



ESTADO LIBRE ASOCIADO DE  
**PUERTO RICO**  
Fideicomiso de los Niños

9178-1

6 de mayo de 2016

Hon. Eduardo A. Bhatia Gautier  
Presidente  
Senado de Puerto Rico  
El Capitolio  
PO Box 9023431  
San Juan, PR 00902-3431

ll  
RECIBIDO MAY 12 '16 AM 11:22  
SECRETARIA SENADO DE P.R.

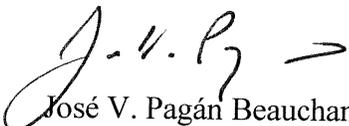
Estimado Presidente:

Informes Anuales del Fideicomiso de los Niños para los Años Fiscales 2012 a 2015

El Artículo 18 de la Ley Núm. 173 del 30 de julio de 1999, según enmendada, requiere que, luego del 31 de marzo de cada año, se rinda un informe a la Asamblea Legislativa y al Contralor de Puerto Rico sobre el Fideicomiso de los Niños que incluya: el estado financiero auditado; una relación de los contratos y transacciones durante el año fiscal a que corresponda el informe; e información sobre el progreso de los financiamientos y actividades hasta la fecha del último informe.

Se incluyen los informes anuales para los años fiscales 2012 a 2015 de acuerdo con los términos de la Ley.

Atentamente,

  
José V. Pagán Beauchamp  
Director Ejecutivo Interino

*Beauchamp*

9178-1



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SECRETARIA SENADO DE P.R.

# FIDEICOMISO DE LOS NIÑOS



**Informe Anual para el Año Fiscal 2011- 2012  
a la Asamblea Legislativa  
y al Contralor de Puerto Rico**



## **Fideicomiso de los Niños**

**Informe a la Asamblea Legislativa y al Contralor de Puerto Rico,  
Según Requerido por la Ley Núm. 173 del 30 de julio de 1999, Según Enmendada  
Año Fiscal 2012**

### **Introducción**

El Artículo 18 de la Ley Núm. 173 del 30 de julio de 1999, según enmendada, requiere que luego del 31 de marzo de cada año, el Fideicomiso de los Niños rinda un informe a la Asamblea Legislativa y al Contralor de Puerto Rico relacionado con el año fiscal anterior. Dicho informe deberá incluir:

1. Un estado financiero auditado por una compañía reconocida e informe completo de las actividades del Fideicomiso para el año fiscal anterior;
2. Una relación completa y detallada de todos los contratos y transacciones durante el año fiscal a que corresponda el informe;
3. Información sobre la situación y progreso de los financiamientos y actividades hasta la fecha del último informe.

Se rinde éste, el undécimo informe del Fideicomiso de los Niños a la Asamblea Legislativa y al Contralor de Puerto Rico, de acuerdo con los términos de Ley.

## Fideicomiso de los Niños

### Año Fiscal 2012

#### I. Estado Financiero Auditado

Se incluyen, como Anejo I, los estados financieros auditados por la firma Aquino, De Córdova, Alfaro & Co., LLP para el año fiscal terminado el 30 de junio de 2012.

#### II. Informe de Actividades

Entidad Líder	Fecha Firma Contrato o Transacciones	Cantidad Aprobada
<u>Año Fiscal 2012</u>		
Departamento de Estado - Actividad Día de Reyes 2012	16-dic-2011	\$925,000

#### III. Situación de Progreso de los Financiamientos y Actividades del Año Fiscal 2012

El Fideicomiso desembolsó \$3,944,976.19 por concepto de Servicios de Ayuda durante el año fiscal que terminó el 30 de junio de 2012. A continuación un detalle de los desembolsos para el año fiscal:

<b>Entidad Líder</b>	<b>Cantidad Aprobada</b>	<b>Total Desembolsado 2011-2012</b>
Centro Esperanza, Inc.	\$551,495	\$55,286
Centros Sor Isolina Ferré (C S M C)	5,608,500	1,243,216
Fundación de Desarrollo Comunal de PR, Inc.	700,953	276,420
Hogar Albergue de Niños Maltratados de San Germán	137,374	34,558
Hogar El Pequeño Joshua de La Perla de Gran Precio	967,562	106,969
Instituto Especial Desarrollo Integral (Yauco)	354,368	21,588
Instituto Especial para el Desarrollo, IDIIFCO	641,200	89,148
Jane Stern Dorado Community Library	29,900	20,235
Niños Escuchas de América	7,477,000	489,173
San Agustín del Coquí	3,294,660	300,266
Universidad Central de Bayamón	96,822	7,343
Departamento de Educación (OMEP)	29,000,000	341,023
Departamento de Educación	10,000,000	142,476
Departamento de Estado (Tres Reyes 2012)	925,000	660,172
Municipio de Vega Baja (2002-32)	49,486	14,766
UPR - Recinto de Ciencias Médicas - Tobacco (2002-29)	1,576,319	142,339
		<b>\$3,944,976</b>

El total acumulado de desembolsos por año fiscal se detalla de la siguiente manera:

