

**INSTITUTE OF PUERTO RICAN CULTURE  
(A Component Unit of the Commonwealth of Puerto Rico)**

**INDEPENDENT AUDITORS' REPORT  
AND  
AUDITED FINANCIAL STATEMENTS**

**June 30, 2012**

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
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## **INDEPENDENT AUDITORS' REPORT**

To the Board of Directors of  
The Institute of Puerto Rican Culture

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Institute of Puerto Rican Culture (the "Institute"), as of and for the year ended June 30, 2012, which collectively comprise the Institute's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Institute's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Institute as of June 30, 2012, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America and the respective budgetary comparison for the General Fund.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the *Governmental Accounting Standards Board*, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries to management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

As discussed in Note 1 to the financial statements the Institute adopted the *Governmental Standard Board Statement No. 63, Statement of Net Position*, effective for periods beginning after December 15, 2011, with earlier application encouraged.

September 19, 2012

*Horwath Vilez & Co. PSC*

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**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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Our discussion and analysis of the Institute of Puerto Rican Culture (the "Institute") financial performance provide a narrative overview of the Institute's financial activities for the fiscal year ended June 30, 2012, and is intended to serve as an introduction to the basic financial statements, which have the following components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements. This Management Discussion and Analysis (the "MD&A") is designed to: (a) assist the reader in focusing on significant financial matters; (b) provide an overview of the Institute's financial activities; (c) identify any material changes from the original budget; and (d) highlight individual fund matters. We encourage readers to review this information together with the Institute's basic financial statements that follow.

**FINANCIAL HIGHLIGHTS**

- The Institute's net position decreased by \$9,503,627, or nearly 12%, mostly as a result of an increase on early retirement pension liability and a decrease from accounts receivable from federal Funds and cash.
- During the current year, the Institute's total expenses (excluding grants for capital improvements) exceeded revenues (excluding capital outlays) by \$5,524,966. This amount impacted the administrative expenses, which in turn upset the revenues and therefore resulting in a net loss in the General Fund Balance. This transaction extended its impact in other statements such as the Statement of Net Position (Liabilities and Unrestricted portion of Fund), Statement of Revenues, Expenditures and Changes in Fund Balance (Unassigned Funds), and the Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual Governmental Funds (Excess). As stated in the Circular # 98-12, these funds will be received from the OGP agency, therefore clearing the recognized expense. (See Note 8 for detail)
- General fund's operations resulted in deficiency of \$3,523,485 mostly as a result of the recognition of the early retirement pension plan by \$2,627,798.
- This year's total expenses of \$27,850,919 in the Governmental Funds segregate as follows: \$6,025,585 from previous years Fund Balance, \$2,627,798 from the accumulation of the Early Retirement Pension Plan, and \$19,197,536 from current year expenditures. This consideration of the previous year expense accumulation as well as the accumulation of the Retirement plan cause present excess of expenditures of \$8,653,104 in the total accumulation of Governmental Funds. (See Note 10 for detail)

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**MAJOR FINANCIAL ELEMENTS**

*Revenues* – The General Fund is the primary operating fund of the Institute. General Fund revenues are broadly based and include revenues not accounted for in other funds. All funds received from the Government of the Commonwealth of Puerto Rico (the “Commonwealth”) that are not restricted by law or by contractual agreements are recorded in this fund. In addition, it accounts for the funds available and not used in prior years by the budgetary fund. Special Revenue Funds includes the proceeds from special resolutions from the Commonwealth and private entities for assessments and/or capital projects. This fund includes the federal awards by the National Endowment for the Arts.

*Expenditures* – Expenditures consist principally of payroll, materials and supplies, equipment purchases, capital outlays, and transfers.

*Debt* – Comprises non-revolving lines of credit agreements to finance the capital projects. These credit facilities were granted by the Government Development Bank for Puerto Rico (the “GDB”).

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This MD&A is intended to serve as an introduction to the Institute’s basic financial statements. The Institute’s basic financial statements include three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements. This report contains additional supplementary information required to complement the basic financial statements.

The basic financial statements include two kinds of financial statements that present different views of the Institute, the government-wide financial statements and the fund financial statements. These financial statements also include the notes to the basic financial statements that explain some of the information in the financial statements and provide more detail.

**Government-wide Financial Statements**

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

- *Statement of Net Position* – This presents all of the government’s assets, deferred outflows of resources, liabilities, and deferred inflows of resources with the difference between the four reported as net position. Over time, increases or decreases in the Institute’s net position may serve as a useful indicator of whether the financial position of the Institute is improving or deteriorating.

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In the Statement of Net Position and the Statement of Activities, the governmental activities represent the basic services provided by the following departments: administrative services, culture promotion, documental and historic patrimony conservation, and interest on lines of credits.

- **Statement of Activities** – This presents information showing how the government’s net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenue for each function of the Institute.

**Fund Financial Statements**

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

- **Governmental Funds Financial Statements** – Most of the basic services provided by the Institute are financed through governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, the governmental fund financial statements focus on near-term inflows and outflows of expendable resources. They also focus on the balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Institute’s near term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting.

These statements provide a detailed short-term view of the Institute’s finances that assist in determining whether there will be adequate financial resources available to meet the current needs of the Institute. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government’s near term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the governmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The Institute has two major governmental funds. That is, each major fund is presented in a separate column in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances. The Institute’s two major governmental funds are the

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General Fund and the Special Revenue Fund. The remaining nonmajor governmental funds are grouped and presented in a single column in the governmental funds financial statements. The basic governmental funds financial statements can be found immediately following the government-wide financial statements.

The Institute adopts an annual appropriated budget for its General Fund. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with this budget. The statement of revenue and expenditures — budget and actual — budget basis — general fund only presents the information for the general fund for which there is a legally adopted budget, as required by GAAP.

- ***Agency fund Financial Statement*** – The Institute has the responsibility to transfer funds to other entities or governmental agencies. The Institute's agency activities are reported in the separate Statement of Fiduciary Net Position. Fiduciary activities are excluded from the Institute's financial statements because the Institute cannot use these assets to finance its operations. The Institute is responsible for ensuring that the assets reported in these funds are passed to the designated entity and that such entity uses these funds for the intended purpose established in the granting law. They use the accrual basis of accounting.

The basic fiduciary funds financial statements can be found immediately following the governmental funds financial statements.

**Notes to Basic Financial Statements**

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

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**MANAGEMENT DISCUSSION AND ANALYSIS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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**THE INSTITUTE AS A WHOLE:**

The Institute's Net Position decreased from prior year by \$9,503,672 or 12%, mainly as a result of a decrease of cash, accounts receivable from Federal Grants and an increase in the pension liability. Unrestricted funds - the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, legislation, or legal requirements decreased from \$1,508,969 at June 30, 2011 to (\$1,678,677) at June 30, 2012.

