

***The Commonwealth of Puerto Rico  
Judiciary Retirement System  
(A Pension Trust Fund of the Commonwealth of  
Puerto Rico)***

*Basic Financial Statements for the Years  
Ended June 30, 2008 and 2007,  
and Independent Auditors' Report*

*The Commonwealth of Puerto Rico*  
*Judiciary Retirement System*  
*(A Pension Trust Fund of the Commonwealth of Puerto Rico)*

*Basic Financial Statements for the Years Ended June 30, 2008 and 2007*  
*and Independent Auditors' Report*

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## Independent Auditors' Report

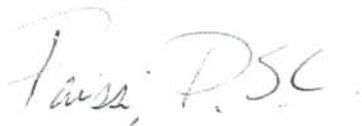
To the Board of Trustees of  
The Commonwealth of Puerto Rico Judiciary Retirement System  
San Juan, Puerto Rico

We have audited the accompanying statements of plan net assets of The Commonwealth of Puerto Rico Judiciary Retirement System (the System) (a pension trust fund of the Commonwealth of Puerto Rico) as of June 30, 2008 and 2007 and the related statement of changes in plan net assets for the years then ended. These basic financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the System as of June 30, 2008 and 2007, and the changes in its net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the schedules of employers' contributions, funding progress and notes to supplementary schedules on pages 2 through 9, and 25 through 27, respectively, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



April 27, 2009  
San Juan, Puerto Rico

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***Introduction***

The Commonwealth of Puerto Rico Judiciary Retirement System (the System) administers retirement and other plan member benefits, such as personal, cultural and mortgages loans, occupational and non-occupational disability annuities and death benefits. The System is a pension trust fund of the Commonwealth of Puerto Rico. The pension trust resources are only held in trust to pay retirement benefits to plan members. The System presents the annual basic financial statements and provides a narrative discussion and analysis of the financial activities for the fiscal years ended June 30, 2008 and 2007. The financial performance of the System is discussed and analyzed within the context of the accompanying basic financial statements and disclosures.

***Overview of the Basic Financial Statements***

The Management's Discussion and Analysis introduces the System's basic financial statements. The basic financial statements include: (1) statements of plan net assets, (2) statements of changes in plan net assets, and (3) notes to basic financial statements. The System also includes additional information to supplement the basic financial statements.

***Statements of Plan Net Assets and Statements of Changes in Plan Net Assets***

Both these statements provide information about the overall status of the System. The System uses accrual basic accounting to prepare its financial statements.

The Statements of Plan Net Assets include all of the System's assets and liabilities, with the difference reported as net assets held in trust for pension benefits. Overtime, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the System as a whole is improving or deteriorating.

The Statements of Changes in Plan Net Assets report changes in the System's assets and liabilities during the fiscal year. All current year additions and deductions are included regardless of when cash is received or paid.

***Notes to Basic Financial Statements***

The notes to basic financial statements provide additional information that is essential for an understanding of the data provided in the Statements of Plan Net Assets and Changes in Plan Net Assets.

***Required Supplementary Information***

The required supplementary information consists of two schedules and related notes concerning the funded status of the pension plan administered by the System.

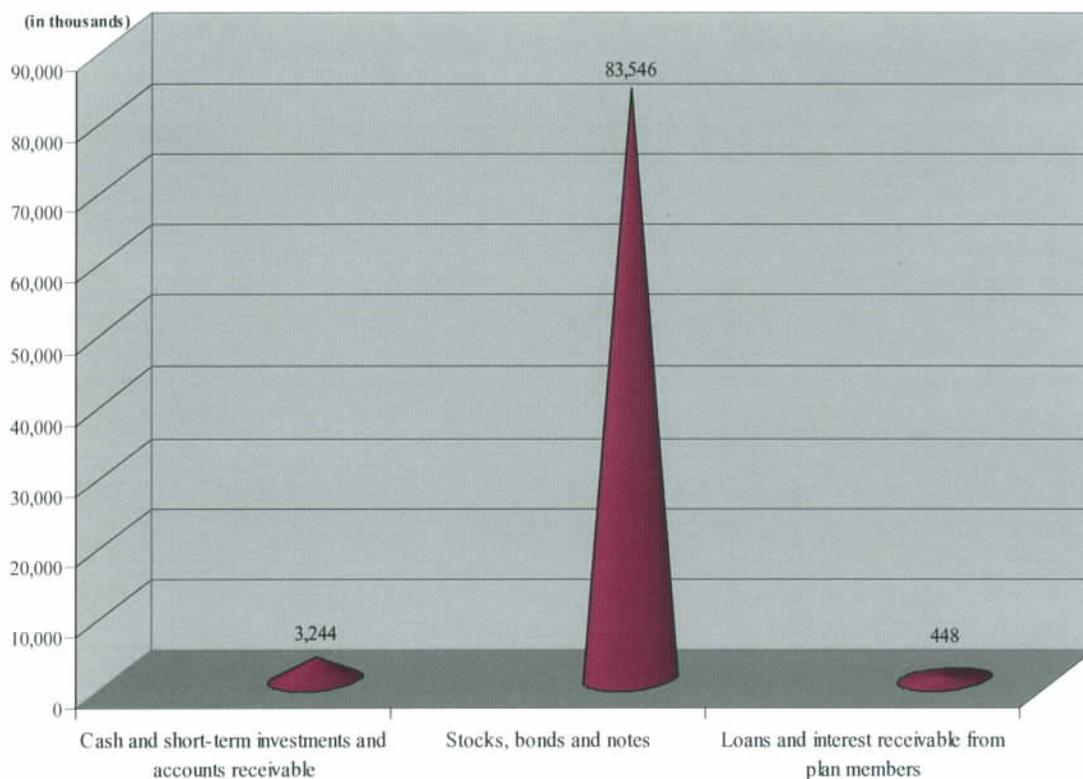
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***Financial Highlights***

