



**PUERTO RICO SYSTEM OF ANNUITIES
AND PENSIONS FOR TEACHERS—
“TRS LEGACY TRUST”**

(A Component Unit of the Commonwealth of Puerto Rico)

Basic Financial Statements and
Required Supplementary Information

June 30, 2019

(With Independent Auditors' Report Thereon)

**PUERTO RICO SYSTEM OF ANNUITIES AND PENSIONS FOR TEACHERS—
“TRS LEGACY TRUST”**

(A Component Unit of the Commonwealth of Puerto Rico)

June 30, 2019

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Independent Auditors' Report

The Retirement Board of
the Government of Puerto Rico
Puerto Rico System of Annuities
and Pensions for Teachers – "TRS Legacy Trust"

We have audited the accompanying financial statements of the governmental activities and the general fund of the Puerto Rico System of Annuities and Pensions for Teachers – "TRS Legacy Trust" (the Trust), a component unit of the Commonwealth of Puerto Rico (the Commonwealth), as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Trust's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express opinions 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinions, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, and the general fund of the Puerto Rico System of Annuities and Pensions for Teachers – "TRS Legacy Trust", as of June 30, 2019, and the respective changes in financial position for the year then ended, in accordance with U.S. generally accepted accounting principles.



Emphasis of Matter

Uncertainty about the Ability to Continue as a Going Concern

The accompanying financial statements have been prepared assuming that the Trust will continue as a going concern. As discussed in note 3 to the basic financial statements, 1) the Trust is economically dependent on the Commonwealth, which filed a petition for relief under Title III of the Puerto Rico Oversight Management and Economic Stability Act (PROMESA) in the United States District Court for the District of Puerto Rico; 2) the Trust's operations are limited to maintaining custody of the unliquidated assets (excluding the building and building improvements) that are pending to be transferred to the Commonwealth, rental activities and administrative services on behalf of the Commonwealth as a result of Act 106-2017; and 3) management has stated that substantial doubt exists about the Trust's ability to continue as a going concern. Management's evaluation of the events and conditions and management's plans regarding these matters are also described in note 3. The basic financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinions are not modified with respect to this matter.

Other Matter

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3–8 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 of 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.

KPMG LLP

San Juan, Puerto Rico
December 16, 2021

Stamp No. E470403 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

**PUERTO RICO SYSTEM OF ANNUITIES AND PENSIONS FOR TEACHERS—
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Management’s Discussion and Analysis (Unaudited)

June 30, 2019

Introduction

The following management’s discussion and analysis (MD&A) of the financial performance of the Puerto Rico System of Annuities and Pensions for Teachers— “TRS Legacy Trust” (the “Trust”) provides an overview of its activities for the fiscal year ended June 30, 2019. This MD&A is intended to be read in conjunction with the Trust’s financial statements.

Prior to July 1, 2017, the Trust was a pension trust fund created in 1951 by the Legislative Assembly (the Legislature) of the Commonwealth of Puerto Rico (the Commonwealth) to provide pension and other benefits mainly to retired teachers of the Puerto Rico Department of Education (the Department of Education), an agency of the Commonwealth, and the employees of the Trust.

On August 23, 2017, the Governor of Puerto Rico signed into law Act No. 106 of 2017, known as the *Law to Guarantee the Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants* (Act 106-2017), which transformed the Trust effective as of July 1, 2017 by, among other things, (i) replacing the Trust’s Board of Trustees and the governing boards for the Employees’ Retirement System of the Government of the Commonwealth of Puerto Rico (ERS) and the Retirement System for the Judiciary of the Commonwealth of Puerto Rico (JRS), and collectively with the Trust and ERS, the Retirement Systems) with a single Retirement Board of the Commonwealth of Puerto Rico (the Retirement Board); and (ii) implementing a pay-as-you-go (PayGo) system in which direct payments to pension beneficiaries are made by the Commonwealth and reimbursed by applicable government employers (excluding the Trust) through an applicable PayGo fee. The Trust’s assets are being liquidated, and programs and activities were terminated or suspended. Refer to Notes 1 and 4 to the basic financial statements for further information regarding Act 106-2017.

Since Act 106-2017 transferred the primarily responsibility of the payment of the pensions to the Commonwealth and instructed the Trust to liquidate its assets (excluding the building and building improvements) to fund the pension benefits, it is determined that the Trust’s assets and activities should not be reported as a pension trust fund. Instead, since fiscal year 2018, the Trust will be reported as a blended component unit in the Commonwealth’s financial statements. Accordingly, the financial activities of the Trust consist only of governmental activities. For its reporting purposes, the Trust has combined the General Fund and government-wide financial statements using a columnar format that reconciles individual line items of fund financial data to government-wide data in a separate column. As of June 30, 2019, the Trust has not completed the transfer of the net assets to the Commonwealth and it is managing the remaining assets as the custodian. Accordingly, the Trust’s operations during the year ended June 30, 2019 were subsidized with revenues from the Commonwealth through the utilization of the assets on their custody. The most significant changes in the presentation of the basic financial statements is that current year revenues and expenses (expenditures) are limited to the administration of the assets under its custody. Revenues and expenses (expenditures), associated to the assets under the Trust’s custody are presented as part of the change in Due to Commonwealth.

Both before and after the enactment of Act 106-2017, the Trust continues to administer data of postemployment healthcare benefits provided by the Commonwealth to retired teachers of the Department of Education and retired employees of the Trust.