	<u>2012</u>	<u>2011</u>	<u>Increase / (Decrease)</u>	
			<u>Amount</u>	<u>%</u>
Current and other assets	\$ 22,535,665	\$ 27,184,906	\$( 4,649,241)	( 17)%
Capital assets, net	<u>58,824,290</u>	<u>59,322,804</u>	<u>( 498,514)</u>	<u>( 1)%</u>
Total assets	<u>\$ 81,359,955</u>	<u>\$ 86,507,710</u>	<u>\$( 5,147,755)</u>	<u>( 6)%</u>
Lines of credit and long-term liabilities	<u>\$ 12,390,662</u>	<u>\$ 8,034,745</u>	<u>\$ 4,355,917</u>	<u>54 %</u>
Total liabilities	<u>\$ 12,390,662</u>	<u>\$ 8,034,745</u>	<u>\$ 4,355,917</u>	<u>54 %</u>
Net position:				
Invested in capital assets, net of related debt	\$ 56,308,802	\$ 57,495,209	\$( 1,186,407)	( 2)%
Restricted for capital project	8,122,764	11,038,662	( 2,915,898)	( 26)%
Restricted for specific purpose	6,216,404	8,430,125	( 2,213,721)	( 26)%
Unrestricted	<u>( 1,678,677)</u>	<u>1,508,969</u>	<u>( 3,187,646)</u>	<u>( 211)%</u>
Total net position	<u>\$ 68,969,293</u>	<u>\$ 78,472,965</u>	<u>\$( 9,503,672)</u>	<u>( 12)%</u>

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**Governmental activities:**

Revenues for the Institute's governmental funds (including grants for capital improvements) decreased by 16% or \$3,722,454. Total expenditures (including capital outlays) increased by 21% or \$4,762,517.

<u>Functions/Programs</u>	<u>Revenues</u>		<u>Increase / (Decrease)</u>	
	<u>2012</u>	<u>2011</u>	<u>Amount</u>	<u>%</u>
<b>Governmental activities:</b>				
Administrative services	\$ 15,005,861	\$ 18,050,164	\$( 3,044,303)	( 17)%
Culture promotion	1,982,246	2,022,213	( 39,967)	( 2)%
Documental patrimony conservation	422,755	453,060	( 30,305)	( 7)%
Historic patrimony conservation	<u>1,786,952</u>	<u>2,394,831</u>	<u>( 607,879)</u>	<u>( 25)%</u>
Total revenues	<u>\$ 19,197,814</u>	<u>\$ 22,920,268</u>	<u>\$( 3,722,454)</u>	<u>( 16)%</u>

<u>Functions/Programs</u>	<u>Expenditures</u>		<u>Increase / (Decrease)</u>	
	<u>2012</u>	<u>2011</u>	<u>Amount</u>	<u>%</u>
<b>Governmental activities:</b>				
Administrative services	\$ 15,227,067	\$ 13,564,372	\$ 1,662,695	12 %
Culture promotion	4,467,159	3,483,029	984,130	28 %
Documental patrimony conservation	2,114,623	1,446,676	667,947	46 %
Historic patrimony conservation	6,030,907	4,574,161	1,456,746	32 %
Interest on lines of credit	<u>11,163</u>	<u>20,164</u>	<u>( 9,001)</u>	<u>( 45)%</u>
Total expenditures	<u>\$ 27,850,919</u>	<u>\$ 23,088,402</u>	<u>\$ 4,762,517</u>	<u>21 %</u>

**General Fund Budgetary Highlights:**

The Institute's budget decreased from \$17,430,163 for the fiscal year ended June 30, 2011, to \$13,676,174 for the fiscal year ended June 30, 2012.

**THE INSTITUTE'S COMBINED FUND BALANCE:**

The Institute's governmental funds (as presented in the balance sheet on page 13) reported a combined fund balance of \$14,486,203, in comparison to last year's combined fund balance of \$23,139,307, representing a decrease of \$8,653,104 as a result of the Institute's operations during the fiscal year.

**CAPITAL ASSETS AND DEBT SERVICE:**

As of June 30, 2012, the Institute had \$58,824,290 invested in capital assets net from accumulated depreciation. This amount represents a net decrease of \$571,922 or approximately 1% when compared to the fiscal year ended on June 30, 2011 due to a change in accounting principle adopted by the Institute regarding works of arts and historical treasures. Capital assets depreciation recorded during the fiscal year ended June 30, 2012 amounted to \$3,743,585.

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A detail of the Institute's capital assets at June 30, 2012 and 2011, follow:

	<u>2012</u>	<u>2011</u>
Land	\$ 55,205	\$ 55,205
Historical and archeological patrimony and works of art in museums	-	6,339,311
Construction in progress	2,044,388	2,977,473
Buildings and improvements	96,361,751	91,777,972
Furniture, fixtures and equipment	3,596,386	3,574,440
Computers and software	1,573,172	1,512,626
Vehicles	678,458	596,558
Improvements to buildings under custody	<u>2,713,766</u>	<u>3,322,448</u>
	107,023,126	110,156,033
Less: accumulated depreciation	<u>( 48,198,836)</u>	<u>( 44,493,918)</u>
	<u>\$ 58,824,290</u>	<u>\$ 65,662,115</u>

The Institute's capital budget for the fiscal year ended June 30, 2012 called for the spending of \$3,433,025. In addition, the Institute has remaining balances on certain capital expenditure projects from previous fiscal years. Therefore, the Institute's Capital Improvement Fund balance at June 30, 2012 amounted to \$8,122,764. In addition, the Institute has remaining balances on lines of credit for which an aggregate amount of \$36,100,000 was granted at inception, and for which the following amounts are available to be disbursed:

	<u>Credit Granted In Prior Years</u>	<u>Cummulative Expenditures</u>	<u>Available Amount</u>
Fortin San Geronimo	\$ 3,010,000	\$ 2,385,302	\$ 624,698
Antiguo Asilo de Beneficiencia (headquarters of the Institute)	1,000,000	857,120	142,880
Convento Los Dominicos	2,000,000	1,897,045	102,955
Museo de Artes Populares	250,000	19,851	230,149
Casa Urrutuia and Casa Blanca	400,000	282,615	117,385
Juan Ponce de Leon	663,000	486,583	176,417
Casa Wiechers Villaronga	150,000	150,000	-
Casa Armstrong	1,500,000	1,450,153	49,847
Centro Ceremonial Indigena	1,027,000	512,830	514,170
Archivo General de Puerto Rico	18,500,000	18,500,000	-
Teatros Matienzo and Music Hall	<u>7,600,000</u>	<u>7,316,371</u>	<u>283,629</u>
	<u>\$ 36,100,000</u>	<u>\$ 33,857,870</u>	<u>\$ 2,242,130</u>

Funding for these projects are mostly obtained from lines of credit granted by the Government Development Bank of Puerto Rico, and the underlying drawings shall be paid from annual budget appropriations from the "Fondo de Mejoras Permanentes" at the Central Government level.