- Año Fiscal 2001 - \$ 75,211,960.35
- Año Fiscal 2002 - \$171,690,102.13
- Año Fiscal 2003 - \$483,762,894.97
- Año Fiscal 2004 - \$149,142,073.47
- Año Fiscal 2005 - \$182,975,610.14
- Año Fiscal 2006 - \$ 44,250,818.76
- Año Fiscal 2007 - \$ 96,800,748.97
- Año Fiscal 2008 - \$112,855,926.94
- Año Fiscal 2009 - \$ 11,236,966.30
- Año Fiscal 2010 - \$ 5,851,868.88
- Año Fiscal 2011 - \$ 8,443,371.59
- Año Fiscal 2012 - \$ 3,944,976.19



**Anejo I**

**Fideicomiso de los Niños**

**Estados Auditados al 30 de junio de 2012**

# *Financial Statements*

## The Children's Trust

(A Component Unit of the Commonwealth of Puerto Rico)

Basic Financial Statements and Required Supplementary  
Information as of and for the Year Ended June 30, 2012,  
and Independent Auditors' Report

**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**TABLE OF CONTENTS**

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	<b>Pages</b>
Independent Auditors' Report	1
Management's Discussion and Analysis	2-6
Basic Financial Statements as of and for the Year Ended June 30, 2012:	
Government-Wide Financial Statements:	
Statement of Net Deficit	7
Statement of Activities	8
Fund Financial Statements:	
Balance Sheet – Governmental Funds	9
Reconciliation of Balance Sheet – Governmental Funds to the Statement of Net Deficit	10
Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds	11
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds to the Statement of Activities	12
Notes to Basic Financial Statements	13-23





## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of  
The Children's Trust

We have audited the accompanying financial statements of the governmental activities and each major fund of The Children's Trust (the "Trust"), a component unit of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2012, which collectively comprise the Trust's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Trust'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. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of The Children's Trust as of June 30, 2012, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 2 through 6 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.

September 28, 2012

Stamp No. 2664178  
has been affixed  
to the original report

Aquino, De Córdova, Alfaro & Co., LLP  
by   
Lic # 3171

**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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As management of The Children's Trust (the "Trust"), we offer readers of the Trust's financial statements this narrative overview and analysis of the Trust's financial performance during the fiscal year ended June 30, 2012. Please read it in conjunction with the Trust's basic financial statements including the notes thereto, which follow this section.

**(1) Financial highlights:**

- The Trust's net deficit increased by \$18.4 million over the course of the year's operations ending with a net deficit of \$1,174.9 million, from a total net deficit at beginning of year of \$1,156.5 million.
- Global Settlement Agreement (GSA) revenues for the fiscal year amounted to \$72.5 million, an increase of \$1.5 million, or 2%, from the \$71 million for 2011.
- The Trust's operating expenses consist of payments for programs and activities permitted by the enabling legislation. Grants during 2012 totaled \$3.7 million, a decrease of \$4.9 million, or 57%, from the \$8.6 million granted during 2011.

**(2) Overview of the financial statements:**

The financial statements include the management's discussion and analysis section, the independent auditors' report, and the basic financial statements of the Trust. The basic financial statements also include notes that explain in more detail some of the information in the basic financial statements.

**(3) Required financial statements:**

*Government-Wide Financial Statements* — The statement of net deficit and the statement of activities report information on all activities of the Trust. Only governmental activities are presented in the Trust's financial statements. Governmental activities, generally are financed through nonexchange revenues. Following is a description of the Trust's government-wide financial statements.

- The statement of net deficit presents the Trust's assets and liabilities, with the difference reported as net deficit.
- The statement of activities demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include: (1) interest income on investments and interest bearing deposits, (2) grants and contributions that are restricted to meet the operational or capital requirements of a particular function. Other items not meeting the definition of program revenues are reported as general revenues.

*Fund Financial Statements* — Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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activities. A fund is a separate accounting entity with a self-balancing set of accounts that comprise its assets, liabilities, fund balances, revenue and expenditures, as appropriate. The financial activities of the Trust reported in the accompanying basic financial statements were classified into governmental funds. All funds of the Trust are major funds.

**(4) Financial analysis of the Trust:**

The statement of net deficit and the statement of activities report information about the Trust's activities in a way that will help understand if the Trust as a whole is better or worse as a result of this year activities. These two statements report the net deficit of the Trust and the changes in them.

One can think of the Trust's net deficit — the difference between assets and liabilities — as one way to measure financial health or financial position. Over time, increases or decreases in the Trust's net deficit are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors such as changes in economic conditions including economic conditions of the tobacco industry, and new or changed government legislation needed to be considered.