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June 30, 2019

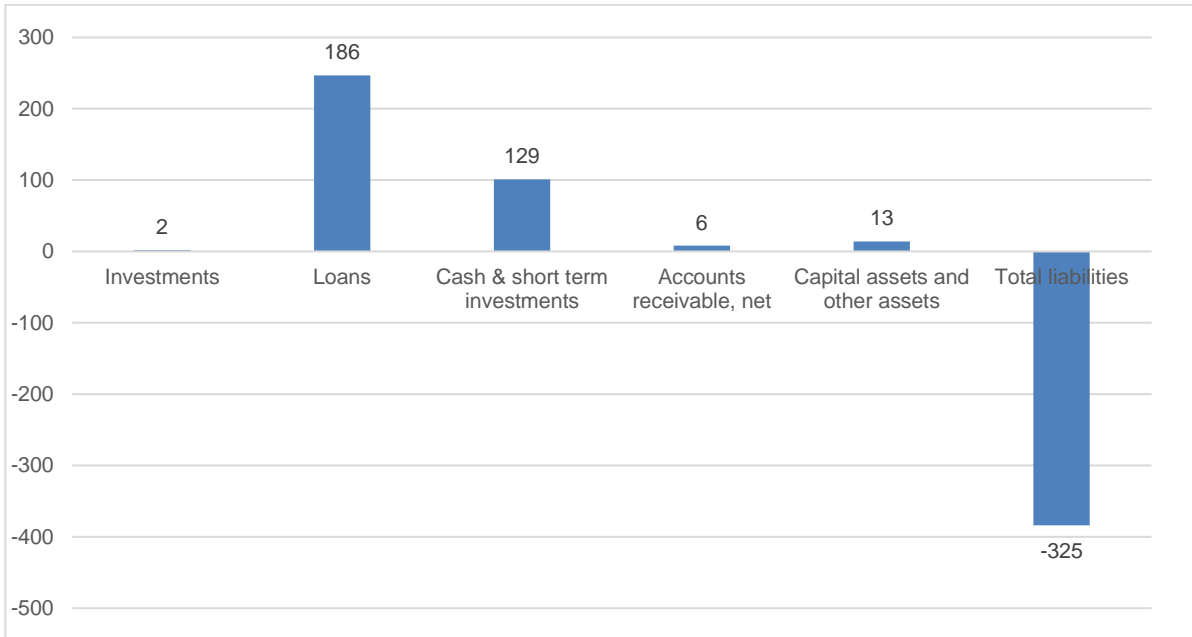
Financial Highlights

During fiscal year 2019, the Trust’s net position decreased by approximately \$723 thousand from \$12 million as of June 30, 2018 to \$11.3 million as of June 30, 2019. The decrease was mainly attributable to building depreciation expense during fiscal year ended on June 30, 2019.

As of June 30, 2019, the Trust’s total assets, including Commonwealth’s assets under the custody of the Trust, consisted of the following:

- \$11.3 million in capital assets
- 325 million in Commonwealth’s assets under the custody of the Trust, which includes:
 - \$129 million in cash and cash equivalents
 - \$2 million in investments;
 - \$186 million in loans to plan members, net
 - \$6 million in accounts receivable, net
 - \$1.3 million in net of capital assets and other assets.

The Trust net position is presented in the following chart (in millions):



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- Investments under custody of the Trust (excluding loans to participants) at June 30, 2019 amounted to approximately \$2 million, similar to the investments balance as of June 30, 2018.
- Administrative expenses for the fiscal year ended June 30, 2019 amounted to approximately \$21 million, as compared to approximately \$15 million for the year ended June 30, 2018.
- The Trust recognized approximately \$19.5 million in revenues from the Commonwealth in the fiscal year ended June 30, 2019, to cover part of the administrative expenses, as compared to approximately \$13 million in fiscal year ended June 30, 2018.

Overview of the Basic Financial Statements

The Trust’s basic financial statements comprise three components: 1) government-wide financial statements on all of the activities of the Trust, 2) fund financial statements, and 3) notes to basic financial statements.

- *Government-wide Financial Statements* – The government-wide financial statements are designed to provide readers with a broad overview of the Trust’s financial position, in a manner similar to a private-sector business. 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 cash flows.

The statement of net position presents information of the Trust’s assets and deferred outflows of resources, and liabilities and deferred inflow of resources, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Trust is improving or deteriorating as a result of the year’s operations.

The statement of activities presents information showing how the Trust’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, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

- *Fund Financial Statements* – For accounting purposes, 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 Governmental Fund Financial Statement focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the Trust’s near term financing requirements. Because the focus of governmental fund is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental fund 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 financial decisions related to the Trust’s governmental activities. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and change in fund balance provide a reconciliation to facilitate this comparison between governmental fund and governmental activities.

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- *Notes to the Basic Financial Statements* – provide additional information that is essential for an understanding of the data provided in the financial statements. The notes present information about the Trust’s accounting policies, significant account balances and activities, material risks, obligations, contingencies, and subsequent events, if any.

