AUDITED FINANCIAL STATEMENTS

University of Puerto Rico
Year Ended June 30, 2008
With Report of Independent Auditors

ERNST & YOUNG

University of Puerto Rico

Audited Financial Statements

Years Ended June 30, 2008 and 2007

Contents

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Report of Independent Auditors

Board of Trustees
University of Puerto Rico

We have audited the accompanying financial statements of the business-type activities and the aggregate discretely presented component units of the University of Puerto Rico (the University), a component unit of the Commonwealth of Puerto Rico, as of and for the years ended June 30, 2008 and 2007, which collectively comprise the University's financial statements, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audits. We did not audit the financial statements of Servicios Médicos Universitarios, Inc. (the Hospital) and Desarrollos Universitarios, Inc. (the Company), which represent 100% of the aggregate discretely presented component units, as of and for the years ended June 30, 2008 and 2007 and March 31, 2008 and 2007, respectively. Those financial statements were audited by other auditors whose reports thereon have been furnished to us. The Hospital's report included an explanatory paragraph stating that it has experienced recurring losses since it commenced operations and has a net capital deficiency, and this raises substantial doubt about its ability to continue as a going concern. Our opinion, insofar as it relates to amounts included for the Hospital and the Company, is solely based on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the University's internal control over financial reporting. Our audit included 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 University'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, and evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the University of Puerto Rico and the aggregate discretely presented component units of the University of Puerto Rico as of June 30, 2008 and 2007, and the respective changes in financial position and cash flows thereon for the years then ended in conformity with accounting principles generally accepted in the United States.

As discussed in Note 1 to the financial statements, effective July 1, 2007, the University changed its accounting policy related to accounting for its other post-employment benefits to comply with the provisions of Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.*

As discussed in Note 13 to the financial statements, the Hospital has experienced recurring losses since it commenced operations and has a net capital deficiency, this raises substantial doubt about its ability to continue as a going concern.

In accordance with *Government Auditing Standards*, we have also issued our report, dated June 5, 2009, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Management's Discussion and Analysis and the Schedule of Funding Progress of the University of Puerto Rico Retirement System, as listed in the table of contents, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the University of Puerto Rico financial statements. The schedule of changes in sinking fund reserves included in page 58 is presented for purposes of additional analysis and is not a required part of the financial statements. The schedule of changes in sinking fund reserves has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, are fairly stated in all material respects in relation to the financial statements taken as a whole.

Ernst & Young LLP

June 9, 2009

Stamp No. 2410340
affixed to
original of
this report.

Introduction

The following discussion presents an overview of the financial position and financial activities of the University of Puerto Rico (the University) for the years ended June 30, 2008 and 2007. This discussion and analysis was prepared by University management and should be read in conjunction with the financial statements and notes thereto, which follow.

The financial operations and position of two not-for-profit organizations, Servicios Médicos Universitarios, Inc. and Desarrollos Universitarios, Inc. are considered component units of the University and are discretely presented in the University's financial statements. An annual audit of each organization's financial statement is conducted by independent certified public accountants. Financial statements and information relating to the component units may be obtained from their respective administrative officers.

Financial Highlights

The financial position of the University remains strong at June 30, 2008, with total assets of $1,495,128,612, total liabilities of $1,069,106,547 and net assets of $426,022,065. The University's net assets decreased ($697,806) during the year ended June 30, 2008, when compared to the year ended June 30, 2007. These changes are explained in the section entitled "Analysis of Financial Position and Changes in Financial Position." An overview of the statements is presented below along with a financial analysis of the transactions impacting the statements.