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MANAGEMENT DISCUSSION AND ANALYSIS  
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**ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES:**

The indicators that follow were taken into account when adopting the General Fund budget for 2012. The original and the final amount available for appropriation in the General Funds budget for the fiscal year 2012 were \$13,906,000 and \$13,676,174, respectively.

**CONTACTING THE INSTITUTE'S FINANCIAL MANAGEMENT:**

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the Institute's finances and to show the Institute's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Institute of Puerto Rican Culture, Finance Department, PO Box 9024184, San Juan, Puerto Rico 00902-4184.

**INSTITUTE OF PUERTO RICAN CULTURE**  
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**STATEMENT OF NET POSITION - GOVERNMENTAL FUNDS**  
**JUNE 30, 2012**

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**ASSETS**

CASH AND CASH EQUIVALENTS	\$ 20,129,803
CASH WITH FISCAL AGENT	( 205,840)
ACCOUNTS RECEIVABLE:	
Trade, net of allowance for doubtful accounts of \$615,434	680,456
ACCOUNTS RECEIVABLE FROM FEDERAL GRANTS	31,512
INVENTORY	1,899,734
CAPITAL ASSETS:	
Land and construction in progress	2,099,593
Capital assets, net of depreciation and amortization	<u>56,724,697</u>
Total capital assets	<u>58,824,290</u>
Total Assets	<u>\$ 81,359,955</u>

**LIABILITIES**

LINES OF CREDIT	\$ 2,515,489
ACCOUNTS PAYABLE:	
Trade	2,838,285
Retainage	385,787
COMPENSATED ABSENCES:	
Due within one year	150,718
Due over one year	1,674,994
OTHER LONG TERM DEBT:	
Due within one year	545,746
Due over one year	<u>4,279,643</u>
Total Liabilities	<u>\$ 12,390,662</u>

**NET POSITION**

INVESTED IN CAPITAL ASSETS, net of related debt	\$ 56,308,801
RESTRICTED FOR:	
Capital projects	8,122,764
Specific Purposes	6,216,404
UNRESTRICTED	<u>( 1,678,676)</u>
Total Net Position	<u>\$ 68,969,293</u>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
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**STATEMENT OF ACTIVITIES - GOVERNMENTAL FUNDS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenue</u>		<u>Net (Expenses) Revenues and Changes in Net Assets</u>
		<u>Operating Grants</u>	<u>Capital Grants</u>	
<b>Governmental activities:</b>				
Administrative services	\$ 15,227,067	\$ 8,898,211	\$ -	\$( 6,328,856)
Culture promotion	4,467,159	1,633,840	-	( 2,833,319)
Documental patrimony	2,114,623	1,596,529	-	( 518,094)
Historic patrimony	6,030,907	1,796,757	935,196	( 3,298,954)
Interest on lines of credit	11,163	-	11,163	-
<b>CHANGES IN NET POSITION</b>	<u>\$ 27,850,919</u>	<u>\$ 13,925,337</u>	<u>\$ 946,359</u>	<u>( 12,979,223)</u>
NET POSITION, beginning of fiscal year				84,912,784
Inexhaustible assets				( 6,366,411)
OTHER SOURCES OF FUNDS				<u>3,402,143</u>
NET POSITION, end of fiscal year				<u>\$ 68,969,293</u>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
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**BALANCE SHEET - GOVERNMENTAL FUNDS**  
**JUNE 30, 2012**

	General Fund	Special Appropriation Fund	Other Governmental Funds	Capital Improvement Fund	Total Governmental Funds
<b>ASSETS</b>					
CASH AND CASH EQUIVALENTS	\$ 1,251,050	\$ 3,681,291	\$ 5,543,492	\$ 9,653,970	\$ 20,129,803
CASH WITH FISCAL AGENT	118,235	( 116,179)	( 207,896)	-	( 205,840)
ACCOUNTS RECEIVABLE					
Trade, Net of Allowance for Doubtful Accounts of \$639,494	143,189	220,000	317,267	-	680,456
ACCOUNTS RECEIVABLE FROM FEDERAL GRANTS INVENTORY	-	-	31,512	-	31,512
DUE FROM OTHER FUNDS	1,899,734	-	-	-	1,899,734
	3,019,570	-	-	-	3,019,570
	\$ 6,431,778	\$ 3,785,112	\$ 5,684,375	\$ 9,653,970	\$ 25,555,235
<b>LIABILITIES AND FUND BALANCES</b>					
<b>LIABILITIES</b>					
Accounts payable trade	\$ 1,387,727	\$ 160,586	\$ 98,674	\$ 1,191,299	\$ 2,838,286
Retainage	61,154	-	-	324,633	385,787
Due to other funds	10,473	4,310	2,989,513	15,274	3,019,570
Other liabilities	4,825,389	-	-	-	4,825,389
Total liabilities	6,284,743	164,896	3,088,187	1,531,206	11,069,032
<b>FUND BALANCES</b>					
Non-spendable	1,899,734	-	-	-	1,899,734
Restricted	-	3,620,216	2,596,188	8,122,764	14,339,168
Unassigned	( 1,752,699)	-	-	-	( 1,752,699)
Total fund balances	147,035	3,620,216	2,596,188	8,122,764	14,486,203
	\$ 6,431,778	\$ 3,785,112	\$ 5,684,375	\$ 9,653,970	\$ 25,555,235

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
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**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO**  
**STATEMENT OF NET POSITION**

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TOTAL FUND BALANCES - GOVERNMENTAL FUNDS	\$ 14,486,203
Amounts reported for governmental activities in the statement of net position are different because:	
Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in the governmental funds balance sheet	65,190,701
Inexhaustible assets, are not being capitalized since these are preserved and protected with cultural or historical value and generally have extraordinary long useful lives	( 6,366,411)
Lines of credit used to finance capital assets do not require financial resources and, therefore, are not reported in the governmental funds balance sheet	( 2,515,490)
Compensated absences not liquidated immediately with current financial resources are not reported in the governmental funds balance sheet	<u>( 1,825,710)</u>
NET POSITION OF GOVERNMENTAL ACTIVITIES	<u>\$ 68,969,293</u>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
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**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	General Fund	Special Appropriation Fund	Other Governmental Funds	Capital Improvement Fund	Total Governmental Funds
REVENUES	\$ 14,505,544	\$ 2,909,549	\$ 836,362	\$ 946,359	\$ 19,197,814
EXPENDITURES:					
Administrative Services	12,775,118	102,779	1,998,633	361,700	15,238,230
Culture Promotion:					
Plastic Arts	635,013	791,662	-	-	1,426,675
Popular Arts	222,657	382,795	-	-	605,452
Cultural Centers	436,678	-	-	-	436,678
Music	160,062	586,573	-	-	746,635
Theater	193,493	1,058,226	-	-	1,251,719
	1,647,903	2,819,256	-	-	4,467,159
Document Patrimony Conservation:					
General Archives of Puerto Rico	723,748	168,845	42,771	-	935,364
Publications	494,757	199,909	-	-	694,666
General Library	377,302	102,247	5,044	-	484,593
	1,595,807	471,001	47,815	-	2,114,623
Historic Patrimony Conservations:					
Historic Patrimony	521,069	215,012	-	-	736,081
Archeology	499,657	10,819	-	-	510,476
Museums and Parks	989,475	627,053	96,496	-	1,713,024
Capital Outlays	-	-	-	3,071,325	3,071,325
	2,010,201	852,884	96,496	3,071,325	6,030,906
Total expenditures	18,029,029	4,245,920	2,142,944	3,433,025	27,850,918
(DEFICIENCY)/EXCESS OF REVENUES OVER EXPENDITURES	( 3,523,485)	( 1,336,371)	( 1,306,582)	( 2,486,666)	( 8,653,104)

