expressed in thousands):

Carrying amounts of deposits in governmental banks	\$ 1,793,324
Carrying amount of deposits in commercial banks	1,400,321
Carrying amount of deposits in US Government	617,865
Cash equivalents disclosed as investment for GASB 9	(327,954)
Investments disclosed as cash equivalents for GASB 9	<u>366,326</u>
Total carrying amount of deposits as reported on the combined balance sheet	<u>\$ 3,849,882</u>

Bank balance of deposits in commercial banks:	
Category 1	\$ 1,369,655
Category 2	6,073
Category 3	<u>2,056</u>
Total bank balance of deposits in commercial banks	<u>\$ 1,377,784</u>

The amount of the bank balance of deposits in commercial banks uninsured or uncollateralized at June 30, 1997 shown above, belong to the Puerto Rico Public Building Authority.

The bank balance of deposits in governmental banks, which as of June 30, 1997, is uninsured and uncollateralized, is approximately \$2 billion. Such deposits are maintained in the Government Development Bank for Puerto Rico.

The deposit of approximately \$618 million with the US Government represents unemployment insurance taxes collected from employers which are transferred to the Federal Unemployment Insurance Trust Fund in the United States Treasury.

Deposits in governmental banks represent the balance of interest and non-interest bearing accounts in GDB. The deposit liability at GDB is substantially related to deposits from other component units and of the Commonwealth. Such deposit liability is not in agreement with governmental cash balances shown because of reconciling items such as outstanding checks and deposits in transit.

The bank balance of GDB's deposits at June 30, 1997 is broken down as follows (expressed in millions):

Primary government	\$ 2,066
Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation	7
Public university funds	17
Other discretely presented components units	<u>567</u>
Total reporting entity	2,657
Effect of the inclusion of financial statements of a component unit with different date of financial statements	101
Municipalities of Puerto Rico	517
Other non-governmental entities	134
Certificates of indebtedness	<u>168</u>
Total deposits per GDB	<u>\$ 3,577</u>

On February 22, 1996, the Board of Directors of the Government Development Bank for Puerto Rico adopted the *Statement of Investment Guidelines for the Government of Puerto Rico*. These guidelines promulgate a uniform investment policy for the Government of Puerto Rico. The guidelines under this statement are to be followed by municipalities, agencies and public corporations, public insurance companies and public retirement plans. These guidelines include the allowable and the prohibited assets that each governmental entity may invest, except for the Government Development Bank for Puerto Rico and the Economic Development Bank for Puerto Rico, which may establish their own investment policy with the approval of the Board of Directors of the Government Development Bank.

Pursuant to the Statement of Investment Guidelines, the agencies and public corporations may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposits, commercial paper, banker's acceptances, or in pools of obligations of the municipalities of Puerto Rico, among others.

The retirement systems may invest in stocks, corporate bonds, obligations of the United States, mortgage loans, private equity and others.

The Commonwealth's investments are categorized to provide an indication of the level of collateral 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 agent 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.

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

	1	Category 2	3	Carrying Amount	Fair Value
<u>Unrestricted</u>					
US Government and agencies securities	\$ 42,695	\$ 537,685	\$	\$ 580,380	\$ 580,370
Stocks	1,772,677	143,176		1,915,853	1,915,853
Corporate bonds	17,853			17,853	17,853
Repurchase agreements	7,900		40,437	48,337	48,337
Mortgage-backed securities	<u>50</u>	<u>          </u>	<u>          </u>	<u>50</u>	<u>50</u>
Subtotal	<u>1,841,175</u>	<u>680,861</u>	<u>40,437</u>	<u>2,562,473</u>	<u>2,562,463</u>
Investments not subject to categorization:					
Mortgage loans				9,620	
PR Government Trust Fund				443,310	443,310
Limited partnership/private equity				<u>3,683</u>	<u>          </u>
Total - unrestricted				<u>3,019,086</u>	<u>3,005,773</u>
<u>Restricted</u>					
US Government and agencies securities		36,354		36,354	36,354
Repurchase agreements	<u>21,651</u>	<u>          </u>	<u>          </u>	<u>21,651</u>	<u>21,651</u>
Subtotal	<u>21,651</u>	<u>36,354</u>	<u>          </u>	<u>58,005</u>	<u>58,005</u>
Investments not subject to categorization:					
Annuity contracts				<u>180,523</u>	<u>185,661</u>
Total - restricted				<u>238,528</u>	<u>243,666</u>
Total	<u>\$ 1,862,826</u>	<u>\$ 717,215</u>	<u>\$ 40,437</u>	<u>\$3,257,614</u>	<u>\$3,249,439</u>

The following schedule reconciles the carrying amount of investments as disclosed above to the combined balance sheet (expressed in thousands):

Carrying amount of investments	\$3,257,614
Cash equivalents disclosed as investments for GASB 9	327,954
Investments disclosed as cash equivalents for GASB 9	<u>(366,326)</u>
Investments reported on the combined balance sheet	<u>\$3,219,242</u>

Unrestricted investments include approximately \$323 million of deposits from the Commonwealth that are invested in the Puerto Rico Government Investment Trust Fund (See Note 4). Such amount has been included as cash and cash equivalents in the combined balance sheet.

Annuity contracts included as restricted investments are purchased from the Government Development Bank for Puerto Rico to fund Lotto prizes of \$200 thousand or more payable on an installment basis. Investments in zero coupon US Treasury strips (with maturity dates that coincide with pay-out schedules of the Lotto prizes) constitute collateral for the annuities. As of June 30, 1997, fair value of such collateral amounts to approximately \$186 million. Annuity contracts are recorded at present value of future installment prize payments. Interest earned is not recognized as revenue, but credited to obligations for unpaid prize awards.

Local laws require that annuity contracts be held until maturity, unless the prizes to which they relate are not claimed within the statutory period. If not claimed, the annuities are canceled and proceeds thereof are transferred to the General Fund.

**Public University Funds**

Cash and investments of the public university funds at June 30, 1997 consist of (expressed in thousands):

	Unrestricted	Restricted	Total
Cash in commercial banks	\$ 63,841	\$ 66,863	\$ 130,704
Cash in governmental banks	72,522	5,000	77,522
Investments	<u>353,081</u>	<u>63,368</u>	<u>416,449</u>
<b>Total</b>	<b><u>\$489,444</u></b>	<b><u>\$ 135,231</u></b>	<b><u>\$ 624,675</u></b>

As of June 30, 1997, cash mainly include certificates of deposits, demand and interest bearing accounts in commercial and governmental banks. The carrying amount and the bank balance of deposits at June 30, 1997 consists of (expressed in thousands):

	Carrying Amount	Bank Balance
Commercial banks	\$ 95,131	\$ 79,744
Governmental banks	<u>93,049</u>	<u>92,892</u>
<b>Total</b>	<b><u>\$ 188,180</u></b>	<b><u>\$ 172,636</u></b>
Bank balances of deposits uninsured or uncollateralized		<u>\$ 92,892</u>

The following schedule reconciles the carrying amount of deposits as disclosed above to the combined balance sheet (expressed in thousands):

Carrying amount of deposits	\$ 188,180
Cash equivalents disclosed as investments for GASB 9	(15,672)
Investments disclosed as cash equivalents for GASB 9	<u>35,718</u>
Deposits as reported on the combined balance sheet	<u>\$ 208,226</u>

The uninsured bank balance mainly includes deposits with Government Development Bank for Puerto Rico and Economic Development Bank for Puerto Rico.

Investments of the public university funds are as follows (expressed in thousands):

	1	Category 2	3	Carrying Amount	Fair Value
<u>Unrestricted</u>					
Stocks	\$	\$ 213,273	\$	\$ 213,273	\$ 213,273
US Government and agencies securities	2,060	53,307		55,367	55,367
Corporate bonds		35,117		35,117	35,117
Mortgage-backed securities		34,249		34,249	34,249
Negotiable certificates of deposits	33,092			33,092	33,092
Foreign and municipal bonds		13,552		13,552	13,552
Subtotal	<u>35,152</u>	<u>349,498</u>	<u>_____</u>	<u>384,650</u>	<u>384,650</u>
Investments not subject to categorization:					
Mortgage loans				3,024	
PR Government Investment Trust Fund				19	19
Limited partnerships/private equity				382	
Total-unrestricted				<u>388,075</u>	<u>384,669</u>
<u>Restricted</u>					
Stocks	14			14	14
US Government and agencies securities	27,866			27,866	27,866
Negotiable certificates of deposits	2,015			2,015	2,015
Subtotal	<u>29,895</u>	<u>_____</u>	<u>_____</u>	<u>29,895</u>	<u>29,895</u>
Investments not subject to categorization:					
Mortgage loans				3	3
Real estate				532	532
PR Government Investment Trust Fund				2,379	2,379
Mutual funds				15,611	15,611
Total-restricted				<u>48,420</u>	<u>48,420</u>
Total	<u>\$65,047</u>	<u>\$ 349,498</u>	<u>\$ _____</u>	<u>\$ 436,495</u>	<u>\$ 433,089</u>

The following schedule reconciles the carrying amount of investments as disclosed above to the combined balance sheet (expressed in thousands):

Carrying amounts of investments	\$ 436,495
Cash equivalents disclosed as investments for GASB 9	15,672
Investments disclosed as cash equivalents for GASB 9	<u>(35,718)</u>
Investments as reported on the combined balance sheet	<u>\$ 416,449</u>

Unrestricted investments mainly belong to the University of Puerto Rico Retirement System. Such investments have been presented in the general purpose financial statements at their fair value, which as of June 30, 1997 amounts to approximately \$355 million.

The fair value of investments held in foreign currencies are translated into US dollars generally using current rates of exchange. The related translation adjustments and the unrealized appreciation (depreciation) in fair value of investments is recorded in the statement of changes in fund balances as investment income.

**Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation**

Cash, cash equivalents and restricted assets of the Office at June 30, 1997 consist of deposits with commercial and governmental banks which carrying amounts and bank balances are as follows (expressed in thousands):

	Carrying Amount	Bank Balance
Cash in commercial banks	\$ 1,241	\$ 1,252
Cash in governmental banks	5,869	7,021
Total	<u>\$ 7,110</u>	<u>\$ 8,273</u>

As of June 30, 1997, the bank balance of deposits in commercial banks amounting to approximately \$1.2 million was fully insured and collateralized.

The bank balance of deposits in governmental banks consists of interest bearing deposits maintained in Government Development Bank for Puerto Rico. No insurance or collateral is held for such deposits.

**Component Units - Other**

Cash, cash equivalents and investments of the component units - other at June 30, 1997 consist of (expressed in thousands):

	Unrestricted	Restricted	Total
Cash and cash equivalents	\$ 359,866	\$ 362,860	\$ 722,726
Investments	<u>5,598,064</u>	<u>3,618,723</u>	<u>9,216,787</u>
Total	<u>\$5,957,930</u>	<u>\$3,981,583</u>	<u>\$ 9,939,513</u>

Cash and cash equivalents consist of demand deposits, interest bearing accounts, certificates of deposits 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):

	Carrying Amount	Bank Balance
Deposits in commercial banks	\$2,548,591	\$ 2,555,112
Deposits in governmental banks	<u>643,739</u>	<u>600,765</u>
Total	<u>\$3,192,330</u>	<u>\$ 3,155,877</u>
Bank balance of deposits in commercial banks:		
Category 1		\$ 823,689
Category 3		<u>1,731,423</u>
Total bank balance of deposits in commercial banks		<u>\$2,555,112</u>

The following schedule reconciles the carrying amount of deposits as disclosed above to the combined balance sheet (expressed in thousands):

Carrying amount of deposits	\$ 3,192,330
Cash equivalents disclosed as investments for GASB 9	(2,498,119)
Investments disclosed as cash equivalents for GASB 9	<u>28,515</u>
Deposits as reported on the combined balance sheet	<u>\$ 722,726</u>

The bank balance of deposits in governmental banks is uninsured and uncollateralized. Such deposits are maintained with the Government Development Bank for Puerto Rico and with the Economic Development Bank for Puerto Rico.

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

	1	Category 2	3	Carrying Amount	Fair Value
<u>Unrestricted</u>					
US Government and agencies securities	\$1,293,286	\$ 127,417	\$ 5,000	\$1,425,703	\$1,425,374
Commercial paper	15,724	246,081	8,958	270,763	270,795
Mortgage-backed securities	374,419		992	375,411	376,611
Corporate bonds	137,230	36,991	3,000	177,221	177,271
Repurchase agreements	192,295		163,151	355,446	355,446
Stocks	213,811		307	214,118	213,147
Commonwealth securities	2,410			2,410	2,420
Negotiable certificates of deposits	7,868			7,868	7,868
Trading securities		189,583		189,583	189,583
Foreign and municipal bonds	1,005			1,005	1,005
Bank notes		62,999		62,999	63,003
Bankers acceptance		51,317		51,317	51,315
Subtotals	<u>2,238,048</u>	<u>714,388</u>	<u>181,408</u>	<u>3,133,844</u>	<u>3,133,838</u>
Investments not subject to categorization:					
PR Government Investment Trust Fund				108,720	107,414
Mortgage loans				70	70
Investment contracts				225,000	225,000
Securities lending underlying securities				<u>205,599</u>	<u>205,599</u>
Total - unrestricted				<u>3,673,233</u>	<u>3,671,921</u>
<u>Restricted</u>					
US Government and agencies securities	84,834	459,178		544,012	551,163
Mortgage-backed securities	12,662	626,238		638,900	656,169
Foreign and municipal bonds	566,226			566,226	566,226
Repurchase agreements	6,962	252,000		258,962	258,962
Commonwealth securities	19,000			19,000	18,810
Negotiable certificates of deposits	10,658		90,004	100,662	100,662
Bank notes	<u>499,202</u>			<u>499,202</u>	<u>499,125</u>
Subtotals	<u>1,199,544</u>	<u>1,337,416</u>	<u>90,004</u>	<u>2,626,964</u>	<u>2,651,117</u>
Investments not subject to categorization:					
Investment contracts				368,691	406,268
PR Government Investment Trust Fund				<u>78,295</u>	<u>78,295</u>
Total - restricted				<u>3,073,950</u>	<u>3,135,680</u>
Total	<u>\$3,437,592</u>	<u>\$2,051,804</u>	<u>\$ 271,412</u>	<u>\$6,747,183</u>	<u>\$6,807,601</u>

The following schedule reconciles the carrying amount of investments as disclosed above to the combined balance sheet (expressed in thousands):

Carrying amounts of investments	\$6,747,183
Cash equivalents disclosed as investments for GASB 9	2,498,119
Investments disclosed as cash equivalents for GASB 9	<u>(28,515)</u>
Investments as reported on the combined balance sheet	<u>\$9,216,787</u>

Unrestricted investments do not include approximately \$1.9 billion of interest bearing deposits, which have been classified as investments in the combined balance sheet. Such amount has been categorized as deposits with financial institutions.

In addition, contributions made by the Government Development Bank for Puerto Rico and Subsidiaries to the Puerto Rico Government Investment Trust Fund amounting to approximately \$7.4 million are included as investments in the combined balance sheet.

Restricted investments do not include approximately \$545 million of interest bearing deposits, which have been classified as investments in the combined balance sheet. Such amount has been categorized as deposits with financial institutions.

Unrestricted repurchase agreements of approximately \$189 million belong to the Economic Development Bank for Puerto Rico. As of June 30, 1997, the fair value of the collateral for the repurchase agreements amounted to approximately \$192 million and consisted mainly of mortgage-backed securities held under safekeeping by a financial institution independent of the transaction.

During the year ended June 30, 1997, the Government Development Bank for Puerto Rico (GDB), and the Economic Development Bank for Puerto Rico (EDB) entered into investment transactions in commercial paper. Information related to these transactions are as follows (expressed in thousands):

	GDB	EDB
Carrying amount as of June 30, 1997	-	-
Maximum amount outstanding at any month-end	\$1,051,492	\$119,732
Average amount outstanding during the year	334,202	66,166
Weighted average interest rate for the year	5.63%	5.09%
Weighted average interest at year end	-	-

Restricted repurchase agreements of approximately \$252 million correspond to the Puerto Rico Housing Bank and Finance Agency and are funded through obligations under reverse repurchase agreements. As of June 30, 1997, the fair value of the underlying securities amounted to approximately \$252 million and mainly consisted of US government obligations and mortgage backed securities held by the broker, or his agent, with whom the agreement is transacted.

## 6. SECURITIES LENDING TRANSACTIONS AND REVERSE REPURCHASE AGREEMENTS

During the year the State Insurance Fund Corporation, the Puerto Rico Housing Bank and Finance Agency, the Automobile Accident Compensation Administration, the Economic Development Bank for Puerto Rico, and the Government Development Bank for Puerto Rico, five discretely presented component units, entered into securities lending transactions.

## State Insurance Fund Corporation (SIFC)

The SIFC securities custodian, as agent of SIFC, manages the securities lending program and receives cash collateral, securities or irrevocable bank letters of credit as collateral. The collateral securities cannot be pledged or sold by SIFC unless the borrower defaults. 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 or fail to pay SIFC for income distributions by the securities' issuers while the securities are on loan.

All securities 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 investments of the cash collateral. Such matching existed at year-end.

Securities lending obligations for which cash was received as collateral as of June 30, 1997 consist of (expressed in thousands):

Securities Lent	Fair Value of Underlying Securities
U.S. Government and agencies obligations	\$ 85,590
Corporate bonds and notes	2,614
Equity securities	<u>696</u>
	<u>\$ 88,900</u>

Cash collateral received amounted to \$92.4 million and it was invested \$3 million in corporate bonds and notes and \$89.4 million in repurchase agreements.

In addition, SIFC had the following securities lending obligations collateralized by letters of credit as of June 30, 1997 (expressed in thousands):

Securities Lent	Fair Value of Underlying Securities	Collateral Received
U.S. Government and agencies obligations	<u>\$ 12,377</u>	<u>\$ 12,690</u>

Securities lending transactions collateralized by letters of credit are not reported as assets and liabilities in the combined balance sheet.

### **Puerto Rico Housing Bank and Finance Agency (PRHBFA)**

The Housing Bank entered into obligations under reverse repurchase agreements. These agreements represent short-term debts and are reflected as a liability. The securities underlying these agreements remain in the asset accounts and are usually held by the broker, or his agent, with whom the agreement is transacted. The maturities of the investments made with the proceeds obtained from the obligations under reverse repurchase agreements are generally matched to the maturities of such obligations. As of June 30, 1997, \$250 million had been received and is invested in repurchase agreements. The aggregate market value of the underlying securities, mainly United States Government obligations and mortgage backed securities, exceeds by approximately \$2 million the obligations under reverse repurchase agreement.

### **Automobile Accident Compensation Administration (AACA)**

Under the provisions of the Commonwealth statutes and Board of Directors, AACA lends securities to broker-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The custodial bank manages the securities lending program and receives cash, government securities and letters of credit as collateral. The collateral securities cannot be pledged or sold by AACA unless the borrower defaults. The borrower agreement shall provide for a minimum collateralization equal to such percentage of the market value of the borrowed securities as the custodial bank and the borrower shall agree, except that the percentage shall not be less than 100 percent. Additional collateral has to be provided by the close of the next business day if its value falls to less than 100 percent. The contract with the custodian bank requires it to indemnify AACA if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay AACA for income distributions by the securities' issuers while the securities are on loan.

All securities loans can be terminated at any time by either the custodian bank or the borrower. Collateral received consists of an investment in the lending agent's investment pools. The relationship between maturities of the investment pool and AACA's loans cannot be determined.

The following represent the balances relating to the securities lending transactions as of June 30, 1997 (expressed in thousands):

<b>Securities Lent</b>	<b>Fair Value of Underlying Securities</b>
Common stocks and preferred stocks	\$ 23,745
Corporate bonds	2,257
US Treasury bills, bonds and notes	<u>21,539</u>
<b>Totals</b>	<b><u>\$ 47,541</u></b>

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 combined balance sheet.

### **Economic Development Bank for Puerto Rico (EDB)**

EDB enters into sales of securities under agreements to repurchase. These agreements generally represent short-term borrowings and are presented as a liability. The securities underlying these agreements are usually held by the broker, or its agent, with whom the agreement is transacted.

The following table summarizes certain information on securities sold under agreements to repurchase (expressed in thousands):

Carrying amount at June 30, 1997	\$ 300,694
Average amount outstanding during the year	523,135
Maximum amount outstanding at any month-end	1,146,725
Weighted average interest rate for the year	5.06%
Weighted average interest rate at year-end	5.32%

Securities sold under agreements to repurchase represent borrowings with maturities ranging from one to ninety days at June 30, 1997.

As of June 30, 1997, securities sold under agreements to repurchase were collateralized with mortgage backed securities, U.S. Treasury and other government agencies securities, and other investments received as collateral under purchases of securities under resell agreements with a market value of approximately \$302 million.

#### Government Development Bank for Puerto Rico (GDB)

GDB enters into sale of securities under agreement to repurchase. These agreements generally represent short-term borrowings with maturities ranging from two days to over ninety days, and are presented as a liability in the general purpose financial statements. The securities underlying these agreements, mainly mortgage-backed securities and US government obligations, are usually held by the broker, or its agent, with whom the agreement is transacted.

Following is selected information concerning securities sold under agreements to repurchase (expressed in thousands):

Carrying amount at June 30, 1997	\$ 303,708
Maximum amount outstanding at any month-end	551,548
Average amount outstanding during the year	262,714
Weighted average interest rate for the year	4.86%
Weighted average interest rate at year-end	5.24%

Securities sold under agreements to repurchase classified by maturity at June 30, 1997 are as follows (expressed in thousands):

Term	Carrying Amount	Description of Security	Collateral	
			Carrying Amount	Fair Value
Within one day	\$ 25,000	United States Government and Agencies Obligations	\$ 25,126	\$ 25,126
Up to 30 days	209,773	United States Government and Agencies Obligations	230,226	230,065
Over 90 days	<u>68,935</u>	United States Government and Agencies Obligations	<u>70,058</u>	<u>69,852</u>
	<u>\$ 303,708</u>		<u>\$ 325,410</u>	<u>\$ 325,043</u>

All sales of investments under agreements to repurchase are for fixed terms. In investing the proceeds of securities sold under agreements to repurchase, GDB's policy is for the term to maturity of investments to be on or before the maturity of the securities sold under agreements to repurchase. This condition existed at year end.

## 7. INVESTMENT IN LIMITED PARTNERSHIPS

Pursuant to the Statement of Investment Guidelines for the Government of Puerto Rico, the Pension Trust Funds, the University of Puerto Rico Retirement System and a component unit invested \$4.2 million in limited partnerships.

The amount of \$2.7 million was invested in Guayacán Funds, L.P., a Delaware limited partnership created by Grupo Guayacán, Inc. as General Partner that has committed \$55.5 million from public pension funds and private corporate investors. This fund invests in United States and international private equity partnerships that in turn invest in private companies.

The amount of \$1.5 million was invested in Guayacán Private Equity Fund, L.P., a Delaware limited partnership created by Advent/Morro Partners as General Partners that has committed \$41.9 million from the government pension funds and private corporate investors in Puerto Rico. This fund invests in Puerto Rico private equity.

The allocations of net gain and net loss to the limited partners are based on certain percentages, as established in the Limited Partnership Agreements. As of June 30, 1997, the unaudited financial statements of Guayacán Fund of Funds, LP and Guayacán Private Equity Fund, LP reflect a net loss of \$364 thousand and \$230 thousand, respectively.

As of June 30, 1997 the primary government and discretely presented component units had capital commitments and contributions as follows (expressed in thousands):

**Guayacán Funds of Funds, LP**

	<b>Commitments</b>	<b>Contributions</b>
<u>Primary Government</u>		
Employee's Retirement System of the Government of Puerto Rico	\$25,000	\$1,351
Annuity and Pension System for the Teachers of Puerto Rico	20,000	1,080
<u>Public University Fund</u>		
University of Puerto Rico Retirement System	<u>5,000</u>	<u>269</u>
Subtotal	<u>50,000</u>	<u>2,700</u>
 <b>Guayacán Private Equity Fund, LP</b>		
<u>Primary Government</u>		
Employee's Retirement System of the Government of Puerto Rico	5,000	226
Annuity and Pension System for the Teachers of Puerto Rico	5,000	226
<u>Public University Fund</u>		
University of Puerto Rico Retirement System	2,500	113
<u>Component Units - Other</u>		
Government Development Bank for Puerto Rico	<u>20,000</u>	<u>902</u>
Subtotal	<u>32,500</u>	<u>1,467</u>
Total	<u>\$82,500</u>	<u>\$4,167</u>

**8. RECEIVABLES**

Receivables in the general fund include approximately \$78 million of accrued income and excise taxes and \$125 million of receivables from the Federal government. In addition, there are also included in the Trust and Agency funds \$67.5 million of accrued unemployment and disability taxes.



## 9. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 1997 are summarized as follows (expressed in thousands):

Due from/to other funds:

Receivable fund	Payable fund	Amount
General	Agency fund - Governmental Board 911 Service	\$ 5,490
	The Additional Lottery System	3,238
	Lottery of Puerto Rico	20,849
Capital	General	11,959
	Public Buildings Authority	36,491
	Puerto Rico Highway Transportation Authority	2,488
	General	5,818
Fiduciary	Health Facilities and Services Administration of Puerto Rico Trust Fund	4,624
Enterprise	Puerto Rico Highway Transportation Authority	<u>2,573</u>
<b>Total</b>		<b><u>\$ 93,530</u></b>

Due from/to primary government and component units:

Receivable Entity	Payable Entity	
Public University Funds	Health Facilities and Services Administration of Puerto Rico	\$ 21,672
	General Fund	12,344
Puerto Rico Electric Power Authority	General Long-Term Debt Account Group	64,973
Puerto Rico Metropolitan Bus Authority	General Fund	3,985
Tourism Company of Puerto Rico	General Fund	1,975
Puerto Rico Medical Services Administration	Health Facilities and Services Administration of Puerto Rico	24,000
Puerto Rico Health Insurance Administration	Health Facilities and Services Administration of Puerto Rico	<u>207</u>
<b>Total</b>		<b><u>\$ 129,156</u></b>
Commercial and Farm Credit and Development Corporation	Farm Credit Guarantee Fund and Guarantee Loan Fund	\$ 8,021
Economic Development Bank for Puerto Rico	Commercial and Farm Credit and Development Corporation	<u>797</u>
<b>Total</b>		<b><u>\$ 8,818</u></b>

Advances to/from primary government and component units

Receivable Entity	Payable Entity	Amount
Government Development Bank for Puerto Rico	Puerto Rico Aqueduct and Sewer Authority	\$ 689,408
	General Long-Term Debt Account Group	629,119
	Health Facilities and Services Administration of Puerto Rico	578,292
	Tourism Company of Puerto Rico	134,846
	Puerto Rico Ports Authority	129,225
	Public Buildings Authority	71,259
	Land Authority of Puerto Rico	65,798
	Agricultural Services and Development Administration	57,139
	Puerto Rico Industrial Development Company	26,516
	Puerto Rico Housing Bank and Finance Agency	21,994
	Puerto Rico Electric Power Authority	15,000
	Commercial and Farm Credit and Development Corporation for Puerto Rico	14,000
	Solid Waste Authority of Puerto Rico	12,479
	Puerto Rico Metropolitan Bus Authority	11,272
	Institutional Trust of the National Guard of Puerto Rico	4,971
	Sugar Corporation of Puerto Rico	3,086
	Puerto Rico Land Administration	3,070
	Fine Arts Center Corporation	1,021
	General Fund	962
	Economic Development Bank for Puerto Rico	Commercial and Farm Credit and Development Corporation of Puerto Rico
Puerto Rico Electric Power Authority	Puerto Rico Land Administration	185
	Agricultural Services and Development Administration	492
Puerto Rico Public Finance Corporation	General Long-Term Debt Account Group	<u>476,798</u>
		<u>\$ 2,964,103</u>
Debt Service Fund	Recreational Development Company of Puerto Rico	<u>\$ 1,557</u>

The difference between due and advances to/from is mainly due to:

- a. Differences reported by the blended and discretely presented component units in their separately issued financial statements due to their different specialized industries reporting practices.
- b. Reconciling items between component units with different fiscal years.
- c. Reporting net operations for component units with governmental funds pursuant to GASB Statement Number 14.
- d. Different measurement focuses between primary government governmental funds and component unit other proprietary activity.

## 10. RESTRICTED ASSETS

Restricted assets included in the general purpose financial statements at June 30, 1997 consist of cash, investments and other assets to be used for the following purposes (expressed in thousands):

### Primary Government

Tax revenue anticipation notes	\$ 563,628
Debt service and sinking fund requirements	45,807
Payment of lottery prizes	180,523
Purchase of assets	<u>1,431</u>
Total for the primary government	<u>\$ 791,389</u>

### Public University Funds

University future development funds*	\$ 60,835
Construction funds	56,819
Debt service and sinking fund requirements	48,303
Retirement plan	19,222
Federal grants and contracts	10,492
Renewal and replacement funds	<u>461</u>
Total for public university funds	<u>\$196,132</u>

\* Included are \$21.6 million classified as advances to Health Facilities and Services Administration of Puerto Rico in the combined balance sheet.

### Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation

Residual receipts of Housing Projects	\$ 283
Replacement and Maintenance of Housing Projects	81
Tenants security deposits	<u>8</u>
Total	<u>\$ 372</u>

### Component Units - Other

Debt service and sinking fund requirements	\$3,235,591
Payment of reverse repurchase agreements*	455,521
Construction funds	230,420
Death, catastrophe and disability funds	18,734
Renewal and replacement funds	16,500
Purchase of assets	8,910
Agroindustrial unused funds	6,255
Court order restriction	3,431
Maintenance reserve fund	2,832
Severance payment	1,576
EDA reserve fund	1,538
Production and personnel funds	132
Federal grants	123
Child care funds	18
General reserve fund	<u>2</u>
Total for component units - other	<u>\$3,981,583</u>

\* Included are approximately \$252 million repurchase agreements that generate interest income that must be used mainly to subsidize low-income housing mortgage activities.