Financial Analysis of the Governmental Activities

The following schedules present comparative summary of the Trust’s net position and changes in net position for fiscal years 2019 and 2018:

Condensed Summary of Net Position (in thousands):

	2019	2018	Change	
			Amount	Percentage
Assets:				
Trust’s assets	\$ 11,295	\$ 12,018	\$ (723)	-6%
Assets under custody of the Trust	<u>324,670</u>	<u>372,169</u>	<u>(47,499)</u>	-13%
Total assets	<u>335,965</u>	<u>384,187</u>	<u>(48,222)</u>	-13%
Liabilities and Net Position:				
Other liabilities	2,045	1,707	338	20%
Due to Commonwealth	317,917	353,060	(35,143)	-10%
Due to Hybrid Program Members	699	12,408	(11,709)	-94%
Long term liabilities	<u>4,009</u>	<u>4,994</u>	<u>(985)</u>	-20%
Total liabilities	<u>324,670</u>	<u>372,169</u>	<u>(47,499)</u>	-13%
Net Position				
Net investment in capital assets	11,295	12,018	(723)	-6%
Unrestricted deficit	-	-	-	0%
Total net position	<u>\$ 11,295</u>	<u>\$ 12,018</u>	<u>\$ (723)</u>	-6%

The decrease in total assets is mostly due to the use of existing cash for the payment on behalf of the Commonwealth of expenses like refunds of contributions, death benefits payments, and administrative expenses. The decrease in due to Commonwealth is mostly related to the use of Trust assets, to cover operational and administrative payments on behalf of the Commonwealth. Decrease in due to Hybrid Program Members is explained by the transfer of \$12 million to a temporary Trust for the new Defined Contribution Program under Act 106-2017. The decrease in long-term liabilities is mainly due to a decrease in accrued expenses related to reduced salaries payable.

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Management’s Discussion and Analysis (Unaudited)

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Condensed Summary of Statement of Activities (in thousands):

	<u>2019</u>	<u>2018</u>	<u>Amount</u>	<u>Percentage</u>
Revenues:				
Revenues from Commonwealth	19,563	13,111	6,452	49%
Other income	<u>358</u>	<u>1,001</u>	<u>(643)</u>	-64%
Total revenues	<u>19,921</u>	<u>14,112</u>	<u>5,809</u>	41%
Expenditures/expenses:				
General and administrative expenses	<u>20,644</u>	<u>14,728</u>	<u>5,916</u>	40%
Total expenses	20,644	14,728	5,916	40%
Special items:				
Loss on implementation of Act 106-2017	-	491,923	504,754	100%
Distribution to hybrid program members	<u>-</u>	<u>12,408</u>	<u>12,408</u>	100%
Changes in net position	(723)	(504,947)	(517,269)	102%
Fund balance/net position				
Beginning of year	<u>12,018</u>	<u>516,965</u>	<u>(504,947)</u>	-98%
End of year	<u>\$ 11,295</u>	<u>\$ 12,018</u>	<u>\$ (723)</u>	-6%

Increase in general and administrative expenses is mostly related to the adoption during fiscal year 2019 of a voluntary transition program that granted eligible employees certain increased benefits for their resignation or retirement.

Financial Analysis of the Trust

The Trust’s net position as of June 30, 2019, amounted to approximately \$11 million, a decrease of approximately \$723 thousand from approximately \$12 million at June 30, 2018. Said decrease is attributed to the depreciation expense incurred on the building during fiscal year 2019.

Investment Portfolio

As of June 30, 2019, the Trust had some exposure to limited partnerships of private equity investments valued at approximately \$2 million, not a significant change in value with respect of fiscal year 2018.

Loans Portfolio

As of June 30, 2019, the Trust held \$186 million in loans to participants. Loan balances as of June 30, 2019 were approximately \$61 million lower than the prior fiscal year ended June 30, 2018 mainly as a result of principal repayments and the suspension of originations in prior year.

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June 30, 2019

Capital Assets

Capital assets of the Trust as of June 30, 2019 and 2018 amounted to approximately \$11 and \$12 million, respectively, net of accumulated depreciation and amortization. Also as of June 30, 2019, the Trust held in custody on behalf of the Commonwealth \$1.3 million in capital assets, net of accumulated depreciation. Capital assets include building and improvements, furniture, equipment and software. Building and improvements consist of the facilities in which the Trust has its operations. Refer to Note 6 of the basic financial statements for further information regarding the Trust’s net capital assets.

Management’s Conclusion on Going Concern

The Trust’s management believes that as of June 30, 2019 there is substantial doubt as to the ability of the Trust to continue as a going concern in accordance with the Governmental Accounting Standard Board (GASB) Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in AICPA Statements on Audit Standards*. After Act 106-2017, the Trust is economically dependent of the Commonwealth, which is facing significant risks and uncertainties, including liquidity risk.

The Commonwealth has incurred recurring deficits, has a negative financial condition, has experienced further deterioration of its economic condition, has not been able to access the credit markets, and has stated that substantial doubt exists about the Commonwealth’s ability to continue as a going concern. Additionally, the Commonwealth is currently restructuring its obligations in an orderly fashion under Title III of the U.S. Congress Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), which was signed by the U.S. President on June 30, 2016.

Detailed information about the Commonwealth’s conditions and events that raise doubt about its ability to continue as a going concern and the corresponding remediation plans are disclosed in the notes of the Commonwealth’s 2018 audited basic financial statements. Also, refer to Note 3 to the basic financial statements for additional management’s considerations and remediation plan.

Request for Information

The financial report is designed to provide a general overview of the Trust’s financial status, comply with related laws and regulations, and demonstrate commitment to public accountability. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Puerto Rico System of Annuities and Pensions for Teachers, Capital Center Building, #235 Arterial Hostos Ave., North Tower, 8th floor, Hato Rey, P.R. 00919-1879.

