

**RUMS OF PUERTO RICO FUND**  
**(A fund of the Commonwealth of Puerto Rico)**  
*Basic Financial Statements as of and*  
*for the Year Ended June 30, 2011*  
*and Independent Auditors' Report*



**RUMS OF PUERTO RICO FUND**  
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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of the  
Puerto Rico Industrial Development Company:

We have audited the accompanying basic financial statements of the Rums of Puerto Rico Fund (the "Fund"), a Fund of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2011, as listed in the table of contents. These financial statements are the responsibility of the Fund'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.

As discussed in Note 1, the financial statements present only the Rums of Puerto Rico Fund, a Fund of the Commonwealth of Puerto Rico and do not purport to, and do not, present the financial position of the Commonwealth of Puerto Rico as of June 30, 2011, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and major fund information for the Rums of Puerto Rico as of June 30, 2011, and the respective changes in financial position of those activities for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated March 2, 2012 on our consideration of Fund's internal controls over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

To the Board of Directors of the  
Puerto Rico Industrial Development Company  
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The management's discussion and analysis on pages 3 through 6 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 inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

*Scherrer Hernández & Co.*

San Juan, Puerto Rico

March 2, 2012

Certified Public Accountants  
(of Puerto Rico)

License No. 53 expires December 1, 2012  
Stamp 2619587 of the P.R. Society of  
Certified Public Accountants has been  
affixed to the file copy of this report



**RUMS OF PUERTO RICO FUND**  
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**MANAGEMENTS' DISCUSSION AND ANALYSIS**  
**JUNE 30, 2011**

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**Overview of the Financial Statements**

Following is an overview and analysis of the financial activities of the Rums of Puerto Rico Fund (the "Fund") for the fiscal year ended June 30, 2011. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities and to identify any significant changes in financial position. It is intended to serve as an introduction to the Fund's financial statements, which are comprised of the basic financial statements and the notes to the financial statements. We encourage readers to consider the information presented here in conjunction with the financial statements taken as a whole.

**Government Wide Highlights**

The statement of net assets and governmental fund balance sheet present information on all of the Fund's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Fund is improving or deteriorating. Net assets increase when revenues exceed expenses. Increases to assets without a corresponding increase to liabilities, result in increased net assets, which also indicates an improved financial position.

The statement of activities and governmental fund revenues, expenditures, and changes in net assets present information showing how the Fund's net assets are reported as soon the underlying event occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

**Fund Highlights**

The Fund's financial statements provide more detailed information about the Fund's most current financial resources. Funds are accounting devices that the Fund uses to keep track of specific sources of funding and spending for particular purposes.

The Fund's basic service is included in a governmental fund, which is used to account for essentially the same functions reported as governmental activities in the government-wide statements. However, unlike the government-wide statements, the governmental funds are prepared using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this approach, the financial statements focus on near-term inflows and outflows of external resources, as well as on balances of expendable resources available at year end. Consequently, the governmental fund statements provide a detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Fund's programs. Because this information does encompass the additional long-term focus of the government-wide statements, there are no differences between the government-wide and fund statements.

The governmental fund statements focus on only one major fund. The Fund's major fund is the general fund (which accounts for the main operating activities of the Fund).

The notes to the basic financial statements provide additional information that is essential to the full understanding of the data provided in the basic financial statements.

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**MANAGEMENTS' DISCUSSION AND ANALYSIS**  
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**Financial Analysis of the Fund (In thousands):**

Net assets – The condensed net assets information of the Fund is presented below:

	2011	2010	Change	
			In dollars	Percentage
Assets	\$ 58,826	\$ 23,536	\$ 35,290	149.94%
Liabilities	\$ 2,607	\$ 3,750	\$ (1,143)	(30.48)%
Net assets:				
Nonspendable	4	-	4	100.00%
Restricted	56,215	19,786	36,429	184.12%
Total liabilities and net assets	\$ 58,826	\$ 23,536	\$ 35,290	149.94%

**Analysis of Net Assets at June 30, 2011 and 2010**

The Rums of Puerto Rico Fund (the Fund) was created through Law 143 of June 30, 1969 and is a fund of the Commonwealth of Puerto Rico, (the Commonwealth). It is administered by the Puerto Rico Industrial Development Company (PRIDCO), a component unit of the Commonwealth. The Fund was created to promote the sales of Puerto Rican Rums in the United States. As per the provisions of Title 26 of the United States Internal Revenue Code, all excises taxes collected on rum imported into the United States which has been produced in Puerto Rico shall be reimbursed to the Commonwealth. These monies are used by the Commonwealth for infrastructure projects and continuing marketing and promotion efforts of the Puerto Rican rums in the United States, among other uses related to the socioeconomic development of Puerto Rico.