## 11. FIXED ASSETS

### Primary Government

Activity in the general fixed assets account group for the fiscal year ended June 30, 1997, was as follows (expressed in thousands):

	Balance July 1, 1996	Additions	Retirements	Balance June 30, 1997
Land	\$ 72,717	\$ 4,589	\$ 2,416	\$ 74,890
Buildings and improvements	1,399,702	147,977	2,778	1,544,901
Equipment	92,981	21,025	3,060	110,946
Construction in progress	<u>705,144</u>	<u>297,868</u>	<u>143,554</u>	<u>859,458</u>
Total	<u>\$ 2,270,544</u>	<u>\$471,459</u>	<u>\$151,808</u>	<u>\$2,590,195</u>

Fixed assets for the proprietary and fiduciary fund types as of June 30, 1997, were as follows (expressed in thousands):

	Enterprise Funds	Fiduciary Funds
Land	\$358,760	\$ 969
Buildings and improvements	88,492	20,635
Equipment	137,349	11,676
Construction in progress	170,875	
Other fixed assets	<u>12,458</u>	<u>          </u>
Total	767,934	33,280
Less: accumulated depreciation	<u>210,094</u>	<u>8,826</u>
Fixed assets, net	<u>\$557,840</u>	<u>\$24,454</u>

**Discretely Presented Component Units**

	Public University Funds	Office for the Liquidation	Component Units - Other
Land	\$ 19,534	\$	\$ 358,950
Buildings and improvements	318,640		11,339,936
Equipment	214,905	136	1,503,756
Construction in progress	70,004		1,636,053
Other fixed assets	<u>2,749</u>	<u>          </u>	<u>297,542</u>
Total	625,832	136	15,136,237
Less accumulated depreciation and amortization	<u>198</u>	<u>73</u>	<u>4,769,266</u>
Fixed assets, net	<u>\$ 625,634</u>	<u>\$ 63</u>	<u>\$10,366,971</u>

## 12. OBLIGATIONS UNDER LEASE/PURCHASE ARRANGEMENTS

The Commonwealth and its component units are obligated under capital leases with third parties that expire through 2018 for buildings and equipment. At June 30, 1997, the capitalized cost of the buildings and equipment amounted to approximately \$24.8 million and is included in the general fixed assets account group. The present value of future minimum capital lease payments as of June 30, 1997, included in other long-term liabilities in the general long-term debt account group is as follows (expressed in thousands):

Year Ending June 30,	Amount
1998	\$ 5,042
1999	4,653
2000	3,646
2001	3,664
2002	3,491
Thereafter	<u>31,327</u>
Total minimum lease payments	51,823
Less: amount representing interest	<u>27,060</u>
Present value of minimum lease payments	<u>\$24,763</u>

The Commonwealth and its component units, are also committed under numerous operating leases, excluding those with the Public Buildings Authority, covering real property and equipment. Rental expenditures within the general fund for the year ended June 30, 1997, under such operating leases were approximately \$129 million. Management believes that the summary of the future minimum rental commitments under noncancelable real property and equipment leases with terms exceeding one year is not significant.

## 13. ADVANCES FROM COMPONENT UNITS TO PRIMARY GOVERNMENT

### General Fund

The general fund has advances related to the Law 89, from the Government Development Bank for Puerto Rico, a discrete component unit, amounting to approximately \$962 thousand as of June 30, 1997. Law 89 loan was used to pay the balance of back pay owed to the teachers and other employees that had not received a salary raise in five years. The loan will be paid on July 1, 1997 and accrues interest at 6.5% per annum.

### Capital Projects Funds

The loans from the Government Development Bank for Puerto Rico represent a construction credit as part of the construction financing activities of the Public Buildings Authority (PBA). At June 30, 1997, PBA had an authorized line of credit of approximately \$694.5 million, due December 31, 1997. Advances outstanding and the interest rate under the line of credit amounted to approximately \$71.3 million at 5.52%.

#### 14. NOTES PAYABLE

Notes payable in the general fund include \$550 million of tax revenue anticipation notes plus accrued interest due on July 30, 1997. The proceeds of the tax revenue anticipation notes were used to cover a temporary cash deficiency resulting from the timing difference between the time tax collections are received and the payment of current expenditures.

#### 15. LONG-TERM DEBT

##### Governmental Funds Operations

##### Summary of General Long-Term Debt

The following schedule shows the changes in the general long-term debt account group for the year ended June 30, 1997 (expressed in thousands):

	Balance at July 1, 1996	Debt Issued	Debt paid or defeased	Other Net Increases (Decreases)	Balance at June 30, 1997
Bonds payable	\$ 7,908,435	\$1,415,292	\$ 647,186	\$ 21,487	\$ 8,698,028
Notes payable	9,260	12,633		(477)	21,416
Due to component unit	88,759			(23,786)	64,973
Advances from component units	708,140	105,872	37,557	329,462	1,105,917
Compensated absences	637,788			47,152	684,940
Net pension obligation	1,612,738			222,591	1,835,329
Other long-term liabilities	<u>716,302</u>	<u>76,008</u>	<u>2,768</u>	<u>150,736</u>	<u>940,278</u>
Total	<u>\$11,681,422</u>	<u>\$1,609,805</u>	<u>\$ 687,511</u>	<u>\$ 747,165</u>	<u>\$13,350,881</u>

##### A. Debt Limitation

The Constitution authorizes the contracting of debts as determined by the Legislature. Nevertheless, the Constitution 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, 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 issued thereafter which is 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 revenues raised under the provisions of Commonwealth legislation and conveyed into the Treasury (hereinafter "internal revenues") in 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 revenues consist principally of income taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages, tobacco products and customs duties, which are collected by the United States Government and returned to the Commonwealth, and motor vehicle fuel taxes and license fees, which are allocated to the Puerto Rico

Highway and Transportation Authority, a blended component unit, are not included as revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service. The Commonwealth has never defaulted on the payment of principal or interest on any of its general long-term debt obligations. At June 30, 1997, the Commonwealth is in compliance with the debt limitation requirement.

**B. Bonds Payable**

The Constitution of the Commonwealth provides that public debt will constitute a first claim on the available revenues 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.

Law 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 the Municipal Revenues Collection Center (MRCC), a municipal corporation. MRCC is required to remit the 1.03% of property tax collected to the Commonwealth to be used by the Commonwealth's debt service funds for payment of debt service on general obligations and notes of the Commonwealth. For financial reporting purposes, long-term bonds are carried at their face amount, without premium or discount. The outstanding amount represents the total principal to be repaid; for capital appreciation bonds, it represents total principal and accreted interest to be repaid.



Bonds payable outstanding at June 30, 1997 are as follows (expressed in thousands):

	General Obligation	Revenue Bonds	Total
Term bonds payable through 2025; interest payable semiannually at rates varying from 3% to 9%	\$1,726,010	\$2,302,650	\$4,028,660
Serial bonds payable through 2015; interest payable semiannually at rates varying from 3.75% to 8.0%	1,823,460	1,741,170	3,564,630
Capital appreciation bonds payable through 2011; no interest rate, yield ranging from 7% to 7.8%. Net of unaccrued discount of \$212 million	304,065	104,826	408,891
Appropriation Refunding Bonds for Low Income Housing payable through 2005, interest rate from 6.9% to 8%.	128,332		128,332
Bond payment obligation payable through 2008; interest payable at rates varying from 3.5% to 5.5%	33,450		33,450
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
Auction rate notes payable from 2007 through 2008; and from 2015 through 2020; interest payable in arrears from 2007 through 2008 at rates varying from 2.65% to 11.564%, and from 2015 through 2020 at rates varying from 2.65% to 11.662%	136,600		136,600
Yield curve notes payable from 2007 through 2008; no interest rate, yield of 8.914%	26,700		26,700
Yield curve notes payable from 2015 through 2020; no interest rate, yield of 9.012%	94,900		94,900
Tax-exempt components maturing through 2007 and 2008 interest rates range from 5.5% to 5.6%		72,160	72,160
Deferred interest bonds payable through 2002; interest payable semiannually at 8%	50,000		50,000
Indexed inverse floaters maturing through 2016 interest rate at 5.70%		46,000	46,000
Inverse rate securities payable from 2009 through 2011, at an interest rate of 6%	<u>15,000</u>	<u>          </u>	<u>15,000</u>
Total	4,430,977	4,266,806	8,697,783
Savings Bonds	<u>245</u>	<u>          </u>	<u>245</u>
Total bonds payable	<u>\$4,431,222</u>	<u>\$4,266,806</u>	<u>\$8,698,028</u>

On July 6, 1996, the Public Buildings Authority issued approximately \$224.8 million Government Facilities Revenue Bonds, Series A, which are guaranteed by the Commonwealth.

The appropriation refunding bonds for low income housing is the balance of bonds payable assumed by the Commonwealth pursuant to Law No. 134 dated December 13, 1994. This Law authorized the assumption of bonds payable by the former Puerto Rico Urban Renewal and Housing Corporation. The Commonwealth had been funding this liability.

During the year ended June 30, 1997, the following changes occurred in the bonds payable (expressed in thousands):

	Outstanding July 1, 1996	Issued	Discount Accretion (Redeemed)	Outstanding June 30, 1997
Term bonds	\$ 3,860,710	\$ 497,350	\$ (329,400)	\$4,028,660
Serial bonds	2,952,950	911,246	(299,566)	3,564,630
Capital appreciation bonds	380,708	6,696	21,487	408,891
Appropriation refunding bonds	146,527		(18,195)	128,332
Auction rate notes	136,600			136,600
Bond payment obligations	125,910			125,910
Yield curve notes	121,600			121,600
Tax-exempt components	72,160			72,160
Deferred interest bonds	50,000			50,000
Indexed inverse	46,000			46,000
Inverse rate notes	15,000			15,000
Savings bonds	<u>270</u>	<u>          </u>	<u>(25)</u>	<u>245</u>
<b>Total</b>	<b><u>\$ 7,908,435</u></b>	<b><u>\$1,415,292</u></b>	<b><u>\$ (625,699)</u></b>	<b><u>\$8,698,028</u></b>

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

Year Ending June 30	Principal	Interest	Total
1998	\$ 328,962	\$ 509,776	\$ 838,738
1999	339,204	481,764	820,968
2000	363,109	461,461	824,570
2001	387,512	434,827	822,339
2002	393,544	415,876	809,420
Thereafter	<u>6,737,956</u>	<u>5,116,458</u>	<u>11,854,414</u>
Total	8,550,287	<u>\$7,420,162</u>	<u>\$ 15,970,449</u>
Plus accreted discount	<u>147,741</u>		
<b>Total</b>	<b><u>\$8,698,028</u></b>		

**C. Special Promissory Note**

The note payable of approximately \$21.4 million is a special promissory note, which bears interest ranging between 5.875% and 8%. It represents the amount paid for insurance premiums by the Commonwealth on behalf of the municipalities of Puerto Rico which was not financed as part of the property tax settlement loan (See E below). The note is payable from property tax collections that the municipalities of Puerto Rico shall remit to the Secretary of the Treasury over a period not to exceed fifteen (15) years.

**D. Due to Component Unit**

The amount due to the Puerto Rico Electric Power Authority (PREPA), a discretely presented component unit, consists of the following subsidy reimbursements (expressed in thousands):

Fuel adjustment subsidy	\$ 63,294
Rural irrigation system cost reimbursement	<u>1,679</u>
Total	<u>\$ 64,973</u>

On October 29, 1991, the Commonwealth entered into an agreement with PREPA for the payment of the outstanding fuel adjustment subsidy as of June 30, 1991 whereby the Commonwealth will pay the outstanding balance over a fifteen-year period in installments of approximately \$6.3 million per annum, without interest.

The rural irrigation system cost reimbursement debt is repaid by the Commonwealth by offsetting certain contributions in lieu of taxes that PREPA must remit to the Commonwealth. The yearly amortization will vary depending on the electric gross sales for the year. The amortized amount for the year ended June 30, 1997 was approximately \$17.5 million.

**E. Advances from Component Unit**

The Commonwealth financed certain long-term liabilities through the Government Development Bank for Puerto Rico (GDB), and the Puerto Rico Public Finance Corp., (PFC), a component unit of GDB. The Commonwealth considers these loans long-term because the term and repayment structure is tantamount to bonded debt. The proceeds were used for the following purposes (expressed in thousands):

The financing provided by GDB is composed of the following:

Health Facilities and Services Administration of Puerto Rico	\$ 329,462
Public schools infrastructure improvement loan	198,836
Disaster assistance loan	70,335
Police Department loan	30,211
Other	<u>275</u>
Total with GDB	<u>629,119</u>

The financing provided by PFC is composed of the following:

Promissory note for the Puerto Rico Maritime Shipping Authority	293,964
Property tax settlement loan	<u>182,834</u>
Total provided by PFC	<u>476,798</u>
Total	<u>\$1,105,917</u>

On February 5, 1997, the Health Facilities and Services Administration of Puerto Rico (HFSA) entered into a revolving line of credit agreement with the Government Development Bank for Puerto Rico (GDB) which provides borrowings up to \$332 million. Borrowings outstanding under this revolving line of credit bear variable interest and are payable quarterly before the tenth (10) day of July, October, January and April. Advances under the revolving line of credit are made only upon the authorization of the Director of the Office of Management and Budget of the Commonwealth of Puerto Rico. The line of credit will be used solely for the purpose of implementing the Health Care Reform. As of June 30, 1997, \$329.5 million were still outstanding. The proceeds of the line of credit were recorded in the accompanying financial statements of the Puerto Rico Health Insurance Administration, a discretely presented component unit, as transfers from the primary government.

The public schools infrastructure improvement loan provided additional funds for major repairs and improvements of the public schools in Puerto Rico. This activity is administered by the Office for the Improvement of the Public Schools of Puerto Rico. The loan is repaid by the Commonwealth using the contributions in lieu of taxes that the Commonwealth collects from the Puerto Rico Telephone Authority, a discretely presented component unit, of at least \$20 million per year, plus \$15 million per year from legislative appropriations from the General Fund. During the year ended June 30, 1997, the Commonwealth obtained an additional advance of \$70.3 million, for the same purposes. Minimum payments in future years, including interest, are as follows (expressed in thousands):

Year Ending June 30,	Payments
1998	\$ 35,000
1999	35,000
2000	35,000
2001	35,000
2002	35,000
Thereafter	<u>175,000</u>
Total	<u>\$350,000</u>

On July 31, 1996, a loan for \$35.5 million was approved to the Police Department to pay for the lawsuit of Rivera Correa and others vs. Betancourt Lebrón and the Commonwealth of Puerto Rico and related expenses. As of June 30, 1997, the balance outstanding for this loan was approximately \$30.2 million. Debt service requirements in future years, including principal and interest, are as follows (expressed in thousands):

Year Ending June 30	Payments
1998	\$ 7,505
1999	7,505
2000	7,505
2001	7,506
2002	<u>7,506</u>
<b>Total</b>	<b><u>\$ 37,527</u></b>

The disaster assistance loan of approximately \$93.9 million was used to repay a debt for such amount to the Federal Emergency Management Agency, which funded the Commonwealth's share of the relief grants for the residents of Puerto Rico affected by Hurricane Hugo in 1989. Debt service requirements in future years are as follows (expressed in thousands):

Year Ending June 30,	Principal	Interest	Total
1998	\$ 8,638	\$ 3,517	\$ 12,155
1999	9,071	3,085	12,156
2000	9,524	2,631	12,155
2001	10,000	2,155	12,155
2002	10,500	1,655	12,155
Thereafter	<u>22,602</u>	<u>1,709</u>	<u>24,311</u>
<b>Total</b>	<b><u>\$ 70,335</u></b>	<b><u>\$14,752</u></b>	<b><u>\$ 85,087</u></b>

The promissory note payable of approximately \$294 million is the liability owed by the Puerto Rico Maritime Shipping Authority (PRMSA) to GDB that was assumed by the Commonwealth in connection with the sale of the maritime operations of PRMSA. GDB, through one of its component units, issued bonds to restructure this liability, and pledged the note receivable for the payment of the bonds, thus, the bonds are considered to be conduit debt. The promissory note payable bears interest at a variable rate not to exceed 12% (6% at June 30, 1997). 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>
1998	\$ 5,140	\$ 19,081	\$ 24,221
1999	5,360	18,860	24,220
2000	5,650	18,570	24,220
2001	5,935	18,210	24,145
2002	6,325	18,022	24,347
Thereafter	<u>265,554</u>	<u>312,202</u>	<u>577,756</u>
<b>Total</b>	<b><u>\$ 293,964</u></b>	<b><u>\$ 404,945</u></b>	<b><u>\$ 698,909</u></b>

During fiscal year 1996, the Commonwealth refinanced the liability for the settlement of the property taxes owed to the municipalities of Puerto Rico. GDB, through one of its subsidiaries, issued bonds to restructure this liability. The new financing is approximately \$183 million, bearing interest 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>
1998	\$ 7,485	\$ 9,886	\$ 17,371
1999	8,015	9,482	17,497
2000	8,590	8,964	17,554
2001	9,200	8,410	17,610
2002	9,850	7,819	17,669
Thereafter	<u>139,694</u>	<u>95,325</u>	<u>235,019</u>
<b>Total</b>	<b><u>\$ 182,834</u></b>	<b><u>\$ 139,886</u></b>	<b><u>\$ 322,720</u></b>

**F. Compensated Absences**

General long-term debt includes approximately \$343 million of accrued sick leave benefits, and approximately \$342 million of accrued vacation benefits, representing the Commonwealth's commitment to fund such costs from future operations.

**G. Net Pension Obligation**

The amount presented as net pension obligation of approximately \$1.8 billion represents the cumulative amount owed by the Commonwealth to the pension plans that are necessary to cover the annual pension costs. (See Note 22).

## H. Other Long-Term Liabilities

The remaining long-term liabilities include (expressed in thousands):

Advances for construction	\$ 487,928
Provisions for legal claims and judgments	307,206
Provision for federal cost disallowances	118,482
Obligations under capital lease	24,763
Other	<u>1,899</u>
<b>Total</b>	<b><u>\$ 940,278</u></b>

Changes in the provision for legal claims and judgments for the year ended June 30, 1997 were as follows:

Provisions for legal claims and judgments - July 1, 1996	\$ 240,959
Incurred Claims and Changes in Estimates	73,087
Payments for Claims and Adjustment Expenses	<u>(6,840)</u>
 Provision for legal claims and judgments - June 30, 1997	 <u>\$ 307,206</u>

## I. Advance Refunding and Defeased Bonds

The Commonwealth advance refunded certain general obligation bonds through the issuance of approximately \$326.8 million of general obligation public improvements refunding bonds during the year ended June 30, 1997. The Commonwealth used approximately \$333.1 million from the net proceeds of the issued bonds which were used to purchase US 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 therefore have been removed from the general long-term debt account group. 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 decreased its aggregate debt service payments by approximately \$11.7 million over the next 5 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 \$10.2 million. At June 30, 1997 approximately \$325.1 million of the bonds refunded 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 trust account assets and liabilities for the defeased bonds are not included in the general purpose financial statements. At June 30, 1997 approximately \$1,270 billion of bonds outstanding from prior years advance refundings are considered defeased.

In addition, the Public Buildings Authority (PBA) and the Puerto Rico Highway and Transportation Authority (PRHTA), blended 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 account assets and liabilities for the defeased bonds are not included in the general purpose financial statements. As of June 30, 1997, approximately \$1,232 billion for PBA and \$797 million for PRHTA are considered defeased.

**J. Pension Trust Funds**

On August 1, 1996, the Puerto Rico System of Annuities and Pensions for Teachers (TRS) entered into a loan agreement with the Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority (AFICA), a discretely presented component unit, to secure the Authority'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 System.

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.

Bonds payable outstanding at June 30, 1997 are as follows (expressed in thousands):

Term Bonds Series A payable through 2011; interest payable on a monthly basis at rates varying from 6.3% to 6.65%	\$ 11,735
Term Bonds Series B payable through 2021; interest payable semiannually at 5.50%	<u>15,210</u>
Total	<u>\$ 26,945</u>

Maturities of the Term Bonds are as follows (expressed in thousands):

Year Ending June 30,	Principal	Interest	Total
1998	\$ 435	\$ 1,468	\$ 1,903
1999	520	1,575	2,095
2000	555	1,542	2,097
2001	590	1,507	2,097
2002	625	1,470	2,095
Thereafter	<u>24,220</u>	<u>16,930</u>	<u>41,150</u>
Totals	<u>\$ 26,945</u>	<u>\$24,492</u>	<u>\$ 51,437</u>

The Series A and Series B Bonds are subject to partial redemptions commencing on July 1, 1997, July 1, 2002 and July 1, 2007, for series A and on July 1, 2012 and July 1, 2017, for Series B and on each July thereafter to the extent of the respective sinking fund requirement, as defined in the Trust Agreement, at a redemption price equal to the principal amount thereof, plus accrued interest to the redemption date.

**K. Discretely Presented Component Units**

**Public University Funds**

The University of Puerto Rico has issued revenue bonds designated as *University System Revenue Bonds*, the proceeds of which have been used mainly to finance new activities in connection with its educational facilities construction program and to cancel and refinance previous debts.



Revenue bonds outstanding at June 30, 1997, were approximately \$324.9 million net of discounts of approximately \$36.1 million with interest rates varying from 2.75% to 7.67% and a final maturity date of 2025. Future amounts required to pay principal and interest on University System Revenue Bonds at June 30, 1997, are as follows (expressed in thousands):

Year Ending June 30,	Principal	Interest	Total
1998	\$ 13,312	\$ 16,420	\$ 29,732
1999	13,878	15,864	29,742
2000	14,652	15,083	29,735
2001	15,340	14,402	29,742
2002	16,075	13,671	29,746
Thereafter	<u>287,862</u>	<u>137,044</u>	<u>424,906</u>
Subtotal	361,119	212,484	573,603
Discounts	<u>(36,145)</u>		<u>(36,145)</u>
Total	<u>\$ 324,974</u>	<u>\$ 212,484</u>	<u>\$ 537,458</u>

The bonds are collateralized by the pledge of certain revenues of the University. The outstanding balance of the bond issues defeased by the University at June 30, 1997 was approximately \$64.4 million.

In prior years, the University defeased certain revenue bonds by placing the proceeds in irrevocable trusts to provide for all future debt service payments. Accordingly, the trust account assets and liabilities for the defeased bonds are not included in the public university funds. At June 30, 1997, approximately \$64.4 million of bonds refunded remain outstanding and are considered defeased.

Office for the Liquidation of the Accounts of the  
Puerto Rico Urban Renewal and Housing Corporation

Long-term debt of the Office at June 30, 1997 consisted of approximately \$55.9 million mortgage notes payable to the Farmer Home Administration and the US Department of Housing and Urban Development, secured by land. The notes are due in monthly installments of varying amounts, including interest through the year 2032, and bear interest of 3% to 11.25%.

Future amounts required to pay principal balances at June 30, 1997 are as follows (expressed in thousands):

1998	\$ 1,415
1999	1,529
2000	1,644
2001	1,763
2002	1,833
Thereafter	<u>47,812</u>
Total	<u>\$ 55,996</u>

### Component Units - Other

Bonds and notes payable are those liabilities that are paid out of resources pledged by the other component units. These notes and revenue bonds do not constitute a liability or debt of the Commonwealth. Bonds payable and notes payable outstanding at June 30, 1997, (December 31, 1996 for the Puerto Rico Telephone Authority) are as follows (expressed in thousands):

	Final Maturity Date	Interest Rates	Balance
<u>Bonds Payable:</u>			
Puerto Rico Electric Power Authority	2028	4.2% to 8.7%	\$ 3,511,102
Government Development Bank for Puerto Rico	2021	Variable	1,037,953
Puerto Rico Telephone Authority	2022	3.4% to 8%	901,268
Puerto Rico Housing Bank and Finance Agency	2029	3.8% to 7.5%	755,873
Puerto Rico Municipal Finance Agency	2008	4.4% to 9.25%	642,491
Puerto Rico Aqueduct and Sewer Authority	2035	Variable	438,349
Puerto Rico Infrastructure Financing Authority	2009	Variable	228,850
Puerto Rico Industrial Development Company	2016	3.88% to 8.27%	158,394
Puerto Rico Ports Authority	2021	5% to 7.3%	122,289
Recreational Development Company of Puerto Rico	1997	4%	<u>60</u>
Total bonds payable			<u>\$ 7,796,629</u>
<u>Notes Payable:</u>			
Government Development Bank for Puerto Rico	1999	Variable	\$ 1,191,317
Puerto Rico Infrastructure Financing Authority	Not fixed	Variable	149,164
Puerto Rico Electric Power Authority	Not fixed	Variable	125,000
Puerto Rico Aqueduct and Sewer Authority	2001	5.75% to 7.25%	72,434
Economic Development Bank for Puerto Rico	2001	Variable	42,000
Sugar Corporation of Puerto Rico	Not fixed	Variable	16,032
Puerto Rico Industrial and Development Corp.	1998	7.125%	10,537
Puerto Rico Telephone Authority	1999	Variable	9,380
Commercial, Farm Credit and Development Corp. of Puerto Rico	Not fixed	Variable	8,926
Automobile Accident Compensation Administration	1999	4.7% to 6.63%	7,529
Tourism Company of Puerto Rico	2002	7.85% to 8.35%	3,019
Puerto Rico Ports Authority	Not fixed	Variable	534
Corporation of Stocks and Deposit Insurance for the Savings and Loans Cooperatives	2003	N/A	<u>464</u>
Total notes payable			<u>\$ 1,636,336</u>

Notes payable of \$72.4 million of the Puerto Rico Aqueduct and Sewer Authority include \$53.5 million from a State Revolving Fund Program that has no fixed maturity date and variable interest rates.

Fixed maturities required to pay principal and interest on other component units bonds and notes payable with fixed maturities at June 30, 1997, were as follows (expressed in thousands):

Bonds Payable Year Ending June 30,	Principal	Interest	Total
1998	\$ 421,256	\$ 545,892	\$ 967,148
1999	313,873	356,961	670,834
2000	643,455	341,951	985,406
2001	316,551	327,136	643,687
2002	332,465	315,667	648,132
Thereafter	<u>6,026,765</u>	<u>4,140,906</u>	<u>10,167,671</u>
	8,054,365	6,028,513	14,082,878
Discounts	<u>(257,736)</u>	<u>                    </u>	<u>(257,736)</u>
Total	<u>\$7,796,629</u>	<u>\$6,028,513</u>	<u>\$13,825,142</u>
Notes Payable Year Ending June 30,	Principal	Interest	Total
1998	\$ 1,142,422	\$ 4,130	\$ 1,146,552
1999	27,912	3,051	30,963
2000	97,516	2,669	100,185
2001	14,226	219	14,445
2002	586	37	623
Thereafter	<u>484</u>	<u>63</u>	<u>547</u>
Total	<u>\$1,283,146</u>	<u>\$ 10,169</u>	<u>\$ 1,293,315</u>

## 16. GUARANTEED AND APPROPRIATION DEBT

### Guaranteed Debt

The Commonwealth may provide guarantees for the repayment of certain borrowings of component units to carry out designated projects. At June 30, 1997, the following component units debts are guaranteed by the Commonwealth (expressed in thousands):

	Maximum Guarantee	Outstanding Balance
Public Buildings Authority	\$ 2,100,000	\$ 1,858,836
Puerto Rico Aqueduct and Sewer Authority	400,340	400,340
Government Development Bank for Puerto Rico	550,000	267,000
Puerto Rico Housing Bank and Finance Agency	<u>325,000</u>	<u>56,120</u>
Total	<u>\$ 3,375,340</u>	<u>\$ 2,582,296</u>

Law 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 these outstanding bonds of the Puerto Rico Aqueduct and Sewer Authority (PRASA). During December 1995, PRASA issued refunding bonds to refinance all outstanding bonds amounting to approximately \$400.3 million.

The Farm Credit Guarantee Fund, administered by the Commercial and Farm Credit and Development Corporation of Puerto Rico, a subsidiary of the Economic Development Bank for Puerto Rico, has guaranteed, under the full faith, credit and taxing power of the Commonwealth, certain loans made by private institutions, and guaranteed by the former component unit Farm Credit Corporation and the Guarantee Loan Fund for Eligible Businesses. This fund guarantees loans for approximately \$12 million as of June 30, 1997.

The Puerto Rico Housing Bank and Finance Agency (Housing Bank) insures 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, 1997, the mortgage loan insurance program was insuring loans aggregating \$396.4 million and had not issued any debenture bonds. Currently, the Commonwealth has not been called to make any direct payments pursuant to these guarantees.

During the fiscal year ended June 30, 1996, Housing Bank created a new loan insurance program to provide mortgage credit insurance to low and moderate-income families for the purchase of land lots. The program began with an initial contribution of \$500 thousand from Housing Bank's Governmental Funds. In addition, the programs are to be financed by further legislative appropriations from the Commonwealth, and proceeds from mortgage insurance premiums and any other income derived from the insurance activity. Under this program, Housing Bank is authorized to commit the good faith and credit of the Commonwealth for up to \$5 million in connection with the issuance of debenture bonds.

The Commonwealth guarantees the Adjustable Refunding Bonds, Series 1985, issued by the Government Development Bank for Puerto Rico, a discretely presented component unit.

The Commonwealth has guaranteed the payments of rentals of its departments, agencies and component units to the Public Buildings Authority (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 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 as of June 30, 1997 for the next five years and thereafter follows (expressed in thousands):

Year Ending June 30,	Principal	Interest
1998	\$ 52,455	\$ 97,553
1999	72,095	91,939
2000	68,960	96,573
2001	69,645	96,472
2002	70,000	95,000
Thereafter	<u>1,521,696</u>	<u>1,022,623</u>
Total	<u>\$1,854,851</u>	<u>\$1,500,160</u>

### Appropriation Debt

At June 30, 1997, the outstanding balances of debt payable by government appropriations and which are included in the individual financial statements of these entities (expressed in thousands):

#### Enterprise Funds:

Health Facilities and Services Administration of Puerto Rico \$578,292

#### Component Units - Other:

Puerto Rico Housing Bank and Finance Agency	\$729,436
Puerto Rico Infrastructure and Finance Agency	228,500
Puerto Rico Aqueduct and Sewer Authority	85,904
Sugar Corporation of Puerto Rico	30,093
Puerto Rico Industrial Development Company	14,122
Puerto Rico Solid Waste Authority of Puerto Rico	12,479
Puerto Rico Metropolitan Bus Authority	11,272
Tourism Company of Puerto Rico	3,312
Puerto Rico Land Administration	3,070
Musical Arts Corporation and Subsidiaries	332

### 17. CONDUIT DEBT OBLIGATIONS

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, commercial facilities, and Caribbean 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 financial statements of the issuing entities.

As of June 30, 1997, conduit debt obligations consisted of the following bonds issued by component units (expressed in thousands):

Issuing Entity	Issued To Date	Amount Outstanding
<b>Blended Component Units:</b>		
Puerto Rico Highway and Transportation Authority	\$117,000	\$126,013*
<b>Discretely Presented Component Units:</b>		
Caribbean Basin Projects Financing Authority	\$ 676	\$ 635
Puerto Rico Ports Authority	155,410	**
Puerto Rico Industrial Development Company	23,820	10,036
Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority	3,831,000	2,193,000

\* Including accrued interest

\*\* The aggregate principal amount payable as of June 30, 1997 could not be determined.

### **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 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 of the operations 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. At June 30, 1997, the outstanding debt fund balance, including accrued interest, amounted to approximately \$126 million and the sinking fund balance amounted to \$1.4 thousand.