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	General Fund	Special Appropriation Fund	Other Governmental Funds	Capital Improvement Fund	Total Governmental Funds
(DEFICIENCY)/EXCESS OF REVENUES OVER EXPENDITURES (brought forward)	( 3,523,485)	( 1,336,371)	( 1,306,582)	( 2,486,666)	( 8,653,104)
OTHER FINANCING SOURCES (USES), INCLUDING TRANSFERS:					
Other sources of funds to pay interest	-	-	-	717,006	717,006
Other sources of funds to pay lines of credit	-	-	-	29,111	29,111
Other uses to pay interest	-	-	-	( 717,006)	( 717,006)
Other uses to pay lines of credit	-	-	-	( 29,111)	( 29,111)
Total other financing sources	-	-	-	-	-
<b>NET CHANGE IN FUND BALANCE</b>	<b>( 3,523,485)</b>	<b>( 1,336,371)</b>	<b>( 1,306,582)</b>	<b>( 2,486,666)</b>	<b>( 8,653,104)</b>
<b>FUND BALANCES, beginning of fiscal year</b>	<b>3,670,520</b>	<b>4,956,587</b>	<b>3,902,770</b>	<b>10,609,430</b>	<b>23,139,307</b>
<b>FUND BALANCES, end of fiscal year</b>	<b>\$ 147,035</b>	<b>\$ 3,620,216</b>	<b>\$ 2,596,188</b>	<b>\$ 8,122,764</b>	<b>\$ 14,486,203</b>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTORICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND**  
**CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS WITH THE STATEMENT**  
**OF ACTIVITIES**  
**FOR THE YEAR ENDED JUNE 30, 2012**

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NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS

Amounts reported for governmental activities in the statement of activities are different because:	\$( 8,653,104)
Governmental funds report capital outlays as expenditures. However, in the government-wide statement of activities and changes in net assets, the cost of those assets is allocated over their estimated useful lives	3,071,325
The advances from lines of credit provide current financial resources to governmental funds, whereas the corresponding line of credit liability is non-current	( 717,006)
Other sources of funds to pay lines of credit provide current financial resources to the governmental funds, whereas the corresponding line of credit liability is non-current	29,111
Depreciation expense on capital assets is reported in the government-wide statement of activities and changes in net assets, but do not require the use of current financial resources. Therefore, depreciation expense on capital assets is not reported as expenditure in the governmental funds	( 3,743,585)
Interest expense in the statement of activities do not require the use of current financial resources; therefore, are not reported as expenditure over governmental funds.	( 11,163)
Expense related to Law No. 70 for voluntary termination benefits reported in the statement of activities do not required the use of current financial resources; therefore, are not reported as governmental funds	( 2,393,292)
Some expenses reported in the statement of activities do not require the use of current financial resources; therefore, are not reported as governmental funds	( 666,869)
A reduction in the compensated absences liability represents a long-term effect in net assets that is not reported as part of net changes in governmental funds	335,840
The net effect of various transactions involving capital assets (i.e. sales, disposals, and donations) is to decrease net position.	<u>3,171,663</u>
<b>CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES</b>	<b><u>\$( 9,577,080)</u></b>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**STATEMENT OF FIDUCIARY NET POSITION - FIDUCIARY FUNDS**  
**JUNE 30, 2012**

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**ASSETS**

CASH AND CASH EQUIVALENTS	\$ 3,200,574
ACCOUNT RECEIVABLE, net of allowance for doubtful accounts of \$23,000	<u>2,000,000</u>
	<u>\$ 5,200,574</u>
<b>NET ASSETS HELD FOR OTHERS</b>	<u>\$ 5,200,574</u>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -**  
**BUDGET AND ACTUAL GOVERNMENTAL FUNDS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	<b>GENERAL FUND</b>			
	<b>Budget Amounts</b>		<b>Actual Amounts</b>	<b>Variance with Final Budget</b>
	<b>Original</b>	<b>Final</b>		
REVENUES	\$ 13,906,000	\$ 13,676,174	\$ 14,505,544	\$ 829,370
EXPENDITURES:				
Administration	8,757,000	8,649,048	12,775,118	4,126,070
Culture promotion	1,685,000	1,633,840	1,647,903	14,063
Documentary patrimony conservation	1,623,000	1,596,529	1,595,807	( 722)
Historic patrimony conservation	1,841,000	1,796,757	2,010,201	213,444
Total expenditure	<u>13,906,000</u>	<u>13,676,174</u>	<u>18,029,029</u>	<u>4,352,855</u>
EXCESS OF EXPENDITURES OVER REVENUES	<u>-</u>	<u>-</u>	<u>( 3,523,485)</u>	<u>( 3,523,485)</u>
OTHER FINANCING SOURCES:				
Transfer from other funds	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
NET CHANGE IN FUND BALANCE	<u>-</u>	<u>-</u>	<u>( 3,523,485)</u>	<u>( 3,523,485)</u>
FUND BALANCE, beginning of fiscal year	<u>-</u>	<u>-</u>	<u>3,670,520</u>	<u>3,670,520</u>
FUND BALANCE, end of fiscal year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 147,035</u>	<u>\$ 147,035</u>

See accompanying notes to the basic financial statements

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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**1. NATURE OF THE INSTITUTE**

*Organization* - The Institute of Puerto Rican Culture (the "Institute") is an official, autonomous and corporate entity of the Commonwealth of Puerto Rico (a component unit), created by law No. 89 of June 21, 1955. The Institute is responsible for implementing the public policy related to the development of Puerto Rico arts, humanities and culture.

*Financial Independence* – The Institute is responsible for its debts and has the right to its surplus. No governmental agency receives the benefit nor can impose financial restraints on the Institute.

*Board of Directors* – The Institute is governed a nine member board comprising the President of the Music Art Corporation and eight members appointed by the Governor of the Commonwealth of Puerto Rico, with the advice and consent of the Senate of Puerto Rico. The Board has the power to make decisions and is responsible for them.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting and reporting policies of the Institute conform to accounting principles generally accepted in the United States of America ("U.S. GAAP"), as applicable to governmental entities.