# THE CHILDREN'S TRUST

(A Component Unit of the Commonwealth of Puerto Rico)

## MANAGEMENT'S DISCUSSION AND ANALYSIS AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

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### (5) Government-wide financial analysis:

The government wide financial statements were designed so that the user could determine whether the Trust is in a better or worse financial condition when compared to the prior year. The following is a condensed summary of net deficit of the Trust compared with prior year (amounts in thousands):

	June 30,		Change	
	2012	2011	Amount	Percent
Assets:				
Current assets	\$ 43,696	\$ 47,488	\$ (3,792)	(8.0%)
Non-current restricted assets	158,973	160,448	(1,475)	(0.9%)
Total assets	202,669	207,936	(5,267)	(2.5%)
Liabilities:				
Current liabilities	22,829	21,462	1,367	6.4%
Non-current liabilities	1,354,802	1,343,039	11,763	0.9%
Total liabilities	1,377,631	1,364,501	13,130	1.0%
Net deficit	\$ (1,174,962)	\$ (1,156,565)	\$ (18,397)	1.6%

As noted above, the Trust's net deficit increased by \$18.4 million, from a net deficit of \$1,156.5 million in 2011 to \$1,174.9 million in 2012. This increase results from two major facts: the decrease in total assets of \$5.3 million, mainly resulting from grants disbursements of approximately \$4 million during the year, and \$13.1 million increase in liabilities, mainly due to the net effect of the amortization of loss on refunded bonds and discount of approximately \$4.5 million, the effect of interest capitalization for fiscal year 2012 of approximately \$31 million, and the payment of principal on bonds of approximately \$22 million.



Aquino, De Córdova, Alfaro & Co., LLP

CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS ADVISORS

**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

Condensed program revenues, expenses, and change in net deficit are presented below (amounts in thousands):

Function/program	Year ended June 30,		Change	
	2012	2011	Amount	Percent
Governmental activities:				
Education	\$ 449	\$ 2,527	\$ (2,078)	(82.2%)
Health	1,376	4,359	(2,983)	(68.4%)
Recreation	1,255	1,254	1	0.1%
Intergovernmental	660	469	191	40.7%
Interest on long-term debt and other – net	87,609	86,699	910	1.0%
	<u>91,349</u>	<u>95,308</u>	<u>(3,959)</u>	<u>(4.2%)</u>
General revenues:				
Investment earnings	47	49	(2)	(4.1%)
Global settlement agreement	72,500	71,002	1,498	2.1%
Other income	405		405	100.0%
	<u>72,952</u>	<u>71,051</u>	<u>1,901</u>	<u>2.7%</u>
Change in net deficit	<u>\$ (18,397)</u>	<u>\$ (24,257)</u>	<u>\$ 5,860</u>	<u>(24.2%)</u>

While comparative statements of net deficit show the changes in financial position, the statement of activities provides answers as to the nature and source of these changes. As noted, the decrease in the change in deficit of \$5.8 million is mainly due to the increase of \$1.9 million in Global Settlement agreement and other revenues, and the decrease in governmental activities of \$4 million.

**(6) Governmental fund financial analysis:**

The Trust's governmental funds reported fund balances of \$153.9 million as of June 30, 2012, which is \$4.4 million less than prior year. The decrease in fund balance in the governmental funds is mainly due to a decrease in grants disbursement of \$4.9 million during fiscal year 2012.

**(7) Debt administration:**

During the year ended June 30, 2012, the Trust repaid \$22 million of its bonds payable, and has a remaining balance of bonds outstanding of \$1,370 million, net of \$23.4 million of unaccrued bond discount and an unamortized deferred loss on refunded bonds of \$30.4 million, due through year 2057.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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**(8) Request for information:**

This financial report is designed to provide those interested with a general overview of the Trust's finances and to enhance the Trust's accountability for the funds it receives. Questions about this report or requests for additional information should be addressed to The Children's Trust, PO Box 42001, San Juan, Puerto Rico, 00940-2001.



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**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**STATEMENT OF NET DEFICIT**  
**JUNE 30, 2012**

<b>ASSETS</b>	<b>Governmental Activities</b>
<b>CURRENT ASSETS:</b>	
Interest-bearing deposits with Government Development Bank for Puerto Rico	\$ 20,426,840
Investments and investment contracts	23,267,613
Accrued interest receivable	<u>1,675</u>
Total current assets	43,696,128
<b>NON-CURRENT RESTRICTED ASSETS:</b>	
Investments and investment contracts	110,454,812
Accrued interest receivable	441,607
Receivable from Global Settlement Agreement to be applied to debt service	40,584,528
Deferred bond issue costs	<u>7,492,174</u>
Total non-current restricted assets	<u>158,973,121</u>
Total assets	<u>202,669,249</u>
<b>LIABILITIES</b>	
<b>CURRENT LIABILITIES:</b>	
Accounts payable	632,851
Liabilities payable from restricted assets:	
Accrued interest payable	6,691,109
Bonds payable due in one year, net	<u>15,505,000</u>
Total current liabilities	22,828,960
<b>NON-CURRENT LIABILITY —</b>	
Bonds payable due in more than one year, net	<u>1,354,801,902</u>
Total liabilities	<u>1,377,630,862</u>
<b>NET DEFICIT</b>	<u>\$ (1,174,961,613)</u>

See notes to basic financial statements.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**STATEMENT OF ACTIVITIES**  
**FOR THE YEAR ENDED JUNE 30, 2012**