### **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 the 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 United States banks or United States 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. At June 30, 1997, \$635 million of these bonds were outstanding.

### **Puerto Rico Ports Authority**

The Puerto Rico Ports Authority (PRPA) issued Special Facilities Revenue Bonds (1993 Series A) under the provisions of a Trust Agreement between PRPA and a private bank. The proceeds from the sale of the bonds were used to finance the construction of facilities, acquisition of equipment, and improvements to the Luis Muñoz Marín 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 agreement 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.

### **Puerto Rico Industrial Development Company (PRIDCO)**

Puerto Rico Industrial Development Company submits annual requests to the Legislature for appropriations to continue the Special Incentives Program. Upon receipt from the Legislature, PRIDCO deposits such funds in a special account over which the Company only has administrative responsibilities; the funds do not belong to PRIDCO. Consequently, the available funds together with the corresponding liabilities are maintained off the balance sheet.

### **Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority**

The revenue bonds of the Authority 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 the Authority 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 the Authority 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 US banks or US branches of international banks. Since inception and up to June 30, 1997, the Authority has sold revenue bonds aggregating \$3,831 million, \$2,193 of which were outstanding as of June 30, 1997.

## 18. CONTRIBUTED CAPITAL

The changes in the government's contributed capital accounts for its enterprise funds and discretely presented component units were as follows (expressed in thousands):

	Enterprise Funds	Component Units Other
Contributed capital, at beginning of year	\$ 60,646	\$ 4,504,373
Contributing sources (uses):		
Payments for acquisition of fixed assets	310	
Payments of principal on capital leases	356	
Transfers to transportation projects	88,785	
Change in method of financial reporting for capital contributions (See Note 19)		124,411
Transfers from retained earnings		100,000
Capital assets appropriations from the Commonwealth		68,244
Capital projects assistance from Federal government	27,090	69,252
Combination of Irrigation Systems		19,269
Retirement of equipment acquired through capital contributors		(3,539)
Contributions from cooperatives		2,528
Depreciation on equipment acquired through capital contributions	(1,337)	(51,267)
Loan assumed by the Commonwealth	<u>          </u>	<u>(2,653)</u>
Contributed capital, at end of year	<u>\$ 175,850</u>	<u>\$ 4,830,618</u>

- a) During the year ended June 30, 1997, the Puerto Rico Highway and Transportation Authority, a blended component unit, transferred from its debt service funds approximately \$88 million related to Metrobus and Tren Urbano projects.
- b) The transfer from retained earnings represents the decision of the Board of Directors of the Government Development Bank for Puerto Rico to transfer from the surplus account to the capital account the amount of \$100 million.
- c) The \$68.2 million of legislative appropriations represent amounts designated as source funds to offset construction projects.

## 19. RESTATEMENTS

The Commonwealth has restated its beginning balances of the following fund types and discrete component units to reflect the change in accounting policies and restatements made by various component units (expressed in thousands):

	General	Capital Projects	Enterprise	Component Units-Other
Beginning fund balances/retained earnings, (Deficit), as previously reported	\$ 397,187	\$ 830,815	\$(511,841)	\$2,917,960
Change in reporting entity:				
Change in financial reporting presentation of the Office for the Improvement of Public Schools (See Note 1)	(59,493)	59,493		
Change in method of financial reporting for contributed capital (See Note 2)				(124,411)
Other changes:				
a) Health Facilities and Services Administration of Puerto Rico			(8,613)	
b) Agricultural Services and Development Administration				12,767
c) Puerto Rico School of Plastic Arts				712
d) Right to Employment Administration				642
e) Employment and Training Enterprises Corporation				(210)
	_____	_____	_____	_____
Beginning fund balances/retained earnings (deficit), as restated	<u>\$ 337,694</u>	<u>\$ 890,308</u>	<u>\$(520,454)</u>	<u>\$2,807,460</u>

1. The Commonwealth changed its financial reporting presentation for the Office for the Improvement of Public Schools from the general fund to the capital project fund in order to record the transactions related to major construction projects.
2. The Puerto Rico Housing Bank and Finance Agency changed its method of financial reporting for contributed capital.
3. Other opening adjustments are:
  - a. The Health Facilities and Services Administration of Puerto Rico (HFSA), had opening adjustments due to a change of accounting for certain lease contracts to conform with the requirements of the Financial Accounting Standards Board Statement No. 13, *Accounting for Leases*, for approximately (\$830,000) the correction of various accruals made before 1996 and the amount due from the Federal Government. The net effect of these adjustments was to increase the deficit by approximately (\$5.1) million. In addition, HFSA corrected an accounting error regarding the estimated receivable from third party payor settlements for Medicare by approximately (\$2.7).



- b. The Agricultural Services and Development Administration (ASDA) changed its method of accounting for its long-term debts from the general fund to the general long-term debt account group for approximately \$10.6 million. In addition, ASDA reclassified some of their programs from the general and special revenue funds to the enterprise fund for approximately \$1.3 million and the correction of various overaccruals from prior years of approximately \$840 thousand.
- c. The \$712 thousand represents the inclusion of the financial activities of the Puerto Rico School of Plastic Arts that was not presented as of June 30, 1996.
- d. The Right to Employment Administration adjusted its beginning retained earnings to eliminate receivables and payables from prior years.
- e. The Employment and Training Enterprises Corporation adjusted the beginning accumulated deficit to correct an overstatement of accounts receivable.

## 20. RISK MANAGEMENT

The following describes the risk management programs administered by the University of Puerto Rico, the Puerto Rico Electric Power Authority, and the Puerto Rico Aqueduct and Sewer Authority.

### Public University Funds

The University of Puerto Rico (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. Through January 1993 UPR was insured under claims-made insurance policies with respect to medical malpractice risks for \$250 thousand per occurrence up to an annual aggregate of \$500 thousand. Subsequent to such date UPR was unable to obtain insurance at a cost it considered to be economically justifiable, consequently, UPR is now self-insured for such risks. Under Law Number 98 of August 24, 1994, the responsibility of UPR is limited to a maximum amount of \$75 thousand per person, or \$150 thousand 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 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 claims liabilities does not necessarily

result in an exact amount. Claims liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. Changes in the claims liability amount for the current and prior fiscal year were as follows (expressed in thousands):

	1997	1996
Claims payable - July 1	\$ 7,000	\$ 6,000
Incurred Claims and Changes in Estimates	1,298	1,691
Payments for Claims and Adjustment Expenses	<u>(698)</u>	<u>(691)</u>
Claims payable - June 30	<u>\$ 7,600</u>	<u>\$ 7,000</u>

UPR continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

During 1997, UPR implemented Statement No. 30 of the Governmental Accounting Standards Boards, "*Risk Financing Omnibus*". This Statement requires the inclusion of specific, incremental claim adjustment expenditures/expenses and estimated recoveries (such as salvage and subrogation) in the determination of the liability for unpaid claims. The implementation of this Statement did not have a material effect on claims liability.

#### **Puerto Rico Electric Power Authority (PREPA)**

The Puerto Rico Electric Power Authority (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. Under the property and casualty insurance program PREPA provides coverage, among others, for up to a maximum of \$250 thousand for each general and liability claim, and \$2 million, for each boiler and machinery and property liability claim. In addition, the property liability policy imposes windstorm and earthquake deductibles at 2% and 5% of the locations value subject to a maximum deductible of \$25 million per occurrence. PREPA purchases commercial insurance for claims in excess of coverage provided through the property and casualty insurance program. PREPA considers its Self-Insurance Fund to provide for its self-insurance risk. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated.

PREPA has a cost plus health insurance program, except that in 1997, the prescribed medicine cost is based on a fixed cost premium, covering substantially all employees. PREPA entered into contracts with two plan administrators for the processing, approval and payment of claims plus an administrative fee. The accrual includes claims processed and an estimate for claims incurred but not reported.

In addition, PREPA is self-insured for its transmission and distribution lines since June 1993. Transmission and distribution plant amounted to approximately \$2.1 billion at June 30, 1997. The Authority Self-Insurance Fund provides for its self insurance risk. This fund represents, principally retained earnings and restricted assets set aside for self insurance amounting to approximately \$86.7 million in 1997.

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

	1997	1996
Claims payable - July 1	\$ 22,892	\$ 20,660
Incurred claims	65,945	59,389
Claim payments	<u>(59,521)</u>	<u>(57,157)</u>
Claims payable - June 30	<u>\$ 29,316</u>	<u>\$ 22,892</u>

**Puerto Rico Aqueduct and Sewer Authority (PRASA)**

The Puerto Rico Aqueduct and Sewer Authority (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 \$200 million blanket insurance on all real and personal property. The deductible for windstorm and flood is 2% and 5% for earthquake. All other perils have a deductible of \$250 thousand per occurrence except underground perils with \$2.5 million deductible.

The Comprehensive General liability and Automobile liability has basic limits of \$3 million and the umbrella is \$47 million per occurrence.

The Boiler and Machinery Policy has a \$12.5 million aggregate and the Director and Officers Liability policy has a \$12 million aggregate.

Also Crime Insurance Policy is provided with \$1 million fidelity bond, \$500 thousand premises, transit, and depositors forgery coverages. There is a \$10 thousand deductible for money, securities and other properties. There is a sublimit of \$20 thousand for money orders and counterfeit currency coverages.

PRASA's insurance program is carried out by insurance brokers in coordination with the Insurance Office. Claims and liabilities are accounted for when it is probable that a claim has occurred and the amount of loss can be reasonably estimated.

PRASA has a cost plus health insurance program covering its managerial employees. The plan administrator has a contract for the processing, approval and payment of claims plus an administrative fee. The Authority incurred health insurance claims including an estimate for incurred but not reported claims of \$3.9 million for the year ended June 30, 1997.

**21. 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 thousand or \$150 thousand 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 judgment.

With respect to pending and threatened litigation, excluding the litigation mentioned in the following paragraph, the Commonwealth has reported liabilities of approximately \$106 million for awarded and anticipated unfavorable judgments. This amount was included as other long-term liabilities in the general long-term debt account group and represents the amount estimated as a probable liability or a liability with a fixed or expected due date which 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 and various component units are defendants in a lawsuit alleging violations of civil rights. Preliminary hearings and discovery proceedings are in progress. The amounts claimed exceed \$50 billion; however, the ultimate liability cannot be presently determined. It is the opinion of management that the claim is excessive and exaggerated. No provision for any liability that may result upon adjudication of this lawsuit has been recognized in the financial statements by the Commonwealth.

On July 28, 1994, the Commonwealth enacted Law No. 45 (the Law) and Joint Resolution No. 298 (Joint Resolution) through which the Commonwealth guarantees the principal, premium and interest payments to the bondholders of all outstanding bonds issued by PRASA at the effective date of this law (approximately \$397 million) and of all future bond issued or any other obligations incurred by PRASA to refinance all outstanding bonds covered by the guarantee. According to the Law, if PRASA's funds are not available for bond payments of principal, premium and interest, the Commonwealth will provide such funds to cover all required payments. On December 21, 1995, Law 45 was enforced resulting in the issuance of refunding bonds for approximately \$400.3 million, which are guaranteed by the Commonwealth. Also, the Puerto Rico Legislature enacted a Joint Resolution to provide a subsidy of \$35 million for fiscal year ended 1998. On August 1, 1997 a new Joint Resolution was approved by the Puerto Rico Legislature to provide a subsidy of \$35 million annually for the fiscal years 1999 through 2008. The Authority received payments of \$30 million of this subsidy for the fiscal year ended June 30, 1997.

The Commonwealth's escheat bank account regulations require the financial institutions doing business in Puerto Rico to remit to the Commonwealth all balances in deposit accounts under their custody that have been inactive for a period of five years. The Commonwealth shall reimburse any claims received from the owners of those accounts for a period of 10 years from the date of receipt from the financial institution. The balance of unclaimed escheat bank accounts as of June 30, 1997 is approximately \$41.5 million. No liability has been recorded at June 30, 1997 because subsequent payments are immaterial.

The minimum annual payments related to unpaid awards for the Additional Lottery, an enterprise fund, during the next five years is approximately \$18.7 million from 1998 through 2002 inclusive, and \$18.7 million from 2001 and 2002, and \$207.8 million thereafter. Imputed interest amounts to approximately \$121.1 million at June 30, 1997.

Public Buildings Authority (PBA), entered into an interest rate swap agreement with the Government Development Bank for Puerto Rico (GDB) to reduce the impact of changes in interest rates on certain of its Series M Public Education and Health Facilities Refunding Bonds with an outstanding balance of \$46 million at June 30, 1997, and which bear interest at a variable rate. Under the swap agreement, PBA will pay GDB an amount equal to 5.64% and GDB is obligated to pay a variable amount equal to the interest rate that PBA is required to pay on said variable rate bonds. The swap agreement is for a notional amount equal to the principal amount outstanding of said variable rate bonds and expires on July 1, 1998.

The Commonwealth receives financial assistance from the federal government in the form of grants and entitlements. Non-cash federal financial assistance programs received by the Commonwealth amounted to approximately \$15.1 million. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under the Single Audit Act of 1984, as amended, all of which are performed at the individual agency level. Disallowances as a result of these audits may become liabilities of the Commonwealth. At June 30, 1997, based on an evaluation of pending disallowances, the Commonwealth has recorded approximately \$118.4 million as other long-term liabilities in the general long-term debt account group for this purpose. The United States Congress is studying several cost-reduction measures to balance the federal budget deficit. As part of this process, the Congress is considering reductions to the federal financial assistance programs in which the Commonwealth, together with the States, participates. Management of the Commonwealth believes that the future outcome of any changes in federal financial assistance programs does not have a material effect on the general purpose financial statements.

Construction commitments at June 30, 1997 for the Public Buildings Authority and for the Puerto Rico Highway and Transportation Authority, blended component units, amounted to approximately \$842 and \$352 million, respectively.

#### **Public University Funds**

The University of Puerto Rico (UPR) capital construction program for educational facilities for the fiscal year ended on June 30, 1997 amounts to approximately \$36 million. This program is intended to be permanently financed with a future bond issuance.

UPR participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of the Single Audit Act of 1984 as amended, and U.S. Office of Management and Budget Circular A-133, "*Audits of State, Local Governments, and Non-Profit Organizations*" or to compliance audit by grantor agencies. Although these programs have been audited through June 30, 1997 under the Single Audit Act of 1984, as amended, and through various dates by grantor agencies, the resolution of certain previously identified questioned costs has not been resolved. The amount, if any, of expenditures which may be disallowed by the grantor agencies cannot be determined at this time, although, UPR's management expects such amounts, if any, will be immaterial.

**Office for the Liquidation of the Accounts of the Puerto Rico  
Urban Renewal and Housing Corporation (the Office)**

During the year ended June 30, 1997, the Office prepared a detailed inventory of housing units and land lots held for sale. However, this inventory does not include all the real property that could be owned by the Office since the former Urban Renewal and Housing Corporation did not maintain complete and accurate records of such units and land lots. The Office continues its efforts to identify all housing units and lots held for sale.

The Government of Puerto Rico is evaluating a change in law regarding the termination of the liquidation process. According to such proposed change, the Office could cease operations as of June 30, 1998. Except for certain employee benefits accrued, the cost to be incurred in the liquidation process cannot be determined. Therefore, the Office's management adopted the policy of recording such costs in the combined financial statements as incurred. The net assets as of the termination date will be transferred to the primary government.

The Office is a party to a number of lawsuits and claims, which it is vigorously defending. Such matters arise out of the normal course of operations related to construction projects deficiencies, government regulations and other issues. These actions seek damages amounting to approximately \$14.8 million. While the results of litigation cannot be predicted, the likelihood of loss as defined by Financial Accounting Standards Board Statement No. 5 is considered remote for approximately \$5.7 million, reasonably possible for \$234 thousand and probable for approximately \$1.8 million of the total claims. A provision of \$3 million has been established, which exceed the required reserve, as of June 30, 1997 to cover for the ultimate outcome of those legal claims which are considered probable loss as required by generally accepted accounting principles.

**Component Units - Other**

In the normal course of their operations the various component units-other are subject to actions brought by third parties seeking damages or enter into commitments. Such actions are disclosed in the separately issued reports of the component units and are summarized below if material to the Commonwealth's reporting entity.

**Government Development Bank for Puerto Rico and Subsidiaries**

In the normal course of business, GDB is party to financial instruments with off-balance sheet risk to meet the financing needs of the Commonwealth and of its private sector clients, and to reduce their own exposure to fluctuation in interest rates. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the financial statements of GDB. These off-balance sheet risk is managed in a manner similar to that used for on-balance sheet risks. GDB exposure to credit loss for lending commitments and letters of credit are represented by the contractual amount of those transactions. The notional amounts for other off-balance sheet risks express the dollar volume of the transactions, but the credit risk might be lower.

At June 30, 1997, GDB has financial guarantees for public entities for approximately \$146.9 million and for private sector of approximately \$290.5 million. In addition, standby letters of credit to public entities were approximately \$131.8 million and to private sector were approximately \$25 million. Commitments to extend credit to public entities was approximately \$1.251 billion, and to private sector was approximately \$20.9 million.

GDB entered into various interest rate swaps during 1997. These interest rate swaps are hedging investments in mortgage-backed securities. Interest rate swaps involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying principal amounts. Entering into interest rate swap agreements involves the risk of dealing with counterparts and their ability to meet the terms of the contracts and the interest rate risk associated with unmatched positions. Notional principal amounts often are used to express the volume of these transactions, but the amounts potentially subject to credit risk are much smaller. The notional principal amount of interest rate swap contracts outstanding at June 30, 1997 was approximately \$320.4 million where GDB is the fixed rate payer and the counterparts are the floating rate payer using LIBOR or S&P rates. Settlements are made monthly.

GDB issues commercial paper in the United States taxable and tax exempt commercial paper markets, the Euro-dollar commercial paper market and to corporations that have tax exemption under the Commonwealth's Industrial Incentive Act, and that qualify for benefits provided by the US Internal Revenue Code Section 936. Commercial paper represents unsecured obligations of GDB. The carrying amount of commercial paper at June 30, 1997 was approximately \$1.115 billion, the maximum amount outstanding at any month-end was approximately \$1.733 billion, the weighted average amount outstanding during the year was approximately \$1.411 billion, and the weighted average interest rate for the year and at year end was approximately 3.97% and 4.37%, respectively.

During 1996 GDB designated certain real estate for the site to be known as the Puerto Rico Art Museum. The Museum has been organized as a nonprofit organization which will have a separate board of directors. GDB intends to invest approximately \$55 million in refurbishing the property. At June 30, 1997, the amount incurred in connection with the project and charged to operations was approximately \$6.1 million.

#### **Puerto Rico Electric Power Authority (PREPA)**

The Puerto Rico Electric Power Authority is required to make contributions to the Commonwealth, and to the municipalities, to the extent net revenues (as defined by the bond indentures of PREPA), are available. For the year ended June 30, 1997, PREPA contributed approximately \$12.7 and \$78.9 million, to the Commonwealth and to the municipalities of Puerto Rico, respectively.

Retained earnings at June 30, 1997 include approximately \$86.7 million to provide for damaged or destroyed property not covered by insurance as required by the 1974 Trust Agreement. In addition, PREPA is self-insured for its transmission and distribution lines. Transmission and distribution lines amounted to approximately \$2.054 billion at June 30, 1997.

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. In February 1992, the Environmental Protection Agency (EPA) performed an inspection of various facilities of PREPA and noted deficiencies in different areas. EPA is claiming alleged civil violations for \$50 million. Since 1993, the EPA, the Federal Department of Justice (DOJ) and PREPA have been involved in negotiations to pursue a comprehensive settlement of the case and assure future compliance with applicable regulatory provisions. Among other things, the settlement proposal considers investment in capital improvements and Supplemental Environmental Projects estimated at approximately \$81 million during the five fiscal years ending June 30, 1998. Also, PREPA agreed to other conditions, with an additional annual cost of approximately \$54 million.

On October 27, 1993, DOJ and EPA filed a complaint in the United States District Court for the District of Puerto Rico based upon the above violations. PREPA and EPA undertook negotiations to resolve the issues and to ensure future compliance with all applicable regulations. As a result of the negotiations, PREPA and EPA, with the active participation of the United States Department of Justice, reached an agreement which resulted in a proposed Consent Decree. In the proposed Consent Decree, PREPA agreed to pay a civil penalty of \$1.5 million, to implement additional compliance projects costing \$4.5 million, both which the PREPA has accrued as of June 30, 1997, and to undertake improvements to its existing compliance programs and its operations in order to assure compliance with environmental laws and regulations.

The Consent Decree was signed on December 19, 1996 and filed on January 10, 1997 in the United States District Court for the District of Puerto Rico for approval. The Department of Justice extended the comment period up to June 18, 1997. Comments received are being evaluated by PREPA and EPA.

On August 25, 1992, PREPA entered into an agreement with a private party for the construction of a 249 megawatt generation plant of open cycle combustion turbines. PREPA's estimated obligation under this agreement amounts to approximately \$147.3 million, as amended. The total obligation under the agreement will be subject to price adjustments (escalation formula). At June 30, 1997, the Authority had incurred construction costs amounting to approximately \$155.7 million.

#### **Puerto Rico Aqueduct and Sewer Authority (PRASA)**

PRASA is a defendant or co-defendant in various claims for damages and lawsuits for approximately \$80.3 million. Most of the cases are pending trial or final judgment. Management of PRASA and legal counsel are of the opinion that any liability that may result from such claims and lawsuits would not have a material adverse effect on PRASA's financial position as of June 30, 1997.

Facilities and operations of PRASA's system are subject to regulation under numerous Federal and Commonwealth environmental laws, including the Federal Clean Water Act (the Act), administered by the Environmental Protection Agency (EPA). In January 1978, the United States, acting on behalf of EPA initiated litigation against PRASA and the Commonwealth to enforce compliance with the Act, with respect to violations of the Act occurring at numerous plants in the Authority's sewer system. On April 20, 1988, PRASA and EPA reached an agreement to settle and resolve all the outstanding and claimed assessment amounts embodied in a Supplemental Consent Order modifying the Final Order (the 1988 Supplemental Order). The 1988 Supplemental Order was entered by the Court on September 27, 1988, in substantially the form lodged. Provisions of the 1985 Order not amended or replaced by the 1988 Supplemental Order remain in effect. The outstanding noncompliance penalty pending before the Court amounts to approximately \$3.3 million as of June 30, 1997. PRASA estimates that the capital cost of complying with the terms of the 1988 Supplemental Order will be approximately \$300 thousand through fiscal year 1998. These costs are included in PRASA's capital improvement program. Amounts required to insure compliance with the 1988 Supplemental Order are expected to be derived from a combination of appropriations to be made by the Commonwealth, Federal Government grants and loans and future revenue bonds of PRASA.

On August 1, 1997, the United States and PRASA lodged a proposed consent decree with the United States District Court for the District of Puerto Rico. The consent decree, pending Court approval, resolves the claims against PRASA regarding the compliance of its National Pollutant Discharge Elimination System (NPDES) at Mayaguez. PRASA will pay \$150 thousand and perform activities



directed at either constructing facilities necessary to meet NPDES permit compliance, or if authorized by Congress and EPA, construct an outfall away from its present location farther out to sea at an estimated cost of \$35 million. In addition, will need to comply with interim effluent limitations and pay \$400 thousand over three years for the development of a comprehensive watershed management plan for the Añasco River.

On December 5, 1995, the Court approved the PRASA and EPA Consent Decree lodged by PRASA and EPA. The Consent Decree provides for the construction of sludge treatment facilities for the filter backwash discharges of eight (8) major water treatment plants. The PRASA paid to the Treasury of the United States \$200 thousand. PRASA estimates that the capital cost of complying with the terms of the Consent Decree will be approximately \$14.4 million through June 30, 2001. PRASA, also, subscribed concurrently to an Administrative Order and Consent for the construction of sludge treatment facilities at seventy-four (74) other minor water treatment plants which requires a capital cost of \$41.4 million during fiscal years 1998 through 2000. Quarterly Compliance Reports, in which self-assessed noncompliance penalties were made for the eight plants subject to the Consent Decree, were submitted to EPA. For the fiscal year ended June 30, 1997, self assessments paid amounted to \$441 thousand.

On May 26, 1995, PRASA and Professional Services Group, Inc. (PSG) entered into an agreement (Agreement) for the operation, management, repair and maintenance of PRASA's aqueduct, sewer and customer services systems (System). The Agreement commenced on September 1, 1995 for a five-year term, but is cancelable at PRASA's option, without cause, at the third anniversary date of the operations date, as defined. PRASA will pay PSG for reimbursement of expenses and for administrative fees between \$96.5 and \$98 million in years one through four, and \$16 million in year five. A portion of PRASA's payment obligations to PSG will be guaranteed by the Government Development Bank for Puerto Rico up to \$10 million in each of the first three years, if PRASA does not otherwise have the cash available for such payments.

On January 31, 1996, PRASA entered into an agreement for the planning, design, construction, operation and maintenance, as defined, of the North Coast Superaqueduct Project (the Project), to supply additional potable water to certain municipalities. The total estimated cost for the project is approximately \$305 million. The Government Development Bank for Puerto Rico has committed to provide interim financing for this project up to \$305 million and is expected that this amount shall be repaid from Commonwealth appropriations in the future. The Commonwealth provided approximately \$19 million of appropriations for the year ended June 30, 1997.

The estimated cost of construction of contracts in progress at June 30, 1997 amounted to approximately \$480 million.

#### **Puerto Rico Telephone Authority and Subsidiary, and Puerto Rico Telephone Company (PRTA)**

In September 1993, the National Exchange Carrier Association informed PRTA that they would not accept the inclusion of the additional in-lieu-of taxes payment corresponding to 1992, for interstate settlement purpose unless the PRTA obtains approval from the Federal Communications Commission (FCC). On November 30, 1993, the PRTA submitted a request for ruling by the FCC on the issue. On February 5, 1997, the FCC concluded that PRTA could not include additional payments in-lieu-of taxes for interstate settlement purposes. On March 6, 1997, PRTA filed a petition for reconsideration with the FCC seeking a reversal of the decision. The amount of the potential liability is recorded in PRTA's financial statements as of December 31, 1996.

During the year ended December 31, 1996, PRTA made operational contributions to the Puerto Rico Public Broadcasting Corporation, a discrete component unit of the Commonwealth, amounting to approximately \$15.5 million.

PRTA has entered into an interest rate swap agreement to reduce the impact of changes in interest rates on its variable interest rate subordinated notes. The interest rate swap agreement requires PRTA to pay a fixed rate while receiving amounts at a variable rate based on LIBOR, settled every six months, on notional principal amounts ranging from a high of approximately \$6.2 million up to February 15, 1997, to a low of \$1.3 million from February 15, 1999 to August 15, 1999, dates of maturity of the notes and the swap agreement. As a result of this agreement, the effective rate on the variable interest rate subordinated notes of approximately \$9.4 million was 5.32% at December 31, 1996. The obligations of the other party in the agreement have been guaranteed by its parent company. PRTA is exposed to credit loss in the event of nonperformance by the other party to the interest rate swap agreement. However, PRTA does not anticipate nonperformance by the counterparty.

PRTA is organized under the laws of the state of Delaware, USA. As such, PRTA is subject to United States federal income taxes. The United States Internal Revenue Code, Section 936, allows certain income tax benefits to United States corporations deriving substantially all of their income from sources within possessions of the United States, including Puerto Rico. PRTA has exercised the corresponding election to claim these benefits and has complied with the requirements of the United States Internal Revenue Code; accordingly, liability for US federal income taxes, if any, would arise only on income from sources outside Puerto Rico. PRTA elected to compute its credit under the economic activity method, which provided in fiscal year 1996 a credit in excess of the credit needed to offset any U.S. federal income tax liability.

On August 20, 1996, the U.S. Congress enacted the Small Business Job Protection Act of 1996 (the "Act"). Under the Act, the tax credits allowable on business income under Section 936 are restricted for taxable years beginning between the period from January 1, 2002 and December 31, 2005. Thereafter, all such credits will be eliminated.

On August 10, 1993, the President of the United States signed into law The Omnibus Budget Reconciliation Act of 1993 (the Act). The Act enacts significant tax changes including a provision that the Section 936 credit allowed to a possession corporation for a taxable year against US tax on its business income would be computed as under present laws, but would be subject to one of two alternative limitations. Under the alternative limitation method selected by PRTA, there was no tax liability for the year ended December 31, 1996.

On April 7, 1997, the Governor of Puerto Rico announced the intention of the Commonwealth of Puerto Rico to sell PRTA and its subsidiaries. This sale is expected to be completed within one year, subject to approval of the related legislation by the Legislature of Puerto Rico.

The consolidated construction program for 1997 amounts to approximately \$384 million.

#### **Puerto Rico Industrial Development Company (PRIDCO)**

PRIDCO estimates expenditures of approximately \$35 million for construction, land acquisition and development for the year ending June 30, 1998. The expenditures will be financed through internally generated funds, federal grants and external financing sources.

A significant amount of PRIDCO's revenues is derived from United States mainland companies most of which operate in Puerto Rico under the benefits of US Internal Revenue Code Section 936. On August 20, 1997, the President of the United States signed into law a minimum wage legislative package which, among other matters, eliminated US Tax Code Section 936. However, the management of PRIDCO does not foresee a major impact in PRIDCO's operations due to the elimination of Section 936.

#### **Puerto Rico Infrastructure Financing Authority (PRIFA)**

The law that created PRIFA requires that, up to fiscal year ending June 30, 2018 the first \$40 million of Federal excise taxes refunded to the Commonwealth shall be deposited in PRIFA, which in turn shall deposit such funds as needed to meet debt service requirements of PRIFA. If the Federal excise taxes received are not sufficient to provide for the \$40 million deposit, PRIFA shall request from the Commonwealth's Office of Management and Budget to appropriate such required amounts. However, the Commonwealth is not legally obligated to make such appropriation.

PRIFA has provided financing assistance to the Puerto Rico Aqueduct and Sewer Authority (PRASA), a discretely presented component unit, since January of 1990. On October 4, 1995, PRIFA provided a line of credit to PRASA in the amount of approximately \$118.3 million, to refinance previous loans, and to provide additional funds for capital improvements. This line of credit bears interest at a variable rate. On June 4, 1996, this loan was increased to approximately \$158.3 million to cover additional capital improvements. At June 30, 1997, the outstanding balance is approximately \$149.1 million, at a variable interest rate between 4.82% and 6.81%.

#### **Puerto Rico Housing Bank and Finance Agency (PRHBFA)**

The PRHBFA is an "Eligible Similar Institution", as defined by the Puerto Rico Commissioner of Financial Institutions. Such designation allows PRHBFA to receive up to \$250 million in eligible funds (commonly known as "936 tax exempt funds") which are received through obligation under reverse repurchase agreements and used for an arbitrage program. At June 30, 1997, PRHBFA has approximately \$250 million in such funds, through obligations under reverse repurchase agreements. On August 20, 1997, the President of the United States signed into law a minimum wage legislative package which, among other matters, eliminated US Tax Code Section 936. The effect of such elimination has not been determined by the management of PRHBFA.