*Measurement Focus, Basis of Accounting, and Financial Statement Presentation:*

*Government Wide Financial Statements* — The government wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Revenues from property tax are recognized in the fiscal year for which the taxes are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

*Governmental Fund Financial Statements* — The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. Principal revenue sources considered susceptible to accrual, as sales are made (consumption, and sales) and as cash is received. For this purpose, the Institute considers and consumption sales if collected within 30 days after the end of the current fiscal year. In applying the susceptible to accrual concept to federal grants, there are essentially two types of revenue. For the majority of grants, moneys must be expended by the Institute on the specific purpose or project before any amounts will be reimbursed.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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Revenue is, therefore, recognized as expenditures are incurred to the extent available. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the susceptible to accrual criteria is met. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- Employees' vested annual vacation and sick leave are recorded as expenditures when utilized.
- The amount of accumulated annual vacation and sick leave unpaid at June 30, 2012 has been reported only in the government wide financial statements.
- Interest and principal on general long-term obligations are recorded when due, except for interest and principal due on July 1 of the following fiscal year, if resources are available for its payment as of June 30.
- Executory purchase orders and contracts are recorded as a reservation of fund balance.
- Debt service expenditures, federal funds' cost disallowances, other long-term obligations, and amounts subject to judgments under litigation are recorded only when payment is due.

The Institute is organized on the basis of funds, each of which is considered to be a separate accounting entity. The transactions of each fund are summarized by providing a separate set of self-balancing accounts which include their revenues and expenditures. An emphasis is placed on major funds. A fund is considered major if it meets both of the following criteria:

***Ten Percent Criterion*** – an individual governmental fund reports at least 10% of any of the following: (a) total governmental fund assets, (b) total governmental fund liabilities, (c) total governmental fund revenues, or (c) total governmental fund expenditures.

***Five Percent Criterion*** – an individual governmental fund reports at least 5% of the total for both governmental and enterprise funds of any one of the items for which the 10% criterion is met.

Governmental funds are those through which the general functions of the Institute are financed. The acquisition, use and balance of the Institute expendable financial resources (except those accounted for in the Fiduciary funds) are accounted for through the governmental funds.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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The following are the Institute's major governmental funds:

**General fund** - The General fund is the Institute's primary operating fund. It accounts for all financial resources not accounted for in other funds. All funds received from the Government that is not restricted by law or contractual agreement is recorded in this fund. Also, it accounts for the Government funds available and not used in prior years by the budgetary fund.

Capital outlays in the General Fund and Capital Improvements Funds are recorded as expenditures of those funds at the time of purchase.

To provide the details of capital assets for the primary government, the Institute segregates land, historic buildings, improvements, works of art and equipment stated at cost in a note to financial statements. Cost of maintenance and repairs that do not improve or extend the life of the respective assets are expensed as incurred. Cost of restorations and improvements are capitalized for this purpose.

**Special revenue funds** – The special revenue funds are composed of: (a) the special appropriations fund and (b) the capital improvements fund.

- **Special appropriations fund** – The Special Appropriations fund accounts for the proceeds of special resolutions of the Government of the Commonwealth of Puerto Rico and private entities (other than assessments or capital projects) that are legally restricted to expenditures for specified purposes.
- **Capital improvements fund** – This fund accounts for financial resources to be used for the acquisition or construction of major capital facilities. It includes the capital improvements fund used to account for the restoration and improvements to historic monuments and buildings. They are financed from resolutions of the Government of the Commonwealth of Puerto Rico and the corresponding interest earned from the corresponding bank accounts.

The non-major funds are presented in one column in the financial statements and include the following:

**Endowment fund** – The Endowment fund accounts for federal block grants awarded by the National Endowment for the Arts.

**National fund** – This fund is used to account for the proceeds of joint resolutions of the Commonwealth of Puerto Rico Government that are donated to qualified individuals and entities that are engaged in the promotion of theatrical, musical and general arts in Puerto Rico.

**Total Governmental Funds column** – The total columns on the statements are provided only to facilitate additional analysis. Inter-fund transactions have not been eliminated; therefore, total columns are not comparable to a consolidation.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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**Fund Balance** – In accordance with Government Accounting Standards Board (the “GASB”) No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, fund balance is composed of five classifications designed to disclose the hierarchy of constraints placed on how fund balance can be spent, as follows:

**Non-spendable fund balance** – amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

- **Inventory** – the portion of fund balance that is not available resource because it represents the year-end balance of ending inventory, which is a non-spendable resource.

**Restricted fund balance** – amounts that are restricted to specific purposes externally imposed by creditors or imposed by law. The Institute’s restricted fund balance consists of the special appropriations fund, capital improvement fund, endowment fund and national fund. These fund balance amounts arise from special resolutions of the Government of the Commonwealth of Puerto Rico and private entities that can only be spent in specified purposes.

**Committed fund balance** – amounts that can be used only for specific purposes imposed by formal action (resolution) of the Board of Directors (the “Board”). Those committed amounts cannot be used for any other purpose unless the Board removes or changes the specified use by taking the same type of action (resolution) it employed to previously commit those amounts. In contrast to fund balance that is restricted by enabling legislation, committed fund balance classification may be redeployed for other purposes with appropriate due process.

**Assigned fund balance** – amounts in the assigned fund balance classification are intended to be used by the Institute for specific purposes but do not meet the criteria to be classified as restricted or committed. In governmental funds other than General Fund, assigned fund balance represents the remaining that is not restricted or committed. In the General Fund, assigned amounts represent intended uses established by the Board or the Institute official delegated that authority by Board resolution.

**Unassigned fund balance** – the portion of fund balance that has not been restricted, committed, or assigned to specific purposes or other funds. The Institute’s unassigned fund balance consists of the fund balance amount in the General Fund minus the Inventory. These fund balances are available for any purpose and management will determine how to spend it.

The Institute applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amount are available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

The Institute does not have a formal minimum fund balance policy.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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*Fiduciary fund type* – Fiduciary fund type is used to report assets held by the Institute as an agent for individuals, private organizations, other governmental entities, and/or other funds. The Institute's Fiduciary fund is also named as the agency fund. The Agency fund is custodial in nature (assets equal liabilities) and does not involve measurement of results of operations.

*Use of Estimates in the Preparation of Financial Statements* - The preparation of financial statements in conformity with accounting principles generally accepted of the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, deferred outflows of resources, liabilities and deferred inflows of resources, and related disclosures at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

*Concentration of Credit Risk* - The Institute maintains cash on deposit with higher rated financial institutions and with the Puerto Rico Treasury Department ("PRTD"). The laws of the Commonwealth of Puerto Rico require public funds deposited in commercial banks to be collateralized by the bank when funds exceed the amount insured by the Federal Government. The securities pledged by the banks as collateral for those deposits are under the custody of the Secretary of the Treasury in the name of the Commonwealth of Puerto Rico. Deposits with the Governmental Development Bank of Puerto Rico are exempt of the collateralization requirement and represent a credit risk of custody, because in case of bankruptcy of the bank the entity will not recover its deposits.

*Cash and Cash Equivalents* – Cash and cash equivalents include petty cash, checking and other instruments with original maturities of less than three months.