**PUERTO RICO SYSTEM OF ANNUITIES AND PENSIONS FOR TEACHERS—
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(A Component Unit of the Commonwealth of Puerto Rico)

General Fund Balance Sheet and Statement of Net Position

June 30, 2019

(in thousands)

Assets	General fund balance sheet	Adjustments	Statement of net position
	<u> </u>	<u> </u>	<u> </u>
Commonwealth's assets in custody of the Trust:			
Cash and cash equivalents:			
Deposits at Puerto Rico commercial banks	\$ 108,999	—	108,999
Money market funds	19,998	—	19,998
Accrued interest and dividends receivable	38	—	38
Other, net	6,094	—	6,094
Investments in limited partnerships	2,133	—	2,133
Loans to plan members, net	185,946	—	185,946
Capital assets, net	—	1,297	1,297
Other assets	—	165	165
Capital assets, net	<u>—</u>	<u>11,295</u>	<u>11,295</u>
Total assets	<u>\$ 323,208</u>	<u>12,757</u>	<u>335,965</u>
Liabilities			
Accounts payable	\$ 1,007	—	1,007
Accrued expenses	1,038	—	1,038
Due to Commonwealth	320,464	(2,547)	317,917
Other long-term liabilities, due within one year	—	1,069	1,069
Due to Hybrid Program Members	699	—	699
Other long-term liabilities, due after one year	<u>—</u>	<u>2,940</u>	<u>2,940</u>
Total liabilities	<u>323,208</u>	<u>1,462</u>	<u>324,670</u>
Fund balance/net position:			
Fund balance — Restricted	<u>—</u>	<u>—</u>	<u>—</u>
Total liabilities and fund balance	<u>\$ 323,208</u>		
Net position:			
Net investment in capital assets		\$ 11,295	11,295
Unrestricted deficit		<u>—</u>	<u>—</u>
		<u>\$ 11,295</u>	<u>11,295</u>

The accompanying notes are an integral part of the financial statements.

**PUERTO RICO SYSTEM OF ANNUITIES AND PENSIONS FOR TEACHERS—
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(A Component Unit of the Commonwealth of Puerto Rico)

General Fund Statement of Revenues, Expenditures, and Changes in Fund Balance and Statement of Activities
Year ended June 30, 2019

(in thousands)

	General fund revenue, expenditures, and changes in Fund Balance	Adjustments	Statement of activities
Revenues:			
Revenues from Commonwealth	\$ 20,548	(985)	19,563
Other income	358	—	358
Total revenues	<u>20,906</u>	<u>(985)</u>	<u>19,921</u>
Expenditures/expenses:			
General and administrative expenses	<u>20,906</u>	<u>(262)</u>	<u>20,644</u>
Total expenditures/expenses	<u>\$ 20,906</u>	<u>(262)</u>	<u>20,644</u>
Changes in fund balance/net position		(723)	(723)
Fund balance/net position:			
Beginning of year	\$ —	12,018	12,018
End of year	<u>\$ —</u>	<u>11,295</u>	<u>11,295</u>

The accompanying notes are an integral part of the financial statements.

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Notes to Basic Financial Statements

June 30, 2019

(1) Organization

Prior to July 1, 2017, the Puerto Rico System of Annuities and Pensions for Teachers— TRS Legacy Trust (the Trust) was a pension trust fund created by the Legislature of Puerto Rico in 1951 to provide pension and other benefits mainly to retired teachers of the Department of Education, an agency of the Commonwealth of Puerto Rico (the Commonwealth), and the employees of the Trust. After the enactment of Act No. 106 of 2017, known as the *Law to Guarantee the Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants (Act 106-2017)*, the Trust's operations are limited to maintaining custody of the unliquidated assets (excluding the building and building improvements) that are pending to be transferred to the Commonwealth's General Fund, rental activities and administrative services on behalf of the Commonwealth. The Trust also administers, on behalf of the Commonwealth, the data related to postemployment healthcare benefits provided by the Commonwealth to retired teachers of the Department of Education and retired employees of the Trust.

The Commonwealth's General Fund became the only recipient of the assets maintained under the custody of the Trust. The product of the liquidation of said assets is designated by law to be used by the General Fund to cover pension benefits that used to be administered by the Trust. Therefore, the Trust's assets and activities should not be reported as a pension trust fiduciary fund. Instead, starting in fiscal year 2018, the Trust is reported as part of the blended component units in the Commonwealth's financial statements. Accordingly, the financial activities of the Trust consist only of governmental activities. For its reporting purposes, the Trust has combined the General Fund and government-wide financial statements using a columnar format that reconciles individual line items of fund financial data to government-wide data in a separate column.

The Retirement Board is responsible for governing the Trust, ERS and the Retirement System for the Judiciary of the Commonwealth of Puerto Rico (JRS). The Retirement Board is comprised of 13 members, including (i) six ex officio members (or their designees): (1) the Executive Director of the Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA), (2) the Secretary of Treasury of the Commonwealth, (3) the Director of the Office of Management and Budget, (4) the Director of the Office for the Administration and Transformation of Human Resources of the Government of Puerto Rico, (5) the President of the Federation of Mayors, and (6) the President of the Association of Mayors; (ii) three Governor-appointed representatives of the teachers of the Department of Education, the public corporations, and the Judiciary Branch; and (iii) four additional Governor-appointed members as representatives of the public interest.