The \$250 million of 936 funds received under reverse repurchase agreements are presented as a liability in the general purpose financial statements at June 30, 1997. As of June 30, 1997, the aggregate market value plus accrued interest exceeds by approximately \$2 million the obligations under reverse repurchase agreement including interest.

PRHBFA guarantees mortgage loans sold to third parties. At June 30, 1997, the outstanding balance of such mortgage loan was approximately \$9.4 million.

#### **Land Authority of Puerto Rico (LAPR)**

LAPR is a defendant under a claim brought by a group of pineapple farmers amounting to approximately \$111 million. LAPR is litigating this action, but the ultimate outcome cannot be presently determined due to the stage of proceedings. Accordingly, no provisions for any liability that may result upon a final resolution of these actions has been made in the financial statements of LAPR.

## **Corporation of Stocks and Deposit Insurance for the Savings and Loans Cooperatives (CSDISLC)**

CSDISLC was a defendant in a case where the plaintiffs claimed damages allegedly suffered due to the imposition by CSDISLC of a special premium and requested that the special premium be deemed illegal and therefore eliminated. During fiscal year 1997, the court ruled in favor of CSDISLC and, consequently, the amount of \$5.2 million assessed to the insured cooperatives previously recorded as deferred revenue was credited to income during fiscal year 1997.

At June 30, 1997, the maximum limit of the insurance coverage was \$50 thousand per member or depositor, and may be increased annually to a maximum of \$100 thousand. Effective July 1, 1997, such insurance coverage was increased to \$75 thousand. The total shares and deposits of insured cooperatives as of June 30, 1997 approximated \$3.5 billion.

Under the terms of certain merger agreements for troubled cooperatives, CSDISLC has agreed to repurchase certain loans. CSDISLC's management is of the opinion that any liability ultimately arising from these agreements will not be material.

## **Economic Development Bank for Puerto Rico (EDB)**

Time deposits of approximately \$235.7 million at June 30, 1997 consist principally of certificates of indebtedness from eligible or similar depository institutions which are recipients of funds from corporations that have grants of tax exemptions under the Commonwealth's Industrial Incentives Act, and that qualify for the benefits provided under US Internal Revenue Code Section 936, pursuant to the investment requirements under Regulation 5105 of the Commissioner of Financial Institutions of the Commonwealth. On August 20, 1997, the President of the United States signed into law a minimum wage legislative package which, among other matters, eliminated the US Internal Revenue Code Section 936. The effect of this elimination on these deposits can not be determined.

The EDB enters into interest rate swaps as part of its asset/liability management. Interest rate swaps involve the exchange of fixed and floating rate payment obligations without the exchange of the underlying principal amounts. Entering into interest rate exchange agreements involves the risk of dealing with counterparts and their ability to meet the terms of the contracts. Notional principal amounts often are used to express the volume of these transactions, but the amounts potentially subject to credit risk are much smaller. The notional principal amount of interest rate swap contracts outstanding at June 30, 1997 was approximately \$15 million where the Bank is the fixed rate payer and the counterparts are the floating rate payer using LIBOR rate. Settlements are made monthly. EDB is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreements. However, the Bank does not anticipate nonperformance by the counterparts.

## **Sugar Corporation of Puerto Rico (SCPR)**

SCPR is a defendant in various legal actions and has recorded a reserve for possible losses of approximately \$9.9 million; however, the ultimate outcome of these actions cannot presently be determined and it is not presently known whether this reserve will be sufficient to provide for possible losses as a result of the final outcome of such claims. SCPR depends on subsidies from the Commonwealth to provide the necessary funds to cover cash deficits. During the year, subsidies to finance cash deficit amounted to \$12 million.

During the year ended December 31, 1994, SCPR closed the operation of certain sugar mill operations which resulted in the disbursement of severance compensation to laid-off employees for approximately \$2.3 million for the year ended December 31, 1996 (See Note 26).

#### **Tourism Company of Puerto Rico (TCPR)**

TCPR has entered into several agreements with private third parties to make capital contributions and investments in several hotel development projects. At June 30, 1997, capital contributions made amounted to approximately \$37.3 million.

In June 1997, TCPR discontinued the operations of a hotel and convention center complex. In connection with the closing, TCPR was committed to certain payments to the hotel and convention center complex's employees. TCPR maintains an accrual of approximately \$2.9 million to cover these and other related costs.

#### **Puerto Rico Solid Waste Authority (PRSWA)**

PRSWA initiated in 1996 the implementation and development of the first stage of the Infrastructure Regional Plan for Recycling and Disposal of Solid Waste in Puerto Rico at an estimated cost of approximately \$43 million. The first stage consist of the construction of seventeen projects to be financed through an interim financing agreement with the Government Development Bank for Puerto Rico, a discrete component unit, of which \$20 million were approved through a line of credit.

As of June 30, 1997 PRSWA is committed with various municipalities and governmental agencies to acquire the land in which the projects will be developed.

The Authority is also in negotiations with the Puerto Rico Aqueduct and Sewer Authority to purchase two yard waste composting plants at Mayagüez and Arecibo respectively, with an estimated total cost of \$13 million.

## **22. RETIREMENT SYSTEMS**

The Commonwealth has three contributory defined benefit pension plans which are reported in the pension trust fund:

- Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities
- Puerto Rico Judiciary Retirement System
- Annuity and Pension System for the Teachers of Puerto Rico

Each system is independent, thus assets may not be transferred from one system to another or used for any purpose other than to benefit each system's participants. In addition, the University of Puerto Rico Retirement System audited financial statements are included in the public university funds.

The retirement systems issue publicly available financial reports that include their financial statements and required supplementary information for each of them. Those reports may be obtained by writing to the corresponding administrator of each retirement system at the addresses detailed in Note 1 to the general purpose financial statements.

The pension plans engaged from time to time in securities lending transactions as authorized by local laws and regulations. Credit risk is controlled and monitored by the securities brokers and dealers contracted by the pension plans. There were no securities lending transactions during the year ended June 30, 1997.

**Employees' Retirement System of the Government of PR and Its Instrumentalities (ERS)**

**Plan Description:**

The ERS is the administrator of a single-employer (as related to the Commonwealth financial reporting entity) defined benefit pension plan established by the Commonwealth. The System was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems.

The System provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation.

**Funding Policy:**

Contribution requirements are established by law and are as follows:

Commonwealth	9.275% of gross salary
Employees:	
Hired on or before March 31, 1990	5.775% of gross salary up to \$6,600 8.275% of gross salary over \$6,600
Hired on or after April 1, 1990	8.275% of gross salary

## **Puerto Rico Judiciary Retirement System (JRS)**

### **Plan Description:**

The JRS is a single-employer defined benefit plan which is administered by the ERS. The System was created under Act 12, approved on October 19, 1954. The membership includes all individuals holding a position as Judge of the Supreme Court, Judge of the Superior Court or the District Court or Municipal Judges of the Commonwealth of Puerto Rico.

The System provides retirement as well as death and disability benefits. Benefits vest after 10 years of service.

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 three years of service (effective July 28, 1993, highest annual salary), except for judges of the Supreme Court for whom it is based on the last month of compensation. The retirement annuity is limited to a minimum of 25% and a maximum of 100% of the average compensation.

### **Funding Policy:**

All participants are required to make contributions to the plan equal to 8% of gross salary. The Commonwealth must contribute 20% of the applicable payroll. Contributions are established by law, and are not actuarially determined.

## **Annuity and Pension System for the Teachers of Puerto Rico (TRS)**

### **Plan Description:**

The TRS is a single-employer defined benefit plan (as related to the Commonwealth's financial reporting entity) which was created under Act 218 approved on May 6, 1951. TRS provides retirement benefits to all teachers of the Department of Education of the Commonwealth, those holding positions in the Retirement Board, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education.

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 final average salary, which is the highest average over three years. The Retirement Annuity is a minimum of \$300 per month and a maximum of 75% of final average salary.

Funding Policy:

A member should contribute to the plan 7% of total salary. The Commonwealth matches the member's contribution at a rate of 8.5% of total salary. Contribution rates are established by law, and are not actuarially determined.

Membership:

	ERS	JRS	TRS
Retirees and beneficiaries currently receiving benefits	67,700	230	17,901
Current Employees	<u>159,600</u>	<u>306</u>	<u>43,432</u>
Total	<u>227,300</u>	<u>536</u>	<u>61,333</u>

Annual Pension Cost and Net Pension Obligation:

The Commonwealth's annual pension cost and net pension obligation to the three pension plans for the year ended June 30, 1997 were as follows (expressed in thousands):

	ERS	JRS	TRS
Annual required contributions	\$ 722,270	\$ 1,894	\$ 112,198
Interest on net pension obligation	117,302	(806)	18,617
Adjustment to annual required contribution	<u>(177,254)</u>	<u>1,218</u>	<u>(13,531)</u>
Annual pension cost	662,318	2,306	117,284
Statutory contributions made	454,600	5,900	82,431
Estimated interest for six months at 8.5%	19,930	215	-
Increase (decrease) in net pension obligation	187,788	(3,809)	34,853
Net pension obligation (asset) at beginning of year	<u>1,380,022</u>	<u>(9,480)</u>	<u>232,716</u>
Net pension obligation (asset) at end of year	<u>\$ 1,567,810</u>	<u>\$ (13,289)</u>	<u>\$ 267,569</u>

The net pension obligation for ERS and TRS of approximately \$1.8 billion is recorded in the general long-term debt account group. (See Note 15). No asset is recognized for JRS excess of contributions over annual pension costs due to the measurement focus of the general fund.



The annual required contribution was determined by actuarial valuations for each of the pension plans as described below:

	ERS	JRS	TRS
Date of actuarial valuation	July 1, 1997	July 1, 1997	July 1, 1996
Actuarial cost method	Projected unit credit cost	Projected unit credit cost	Entry age normal
Amortization method	Level percentage of the projected payroll	Level percentage of the projected payroll	Level percent, closed
Remaining amortization period	29 years	29 years	24 years
Amortization approach	Closed	Closed	Closed
Asset valuation method	Market value	Market value	Market value
<b>Actuarial assumptions:</b>			
Inflation	3.5%	3.5%	3.5%
Investment rate of return	8.5%	8.5%	8.0%
Projected salary increases	5%	5%	5.0%
Cost of living adjustments	3% every three years	3% every three years	No future retiree increases assumed

Three Year Trend Information:

The three-year trend information is as follows (expressed in thousands):

<b>Annual Pension Cost (APC):</b>	ERS	JRS	TRS
Year Ended June 30, 1997	\$662,318	\$2,306	\$117,284
Year Ended June 30, 1996	627,205	2,750	113,806
Year Ended June 30, 1995	567,425	2,967	95,924
<b>Percentage of APC Contributed:</b>	ERS	JRS	TRS
Year Ended June 30, 1997	68.6%	255.8%	70.2%
Year Ended June 30, 1996	63.3%	158.0%	69.7%
Year Ended June 30, 1995	65.0%	153.8%	75.1%
<b>Net Pension Obligation (Asset):</b>	ERS	JRS	TRS
Year Ended June 30, 1997	\$1,567,810	\$(13,289)	\$267,519
Year Ended June 30, 1996	1,380,022	(9,480)	232,716
Year Ended June 30, 1995	1,149,743	(7,462)	198,234

Schedule of Funding Progress (expressed in thousands):

Employees Retirement System of the Government of Puerto Rico:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 1997	\$1,444,000	\$ 6,914,000	\$5,470,000	21%	\$2,363,000	231%
July 1, 1996	1,230,000	6,320,000	5,090,000	19%	2,223,000	229%
July 1, 1995	1,075,000	6,033,000	4,958,000	18%	2,087,000	238%

Puerto Rico Judiciary Retirement System:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 1997	\$57,300	\$76,500	\$19,200	75%	\$18,000	107%
July 1, 1996	50,000	63,100	13,100	79%	16,600	79%
July 1, 1995	42,100	60,800	18,700	69%	15,800	118%

Teachers Retirement System:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 1996	\$1,653,000	\$2,616,000	\$ 963,000	63%	\$838,000	115%
July 1, 1995	1,474,000	2,600,000	1,126,000	57%	849,000	133%
July 1, 1994	1,231,000	2,272,000	1,041,000	54%	729,000	143%

**D. University of Puerto Rico Retirement System**

Plan Description:

The University of Puerto Rico (the University) contributes to the University of Puerto Rico Retirement System (UPRRS), a single-employer defined benefit public employee retirement system that acts as a common investment and administrative agent for the University. The System is the administrator of the plan created under Act No. 135, approved on May 7, 1942, and became effective on January 1, 1945. UPRRS covers all employees of the University, except hourly, temporary, part time, contract and substitute employees, and visiting professionals.

The System provides retirement, disability, and death benefits. Cost-of-living adjustments are provided at the discretion of the Board of Trustees. 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 of the members average compensation.

Funding Policy:

University employees are required to contribute 4% to 8% of their annual salary to the System, depending on certain qualifications. The University is required to contribute 15% of applicable payroll, for 1997 which increased from 14% during 1996 . The contributions are established by law, and are not actuarially determined. Although the University has not expressed any intent to terminate the Plan administered by the System, it may do so at any time. In the event of termination, the rights of participants and beneficiaries are non-forfeitable to the extent funded.

During fiscal 1997, the University of Puerto Rico offered employees with 30 years of service the option of early retirement either on September 30, 1997 or January 31, 1998.

Membership:

Retirees and beneficiaries currently receiving benefits	4,760
Terminated-vested	6,980
Current employees	<u>12,133</u>
	<u>23,873</u>

Annual Pension Cost and Net Pension Obligation:

The University's annual pension cost and net pension obligation to the System for the year ended June 30, 1997 is as follows (expressed in thousands):

Annual required contributions	\$43,544
Interest on net pension obligation	2,741
Adjustment to annual required contribution	<u>(2,671)</u>
Annual pension cost	43,614
Contributions made	<u>46,601</u>
Decrease in net pension obligation	(2,987)
Net pension obligation at beginning of year	<u>34,260</u>
Net pension obligation at end of year	<u>\$31,273</u>

The annual required contribution was determined as part of the June 30, 1997 actuarial valuation using the entry age actuarial cost method. The actuarial assumptions included (a) 8% investment rate of return and (b) projected salary increases of 5% per year. The assumptions did not include postemployment benefit increases, which are funded by the University when granted. The actuarial value of assets is equal to the fair value of the assets. The unfunded accrued liability is being amortized as a level dollar on a declining basis from 40 to 30 years starting on June 30, 1995. The remaining amortization period at June 30, 1997 is 38 years.

Three Year Trend Information (expressed in thousands):

Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
June 30, 1997	\$43,614	106.8%	\$31,273
June 30, 1996	40,982	101.3%	34,260
June 30, 1995	38,795	94.0%	34,794

Schedule of Funding Progress (expressed in thousands):

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll**	UAAL as a Percentage of Covered Payroll
June 30, 1997	\$505,467	\$957,716	\$452,249	52.8%	\$305,498	148.0%
June 30, 1996	427,435	912,242	484,807	46.9%	283,798	170.8%
June 30, 1995*	382,934	856,494	473,560	44.7%	261,466	181.1%
June 30, 1993*	343,302	748,243	404,941	45.9%	221,986	182.4%

\* Changes in plan benefit provisions

\*\* Rate of pay as of the valuation date.

**23. SEGMENT INFORMATION - Enterprise Funds**

**Health Facilities and Services Administration of Puerto Rico (HFSA)**

Health Facilities and Services Administration of Puerto Rico (HFSA) was created as an executive agency in 1975 to lease and operate hospitals and other health facilities and to provide for the improvement, alteration or repair of such facilities. HFSA is authorized to borrow money and issue notes or other obligations for the purpose of financing the costs of improvements and providing health services to the general public. Patients, admitted to an institution under the jurisdiction of HFSA who are indigent, receive hospital and medical services free of charge; otherwise, payments for services rendered are required.

On February 1, 1993, the Commonwealth enacted legislation that changed the functions of HFSA from health care provider to regulator and evaluator of health care services provided by private corporations. The health services are to be provided in the facilities of HFSA, for a rental fee, and in privately owned units. HFSA will continue to operate until all its facilities are privatized. Afterwards, its resources will be combined with that of the Puerto Rico Health Department, an executive agency of the Commonwealth.

### Lottery of Puerto Rico (Lottery)

The Lottery was created in 1947 and is an operational unit of the Commonwealth's Treasury Department. It was created to provide authorized agents with an additional source of revenues and to supplement revenues for the general fund of the Commonwealth. It is engaged in the sale of tickets through authorized agents. The Lottery's revenues from the sale of tickets are distributed pursuant to the approved budget to cover the payment of prizes and general and administrative expenses. The excess of revenues over prizes and expenses must be transferred to the general fund of the Commonwealth.

### The Additional Lottery System (Additional Lottery)

The Additional Lottery was created in 1989 as an operational unit of the Commonwealth's Treasury Department. Presently, two games (Pick 3 and Lotto) with several betting alternatives are offered. The Additional Lottery is required to remit the excess of revenues over expenses to the Commonwealth. Deficits are not allowed to be offset against the excess of revenues over expenses. Remittances are earmarked as follows: 5% of the excess of revenues over expenses (net revenues) to a Contingency fund, 35% of remaining balance to the Municipal Autonomy fund, and the rest to the Commonwealth. Prizes expire in 180 days. Expired prizes transferred to the general fund during 1997 approximated \$2.2 million.

### Puerto Rico Highway and Transportation Authority (PRHTA) (Enterprise fund only)

PRHTA is a blended component unit, created to provide roads and other transportation facilities for the planning, promotion and feasibility of mass transportation systems. (See Note 1).

Segment information for the enterprise funds is as follows (expressed in thousands):

	HFSA	Lottery of PR	Additional Lottery	PRHTA
Operating revenues	\$ 202,995	\$457,462	\$215,596	\$ 3,611
Depreciation and amortization	25,945	661	45	676
Operating income (loss)	(509,086)	62,459	73,480	(8,065)
Intergovernmental revenues	2,173			
Non-operating revenues	32,414	982		
Operating transfers-in (out)	374,231	(63,435)	(73,480)	7,389
Net income (loss)	(169,442)	6		(676)
Current capital:				
Contribution		667		
Depreciation on contributed fixed assets		(661)		(676)
Property, plant and equipment:				
Additions and adjustments	13,555	310	43	115,890
Deletions and adjustments	6,014			
Net working capital (deficit)	(167,491)	590		
Long-term liabilities	903,593	1,337	185,816	9,460
Total assets	478,480	46,720	189,418	184,590
Total equity (deficit)	(688,571)	760	(1,365)	175,130

## 24. SUBSEQUENT EVENTS

### Primary Government

As part of the Health Care Reform, the Department of Health (the Department) and the Health Facilities and Services Administration of Puerto Rico (HFSA) have entered into various lease agreements as lessors for certain property which consists principally of health facilities. On October 8, 1997, the Department and HFSA had to take over the health facilities of nine institutions which were not being administered according to contracted terms.

On July 16, 1997, Law Number 34 was approved to assign additional recurring revenues to the Puerto Rico Highway and Transportation Authority (PRHTA) up to a maximum of \$10 million monthly derived from excise taxes over crude oil and its derivatives.

In addition, on July 18, 1997, PRHTA requested a line of credit of \$100 million with the Government Development Bank for Puerto Rico expiring on July 1, 1999. This line of credit will be paid with the proceeds of future bond issuance.

During December 1997, the Commonwealth issued \$600 million of tax and revenues anticipation notes due in July 1998.

The Government Development Bank for Puerto Rico approved two \$150 million lines of credit for the Commonwealth. The proceeds from one of the lines is to be used to provide interim financing for capital projects. This line is to be repaid with the proceeds from a future general obligations bond issuance.

The second line of credit is to provide cash to cover the temporary needs of the Commonwealth for operational purposes. This line of credit is to be repaid from the proceeds of the Bond Issuance of \$600 million of Tax and Revenue Anticipation Notes Series 1998A of December 1997.

### Component Units - Other

#### **Puerto Rico Electric Power Authority (PREPA)**

On July 10, 1997, PREPA issued \$128.7 million Power Revenue Bonds with an average interest rate of 5.13% to advance refund \$127.1 million of outstanding Series N and O. The net proceeds of \$129.7 million (after a premium of \$2 million and payment of \$1 million in underwriting fees, insurance and other issuance costs) were used to purchase U.S. Treasury securities. Those securities were deposited in irrevocable trusts with an escrow agent to provide for all future debt service payments. PREPA defeased the bonds to reduce its total debt service payments over the next 13 years by almost \$9.6 million, an accounting loss of \$17.6 million and to obtain an economic gain (difference between the net present value of the old and new debt service payments) of \$7.5 million.

#### **Tourism Company of Puerto Rico (TCPR)**

On August 8, 1997, TCPR loaned Waterfront Hotel Associates, S.E. \$4 million. At September 10, 1997 there was no definite interest rate nor repayment term for this loan.

On September 10, 1997 TCPR delivered a letter of intent to Atlantic Gulf Communities Corp. for the sale of the Condado Beach Trio. The sale is expected to be consummated during fiscal year 1998.

**Puerto Rico Aqueduct and Sewer Authority (PRASA)**

On October 23, 1997, the Government Development Bank for Puerto Rico, a discrete component unit, approved increases of \$100 million in the \$464.8 million line of credit and \$40 million in the \$305 million line of credit to cover additional estimated costs for the Superaqueduct Project.

**Puerto Rico Infrastructure Financing Authority (PRIFA)**

On July 7, 1997, the Commonwealth Legislature enacted legislation which, among other, amends Act No. 44 by increasing the amount of excise taxes to be transferred to PRIFA as follows (expressed in thousands):

<b>Fiscal Year</b>	<b>Maximum Amount</b>
1998	\$60,000
Each subsequent fiscal year up to 2028	70,000

The increase is expected to allow the Government Development Bank for Puerto Rico (GDB), a discrete component unit, to consider financing opportunities for PRIFA in order to reduce the regular line of credit granted by GDB to the Puerto Rico Aqueduct and Sewer Authority, or to implement any other financial mechanism to achieve said purpose.

The new legislation also establishes a Commonwealth Potable Water Rotating Fund with the purpose of receiving financial assistance under the Federal Clean Water Act, and provides for the participation of PRIFA in the administration of said fund.

During December 1997, PRIFA issued \$800 million of special Tax Revenue Bonds.

**25. PARTIAL SETTLEMENT OF CONTINGENCY**

On January 22, 1996, the US District Court in Puerto Rico consolidated all cases against the Commonwealth related to the complaints filed in 1979 by the inmates of the correctional facilities in Puerto Rico. The Court ruled a permanent order requiring the Commonwealth to comply with the requirement of the minimum fixed living space per inmate. In the opinion of management, based on advice of their legal counsel, this order will limit the imposition of further fines and the fines already paid together with the accrued liability in the general long-term debt account group, (which amount to approximately \$200 million at June 30, 1997) shall be sufficient to carry out the Court's requirements.

## 26. SUGAR CORPORATION OF PUERTO RICO

On September 5, 1996 the Commonwealth enacted Law No. 189 to authorize the negotiation for the transfer of certain assets, liabilities and operations of the Sugar Corporation of Puerto Rico (SCPR), for a nominal value, to the sugar cane farmers. The effective date and final terms have not been yet determined. Until such agreement is completed and approved by the Land Authority of Puerto Rico, (the parent company of SCPR), and the Legislature of Puerto Rico, SCPR will continue as a going concern. At December 31, 1996, SCPR has an accumulated deficit of approximately \$153.7 million, and contributed capital of approximately \$168.9 million. Should the negotiation be completed, the enabling law also provides for the liquidation of the remaining assets and liabilities of SCPR after the transfer. Management of SCPR expect the negotiations to be completed during natural year 1998.



**COMBINING, INDIVIDUAL FUND  
FINANCIAL STATEMENTS AND SCHEDULES**



## **GENERAL FUND**

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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. Following is the Schedule of Revenues and Expenditures - Budget to Actual - Budget Basis.



COMMONWEALTH OF PUERTO RICO

SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
 BUDGET BASIS - GENERAL FUND  
 YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Budget	Actual	Variance Favorable (Unfavorable)
EXPENDITURES:			
Current:			
General government:			
Comptroller's Office	\$ 17,216	\$ 17,214	\$ 2
Governor's Office	12,577	12,566	11
Office of Management and Budget	22,625	22,622	3
Planning Board	9,805	9,787	18
Constructions and Land Subdivisions Appeals Board	784	780	4
Department of State	8,607	8,565	42
Department of Treasury	123,346	122,854	492
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	21,749	21,749	
Personnel Administration Central Office	5,779	5,779	
Commonwealth Electoral Commission	36,063	31,239	4,824
Federal Affairs Administration	9,332	9,332	
General Services Administration	2,201	2,061	140
Department of Justice	10,115	10,115	
Office of the Citizens Ombudsman	1,799	1,799	
Department of Health	160	160	
Personnel Administration System Appeals Board	812	812	
Regulations and Permits Administration	12,106	12,106	
Municipal Complaints Hearing Commission	118	118	
Legislative Assembly	49,679	48,949	730
Public Policy and Organization Bureau	364	364	
Strategic Development Secretariat	162	162	
Central Communications Office	2,649	2,649	
Government Ethics Office	2,519	2,517	2
Total General government	350,567	344,299	6,268

COMMONWEALTH OF PUERTO RICO

SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
 BUDGET BASIS - GENERAL FUND  
 YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Budget	Actual	Variance Favorable (Unfavorable)
Public safety:			
General Court of Justice	149,512	149,490	22
Civil Defense State Agency	2,467	2,376	91
Investigation, Prosecution, and Appeals Commission	508	508	
Civil Rights Commission	388	387	1
Department of Justice	70,031	69,570	461
Puerto Rico Police Department	443,568	442,689	879
Puerto Rico Firefighters Corps and Medical Emergency Services	34,712	34,701	11
Puerto Rico National Guard	9,553	9,523	30
Public Service Commission	5,980	5,980	
Consumer Affairs Department	8,687	8,687	
Juvenile Institutions Administration	44,834	44,824	10
Women's Affairs Commission	1,293	1,290	3
Correction Administration	240,376	240,347	29
Public Safety and Protection Commission	150	150	
Natural Resources Administration	1,935	1,928	7
Department of Correction and Rehabilitation	1,432	1,430	2
Institutional Trust of the National Guard of Puerto Rico	632	632	
Parole Board	1,983	1,981	2
Forensic Sciences Institute	6,538	6,538	
Special Independent Prosecutor Selections Board	1,295	1,295	
Pre-Trial Services Office	1,267	1,264	3
Total Public safety	1,027,141	1,025,590	1,551
Health:			
Health Facilities and Services Administration of Puerto Rico	49,410	49,410	
Environmental Quality Board	7,378	7,373	5
Department of Health	25,196	23,026	2,170
Juvenile Institutions Administration	3,387	3,286	101
Mental Health and Drug Addiction Services Administration	85,989	85,451	538
Puerto Rico Aqueeduct and Sewer Authority	76,979	76,979	
Total Health	248,339	245,525	2,814

(Continued)

COMMONWEALTH OF PUERTO RICO

SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
 BUDGET BASIS - GENERAL FUND  
 YEAR ENDED JUNE 30, 1997 (Expressed In Thousands)

	Budget	Actual	Variance Favorable (Unfavorable)
Public housing and welfare:			
Minors Support Administration	3,074	3,074	
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	3,651	3,651	
Housing Development and Improvement Administration	7,340	5,982	1,358
Puerto Rico Volunteers Service Corps	14,220	14,204	16
Puerto Rico Police Department	648	639	9
Department of Labor and Human Resources	7,460	7,459	1
Labor Relations Board	1,025	1,025	
State Insurance Fund Corporation	700	700	
Department of Health	1,071	1,070	1
Department of Housing	7,291	7,269	22
Department of Education	451	451	
Department of Recreation and Sports	34,156	32,791	1,365
Recreational Development Company	875	875	
Administration for the Horse Racing Sport and Industry	2,143	2,142	1
Mental Health and Drug Addiction Services Administration	13,100	13,091	9
Women's Affairs Commission	52	52	
Public Housing Administration	2,008	1,528	480
Citizens Rights Commission	110	109	1
Office of the Veterans Ombudsman	1,307	912	395
Department of Family	27,449	27,277	172
Family and Children Administration	58,902	58,888	14
Minors Support Administration	7,264	7,264	
Vocational Revitalization Administration	11,450	11,441	9
Social Economic Development Administration	71,017	71,002	15
Minimum Wage Board	946	946	
Office of the Disabled Persons Ombudsman	1,678	1,672	6
Elderly Affairs Office	2,079	2,077	2
Right to Employment Administration	29,853	29,853	
Cantera's Peninsula Integral Development Company	294	294	
Puerto Rico Housing Bank and Finance Agency	36,797	36,797	
Trust for the Development, Operation and Conservation of National Parks of Puerto Rico	2,300	2,300	
Communities Revitalization Administration	4,611	4,591	20
Total Public housing and welfare	355,322	351,426	3,896

**COMMONWEALTH OF PUERTO RICO**

**SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
BUDGET BASIS - GENERAL FUND  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

	Budget	Actual	Variance Favorable (Unfavorable)
Education:			
Department of Justice	21	21	
Puerto Rico Police Department	9,027	9,027	
Department of Transportation and Public Works	60	21	39
Department of Education	1,307,371	1,306,599	772
	20		20
Puerto Rico Culture Institute	368	368	
Mental Health and Drug Addiction Services Administration	1,084	1,079	5
State Office for Historical Development	2,289	2,289	
General Education Council	5,484	5,484	
Agricultural Extension Service	8,902	8,902	
Higher Education Council	76	76	
Musical Arts Corporation and Subsidiaries	300	300	
Atheneum of Puerto Rico			
<b>Total Education</b>	<b>1,335,002</b>	<b>1,334,166</b>	<b>836</b>
Economic development:			
Environmental Quality Board	52	52	
Department of Treasury	342	342	
Industrial Tax Exemption Office	49	49	
Department of Transportation and Public Works	56,246	54,353	1,893
Department of Natural and Environmental Resources	744	729	15
Department of Agriculture	15,863	15,535	328
Commercial Development Administration	5,398	5,388	10
Economic Development Administration	19,262	19,259	3
Cooperative Enterprises Development Administration	2,810	2,807	3
Cooperative Inspector's Office	683	683	
Rural Development Corporation	3,731	2,033	1,698
Department of Economic Development and Commerce	117	117	
Energy Affairs Administration	495	495	
Natural Resources Administration	23,512	23,487	25
Puerto Rico Development Film Arts Corporation	900	851	49