Condensed financial statements for the University as of and for the years ended June 30, 2008, 2007 and 2006 follow:

Condensed Statements of Net Assets

	June 30 2008	2007	2006
Assets			
Current assets	**$ 292,427,106**	$ 344,095,972	$ 341,443,766
Noncurrent assets:			
Due from Commonwealth of Puerto Rico	**96,770,389**	84,232,509	56,000,001
Capital assets	**834,398,195**	796,685,602	659,326,528
Other assets	**271,532,922**	258,215,364	81,705,901
Total assets	**1,495,128,612**	1,483,229,447	1,138,476,196
Liabilities			
Current liabilities	**144,435,900**	133,037,509	199,479,385
Noncurrent liabilities	**924,670,647**	923,472,066	552,867,652
Total liabilities	**1,069,106,547**	1,056,509,575	752,347,037
Net assets			
Invested in capital assets net of related debt	**275,018,751**	231,026,259	207,167,597
Restricted:			
Nonexpendable	**65,446,685**	62,406,256	52,247,594
Expendable	**86,479,410**	120,847,524	113,179,703
Unrestricted	**(922,781)**	12,439,834	13,534,265
Total net assets	**$ 426,022,065**	$ 426,719,873	$ 386,129,159

Condensed Statements of Revenues, Expenses and Changes in Net Assets

	Year Ended June 30		
	2008	**2007**	**2006**
Operating revenues			
Tuition and fees (net of scholarship)	**$ 51,286,439**	$ 49,269,042	$ 51,115,866
Grants and contracts	**140,464,523**	148,409,147	133,858,642
Patient services	**48,665,826**	48,669,981	49,667,252
Other operating revenues	**37,860,307**	39,919,317	45,743,758
Total operating revenues	**278,277,095**	286,267,487	280,385,518
Operating expenses	**1,351,283,567**	1,266,523,365	1,196,233,066
Operating loss	**(1,073,006,472)**	(980,255,878)	(915,847,548)
Nonoperating revenues and expenses			
State appropriations	**935,880,735**	896,492,596	854,981,674
Other nonoperating revenues and expenses, including interest on indebness	**116,162,315**	104,908,125	125,315,363
Net nonoperating revenues	**1,052,043,050**	1,001,400,721	980,297,037
(Loss) income before other revenues	**(20,963,422)**	21,144,843	64,449,489
Capital appropriations	**17,576,892**	12,607,556	10,160,608
Addition to permanent endowment	**2,688,724**	6,838,313	3,865,074
Total increase/decrease in net assets	**$ (697,806)**	$ 40,590,712	$ 78,475,171

Using the Financial Statements

The University's financial statements were prepared in accordance with standards issued by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments.* This was followed in November 1999 by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities – an amendment of GASB Statement No. 34.* The financial statement presentation required by GASB Statements No. 34 and 35 provides a comprehensive, entity-wide perspective of the University's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Analysis of Financial Position and Changes in Financial Position

Statements of Net Assets

The statements of net assets present the assets, liabilities and net assets of the University as of June 30, 2008 and 2007. The net assets are displayed in three parts, invested in capital assets net of related debt, restricted and unrestricted. Restricted net assets may either be expendable or nonexpendable and are those assets that are restricted by law or by an external donor. Unrestricted net assets, while they are generally designated for specific purposes, are available for use by the University to meet current expenses for any purposes. The statements of net assets, along with all of the University's basic financial statements, are prepared under the accrual basis of accounting, whereby revenues are recognized when the service is provided by and expenses are recognized when others provide the service to the University, regardless of when cash is exchanged.

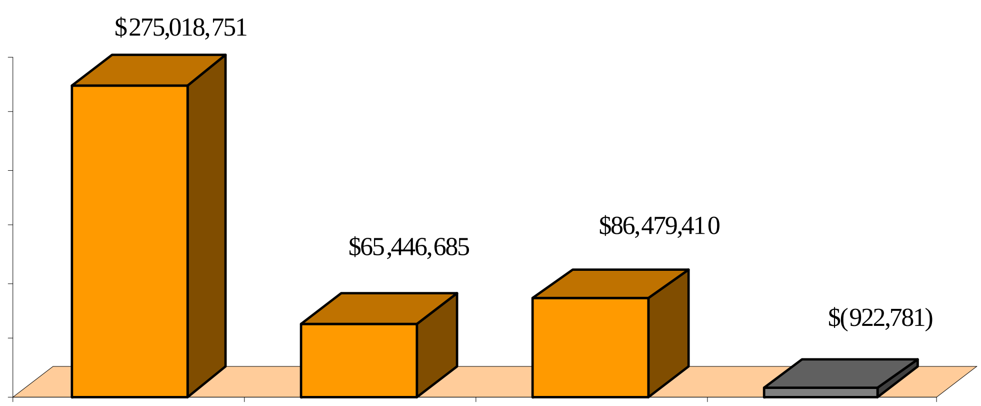
Assets included in the statements of net assets are classified as current or noncurrent. Current assets consist primarily of cash and cash equivalents, short-term investments and accounts receivable. Of these amounts, cash and cash equivalents, investments and accounts receivable comprise approximately 6%, 38% and 54%, respectively, of current assets and 69% of noncurrent assets are capital assets as of June 30, 2008. As of June 30, 2007, these amounts comprise approximately 14%, 35% and 46% of current assets and 70% of noncurrent assets are capital assets. As of June 30, 2006, these amounts comprise approximately 26%, 29% and 42% of current assets and 83% of noncurrent assets are capital assets.