*Cash with Fiscal Agent* – The Institute's budgetary assignments from the Central Government are under the custody of the PRTD. The PRTD processes the Institute's payroll and such payments are deducted from the budgetary assignments. Money transfers for budgetary assignments other than payroll may be requested by the Institute at any time during the normal course of operations, subject to the Central Government's budgetary management procedures. At June 30, 2012, the Institute maintained \$(205,840) under the PRTD's custody.

*Accounts receivable* - Accounts receivable are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions.

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

*Inventory* - Inventory is stated at cost based on the first-in, first-out method and reported at cost when individual inventory items are used.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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*Capital Assets* - Capital assets are stated at historical cost when purchased or at estimated fair market value when donated. Costs of repairs and maintenance, which do not increase or extend the life of the respective assets are expensed as incurred. Assets which cost or estimated fair value is stated over \$500 are capitalized when purchased or received as a donation. The historic buildings are at the value established when acquired or received and buildings improvements are capitalized as buildings are constructed or repaired. The artwork and historic collections are partially included in the financial statements of the Institute, but there are some collections for which no valuation was performed, therefore, were not included. The cost or donation amount was assigned to those included at the time of the acquisition.

Major outlays for capital assets, renewals, and betterments are capitalized. In accordance to the presentation of a component unit, capital assets (depreciated for the purpose of presentation by the primary government) are depreciated using the straight-line method over the following estimated useful lives:

<u>Asset Category</u>	<u>Years</u>
Buildings	50
Leasehold improvements	20
Furniture and fixtures	10
Vehicles	5
Computer equipment	3

*Compensated Absences* – It is the Institute’s policy to permit employees to accumulate earned but unused vacation and sick pay benefits. The excess over 60 days of vacations and over 90 days of sick leave benefits are paid to the employee. A liability is reported only for the amount due, for example, as a result of employee resignation and retirement.

*Accounting for Pension Costs* – The Institute accounts for pension costs in accordance with the provisions of GASB N0. 27, Accounting for Pensions by States and Local Governmental Employers, as amended by GASB No. 50, Pension Disclosures. GASB No. 27 establishes standards of accounting and financial reporting for pension expenditures/expenses and related pension liabilities, pension assets, financial statements disclosures, and required supplementary information in the financial reports of state and local governmental employers. The Statement defines that the pension expenses is equal to the statutory required contribution to the employee’s retirement system. A pension liability or assets is reported equal to the cumulative difference between statutory required and actual contributions.

*Termination Benefits* – The Institute accounts for termination benefits in accordance with the provisions of GASB No. 47, Accounting for Termination Benefits, which indicates that employers should recognize a liability and expense for voluntary termination benefits when the offer is accepted and the amount can be estimated. A liability and expense for involuntary termination benefits should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees, and the amount can be estimated.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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*Budgetary Data* – The Budget is prepared following the modified accrual basis of accounting. The actual results of operations, presented in the Statement of Revenues, Expenditures, and Changes in Fund Balances – Budgets and Actual, is in conformity with the budgetary accounting of the Institute for a better comparison with the budget information.

*Inexhaustible Works of Arts and Collections* – The Institute has adopted guidelines promoted under GASB No. 34 which establishes that works of arts and collections are exempt from capitalization if these are: (a) held for public exhibition, education or research in furtherance of public service rather than financial gain; (b) protected, kept unencumbered, cared for, and preserved; and (c) subject to an organizational policy that requires the proceeds from sales of collections items to be used to acquire other items for collection.

This adoption was accounted by excluding from the accompanying statement of net position works of arts and collections amounting to \$6,366,411 and presenting those as a reduction of unrestricted net assets.

The Institute works of arts and collections consist of painting, sculptures and similar assets that are held generally at museums and these are not being capitalized since these are preserved and protected with cultural, aesthetic or historical value and generally have extraordinary long useful lives and would then be considered inexhaustible.

The Institute is engaged in the attained, promotion, enrichment and divulgating of the Puerto Rican cultural values and its activities are exclusive fir this purpose.

*New Accounting Statement Adopted* – Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position – In June 2011, GASB issued GASB 63, which requires proprietary funds, fiduciary funds and activities, and governmental- and business-type activities to report net position (not net assets), as well as deferred outflows of resources and deferred inflows of resources. GASB No. 63 is effective for financial statements for periods beginning December 15, 2011, with earlier implementation encouraged.

*Subsequent Events* – For purposes of these financial statements, subsequent events have been evaluated through September 19, 2012, which is the date the financial statements were available to be issued. There are no material subsequent events that require further disclosures in the Institute’s financial statements.

**3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

(a) *Budgetary Control* - The Institute is constitutionally required to submit to the Office of Management and Budget an annual balanced budget for the ensuing fiscal year. Section 7 of Article VI of the Constitution of Puerto Rico provides that “The appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for the said fiscal year, unless the imposition of taxes sufficient to cover the said appropriations is provided by law”.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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The annual budget, which is developed utilizing elements of program budgeting, includes an estimate of revenue and other resources for the ensuing fiscal year under: (i) laws existing at the time the budget are submitted.

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

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

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

**(b) Budget/GAAP Reconciliation** - The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity, timing, and basis differences in the excess (deficiency) of revenue and other financing sources over expenditures and other financing uses for the year ended June 30, 2010 is presented below for the general fund (expressed in thousands):

Excess of expenditures and other financing uses over revenues and other financing sources - budget basis \$3,523,485.

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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**4. CASH AND CASH EQUIVALENTS – CUSTODIAL CREDIT RISK DEPOSITS**

The Institute is authorized to deposit only in institutions approved by the PRTD, and such deposits should be kept in separate accounts in the name of the Institute. Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. The Institute’s policy regarding deposits requires for all opening of banks accounts to be approved by its Board of Directors.

Custodial credit risk is the risk that, in an event of a bank failure, the Institute’s deposits might 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 PRTD.

Although the Institute is not exposed to custodial credit risk, the following disclosure is made for reader’s convenience. The Institute had the following depository accounts in commercial banks. All deposits are carried at cost plus accrued interest:

Insured by FDIC	\$ 500,000
Bank balances:	
Cash in the bank held in the Institute's name	<u>17,294,745</u>
Total deposits	<u>\$ 17,794,745</u>

The securities pledged to the PRTD by the financial institution are sufficient to cover the Institute’s deposits.