(Continued)



**COMMONWEALTH OF PUERTO RICO**

**SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
BUDGET BASIS - GENERAL FUND  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

	Budget	Actual	Variance Favorable (Unfavorable)
Puerto Rico Infrastructure Financing Authority	40,000	40,000	
Puerto Rico Industrial Development Company	19,967	19,967	
Puerto Rico Electric Power Authority	3	3	
Agricultural Extension Service	261	261	
Puerto Rico Metropolitan Bus Authority	3,480	3,480	
Puerto Rico Land Administration	550	550	
Tourism Company of Puerto Rico	22,581	22,581	
Agricultural Development and Services Administration	81,091	81,091	
Culebra Conservation and Development Authority	294	294	
Sugar Corporation of Puerto Rico	2,920	2,920	
<b>Total Economic development</b>	<b>301,351</b>	<b>297,327</b>	<b>4,024</b>
<b>Intergovernmental:</b>			
Municipal Services Administration	3,643	3,626	17
Municipal Revenues Collection Center	15	15	
Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation	6	6	
Municipal Contributions	260,334	259,660	674
<b>Total Intergovernmental</b>	<b>263,998</b>	<b>263,307</b>	<b>691</b>
<b>Debt service:</b>			
Principal	54,933	55,174	(241)
Interest and other	50,533	44,900	5,633
<b>Total expenditures</b>	<b>\$ 3,987,186</b>	<b>\$ 3,961,714</b>	<b>\$ 25,472</b>

COMMONWEALTH OF PUERTO RICO

SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
 BUDGET BASIS - GENERAL FUND  
 YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)

	Budget	Actual	Variance Favorable (Unfavorable)
OTHER FINANCING USES:			
Operating transfers-out to other funds:			
Comptroller's Office	\$ 1,233	\$ 1,233	
Health Facilities and Services Administration of Puerto Rico	301,527	301,527	
General Court of Justice	3,050	3,050	
Juvenile Institutions Administration	70	70	
Environmental Quality Board	813	813	
Governor's Office	867	867	
Office of Management and Budget	39,506	39,506	
Planning Board	480	480	
Constructions and Land Subdivisions Appeals Board	24	24	
Civil Defense State Agency	213	213	
Department of State	281	281	
Department of Treasury	1,053	1,053	
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	20,871	20,871	
Personnel Administration Central Office	190	190	
Commonwealth Electoral Commission	324	324	
Federal Affairs Administration	448	448	
General Services Administration	3	3	
Housing Development and Improvement Administration	206	206	
Investigation, Prosecution, and Appeals Commission	31	31	
Industrial Tax Exemption Office	1	1	
Municipal Services Administration	481	481	
Civil Rights Commission	11	11	
Department of Justice	150	150	
Puerto Rico Volunteers Service Corps	396	396	
Puerto Rico Police Department	1,637	1,637	
Puerto Rico Firefighters Corps and Medical Emergency Services	544	544	
Puerto Rico National Guard	34	34	
Department of Transportation and Public Works	545	545	
Department of Agriculture	331	331	
Commercial Development Administration	122	122	
Economic Development Administration	1,724	1,724	
Office of the Citizens Ombudsman	1	1	

COMMONWEALTH OF PUERTO RICO

SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
 BUDGET BASIS - GENERAL FUND  
 YEAR ENDED JUNE 30, 1987 (Expressed In Thousands)

	Budget	Actual	Variance Favorable (Unfavorable)
Cooperative Enterprises Development Administration	81	81	
Public Service Commission	119	119	
Department of Labor and Human Resources	398	398	
Labor Relations Board	61	61	
Consumer Affairs Department	311	311	
Department of Health	1,254	1,254	
Juvenile Institutions Administration	2,998	2,998	
Cooperative Inspector's Office	17	17	
Department of Housing	911	911	
Department of Education	1,950	1,950	
Puerto Rico Culture Institute	18,461	18,461	
Rural Development Corporation	19	19	
Department of Recreation and Sports	1,488	1,488	
Administration for the Horse Racing Sport and Industry	54	54	
Puerto Rico System of Annuities and Pensions for Teachers	11,071	11,071	
Personnel Administration System Appeals Board	100	100	
Regulations and Permits Administration	394	394	
Mental Health and Drug Addiction Services Administration	147	147	
Women's Affairs Commission	232	232	
Municipal Complaints Hearing Commission	16	16	
Correction Administration	2,205	2,205	
Legislative Assembly	1,054	1,054	
Public Housing Administration	1,072	1,072	
Puerto Rico Plastic Arts School	1,260	1,260	
Public Safety and Protection Commission	350	350	
Citizens Rights Commission	10	10	
Department of Economic Development and Commerce	83	83	
Office of the Veterans Ombudsman	30	30	
Department of Family	39	39	
Family and Children Administration	435	435	
Minors Support Administration	396	396	
Public Debt	375,000	375,000	
Vocational Revitalization Administration	108	108	
Social Economic Development Administration	960	960	

**COMMONWEALTH OF PUERTO RICO**

**SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
BUDGET BASIS - GENERAL FUND  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

	Budget	Actual	Variance Favorable (Unfavorable)
Public Policy and Organization Bureau	61	61	
Strategic Development-Secretariat	98	98	
Natural Resources Administration	251	251	
Department of Correction and Rehabilitation	40	40	
Parole Board	22	22	
Minimum Wage Board	254	254	
Office of the Disabled Persons Ombudsman	22	22	
Elderly Affairs Office	378	378	
State Office for Historic Preservation	1,098	1,098	
General Education Council	502	502	
Central Communications Office	351	351	
Right to Employment Administration	6	6	
Cantera's Peninsula Integral Development Company	6	6	
Puerto Rico Metropolitan Bus Authority	346	346	
Puerto Rico Solid Waste Authority	30	30	
Culebra Conservation and Development Authority	7	7	
Puerto Rico Health Insurance Administration	162	162	
Musical Arts Corporation and Subsidiaries	7	7	
Contributions to Political Parties	6,571	6,571	
Communities Rehabilitation Administration	649	649	
Pre-Trial Services Office	1,333	1,333	
<b>Total operating transfers-out to other funds</b>	<b>\$ 812,445</b>	<b>\$ 812,445</b>	<b>\$</b>
<b>Transfers-out to component units:</b>			
Institutional Trust of the National Guard of Puerto Rico	\$ 1,198	\$ 1,198	
Puerto Rico Aqueduct and Sewer Authority	30,000	30,000	
Land Authority of Puerto Rico	600	600	
Puerto Rico Metropolitan Bus Authority	21,644	21,644	
Industries for the Blind, Mentally Retarded, and Other Disabled Persons of Puerto Rico	150	150	
University of Puerto Rico	450,513	450,513	
Solid Waste Authority of Puerto Rico	10,738	10,738	
Agricultural Services and Development Administration	18,564	18,564	
Puerto Rico Health Insurance Administration	299,838	263,838	36,000

(Continued)

**COMMONWEALTH OF PUERTO RICO**

**SUPPLEMENTAL SCHEDULE OF EXPENDITURES BY AGENCY - BUDGET AND ACTUAL -  
BUDGET BASIS - GENERAL FUND  
YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

	Budget	Actual	Variance Favorable (Unfavorable)
Puerto Rico and Caribbean Cardiovascular Center Corporation	7,377	7,377	
Musical Arts Corporation and Subsidiaries	5,616	5,616	
Fine Arts Center Corporation	2,000	2,000	
Sugar Corporation of Puerto Rico	12,359	12,359	
Puerto Rico Public Broadcasting Corporation	3,031	3,031	
Commercial and Farm Credit and Development Corporation of Puerto Rico	12,000	12,000	
Puerto Rico Conservatory of Music Corporation	3,342	3,342	
<b>Total transfers-out to component units</b>	<b>\$ 878,970</b>	<b>\$ 842,970</b>	<b>\$ 36,000</b>



## DEBT SERVICE FUNDS

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The debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs other than bonds payable from the operations of proprietary fund types, nonexpendable trust funds and discretely presented component units.

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**Debt Redemption Fund:** This fund is used to account for the accumulation of resources for the payment of general obligation bonds issued by the Commonwealth's central government.

**Puerto Rico Highway and Transportation Authority:** A blended component unit engaged in the construction and supervision of highways and other transportation facilities. Its debt service fund is used to account for the accumulation of resources for the payment of revenue bonds issued to finance the construction of the highways and other facilities.

**Public Buildings Authority:** 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:** 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 maritime operations. This fund is mainly subsidized from appropriations and operating transfers-in from the general fund.

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING BALANCE SHEET - DEBT SERVICE FUNDS**  
**JUNE 30, 1997**  
(Expressed in Thousands)

	Debt Redemption Fund	Puerto Rico Highway and Transportation Authority	Public Buildings Authority	Puerto Rico Maritime Shipping Authority	Totals
<b>ASSETS</b>					
Cash and cash equivalents	\$ 15,962	\$ 2,488	\$ 55,118	\$ 2,508	\$ 76,076
Cash and cash equivalents in governmental banks	273,385	22,153	4,412	6,085	306,035
Investments		327,954	21,651		349,605
Receivables, net:					
Accounts	28,517	2,755	36,335	260	67,867
Loans and advances				16,786	16,786
Accrued interest		3,119			3,119
Advances to component units	1,557			6,429	1,557
Other assets					6,429
<b>TOTAL ASSETS</b>	<u>\$ 319,421</u>	<u>\$ 358,469</u>	<u>\$ 117,516</u>	<u>\$ 32,068</u>	<u>\$ 827,474</u>
<b>LIABILITIES AND FUND BALANCES</b>					
<b>Liabilities:</b>					
Accounts payable and accrued liabilities	\$	\$	\$	\$ 7,061	\$ 7,061
Due to other funds		5,061	36,491		41,552
Interest payable	105,214	68,405	36,700	8,014	218,333
Bonds payable	207,980	47,260	44,325		299,565
Other liabilities	4,005				4,005
Total liabilities	<u>317,199</u>	<u>120,726</u>	<u>117,516</u>	<u>15,075</u>	<u>570,516</u>
<b>Fund balances:</b>					
Reserved for debt service	2,222	237,743		16,993	256,958
Total fund balances:	<u>2,222</u>	<u>237,743</u>		<u>16,993</u>	<u>256,958</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 319,421</u>	<u>\$ 358,469</u>	<u>\$ 117,516</u>	<u>\$ 32,068</u>	<u>\$ 827,474</u>



**COMMONWEALTH OF PUERTO RICO**

**COMBINING STATEMENT OF REVENUES,  
EXPENDITURES AND CHANGES IN FUND BALANCES  
DEBT SERVICE FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)**

	Debt Redemption Fund	Puerto Rico Highway and Transportation Authority	Public Buildings Authority	Puerto Rico Maritime Shipping Authority	Totals
<b>REVENUES:</b>					
Excise taxes	\$ 14,560	\$ 180,132	\$	\$	\$ 194,692
Charges for services	50,133	130,241	220,056		350,297
Intergovernmental	7,603	16,942			50,133
Interest					24,545
<b>Total revenues</b>	<b>72,296</b>	<b>327,315</b>	<b>220,056</b>		<b>619,667</b>
<b>EXPENDITURES:</b>					
Debt Service:					
Principal	208,005	51,510	41,815		301,330
Interest and other	222,148	169,805	69,020	26,963	487,736
<b>Total expenditures</b>	<b>430,153</b>	<b>221,115</b>	<b>110,835</b>	<b>26,963</b>	<b>789,066</b>
<b>EXCESS/DEFICIENCY OF REVENUES OVER (UNDER) EXPENDITURES</b>	<b>(357,857)</b>	<b>106,200</b>	<b>109,221</b>	<b>(26,963)</b>	<b>(169,399)</b>
<b>OTHER FINANCING SOURCES (USES):</b>					
Proceeds from refunding bonds	335,155				335,155
Operating transfers-in from other funds	374,999	31,836		25,576	432,411
Operating transfers-out to other funds	(12,833)	(39,059)	(109,221)	(10,000)	(171,113)
Payment to refunded bond escrow agent	(333,111)				(333,111)
<b>Total other financing sources (uses)</b>	<b>364,210</b>	<b>(7,223)</b>	<b>(109,221)</b>	<b>15,576</b>	<b>263,342</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	6,353	98,977		(11,387)	93,943
<b>FUND BALANCES (DEFICIT) AT BEGINNING OF YEAR</b>	<b>(4,131)</b>	<b>227,551</b>		<b>28,380</b>	<b>251,800</b>
<b>RESIDUAL EQUITY TRANSFER</b>		<b>(88,785)</b>			<b>(88,785)</b>
<b>FUND BALANCES AT END OF YEAR</b>	<b>\$ 2,222</b>	<b>\$ 237,743</b>	<b>\$</b>	<b>\$ 16,993</b>	<b>\$ 256,958</b>



## CAPITAL PROJECTS FUNDS

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Capital projects funds are used to account for the financial resources used for acquisition or construction of major capital facilities not being financed by proprietary fund types, nonexpendable trust funds and discretely presented component units.

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**Public Improvements Funds and Other Funds:** These funds present the activities of the capital improvements program of the Commonwealth, financed with the proceeds of general obligation bonds.

**Puerto Rico Highway and Transportation Authority:** A blended component unit. Its capital projects fund is used to account for the construction costs, and related financing means, for highways and other transportation projects.

**Public Buildings Authority:** A blended component unit. Its capital projects fund is used to account for the construction activities, and related financing means, for buildings and facilities that, when completed, are leased to the Commonwealth's primary government agencies.

**Office for the Improvements of the Public Schools:** Created by the Joint Resolution No. 3 of August 28, 1990. The primary functions of the office are the development and implementation of a repairs and improvement plan of the public schools in Puerto Rico.

**Electronic Information Systems Fund:** Created pursuant to the provisions of Law No. 259 of December 29, 1995. The primary purpose of the fund is to finance the capital improvement program which consists of the acquisition and installation of computer equipment and software and the development of computer systems to be used in the establishment of a wide area network and remote communication network connecting all government agencies.

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING BALANCE SHEET - CAPITAL PROJECTS FUNDS**  
**JUNE 30, 1997**  
(Expressed in Thousands)

	1996 Public Improvements Fund	1995 Public Improvements Fund	1994 Public Improvements Fund	1993 Public Improvements Fund	Electronic Information Systems Fund
<b>ASSETS</b>					
Cash and cash equivalents	\$ 140,505	\$ 74,803	\$ 39,962	\$ 33,069	\$ 101,983
Cash and cash equivalents in governmental banks					
Investments					
Receivables, net:					
Intergovernmental	663	547			
Accounts					
Loans and advances					
Accrued interest					
Other	4,129	3,487	1,283	805	
Due from other funds					
Other assets					
<b>TOTAL ASSETS</b>	<b>\$ 145,297</b>	<b>\$ 78,837</b>	<b>\$ 41,245</b>	<b>\$ 33,874</b>	<b>\$ 101,983</b>
<b>LIABILITIES AND FUND BALANCES</b>					
<b>Liabilities:</b>					
Accounts payable and accrued liabilities	\$ 16,266	\$ 2,013	\$ 593	\$ 488	\$ 1,772
Advances from component units					
Accrued compensated absences	2,389	4,314	1,032	1,826	6
Other liabilities					
<b>Total liabilities</b>	<b>18,655</b>	<b>6,327</b>	<b>1,625</b>	<b>2,314</b>	<b>1,778</b>
<b>Fund balances:</b>					
Reserved for encumbrances	5,598	18,095	2,454	7,086	18,861
Reserved for public improvements	121,044	54,415	37,166	24,474	81,344
<b>Total fund balances</b>	<b>126,642</b>	<b>72,510</b>	<b>39,620</b>	<b>31,560</b>	<b>100,205</b>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b>\$ 145,297</b>	<b>\$ 78,837</b>	<b>\$ 41,245</b>	<b>\$ 33,874</b>	<b>\$ 101,983</b>

COMMONWEALTH OF PUERTO RICO  
 COMBINING BALANCE SHEET - CAPITAL PROJECTS FUNDS  
 JUNE 30, 1997  
 (Expressed in Thousands)

	Puerto Rico Highway and Transportation Authority	Publico Buildings Authority	Office for the Improvement of Public Schools	Other Funds	Totals
<b>ASSETS</b>					
Cash and cash equivalents	\$ 41,873	\$ 433,192	\$	\$ 59,019	\$ 924,406
Cash and cash equivalents in governmental banks	1,279	40,618	72,288		114,185
Investments	14,813	84,177			98,790
Receivables, net:					
Intergovernmental	33,369				33,369
Accounts			168		1,378
Loans and advances	16,410			36	16,446
Accrued interest	5,679				5,679
Other		9,475			9,475
Due from other funds	2,488	36,491		2,255	50,938
Other assets	1,270	14,493			15,763
<b>TOTAL ASSETS</b>	<b>\$ 116,881</b>	<b>\$ 618,446</b>	<b>\$ 72,456</b>	<b>\$ 61,310</b>	<b>\$ 1,270,329</b>
<b>LIABILITIES AND FUND BALANCES</b>					
<b>Liabilities:</b>					
Accounts payable and accrued liabilities	\$ 75,509	\$ 141,015	\$ 3,636	\$ 1,562	\$ 242,854
Advances from component units		71,259			71,259
Accrued compensated absences	10,307				10,307
Other liabilities	4,286			1,331	15,184
Total liabilities	90,102	212,274	3,636	2,893	339,604
<b>Fund balances:</b>					
Reserved for encumbrances			35,946	2,620	90,660
Reserved for public improvements	26,779	406,172	32,874	55,797	840,065
Total fund balances	26,779	406,172	68,820	58,417	930,725
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b>\$ 116,881</b>	<b>\$ 618,446</b>	<b>\$ 72,456</b>	<b>\$ 61,310</b>	<b>\$ 1,270,329</b>

**COMMONWEALTH OF PUERTO RICO**

**COMBINING STATEMENT OF REVENUES,  
EXPENDITURES AND CHANGES IN FUND BALANCES -  
CAPITAL PROJECTS FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)**

	1996 Publio Improvements Fund	1995 Publio Improvements Fund	1994 Publio Improvements Fund	1993 Publio Improvements Fund	Electronic Information Systems Fund
<b>REVENUES:</b>					
Charges for services	\$ 28	\$ 245	\$ 87	\$ 37	\$ 5
Intergovernmental		60	252	5	
Interest					
Other					
Total revenues	<u>28</u>	<u>305</u>	<u>339</u>	<u>42</u>	<u>5</u>
<b>EXPENDITURES:</b>					
Capital outlay	<u>207,952</u>	<u>102,453</u>	<u>21,165</u>	<u>21,183</u>	<u>24,137</u>
Total expenditures	<u>207,952</u>	<u>102,453</u>	<u>21,165</u>	<u>21,183</u>	<u>24,137</u>
Deficiency of revenues under expenditures	<u>(207,924)</u>	<u>(102,148)</u>	<u>(20,826)</u>	<u>(21,141)</u>	<u>(24,132)</u>
<b>OTHER FINANCING SOURCES (USES):</b>					
Proceeds from long-term debt issues	374,430				152,390
Operating transfers-in from other funds	(37,758)	(1,127)			
Operating transfers-out to other funds	(2,106)	(921)			
Transfers-out to component units					
Total other financing sources (uses)	<u>334,566</u>	<u>(2,048)</u>			<u>152,390</u>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	126,642	(104,196)	(20,826)	(21,141)	128,258
<b>FUND BALANCES (DEFICIT) AT BEGINNING OF YEAR, (as restated)</b>					
		176,706	60,446	52,701	(28,053)
<b>FUND BALANCES AT END OF YEAR</b>	<u>\$ 126,642</u>	<u>\$ 72,510</u>	<u>\$ 39,620</u>	<u>\$ 31,560</u>	<u>\$ 100,205</u>

**COMMONWEALTH OF PUERTO RICO**

**COMBINING STATEMENT OF REVENUES,  
EXPENDITURES AND CHANGES IN FUND BALANCES -  
CAPITAL PROJECTS FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)**

	Puerto Rico Highway and Transportation Authority	Public Buildings Authority	Office for the Improvement of Public Schools	Other Funds	Totals
<b>REVENUES:</b>					
Charges for services	\$ 82,684		\$ 14,205	\$ 38	\$ 440
Intergovernmental	16,225	15,811	3,250	6	97,212
Interest		5,004	841		35,286
Other					5,945
<b>Total revenues</b>	<b>98,909</b>	<b>20,815</b>	<b>18,396</b>	<b>44</b>	<b>138,883</b>
<b>EXPENDITURES:</b>					
Capital outlay	500,708	396,343	79,441	22,086	1,375,468
<b>Total expenditures</b>	<b>500,708</b>	<b>396,343</b>	<b>79,441</b>	<b>22,086</b>	<b>1,375,468</b>
Deficiency of revenues under expenditures	(401,799)	(375,528)	(61,045)	(22,042)	(1,236,585)
<b>OTHER FINANCING SOURCES (USES):</b>					
Proceeds from long-term debt issues		613,084	70,372		1,210,276
Operating transfers-in from other funds		109,221			109,221
Operating transfers-out to other funds	(168)			(5)	(39,058)
Transfers-out to component units				(410)	(3,437)
<b>Total other financing sources (uses)</b>	<b>(168)</b>	<b>722,305</b>	<b>70,372</b>	<b>(415)</b>	<b>1,277,002</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	(401,967)	346,777	9,327	(22,457)	40,417
<b>FUND BALANCES (DEFICIT) AT BEGINNING OF YEAR, (as restated)</b>	<b>428,746</b>	<b>59,395</b>	<b>59,493</b>	<b>80,874</b>	<b>890,308</b>
<b>FUND BALANCES AT END OF YEAR</b>	<b>\$ 26,779</b>	<b>\$ 406,172</b>	<b>\$ 68,820</b>	<b>\$ 58,417</b>	<b>\$ 930,725</b>

**COMMONWEALTH OF PUERTO RICO**  
**SCHEDULE OF COMMONWEALTH CAPITAL PROJECTS EXPENDITURES AND AUTHORIZATIONS**  
**JUNE 30, 1997**  
**(Expressed in Thousands)**

	Authorization	Bond Proceeds	Cumulative Expenditures	Current Expenditures	Year to Date			Remaining Authorization
					Expenditures	Encumbrances	Expenditures	
Electronic Information Systems Fund	\$ 150,000	\$ 152,395	\$ 28,053	\$ 24,137	\$ 52,190	\$ 18,861	\$ 81,344	
1996 Public Improvements Bond	369,000	374,457		247,816	247,816	5,598	121,043	
1995 Public Improvements Bond	355,000	356,526	179,509	104,501	284,010	18,095	54,421	
1994 Public Improvements Bond	325,000	327,058	266,271	21,165	287,436	2,454	37,168	
1993 Public Improvements Bond	305,000	306,595	250,791	21,183	271,974	7,086	27,535	
1992 Public Improvements Bond	310,000	305,616	292,676	5,209	297,885	447	7,284	
1991 Public Improvements Bond	305,000	298,065	286,110	5,663	291,773	386	5,906	
1990 Public Improvements Bond	250,000	252,914	245,663	2,742	248,405	384	4,125	
1989 Public Improvements Bond	275,000	271,719	270,336	832	271,168	166	385	
1988 Public Improvements Bond	245,000	244,408	243,259	24	243,283	390	735	
1987 Public Improvements Bond	231,000	233,019	231,880	450	232,330	152	537	
Prior to 1987				7,581		695		
				<u>\$ 441,303</u>		<u>\$ 54,714</u>		



## ENTERPRISE FUNDS

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Enterprise 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.

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**Health Facilities and Services Administration of Puerto Rico:** Created as an executive agency in 1975 to lease, operate hospitals and other health facilities and to provide for the improvement, alteration or repair of such facilities. Accounts for the cost of providing health services to the general public.

**The Additional Lottery System:** Created by Law No. 10 of May 24, 1989, as amended, and commenced operations on June 1, 1990. The Additional Lottery is an operational unit of the Commonwealth of Puerto Rico Treasury Department. Presently, two games (Pick 3 and Lotto) with several betting alternatives are offered by the Additional Lottery.

**Lottery of Puerto Rico:** Created under Law No. 465 of May of 1947. The Lottery is an operational unit of the Commonwealth of Puerto Rico Treasury Department and is engaged in the sales of tickets to authorized agents throughout the Commonwealth. It was created to help those authorized agents with an additional source of revenues and to supplement revenues for the general fund of the Commonwealth.

**Puerto Rico Highway and Transportation Authority:** A blended component unit. Its enterprise fund is used to account for the activities of certain transportation projects that are operated and financed through user charges.



COMMONWEALTH OF PUERTO RICO  
 COMBINING BALANCE SHEET - ENTERPRISE FUNDS  
 JUNE 30, 1997  
 (Expressed in Thousands)

	Health Facilities and Services Administration of Puerto Rico	The Additional Lottery System	Lottery of Puerto Rico	Puerto Rico Highway and Transportation Authority	Totals
<b>ASSETS</b>					
Cash and cash equivalents	\$ 4,946	\$ 4,351	\$ 20,562	\$	\$ 29,859
Cash and cash equivalents in governmental banks			24,358		24,358
Receivables, net:					
Intergovernmental	6,790				6,790
Accounts	44,235	4,519	24		48,778
Other	25,611				25,611
Due from other funds	4,619			2,573	7,192
Inventories	15,076		270		15,346
Restricted assets:					
Cash and cash equivalents	1,431				1,431
Other restricted assets		180,523			180,523
Fixed assets, net	374,292	25	1,506	182,017	557,840
Other assets	1,480				1,480
<b>TOTAL ASSETS</b>	<b>\$ 478,480</b>	<b>\$ 189,418</b>	<b>\$ 46,720</b>	<b>\$ 184,590</b>	<b>\$ 899,208</b>
<b>LIABILITIES AND FUND EQUITY (DEFICIT)</b>					
<b>Liabilities:</b>					
Accounts payable and accrued liabilities	\$ 97,418	\$ 1,730	\$ 622	\$	\$ 99,770
Due to:					
Other funds		3,237	20,850		24,087
Component units	45,879				45,879
Advances from component units	578,292				578,292
Interest payable	36,923				36,923
Deferred revenues			14,362		14,362
Lottery prizes payable		185,816	8,008		193,824
Accrued compensated absences	80,383		1,355		81,738
Other liabilities				9,460	9,460
Other long-term liabilities	328,156		763		328,919
<b>Total liabilities</b>	<b>1,167,051</b>	<b>190,783</b>	<b>45,960</b>	<b>9,460</b>	<b>1,413,254</b>
<b>Fund Equity (Deficit):</b>					
Contributed capital			720	175,130	175,850
Retained earnings (deficit)	(688,571)	(1,365)	40		(689,896)
<b>Total fund equity (deficit)</b>	<b>(688,571)</b>	<b>(1,365)</b>	<b>760</b>	<b>175,130</b>	<b>(514,046)</b>
<b>TOTAL LIABILITIES AND FUND EQUITY (DEFICIT)</b>	<b>\$ 478,480</b>	<b>\$ 189,418</b>	<b>\$ 46,720</b>	<b>\$ 184,590</b>	<b>\$ 899,208</b>

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING STATEMENT OF REVENUES, EXPENSES AND**  
**CHANGES IN RETAINED EARNINGS (DEFICIT) - ENTERPRISE FUNDS**  
**YEAR ENDED JUNE 30, 1997**  
*(Expressed in Thousands)*

	Health Facilities and Services Administration of Puerto Rico	The Additional Lottery System	Lottery of Puerto Rico	Puerto Rico Highway and Transportation Authority	Totals
<b>OPERATING REVENUES:</b>					
Charges for services	\$ 202,995	\$ 216,596	\$ 457,462	\$ 3,611	\$ 879,664
Total operating revenues	<u>202,995</u>	<u>216,596</u>	<u>457,462</u>	<u>3,611</u>	<u>879,664</u>
<b>OPERATING EXPENSES:</b>					
Cost of services	686,136	142,071	394,342	11,000	1,233,549
Depreciation and amortization	25,945	45	661	676	27,327
Total operating expenses	<u>712,081</u>	<u>142,116</u>	<u>395,003</u>	<u>11,676</u>	<u>1,260,876</u>
<b>OPERATING INCOME (LOSS)</b>	<u>(509,086)</u>	<u>73,480</u>	<u>62,459</u>	<u>(8,065)</u>	<u>(381,212)</u>
<b>NON-OPERATING REVENUES (EXPENSES):</b>					
Intergovernmental	2,173		881		2,173
Interest income	(58,449)		(76)		(58,525)
Interest expense	21,689		177		21,866
Other, net					
Total non-operating revenues (expenses), net	<u>(34,587)</u>		<u>982</u>		<u>(33,605)</u>
<b>INCOME (LOSS) BEFORE OPERATING TRANSFERS</b>	<u>(543,673)</u>	<u>73,480</u>	<u>63,441</u>	<u>(8,065)</u>	<u>(414,817)</u>
<b>TRANSFERS:</b>					
Operating transfers from other funds	374,231	(73,480)	(63,435)	7,389	381,620
Operating transfers to other funds					(136,915)
Total transfers, net	<u>374,231</u>	<u>(73,480)</u>	<u>(63,435)</u>	<u>7,389</u>	<u>244,705</u>
<b>NET INCOME (LOSS)</b>	<u>(169,442)</u>		<u>6</u>	<u>(676)</u>	<u>(170,112)</u>
<b>DEPRECIATION ON FIXED ASSETS ACQUIRED THROUGH CAPITAL CONTRIBUTIONS</b>					
<b>INCREASE (DECREASE) IN RETAINED EARNINGS (DEFICIT)</b>	<u>(169,442)</u>		<u>667</u>		<u>(168,775)</u>
<b>RETAINED EARNINGS (DEFICIT) AT BEGINNING OF YEAR, (as restated)</b>	<u>(519,129)</u>	<u>(1,365)</u>	<u>40</u>		<u>(520,454)</u>
<b>TRANSFERS TO CONTRIBUTED CAPITAL</b>			<u>(667)</u>		<u>(667)</u>
<b>RETAINED EARNINGS (DEFICIT) AT END OF YEAR</b>	<u>(688,571)</u>	<u>(1,365)</u>	<u>40</u>	<u>676</u>	<u>(688,896)</u>

COMMONWEALTH OF PUERTO RICO  
 COMBINING STATEMENT OF CASH FLOWS - ENTERPRISE FUNDS  
 YEAR ENDED JUNE 30, 1997  
 (Expressed in Thousands)

	Health Facilities and Services Administration of Puerto Rico	The Additional Lottery System	Puerto Rico Highway and Transportation Authority	Totals
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>				
Operating income (loss)	\$ (509,086)	\$ 73,480	\$ (8,065)	\$ (381,212)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization	25,945	45	676	27,327
Provision for uncollectible accounts	23,733			23,793
Changes in assets and liabilities:				
Increase in:				
Receivables	(19,461)	(138)		(19,599)
Due from other funds	(640)			(640)
Inventories				(91)
Accounts payable and accrued liabilities	8,110	1,792		9,110
Due to other funds				1,792
Deferred revenues		20,563		56
Lottery prizes payable				389
Decrease in:				
Inventories	2,672			2,672
Other assets	60	10		70
Accounts payable and accrued liabilities		(463)		(962)
Accrued compensated absences				(32)
Total adjustments	41,479	21,809	676	64,448
	(467,607)	95,289	(7,389)	(316,764)
Net cash provided by (used in) operating activities				
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>				
Operating grants received	1,894			2,071
Operating transfers-in from other funds	515,813			523,202
Operating transfers-out to other funds		(73,480)		(128,603)
Capital contributions				115,890
Net cash provided by (used in) noncapital financing activities	517,707	(73,480)	123,279	512,560
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>				
Acquisition and construction of capital assets	(13,555)	(42)	(115,890)	(129,797)
Principal paid on bonds and notes	(54,605)			(357)
Interest paid on bonds and notes	(68,160)	(42)	(115,890)	(54,681)
Net cash used in capital and related financing activities	(135,320)	(84)	(115,890)	(184,835)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>				
Purchase of investments securities	7,463	(20,064)		(20,064)
Interest and dividends on investments	7,463	(20,064)		8,344
Net cash provided by (used in) investing activities	(10,597)	1,703		(759)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>				
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	16,974	2,648		56,407
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	6,377	4,351		55,648



## TRUST AND AGENCY FUNDS

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Trust funds are used to account for assets held by the government in a trustee capacity. Agency funds are used to account for assets held by the government as an agent for individuals, private organizations, other governments and/or other funds.

