

ARTHUR ANDERSEN LLP

THE COMMONWEALTH OF PUERTO RICO
JUDICIARY RETIREMENT SYSTEM

FINANCIAL STATEMENTS
AS OF JUNE 30, 1996 AND 1995
TOGETHER WITH AUDITORS' REPORT

ARTHUR ANDERSEN LLP

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Trustees of
The Commonwealth of Puerto Rico
Judiciary Retirement System:

We have audited the accompanying statements of net assets available for benefits of The Commonwealth of Puerto Rico Judiciary Retirement System (the System) as of June 30, 1996 and 1995, and the related statements of changes in net assets available for benefits for the years then ended. These financial statements and the schedules referred to below are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As explained in Note 3 to the financial statements, the report of the System's actuary reflects that, as of June 30, 1996 and 1995, the unfunded actuarial accrued liability was approximately \$13,100,000 and \$18,700,000, respectively.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of The Commonwealth of Puerto Rico Judiciary Retirement System as of June 30, 1996 and 1995, and the changes in its net assets for the years then ended in conformity with generally accepted accounting principles.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information shown in the accompanying schedules of Funding Progress and Contributions and related notes are presented for purposes of additional analysis and are not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Arthur Andersen LLP

San Juan, Puerto Rico,
October 7, 1996.

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THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

STATEMENTS OF NET ASSETS AVAILABLE FOR BENEFITS

JUNE 30, 1996 AND 1995

(In thousands)

	<u>1996</u>	<u>1995</u>
CASH AND INVESTMENTS:		
Cash and cash equivalents	\$ 1,102	\$ 2,466
Cash deposited with Government Development Bank for Puerto Rico	1,122	-
	<u>2,224</u>	<u>2,466</u>
Marketable securities-		
Notes and bonds	11,066	13,844
Stocks	37,569	26,736
Total marketable securities	<u>48,635</u>	<u>40,600</u>
Mortgage notes acquired from third parties	350	438
Total cash and investments	<u>51,199</u>	<u>43,504</u>
LOANS TO PLAN MEMBERS:		
Mortgage	418	517
Personal	90	79
Cultural trips	53	23
Total loans to plan members	<u>561</u>	<u>619</u>
Total cash, investments and loans to plan members	<u>51,760</u>	<u>44,123</u>
RECEIVABLES:		
Accrued interest	275	228
Other	91	108
	<u>366</u>	<u>336</u>
Total assets	<u>52,126</u>	<u>44,459</u>
DUE TO THE GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO	-	1,005
DUE TO THE EMPLOYEES' RETIREMENT SYSTEM OF THE GOVERNMENT OF PUERTO RICO	1,651	721
ESCROW FUNDS OF MORTGAGE LOANS TO PLAN MEMBERS	154	154
OTHER LIABILITIES	326	522
Total liabilities	<u>2,131</u>	<u>2,402</u>
Net assets available for benefits	<u>\$49,995</u>	<u>\$42,057</u>

The accompanying notes are an integral part of these statements.

THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

STATEMENTS OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

FOR THE YEARS ENDED JUNE 30, 1996 AND 1995

(In thousands)

	<u>1996</u>	<u>1995</u>
INCOME FROM CASH, INVESTMENTS AND LOANS:		
Interest and dividends	\$ 1,419	\$ 1,436
Net appreciation of investments	7,808	5,671
Other	121	225
Total income from cash, investments and loans	<u>9,348</u>	<u>7,332</u>
CONTRIBUTIONS:		
Employer	3,890	3,228
Participating employees	1,618	1,346
Total contributions	<u>5,508</u>	<u>4,574</u>
Total additions	<u>14,856</u>	<u>11,906</u>
BENEFITS AND EXPENSES:		
Annuities	5,846	5,194
Administrative expenses	1,072	262
Total deductions	<u>6,918</u>	<u>5,456</u>
Net increase in net assets available for benefits	<u>7,938</u>	<u>6,450</u>
NET ASSETS AVAILABLE FOR BENEFITS:		
Beginning of year	<u>42,057</u>	<u>35,607</u>
End of year	<u>\$49,995</u>	<u>\$42,057</u>

The accompanying notes are an integral part of these statements.

THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 1996 AND 1995

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The Commonwealth of Puerto Rico Judiciary Retirement System (the System) was created by Act No. 12 on October 19, 1954. The System is considered an integral part of the Commonwealth of Puerto Rico (the Commonwealth) financial reporting entity and is included in the Commonwealth's financial statements as a trust fund. The System, as a governmental retirement plan, is excluded from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

The responsibility for the operation and administration of the System is vested in a Board of Trustees, composed of two participating employees and one pensioner, who are appointed by the Governor of the Commonwealth, and four Commonwealth government agency representatives.

The System is not an employer. The System's operations are managed by the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). During the year ended June 30, 1996, ERS commenced allocating administration costs to the System, which amounted to \$754,000.

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

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with the provisions of Statement of Governmental Accounting Standards No. 25 (SGAS No. 25), "Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans". The provisions of SGAS No. 25 have been retroactively implemented effective July 1, 1994, however, the effects of this retroactive implementation relate only to the note disclosures and the presentation of required supplementary information. Participating employees' and employer's contributions are recognized as revenues in the period in which the employee services are rendered.

Cash and Cash Equivalents

Cash and cash equivalents consist of "overnight deposits" guaranteed by the custodial bank.

Investments

Investments are carried at fair value, except for certain mortgage notes which have no market. The fair value of notes, bonds and stocks is based on quotations obtained from national securities exchanges.

Securities transactions are accounted for on the trade date. Realized gains and losses on securities are determined by the average cost method and are included in the statement of changes in net assets available for benefits.

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

No investment in any organization represents 5% or more of the System's net assets available for benefits.

Loans to Plan Members

Mortgage, personal and cultural trip loans to plan members are stated at their outstanding principal balance. No allowance for uncollectible amounts has been established since loans to plan members are secured by mortgage deeds, judges' contributions and any unrestricted amount remaining in the escrow funds. Maximum amounts that may be granted for mortgage, personal and cultural trip loans to plan members are \$100,000, \$3,000 and \$5,000, respectively. The carrying value of these loans approximates their fair value.

2. PLAN DESCRIPTION:

The System is a defined benefit single-employer plan sponsored by the Commonwealth. Under the terms of the Act No. 12 of 1954, as amended, all judges of the Judiciary Branch of the Commonwealth are plan members of the System. At June 30, 1996 and 1995, membership consisted of the following:

	<u>1996</u>	<u>1995</u>
Retirees and beneficiaries currently receiving benefits	229	220
	====	====
Current participating employees	285	271
	====	====

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

Retirement Annuity

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

Plan members are eligible for monthly benefit payments determined by the application of stipulated benefit ratios to the plan member's average compensation. Average compensation is computed based on the last three years of service (effective July 28, 1993, highest annual salary), except for the judges of the Supreme Court for whom it is based on the last month of compensation. The annuity for which a plan member is eligible is limited to a minimum of 25% and a maximum of 100% of the average compensation.

Reversionary Annuity

A plan member, upon retirement, could elect to receive a reduced retirement annuity giving one or more benefit payments to his/her dependents. The payments would start after the death of the retiree, in an amount not less than \$120 yearly nor greater than the annuity payments being received by the retiree.

Occupational Disability Annuity

A participating employee permanently disabled is eligible for a disability annuity of 50% of the compensation received at the time of the disability.

Nonoccupational Disability Annuity

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

Death Benefits

Occupational-

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

Nonoccupational-

- Beneficiary ineligible for survivor benefit - the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of the death.
- Surviving spouse and child, 21 or under - up to 60% of the pension that would have been payable had the participating employee retired on the date of death.

Post-retirement-

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

Refunds

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

Termination

Although the Commonwealth has not expressed any intent to terminate the plan, it may do so at any time. In the event of termination of the plan, the rights of all affected plan members and beneficiaries to whom benefits have accrued under the plan shall be nonforfeitable to the extent funded.

3. FUNDING POLICY:

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

Calculations of the present value of benefits under the System were made by consulting actuaries as of June 30, 1996 and 1995, using the projected unit credit actuarial cost method. Significant assumptions underlying the actuarial computations include: (a) assumed rate of return on investments of 8.5%, (b) assumed compound rate of wage increases of 5%; and (c) assumed mortality rate based on the Group Annuity Table for 1951.