The System provides the retirement benefits to the employees of the Judiciary System of Puerto Rico. The System has \$87.2 million in total assets as of June 30, 2008. The amount consists of the following:

- \$3.2 million in cash and short-term investments and accounts receivable
- \$83.5 million in stocks, bonds and notes
- \$448 thousand in loans and interest receivable from plan members

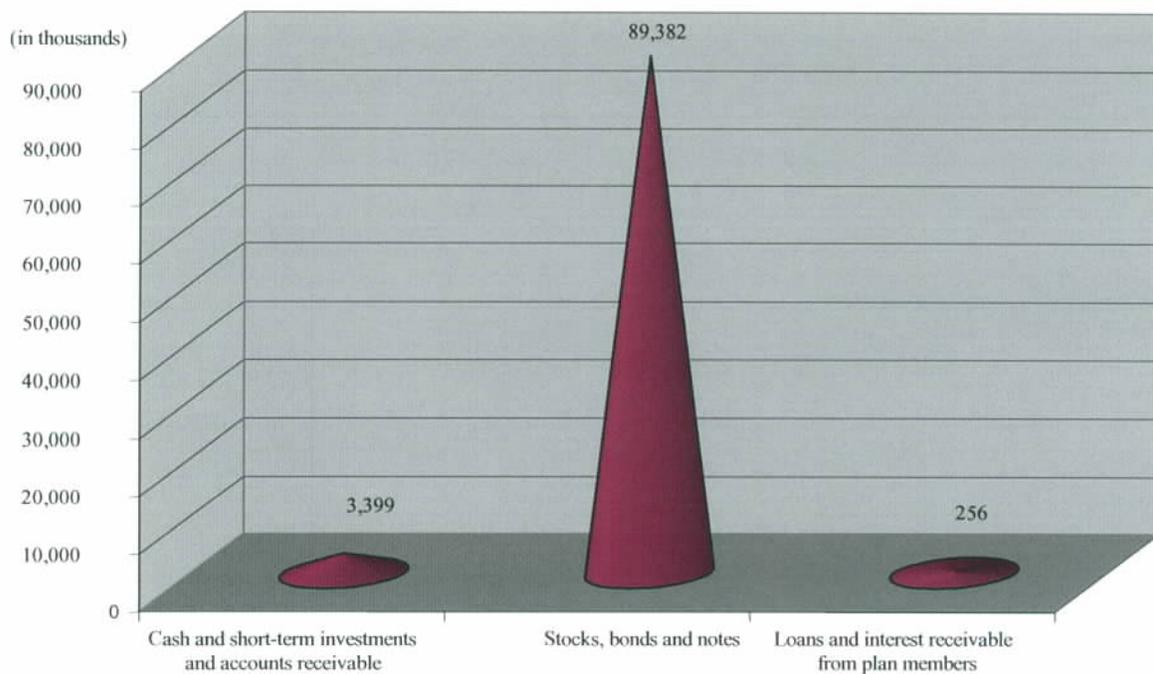


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For the fiscal year ended June 30, 2007, the System has \$93 million in total assets. The amount consists of the following:

- \$3.4 million in cash and short-term investments and accounts receivable
- \$89.4 million in stocks, bonds and notes
- \$256 thousand in loans and interest receivable from plan members



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The following provides a comparison of certain items within the basic financial statements:

	<u>2008</u>	<u>2007</u>	<u>Total Dollar Change</u>	<u>Total Percentage Change</u>
	(in thousands)			
Assets				
Cash and short term investments and total accounts receivable	\$ 3,244	3,399	(155)	-4.6%
Investments at fair value	83,546	89,382	(5,836)	-6.5%
Loans and interest receivable from plan members	448	256	192	75.0%
Total assets	<u>87,238</u>	<u>93,037</u>	<u>(5,799)</u>	<u>-6.2%</u>
Liabilities				
Accounts payable	16,714	10,528	6,186	58.8%
Insurance reserve for loans to plan members and investments purchases	401	233	168	72.1%
Other liabilities	812	803	9	1.1%
Total liabilities	<u>17,927</u>	<u>11,564</u>	<u>6,363</u>	<u>55.0%</u>
Net assets held in trust for pension benefits	<u>\$ 69,311</u>	<u>81,473</u>	<u>(12,162)</u>	<u>-14.9%</u>

	<u>2007</u>	<u>2006</u>	<u>Total Dollar Change</u>	<u>Total Percentage Change</u>
	(in thousands)			
Assets				
Cash and short term investments and total accounts receivable	\$ 3,399	2,635	764	29.0%
Investments at fair value	89,382	75,930	13,452	17.7%
Loans and interest receivable from plan members	256	274	(18)	-6.6%
Total assets	<u>93,037</u>	<u>78,839</u>	<u>14,198</u>	<u>18.0%</u>
Liabilities				
Accounts payable	10,528	5,063	5,465	107.9%
Insurance reserve for loans to plan members and investments purchases	233	119	114	95.8%
Other liabilities	803	807	(4)	-0.5%
Total liabilities	<u>11,564</u>	<u>5,989</u>	<u>5,575</u>	<u>93.1%</u>
Net assets held in trust for pension benefits	<u>\$ 81,473</u>	<u>72,850</u>	<u>8,623</u>	<u>11.8%</u>