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**Pension Trust Funds:** These funds are used to account for the accumulation of resources for pension benefit payments of qualified public employees. The pension trust funds included are the:

**Employees Retirement System of the Government of Puerto Rico and its Instrumentalities** Is the administrator of a single-employer retirement system established by the Commonwealth. The System was created under Act 477, approved on May 15, 1951, as amended, and became effective on January 1, 1952. The System covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and component units not covered by their own retirement systems.

**Judiciary Retirement System** Is a single-employer defined benefit plan which is administered by the Employee Retirement System mentioned above. It was created under Act 12, approved on October 19, 1954. The membership includes all individuals holding a position as Justice of the Supreme Court, Judge of the Superior Court or the District Court or Municipal Judge of the Commonwealth of Puerto Rico. The System provides retirement as well as death and disability benefits.

**Annuity and Pension System for the Teachers of Puerto Rico:** Is a single-employer plan which was created under Act 218 approved on May 6, 1951. The System provides retirement benefits to all teachers of the Department of Education of the Commonwealth, those holding positions in the Retirement Board, all pensioned teachers transferred to an administrative position in the Department of Education, teachers who worked in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education.

**Expendable Trust Funds:** These funds are used to account for the following activities:

- **Health Facilities and Services Administration of Puerto Rico Trust Fund:** This specific purpose fund accounts for monies received by the Administration on a fiduciary basis to acquire certain goods or render certain services, or monies to be kept on behalf of inpatients or outpatients attended in the facilities administered by the Administration. The patient funds are used to acquire personal goods or services for specific patients.

- **Unemployment Trust Fund:** The unemployment trust funds account for funds received from the United States Department of Labor to reimburse fifty percent of the administrative costs of extended benefits paid under the provisions of Puerto Rico laws, which conform to the provisions of the Federal Social Security and Unemployment Tax Acts. Also, they account for contributions received to reimburse the benefits paid to unemployed ex-military and civilian ex-federal employees, whose unemployment is caused by a presidentially declared disaster under the Disaster Relief Act, and adversely affected works under the Trade Act.

**Agency Fund** - This fund is custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

- **Special Deposits Fund:** This agency fund acts in a fiduciary capacity in order to account for monies received with specific 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, deposits under the custody of the Insurance Commissioner for escheated property and for insurance companies under bankruptcy.



COMMONWEALTH OF PUERTO RICO

COMBINING BALANCE SHEET -  
TRUST AND AGENCY FUNDS  
JUNE 30, 1997

(Expressed in Thousands)

	Pension Trust	Expendable Trust	Agency	Totals
<b>ASSETS</b>				
Cash and cash equivalents	\$ 101,022	\$ 183,365	\$ 467,010	\$ 751,397
Cash and cash equivalents in governmental bank:	132,474	617,865		750,339
Investments	2,529,925		16,145	2,546,070
Receivables, net:				
Taxes		67,514		67,514
Accounts	30,897	27,838	3	58,738
Loans and advances	580,782			580,782
Accrued interest	12,256	493		12,749
Other	8,948			8,948
Due from other funds		5,818		5,818
Restricted assets:				
Cash and cash equivalents	6,356			6,356
Other restricted assets	36,354			36,354
Fixed assets, net	24,454			24,454
Other assets	32,470			32,470
<b>TOTAL ASSETS</b>	<b>\$ 3,495,938</b>	<b>\$ 902,893</b>	<b>\$ 483,158</b>	<b>\$ 4,881,989</b>
<b>LIABILITIES AND FUND BALANCES</b>				
Liabilities:				
Accounts payable and accrued liabilities	\$ 70,289	\$ 35,421	\$ 51,265	\$ 156,975
Due to other funds		4,624	5,490	10,114
Bonds payable	26,945			26,945
Accrued compensated absences	4,595			4,595
Other liabilities	241	16,989	426,403	443,633
Total liabilities	102,070	57,034	483,158	642,262
Fund balances:				
Reserved for:				
Encumbrances		2,768		2,768
Unemployment benefits		803,282		803,282
Employees' pension benefits	3,393,868			3,393,868
Advances and other specified purposes		8,767		8,767
Unreserved		31,042		31,042
Total fund balances	3,393,868	845,859		4,239,727
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b>\$ 3,495,938</b>	<b>\$ 902,893</b>	<b>\$ 483,158</b>	<b>\$ 4,881,989</b>

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING STATEMENT OF PLAN NET ASSETS AVAILABLE**  
**FOR PENSION BENEFITS - PENSION TRUST FUNDS**  
**JUNE 30, 1997**  
**(Expressed in Thousands)**

	Employees Retirement System	Teachers Retirement System	Judiciary Retirement System	Eliminations	Totals
<b>ASSETS</b>					
Cash and cash equivalents	\$ 91,012	\$ 8,834	\$ 1,176	\$	\$ 101,022
Cash and cash equivalents in governmental banks	108,314	23,238	922		132,474
Investments	930,686	1,543,454	55,785		2,529,925
Receivables, net:					
Accounts	25,018	5,879			30,897
Loans and advances	283,955	296,334	493		580,782
Accrued interest	1,223	10,612	421		12,256
Other	3,472	5,374	102	(1,268)	8,948
Due from other funds	1,268				
Restricted assets:					
Cash and cash equivalents	3,543	2,794	19		6,356
Other restricted assets	9,768	36,354			36,354
Fixed assets, net	17,360	14,686			24,454
Other assets		15,110			32,470
<b>TOTAL ASSETS</b>	<b>1,475,619</b>	<b>1,962,669</b>	<b>58,918</b>	<b>(1,268)</b>	<b>3,495,938</b>
<b>LIABILITIES:</b>					
Accounts payable and accrued liabilities	28,179	41,956	154		70,289
Due to other funds			1,268	(1,268)	
Bonds payable		26,945			26,945
Accrued compensated absences	2,969	1,626			4,595
Other liabilities			241		241
<b>TOTAL LIABILITIES</b>	<b>31,148</b>	<b>70,527</b>	<b>1,663</b>	<b>(1,268)</b>	<b>102,070</b>
<b>NET ASSETS AVAILABLE FOR PENSION BENEFITS</b>	<b>\$ 1,444,471</b>	<b>\$ 1,892,142</b>	<b>\$ 57,255</b>	<b>\$</b>	<b>\$ 3,393,868</b>

COMMONWEALTH OF PUERTO RICO

COMBINING STATEMENT OF CHANGES IN PLAN NET ASSETS  
AVAILABLE FOR PENSION BENEFITS - PENSION TRUST FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)

	Employees Retirement System	Teachers Retirement System	Judiciary Retirement System	Totals
<b>ADDITIONS:</b>				
Contributions:				
Employer	\$ 232,674	\$ 82,431	\$ 4,102	\$ 319,207
Employees	206,094	68,777	1,763	276,634
Special	15,849	10,071		25,920
Total contributions	454,617	161,279	5,865	621,761
Investment income:				
Interest	40,334	65,513	1,073	106,920
Dividends	11,463	5,111	541	17,115
Net appreciation of investments	173,281	197,476	7,648	378,405
Total investment income	225,078	268,100	9,262	502,440
Other income	5,334	67	28	5,429
Total additions	685,029	429,446	15,155	1,129,630
<b>DEDUCTIONS:</b>				
Benefits	425,168	154,974	6,080	586,222
Refunds of contributions	11,901	13,669		25,570
General and administrative	33,001	21,480	1,815	56,296
Total deductions	470,070	190,123	7,895	668,088
<b>NET INCREASE</b>	214,959	239,323	7,260	461,542
<b>NET ASSETS AVAILABLE FOR PENSION BENEFITS AT BEGINNING OF YEAR</b>	1,229,512	1,652,819	49,995	2,932,326
<b>NET ASSETS AVAILABLE FOR PENSION BENEFITS AT END OF YEAR</b>	\$ 1,444,471	\$ 1,892,142	\$ 57,255	\$ 3,393,868

**COMMONWEALTH OF PUERTO RICO**

**COMBINING BALANCE SHEET -  
EXPENDABLE TRUST FUNDS**

**JUNE 30, 1997**

(Expressed in Thousands)

	Unemployment Trust Fund	Health Facilities and Services Administration of Puerto Rico Trust Fund	Other Funds	Totals
<b>ASSETS</b>				
Cash and cash equivalents	\$ 128,147	\$ 8,096	\$ 47,122	\$ 183,365
Cash and cash equivalents in governmental banks	617,865			617,865
Receivables, net:				
Taxes	67,514			67,514
Accounts	135	4,325	23,378	27,838
Accrued interest	493		5,818	493
Due from other funds				5,818
<b>TOTAL ASSETS</b>	<b>\$ 814,154</b>	<b>\$ 12,421</b>	<b>\$ 76,318</b>	<b>\$ 902,893</b>
<b>LIABILITIES AND FUND BALANCES</b>				
<b>Liabilities:</b>				
Accounts payable and accrued liabilities	\$ 8,987	\$ 358	\$ 26,076	\$ 35,421
Due to other funds		4,619	5	4,624
Other liabilities	62		16,927	16,989
Total liabilities	9,049	4,977	43,008	57,034
<b>Fund balances:</b>				
Reserved for:				
Encumbrances	1,823		945	2,768
Unemployment benefits	803,282			803,282
Advances and other specified purposes		7,444	1,323	8,767
Unreserved			31,042	31,042
Total fund balances	805,105	7,444	33,310	845,859
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b>\$ 814,154</b>	<b>\$ 12,421</b>	<b>\$ 76,318</b>	<b>\$ 902,893</b>

COMMONWEALTH OF PUERTO RICO

COMBINING STATEMENTS OF REVENUES,  
EXPENDITURES AND CHANGES IN FUND BALANCES -  
EXPENDABLE TRUST FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)

	Unemployment Trust Fund	Health Facilities and Services Administration of Puerto Rico Trust Fund	Other Funds	Totals
<b>REVENUES:</b>				
Unemployment taxes	\$ 236,171	\$	\$	\$ 236,171
Charges for services	422	141	3,021	3,584
Intergovernmental	15,299		15,641	30,940
Interest	49,460		12	49,472
Other			4,118	4,118
Total revenues	301,352	141	22,792	324,285
<b>EXPENDITURES:</b>				
Current:				
General government	1,928		3,025	4,953
Public safety	1,135		296	1,431
Health		1,486		1,486
Public housing and welfare	306,296		14,865	321,161
Economic development	661		8,558	9,219
Capital outlay	318		10,516	10,834
Total expenditures	310,338	1,486	37,260	349,084
Deficiency of revenues under expenditures	(8,986)	(1,345)	(14,468)	(24,799)
<b>OTHER FINANCING SOURCES (USES):</b>				
Operating transfers-in from other funds	(2,304)		3,061	757
Operating transfers-out to other funds	(657)			(657)
Total other financing sources (uses)	(2,961)		3,061	100
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	(11,947)	(1,345)	(11,407)	(24,699)
<b>FUND BALANCES AT BEGINNING OF YEAR</b>	817,052	8,789	44,717	870,558
<b>FUND BALANCES AT END OF YEAR</b>	\$ 805,105	\$ 7,444	\$ 33,310	\$ 845,859

**COMMONWEALTH OF PUERTO RICO**

**COMBINING BALANCE SHEET -  
AGENCY FUNDS  
JUNE 30, 1997  
(Expressed in Thousands)**

	Special Deposits Fund	Other Funds	Totals
<b>ASSETS</b>			
Cash and cash equivalents	\$ 456,427	\$ 10,583	\$ 467,010
Investments	16,145		16,145
Accounts receivable	2	1	3
<b>TOTAL ASSETS</b>	<u>\$ 472,574</u>	<u>\$ 10,584</u>	<u>\$ 483,158</u>
<b>LIABILITIES</b>			
Accounts payable and accrued liabilities	\$ 50,058	\$ 1,207	\$ 51,265
Due to other funds		5,490	5,490
Other liabilities	422,516	3,887	426,403
<b>TOTAL LIABILITIES</b>	<u>\$ 472,574</u>	<u>\$ 10,584</u>	<u>\$ 483,158</u>

**COMMONWEALTH OF PUERTO RICO**

**STATEMENT OF CHANGES IN ASSETS AND LIABILITIES -  
AGENCY FUNDS  
YEAR ENDED JUNE 30, 1997  
(Expressed in Thousands)**

	Balance July 1, 1996	Additions	Deletions	Balance June 30, 1997
<b>Assets:</b>				
Cash and cash equivalents	\$ 324,847	\$ 2,624,291	\$ (2,482,128)	\$ 467,010
Investments		16,145		16,145
Accounts receivable	2.	1		3
<b>Total Assets</b>	<b>\$ 324,849</b>	<b>\$ 2,640,437</b>	<b>\$ (2,482,128)</b>	<b>\$ 483,158</b>
<b>Liabilities:</b>				
Accounts payables and accrued liabilities	\$ 31,908	\$ 1,079,429	\$ (1,060,072)	\$ 51,265
Due to other fund		5,490		5,490
Other liabilities	334,391	2,572,907	(2,480,895)	426,403
<b>Total Liabilities</b>	<b>\$ 366,299</b>	<b>\$ 3,657,826</b>	<b>\$ (3,540,967)</b>	<b>\$ 483,158</b>





## PUBLIC UNIVERSITY FUNDS

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The public university funds are used to account for the activities of the public university and the public employee retirement system of the university. Funds are an aggregate of the funds required by the American Institute of Certified Public Accountants, Industry Audit Guide, *Audits of Colleges and Universities*.

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**University of Puerto Rico:** The University of Puerto Rico is the largest institution of higher education in Puerto Rico.

**University of Puerto Rico Retirement System** The University of Puerto Rico Retirement System is the administrator of the retirement system of the employee of the University of Puerto Rico, created under Act No. 135 approved on May 7, 1942 and became effective on January 1, 1945. Its a single-employer defined-benefit retirement system.



## COMMONWEALTH OF PUERTO RICO

## COMBINING BALANCE SHEET - PUBLIC UNIVERSITY FUNDS

JUNE 30, 1997

(Expressed in Thousands)

	University of Puerto Rico	University of Puerto Rico Retirement System	Eliminations	Total
<b>ASSETS</b>				
Cash and cash equivalents	\$ 38,392	\$ 25,449	\$	\$ 63,841
Cash and cash equivalents in governmental banks	72,522			72,522
Investments	19	353,062		353,081
Receivables, net:				
Accounts	3,026			3,026
Loans and advances	1,985	116,210		118,195
Accrued interest	264	2,814		3,078
Other	2,330	12,066		14,396
Due from:				
Other funds		351	(351)	
Primary government	34,016			34,016
Inventories	5,810			5,810
Restricted assets:				
Cash and cash equivalents	64,863	7,000		71,863
Other restricted assets	100,218	2,379		102,597
Fixed assets, net	625,430	204		625,634
Other assets	74			74
<b>TOTAL ASSETS</b>	<b>\$ 948,949</b>	<b>\$ 519,535</b>	<b>\$ (351)</b>	<b>\$ 1,468,133</b>
<b>LIABILITIES, FUND BALANCE AND OTHER CREDITS</b>				
<b>Liabilities:</b>				
Accounts payable and accrued liabilities	\$ 76,121	\$ 10,858	\$	\$ 86,979
Deposits		2,868		2,868
Due to other funds	351		(351)	
Interest payable	1,368	142		1,510
Bonds payable	324,974			324,974
Accrued compensated absences	77,454	201		77,655
Deferred compensation payable	15,611			15,611
Other liabilities	4,439			4,439
Net pension obligation	31,273			31,273
<b>Total liabilities</b>	<b>531,591</b>	<b>14,069</b>	<b>(351)</b>	<b>545,309</b>
<b>Fund Balance and Other Credits:</b>				
Investment in general fixed assets	325,751			325,751
Fund balance:				
Reserved for:				
Encumbrances	28,951			28,951
Debt service	25,364			25,364
Employee's pension benefits		505,466		505,466
Advances and other specified purposes	20,697			20,697
Unreserved	16,595			16,595
<b>Total fund balance and other credits</b>	<b>417,358</b>	<b>505,466</b>		<b>922,824</b>
<b>TOTAL LIABILITIES, FUND BALANCE AND OTHER CREDITS</b>	<b>\$ 948,949</b>	<b>\$ 519,535</b>	<b>\$ (351)</b>	<b>\$ 1,468,133</b>



## COMPONENT UNITS - OTHER

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The component units - other column is a combination of all of the public corporations that should be reported in the general purpose financial statements as required by generally accepted accounting principles. These entities are presented because the nature and significance of their relationship with the primary government are such that their exclusion would cause the general purpose financial statements to be misleading. These are discretely presented in a separate column in the general purpose financial statements due to the 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 (i.e. banking, construction, public utilities, etc.). 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, pages 15 to 29 of the general purpose financial statements included in the Financial Section of this report.

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**COMMONWEALTH OF PUERTO RICO**  
**COMBINING BALANCE SHEET - COMPONENT UNITS - OTHER**  
**JUNE 30, 1997**  
*(Expressed in Thousands)*

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation
<b>ASSETS AND OTHER DEBITS</b>						
<b>Assets:</b>						
Cash and cash equivalents	\$ 18,357	\$ 79,259	\$ 18,583	\$ 40,566	\$ 1,023	\$ 7,964
Cash and cash equivalents in governmental banks	3	2,274	791	2,463	2,985	5,310
Investments	2,974,741			96,649		1,041,234
Receivables, net:						
Intergovernmental		360,307	58,561	306,925	7,558	71,854
Accounts	213,451				79,455	
Loans and advances	132,171	4,699				7,730
Accrued interest						
Other		64,973				
Due from:						
Primary government						
Component units						
Other governmental entities						
Advances to:						
Primary government	1,279,632	677				
Component units	1,216,822					
Other governmental entities	326,706	186,974	11,666	59,432	4,951	5,713
Inventories						
Restricted assets:						
Cash and cash equivalents	1,302,790	668,269	150	81,544	239,604	
Other restricted assets			31,049		635,077	
Housing units and land lots held for sale		3,263,107	3,471,500	1,946,955	1,019	27,667
Fixed assets, net	57,983	50,760	13,811	30,980	3,711	
Other assets						
<b>Other Debits:</b>					36,766	
Amount available in debt service funds						
Amount to be provided for retirement of bonds and notes payable						
Amount to be provided for payment of accrued compensated absences and other long-term liabilities						
<b>TOTAL ASSETS AND OTHER DEBITS</b>	<b>\$ 7,522,656</b>	<b>\$ 4,681,299</b>	<b>\$ 3,606,091</b>	<b>\$ 2,565,514</b>	<b>\$ 1,318,331</b>	<b>\$ 1,167,472</b>

COMMONWEALTH OF PUERTO RICO

COMBINING BALANCE SHEET - COMPONENT UNITS - OTHER

JUNE 30, 1997

(Expressed in Thousands)

	Economic Development Bank for Puerto Rico	Puerto Rico Government Investment Trust Fund	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
<b>ASSETS AND OTHER DEBITS</b>					
<b>Assets:</b>					
Cash and cash equivalents	\$ 4,266	\$ 5	\$ 7,404	\$ 85,360	\$ 262,767
Cash and cash equivalents in governmental banks	2			83,271	97,099
Investments	517,829	621,859		345,752	5,598,064
Receivables, net:					
Intergovernmental				15,393	15,393
Accounts			15,465	210,579	1,031,249
Loans and advances	114,282	3,099		9,991	420,278
Accrued interest	4,396		2,610	19,841	171,447
Other	31,103			13,133	44,236
Due from:					
Primary government				30,167	95,140
Component units	797			8,021	8,818
Other governmental entities				77,564	77,564
Advances to:					
Primary government					
Component units	17,171				1,279,632
Other governmental entities					1,234,670
Inventories					326,706
Restricted assets:				119,907	388,643
Cash and cash equivalents				123,106	362,860
Other restricted assets			55,425	844,569	3,618,723
Housing units and land lots held for sale				132,433	132,433
Fixed assets, net	1,829		516,784	1,138,110	10,366,971
Other assets	1,762		3,667	97,169	259,843
<b>Other Debits:</b>					
Amount available in debt service funds				24,088	60,854
Amount to be provided for retirement of bonds and notes payable				369,990	369,990
Amount to be provided for payment of accrued compensated absences and other long-term liabilities					
<b>TOTAL ASSETS AND OTHER DEBITS</b>	<b>\$ 693,437</b>	<b>\$ 624,963</b>	<b>\$ 801,355</b>	<b>\$ 3,760,793</b>	<b>\$ 26,541,911</b>

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING BALANCE SHEET - COMPONENT UNITS - OTHER**  
**JUNE 30, 1997**  
*(Expressed in Thousands)*

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation
<b>LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS</b>						
Liabilities:						
Accounts payable and accrued liabilities	\$ 75,298	\$ 285,201	\$ 252,757	\$ 301,730	\$ 20,716	\$ 884,478
Deposits	3,577,185	95,012	46,727	40,277		
Due to :						
Primary government						
Component units						
Other governmental entities						
Advances from primary government		15,000	689,408		21,994	92,473
Advances from component units	303,708				250,000	
Securities lending transactions and reverses repurchases	55,757	90,575	6,918	5,855		40,465
Interest payable						
Deferred revenues						
Notes payable	1,191,317	125,000	72,434	9,380		
Bonds payable	1,037,953	3,511,102	438,349	901,268	755,873	24,438
Accrued compensated absences	3,518	190,829	26,144	32,422	58	
Other liabilities		3,118			43,776	
Other long-term liabilities		21,759		12,504	2,884	
Net pension obligation						
<b>Total liabilities</b>	<b>6,244,736</b>	<b>4,337,596</b>	<b>1,532,737</b>	<b>1,360,220</b>	<b>1,095,825</b>	<b>1,041,854</b>
<b>Equity (Deficit) and Other Credits:</b>						
Investment in general fixed assets						
Contributed capital	1,225,000	139,983	1,781,179	24,962	129,318	111,618
Retained earnings (deficit)	53,365	203,720	292,175	1,160,332		14,000
Unrealized gain (loss) in value of debt and equity securities	(445)					
Fund balances:						
Reserved for:						
Encumbrances						
Debt service						
Advances and other specified purposes						
Net asset available in the investment trust fund						
Unreserved						
<b>Total equity (deficit) and other credits</b>	<b>1,277,920</b>	<b>343,703</b>	<b>2,073,354</b>	<b>1,185,294</b>	<b>222,506</b>	<b>125,618</b>
<b>TOTAL LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS</b>	<b>\$ 7,522,656</b>	<b>\$ 4,681,299</b>	<b>\$ 3,606,091</b>	<b>\$ 2,545,514</b>	<b>\$ 1,318,331</b>	<b>\$ 1,167,472</b>



COMMONWEALTH OF PUERTO RICO

COMBINING BALANCE SHEET - COMPONENT UNITS - OTHER

JUNE 30, 1997

(Expressed in Thousands)

LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS

	Economía Development Bank for Puerto Rico	Puerto Rico Government Investment Trust Fund	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
<b>Liabilities:</b>					
Accounts payable and accrued liabilities	\$ 4,446	\$ 764	\$ 32,946	\$ 500,584	\$ 2,358,920
Deposits	2,366,002			47,744	4,042,947
Due to:					
Primary government					
Component units			39,374		39,374
Other governmental entities			21,238		21,238
Advances from primary government			1,444		1,444
Advances from component units			1,557		1,557
Securities lending transactions and reverses repurchases			26,516	454,755	1,207,673
Interest payable	300,694				946,875
Deferred revenues	2,626		4,822	26,633	193,186
Notes payable	30,698			131,071	202,234
Bonds payable	42,000		10,537	185,668	1,636,336
Accrued compensated absences			158,394	993,690	7,796,629
Other liabilities	1,756		5,846	33,157	318,692
Other long-term liabilities				12,305	56,081
Net pension obligation				215,539	298,325
<b>Total liabilities</b>	<b>618,222</b>	<b>764</b>	<b>239,061</b>	<b>2,664,759</b>	<b>19,155,774</b>
<b>Equity (Deficit) and Other Credits:</b>					
Investment in general fixed assets				195,445	195,445
Contributed capital	53,491		314,473	1,162,212	4,830,618
Retained earnings (deficit)	23,079		47,821	(424,009)	1,468,101
Unrealized gain (loss) in value of debt and equity securities	(1,355)			52,363	64,583
Fund balances:					
Reserved for:					
Encumbrances				1,181	1,181
Debt service				31,458	66,224
Advances and other specified purposes				72,087	93,841
Net assets available in the investment trust fund		624,199			624,199
Unreserved				5,277	39,945
<b>Total equity (deficit) and other credits</b>	<b>75,215</b>	<b>624,199</b>	<b>362,294</b>	<b>1,096,034</b>	<b>7,386,137</b>
<b>TOTAL LIABILITIES, EQUITY (DEFICIT) AND OTHER CREDITS</b>	<b>\$ 693,437</b>	<b>\$ 624,963</b>	<b>\$ 601,355</b>	<b>\$ 3,760,793</b>	<b>\$ 26,541,911</b>

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN**  
**RETAINED EARNINGS (DEFICIT) / FUND BALANCES -**  
**COMPONENT UNITS - OTHER**  
**Year Ended June 30, 1997**  
**(Expressed in Thousands)**

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation
<b>OPERATING REVENUES:</b>						
Charges for services	\$ 172,423	\$ 1,637,802	\$ 308,700	\$ 1,175,528	\$ 2,877	\$ 430,125
Financing income	267,138				44,577	
Investment earnings	21,030					
Other	480,591	1,637,802	308,700	1,175,528	47,454	430,125
<b>Total operating revenues</b>	<b>841,182</b>	<b>3,275,604</b>	<b>617,400</b>	<b>2,351,056</b>	<b>52,331</b>	<b>860,250</b>
<b>OPERATING EXPENSES:</b>						
Cost of services	55,785	1,201,833	299,263	709,551	6,790	470,362
Interest	277,755	164,030	96,366	254,809	38,904	4,165
Depreciation and amortization	1,401				94	
Other	334,941	1,365,863	395,629	964,160	45,788	474,527
<b>Total operating expenses</b>	<b>669,882</b>	<b>2,731,726</b>	<b>791,258</b>	<b>1,928,520</b>	<b>91,576</b>	<b>949,054</b>
<b>OPERATING INCOME (LOSS)</b>	<b>171,300</b>	<b>543,878</b>	<b>(173,858)</b>	<b>422,536</b>	<b>60,755</b>	<b>(168,804)</b>
<b>NON-OPERATING REVENUES (EXPENSES):</b>						
Intergovernmental		37,112	54,671	(32,485)		57,676
Interest income		(208,575)	(52,983)	(53,920)		18,439
Interest expense		(107,841)		19,493	3,693	
Other; net		(279,304)	1,688	(50,398)	3,693	76,115
<b>Total non-operating revenues (expenses)</b>	<b>125,650</b>	<b>(7,365)</b>	<b>(85,241)</b>	<b>160,970</b>	<b>5,359</b>	<b>31,713</b>
<b>INCOME (LOSS) BEFORE TRANSFERS</b>	<b>125,650</b>	<b>(7,365)</b>	<b>(85,241)</b>	<b>160,970</b>	<b>5,359</b>	<b>31,713</b>
<b>TRANSFERS:</b>						
From component units - other			30,000	(41,873)		(22,347)
From (to) primary government				(15,500)		
To component units - other			30,000	(57,373)		(22,347)
<b>TRANSFERS, net</b>	<b>125,650</b>	<b>(7,365)</b>	<b>(55,241)</b>	<b>103,597</b>	<b>5,359</b>	<b>9,366</b>
<b>NET INCOME (LOSS)</b>	<b>125,650</b>	<b>(7,365)</b>	<b>(55,241)</b>	<b>103,597</b>	<b>18,023</b>	<b>41,079</b>
<b>EXCESS OF REVENUES OVER EXPENDITURES</b>						
<b>FROM GOVERNMENTAL OPERATIONS</b>						
<b>CONTRIBUTIONS</b>						
<b>WITHDRAWALS</b>						
<b>DEPRECIATION ON FIXED ASSETS ACQUIRED</b>						
<b>THROUGH CAPITAL CONTRIBUTIONS</b>						
<b>INCREASE (DECREASE) IN RETAINED EARNINGS/FUND BALANCES</b>	<b>125,650</b>	<b>(7,365)</b>	<b>(6,721)</b>	<b>103,597</b>	<b>23,382</b>	<b>9,366</b>
<b>RETAINED EARNINGS (DEFICIT) / FUND BALANCE</b>	<b>27,715</b>	<b>211,085</b>	<b>298,896</b>	<b>1,056,735</b>	<b>69,806</b>	<b>102,252</b>
<b>AT BEGINNING OF YEAR (as restated)</b>	<b>(100,000)</b>					
<b>TRANSFER TO CONTRIBUTED CAPITAL</b>						
<b>RETAINED EARNINGS (DEFICIT) / FUND BALANCE</b>	<b>53,365</b>	<b>203,720</b>	<b>292,175</b>	<b>1,160,332</b>	<b>93,188</b>	<b>111,618</b>
<b>AT END OF YEAR</b>	<b>53,365</b>	<b>203,720</b>	<b>292,175</b>	<b>1,160,332</b>	<b>93,188</b>	<b>111,618</b>