The actuarial accrued liability was \$63,100,000 and \$60,800,000 as of June 30, 1996 and 1995, respectively. At June 30, 1996 and 1995, the unfunded actuarial accrued liability was approximately \$13,100,000 and \$18,700,000, respectively.

4. CASH AND INVESTMENTS:

Pursuant to the provisions of Act No. 46 of 1988, the System may invest, with certain restrictions, in obligations of the Commonwealth and its Instrumentalities, the United States of America, private corporations and foreign countries. In addition, the System may invest in common and preferred stock, in income-producing real properties and in high-risk securities.

Cash and cash equivalents are guaranteed by the custodial bank. Cash deposited with Government Development Bank of Puerto Rico is not collateralized.

The following table shows the carrying amount and market value of the investments in marketable securities held by the System as of June 30, 1996 and 1995. The following investments are held by agents in the System's name:

	1996		1995	
	Cost or Amortized Cost	Fair Value	Cost or Amortized Cost	Fair Value
		(In thousands)		
U.S. Government and agencies' securities	\$11,063	\$10,828	\$11,625	\$12,086
Corporate bonds	245	238	1,733	1,758
Corporate stocks	30,729	37,569	21,683	26,756
	<u>\$42,037</u>	<u>\$48,635</u>	<u>\$35,041</u>	<u>\$40,600</u>

The net changes in the appreciation (depreciation) of investments in marketable securities are as follows:

	1996	1995
	(In thousands)	
Securities held at year-end-		
Notes and bonds	\$(729)	\$ 936
Stocks	1,701	2,457
	<u>972</u>	<u>3,393</u>
Securities sold during the year	6,836	2,278
	<u>\$7,808</u>	<u>\$5,671</u>

5. GUARANTEE INSURANCE RESERVE OVER LOANS TO PLAN MEMBERS:

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

THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

SCHEDULE OF FUNDING PROGRESS

(Dollars amounts in thousands)

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability (AAL)</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>UAAL as a Percentage of Covered Payroll</u>
7/1/96	\$50,000	\$63,100	\$13,100	79%	\$16,600	79%
7/1/95	42,100	60,800	18,700	69%	15,800	118%
7/1/94	35,600	58,900	23,300	60%	12,600	185%
7/1/93	36,600	57,500	20,900	64%	13,200	158%
7/1/92	33,100	54,000	20,900	61%	13,300	157%
7/1/91	29,900	51,300	21,400	58%	13,400	160%

The accompanying notes to schedules are an integral part of this schedule.

THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

SCHEDULE OF CONTRIBUTIONS

(Dollars amounts in thousands)

<u>Year Ended</u> <u>June 30</u>	<u>Annual Required</u> <u>Contribution</u>	<u>Contributions</u>	<u>Percentage</u> <u>Contributed</u>
1996	\$3,600	\$5,500	153%

The accompanying notes to schedules are an integral part of this schedule.

THE COMMONWEALTH OF PUERTO RICO

JUDICIARY RETIREMENT SYSTEM

NOTES TO SCHEDULES

JUNE 30, 1996 AND 1995

1: SCHEDULE OF FUNDING PROGRESS:

The Schedule of Funding Progress provides information about the funded status of the System and the progress being made in accumulating sufficient assets to pay benefits when due.

2: SCHEDULE OF CONTRIBUTIONS:

The Schedule of Contributions provides information about the annual required contributions (ARC) and the extent to which contributions made cover the ARC. The ARC is the annual required contribution for the year calculated in accordance with certain parameters which include actuarial methods and assumptions. The annual required contributions for the years ended June 30, 1991 through 1995, computed in accordance with the required parameters, are not available.

The System's Schedule of Contributions includes both Commonwealth's and participating employees' contributions as the Commonwealth contributions, ultimately, should cover any deficiency between the participating employees' contributions and, the pension benefits and the Systems' administration costs.

3: ACTUARIAL DATA:

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation Date	July 1, 1996
Actuarial Cost Method	Projected unit credit cost method
Amortization Method	Level percentage of the projected payroll
Remaining Amortization Period	30 years
Asset Valuation Method	Market value
Actuarial Assumptions:	
Investment rate of return*	8.5%
Projected salary increases*	5%
Cost of living adjustment	3%, every three years

*Includes inflation at 3.5%