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	2008	2007	Total Dollar Change	Total Percentage Change
	(in thousands)			
Additions				
Contributions:				
Employers	\$ 6,705	6,632	73	1.1%
Participating employees	3,076	2,828	248	8.8%
Investment (loss) income	(6,334)	13,917	(20,251)	-145.5%
Total additions	<u>3,447</u>	<u>23,377</u>	<u>(19,930)</u>	<u>-85.3%</u>
Deductions				
Retirement and other benefits	14,419	13,461	958	7.1%
Refunds of contributions	169	38	131	344.7%
General and administrative	1,021	1,255	(234)	-18.6%
Total deductions	<u>15,609</u>	<u>14,754</u>	<u>855</u>	<u>5.8%</u>
(Decrease) increase in net assets	<u>\$ (12,162)</u>	<u>8,623</u>	<u>(20,785)</u>	<u>-241.0%</u>

	2007	2006	Total Dollar Change	Total Percentage Change
	(in thousands)			
Additions				
Contributions:				
Employers	\$ 6,632	6,727	(95)	-1.4%
Participating employees	2,828	2,960	(132)	-4.5%
Investment income	13,917	6,964	6,953	99.8%
Total additions	<u>23,377</u>	<u>16,651</u>	<u>6,726</u>	<u>40.4%</u>
Deductions				
Retirement and other benefits	13,461	12,283	1,178	9.6%
Refunds of contributions	38	120	(82)	-68.3%
General and administrative	1,255	1,195	60	5.0%
Total deductions	<u>14,754</u>	<u>13,598</u>	<u>1,156</u>	<u>8.5%</u>
Net increase in net assets	<u>\$ 8,623</u>	<u>3,053</u>	<u>5,570</u>	<u>182.4%</u>

- The System's total assets at June 30, 2008 exceeded total liabilities by \$69.3 million (net assets held in trust for pension benefits). As of June 30, 2007, total assets exceeded liabilities by \$81.5 million.

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- The fair value of the System's investments, excluding loans to plan members, at June 30, 2008 amounted to \$83.5 million compared to \$89.4 million at June 30, 2007.
- Loans and interest from plan members amounted to \$448,000 at June 30, 2008 compared to \$256,000 at June 30, 2007.
- The System's funded ratio of the actuarial accrued liability at June 30, 2007 and 2006 was 31.5% and 40.0%, respectively.

***Financial Analysis of the System***

The basic financial statements of the System for the fiscal year ended June 30, 2008 present a net decrease in net assets held in trust for pension benefits of approximately \$12.1 million as compared to the fiscal year 2007. This was mainly the result of a decrease in net cash of \$146,000, plus a decrease in the fair value of the investments of \$5.8 million, and a net increase of \$6.3 million in total liabilities consisting of an increase of \$11.6 million in the amount due to the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico and a decrease of \$5.4 million in the amount due to the Treasury Department of the Commonwealth of Puerto Rico. The increase in net assets held in trust for pension benefits of approximately \$8.6 million as of June 30, 2007 when compared to the fiscal year 2006 was mainly the result of an increase in net cash of \$1.2 million, plus an increase in the fair value of the investments of \$13.4 million, offset by a reduction in account receivable and other assets of \$389,000 and an increase of \$5.6 million in total liabilities.

The System's net assets held in trust for benefits include employer and plan member contributions as well as investment income. For fiscal year 2008, employer and plan member contributions increased by approximately \$321,000, from \$9.5 million during fiscal year 2007 to \$9.8 million during fiscal year 2008. For fiscal year 2007, employer and plan member contributions decreased by approximately \$227,000, from \$9.7 million during fiscal year 2006 to \$9.5 million during fiscal year 2007. The System recognized a net depreciation in the fair value of investments of \$8 million for the fiscal year 2008 compared to a net appreciation of \$12.4 million for the fiscal year 2007.

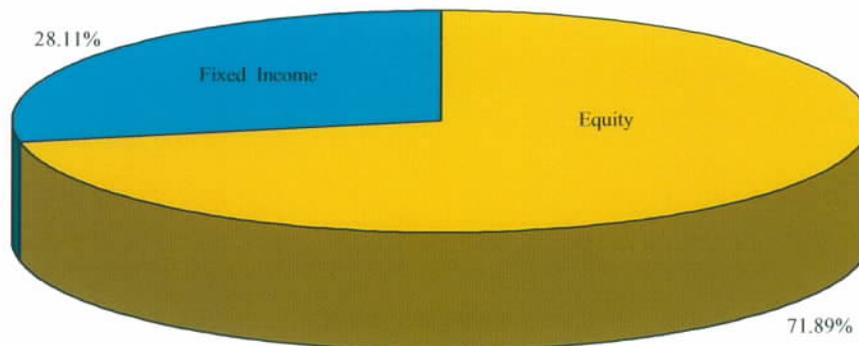
***Investments and Transactions***

At June 30, 2008 and 2007, the System held approximately \$448,000 and \$256,000, respectively, in loans and interests receivable from plan members. As of June 30, 2008 these loans consist of \$9,000 in mortgage loans, \$386,000 in personal loans, \$43,000 in cultural trip loans, and \$10,000 of accrued interest receivable applicable to the pool of loans. As of June 30, 2007 these loans consist of \$17,000 in mortgage loans, \$186,000 in personal loans, \$42,000 in cultural trip loans, and \$11,000 of interest receivable applicable to the pool of loans.