(2) Summary of Significant Accounting Policies

The accounting and reporting policies of the Trust conform to accounting principles generally accepted in the United States of America (GAAP), as applicable to governmental entities. The Trust follows governmental accounting standards board (GASB) standards in the preparation of its basic financial statements.

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Notes to Basic Financial Statements

June 30, 2019

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

(a) Basis of Presentation

The financial activities of the Trust consist only of governmental activities. For its reporting purposes, the Trust has combined the General Fund and government-wide financial statements using a columnar format that reconciles individual line items of fund financial data to government-wide data in a separate column. A brief description of the Trust's government-wide and fund financial statements is as follows:

- (i) *Government-wide Financial Statements:* The government-wide statement of net position and statement of activities report the overall financial activity of the Trust.

The statement of activities demonstrates the degree to which the direct expenses of a given function (i.e., general government) are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. The Trust's sources of revenues include rental income and revenue from the Commonwealth for the custody and administration services performed by the Trust.

- (ii) *Fund Financial Statements:* The fund financial statements provide information about the Trust's General Fund. The General Fund accounts for all financial resources of the Trust.

(b) Basis of accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

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 when a liability is incurred, regardless of the timing of related cash flows.

Fund Financial Statements: The General Fund, as a governmental fund, is reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when the liability is incurred, as under accrual accounting. However, claims and judgments, and compensated absences are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds.

(c) Use of Estimates

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

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June 30, 2019

(d) Cash and Cash Equivalents

Cash and cash equivalents in custody of the Trust on behalf of the Commonwealth or the Hybrid Program Members consist of deposits with commercial banks, and money market funds, which are sufficiently liquid to permit withdrawal of cash at any time without prior notice or penalty.

(e) Investments

Investments are reported at their Net Asset Value (“NAV”). The NAV of each fund includes the market value of the investments in the fund plus any receivables, payables, and accrued fund expenses.

(f) Loans to Plan Members

Mortgages, personal and cultural trip loans to plan members under custody of the Trust are stated at their outstanding principal balance net of allowance for uncollectible amounts. Loans to plan members are collected through payroll withholdings and secured by mortgage deeds, plan members’ contributions, and any unrestricted amount remaining in the escrow funds. Act 106-2017 suspended the issuance of new loans effectively August 23, 2017. The maximum amounts that were loaned to plan members for mortgage and cultural trip loans were \$125,000 and \$5,000, respectively. The maximum amount of personal loans that was granted to participating employees was up to 85% of their accumulated contributions, but not more than \$5,000.

The Commonwealth, through the Trust, provides life insurance that guarantees the payment of the outstanding principal balance of mortgage, personal and cultural trip loans in case of death of a plan member, if the member complies with the agreement conditions. This coverage is paid in its entirety by the plan members either at origination of the loan or as part of the repayment of the loan, depending on the agreement condition. The guarantee insurance reserve for life insurance on loans to plan members is revised by the Trust each year and adjusted accordingly as part of the Trust’s custodial functions related to loans to plan members. This reserve is adjusted each year based on the annual higher claim amount of a five-year period increased by a management determined percentage.

(g) Capital Assets

Capital assets of the Trust include building and building improvements. Capital assets held on behalf of the Commonwealth are composed of equipment, furniture, fixtures and vehicles. Capital assets are defined as assets, which have an initial individual cost of \$500 or more at the date of acquisition and have a useful life of four or more years. Capital assets are recorded at historical cost or at estimated historical cost if actual historical cost is not available. Donated capital assets are recorded at their estimated fair value at the time of donation.

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June 30, 2019

Capital assets are depreciated on the straight-line method over the assets' estimated useful lives. The estimated useful lives of capital assets are as follows:

	Years
Building	40
Building improvements	10
Equipment, furniture, fixtures, and vehicles	4–10

(h) Termination Benefits

The Trust accounts for termination benefits in accordance with GASB Statement No. 47, *Accounting for Termination Benefits*. Pursuant to the provisions of GASB Statement No. 47, the Trust, as an employer, should recognize a liability and expense for voluntary termination benefits (e.g., early retirement incentives) when the offer is accepted, and the amount can be estimated. A liability and expense for involuntary termination benefits (e.g., severance 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.

(i) Fund Balance / Net Position

(a) Fund Balance

The fund balance for the General Fund is reported in classifications based on the extent to which the Trust is bound to honor constraints on the specific purposes for which amounts in the fund can be spent.

- Fund balance is reported as nonspendable when the resources cannot be spent because they are either in a nonspendable form or legally or contractually required to be maintained intact. There was no nonspendable fund balance as of June 30, 2019.
- Fund balance is reported as restricted when the constraints placed on the use of resources are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments; or imposed by law through constitutional provision or by enabling legislation. There was no restricted Fund Balance as of June 30, 2019.
- The Trust's highest decision-making level of authority rests with the Retirement Board. Fund balance is reported as committed when the Board passes a resolution that places specified constraints on how resources may be used. The Retirement Board can modify or rescind a commitment of resources through passage of a new resolution. There was no committed fund balance as of June 30, 2019.
- Resources that are constrained by the government's intent to use them for a specific purpose but are neither restricted nor committed, are reported as assigned fund balance. Intent may be expressed by the Retirement Board. There was no assigned fund balance as of June 30, 2019.