The University's cash, cash equivalents and investments increased from $239,586,325 at June 30, 2006 to $414,403,362 at June 30, 2007 and decreased to $356,401,170 at June 30, 2008. The decrease in investments at fair value is mainly caused by the decrease in market value. Current accounts receivable decreased from $159,522,765 to $158,213,051.

Current liabilities consist primarily of accounts payable and accrued liabilities and the current portion of long-term debt. Accounts payable and accrued liabilities increased from $85,079,562 to $93,117,021 between June 30, 2007 and 2008. Non-current liabilities consist primarily of bonded indebtedness. Long-term debt, net of current portion, decreased from $656,019,072 to $652,511,547 between June 30, 2008 and 2007.

Net assets represent the residual interest in the University's assets after liabilities are deducted. The major classifications of the net assets are shown in the following illustration:

Table 1 - Net Assets - June 30, 2008



Invested in Capital Assets	$	275,018,751
Restricted Nonexpendable		65,446,685
Restricted Expendable		86,479,410
Unrestricted		(922,781)

Net assets invested in capital assets, net of related debt, represent the University's capital assets less accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

Restricted nonexpendable net assets consist primarily of the University's permanent endowment funds. The corpus of these funds may not be expended and must remain with the University in perpetuity. Only the earnings from these funds may be expended. Restricted expendable net assets are subject to externally imposed restrictions governing their use. The funds are restricted primarily for debt service, capital projects, student loans and scholarship purposes.

Unrestricted net assets represent those balances from operational activities that have not been restricted by parties external to the University such as donors or grant agencies.

Statements of Revenues, Expenses and Changes in Net Assets

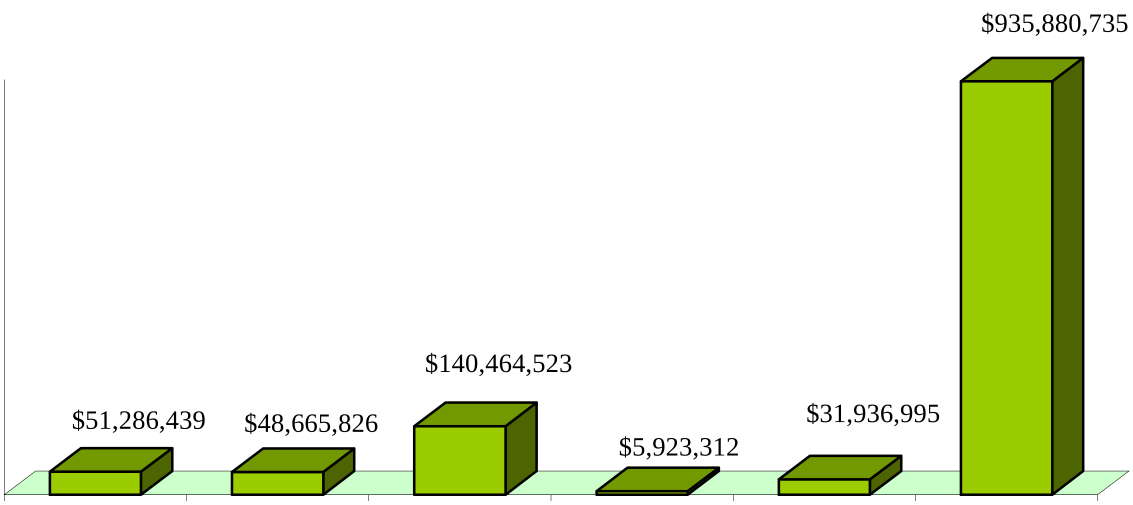
Changes in total University net assets as presented in the statements of net assets are based on the activity presented in the statements of revenues, expenses and changes in net assets. The purpose of these statements are to present the revenues earned by the University, both operating and nonoperating, and the expenses paid and accrued by the University and any other revenues, expenses, gains and losses received or spent by the University.