Total assets increased by approximately \$35.3 million, or 149.94%, mostly due to a decrease in cash and cash equivalents of approximately \$6.4 million and an increase in investments of approximately \$41.5 million. In addition, there was an increase in advances made to PRIDCO of approximately \$94 thousand (\$7.4 million in 2011 versus \$7.3 in 2010).

Liabilities for 2011 amounted to approximately \$2.6 million, a decrease of approximately \$1.1 million, or 30.48%, mostly as a result of a decrease of approximately \$1.1 million in accounts payable.



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The condensed changes in net assets information is presented below:

	2011	2010	Change	
			In dollars	Percentage
Intergovernmental revenue	\$ 62,244	\$ 26,653	\$ 35,591	133.53%
Non-operating revenue:				
Interest income	170	159	11	6.92%
Other income	-	106	(106)	(100.00)%
Total revenue	62,414	26,918	35,496	131.87%
Expenses:				
Marketing	7,497	14,458	(6,961)	(48.15)%
Sponsorships and incentives	17,283	11,464	5,819	50.76%
General and administrative	1,201	1,457	(256)	(17.57)%
Total expenses	25,981	27,379	(1,398)	(5.11)%
Excess (deficiency) of revenues over expenses	36,433	(461)	36,894	(8003.04)%
Net assets, beginning of year	19,786	20,247	(461)	(2.28)%
Net assets, end of year	\$ 56,219	19,786	\$ 36,433	184.14%

**Analysis of Fiscal Year 2011 and 2010**

For the year ended June 30, 2011, operating income amounted to approximately \$62.4 million and consisted funds granted by the Legislature of the Commonwealth. This increase is mostly due to the stipulation of Act. No 178 of December 1, 2010, that required that the total investment that the Commonwealth of Puerto Rico is allowed to make in Puerto Rico promotional activities increased from 10% to 25%. Also, during the year ended June 30, 2011, interest income amounted to approximately \$170 thousand, a decrease of approximately \$11 thousand, mostly related with investments activities in certificates of deposits during the year ended June 30, 2011.

Marketing expenses related to the marketing and promotion efforts made in the United States mainland for the sale of rums manufactured in Puerto Rico decreased by approximately \$6.9 million, or 48.15%, mostly due to a decrease on various marketing contracts during the year ended June 30, 2011. Sponsorships and incentives awarded increased by approximately \$5.8 million, or 50.76%, mostly due funds granted to a local rum manufacturer during the year ended June 30, 2011, to improve its rums producing facilities located in Puerto Rico.

General and administrative expenses decreased by approximately \$256 thousand or 17.57%, mostly due to a decrease in rent expense of approximately \$210 thousand because PRIDCO management restructured rental charges by square feet in the office located in New York City to more accurately reflect actual usage.



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**Governmental fund**

The focus of the Fund's governmental fund is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Fund's financing requirements. For the fiscal year ended June 30, 2011, the governmental fund reported ending fund balance of approximately \$56.2 million, a net increase of approximately \$36.4 million.

**REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of the Fund's finances and to demonstrate the Fund's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Executive Director's Office, Puerto Rico Industrial Development Company, P.O. Box 362530, San Juan, Puerto Rico, 00936-2530.



**RUMS OF PUERTO RICO FUND**  
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**STATEMENT OF NET ASSETS AND GOVERNMENTAL FUND BALANCE SHEET**  
**JUNE 30, 2011**