The carrying amount of deposits at June 30, 2012 as shown in the statement of net assets follows:

	<u>Unassigned</u>	<u>Restricted</u>	<u>Total</u>
Cash and cash equivalent	\$ 1,251,050	\$ 18,878,753	\$ 20,129,803
Cash with fiscal agent	<u>118,235</u>	<u>( 324,075)</u>	<u>( 205,840)</u>
	<u>\$ 1,369,285</u>	<u>\$ 18,554,678</u>	<u>\$ 19,923,963</u>

**INSTITUTE OF PUERTO RICAN CULTURE**  
**(A Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

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**5. CAPITAL ASSETS**

The Institute's capital assets at June 30, 2012 were as follow:

<u>Capital Assets</u>	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Non-depreciable assets:				
Land	\$ 55,205	\$ -	\$ -	\$ 55,205
Historical and archeological patrimony and works of art	6,439,819	27,500	( 6,467,319)	-
Construction in progress	<u>2,977,473</u>	<u>1,052,169</u>	<u>( 1,985,254)</u>	<u>2,044,388</u>
	<u>9,472,497</u>	<u>1,079,669</u>	<u>( 8,452,573)</u>	<u>2,099,593</u>
Depreciable assets:				
Buildings	91,777,972	4,583,779	-	96,361,751
Building improvements	3,322,448	-	( 608,682)	2,713,766
Furniture, fixtures and equipment	3,574,440	173,242	( 151,296)	3,596,386
Computers and software	1,512,626	60,546	-	1,573,172
Vehicles	<u>596,558</u>	<u>81,900</u>	<u>-</u>	<u>678,458</u>
	<u>100,784,044</u>	<u>4,899,467</u>	<u>( 759,978)</u>	<u>104,923,533</u>
Less accumulated depreciation:				
Buildings	( 39,118,994)	( 4,726,523)	-	( 43,845,517)
Furniture, fixtures and equipment	( 3,154,654)	( 157,821)	805,486	( 2,506,989)
Computers and software	( 1,585,055)	( 43,650)	83,794	( 1,544,911)
Vehicles	<u>( 635,215)</u>	<u>( 6,618)</u>	<u>340,414</u>	<u>( 301,419)</u>
	<u>( 44,493,918)</u>	<u>( 4,934,612)</u>	<u>1,229,694</u>	<u>( 48,198,836)</u>
Net depreciable assets	<u>56,290,126</u>	<u>( 35,145)</u>	<u>469,716</u>	<u>56,724,697</u>
Capital assets, net	<u>\$ 65,762,623</u>	<u>\$ 1,044,524</u>	<u>\$( 7,982,857)</u>	<u>\$ 58,824,290</u>

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Depreciation expense was charged to functions/programs as follows:

<u>Program</u>	<u>Amount</u>
Administrative services	\$ 2,321,023
Plastic arts	112,308
Popular arts	74,871
Cultural Centers	149,744
Music	149,744
Theater	149,744
General Archive	149,744
Publications	74,871
General Library	74,871
Historic Patrimony	112,308
Archeology	74,871
Museums and Parks	<u>299,486</u>
Total depreciation expense	<u>\$ 3,743,585</u>

The Institute has active construction projects as of June 30, 2012. The total commitments for ongoing capital projects are composed of the following:

<u>Building</u>	<u>Amount</u>
Fortín San Gerónimo	\$ 624,698
Antiguo Asilo de Beneficiencia (main facilities of the Institute)	142,880
Convento Los Dominicos	102,955
Museo de Artes Populares	230,149
Casa Urrutia, Casa Blanca y complejo Museo	117,385
Juan Ponce de León	176,417
Casa Wiechers Villaronga	-
Casa Armstrong	49,847
Centro Ceremonial Indígena	514,170
Archivo General de Puerto Rico	-
Teatros Matienzo y Music Hall	<u>283,629</u>
Total	<u>\$ 2,242,130</u>

These commitments will be funded by advances from the credit facilities disclosed in Note 6.

**6. LINES OF CREDIT**

The Institute has three non-revolving lines of credit agreements to finance the commitments disclosed in Note 4. These credit facilities were granted by the Puerto Rico Government Development Bank. The Institute may borrow up to \$17,100,000, \$10,000,000, and \$9,000,000, respectively at a 7.00% annual rate.

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At June 30, 2012, lines of credit consisted of the following individual legislative resolutions:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Resolution #718, dated August 17, 2002, for the amount of \$10,000,000 due in annual installments until September 30, 2018	\$ 1,825,624	\$ 429,165	\$ 26,130	\$ 2,228,659
Resolution #1780, dated December 28, 2003, for the amount of \$9,000,000 due in annual installments until December 31, 2007	-	32,579	-	32,579
Resolution #2112, dated September 30, 2004, for the amount of \$17,100,000 due in annual installments until September 30, 2018	<u>1,971</u>	<u>255,262</u>	<u>2,981</u>	<u>254,252</u>
Total lines of credit	<u>\$ 1,827,595</u>	<u>\$ 717,006</u>	<u>\$ 29,111</u>	<u>\$ 2,515,490</u>

During the fiscal year ended June 30, 2012 the Central Government paid approximately \$29,111 of the outstanding balance on the Institute's lines of credit with the Puerto Rico Development Bank, which paid-off these obligations, plus some advances received thereafter. The Central Government also paid accrued interest as of June 30, 2012, amounting to approximately \$901,400. These transactions were disclosed as other sources and other uses of funds in these financial statements.

**7. COMPENSATED ABSENCES**

Compensated absences as of June 30, 2012 were as follow:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due within one year</u>
Vacations and licenses	\$ 863,711	\$ -	\$( 138,277)	\$ 725,434	\$ 57,380
Sick leave benefits	1,252,238	-	( 159,314)	1,092,924	92,501
Compensatory time	<u>45,602</u>	<u>-</u>	<u>( 38,249)</u>	<u>7,353</u>	<u>836</u>
	<u>\$ 2,161,551</u>	<u>\$ -</u>	<u>\$( 335,840)</u>	<u>\$ 1,825,711</u>	<u>\$ 150,717</u>

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**8. FUND BALANCES**

Fund balance is classified as non-spendable, restricted, committed, assigned and/or unassigned based primarily on the extent to which the Institute is bond to observe constraints imposed upon the use of the resources in the government funds. The constraints placed on the fund balance for the major governmental funds and all other governmental funds are as follows:

	<u>General Fund</u>	<u>Special Appropriation Fund</u>	<u>Other Governmental Funds</u>	<u>Capital Improvement Fund</u>	<u>Total Governmental Funds</u>
FUND BALANCES:					
Non-spendable:					
Inventory	\$ 1,899,734	\$ -	\$ -	\$ -	\$ 1,899,734
Restricted:					
Capital projects	-	3,620,216	2,596,188	8,122,764	14,339,168
Unassigned	<u>( 1,752,699)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>( 1,752,699)</u>
Total fund balances	<u>\$ 147,035</u>	<u>\$ 3,620,216</u>	<u>\$ 2,596,188</u>	<u>\$ 8,122,764</u>	<u>\$ 14,486,203</u>

**9. PENSION PLAN**

The Employee's Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS) is a cost-sharing multi-employer defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Institute under age 55 at the date of employment become members of the System as a condition for their employment.

The System provides retirement, death, and disability benefits pursuant to Act 447 approved on May 15, 1951, as amended, and became effective on January 1, 1952. 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 services. Benefits vest after ten years of plan participation. Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years for creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to an annual benefit payable monthly for life.