Generally, operating revenues are received to provide goods and services to the various customers and constituencies of the University. Operating expenses are those expenses paid to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the University. Nonoperating revenues are revenues received for which goods and services are not provided.

Approximately 89% of the operating revenues and non-operating revenues of the University are Federal and Commonwealth appropriations, grants and contracts. The remainder consists primarily of tuition and fees and patient services.

The following illustration presents the major sources of the University revenues (both operating and nonoperating) for the year ended June 30, 2008:

Table 2 - Revenues - Year Ended June 30, 2008

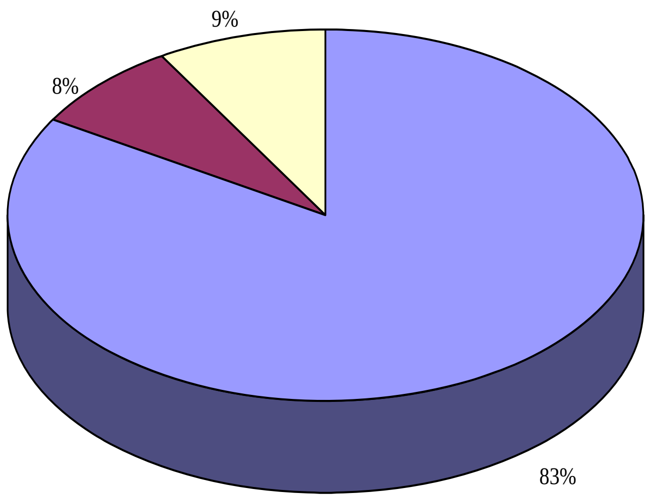


Operating and Nonoperating Revenues

Tuitions & Fees (net of scholarship)	$	51,286,439
Patient services		48,668,826
State and Federal Grants & Contracts		140,464,523
Auxiliary Enterprises		5,923,312
Other Operating Revenues		31,936,995
Commonwealth Appropriations		935,880,735

Federal grants represent 83% of the University grants revenues. The following illustration presents the grants revenues of the University of Puerto Rico, year ended June 30, 2008:

Table 3 - Analysis of Grants Revenues

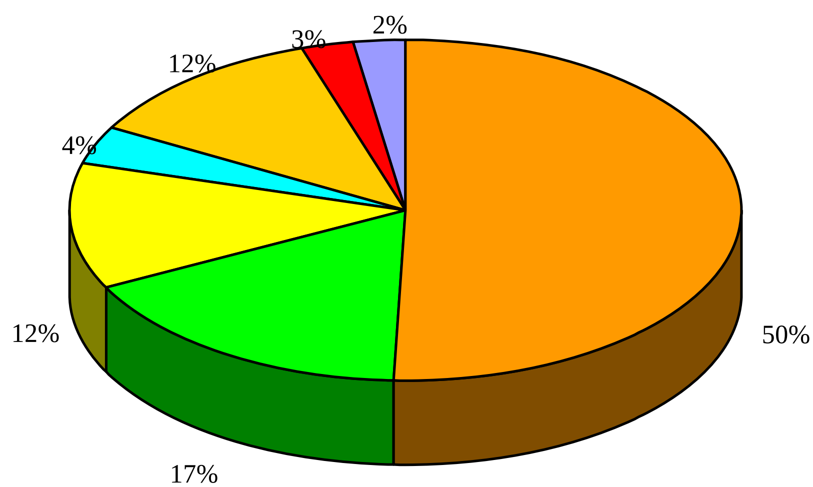


Federal	$	128,404,162	83%
Commonwealth		12,060,361	8%
Other		13,329,915	9%

University expenses are presented using natural expense classifications. Salaries and benefits represent 69% of the University's operating expenses.