Functions/Programs	Expenses	Program Revenues		Net Expenses and Change in Net Deficit
		Investment Earnings	Operating Contributions	
<b>GOVERNMENTAL ACTIVITIES:</b>				
Education	\$ 449,038	\$ -	\$ -	\$ 449,038
Health	1,375,658			1,375,658
Recreation	1,255,257			1,255,257
Intergovernmental grants	660,579			660,579
Interest on long term-debt and other	<u>90,981,815</u>	<u>3,373,323</u>	<u>72,499,728</u>	<u>15,108,764</u>
Total governmental activities	<u>\$ 94,722,347</u>	<u>\$ 3,373,323</u>	<u>\$ 72,499,728</u>	<u>18,849,296</u>
<b>GENERAL REVENUES —</b>				
Investments earnings				47,061
Other income				<u>405,450</u>
Total				452,511
CHANGE IN NET DEFICIT				(18,396,785)
NET DEFICIT — Beginning of year				<u>(1,156,564,828)</u>
NET DEFICIT — End of year				<u>\$ (1,174,961,613)</u>

See notes to basic financial statements.





**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**RECONCILIATION OF BALANCE SHEET- GOVERNMENTAL FUNDS TO THE  
STATEMENT OF NET DEFICIT  
AS OF JUNE 30, 2012**

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**FUND BALANCES OF GOVERNMENTAL FUNDS** \$ 153,959,696

**AMOUNTS REPORTED FOR GOVERNMENTAL ACTIVITIES IN THE  
STATEMENT OF NET DEFICIT ARE DIFFERENT BECAUSE:**

Bond issue costs are reported as an expenditure in the governmental funds financial statements; however, these costs are capitalized and amortized over the life of the bonds and are included in the statement of net deficit.	7,492,174
Discount on bonds issued is reported as an other financing use in the governmental funds financial statements; however, such discount is deferred and accreted over the life of the bonds and is included within bonds payable in the statement of net deficit.	23,406,749
Unamortized loss on bonds defeasance is not reported as an expenditure in the governmental fund financial statements; however, such loss is deferred and amortized over the life of the bonds and is included within bonds payable in the statement of net deficit.	30,455,107
Receivable from Global Settlement Agreement to be applied to debt service will not be received in the current period, and therefore, is not reported in the fund financial statements.	40,584,528
Accrued interest payable is not due and payable in the current period and, therefore, is not reported in the fund financial statements.	(6,691,109)
Bonds payable are not due and payable in the current period and, therefore, are not reported in the fund financial statements.	<u>(1,424,168,758)</u>
<b>NET DEFICIT OF GOVERNMENTAL ACTIVITIES</b>	<b><u>\$ (1,174,961,613)</u></b>

See notes to basic financial statements.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND  
BALANCES — GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED JUNE 30, 2012**

	<u>General Fund</u>	<u>Tobacco Settlement Asset-Backed Bonds Debt Service Fund</u>	<u>Total Governmental Funds</u>
<b>REVENUES:</b>			
Investments earnings	\$ 47,061	\$ 3,373,323	\$ 3,420,384
Revenue from Global Settlement Agreement		72,490,828	72,490,828
Other income	405,450		405,450
Total revenues	<u>452,511</u>	<u>75,864,151</u>	<u>76,316,662</u>
<b>EXPENDITURES:</b>			
Current:			
Education	449,038		449,038
Health	1,375,658		1,375,658
Recreation	1,255,257		1,255,257
Intergovernmental	660,579		660,579
Other	332,830	11,240	344,070
Debt service:			
Principal		22,060,000	22,060,000
Interest		54,474,517	54,474,517
Total expenditures	<u>4,073,362</u>	<u>76,545,757</u>	<u>80,619,119</u>
NET CHANGES IN FUND BALANCES	(3,620,851)	(681,606)	(4,302,457)
FUND BALANCES — Beginning of year	<u>46,684,128</u>	<u>111,578,025</u>	<u>158,262,153</u>
FUND BALANCES — End of year	<u>\$ 43,063,277</u>	<u>\$ 110,896,419</u>	<u>\$ 153,959,696</u>

See notes to basic financial statements.



# THE CHILDREN'S TRUST

(A Component Unit of the Commonwealth of Puerto Rico)

## RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES – GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES FOR THE YEAR ENDED JUNE 30, 2012

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NET CHANGE IN FUND BALANCE-GOVERNMENTAL FUNDS \$ (4,302,457)

### AMOUNTS REPORTED FOR GOVERNMENTAL ACTIVITIES IN THE STATEMENT OF ACTIVITIES ARE DIFFERENT BECAUSE:

Net change in receivable from Global Settlement Agreement is reported as revenue in the statement of activities, but is not reported in the fund financial statement since it does not provide current financial resources. 8,900

Net change in interest payable reported in the statement of activities that does not require the use of current financial resources, and therefore, are not reported as an expenditure in the governmental funds. 161,710

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces bonds payable in the statement of net deficit; this is the amount of redemption on bond principal during the year. 22,060,000