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The asset allocation is the one that fulfills the System's needs and since it is more adequately balanced, it provides protection in case of a market downturn. For fiscal year 2008, the asset allocation for Fixed Income is 28.11% and for Equity is 71.89%.



The System earns additional investment income by lending investment securities to brokers via its custodian's securities lending program. The brokers provide collateral to the System and generally used the borrowed security to over short sales and failed trades. The cash collateral received from the brokers is invested in order to earn interests. For financial statements purposes, the amount of securities that as of June 30, 2008 and 2007 were involved in the securities lending transactions was presented with the required disclosures, according to the current government accounting pronouncements. For the fiscal year 2008 and 2007, income from the custodian securities lending activity amounted to approximately \$15,575 and \$9,000, respectively.

***Funding Status***

According to the actuarial valuation as of June 30, 2007, the System's unfunded liability amounted to \$177 million with a funded ratio of 31.5 %.

In order to protect the System's financial health, the Commonwealth follows the practice of not allowing an increase in benefits unless an actuarial study is performed or the law provides the financing source.

***Increase in Economic Benefits for Retirees***

From 2007 to 2008, the Governor of Puerto Rico granted several new benefits to the System's retirees to help them cope with the increase in the cost of living, which consisted of an increase from \$550 to \$600 in the Christmas Bonus effective on December 2007.

To avoid any adverse economic impact on the System, these benefits are financed through legislative appropriations in the General Fund.

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***Requests for Information***

The financial report is designed to provide a general overview of the System's finances, comply with related laws and regulations, and demonstrate commitment to public accountability. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Commonwealth of Puerto Rico Government Employees and Judiciary Retirement Systems Administration, 437 Ponce de León Avenue, Hato Rey, Puerto Rico, 00918.

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	<u>2008</u>	<u>2007</u>
	(in thousands)	
Assets		
Cash and short-term investments:		
Deposits at commercial banks	\$ 2,519	2,735
Deposits with Government Development Bank for Puerto Rico	64	197
Deposits with Treasury Department of the Commonwealth	203	—
Total cash and short-term investments	<u>2,786</u>	<u>2,932</u>
Investments, at fair value:		
Stocks	61,377	68,654
Bonds and notes	22,169	20,728
Total investments	<u>83,546</u>	<u>89,382</u>
Loans and interest receivable from plan members	448	256
Accounts receivable:		
Accrued interest	237	237
Investment sales	196	179
Other	25	51
Total accounts receivable	<u>458</u>	<u>467</u>
Total assets	<u>87,238</u>	<u>93,037</u>
Liabilities		
Due to the Commonwealth	—	5,415
Due to the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico	16,714	5,113
Escrow funds to plan members and guarantee insurance reserve for loans to plan members	56	53
Investment purchases	345	180
Other liabilities	812	803
Total liabilities	<u>17,927</u>	<u>11,564</u>
Net assets held in trust for pension benefits	<u>\$ 69,311</u>	<u>81,473</u>

See accompanying notes to basic financial statements.

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	<u>2008</u>	<u>2007</u>
	(in thousands)	
Additions		
Contributions:		
Employer	\$ 6,705	6,632
Participating employees	3,076	2,828
Total contributions	<u>9,781</u>	<u>9,460</u>
Investment income:		
Net (depreciation) appreciation of investments	(7,957)	12,438
Dividend income	267	224
Interest income	1,553	1,447
	<u>(6,137)</u>	<u>14,109</u>
Less: Investment expense	197	192
Net investment (loss) income	<u>(6,334)</u>	<u>13,917</u>
Total additions	<u>3,447</u>	<u>23,377</u>
Deductions		
Annuities	14,419	13,461
Refund to participating employees	169	38
General and administrative	1,021	1,255
Total deductions	<u>15,609</u>	<u>14,754</u>
Net (decrease) increase	(12,162)	8,623
Net assets held in trust for pension benefits		
Beginning of year	<u>81,473</u>	<u>72,850</u>
End of year	<u>\$ 69,311</u>	<u>81,473</u>

See accompanying notes to basic financial statements.

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**1. ORGANIZATION, AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Organization***

The Commonwealth of Puerto Rico Judiciary Retirement System (the System) was created by Act No. 12 on October 19, 1954. The System is a pension trust fund of the Commonwealth of Puerto Rico (the Commonwealth). The System, as a governmental retirement plan, is excluded from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

The responsibility for the proper operation and administration of the System is vested on a Board of Trustees, composed of two participating employees and one pensioner, who are appointed by the Governor of the Commonwealth. Also, there are four Commonwealth government agency representatives, which are the Secretary of the Treasury, the President of the Government Development Bank, the Commissioner of Municipalities Affairs, and the Executive Director of the Human Resources Office of the Commonwealth of Puerto Rico.

The System is not an employer. The System's operations are managed by the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (ERS) management. Its allocations of administration costs to the System amounted to approximately \$1 million and \$1.3 million for the years ended June 30, 2008 and 2007, respectively.

The following are the significant accounting policies followed by the System in the preparation of its basic financial statements:

***Basis of Presentation***

The accompanying basic financial statements have been prepared on the accrual basis of accounting in accordance with the provisions of Governmental Accounting Standards Board No. 25 (GASB No. 25), *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* as amended by GASB Statement No. 50, *Pension Disclosures*. Participating employees and employer's contributions are recognized as additions in the period in which the employee services are rendered. Annuities and refunds are recognized as deductions when due and payable in accordance with the terms of the plan.

During the year ended June 30, 2007, the System adopted the provision of the Statement of Governmental Accounting Standards Board No. 43 (GASB No. 43), *Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans*, the objective of which is to establish uniform standards of financial reporting by state and local governmental entities for other post-employment benefits plan. This statement provides standards for measurement, recognition and display of the asset, liabilities, net assets and changes in net assets and for related disclosure.