The following illustration presents the major University operating expenses, using natural classification for the year ended June 30, 2008:

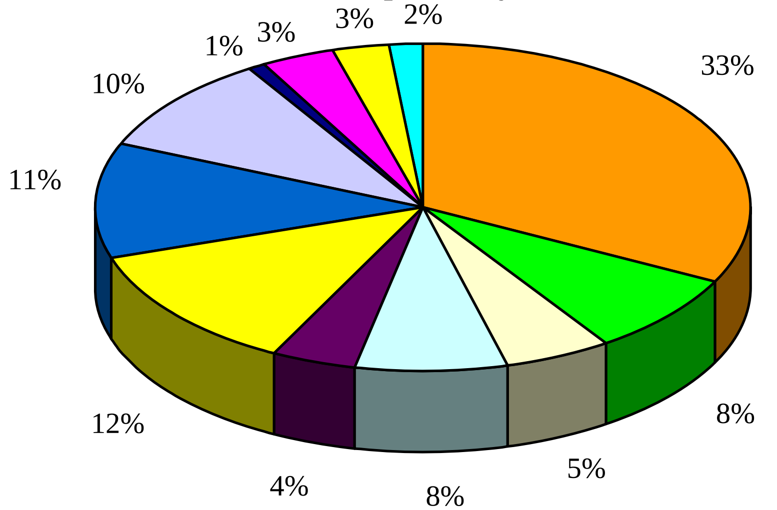
Table 4 - Operating Expenses



Salaries	$	682,306,485	50%
Benefits		230,017,087	17%
Scholarship and other services		160,492,568	12%
Utilites		49,147,600	4%
Supplies and other services		160,098,118	12%
Depreciation		37,125,069	3%
Other expenditures		32,096,640	2%

Functional expense classification presents University expenses in the operational categories they benefit. The following illustration presents the major uses of University revenues (both operating and nonoperating) on a functional basis for the year ended June 30, 2008:

Table 5 - Expenses by Function



Instruction	$	440,662,362	33%
Research		107,219,612	8%
Public Service		70,878,920	5%
Academic Support		101,861,929	8%
Student Services		57,002,998	4%
Institutional Support		166,842,002	12%
Operation and Maintenance of Plant		155,196,511	11%
Scholarships and Fellowships		132,763,706	10%
Auxiliary Enterprises		11,292,906	1%
Patient Service		46,740,070	3%
Depreciation		37,125,069	3%
Other		23,697,480	2%

For the year ended June 30, 2008, the University reported an operating loss of $1,073,006,472. After adding nonoperating revenues and expenses, primarily state appropriations and Federal Pell Grant, the total decrease in net assets for the year amounted to $(697,806).

Statements of Cash Flows

The Statements of Cash Flows present information related to cash flows of the University by the following categories: operating activities, noncapital financing activities, capital and related financing activities and investing activities.

Increases in cash and cash equivalents from noncapital financing activities were due primarily to the receipt of state appropriations. This increase was offset by decreases in cash and cash equivalents from investing activities resulting from purchases of short-term investments, decreases in cash and cash equivalents used for capital and related financing activities and cash used in operating activities. Cash and cash equivalents decrease from capital and related financing activities was due primarily to purchases of capital assets and payments of principal and interest on debt. The decrease in cash and cash equivalents from operating activities is consistent with the University's operating loss.