Interest capitalization on Tobacco Settlement Asset-Backed Bonds Series 2005 do not require the use of current financial resources, and therefore, are not reported as expenditure in governmental funds. (11,039,069)

Interest capitalization on Tobacco Settlement Asset-Backed Bonds Series 2008 do not require the use of current financial resources, and therefore, are not reported as expenditure in governmental funds. (19,984,386)

The amortization of deferred bond issue costs, bonds discount and loss on bonds refunded do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds:

Amortization of bond issue costs	(802,029)
Amortization of bond discount	(1,535,454)
Amortization of loss on bonds refunded	<u>(2,964,000)</u>

CHANGE IN NET DEFICIT OF GOVERNMENTAL ACTIVITIES \$ (18,396,785)

See notes to basic financial statements.



Aquino, De Córdova, Alfaro & Co., LLP

CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS ADVISORS

**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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**1. REPORTING ENTITY**

The Children's Trust (the "Trust") is a component unit of the Commonwealth of Puerto Rico (the "Commonwealth") created by Act No. 173 of the Legislature of the Commonwealth on July 30, 1999, as amended, (the "Act"), and an affiliate of the Government Development Bank for Puerto Rico (the "Bank"), a component unit of the Commonwealth. The Trust was created for the purpose of developing programs aimed at promoting a better quality of life and the well-being of families, children, and youth in Puerto Rico, especially in the areas of education, recreation and health. These programs are financed with the moneys to be received by the Commonwealth from the Global Settlement Agreement dated November 23, 1998 (the "Agreement" or "GSA") between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. Pursuant to the Act, the Commonwealth assigned and transferred to the Trust the contributions which the Commonwealth is entitled to receive under the Agreement. The Agreement calls for annual payments through the year 2025, which will vary due to inflationary and volume adjustments. After 2025, the tobacco companies shall continue making contributions in perpetuity.

The Act provides that the Bank will act as the trustee of the Trust. The Trust is exempt from taxation in Puerto Rico, pursuant to the Act.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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 the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of changes in net assets and revenues and expenditures during the reporting period. Actual results could differ from those estimates.

The accounting and reporting policies of the Trust conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities. The Trust follows Governmental Accounting Standards Board ("GASB") under the hierarchy established by Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements.

Following is a description of the Trust's most significant accounting policies:

**Government-Wide and Fund Financial Statements**

*Government-Wide Financial Statements* — The statement of net deficit and the statement of activities report information on all activities of the Trust. The Trust has only governmental activities. The effect of interfund balances has been removed from the statement of net assets. Governmental activities are financed through revenue from the Agreement, intergovernmental revenue, and other financing sources.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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The statement of net deficit presents the Trust's assets and liabilities, with the difference reported as net deficit.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include earnings (losses) on investments. Other items not meeting the definition of program revenues are reported as general revenues.

*Governmental Fund's Financial Statements* — Separate financial statements are provided for governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. All funds of the Trust are major funds.

**Measurement Focus, Basis of Accounting and Financial Statement Presentation** — The accounts of the Trust are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for within a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenue, and expenditures, as appropriate. Government resources are allocated to and accounted for in individual funds based upon the purpose for which they are to be spent and the means by which spending activities are controlled.

*Government-Wide Financial Statements* — Government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Grants and similar items are recognized as revenue as soon as all of the eligibility requirements imposed by the provider have been met.

*Governmental Fund's Financial Statements* — The governmental fund's financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they become measurable and available.

Revenue resulting from the Tobacco Settlement Agreement is recognized on an annual basis, upon collection. Interest income is recognized when earned, since it is available and measurable. Expenditures are recorded when the related liability is incurred. An exception to this general rule includes principal and interest on general long-term debt, which is recognized when due. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Trust considers revenues to be available if they are to be collected within 60 days after the end of the current fiscal year-end.

**Fund Accounting** — The financial activities of the Trust are recorded in individual funds, each of which is deemed to be a separate accounting entity. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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The financial activities of the Trust that are reported in the accompanying basic financial statements have been classified into the following major governmental funds:

*General Fund* — The general fund is used to account for grants awarded to promote a better quality of life and the well-being of families, children, and youth in Puerto Rico. During the year ended June 30, 2012, grants were awarded for education, health and recreational activities.

*Tobacco Settlement Asset-Backed Bonds Debt Service Fund* — This debt service fund is used to account for proceeds from the Agreement and for the payment of interest and principal on long-term obligations.

Fund balances for each governmental fund are displayed in the following classifications depicting the relative strength of the spending constraints placed on the purposes for which resources can be used:

- *Nonspendable*- amounts that cannot be spent because they are either not in a spendable form (such as inventories and prepaid amounts) or are legally or contractually required to be maintained intact.
- *Restricted*- amounts that can be spent only for specific purposes because of constraints imposed by external providers (such as grantors, bondholders, and higher levels of government), or imposed by constitutional provisions or enabling legislation.
- *Committed*- amounts that can be spent only for specific purposes determined by a formal action of the Trust's highest level of decision-making authority.
- *Assigned fund balance*- amounts the Trust intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed.
- *Unassigned fund balance*- amounts that are available for any purpose.