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- Unassigned fund balance represents fund balance that has not been restricted, committed, or assigned and may be utilized by the Trust for any purpose.

(b) Net Position

Net position represents the difference between assets and liabilities in the government-wide financial statements. Net position is displayed in the following components:

- Net investment in capital assets – This consists of capital assets, less accumulated depreciation and amortization.
- Restricted – This consists of net position that is legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, generally it is the Trust’s policy to use restricted resources first, then unrestricted resources when they are needed. There was no restricted net position at June 30, 2019.
- Unrestricted – This consists of net position that does not meet the definition of restricted or net investment in capital assets.

The following is a reconciliation between the General Fund balance sheet and the statement of net position at June 30, 2019 (in thousands):

Fund balance	\$	—
Add capital assets, net of accumulated depreciation, and repossessed classified as other assets as they are not financial resources and therefore are not reported in the general fund		12,757
Less due to Commonwealth for capital assets and other assets held in custody		<u>(1,462)</u>
Net position	\$	<u>11,295</u>

The following is a reconciliation between the excess of expenditures over revenues and the statement of activities at June 30, 2019 (in thousands):

Revenues related to capital assets as reimbursed by the Commonwealth	\$	(985)
Add expenditures related to capital assets reported on Government-wide financial statements		<u>262</u>
Change in net position	\$	<u>(723)</u>

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(j) Recently Issued Accounting Pronouncements

The following new accounting standards have been issued but are not yet effective during the fiscal year ended June 30, 2019:

- GASB Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2021, as revised by GASB Statement No. 95, *Postponement of the effective dates of Certain Authoritative Guidance*. The Trust is evaluating the impact of this new statement.
- GASB Statement No. 92, *Omnibus 2020*. The objectives of this Statement are to enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the following: The effective date of *Statement No. 87, Leases, and Implementation Guide No. 2019-3, Leases*, for interim financial reports. The Trust is evaluating the impact of this new statement.

The Trust considered the effective dates for the requirements of this Statement considering the COVID-19 pandemic and in concert with Statement No. 95.

(3) Going Concern

Management believes that there is substantial doubt about the ability of the Trust to continue as a going concern because of the following:

- After the effective date of Act 106-2017, the Trust's operations are limited to maintaining custody of the unliquidated assets (excluding the building and building improvements) that are pending to be transferred to the Commonwealth's General Fund, rental activities and administrative services to the Commonwealth. The Trust is economically dependent of the Commonwealth, which is facing significant risks and uncertainties, including liquidity risk.
- As result of fiscal economic challenges, on May 3, 2017, the Financial Oversight and Management Board for Puerto Rico (the Oversight Board), at the request of the Governor, commenced a Title III case for the Commonwealth by filing a petition for relief under Title III of the Puerto Rico Oversight Management and Economic Stability Act (PROMESA) in the United States District Court for the District of Puerto Rico (the Title III Court).

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- On March 8, 2021, the Oversight Board—as representative to the Commonwealth in their Title III case—filed its *Second Amended Title III Joint Plan of Adjustment of the Commonwealth of Puerto Rico, et al.* [ECF No. 15976] (the Second Amended Plan), and on March 9, 2021 filed a corrected disclosure statement related thereto [ECF No. 15988] (the Second Amended Disclosure Statement). The Second Amended Plan incorporates the terms of (i) a plan support agreement (the 2021 PSA), dated February 22, 2021 between the Oversight Board, certain Commonwealth general obligation bondholders and (ii) a restructuring support agreement with the Retiree Committee (the Retiree Committee RSA), in which the Retiree Committee agreed to a maximum 8.5% pension cut that would only be applicable to retirees with monthly retirement benefits of more than \$1,500, as well as freezes in pension benefits for teachers and judges. On May 12, 2021, the Oversight Board announced that it filed a Third Amended Plan of Adjustments that reflects agreements reached with creditors after filing the Second Amended Plan of Adjustments on March 8, 2021. The Trust is not a debtor in a case under Title III of PROMESA, but the results of the Commonwealth case may have an impact on the Trust as the Trust is a component unit of the Commonwealth.

Management's Remediation Plan

In accordance with Act 106-2017, the Trust's remediation plan will be dependent on the Commonwealth plan of adjustment and ongoing measures between the Government and the Oversight Board. As of the date of these financial statements, a plan of adjustment for the Commonwealth has not yet been approved by the Title III Court.

(4) Deposits and Investments

(a) Deposits

Cash and cash equivalents' in custody of the Trust are exposed to custodial credit risk for deposits. Custodial credit risk for deposits is the risk that, in an event of the failure of a depository financial institution, the Commonwealth may not be able to recover deposits or collateral securities that are in the possession of an outside party. The Commonwealth requires that public funds deposited in Puerto Rico commercial banks be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth. Deposits with non-Puerto Rico commercial banks and with money market funds are uninsured and uncollateralized, as these entities are exempt from compliance with the collateralization requirement.

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Cash and cash equivalents in custody of the Trust as of June 30, 2019 consisted of the following (in thousands):

	<u>Carrying amount</u>	<u>Depository bank balance</u>	<u>Amount uninsured and uncollateralized</u>
Deposits at commercial banks	\$ 108,999	110,283	—
Money market funds	<u>19,998</u>	<u>19,998</u>	<u>19,998</u>
Total	<u>\$ 128,997</u>	<u>130,281</u>	<u>19,998</u>

Custodial Credit Risk Loss on Government Development Bank for Puerto Rico (GDB) Deposits

In April 2016, the Commonwealth enacted the Moratorium Act, which imposed emergency operational restrictions and debt moratorium on GDB. Pursuant to the Moratorium Act, the Governor ordered the suspension of loan disbursements from GDB, imposed restrictions on the withdrawal and transfer of deposits from GDB, and imposed a moratorium on debt obligations of GDB, among other measures. On March 23, 2018, GDB ceased its operations and determined to wind down in an orderly fashion under Title VI of PROMESA.