During the year ended June 30, 2008, the System adopted the provision of the Statement of Governmental Accounting Standards Board No. 45 (GASB No. 45), *Accounting and Financial Reporting by Employers for Post-employment Benefits Other than Pensions*, the objective of which is to establish standards for the measurement, recognition, and display of other post employment benefits (OPEB) expenditures and related assets and liabilities, note disclosures, and, if applicable,

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required supplementary information (RSI) in the financial reports of state and local governmental employers.

***Use of Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted (GAAP) in the United States of America requires management to make estimates and assumptions that affect the reported amounts of net assets held in trust for pension benefits, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions to net assets held in trust for pension benefits during the reporting period. Actual results could differ from those estimates.

***Cash and Short-Term Investments***

Cash and short-term investments consist of overnight deposits guaranteed by the custodian bank, certificates of deposits in the Government Development Bank for Puerto Rico (GDB) and a commercial bank.

***Investments***

Investments are carried at fair value. The fair value of notes, bonds and stocks are based on quotations obtained from national securities exchanges. Securities transactions are accounted for on the trade date.

Mortgages, acquired from third parties, are held to maturity and are not readily marketable. Consequently, these are carried at cost.

***Loans to Plan Members***

Mortgages, personal and cultural trip loans to plan members are stated at their outstanding principal balance. Maximum amounts that may be granted to plan members for mortgage, personal and cultural trip loans are \$100,000, \$15,000 and \$10,000, respectively. The carrying value of these loans approximates their fair value.

***Reserve for Life Insurance on Loans to Plan Members***

Premiums collected and benefits claimed are recorded as additions and deductions of the guarantee insurance reserve for life insurance on loans to plan members, respectively.

***Allocation of Administrative Expenses***

The System's operations are managed by the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico management. Administrative expenses were estimated using an allocation percentage of 3% of the ERS's administrative expenses.

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***Future Adoption of Accounting Pronouncements***

The GASB has issued the following accounting standards that have effective dates after June 30, 2008:

- GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which is effective for fiscal years beginning after December 15, 2007.
- GASB Statement No. 51, *Accounting and Reporting for Intangible Assets*, which is effective for fiscal years beginning after June 15, 2009.
- GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which is effective for fiscal years beginning after June 15, 2008.
- GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is effective for fiscal years beginning after June 15, 2009.

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

**2. PLAN DESCRIPTION**

The System is a single-employer defined benefit plan sponsored by the Commonwealth. Under the terms of the Act No. 12 of 1954, as amended, all judges of the Judiciary Branch of the Commonwealth are plan members of the System.

At June 30, 2008 and 2007, membership consisted of the following:

	<u>2008</u>	<u>2007</u>
Retirees and beneficiaries		
currently receiving benefits	348	330
Current participating employees	<u>353</u>	<u>355</u>
Total membership	<u><u>701</u></u>	<u><u>685</u></u>

The plan members of the System are eligible for the following benefits:

***Retirement Annuity***

Plan members with 10 years of credited service are eligible for retirement upon reaching 60 years of age.

Plan members are eligible for monthly benefit payments determined by the application of stipulated benefit to the plan member's average compensation. Average compensation is computed based on the last month of compensation. The annuity, for which a plan member is eligible, is limited to a minimum of 25% and a maximum of 75% of the average compensation except for the judges of the Supreme Court for whom the annuity is limited to a minimum of 50% and a maximum of 100% of the average compensation received by the active members of the Supreme Court.

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***Reversionary Annuity***

A plan member, upon retirement, could elect to receive a reduced retirement annuity giving one or more benefit payments to his/her dependants. The payments would start after the death of the retiree, for an amount not less than \$120 yearly or greater than the annuity payments being received by the retiree.

***Occupational Disability Annuity***

A participating employee, who as a direct result of the performance of his/her occupation is totally and permanently disabled, is eligible for a disability annuity of 50% of the compensation, received at the time of the disability.

***Non-occupational Disability Annuity***

A participating employee totally and permanently disabled for causes not related to his/her occupation, and with no less than 10 years of credited service, is eligible for annuity of 30% of the average compensation of the first 10 years of credited services increased by 1% for every additional year of credited service in excess of 10 years up to a maximum of 50% of the average compensation.

***Death Benefits***

***Occupational:***

- Surviving spouse - annuity equal to 50% of the participating employee's salary at the date of the death.
- Children - \$10 per month for each child, minor or student, up to a maximum benefit per family of 75% of the participating employee's salary at the date of the death. If no spouse survives or dies while receiving the annuity payments, each child, 18 or under, is eligible to receive an annuity of \$20 per month up to the attainment of 18 years of age or the completion of his/her studies.

***Non-occupational:***

The contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of the death.

***Post-retirement:***

- Surviving spouse and child, 21 or under - up to 60% of the retiree's pension.
- Other designated by the retiree - the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$500.

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*Refunds*

A participating employee who ceases his/her employment with the Judiciary Branch without right to a retirement annuity has the right to a refund of the contributions to the System plus any interest earned thereon.

*Cost of Living Adjustment (COLA) for Pension Benefits*

Act No. 177 of 1997 provides, effective January 1, 1999, for increases of 3%, every three years, of the pensions paid by the System to those plan members with three or more years of retirement. The Act requires further legislation to grant this increase every three years. To protect the financial health of the System the increase granted in 2002 is being financed through appropriations by the General Fund.