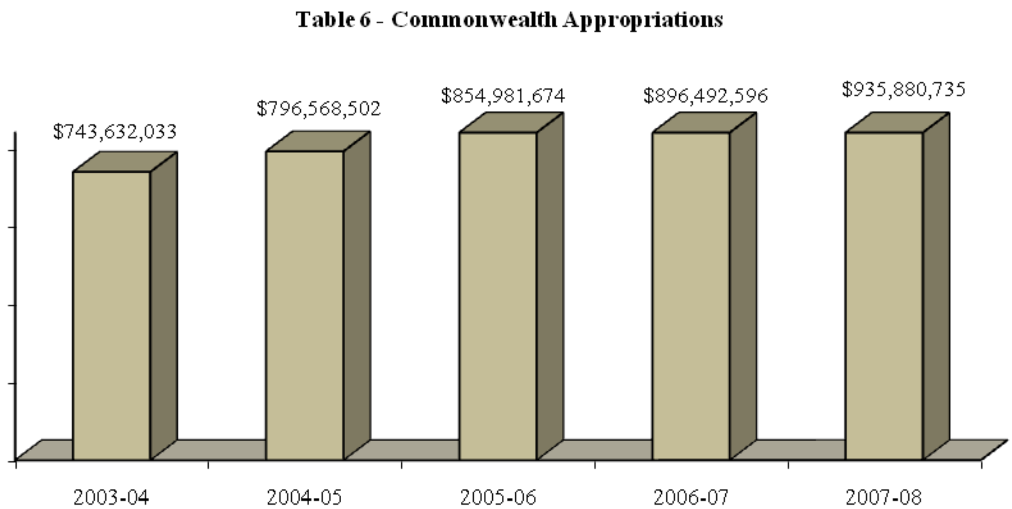
Capital Assets and Debt Administration

Significant capital assets additions for the year ended June 30, 2008 and 2007, consist mainly of renovation and rehabilitation of existing facilities, restoration of historic buildings, and modifications of existing facilities in light of new technology, educational standards and the requirements of modern building codes.

Economic Outlook

The economy of Puerto Rico must be analyzed as a region within the U.S. economy, since it is part of the U.S. monetary and banking system, as well as within its territorial boundaries. The main drive of the Puerto Rican economy is a huge external sector closely tied to the flow of merchandise, tourists, and capital between Puerto Rico and the Mainland.

The Commonwealth appropriations for the last five years are illustrated below:



The University administration is not aware of any currently known facts, decisions or conditions that are expected to have a significant effect on the University's financial position or results of operation during fiscal year 2008 beyond those unknown variations having a global effect on virtually all types of business operations. While the University's overall financial position is strong, various factors influence the University's ultimate financial success.

Request for Information

This financial report is designed to provide a general overview of the University's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Director. The executive offices of the University are located at 1187 Flamboyan Street, Jardín Botánico Sur, San Juan, Puerto Rico 00926.

University of Puerto Rico
Statements of Net Assets

	June 30 2008	June 30 2007
Assets		
Current assets:		
Cash and cash equivalents	**$ 19,167,865**	$ 49,595,830
Investments at fair value	**56,187,238**	64,851,571
Investments with bond trustees at fair value	**54,485,622**	58,233,345
Accounts receivable (less allowances for doubtful accounts of $132,409,296 and $106,514,050 for 2008 and 2007, respectively)	**158,213,051**	159,522,765
Due from Commonwealth of Puerto Rico	**7,570,127**	8,155,254
Inventories	**3,798,653**	4,882,571
Prepaid expenses and deferred charges	**574,677**	7,009,890
Total current assets	**299,997,233**	352,251,226
Noncurrent assets:		
Restricted cash and cash equivalents	**5,826,799**	4,544,892
Investments at fair value	**220,733,646**	237,177,724
Due from Commonwealth of Puerto Rico	**89,200,262**	76,077,255
Prepaid expenses and other assets	**42,628,122**	13,772,652
Notes receivable, net	**2,344,355**	2,720,096
Capital assets (net of accumulated depreciation of $441,681,276 and $411,324,335 for 2008 and 2007, respectively)	**834,398,195**	796,685,602
Total noncurrent assets	**1,195,131,379**	1,130,978,221
Total assets	**1,495,128,612**	1,483,229,447
Liabilities		
Current liabilities:		
Accounts payable and accrued liabilities	**93,117,021**	85,079,562
Current portion of long-term debt	**21,455,000**	19,760,000
Obligation under capital lease, current portion	**1,063,344**	2,178,105
Other current liabilities	**28,800,535**	26,019,842
Total current liabilities	**144,435,900**	133,037,509
Noncurrent liabilities:		
Long-term debt, net of current portion	**652,511,547**	656,019,072
Obligation under capital lease, noncurrent portion	**68,649,242**	68,597,825
Other long-term liabilities	**203,509,858**	198,855,169
Total noncurrent liabilities	**924,670,647**	923,472,066
Total liabilities	**1,069,106,547**	1,056,509,575