As a result, a custodial credit risk loss on deposits held with GDB for \$3.3 million of cash deposited as of June 30, 2016, was recognized in the Trust's basic financial statements for the year ended June 30, 2016.

On October 5, 2018, GDB, FAFAA, the Oversight Board, and the Official Committee of Unsecured Creditors (payment pursuant to settlement with the official committee of unsecured creditors) entered into a stipulation (the "Stipulation") resolving certain litigation that had been commenced by the Committee challenging GDB's restructuring proceeding under Title IV of the Puerto Rico Oversight, Management, and Economic Stability Act (the "GDB Restructuring"). The U.S. District Court for the District of Puerto Rico entered an order on the Stipulation on October 9, 2018 (the "Committee Settlement Stipulation"). As a result of the execution of the Qualify Modification, the Trust did not receive cash or beneficial units in the PET in exchange for the amount of deposits held at GDB.

(b) Investments

Investments under custody of the Trust are classified as limited partnerships, which are measured at Net Asset Value (NAV) for fair value. Investments measured at NAV are not subject to GAAP level hierarchy. The ending balance of limited partnerships at June 30, 2019, amounted to approximately \$2.1 million. The allocations of net gains and losses to limited partners are based on certain percentages, as established in the limited partnership agreements. Investments in limited partnerships are not rated by a nationality recognized statistical rating organization.

In accordance with the partnership agreements, the investments can only be redeemed upon distribution from funds managers; usually in the form of a sale of its holdings or dividends distributed.

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As of June 30, 2019, the Trust does not intend to sell the investments in limited partnerships for an amount different to that presented in the financial statements.

As of June 30, 2019, the Trust had capital commitments and contributions as follows (in thousands):

	<u>Total commitments</u>	<u>Fiscal year contributions</u>	<u>Unfunded commitments</u>	<u>Fair value</u>
Guayacán Fund of Funds II, L.P.	\$ 25,000	—	1,319	374
Guayacán Private Equity Fund, L.P.	<u>5,000</u>	<u>—</u>	<u>355</u>	<u>1,759</u>
Total	<u>\$ 30,000</u>	<u>—</u>	<u>1,674</u>	<u>2,133</u>

- *Net Appreciation in Fair Value of Investments*

For the year ended June 30, 2019, the net appreciation in fair value of investments amounted to approximately \$44 thousand was recorded as an increase in due to Commonwealth. The segregated net appreciation in fair value is as follows (in thousands):

<u>Investment type</u>	<u>Realized gain (loss)</u>	<u>Unrealized gain (loss)</u>	<u>Net appreciation in fair value of investments</u>
Investments in limited partnerships	\$ —	44	44
Total	<u>\$ —</u>	<u>44</u>	<u>44</u>

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(5) Loans to Members

As of June 30, 2019, the composition of loans and interest receivable from plan members is summarized as follows (in thousands):

Loans receivable:	
Personal	\$ 53,131
Mortgage	144,277
Cultural trips	<u>1,065</u>
Total loans to plan members	198,473
Less:	
Escrow funds of mortgage loans and guarantee insurance reserve	(7,555)
Allowance for adjustments and losses in realization	<u>(4,972)</u>
Total loans and interest receivable from plan members – net	<u>\$ 185,946</u>

The originations of mortgage, personal and cultural loans were frozen in August 2017. No originations occurred during fiscal year 2019.

The allowance for adjustments and losses in realization is considered a general allowance for all categories of loans and interest receivable, except mortgage loans.

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(6) Capital Assets

For the year ended June 30, 2019, changes in capital assets consisted of the following (in thousands):

	<u>Beginning balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending balance</u>
Capital assets of the Trust:				
Building	\$ 26,008	—	—	26,008
Building improvements	765	—	—	765
Total capital assets of the Trust, being depreciated	26,773	—	—	26,773
Accumulated depreciation and amortization	(14,755)	(723)	—	(15,478)
Total capital assets of the Trust, being depreciated, net	\$ 12,018	(723)	—	11,295
Capital assets under custody of the Trust:				
Capital assets, being depreciated:				
Furniture and equipment	1,526	—	(260)	1,266
Computers and software	10,646	9	(39)	10,616
Branches improvements	274	—	—	274
Vehicles	109	—	—	109
Total capital assets, being depreciated	12,555	9	(299)	12,265
Accumulated depreciation and amortization	(10,807)	(453)	292	(10,968)
Total capital assets under custody of the Trust, net	\$ 1,748	(444)	(7)	1,297

(7) Long-Term Liabilities

Long-term liabilities activity for the year ended June 30, 2019 was as follows:

	<u>Beginning balance June 30, 2018</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance June 30, 2019</u>	<u>Due within one year</u>	<u>Long-term portion</u>
Accrued compensated absences \$	1,044	—	(174)	870	324	546
Voluntary termination benefits	3,950	—	(526)	3,139	745	2,394
\$	4,994	—	(700)	4,009	1,069	2,940