**3. FUNDING POLICY**

The contribution requirement to the System is established by law and is not actuarially determined. Required contributions consist of 20% of applicable payroll for the employer and 8% for the participating employees. Commonwealth contributions should ultimately cover any deficiency between the participating employers' and employees' contributions and the System's pension benefit obligations and administrative costs.

During fiscal years 2008 and 2007, the System received appropriations from the Commonwealth to cover special laws for \$597,000 and \$500,000, respectively. The appropriations are accounted as a reduction of annuity payments.

Calculations of the present value of benefits under the System were made by consulting actuaries as of June 30, 2007, using the projected unit credit cost method, with straight proration based on service to decrement. The significant assumptions underlying the actuarial computations include: (a) assumed rate of return on investments of 7.5%, (b) assumed projected salary increases of 3%, (c) assumed inflation rate of 2.5%, (d) assumed cost of living adjustments of 0.99% annual COLA to approximate 3% triennial increases, and (e) assumed mortality as follows:

- Pre-Retirement Mortality - RP-2000 Employee Mortality Rates, with white collar adjustments for males and females, projected on a generational basis using Scale AA.
- Post-Retirement Healthy Mortality - RP-2000 Healthy Annuitant Mortality Rates, with white collar adjustments for males and females, projected on a generational basis using Scale AA.
- Post-Retirement Disabled Mortality - RP-2000 Disabled Annuitant Mortality Rates, without projection.

The actuarial accrued liability and the unfunded actuarial accrued liability as of June 30, 2007 were \$258.6 and \$177.1 million, respectively.

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**4. FUNDED STATUS AND FUNDING PROGRESS**

The funded status of each plan as of June 30, 2007, the most recent actuarial valuation date, is as follows (in thousands):

Actuarial Valuation Date	Actuarial Value of Assets	Accrued Liability	Unfunded Liability	Funded Ratio	Annual Salary	Liability as a % of Annual Salary
June 30, 2007	\$ 81,473	258,577	177,104	31.5%	31,256	566.6%

The schedule of funding progress (see page 24), presented as required supplementary information (RSI) following the notes to the financial statements, present multilayer trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the AALs for benefits.

Additional information as of the latest actuarial valuation follows:

Valuation Date	June 30, 2007
Actuarial Cost Method	Projected unit credit actuarial cost method, with straight proration based on service to decrement
Amortization Method	30 years closed, level percentage of payroll
Remaining Amortization Period	19 years
Asset Valuation Method	Market value of assets
Actuarial Assumptions:	
Investment rate of return	7.50%
Projected salary increases	3.00%
Inflation	2.5%
Mortality rate	<u>Pre-Retirement Mortality</u> - RP-2000 Employee Mortality Rates, with white collar adjustments for males and females, projected on a generational basis using Scale AA.  <u>Post-Retirement Healthy Mortality</u> - RP-2000 Healthy Annuitant Mortality Rates, with white collar adjustments for males and females, projected on a generational basis using Scale AA.  <u>Post-Retirement Disabled Mortality</u> - RP-2000 Disabled Annuitant Mortality Rates, without projection.
Cost of living adjustment	0.99% annual COLA to approximate 3% triennial increases.

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**5. CASH AND INVESTMENTS**

***Cash Deposits***

As of June 30, 2008 and 2007, the System's custodial credit risk was approximately \$473,000 and \$197,000, respectively, which is the bank balance of deposits at the Government Development Bank for Puerto Rico (GDB). These deposits are exempt from the collateral requirement established by the Commonwealth.

Custodial credit risk is the risk that, in an event of a bank failure, the System's deposits might not be recovered. The Commonwealth requires that 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 of the Commonwealth of Puerto Rico. Deposits at GDB are uninsured and uncollateralized, as these entities, which are component units of the Commonwealth, are exempt from compliance with the collateralization requirement.

***Investments***

The following table shows the fair value of the investments in marketable securities held by the System as of June 30, 2008 and 2007 (in thousands):

	<u>2008</u>	<u>2007</u>
Bonds:		
US Government and agencies securities	\$ 11,835	11,421
US Corporate bonds	10,334	9,307
Total bonds	<u>22,169</u>	<u>20,728</u>
Equity Investments:		
US Corporate stocks	44,109	50,192
Non-US Corporate stocks	17,268	18,462
Total equity investments	<u>61,377</u>	<u>68,654</u>
Total investments	<u>\$ 83,546</u>	<u>89,382</u>

The System's investments are exposed to custodial credit risk, credit risk, concentration of credit risk, interest rate risk and foreign currency risk. Following is a description of these risks as of June 30, 2008.

***Custodial Credit Risk***

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System may not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. At June 30, 2008 and 2007 securities investments were registered in the name of the System and were held in the possession of the System's custodian banks, State Street Bank and Trust, Citibank N.A., and Morgan Stanley.

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***Credit Risk***

All fixed income securities at the time of purchase must be of investment grade quality. The System's investment policy limits the investment in corporate debt securities to the top ratings issued by nationally recognized statistical rating organizations. The policy requires the debt securities portfolio to maintain a minimum weighted average credit quality of either "A" or better using either Standard and Poor's or Moody's Investor Services credit ratings. The following table presents the bonds and notes Moody's ratings as of June 30, 2008 and 2007, respectively (in thousands):

<b>Moodys Rating</b>	<b>Investment Type</b>	<b>Fair Value</b>	
		<b>2008</b>	<b>2007</b>
AAA	US Government Bonds	\$ 10,999	10,498
AAA	Corporate Bonds	639	1,715
A1	Corporate Bonds	2,290	489
A2	Corporate Bonds	600	496
A3	Corporate Bonds	551	1,090
AA2	Corporate Bonds	790	301
AA3	Corporate Bonds	1,468	2,282
BAA1	Corporate Bonds	1,095	769
BAA2	Corporate Bonds	1,590	1,244
BAA3	Corporate Bonds	1,311	837
AGY	Mortgage Backed	836	923
P-1	Mortgage Backed	—	84
	Total Bond and Notes	\$ <u>22,169</u>	<u>20,728</u>

***Concentration of Credit Risk***

No investment in marketable securities in any organization represents 5% or more of the System's net assets held in trust for pension benefits.