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

**Investments and Investment Contracts** — Investments and investment contracts are carried at fair value, except for money market investments and participating investment contracts with a remaining maturity at the time of purchase of one year or less, and non-participating investment contracts, which are carried at cost. Fair value is determined based on quoted market prices, except for investments in Puerto Rico municipal bonds and notes for which fair value is based on quotations received from independent broker/dealers.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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**Restricted Assets** — Certain resources are set aside for the repayment of bonds payable. These assets are classified as restricted assets on the accompanying Statement of Net Deficit and Balance Sheet – Governmental Funds.

**Deferred Bond Issue Costs and Bond Discount** — Deferred bond issue costs and bond discount are amortized over the life of the debt in the government-wide financial statements. Bond issue costs and discounts are recognized in the period when the related long-term debt is issued in the governmental funds financial statements, and therefore are not accounted for in subsequent periods.

**Interfund Transactions** — The Trust has operating transfers which are legally required transfers that are reported when incurred as “Transfers-in” by the recipient fund and as “Transfers-out” by the disbursement fund.

**Restricted Fund Balance** — Restrictions of fund balance represents portions that can be spent only for specific purposes because of constraints imposed by external providers (such as grantors, bondholders, and higher levels of government), or imposed by constitutional provisions or enabling legislation.

**Refundings** — Refundings involve the issuance of new debt whose proceeds are used to repay immediately (current refunding) or at a future time (advance refunding) previously issued debt. The difference between the reacquisition price and the net carrying amount of the old debt is deferred and amortized as a component of interest expense in the statement of activities, over the remaining life of the old debt or the life of the new debt, whichever is shorter. The deferred amount is reported on the statement of net deficit as an addition to or deduction from the new debt.

**Tobacco Settlement Recognition** — The Trust follows the GASB Technical Bulletin No. 2004-1, *Tobacco Settlement Recognition and Financial Reporting Entity Issue* (the “TB”), as amended by GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, which provides accounting guidance for entities created to obtain the rights to all or a portion of future tobacco settlement resources and for the governments that create such entities.

The TB indicates that the entity created to obtain the rights, which is called the Tobacco Settlement Authority (“TSA”), should be considered a component unit of the government that created it and that the component unit should be blended. The TB also states that the government receiving the payments from the tobacco companies under the Agreement, which is called settling government, should recognize a receivable and revenue for tobacco settlement resources when an event occurs.

The event that results in the recognition of an asset and revenue by a settling government is the domestic shipment of cigarettes. The TB indicates that accruals should be made by the settling government and TSAs for estimated shipments from January 1 to their respective fiscal year-ends, since the annual payments are based on a calendar year. However, under the modified-accrual basis of accounting at the fund level, revenue should be recognized only to the extent that resources are available.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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In accordance with the TB, a receivable of \$40,584,528 was recorded for estimated shipments from January 1, 2012 to June 30, 2012, which will be utilized for debt service upon collection. Additionally, the TB indicates that the TSA should recognize a liability for the bonds payable and an expense (and a liability if unpaid) in the same period in its stand-alone financial statements. The expense (and liability if unpaid) recognizes the contractual obligation to remit the proceeds to the settling government. Finally, the TB addresses the question of how the settling governments should report the receipt of the resources provided by the TSA's remittances of the proceeds of the bonds sold. Since the TSA should be reported as a blended component unit, the TB indicates these remittances should be reported as transfers into the fund receiving the proceeds and transfers out in the fund that accounts for the activities of the TSA.

Since the Trust has no contractual obligation, under its enabling legislation or elsewhere, to remit all bond proceeds or assets related to the GSA to the settling government (the Commonwealth), the Trust has not recognized an expense and liability for unpaid proceeds from the bonds since it records expenses as amounts are disbursed for grants to its settling government (including its instrumentalities) or third parties.

The GASB has issued the following accounting pronouncements that have effective date after June 30, 2012:

- (a) GASB Statements No. 65, *Items Previously Reported as Assets and Liabilities*, which is effective for fiscal years beginning after December 15, 2012.
- (b) GASB Statements No. 66, *Technical Corrections-2012 - an amendment of GASB Statements No. 10 and No. 62*, which is effective for fiscal years beginning after December 15, 2012.
- (c) GASB Statements No. 67, *Financial Reporting for Pension Plans - and amendment of GASB Statement No. 25*, which is effective for fiscal years beginning after June 15, 2013.
- (d) GASB Statements No. 68, *Accounting and Financial Reporting for Pensions - an amendment of GASB Statements No. 27*, which is effective for fiscal years beginning after June 15, 2014.

The impact of these pronouncements in the Trust's financial statements has not yet been determined.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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**3. CUSTODIAL CREDIT RISK**

Custodial credit risk is the risk that in the event of a bank failure, the Trust's deposits may not be returned. The Trust does not have a deposit policy for custodial credit risk. As of June 30, 2012, all of the Trust's depository bank balance, aggregating approximately \$20,427,000, was exposed to custodial credit risk since such deposits, all of which are maintained at the Bank, are uninsured and uncollateralized.