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(8) Voluntary Termination Benefits

On July 2, 2010, the Commonwealth enacted Act No. 70 establishing a program that provides benefits for early retirement or economic incentives for voluntary employment termination to eligible employees, as defined. Act No. 70 also established that early retirement benefits will be provided to eligible employees that have completed at least 15 years of credited services, but less than 30 years of credited services and will consist of monthly benefits ranging from 37.5% to 50% of each employees' monthly salary. Benefits under this program will be paid by the Commonwealth's General Fund and by System, covering their respective employees until the plan member reaches the later of age of retirement or the date the plan member would have completed 30 years of service had the member continued employment. With the enactment of Act 106-2017, the Trust, as an employer, are not required to continue making the required employee and employer pension contributions to the Trust. The PayGo system will be responsible for benefit payments once the retiree is eligible for the pension benefits.

Members who retired under this incentive are not eligible to receive the medical insurance plan contribution. Act No. 106-2017 eliminated since July 1, 2017 the employer's contributions to the Trust's trust fund. Given that, the recorded liability for this voluntary termination benefits as of June 30, 2019 does not consider the future payment of the employer's contributions. As of June 30, 2019, the Trust has recorded a liability of approximately \$3 million for its responsibility as an employer under Act No. 70, which is included within other long term liabilities.

(9) Contingencies

The Trust is a defendant or codefendant in various lawsuits resulting from the ordinary conduct of its operations. Management and legal counsel believe that there are no contingent matters that would have a material adverse effect on the Trust's financial status.

(10) Subsequent Events

Subsequent events were evaluated through December 16, 2021, which is the date these financial statements were available to be issued, to determine if such events should be recognized or disclosed in the 2019 financial statements. The subsequent events disclosed are those which management believes are of public interest for disclosure.

Oversight Board Files Joint Plan of Adjustment for the Commonwealth, ERS, and PBA

On March 8, 2021, the Oversight Board—as representative to the Commonwealth, ERS, and the PBA in their respective Title III cases—filed its *Second Amended Title III Joint Plan of Adjustment of the Commonwealth of Puerto Rico, et al.* [ECF No. 15976] (the Second Amended Plan), and on March 9, 2021 filed a corrected disclosure statement related thereto [ECF No. 15988] (the Second Amended Disclosure Statement). The Second Amended Plan incorporates the terms of (i) a plan support agreement (the 2021 PSA), dated February 22, 2021 between the Oversight Board, certain Commonwealth general obligation bondholders and PBA bondholders; and (ii) a restructuring support agreement with the Retiree Committee (the Retiree Committee RSA), in which the Retiree Committee agreed to a maximum 8.5% pension cut that would only be applicable to retirees with monthly retirement benefits of more than \$1,500, as well as

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freezes in pension benefits for teachers and judges. The Trust is not a debtor in a case under Title III of PROMESA, but the results of the Commonwealth and ERS Title III cases may have an indirect impact on the Trust as the Trust is a component unit of the Commonwealth.

On April 2, 2021, the Oversight Board and ERS bondholders announced their entry to the ERS Stipulation, which set forth an agreement on the economic terms upon which the ERS bondholders would support a plan of adjustment. On May 11, 2021, the Oversight Board—as representative to the Commonwealth, ERS, and PBA in their respective Title III cases—filed its Third Amended Plan and Third Amended Disclosure Statement. The Third Amended Plan remains subject to future amendments and the Title III Court approval, and it is not certain that the Title III Court will ultimately confirm such plan.

On August 2, 2021, the Court entered an order (the “Disclosure Statement Order”) approving the Disclosure Statement for the Seventh Amended Title III Joint Plan of Adjustment of the Commonwealth of Puerto Rico, et al. (the “Disclosure Statement”), filed by the Commonwealth, ERS, and PBA (collectively, the “Debtors”). Pursuant to the Disclosure Statement Order, the Debtors are permitted to solicit from certain creditors votes to accept or reject the Seventh Amended Title III Joint Plan of Adjustment of the Commonwealth of Puerto Rico, et al. (the Plan). The hearings to consider confirmation of the Plan began on November 8, 2021.

For additional information, refer to the publicly available Seventh Amended Plan and Disclosure Statement, which are available at: <https://cases.primeclerk.com/puertorico/Home-DocketInfo>.

Impact of Coronavirus (COVID-19) Pandemic

On March 11, 2020, the World Health Organization (WHO) declared the coronavirus disease caused by a novel coronavirus (COVID-19) as a global pandemic. As a result of the health threat and to contain the virus spread across the island, Governor Vázquez-Garced issued executive order 2020-020, on March 12, 2020, declaring a state of emergency in Puerto Rico to concentrate all efforts and implement necessary measures to safeguard the health, well-being and public safety of the citizens of Puerto Rico. The executive order authorizes the Secretary of the Treasury and the Executive Director of the Oversight Board to set up a special budget, from any available funds, including the Emergency Fund, to cover all necessary costs for the containment of the virus throughout the island and sharing information with the municipalities. Numerous executive orders have been subsequently issued by the governor to manage all COVID-19 matters.

As the Government observes and assesses the results of its measures to control the negative health and economic effects of COVID-19 on the people of Puerto Rico and Puerto Rico’s economy, it will reevaluate and further amend business restrictions as necessary to promote economic recovery while preserving the health, welfare, and safety of the people of Puerto Rico.