(Continues)

Net assets		
Invested in capital assets, net of related debt	**275,018,751**	231,026,259
Restricted, nonexpendable:		
Scholarship and fellowships	**42,774,078**	39,560,872
Research	**18,942,504**	19,080,230
Other	**3,730,103**	3,765,154
Restricted, expendable:		
Research	**18,659,467**	20,946,073
Loans	**7,948,550**	7,685,906
Capital projects	**1,948,575**	24,791,044
Debt service	**51,875,735**	56,233,963
Other	**6,047,083**	11,190,537
Unrestricted	**(922,781)**	12,439,834
Total net assets	**$ 426,022,065**	$ 426,719,872

See accompanying notes.

University of Puerto Rico
Statements of Revenues, Expenses and Changes in Net Assets

	June 30 2008	June 30 2007
Revenues		
Operating revenues:		
Tuitions and fees (net of scholarship allowances of $41,390,629 and $37,277,970 for 2008 and 2007, respectively)	**$ 51,286,439**	$ 49,269,042
Net hospital patient services and other	**48,665,826**	48,669,981
Federal grants and contracts	**128,404,162**	125,667,791
Commonwealth grants and contracts (net of allowances of $6,895,713 and $4,985,386 for 2008 and 2007, respectively)	**12,060,361**	22,741,356
Nongovernmental grants and contracts	**13,329,915**	14,753,879
Sales and services of educational departments	**5,379,271**	4,316,666
Auxiliary enterprises (net of scholarship allowances of $159,257 and $162,750 for 2008 and 2007, respectively)	**5,923,312**	7,157,572
Other operating revenues	**13,227,809**	13,691,200
Total operating revenues	**278,277,095**	286,267,487
Operating Expenses		
Salaries:		
Faculty	**396,824,902**	377,460,983
Exempt staff	**284,370,248**	272,900,601
Nonexempt wages	**1,111,335**	1,656,715
Benefits	**230,017,087**	218,195,408
Scholarship and fellowship	**160,492,568**	150,573,298
Utilities	**49,147,600**	44,530,281
Supplies and other services	**160,098,118**	149,551,732
Depreciation	**37,125,069**	33,774,910
Other expenses	**32,096,640**	17,879,437
Total operating expenses	**1,351,283,567**	1,266,523,365
Operating loss	**(1,073,006,472)**	(980,255,878)
Nonoperating revenues (expenses):		
Commonwealth appropriations	**935,880,735**	896,492,596
Federal Pell Grant program	**121,234,272**	109,492,991
Gifts	**6,279,553**	6,461,769
Net investment income	**4,774,072**	9,116,461
Interest on indebtedness	**(18,607,741)**	(20,812,346)
Other nonoperating revenues	**2,482,159**	649,250
Net nonoperating revenues	**1,052,043,050**	1,001,400,721
(Loss) income before other revenues	**(20,963,422)**	21,144,843
Capital appropriations	**17,576,892**	12,607,556
Additions to term and permanent endowment	**2,688,724**	6,838,313
(Decrease) increase in net assets	**(697,806)**	40,590,712
Net Assets		
Beginning of year	**426,719,871**	386,129,159
End of year	**$ 426,022,065**	$ 426,719,871

See accompanying notes.