**4. TRANSACTIONS WITH GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO**

As described in Note 1, the Bank acts as the trustee of the Trust and the Trust's personnel are provided by the Bank. During the year ended June 30, 2012, the Bank provided certain management and administrative services to the Trust for \$200,000 under a management contract.

**5. INVESTMENTS AND INVESTMENT CONTRACTS**

In accordance with investment guidelines promulgated by the Bank for agencies and public corporations of the Commonwealth under the authority provided by Act No. 113 of August 3, 1995, and Executive Order 1995-50A (the "investment guidelines"), the Trust is authorized to purchase or enter into the following investment instruments:

- United States government and agencies obligations
- Certificates of deposit
- Bankers' acceptances
- Commercial paper
- Participations in the Puerto Rico Government Investment Trust Fund
- Obligations of the Commonwealth, its agencies, municipalities, public corporations, and instrumentalities
- Obligations of state and local governments of the United States of America
- Mortgage and asset-backed securities
- Corporate debt, including investment contracts
- External investment pools



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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The investment guidelines also establish limitations and other guidelines.

Investments consist of a guaranteed investment contract of \$83,684,235 with Bayerische Hypo-und Vereinsbank AG; external investments pools of \$49,971,418, which includes \$23,200,841 invested in Puerto Rico Government Investment Trust Fund (PRGITF) (an internal investment pool of the Commonwealth) and \$26,770,577 invested with Deutsche Bank Trust Company Americas; and State and Local Government securities issued by the United States Treasury Department of \$66,772.

As of June 30, 2012, the rating of PRGITF was AAAM by Standard & Poor's. The rating of Deutsche Bank Trust Company Americas was A+/Neg/A-1 by Standard & Poor's and, the rating of Bayerische Hypo-und Vereinsbank AG was A/Neg/A-1 with Standard & Poor's.

Investment in guaranteed investment contracts represents 63% of the Trust's investments. In addition, this investment is held by the counterparty, not in the name of the Trust.

**6. BONDS PAYABLE**

On October 10, 2002, the Trust refunded its then outstanding \$390,170,000 Tobacco Settlement Asset Backed Bonds, Series 2000 dated as of October 1, 2000, with new 2002 Series bonds (the "Series 2002 Bonds") in the amount of \$1,171,200,000.

As of June 30, 2012, the outstanding balance of these bonds consist of \$32,770,000 serial bonds maturing from May 15, 2013 to 2014 bearing interest at rates ranging from 4.10% to 4.25%, and single rated term bonds (the "Term Bonds") maturing from May 15, 2021 to 2033 (\$342,775,000 at 5.375%), from May 15, 2034 to 2039 (\$310,380,000 at 5.5%) and from May 15, 2040 to 2043 (\$296,255,000 at 5.625%).

The Term Bonds are subject to mandatory redemption in whole or in part prior to their respective stated maturity dates from Surplus Collections, as defined, on each Distribution Date at the redemption price of 100% of the principal amount thereof together with interest accrued thereon to the date fixed for redemption. The Term Bonds are subject to Turbo Redemption, as defined, in order of maturity.

On June 30, 2005, the Trust issued a new series of Tobacco Settlement Asset-Backed Bonds, Series 2005A and 2005B (the "Series 2005A and 2005B Bonds"), for \$108,209,446. The Series 2005A and 2005B consist of term bonds maturing on May 15, 2050 (\$74,523,430 at 6.50%), plus accreted interest and May 15, 2055 (\$33,686,016 at 7.25%), plus accreted interest, respectively. As of June 30, 2012, the outstanding balances of Series 2005A and 2005B consist of \$116,626,045 and \$55,463,233 respectively.

On April 30, 2008, the Trust issued a new series of Tobacco Settlement Asset-Backed Bonds, Series 2008A and 2008B (the "Series 2008A and 2008B Bonds"), for \$195,878,970. The Series 2008A and 2008B consist of term bonds maturing on May 15, 2057 (\$139,003,082 at 7.625%), plus accreted interest and May 15, 2057 (\$56,875,888 at 8.375%), plus accreted interest, respectively. As of June 30,



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

2012, the outstanding balances of Series 2008A and 2008B consist of \$189,847,224 and \$80,052,256 respectively.

The Series 2008A and 2008B Bonds are subordinated to the Trust's Tobacco Settlement Asset-Backed Bonds, and are not entitled to receive any payments until the date when the Series 2002 Bonds and the Series 2005 Bonds are no longer outstanding. In addition, the Series 2008B Bonds are subordinated to the Series 2008A Bonds and are not entitled to receive any payments until the date when the Series 2008A Bonds are no longer outstanding. The bonds are secured by 100% of the annual payments received by the Commonwealth under the Agreement.