***Interest Rate Risk***

In accordance with its investment policy, the System manages its exposure to declines in fair values by structuring the investment portfolio so that securities mature to meet cash requirements for benefit payments, thereby avoiding the need to sell securities on the open market prior to maturity. Investments in equity securities are not subject to the maximum maturity policy since they do not carry a maturity date. The System is expected to achieve capital preservation and income generation by investing in diversified portfolio of marketable, investment grade core fixed income securities.

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The following table summarizes the investments on debt securities of the System at June 30, 2008 (in thousands):

	<b>Maturity from</b>	<b>Fair Value</b>	<b>1-5</b>	<b>More than 5-10</b>	<b>More than 10</b>
U.S Government and Agencies Securities	(2011-2038)	\$ 11,835	4	91	11,740
Corporate Bonds	(2011-2038)	10,334	3,218	3,241	3,875
Total Bonds		\$ 22,169	3,222	3,332	15,615

As of June 30, 2008, investments maturities are as follows:

<b>Maturity</b>	<b>Maximum Maturity</b>
One to five years	15%
More than five to ten years	15%
More than ten years	70%

***Foreign Currency Risk***

The foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit.

The international portfolio is expected to achieve long-term, aggressive capital appreciation by investing in Core EAFE (Europe Australasia and the Far East) securities. The portfolio is expected to be broadly diversified with respect to exposures to countries, economic sectors, industries and individual stock. No single issue is expected to exceed 5% (at market) of the portfolio.

As of June 30, 2008 and 2007, the System owned approximately \$17.3 and \$18.5 million, respectively, in an international equity commingled fund under the custody of Morgan Stanley investment bank, which represented approximately 3.2% and 2.5%, respectively, of the total commingled fund for each year. This pooled trust has an asset mix and country allocation as shown on the following page:

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*Notes to Basic Financial Statements*

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Assets Mix		2008	2007
		Percent	Percent
Cash and Equivalents		8.68	1.51
Future Contracts		8.77	12.14
Equity Securities		82.55	86.35
<b>Total</b>		100.00	100.00

Country Allocation	Currency	Currency Code	Portfolio %	Portfolio %
Poland	Zlotych	PLN	0.68	0.61
Russia	Rubles	RUB	0.94	0.99
Eastern Europe			1.62	1.60
Austria	Euro	EUR	0.00	1.00
Belgium	Euro	EUR	0.46	0.55
Finland	Euro	EUR	1.09	0.95
France	Euro	EUR	8.69	9.39
Germany	Euro	EUR	7.10	11.61
Greece	Euro	EUR	0.56	0.24
Ireland	Euro	EUR	0.00	0.05
Netherlands	Euro	EUR	1.88	2.47
Italy	Euro	EUR	0.00	0.99
Portugal	Euro	EUR	0.16	0.16
Spain	Euro	EUR	2.79	2.02
Euro Europe			22.73	29.43
Brazil	Real	BRL	1.24	1.93
Colombia	Pesos	COP	0.00	0.05
Mexico	Pesos	MXN	0.21	1.05
Latin America			1.45	3.03
Cyprus	Pounds	CYP	0.00	0.04
Turkey	Lira	TRY	0.02	0.22
Middle East			0.02	0.26
Denmark	Kroner	DKK	0.44	0.41
Norway	Kroner	NOK	1.76	1.32
Sweeden	Krona	SEK	1.85	2.61
Switzerland	Francs	CHF	5.56	4.72
United Kingdom	Pounds	GBP	16.32	17.85
Non-Euro Europe			25.93	26.91
Australia	Dollars	AUD	4.80	3.81
China	Yuan Renmimbi	CNY	0.46	1.80
Hong Kong	Dollars	HKD	2.58	1.26
Indonesia	Rupiahs	IDR	0.18	0.48
Japan	Yen	JPY	23.38	24.72
Malasya	Ringgits	MYR	0.08	0.08
New Zealand	Dollars	NZD	0.01	0.01
Philippines	Pesos	PHP	0.02	0.00
Singapore	Dollars	SGD	2.53	2.14
South Korea	Won	KRW	0.02	0.56
Taiwan	New Dollars	TWD	0.70	0.14
Pacific			34.76	35.00
Emu	Euro	EUR	4.51	0.60
Africa	Rand	ZAR	0.08	0.14
India	Rupees	INR	0.22	1.52
Other			4.81	2.26
Cash			8.68	1.51
<b>Total</b>			100.00	100.00

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***Securities Lending Transactions***

The System entered into securities lending transactions. The System's securities custodian, as agent, manages the securities lending program and receives liquid collateral. At June 30, 2008 and 2007, the collateral received represents 103.37% and 101.88%, respectively, of the fair value of the securities lent.

Fair value of securities lending obligations for which collateral was received consisted of \$3.4 million and \$4.3 million in US equity securities at June 30, 2008 and 2007, respectively.