The amount of the annuity shall be 1.5% of the average compensation multiplied by the number-of-years of creditable service up to twenty years, plus 2% of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case will the annuity be less than \$200 per month. For those participant employees after March 31, 1990, the amount of the annuity is 1.5% of the compensation multiplied by the number of years for credited services. The annuity should not be less than \$2,400 in any case.

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Participants who have completed at least thirty years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive 65% of the average compensation or if they attained fifty-five (55) years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service.

No benefit is payable if the participant receives a refund of his accumulated contributions. On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, was enacted with the purpose of establishing a new pension program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, elected either to stay in the defined benefit plan or transfer to the new program. Persons joining on or after January 1, 2000, were only allowed to become members of System 2000. System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age will not be guaranteed by the Commonwealth. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the turn of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000.

The employer's contribution (9.275% of the employee's salary) will be used to fund the deficiency of the defined benefit plan. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

Act number 1 of February 16, 1990 made certain amendments applicable to new participants joining the System effective on April 1, 1990. Changes mainly consisted of an increase of the retirement age to 65 years, the elimination of the Merit Annuity and a reduction of the percentage for disability and death benefits.

The amount of total pension benefit obligation is based on standardized measurement established by generally accepted accounting principles that, with some exceptions, must be used by a public employee retirement system. The standardized measurement is the actuarial present value of credited projected benefits. This pension valuation method reflects the present value of estimated pension benefits that will be paid in future years as a result of employee services performed to date and is adjusted for the effects of projected salary increases. The significant actuarial assumptions used to determine the standardized measurement of the pension benefits obligation as of June 30, 2011 are summarized below:

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- Interest rate 6.40% a year
- Salary increases 3.0% a year
- Pre-retirement Mortality RP 2000 Employee Mortality Rates for males and females projected on a generational basis using Scale AA
- Disability Rates are based on the six-month elimination period rates in the 1987 Commissioners Group Disability Table. Rates of disability ceased to apply once a member is eligible for the 75% of Highest Salary maximum benefit.
- Retirement Rates of retirement vary by employment category, Act, and by age and years of Creditable Service.
- Marriage 50% of current active members, terminated members and retirees are assumed to be married at retirement with males 4 years older than females. 100% of current active members covered under Act 127 who die in service or become disabled are assumed to have qualified beneficiaries.
- Number of Employees Electing Higher Contributions 15% of retiring employees assumed to pay retroactive contributions at retirement.

The financial statements and required supplementary information for the pension plan are available at the administration office of the Employees' Retirement System of the Government of Puerto Rico, P.O. Box 42003 Minillas, San Juan, Puerto Rico 00940.

**10. VOLUNTARY TERMINATION BENEFITS**

On July 2, 2010, the Commonwealth enacted Act No. 70 to establish a program that provides benefits for early retirement or economic incentives for voluntary employment termination to eligible employees, as defined, including employees of the Corporation. Act No. 70 established that early retirement benefits will be provided to eligible employees that have completed between 15 to 29 years of credited service in the Retirement System and will consist of biweekly benefits ranging from 37.5% to 50% of each employee's salary, as defined. In this early retirement benefit program, the Corporation will make the employer

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contributions to the Retirement System and pay the corresponding pension until the employee complies with the requirements of age and 30 years of credited service in the Retirement System. Economic incentives are available to eligible employees who have less than 15 years of credited service in the Retirement System or who have at least 30 years of credited service in the Retirement System and the age for retirement or who have the age for retirement. Economic incentives will consist of a lump-sum payment ranging from one-month to six-month salary based on employment years. Additionally, eligible employees that choose to participate in the early retirement benefit program or that choose the economic incentive and have less than 15 years of credited service in the Retirement System are eligible to receive health plan coverage for up to 12 months in a health plan selected by management of the Corporation.

The financial impact resulting for the benefits granted to participants on this program was the recognition within the Institute's financial statements of a liability of \$2,393,292 in the statement of net position as of June 30, 2012 and a change of \$311,240 in the statement of activities for the year ended June 30, 2012 and 2011, respectively. At June 30, 2012 and 2011, unpaid long-term benefits granted on this program were discounted at 3.46%.

	<u>General Fund</u>	<u>Special Appropriation Fund</u>	<u>Other Governmental Funds</u>	<u>Capital Improvement Fund</u>	<u>Total Governmental Funds</u>
Total Expenses for Governmental Funds	\$ 18,029,030	\$ 4,245,920	\$ 2,142,944	\$ 3,433,025	\$ 27,850,919
Use of Past Years Funds	340,192	1,721,666	1,357,616	2,606,111	6,025,585
Provision for 2012 Voluntary Termination Benefits Expense	<u>2,627,798</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,627,798</u>
Use of Current Years Funds	15,061,040	2,524,254	785,328	826,914	19,197,536
Current Year Revenues	<u>14,595,100</u>	<u>2,909,549</u>	<u>836,362</u>	<u>946,359</u>	<u>19,287,370</u>
Excess of Revenues Over Expenditures	<u>\$( 465,940)</u>	<u>\$ 385,295</u>	<u>\$ 51,034</u>	<u>\$ 119,445</u>	<u>\$ 89,834</u>

The financial statements and required supplementary information for the pension plan are available at the administration office of the Employees' Retirement System of the Government of Puerto Rico, P.O. Box 42003 Minillas, San Juan, Puerto Rico 00940.

**11. CONTINGENCIES**

The Institute of Puerto Rican Culture receives funds under federal grant programs and such awards are to be expended in accordance with the provisions of each grant. Compliance with the grants is subject to audit by various government agencies, which may impose sanctions in the event of non-compliance. Management believes that it has complied with all aspects of grant provisions and the results of adjustments, if any, relating to such audits would not have a material impact on the programs. The Institute is a party to various legal claims resulting from its operations. As a component unit of the Commonwealth of Puerto Rico, all legal claims are handled by the Department of Justice and any liability resulting from these claims is covered by a separate fund established by the Commonwealth of Puerto Rico, if funds are not specifically available at the Institute for this purpose.

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As result of consultation with its in-house and external legal counsels, management believes that the ultimate outcome of any pending litigation will not have a significant impact to the accompanying financial statements.

The Central Government enacted Law # 7 (the "Law") of March 9, 2009, which declares a state of fiscal emergency and establishes a stabilization plan for all governmental entities of the Commonwealth, in an effort to manage the Central Government's structural operating deficit. Pursuant to the provision of the law, a separation plan applicable to certain employees was implemented in certain agencies, based on specific criteria established by the Law.

The separation plan applicable to the Institute was implemented during the period from May 2009 through June 2010. Severance payments related to the implementation were covered by separate budgetary assignments from the Central Government during such period. The Institute's projected payroll cost reduction over the trailing twelve months after full implementation ranges from \$3.5 to \$4.0 million. The Law provides for an appellate process that may be followed by employees after separation, if certain requirements are met. As of the date of issuance of the financial statements, the appeals filed are in their evaluation stage and the monetary impact, if any, will be covered by separate budgetary assignments from the Central Government for those employees that prevail, if any.