Changes in bonds payable for the year ended June 30, 2012 are summarized as follow (in thousands):

	Balance at June 30, 2011	Debt Issued	Debt Paid	Increase (Decrease)	Balance at June 30, 2012	Due Within One Year
Bonds payable	\$ 1,415,205	\$ -	\$(22,060)	\$ 31,024	\$ 1,424,169	\$ 15,505
Less:						
Unaccreted bond discount	(24,942)			1,535	(23,407)	1,438
Unamortized deferred loss on advance refunding of bonds	(33,419)			2,964	(30,455)	2,964
Bonds payable	<u>\$ 1,356,844</u>	<u>\$ -</u>	<u>\$(22,060)</u>	<u>\$ 35,523</u>	<u>\$ 1,370,307</u>	<u>\$ 19,907</u>



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

As of June 30, 2012, debt service requirements for bonds outstanding were as follow (in thousands):

Year Ending June 30,	Principal	Interest	Total
2013	\$ 15,505	\$ 53,529	\$ 69,034
2014	17,265	52,893	70,158
2015	-	52,159	52,159
2016	-	52,159	52,159
2017	-	52,159	52,159
2018-2022	25,280	260,508	285,788
2023-2027	508,692	242,328	751,020
2028-2032	196,720	206,126	402,846
2033-2037	230,135	156,019	386,154
2038-2042	334,210	81,782	415,992
2043-2047	81,395	4,579	85,974
2048-2052	-	-	-
2053-2057	-	-	-
2057	-	-	-
	<u>8,634,580</u>	<u>-</u>	<u>8,634,580</u>
	10,043,782	<u>\$ 1,214,241</u>	<u>\$ 11,258,023</u>
Less:			
Unaccreted discount	23,407		
Unamortized deferred loss on advanced refunding on bonds	30,455		
Unaccreted interest	<u>8,619,613</u>		
	<u>\$ 1,370,307</u>		

**7. COMMITMENTS**

At June 30, 2012, the Trust had approved commitments to provide assistance to several entities through forty-five contracts with balances amounting to approximately \$27,774,000.

**8. GLOBAL SETTLEMENT AGREEMENT**

On November 23, 1998, the Agreement was entered into by and between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The Agreement calls for annual payments through the year 2025 which will vary due to



**THE CHILDREN'S TRUST**  
 (A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

inflationary and volume adjustments. After 2025, the tobacco companies shall continue making contributions in perpetuity.

Following is a summary of estimated payments to be received by the Trust through the year ending June 30, 2025 (unaudited, in thousands):

Year Ending June 30,	Amount
2013	
2014	\$ 80,809
2015	81,698
2016	82,562
2017	83,588
2018-2025	84,617
	<u>799,049</u>
Amount to be collected through the year ending June 30, 2025	<u>\$ 1,212,323</u>

Actual collections from the Agreement will fluctuate due to future cigarette consumption, which could be affected by factors such as inflation, demographics, cigarette prices, disposable income, employment, advertising expenditures, and regulations, among others. During 2012 and 2011, actual collections were \$72,490,828 and \$71,096,520 respectively, 9.07% less than the projected amount in the official statement for the year 2012, and for the year 2011 it was 9.9% less than the projected amount in the official statement for year 2011.

All of the revenue received under the Agreement and investment earnings on certain accounts under the bond indentures are pledged as collateral for the following bond issuances:

- Tobacco Settlement Asset — Backed Bonds, Series 2002
- Tobacco Settlement Asset — Backed Bonds, Series 2005
- Tobacco Settlement Asset — Backed Bonds, Series 2008

As of June 30, 2012, the approximate amount of the pledge is \$1,370,000,000 representing the approximate remaining principal and interest of bond issuances, which are committed through May 15, 2057. Accordingly, until May 15, 2057, such revenues are not available for other purposes.

Amounts received under the bond issuances were used to finance programs aimed at promoting a better quality of life and the well-being of families, children, and youth in Puerto Rico especially in the areas of education, recreation and health in form of grants. In addition, part of the proceeds from the Series 2008A and 2008B Bonds were used to pay certain operating expenses of the Commonwealth.



**THE CHILDREN'S TRUST**  
(A Component Unit of the Commonwealth of Puerto Rico)

**NOTES TO BASIC FINANCIAL STATEMENTS**  
**AS OF AND FOR THE YEAR ENDED JUNE 30, 2012**

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During the year ended June 30, 2012, pledged revenues amounted to \$72,479,588 (net of operating expenses of \$11,240), which were used to pay for \$76,534,517 of related principal and interest of the bond issuances.

**9. INTERGOVERNMENTAL GRANTS**

The detail of intergovernmental grants for the year ended on June 30, 2012 is as follows (in thousands):

<b>Description</b>	<b>Amount</b>
Public Buildings Authority	\$ 139
Department of Transportation and Public Works	181
Office for the Improvement of Public Schools	<u>341</u>
	<u>\$ 661</u>

**10. DATE OF MANAGEMENT'S REVIEW**

Subsequent events were evaluated through September 28, 2012, the date the financial statements were available to be issued, to determine if any such events should either be recognized or disclosed in the 2012 financial statements.

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