	<b>General Fund Balance Sheet (In thousands)</b>	<b>Adjustments (In thousands)</b>	<b>Statement of Net Assets (In thousands)</b>
<b>ASSETS</b>			
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents in commercial banks	\$ 6,947	\$ -	\$ 6,947
Cash in governmental bank	1,999	-	1,999
Investments	41,551	-	41,551
Accrued interest	43	-	43
Due from PRIDCO	7,369	-	7,369
Due from Special Incentive Fund	900	-	900
Accounts Receivable Other	13	-	13
Prepaid expenses	4	-	4
Total assets	<u>\$ 58,826</u>	<u>\$ -</u>	<u>\$ 58,826</u>
<b>LIABILITIES AND FUND BALANCES/NET ASSETS</b>			
<b>CURRENT LIABILITIES -</b>			
Accounts payable	\$ 2,607	\$ -	\$ 2,607
Total liabilities	<u>2,607</u>	<u>-</u>	<u>2,607</u>
<b>FUND BALANCES/NET ASSETS:</b>			
<b>Fund balances:</b>			
Nonspendable	4	(4)	-
Restricted	56,215	(56,215)	-
Total fund balances	<u>56,219</u>	<u>(56,219)</u>	<u>-</u>
Total liabilities and fund balance	<u>\$ 58,826</u>		
<b>Net assets:</b>			
Nonspendable		4	4
Restricted		56,215	56,215
Total net assets		<u>\$ 56,219</u>	<u>\$ 56,219</u>



**RUMS OF PUERTO RICO FUND**  
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**STATEMENT OF ACTIVITIES AND GOVERNMENTAL FUND REVENUES,**  
**EXPENDITURES AND CHANGES IN NET ASSETS**  
**FOR THE YEAR ENDED JUNE 30, 2011**

	<b>General Fund (In thousands)</b>	<b>Adjustments (In thousands)</b>	<b>Statement of Activities (In thousands)</b>
<b>EXPENDITURES/EXPENSES:</b>			
Marketing	\$ 7,497	\$ -	\$ 7,497
Sponsorships and incentives	17,283	-	17,283
General and administrative	1,201	-	1,201
Total expenditures/expenses	<u>25,981</u>	<u>-</u>	<u>25,981</u>
<b>GENERAL REVENUES:</b>			
Intergovernmental revenue	62,244	-	62,244
Investment interest revenue	170	-	170
Total general revenues	<u>62,414</u>	<u>-</u>	<u>62,414</u>
<b>EXCESS OF REVENUES OVER EXPENDITURES/EXPENSES</b>	<u>36,433</u>	<u>(36,433)</u>	<u>-</u>
Change in fund balance/net assets	<u>-</u>	<u>36,433</u>	<u>36,433</u>
<b>FUND BALANCE/NET ASSETS, beginning of the year</b>	<u>19,786</u>	<u>-</u>	<u>19,786</u>
<b>FUND BALANCE/NET ASSETS, end of the year</b>	<u>\$ 56,219</u>	<u>\$ -</u>	<u>\$ 56,219</u>



**RUMS OF PUERTO RICO FUND**  
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**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
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**1. REPORTING ENTITY**

The Rums of Puerto Rico (the Fund), was created through Law 143 of June 30, 1969, and is a Fund of the Commonwealth of Puerto Rico (the Commonwealth). It is administered by the Puerto Rico Industrial Development Company (PRIDCO), which is a component unit of the Commonwealth.

The Fund was created to promote the sales of Puerto Rican Rums in the United States. As per the provisions of title 26 of the United States Internal Revenue Code, all excises taxes collected on rum imported into the United States which has been produced in Puerto Rico shall be covered into the treasuries of Puerto Rico. These monies will be used by the Government of Puerto Rico for infrastructure projects and marketing and promotion efforts of the Puerto Rican Rums in the United States, among other uses related to the socioeconomic development of Puerto Rico.

The source of funding is provided by transfers from the Department of Treasury of the Commonwealth of Puerto Rico.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

*Government Wide and Fund Financial Statements* – The government-wide financial statements report information on all of the activities of the Fund as a whole. The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are specifically associated with a function, which is to provide industrial incentives or grants. Program revenues include (1) non-exchange revenue (legislative appropriations) and (2) interest income from investments.

The fund financial statements provide information about the governmental fund, which is the only fund category.

The Statement of Net Assets presents the Fund's assets and liabilities, with the difference reported as net assets. Net assets are reported as restricted net assets. Restricted net assets present amounts that are restricted to specific purposes externally imposed by creditors or imposed by law. The Fund's restricted fund balance arise from special resolutions of the Government of the Commonwealth of Puerto Rico.

*Measurement Focus, Basis of Accounting, and Financial Statements Presentation* – Basis of accounting refers to when the Fund recognizes revenue and expenditures/expenses and the related assets and liabilities and reports them in the financial statements. The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Incentives are recognized as expenditures as soon as all eligibility requirements imposed by the provider have been met.