**COMMONWEALTH OF PUERTO RICO**

**COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN  
RETAINED EARNINGS (DEFICIT) / FUND BALANCES -  
COMPONENT UNITS - OTHER**

Year Ended June 30, 1997  
(Expressed in Thousands)

	Economic Development Bank for Puerto Rico	Puerto Rico Government Investment Trust Fund	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
<b>OPERATING REVENUES:</b>					
Charges for services	8,033		50,025	695,947	\$ 4,301,004
Financing income	51,196	46,239		1,017	181,473
Investment earnings				35,834	444,984
Other				8,247	29,277
<b>Total operating revenues</b>	<b>59,229</b>	<b>46,239</b>	<b>50,025</b>	<b>741,045</b>	<b>4,956,738</b>
<b>OPERATING EXPENSES:</b>					
Cost of services					
Interest	14,508	1,954	24,949	1,363,114	4,148,109
Depreciation and amortization	44,202			39,738	400,599
Other	692		12,330	62,409	596,096
	8,678				8,678
<b>Total operating expenses</b>	<b>68,080</b>	<b>1,954</b>	<b>37,279</b>	<b>1,465,261</b>	<b>5,153,482</b>
<b>OPERATING INCOME (LOSS)</b>	<b>(8,851)</b>	<b>44,285</b>	<b>12,746</b>	<b>(724,216)</b>	<b>(196,744)</b>
<b>NON-OPERATING REVENUES (EXPENSES):</b>					
Intergovernmental				6,556	(25,929)
Interest income			3,662	23,751	193,386
Interest expense	9,020		(14,087)	(32,628)	(362,193)
Other, net			2,254	39,562	(15,380)
<b>Total non-operating revenues (expenses)</b>	<b>9,020</b>		<b>(8,171)</b>	<b>37,241</b>	<b>(210,116)</b>
<b>INCOME (LOSS) BEFORE TRANSFERS</b>	<b>169</b>	<b>44,285</b>	<b>4,575</b>	<b>(686,975)</b>	<b>(406,860)</b>
<b>TRANSFERS:</b>					
From component units - other				15,500	15,500
From (to) primary government				682,997	646,777
To component units - other				(21,515)	(37,015)
<b>TRANSFERS, net</b>				<b>676,982</b>	<b>627,262</b>
<b>NET INCOME (LOSS)</b>	<b>169</b>	<b>44,285</b>	<b>4,575</b>	<b>(9,993)</b>	<b>220,402</b>
<b>EXCESS OF REVENUES OVER EXPENDITURES FROM GOVERNMENTAL OPERATIONS</b>					
<b>CONTRIBUTIONS</b>					
<b>WITHDRAWALS</b>					
DEPRECIATION ON FIXED ASSETS ACQUIRED THROUGH CAPITAL CONTRIBUTIONS		(689,905)		(9,385)	8,638
<b>INCREASE (DECREASE) IN RETAINED EARNINGS/FUND BALANCES</b>	<b>169</b>	<b>(645,620)</b>	<b>4,575</b>	<b>2,747</b>	<b>51,267</b>
<b>RETAINED EARNINGS (DEFICIT) / FUND BALANCE AT BEGINNING OF YEAR (as restated)</b>	<b>22,910</b>	<b>1,269,819</b>	<b>43,246</b>	<b>(295,004)</b>	<b>2,807,460</b>
<b>TRANSFER TO CONTRIBUTED CAPITAL</b>					
<b>RETAINED EARNINGS (DEFICIT) / FUND BALANCE AT END OF YEAR</b>	<b>\$ 23,079</b>	<b>\$ 624,199</b>	<b>\$ 47,821</b>	<b>\$ (314,006)</b>	<b>\$ 2,295,491</b>

COMMONWEALTH OF PUERTO RICO  
 COMBINING STATEMENT OF CASH FLOWS - COMPONENT UNITS - OTHER  
 Year Ended June 30, 1997  
 (Expressed in Thousands)

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueeduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Operating income (loss)	\$ 125,650	\$ 271,939	\$ (86,929)	\$ 211,368	\$ 1,666	\$ (44,402)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:						
Depreciation and amortization	1,401	164,030	96,366	254,609	94	4,165
Provision for uncollectible accounts	15,923	3,348	13,716		2,914	3,384
Amortization of debt discount	(503)		(487)		236	
Net loss on disposition of fixed assets	(43,834)	(91,686)		(71,255)	(71)	(15,687)
Net gain on sale of investments and fixed assets						
Contribution in lieu of taxes						
Net cash flow effect of noncapital financing, capital and related financing and investing activities included in operating income (loss)	(102,244)			21,247		18,439
Other						
<b>Change in assets and liabilities:</b>						
Increase in:						
Receivables		(31,238)	(10,525)	(39,398)		(42,130)
Inventories		(1,522)	(241)		(3,246)	(766)
Other assets		31,055	47,959	39,331	64	14,654
Accounts payable and accrued liabilities		6,001	2,283			
Deposits						
Interest payable						
Deferred revenues			2,580			
Accrued compensated absences						
Other liabilities						
Decrease in:						
Receivables	874	4,361		1,053	626	
Inventories						
Other assets	295		4,522			
Accounts payable and accrued liabilities	(10,824)					
Deposits						
Interest payable						
Deferred revenues						
Other liabilities						
<b>Total adjustments</b>	<u>(138,912)</u>	<u>84,349</u>	<u>156,173</u>	<u>200,283</u>	<u>617</u>	<u>6,949</u>
<b>Net cash provided by (used in) operating activities</b>	<u>\$ (13,262)</u>	<u>\$ 356,288</u>	<u>\$ 69,244</u>	<u>\$ 411,651</u>	<u>\$ 2,283</u>	<u>\$ (35,553)</u>

COMMONWEALTH OF PUERTO RICO  
 COMBINING STATEMENT OF CASH FLOWS - COMPONENT UNITS - OTHER  
 Year Ended June 30, 1997  
 (Expressed in Thousands)

	Economic Development Bank for Puerto Rico	Puerto Rico Government Investment Trust Fund	Puerto Rico Industrial Development Company	Other Entities	Total Component Units Other
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>					
Operating income (loss)	\$ (8,851)	\$ 44,285	\$ 12,746	\$ (724,216)	\$ (196,744)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
Derogation and amortization	692		12,330	32,409	596,096
Provision for uncollectible accounts	9,131		3,500	16,725	68,641
Amortization of debt discount			998	930	1,174
Net loss on disposition of fixed assets			(2,510)	(1,952)	(4,533)
Net gain on sale of investments and fixed assets	(6,072)			104	(65,489)
Contribution in lieu of taxes					(162,941)
Net cash flow effect of noncapital financing, capital and related financing and investing activities included in operating income (loss)	(15,027)	(44,285)	(8,171)	20,341	(141,215)
Other	11,213			4,216	46,944
<b>Change in assets and liabilities:</b>					
Increase in:					
Receivables				(83,056)	(179,120)
Inventories			(4,011)	(2,107)	(34,352)
Other assets	(311)		(492)	(5,482)	(16,357)
Accounts payable and accrued liabilities			6,903	58,137	198,103
Deposits					8,284
Interest payable				60	60
Deferred revenues				1,865	28,655
Accrued compensated absences				18,647	21,227
Other liabilities				284	284
Decrease in:					
Receivables				15,321	21,182
Inventories				23,202	24,255
Other assets				2,030	6,847
Accounts payable and accrued liabilities	(171)			(14,010)	(25,005)
Deposits				(85)	(85)
Interest payable			(654)	(211)	(865)
Deferred revenues				(7,731)	(7,731)
Other liabilities				(8,713)	(8,713)
<b>Total adjustments</b>	<u>(545)</u>	<u>(44,285)</u>	<u>7,893</u>	<u>100,924</u>	<u>375,346</u>
<b>Net cash provided by (used in) operating activities</b>	<b>\$ (9,396)</b>	<b>\$</b>	<b>\$ 20,639</b>	<b>\$ (623,292)</b>	<b>\$ 178,602</b>

COMMONWEALTH OF PUERTO RICO

COMBINING STATEMENT OF CASH FLOWS - COMPONENT UNITS - OTHER

Year Ended June 30, 1997

(Expressed in Thousands)

	Government Development Bank for Puerto Rico and Subsidiaries	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Telephone Authority	Puerto Rico Housing Bank and Finance Agency	State Insurance Fund Corporation
<b>CASH FLOWS FROM NONCAPITAL FINANCING</b>						
ACTIVITIES:						
Proceeds from notes and loans	\$ 1,267,633	\$ 883,825	\$	\$	\$ 100,381	\$
Principal paid on notes and loans	(927,258)	(885,000)			(8,506)	
Interest paid on notes and loans	(228,528)	(9,267)	(881)		4,907	
Operating grants received			30,000			
Transfers-in from primary government						(22,347)
Transfers-out to primary government				(17,200)		
Transfers from component units						
Transfers to component units						
Capital contributions						92,473
Net increase (decrease) in securities lending transactions						
	111,847	(10,442)	29,119	(17,200)	96,762	70,126
Net cash provided by (used in) noncapital financing activities						
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>						
Acquisition and construction of capital assets		(536,855)	(389,621)	(391,410)	(683)	(10,119)
Proceeds from issuance of bonds and notes		781,337	302,462			
Principal paid on bonds and notes		(433,896)	(31,706)	(45,106)		
Interest paid on bonds and notes		(180,196)	(21,064)	(51,528)		
Proceeds from sale of equipment			32,785	10,681	394	
Capital contributions						
		(369,810)	(107,144)	(477,363)	(289)	(10,119)
Net cash used in capital and related financing activities						
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Purchase of investments securities	(8,187,243)	(67,136)		(543,604)	(523,711)	(1,599,133)
Proceeds from sales and maturities of investments securities	8,709,538	76,649	3,240	631,150	401,113	1,536,953
Purchases of units in the Puerto Rico Government Investment Trust Fund						
Redemptions of units in the Puerto Rico Government Investment Trust Fund						
Interest and dividends on investments	288,558	35,969		15,225		45,932
Principal collected on loans to:						
Public entities of the Commonwealth of Puerto Rico	1,142,170					
Private sector	12,711					
Loans originated to:						
Public entities of the Commonwealth of Puerto Rico	(1,983,143)					
Private sector	(46,069)					
	(83,478)	45,482	3,240	102,771	(15,147)	(16,248)
Net cash provided by (used in) investing activities						
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	15,107	21,718	(5,641)	19,859	(52,391)	8,206
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	3,253	59,815	25,045	23,170	282,550	5,068
<b>CASH AND CASH EQUIVALENTS FROM GOVERNMENTAL OPERATIONS</b>						
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	\$ 18,360	\$ 81,533	\$ 19,504	\$ 43,029	\$ 243,612	\$ 13,274

COMMONWEALTH OF PUERTO RICO

COMBINING STATEMENT OF CASH FLOWS - COMPONENT UNITS - OTHER

Year Ended June 30, 1997

(Expressed in Thousands)

	Economic Development Bank for Puerto Rico	Puerto Rico Government Investment Trust Fund	Puerto Rico Industrial Development Company	Other Entities	Total Component Units
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>					
Proceeds from notes and loans	\$ (151,461)	\$	\$	\$ 458,318	\$ 2,710,137
Principal paid on notes and loans	(45,155)			(139,901)	(2,112,126)
Interest paid on notes and loans				(34,662)	(318,493)
Operating grants received				374,809	409,716
Transfers-in from primary government				15,919	15,919
Transfers-out to primary government				(43,030)	(65,377)
Transfers from component units				346,662	346,662
Transfers to component units					(17,200)
Capital contributions			4,167	18,069	22,236
Net increase (decrease) in securities lending transactions	(52,141)				40,332
	(248,757)		4,167	996,184	1,031,806
Net cash provided by (used in) noncapital financing activities					
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>					
Acquisition and construction of capital assets	(441)		(34,469)	(141,608)	(1,505,208)
Proceeds from issuance of bonds and notes			10,000	40,753	1,134,552
Principal paid on bonds and notes			(24,342)	(28,976)	(564,026)
Interest paid on bonds and notes				(18,097)	(270,885)
Proceeds from sale of equipment			5,799	4,103	53,762
Capital contributions				17,219	17,219
Net cash used in capital and related financing activities	(441)		(43,012)	(126,606)	(1,134,584)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>					
Purchase of investments securities	(500,841)			(692,931)	(12,114,599)
Proceeds from sales and maturities of investments securities	742,709			358,431	12,459,783
Purchases of units in the Puerto Rico Government Investment Trust Fund				(26,124)	(26,124)
Redemptions of units in the Puerto Rico Government Investment Trust Fund				643	643
Interest and dividends on investments	58,492			58,146	482,322
Principal collected on loans to:					
Private sector	1,021			3,383	1,146,574
Public entities of the Commonwealth of Puerto Rico	39,049			4,447	58,805
Loans originated to:					
Public entities of the Commonwealth of Puerto Rico	(79,863)			(27)	(1,983,143)
Private sector					(157,106)
Net cash provided by (used in) investing activities	260,567			(294,032)	(132,845)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	1,973		(18,208)	(47,746)	(57,021)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	2,295		25,610	241,956	668,762
<b>CASH AND CASH EQUIVALENTS FROM GOVERNMENTAL OPERATIONS</b>		5		97,527	110,985
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	\$ 4,268	\$ 5	\$ 7,404	\$ 291,737	\$ 722,726





**GENERAL FIXED ASSETS ACCOUNT GROUP**

# COMMONWEALTH OF PUERTO RICO

## SCHEDULE OF GENERAL FIXED ASSETS - BY SOURCE

JUNE 30, 1997 (Expressed in Thousands)

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### General fixed assets:

Land	\$ 74,890
Buildings	1,544,901
Equipment	110,946
Construction in progress	<u>859,458</u>

**Total general fixed assets** \$ 2,590,195

### Investment in general fixed assets by source:

General fund	\$ 121,305
Capital projects funds	2,467,887
Debt service funds	<u>1,003</u>

**Total investment in general fixed assets** \$ 2,590,195

COMMONWEALTH OF PUERTO RICO  
 SCHEDULE OF GENERAL FIXED ASSETS - BY FUNCTION AND ACTIVITY  
 JUNE 30, 1997 (Expressed in Thousands)

Function and Activity	Land	Buildings	Equipment	Construction in Progress	Total
<b>General Government</b>					
Puerto Rico Maritime Shipping Authority	\$ 74,600	\$ 1,477,637	\$ 1,003	\$ 859,458	\$ 2,420,275
Public Buildings Authority			8,580		1,003
Senate			155		155
House of Representatives			240		240
General Services Administration			16,959		16,959
Municipal Services Administration			734		734
Department of Family Affairs			2,757		2,757
Office of Management and Budget			153		153
Commonwealth Electoral Commission			1,013		1,013
Planning Board			571		571
Department of the Treasury			2,830		2,830
Commissioner of Financial Institutions			185		185
Department of Transportation and Public Works			503		503
Department of Agriculture			110		110
Department of Labor and Human Resources		10,370	1,786		12,156
Industrial Commission			1,645		1,645
Department of Recreation and Sports			295		295
Environmental Quality Board			111		111
Office of the Governor			1,207		1,207
Department of Natural and Environmental Resources			1,111		1,111
<b>Total General government</b>	<b>74,600</b>	<b>1,488,007</b>	<b>41,948</b>	<b>859,458</b>	<b>2,464,013</b>
<b>Economic Development</b>					
Puerto Rico Highway and Transportation Authority	290	12,337	34,985		47,612
<b>Total Economic development</b>	<b>290</b>	<b>12,337</b>	<b>34,985</b>		<b>47,612</b>
<b>Education</b>					
Office for the Improvement of Public Schools			1,409		1,409
Department of Education			7,055		7,055
<b>Total Education</b>			<b>8,464</b>		<b>8,464</b>
<b>Public Safety</b>					
Department of Justice			2,070		2,070
Puerto Rico Volunteers Service Corporation			335		335
Correction Administration			170		170
General Court of Justice		44,557	8,037		52,594
Police Department			7,857		7,857
Puerto Rico Firefighters Corps			5,873		5,873
Juvenile Institutions Administration			1,207		1,207
<b>Total Public safety</b>		<b>44,557</b>	<b>25,549</b>		<b>70,106</b>
<b>Total General Fixed Assets</b>	<b>\$ 74,890</b>	<b>\$ 1,544,901</b>	<b>\$ 110,946</b>	<b>\$ 859,458</b>	<b>\$ 2,590,195</b>

**COMMONWEALTH OF PUERTO RICO**  
**SCHEDULE OF CHANGES IN GENERAL FIXED ASSETS - BY FUNCTION AND ACTIVITY**  
**YEAR ENDED JUNE 30, 1997 (Expressed in Thousands)**

Function and Activity	Balance as of June 30, 1996	Additions	Retirements	Balance as of June 30, 1997
<b>General government</b>	\$ 1,003	\$ 416,928	\$ (148,818)	\$ 1,003
Puerto Rico Maritime Shipping Authority	2,152,165		(302)	2,420,275
Public Buildings Authority	457			155
Senate	240			240
House of Representatives	15,951	1,008	(524)	16,959
General Services Administration	1,258			734
Municipal Services Administration	1,170	1,587		2,757
Department of Family Affairs	153			153
Office of Management and Budget	1,013			1,013
Commonwealth Electoral Commission	156			571
Planning Board	2,284	415		2,830
Department of the Treasury	185	566		185
Commissioner of Financial Institutions	364	139		503
Department of Transportation and Public Works	110			110
Department of Agriculture	12,154			12,154
Department of Labor and Human Resources	170	1,475		1,645
Industrial Commission	295			295
- Department of Recreation and Sports	111			111
- Environmental Quality Board	111			111
Department of Natural and Environmental Resources	1,111			1,111
<b>Total General government</b>	<b>2,190,330</b>	<b>422,118</b>	<b>(149,644)</b>	<b>2,462,804</b>
<b>Economic development</b>	<b>42,750</b>	<b>5,715</b>	<b>(853)</b>	<b>47,612</b>
Puerto Rico Highway and Transportation Authority	42,750	5,715	(853)	47,612
<b>Total Economic development</b>	<b>42,750</b>	<b>5,715</b>	<b>(853)</b>	<b>47,612</b>
<b>Education</b>	<b>1,032</b>	<b>377</b>		<b>1,409</b>
Office for the Improvement of Public Schools	7,055			7,055
Department of Education				
<b>Total Education</b>	<b>8,087</b>	<b>377</b>		<b>8,464</b>
<b>Public safety</b>	<b>15,360</b>	<b>1,308</b>		<b>16,668</b>
Department of Justice	335			335
Puerto Rico Volunteers Service Corporation	170			170
Correction Administration	2,327	37,475	(597)	39,205
General Court of Justice	7,736	835	(714)	7,857
Police Department		1,207		1,207
Juvenile Institutions Administration	3,449	2,424		5,873
Puerto Rico Firefighters Corps				
<b>Total Public safety</b>	<b>29,377</b>	<b>43,249</b>	<b>(1,311)</b>	<b>71,315</b>
<b>Total General Fixed Assets</b>	<b>\$ 2,270,544</b>	<b>\$ 471,459</b>	<b>\$ (151,808)</b>	<b>\$ 2,590,195</b>

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING STATEMENT OF PRIMARY GOVERNMENT**  
**GENERAL FIXED ASSETS ACCOUNT GROUP**  
**JUNE 30, 1997**  
*(Expressed in Thousands)*

ASSETS	Commonwealth of Puerto Rico	Puerto Rico Highway and Transportation Authority	Public Buildings Authority	Office for the Improvement of Public Schools	Puerto Rico Maritime Shipping Authority	Totals
Land	\$	290	\$	\$	\$	\$ 74,890
Building	54,927	12,337	74,600	\$	\$	1,544,901
Equipment	64,969	34,985	1,477,637	1,409	1,003	110,946
Construction in progress	\$	\$	859,458	\$	\$	859,458
<b>TOTAL ASSETS</b>	<b>\$ 119,896</b>	<b>\$ 47,612</b>	<b>\$ 2,420,275</b>	<b>\$ 1,409</b>	<b>\$ 1,003</b>	<b>\$2,590,195</b>
<b>INVESTMENT IN GENERAL FIXED ASSETS</b>	<b>\$ 119,896</b>	<b>\$ 47,612</b>	<b>\$ 2,420,275</b>	<b>\$ 1,409</b>	<b>\$ 1,003</b>	<b>\$2,590,195</b>



**GENERAL LONG-TERM DEBT ACCOUNT GROUP**

**COMMONWEALTH OF PUERTO RICO**  
**COMBINING STATEMENT OF PRIMARY GOVERNMENT**  
**GENERAL LONG TERM DEBT ACCOUNT GROUP**  
**JUNE 30, 1997**  
(Expressed in Thousands)

		Commonwealth of Puerto Rico	Puerto Rico Highway and Transportation Authority	Public Buildings Authority	Puerto Rico Maritime Shipping Authority	Totals
<b>ASSETS</b>						
Amount available in debt service fund	\$	256,958			\$	\$ 256,958
Amount to be provided for retirement of bonds and notes payable		4,452,637	2,411,955	1,854,852		8,719,444
Amount to be provided for payment of accrued compensated absences, and other long term liabilities		3,578,735	13,852	487,928	293,964	4,374,479
<b>TOTAL ASSETS</b>	<b>\$</b>	<b>8,288,330</b>	<b>2,425,807</b>	<b>2,342,780</b>	<b>293,964</b>	<b>\$ 13,350,881</b>
<b>LIABILITIES</b>						
Due to component units	\$	64,973			\$	\$ 64,973
Advances from component units		811,953			293,964	1,105,917
Notes payable		21,416				21,416
Bonds payable		4,431,221	2,411,955	1,854,852		8,698,028
Accrued compensated absences		677,883	7,057			684,940
Other long term liabilities		445,555	6,795	487,928		940,278
Net pension obligation		1,835,329				1,835,329
<b>TOTAL LIABILITIES</b>	<b>\$</b>	<b>8,288,330</b>	<b>2,425,807</b>	<b>2,342,780</b>	<b>293,964</b>	<b>\$ 13,350,881</b>



## **STATISTICAL SECTION**



**Commonwealth of Puerto Rico**  
**General Governmental Expenditures by Function**  
**All Governmental Fund Types**  
**For the Last Eight Fiscal Years**  
**(expressed in thousands)**

Function:	1997	1996	1995	1994	1993	1992	1991	1990	Totals
General government	\$499,652	\$661,359	\$451,275	\$341,066	\$412,606	\$388,053	\$453,827	\$317,946	\$3,525,784
Public safety	1,188,814	926,498	878,673	798,367	679,354	644,666	573,443	541,705	6,231,520
Health	508,659	245,743	231,212	192,118	109,235	189,129	204,030	219,331	1,899,457
Public housing and welfare	2,086,828	1,701,434	1,681,688	1,524,344	1,402,358	1,447,961	1,317,881	1,555,010	12,717,504
Education	1,960,185	1,832,271	1,760,784	1,511,610	1,260,580	1,583,749	1,295,220	1,270,230	12,474,629
Economic development	333,290	88,143	154,796	235,915	405,002	435,215	525,164	530,221	2,707,746
Intergovernmental	496,844	306,226	207,389	184,261	504,244	331,700	372,648	246,105	2,649,417
Lottery prizes	1,395,463	1,255,430	848,801	549,352	630,589	746,708	651,739	497,324	1,335,704
Capital outlays	359,851	367,198	660,133	317,561	294,983	310,166	526,230	232,520	3,068,642
Debt service	556,835	504,480	435,549	348,260	385,664	357,645	358,546	331,548	3,278,527
Interest and other									0
<b>Total Expenditures - All Governmental Fund Types</b>	<b>\$9,386,421</b>	<b>\$7,888,782</b>	<b>\$7,310,300</b>	<b>\$6,002,854</b>	<b>\$6,372,656</b>	<b>\$6,851,865</b>	<b>\$6,593,594</b>	<b>\$6,057,864</b>	<b>\$56,464,336</b>

\* In 1994 the Commonwealth made a change in its financial reporting policy for its Lotteries (Traditional and Additional). The revenues from the Lotteries were reported within the general fund until fiscal 1993, and since 1994 have been reported in the fund. Management believes that this change adequately reflects the operations of the Lotteries.

Note: General governmental expenditures by function were not available for the fiscal years 1988 - 1989.

**Commonwealth of Puerto Rico**  
**General Governmental Revenues by Source**  
**All Governmental Fund Types**  
**For the Last Eight Fiscal Years**  
**(expressed in thousands)**

Source:	1997	1996	1995	1994	1993	1992	1991	1990	Totals
<b>Taxes:</b>									
Income	\$3,622,988	\$3,396,724	\$3,242,876	\$2,876,542	\$2,418,006	\$2,478,803	\$2,318,144	\$2,050,501	\$22,404,584
Property	1,827,305	1,713,537	1,664,529	1,589,770	1,529,241	1,348,022	1,283,270	1,345,668	12,301,342
Excise	64,910	57,662	56,556	53,521	52,787	57,125	47,456	49,249	439,266
Other	464,034	461,736	455,500	236,609	727,093	682,474	550,287	475,414	4,053,147
Charges for services	3,077,042	2,545,615	2,492,443	2,328,427	2,024,451	2,211,605	2,114,584	2,159,501	18,953,668
Intergovernmental	110,777	59,788							170,565
Interest	134,819	186,591	170,025	144,227	116,637	207,207	218,262	220,053	1,397,821
Other									
<b>Total Revenues -</b>									
<b>All Governmental Fund Types</b>	<b>\$9,301,875</b>	<b>\$8,421,653</b>	<b>\$8,081,929</b>	<b>\$7,229,096</b>	<b>\$6,945,504</b>	<b>\$7,106,323</b>	<b>\$6,727,018</b>	<b>\$6,464,949</b>	<b>\$60,278,347</b>

Note: General governmental revenues by source were not available for the fiscal years 1988 - 1989.

**Commonwealth of Puerto Rico**  
**Computation of the Legal Debt Margin**  
**July 1, 1997**  
**(expressed in thousands)**

<b>Statutory Margin</b>	
<b>Section 2, Article VI of Constitution of Puerto Rico</b>	
<b>Internal Revenues for the year ended June 30, 1996</b>	\$4,974,917
<b>Internal Revenues for the year ended June 30, 1997(p)</b>	5,335,879
<b>Total Internal Revenues for the years ended June 30, 1996 - 1997</b>	<u>\$10,310,796</u>
<b>Internal Revenues average for the two years</b>	<u>\$5,155,398</u>
<b>Legal Debt Limit - 15% of Internal Revenues average for the two years</b>	\$773,310
<b>Maximum Debt Service Requirement - 9.292% on Commonwealth Bonds maturing 7/1/98</b>	<u>479,017</u>
<b>Additional Legal Debt Service Requirement Margin</b>	<u>\$294,293</u>

(p) Preliminary.

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 Eight Fiscal Years**  
**(expressed in thousands)**

Fiscal Year	Total Debt Service	General Governmental Expenditures	Ratio
1997	\$430,153	\$9,386,421	4.6%
1996	424,753	7,888,782	5.4
1995	389,278	7,310,300	5.3
1994	362,294	6,002,854	6.0
1993	356,291	6,372,656	5.6
1992	331,290	6,851,865	4.8
1991	296,142	6,593,594	4.5
1990	296,141	6,057,864	4.9

Note: General governmental expenditures were not available for the fiscal years 1988 - 1989.

**Commonwealth of Puerto Rico  
Demographic Statistics  
For the Last Ten Fiscal Years**

Fiscal Year	(1) Population*	Per Capita Income	(1) Median Age**	(2) School Enrollment	(1) Unemployment Rate
1997(p)	3,782	N/A	N/A	N/A	13.1
1996	3,733	\$7,882	29.4	N/A	13.8
1995(r)	3,719	7,374	28.0	709,559	13.8
1994	3,654	7,009	28.0	714,705	16.0
1993	3,600	6,837	28.0	741,914	16.8
1992	3,564	6,428	28.0	755,009	16.5
1991	3,538	6,185	28.0	759,668	15.2
1990	3,513	6,008	28.0	782,175	14.3
1989	3,479	5,518	27.5	784,385	14.4
1988	3,447	5,151	27.2	787,748	15.9

(p) Preliminary

(r) Revised

\* Amounts expressed in thousands

\*\* Estimated value using the distribution of total population.

N/A Not available

(1) Source: Puerto Rico Planning Board

(2) Source: Department of Education of Puerto Rico

**Commonwealth of Puerto Rico  
Construction and Bank Deposits  
For the Last Ten Fiscal Years**

Fiscal Year	Commercial Construction (1)		Residential Construction (1)		Bank Deposits (2)
	Number of Permits	Value *	Number of Permits	Value *	
1997(p)	354	\$149,121	6,159	\$637,699	\$23,191,572
1996(r)	290	85,231	6,180	582,186	24,823,193
1995	346	126,021	6,878	678,040	22,876,069
1994	37	81,087	6,673	470,158	19,350,635
1993	346	89,960	5,806	493,027	18,687,652
1992	48	26,714	5,041	357,792	18,684,334
1991	78	53,736	5,445	458,421	17,443,855
1990	67	31,973	4,702	377,158	18,592,129
1989	134	71,870	4,800	388,960	17,441,200
1988	683	64,249	5,099	319,477	16,200,660

(p) Preliminary

(r) Revised

\* Amounts expressed in thousands

(1) Source: Puerto Rico Planning Board

(2) Source: Financial Institutions Commissioner



**Commonwealth of Puerto Rico**  
**Miscellaneous Statistics**  
**June 30, 1997**

Statistic	Quantity
Population (millions)	3.8
Life expectancy	73.5
Area in square miles	3,426
<b>Fire Protection:</b>	
Number of stations	91
Number of fire personnel and officers	1,791
Calls answered	37,698
Building inspections conducted	32,402
<b>Police Protection:</b>	
Number of stations	448
Police personnel and officers	17,650
Total police vehicles	5,000
<b>Water System:</b>	
Customers	1,132,902
Water consumption (millions of cubic meter)	341.9
<b>Electric Distribution System:</b>	
Customers	1,291,633
Electricity consumption (millions of kilowatt)	16,118
Electricity production (millions of kilowatt)	19,143
<b>Hospital (fiscal year 1994)* :</b>	
Number of hospitals	54
Number of hospital beds in use	7,480
Number of hospital beds authorized	9,394
<b>Education (fiscal year 1997):</b>	
Enrollment in public schools:	
kindergarten to sixth grade	354,226
seventh to ninth grade	145,591
tenth to twelfth grade	117,340
Enrollment in private schools:	
kindergarten to sixth grade	91,284
seventh to ninth grade	31,244
tenth to twelfth grade	26,082
Enrollment in universities and colleges:	
Public	68,838 (p)
Private	106,552 (p)

(p) Preliminary

\* The Health Department has not been able to update these figures do to the sale of the Health Facilities.