The underlying collateral for these securities had a market value of approximately \$3.5 million and \$4.3 million as of June 30, 2008 and 2007, respectively, and was invested as follows (in thousands):

<b>Collateral Description</b>	<b>2008</b>		<b>2007</b>	
Asset Backed Commercial Paper	\$ —	—	631	14.56%
Reverse Repo U.S. Agency Delivered	21	0.61%	423	9.76%
Reverse Repo Corporate Tri-party	3,447	99.39%	3,280	75.68%
Total	<u>\$ 3,468</u>	<u>100.00%</u>	<u>4,334</u>	<u>100.00%</u>

The System has very low credit risk exposure to borrowers. The System's rights to collateral are defined in the contractual agreement. There is excess collateral above 100%. In case of borrower default, the System has immediate rights to collateral. Borrower's creditworthiness is also proactively reviewed by the Lending Agent.

**6. LOANS AND INTEREST RECEIVABLE FROM PLAN MEMBERS**

The loans receivable from plan members are substantially guaranteed by the contributions of plan members and by other sources, including mortgage deeds and any unrestricted amount remaining in the escrow funds. In addition, collections on loans receivable are received through payroll deductions. Effective September 2007, the System increased the maximum amounts that may be granted to plan members for personal and cultural trip loans from \$5,000 to \$15,000 and from \$5,000 to \$10,000, respectively.

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The composition of loans and interest receivable from plan members as of June 30, 2008 and 2007 is summarized as follows (in thousand):

	<u>2008</u>	<u>2007</u>
Loans receivable:		
Mortgage	\$ 9	17
Personal	386	186
Cultural trips	<u>43</u>	<u>42</u>
Total loans to plan members	438	245
Accrued interest receivable	<u>10</u>	<u>11</u>
Total loans and interest receivable	<u>\$ 448</u>	<u>256</u>

***Guarantee Insurance Reserve for Loans to Plan Members***

The System provides life insurance that guarantees the payment of the outstanding principal balance of mortgage, personal and cultural trip loans in case of death of a plan member. This coverage is paid in its entirety by the plan members who obtain these loans from the System. The life insurance rates are actuarially determined and do not vary by age, sex or health status.

\* \* \* \* \*

*Required Supplementary Schedules of Employers'  
Contributions and Funding Progress*

***The Commonwealth of Puerto Rico***  
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***(A Pension Trust Fund of the Commonwealth of Puerto Rico)***  
*Schedule of Employers' Contributions*  
*June 30, 2008*  
*(In thousands)*

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<b>Year Ended June 30,</b>	<b>Actual Employer Contributions</b>	<b>Annual Required Contributions</b>	<b>Percent Contributed</b>	<b>Annual Pension Cost</b>	<b>Percent Contributed</b>
2008	\$ 7,262	19,803	36.67% *	19,829	36.62% *
2007	6,632	9,735	68.12%	9,553	69.42%
2006	6,727	9,735	69.10%	9,553	70.42%
2005	6,470	8,707	74.31%	8,380	77.21%
2004	5,556	8,707	63.81%	8,380	66.30%
2003	5,536	6,892	80.33%	6,464	85.64%
2002	5,412	6,892	78.53%	6,464	83.73%

\* Percentage contributed for the year ended June 30, 2008 assumes the actual employer contribution is 20.0% of expected payroll for the Basic System Benefits plus the expected pay-as-you-go amounts for the selected System Administered Benefits.

The above liabilities are for Basic System Benefits and Selected System Administered Benefits.

See notes to supplementary schedules of employers' contribution and funding progress.

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*Schedule of Funding Progress*  
*June 30, 2008*  
*(In thousands)*

<b>Actuarial Valuation Date</b>	<b>Actuarial Value of Assets</b>	<b>Accrued Liability</b>	<b>Unfunded Liability</b>	<b>Funded Ratio</b>	<b>Annual Salary</b>	<b>Unfunded Liability as a % of Annual Salary</b>
June 30, 2007	\$ 81,473	258,577	177,104	31.5%	31,256	566.6%
June 30, 2006	72,850	N/A	N/A	N/A	N/A	N/A
June 30, 2005	69,797	174,454	104,657	40.0%	29,331	356.8%
June 30, 2004	67,851	N/A	N/A	N/A	N/A	N/A
June 30, 2003	61,781	166,732	104,951	37.1%	25,711	408.2%
June 30, 2002	60,438	N/A	N/A	N/A	N/A	N/A

The above liabilities are for Basic System Benefits and Selected System Administered Benefits.

See notes to supplementary schedules of employers' contribution and funding progress.

*The Commonwealth of Puerto Rico*  
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*Notes to Supplementary Schedules of*  
*Employers' Contributions and Funding Progress*  
*June 30, 2008*

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**1. SCHEDULE OF CONTRIBUTIONS**

The Schedule of Contributions provides information about the annual required contributions (ARC) and the extent to which contributions made cover the ARC. The ARC is the annual required contribution for the year calculated in accordance with certain parameters, which include actuarial methods and assumptions.

The System's Schedule of Contributions is based on total benefit and administration cost, net of member contributions; it includes both Commonwealth's and participating employers' contributions. The Commonwealth's and participating employers' contributions, ultimately, should cover any deficiency between the pension benefits and the System's administration cost, net of member contributions. The information was obtained from the last actuarial report as of June 30, 2007.

**2. SCHEDULE OF FUNDING PROGRESS**

The Schedule of Funding Progress provides information about the funded status of the System and the progress being made in accumulating sufficient assets to pay benefits when due. The information was obtained from the last actuarial report as of June 30, 2007.

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