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The governmental fund follows the modified accrual basis of accounting. Under this basis of accounting, revenues are recorded in the accounting period in which they become susceptible to accrual, that is, when they become both measurable and available. Available is defined as expected to be collected within the current period or soon enough thereafter to be used to pay liabilities of the current period. For this purpose, the Fund considers revenue to be available if they are collected within 60 days of the end of the current fiscal year-end. Expenditures and related liabilities are generally recorded in the accounting period in which the liability is incurred.

**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.

**Prepaid Expenses** – The portion of fund balance that is not an available resource because it represents the year end balance of prepaid expenses, which are not spendable resources.

**Restricted Fund Balance** – amounts that are restricted to specific purposes externally imposed by creditors or imposed by law. The Fund's restricted fund balance arise from special resolutions of the Government of the Commonwealth of Puerto Rico.

**Committed Fund Balance** – amounts that can be used only for the 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 Fund for specific purposes but do not meet the criteria to be classified as restricted or committed. In the General Fund, assigned amounts represent intended uses established by the Board or Fund 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. These fund balances are available for any purpose and management will determine how to spend it.

The Fund applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amounts 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 Fund does not have a formal minimum fund balance policy.



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*Use of Estimates in the Preparation of Financial Statements* – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities 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 Fund maintains cash on deposit with high rated financial institutions and with the Puerto Rico Treasury Department. 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 Government Development Bank for Puerto Rico (GDB) and Economic Development Bank of Puerto Rico (EDB), component units of the Commonwealth are exempt from the collateralization requirement and represent a custodial credit risk, since in case of bankruptcy of the bank, the entity would not recover its deposits. At June 30, 2011, approximately \$2 million and \$5 million, respectively, of the Fund's cash and cash equivalents and investments balances were exposed to custodial credit risk, since represented deposits with the GDB and EDB. Custodial credit risk is the risk that, in an event of a bank failure, the Fund's deposits might not be recovered.

*Cash Equivalents* – The Fund considers all highly liquid investments with original maturity of three months or less to be cash equivalents. At June 30, 2011, cash equivalents amounted to approximately \$3.9 million, and represent two time deposits with one financial institution. One of the time deposits amounted to approximately \$1.9 million and bears interest at 0.75%. The other time deposit amounted to approximately \$2 million and bears interest at 0.70%.

*Budgetary Accounting* – The Fund is not required to submit a budget for approval by the Legislature of the Commonwealth; consequently, no formal budgetary accounting procedures are followed.

*Subsequent Events* – The Fund has evaluated the impact of subsequent events through March 2, 2012, which is the date that these financial statements were available to be issued.



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**3. INVESTMENTS**

As of June 30, 2011, investments consisted in certificates of deposits held with various commercial banks and governmental banks as follows:

Face Amount (in thousands)	Settlement Date	Maturity Date	Interest Rate
\$ 4,525	March 15, 2011	July 13, 2011	0.90%
5,005	May 3, 2011	August 9, 2011	1.15%
3,511	April 26, 2011	August 24, 2011	0.70%
5,000	May 5, 2011	September 6, 2011	0.51%
4,000	May 12, 2011	September 22, 2011	1.15%
5,010	June 7, 2011	September 26, 2011	1.10%
14,500	June 28, 2011	January 17, 2012	1.20%
<u>\$ 41,551</u>			

Pursuant to the Investment Guidelines for the Commonwealth adopted by GDB, the Fund may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper and banker's acceptance.

**4. DUE FROM PRIDCO AND SPECIAL INCENTIVE FUND**

As of June 30, 2011, amounts due from PRIDCO and due from the Special Incentive Fund amounted to approximately \$7.4 million and \$900 thousand, respectively, and consist of operating advances with no formal repayment and bearing no interest.

**5. COMMITMENTS**

PRIDCO leases office in New York City under an operating lease with a third party expiring in the year 2022. Said office space is shared between PRIDCO, GDB, other governmental agencies, and the Fund, aiming towards the presence of the Commonwealth of Puerto Rico in one of the most important cities of the world. PRIDCO charges rent back to the previously mentioned governmental agencies based on space occupancy allocation.



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Future annual minimum lease payments under the operating lease agreement pertaining to the Fund are as follows (in thousands):

<b>Year Ending</b>	
<b>June 30,</b>	<b>Amount</b>
2012	\$ 137
2013	140
2014	144
2015	144
Thereafter	1,113
	<u>\$ 1,678</u>

Rent expense under such lease amounted to approximately \$148 thousand for the year ended June 30, 2011.