Source: Various Commonwealth Public Agencies

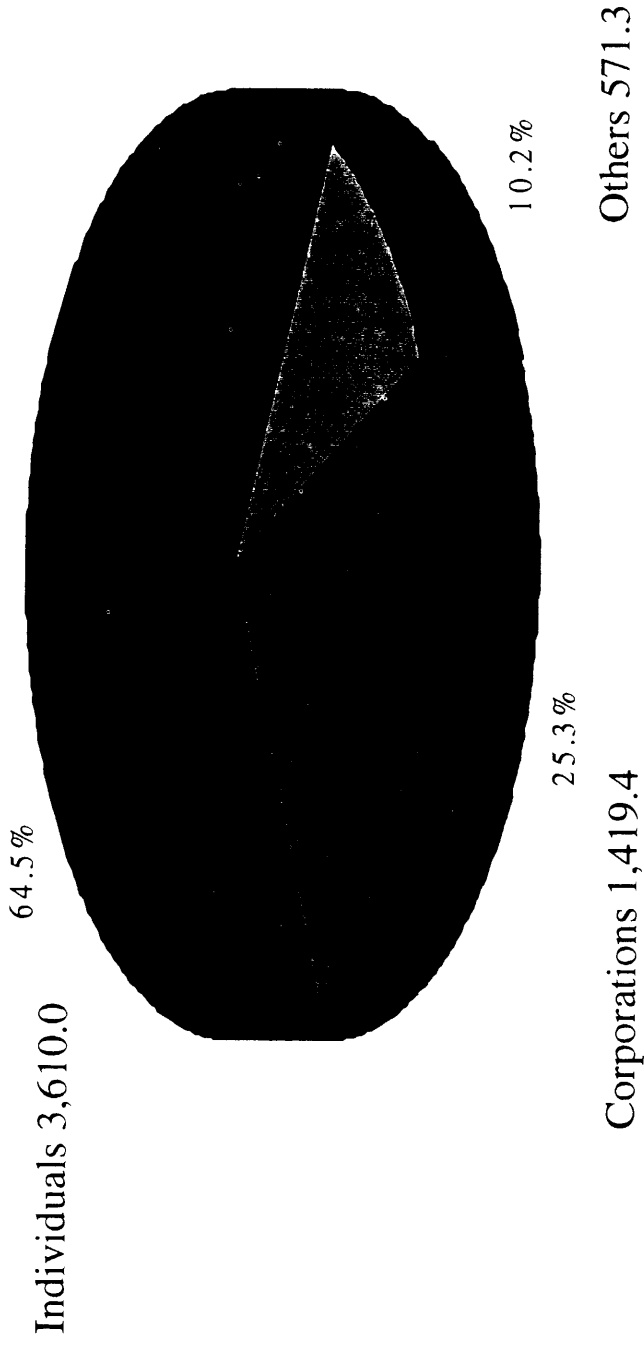
**Commonwealth of Puerto Rico**  
**General Fund Net Revenues**  
**For The Fiscal Years 1988 - 1997**  
**( expressed in thousands )**

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
<b>TOTAL</b>	3,250,249	3,564,448	3,648,124	3,861,981	3,861,136	4,025,305	4,665,331	5,080,139	5,247,616	5,600,748
<b>FROM INTERNAL REVENUES</b>	2,959,318	3,251,502	3,345,161	3,588,810	3,573,070	3,767,832	4,357,589	4,780,482	4,974,917	5,335,879
<b>TAX REVENUES</b>	2,813,755	2,920,111	3,174,949	3,427,499	3,356,945	3,531,014	4,111,119	4,531,788	4,729,350	5,065,218
<b>PROPERTY TAXES</b>	100,639	100,269	109,227	132,360	15,003	12,877	4,567	7,989	5,107	6,266
<b>INCOME TAXES: TOTAL</b>	1,795,229	1,857,898	2,060,499	2,325,513	2,335,631	2,401,279	2,856,134	3,220,937	3,368,175	3,610,016
INDIVIDUALS	818,425	869,415	1,025,084	1,123,733	1,122,335	1,241,924	1,409,824	1,578,269	1,709,116	1,825,337
CORPORATIONS	793,286	786,881	896,337	931,912	1,019,469	975,134	1,107,265	1,304,812	1,348,160	1,440,661
PARTNERSHIPS	4,507	5,034	2,119	4,001	1,167	1,165	1,802	3,391	3,323	2,120
WITHHELD FROM NONRESIDENTS	84,022	46,366	53,510	48,312	62,066	50,531	73,626	79,072	78,235	86,603
TOLLGATE TAX (REGULAR)	118,841	118,751	100,201	176,851	96,502	96,771	190,829	110,845	78,554	83,640
TOLLGATE TAX (PREPAY-IFNT)	12,302	10,910	16,819	15,060	8,505	6,076	93,527	109,928	100,900	128,805
INTEREST SUBJECT TO 17%	22,846	20,531	26,429	25,644	23,588	27,678	33,968	28,650	6,662	7,562
TAXES ON DIVIDENDS	2,431	1,336	820	1,421	1,149	1,072	934	1,535	1,547	4,028
<b>INHERITANCE AND GIFT TAXES</b>	870,208	916,608	961,785	928,722	958,321	1,067,535	1,200,400	1,252,327	1,304,024	1,419,353
<b>EXCISE TAXES: TOTAL</b>	184,146	182,466	222,184	219,055	216,890	215,035	220,882	222,187	237,815	229,043
ALCOHOLIC BEVERAGES: TOTAL	58,044	55,631	54,528	54,634	48,537	46,535	45,884	50,586	54,934	51,855
DISTILLED SPIRITS	115,875	116,707	159,394	157,258	161,484	159,471	169,555	162,630	172,425	167,321
BEER	10,227	10,128	6,262	7,163	6,869	7,029	6,463	6,971	10,596	9,867
OTHER BEVERAGES	586,082	734,152	738,601	709,687	741,431	852,500	979,518	1,030,140	1,066,108	1,180,310
GENERAL TAXES: TOTAL	96,593	97,889	113,809	104,454	102,400	106,740	115,453	107,943	107,177	120,287
CIGARETTES	10,778	6,592	9,048	8,547	10,400	13,415	12,782	16,706	20,006	22,095
PETROL FUEL PRODUCTS	180,579	186,283	178,868	172,272	178,329	217,012	275,654	319,676	307,931	365,820
MOTOR VEHICLE	•	•	•	•	•	•	•	•	•	•
TIRES, TUBES, AND ACCESSORIES	•	•	•	•	•	•	•	•	•	•
ELECTRIC AND GAS APPLIANCES	•	•	•	•	•	•	•	•	•	•
HORSE RACES	•	•	•	•	•	•	•	•	•	•
INSURANCE PREMIUMS	•	•	•	•	•	•	•	•	•	•
CEMENT	•	•	•	•	•	•	•	•	•	•
CRUDE OIL AND DERIVED PRODUCTS	•	•	•	•	•	•	•	•	•	•
5% GENERAL EXCISE TAX	•	•	•	•	•	•	•	•	•	•
OTHERS	•	•	•	•	•	•	•	•	•	•
LICENCES	45,248	44,010	42,618	39,483	46,842	48,251	49,084	49,100	50,467	53,535
MOTOR VEHICLES	37,511	36,077	31,040	29,802	36,964	38,960	39,257	38,530	39,667	42,354
ALCOHOLIC BEVERAGES	1,844	1,963	1,860	1,947	2,025	2,055	2,115	2,172	2,293	2,301
OTHERS	5,893	5,970	9,718	7,934	7,853	7,636	7,712	8,398	8,507	8,860
<b>NON-TAX REVENUES</b>	145,563	156,067	170,212	161,311	216,125	236,818	246,450	246,704	245,597	240,661
TRADITIONAL LOTTERY	60,935	67,520	74,416	68,327	60,597	70,821	62,348	63,317	60,856	52,829
ELECTRONIC LOTTERY	•	•	•	•	•	•	•	•	•	•
MISCELLANEOUS	84,628	90,547	95,796	92,984	96,437	109,713	131,909	125,973	127,733	136,836
<b>AMNESTY FUND</b>	•	•	•	•	•	•	•	•	•	•
<b>FROM NON-INTERNAL REVENUES</b>	280,931	312,946	302,963	293,171	288,066	257,473	307,762	299,647	272,689	264,869
CUSTOM DUTIES	102,883	105,355	89,249	94,364	93,038	89,741	122,477	112,153	77,781	61,114
EXCISES ON OFF-SHORE SHIPMENTS	188,048	207,591	213,714	198,767	195,028	167,732	185,285	187,494	194,918	203,755

Note : The revenues in the General Fund included in the general purpose financial statements reflect revenues from other sources in accordance with generally accepted accounting principles  
 • Amount included in the General 5% Excise Tax category.  
 Source : Puerto Rico Treasury Department

# Commonwealth of Puerto Rico General Fund Net Revenues

For the Fiscal Year 1997  
(expressed in millions of dollars)

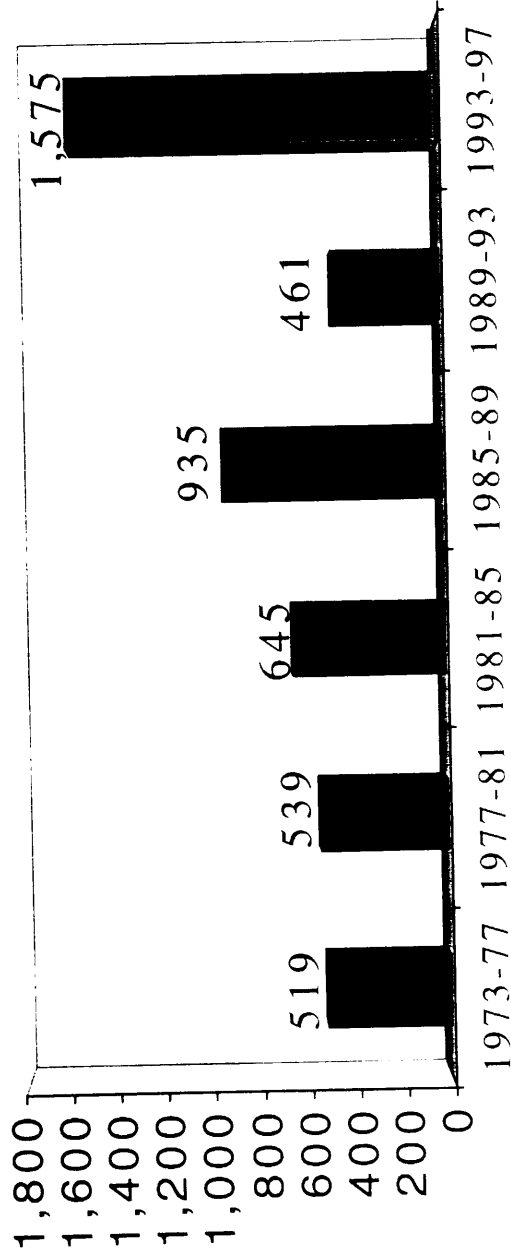


Note: The revenues in the general fund included in the general purpose financial statements reflect revenues from other sources in accordance with generally accepted accounting principles.

Source: Puerto Rico Treasury Department.

# Commonwealth of Puerto Rico Four Year Term Growth in General Fund Net Revenues

Fiscal Years  
(expressed in millions of dollars)

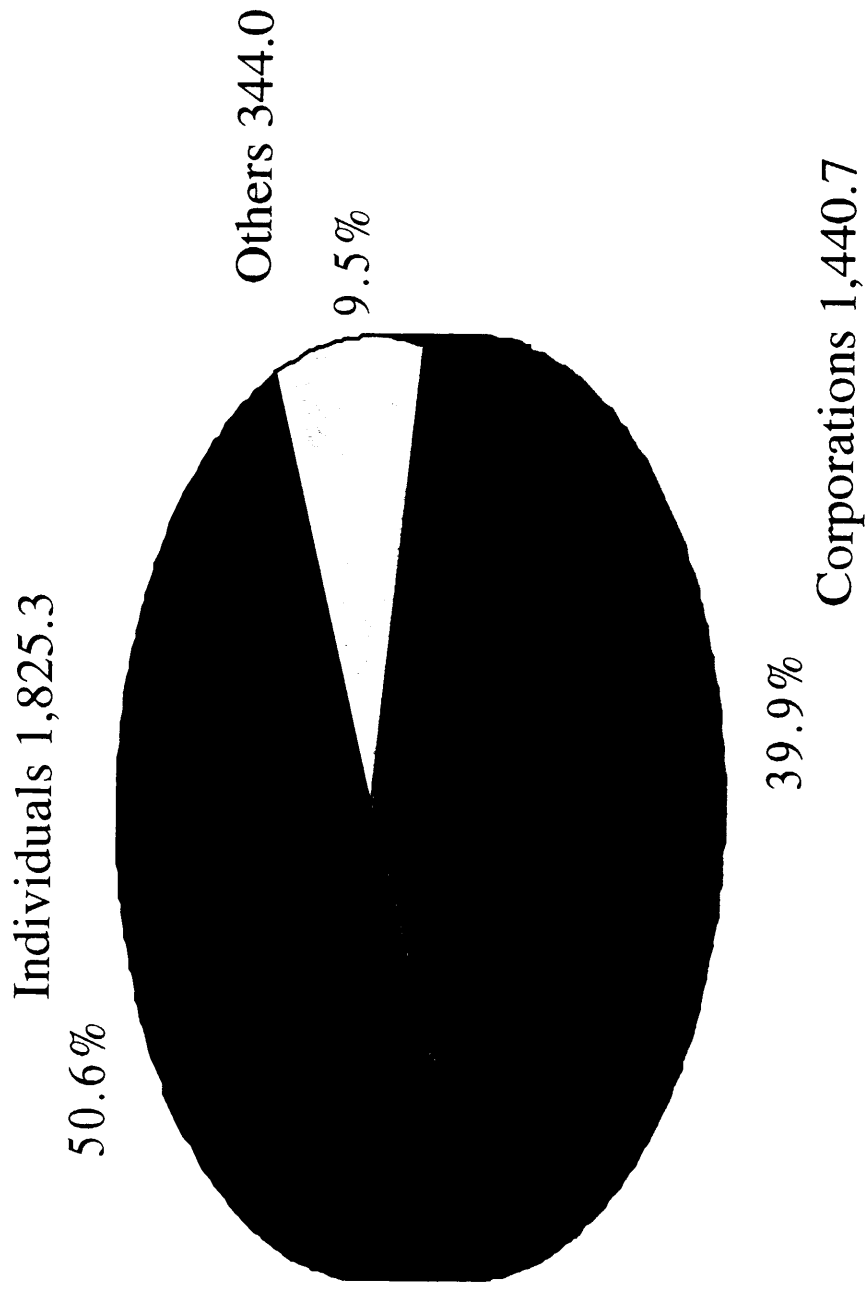


Note: The revenues in the general fund included in the general purpose financial statements reflect revenues from other sources in accordance with generally accepted accounting principles.

Source: Puerto Rico Treasury Department.

# Commonwealth of Puerto Rico Income Tax Receipts

For the Fiscal Year 1997  
(expressed in millions of dollars)



Source: Puerto Rico Treasury Department.

**Commonwealth of Puerto Rico  
Gross Product  
For the Last Seven Fiscal Years  
(expressed in millions)**

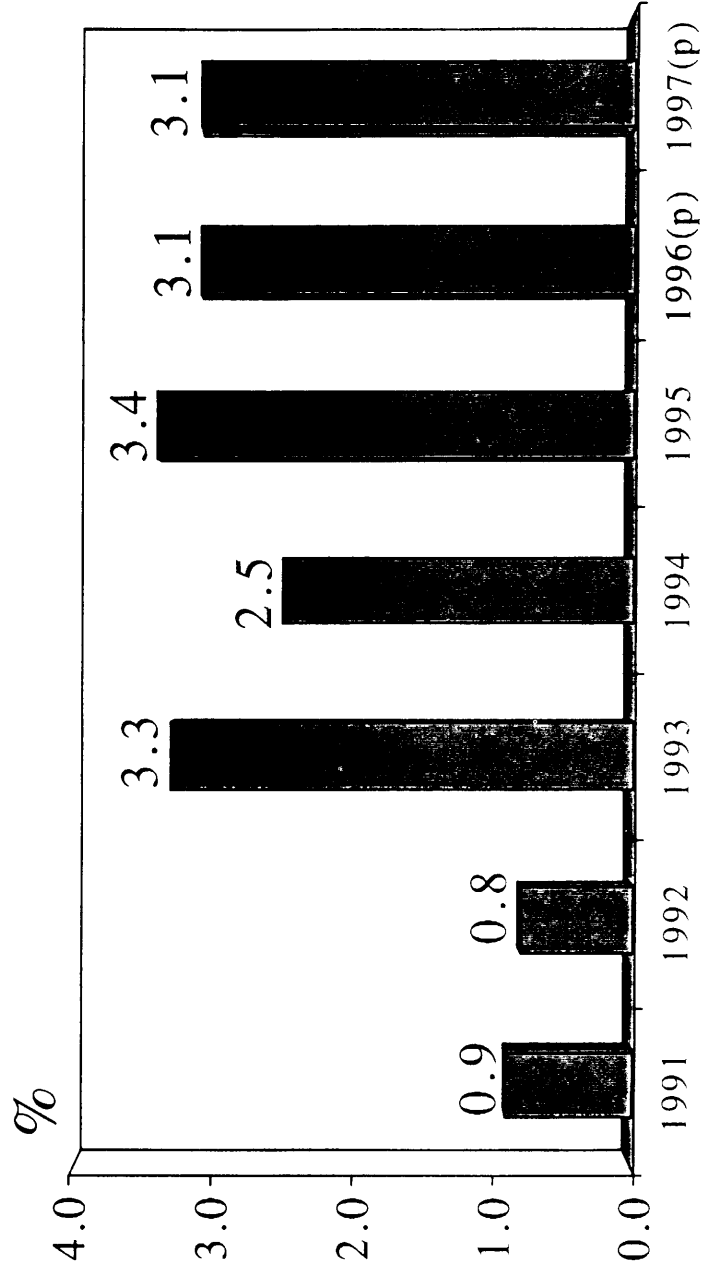
	1997(p)	1996(p)	1995	1994	1993	1992	1991
Gross Product - (Current Prices)	\$32,302	\$30,200	\$28,371	\$26,592	\$25,133	\$23,696	\$22,809
Real Gross Product - (1987 Prices)	22,595	21,919	21,248	20,553	20,054	19,410	19,260
Increase in Real Gross Product Puerto Rico	3.1%	3.1%	3.4%	2.5%	3.3%	0.8%	0.9%
United States	3.2	2.1	3.5	3.0	3.0	0.5	-0.1

(p) Preliminary.

Source: Puerto Rico Planning Board.

# Commonwealth of Puerto Rico Real Gross Product Growth

For the Last Seven Fiscal Years



(p) - Preliminary Figures.  
Source: Puerto Rico Planning Board.

**Commonwealth of Puerto Rico  
Employment and Unemployment  
For the Last Eight Fiscal Years  
(expressed in thousands)**

<b>Fiscal Year</b>	<b>Labor Force</b>	<b>Employed</b>	<b>Unemployed</b>	<b>Unemployment Rate</b>
1997	1,298	1,128	170	13.1%
1996	1,268	1,092	176	13.8%
1995	1,219	1,051	168	13.8%
1994	1,203	1,011	192	16.0
1993	1,201	999	202	16.8
1992	1,170	977	193	16.5
1991	1,152	977	175	15.2
1990	1,124	963	161	14.3

Source: Department of Labor and Human Resources, Household Survey



**Commonwealth of Puerto Rico**  
**Average Employment by Sector**  
**For the Last Eight Fiscal Years**  
**(expressed in thousands)**

Sector:	1997	1996	1995	1994	1993	1992	1991	1990
Agriculture	31	32	34	34	34	34	35	36
Manufacturing	161	167	172	166	168	164	164	168
Construction (1)	64	59	57	54	59	56	55	56
Trade	228	218	211	201	201	193	195	185
Finance, Insurance and Real Estate	37	39	36	33	32	32	32	30
Transportation, Communication and Public Utilities	59	61	59	55	54	55	58	60
Services	285	270	249	244	234	224	221	206
Government (2)	263	246	233	224	217	219	217	222
<b>Total</b>	<b>1,128</b>	<b>1,092</b>	<b>1,051</b>	<b>1,011</b>	<b>999</b>	<b>977</b>	<b>977</b>	<b>963</b>

Note: Includes population of 16 years and older.

(1) Includes mining.

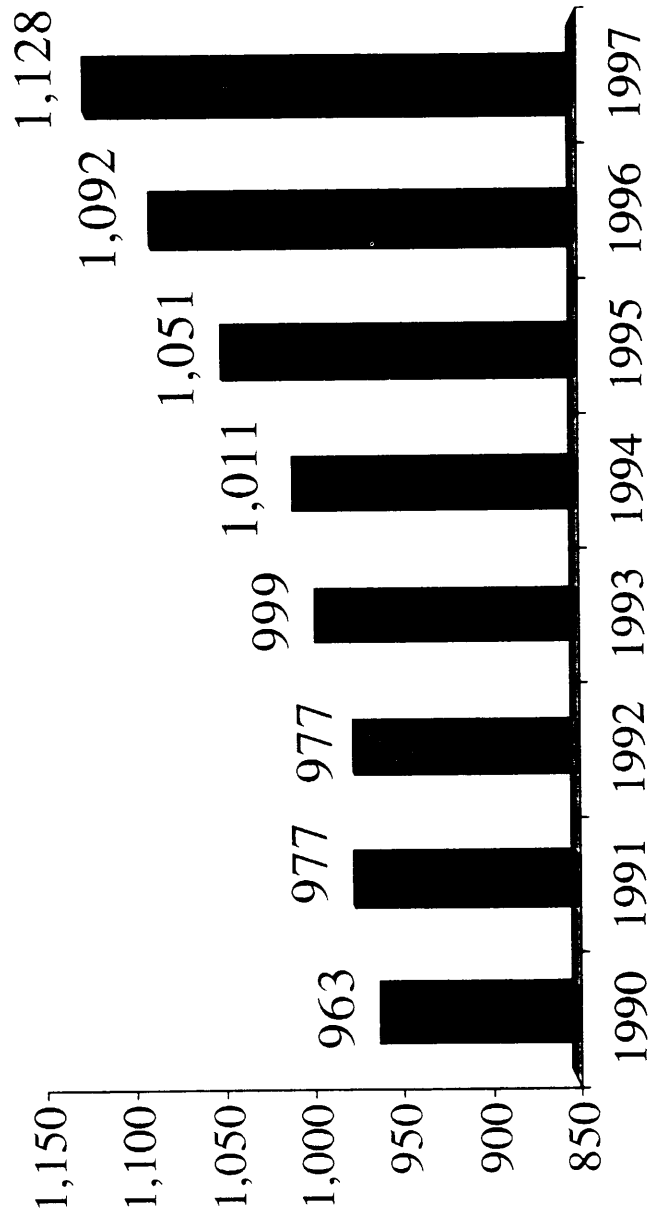
(2) Includes the Commonwealth, its municipalities and federal government, and excludes public corporations.

Source: Department of Labor and Human Resources, Household Survey

# Commonwealth of Puerto Rico

## Employment

For the Last Eight Fiscal Years  
(expressed in thousands)



Source: Department of Labor and Human Resources of Puerto Rico,  
Household Survey.

**Commonwealth of Puerto Rico  
Tourism Indicators  
For the Last Eight Fiscal Years**

	1997	1996(r)	1995	1994	1993	1992	1991	1990
All Hotels and Paradores Registration	1,461,567	1,400,815	1,302,387	1,177,571	1,087,949	1,001,303	982,212	998,396
Occupancy Rates	69.8%	69.0	68.0	68.7	68.5	66.3	69.0	73.1
Rooms Available	10,877	10,249	10,251	9,519	8,581	8,415	7,897	7,838
Visitors Expenditures*	N/A	\$1,898	1,826	1,728	1,628	1,520	1,436	1,366

(r) Revised

\* Amounts expressed in millions

N/A - Not available

Sources: Tourism Company of Puerto Rico and Puerto Rico Planning Board



**B R O W N & W O O D L L P**

**ONE WORLD TRADE CENTER  
NEW YORK, N.Y. 10048-0557**

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**APPENDIX III**

January \_\_, 1998

Hon. Xenia Vélez Silva  
Secretary of the Treasury of Puerto Rico  
San Juan, Puerto Rico

Dear Madam:

We have examined Act. No. 2 of the Legislature of Puerto Rico, approved October 10, 1985 (the "Act"), and certified copies of the legal proceedings, including a resolution adopted by the Secretary of the Treasury of the Commonwealth of Puerto Rico and approved by the Governor of the Commonwealth of Puerto Rico (the "Resolution"), and other proofs submitted relative to the issuance and sale of the following described bonds (the "Bonds"):

**\$503,963,264.10  
COMMONWEALTH OF PUERTO RICO**

**PUBLIC IMPROVEMENT REFUNDING BONDS, SERIES 1998**

Dated, maturing on July 1 of the years and in such principal amounts, bearing interest at the rates and subject to redemption, all as set forth in the Resolution. The Bonds are issuable as registered Bonds without coupons in the manner and in accordance with the terms and conditions of the Resolution.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Act is valid.
2. Said proceedings have been validly and legally taken.
3. The Act and said proceedings and proofs show lawful authority for the issuance and sale of the Bonds, and the Bonds constitute valid and binding general obligations of the Commonwealth of Puerto Rico for the prompt payment of the principal of and the interest on which the good faith, credit and taxing power of the Commonwealth of Puerto Rico are pledged.

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III-1

4. Under the provisions of the Acts of Congress now in force and under existing regulations and judicial decisions, (i) subject to continuing compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), and the Resolution regarding the use, expenditure and investment of Bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes; and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation.

Interest on the Bonds is not an item of tax preference for the purpose of computing the alternative minimum tax on individuals and corporations imposed by the Code. Such interest will, however, be includable in the computation of the alternative minimum tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternate minimum tax) of interest that is excluded from gross income.

The Commonwealth of Puerto Rico has covenanted to comply, to the extent permitted by the Constitution and laws of the Commonwealth of Puerto Rico, with the requirements of the Code so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds. We are not aware of any provisions of the Constitution or laws of the Commonwealth of Puerto Rico which would prevent the Commonwealth of Puerto Rico from complying with the requirements of the Code.

Respectfully submitted,

[To be signed "Brown & Wood LLP"]

## TABLE OF ACCRETED VALUES

**Commonwealth of Puerto Rico**  
**Public Improvement Refunding Bonds, Series 1998**  
**(General Obligation Bonds)**

Date	Capital Appreciation Bonds Due July 1,					
	<u>2008</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
January 29, 1998	3,170.15	2,276.10	2,151.20	2,038.50	1,934.25	1,841.95
July 1, 1998	3,229.25	2,322.60	2,195.65	2,080.85	1,974.60	1,880.40
January 1, 1999	3,300.60	2,378.90	2,249.40	2,132.15	2,023.50	1,926.95
July 1, 1999	3,373.55	2,436.60	2,304.55	2,184.70	2,073.55	1,974.60
January 1, 2000	3,448.10	2,495.70	2,361.00	2,238.60	2,124.90	2,023.50
July 1, 2000	3,524.30	2,556.20	2,418.85	2,293.75	2,177.50	2,073.55
January 1, 2001	3,602.20	2,618.20	2,478.10	2,350.30	2,231.40	2,124.90
July 1, 2001	3,681.80	2,681.70	2,538.80	2,408.25	2,286.60	2,177.50
January 1, 2002	3,763.15	2,746.75	2,601.00	2,467.60	2,343.20	2,231.40
July 1, 2002	3,846.35	2,813.35	2,664.75	2,528.45	2,401.20	2,286.60
January 1, 2003	3,931.35	2,881.55	2,730.05	2,590.75	2,460.65	2,343.20
July 1, 2003	4,018.20	2,951.45	2,796.90	2,654.60	2,521.55	2,401.20
January 1, 2004	4,107.00	3,023.00	2,865.45	2,720.05	2,583.95	2,460.65
July 1, 2004	4,197.80	3,096.35	2,935.65	2,787.10	2,647.90	2,521.55
January 1, 2005	4,290.55	3,171.40	3,007.55	2,855.80	2,713.45	2,583.95
July 1, 2005	4,385.40	3,248.30	3,081.25	2,926.20	2,780.60	2,647.90
January 1, 2006	4,482.30	3,327.10	3,156.75	2,998.35	2,849.40	2,713.45
July 1, 2006	4,581.35	3,407.80	3,234.10	3,072.25	2,919.95	2,780.60
January 1, 2007	4,682.60	3,490.40	3,313.30	3,147.95	2,992.20	2,849.40
July 1, 2007	4,786.10	3,575.05	3,394.50	3,225.55	3,066.25	2,919.95
January 1, 2008	4,891.85	3,661.75	3,477.65	3,305.10	3,142.15	2,992.20
July 1, 2008	5,000.00	3,750.55	3,562.85	3,386.55	3,219.90	3,066.25
January 1, 2009		3,841.50	3,650.15	3,470.05	3,299.60	3,142.15
July 1, 2009		3,934.65	3,739.60	3,555.55	3,381.25	3,219.90
January 1, 2010		4,030.10	3,831.20	3,643.20	3,464.95	3,299.60
July 1, 2010		4,127.80	3,925.05	3,733.00	3,550.70	3,381.25
January 1, 2011		4,227.90	4,021.25	3,825.05	3,638.60	3,464.95
July 1, 2011		4,330.45	4,119.75	3,919.35	3,728.65	3,550.70
January 1, 2012		4,435.45	4,220.70	4,015.95	3,820.95	3,638.60
July 1, 2012		4,543.00	4,324.10	4,114.95	3,915.50	3,728.65
January 1, 2013		4,653.20	4,430.05	4,216.35	4,012.40	3,820.95
July 1, 2013		4,766.00	4,538.60	4,320.30	4,111.70	3,915.50
January 1, 2014		4,881.60	4,649.75	4,426.80	4,213.50	4,012.40
July 1, 2014		5,000.00	4,763.70	4,535.90	4,317.75	4,111.70
January 1, 2015			4,880.40	4,647.75	4,424.65	4,213.50
July 1, 2015			5,000.00	4,762.30	4,534.15	4,317.75
January 1, 2016				4,879.70	4,646.35	4,424.65
July 1, 2016				5,000.00	4,761.35	4,534.15
January 1, 2017					4,879.20	4,646.35
July 1, 2017					5,000.00	4,761.35
January 1, 2018						4,879.20
July 1, 2018						5,000.00

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