University of Puerto Rico
Statements of Cash Flows

	Year Ended June 30	
	2008	**2007**
Cash flows from operating activities		
Tuition and fees	**$ 50,867,832**	$ 49,253,880
Grants and contracts	**142,566,272**	157,423,396
Pell grants	**121,234,272**	109,492,991
Patient services	**48,665,826**	48,669,981
Auxiliary enterprises	**5,926,805**	6,857,754
Sales and services educational departments and other	**18,607,080**	4,358,816
Payments to suppliers and vendors	**(176,721,917)**	(63,480,929)
Payments to employees	**(682,306,485)**	(651,271,784)
Payments for utilities	**(49,147,600)**	(44,044,748)
Payments for benefits	**(230,017,087)**	(140,576,178)
Payments for scholarships and fellowships	**(160,492,568)**	(150,677,612)
New loans issued to students	**(773,384)**	(1,297,397)
Student loan repayments	**1,166,043**	1,046,166
Other payments	**(2,338,352)**	(30,361,913)
Net cash used in operating activities	**(912,763,263)**	(704,607,577)
Cash flows from noncapital financing activities		
Commonwealth appropriations	**935,880,735**	896,492,595
Endowment gifts	**2,688,724**	6,838,313
Gifts and grants for other than capital purposes	**3,899,829**	7,111,019
Net cash provided by noncapital financing activities	**942,469,288**	910,441,927
Cash flows from capital and related financing activities		
Capital appropriations	**17,576,892**	12,607,555
Additions of capital assets	**(76,453,802)**	(172,561,024)
Principal paid on indebtness	**(20,355,173)**	(292,474,805)
Interest paid on capital indebtness	**(18,607,741)**	(20,812,346)
Deposit with trustee	**3,747,723**	(19,117,090)
Capital lease	**(1,063,344)**	(70,775,930)
Proceeds from capital debt	**6,420,879**	503,882,775
Net cash used in capital and related financing activities	**(88,734,566)**	(59,250,865)
Cash flows from investing activities		
Proceeds from sales and maturities of investments	**47,532,056**	36,058,961
Purchase of investments	**(22,423,645)**	(228,742,925)
Interest on investments	**4,774,072**	9,116,461
Net cash provided by (used in) investing activities	**29,882,483**	(183,567,503)
Net change in cash and cash equivalents	**(29,146,058)**	(36,984,018)
Cash and cash equivalents:		
Beginning of year	**54,140,722**	91,124,740
End of year	**$ 24,994,664**	$ 54,140,722

(Continues)

	Year Ended June 30	
	2008	**2007**
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	**$ (1,073,006,472)**	$ (980,255,878)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	**37,125,069**	33,774,910
Reduction of capital assets	**1,616,141**	1,427,039
Amortization on bond premium, discount and future appreciated principal	**2,863,442**	2,276,213
Changes in assets and liabilities, net:		
Grants and contracts receivables	**(11,228,166)**	66,662,920
Prepaid expenses, inventories and other	**(21,336,339)**	10,504,164
Accounts payable, accrued liabilities and capital lease	**15,472,841**	70,755,022
Accrued salaries and wages and other liabilities	**135,730,221**	90,248,033
Net cash used in operating activities	**$ (912,763,263)**	$ (704,607,577)

See accompanying notes.

Discretely Presented Component Unit
Servicios Médicos Universitarios, Inc.
(A Not-for Profit Organization)
Balance Sheets

	June 30 2008	June 30 2007
Assets		
Current assets:		
Cash	**$ 674,716**	$ 32,062
Patient accounts receivable, net of allowance for doubtful accounts of $21,260,231 in 2008 and $41,822,363 in 2007	**14,525,193**	14,367,224
Accounts receivable - other	**232,268**	180,173
Inventories of supplies	**1,605,671**	1,556,395
Prepaid expenses	**247,777**	252,272
Total current assets	**17,285,625**	16,388,126
Property and equipment, net	**4,677,296**	3,660,070
Total assets	**$ 21,962,921**	$ 20,048,196
Liabilities and deficiency in unrestricted net assets		
Current liabilities:		
Current portion of long term debt	**$ 15,367,611**	$ 15,367,611
Accounts payable	**24,946,113**	23,067,511
Accrued interest	**5,700,516**	4,767,455
Estimated third-party payor settlements-medicare	**675,570**	1,047,750
Accrued payroll taxes and employee benefits	**1,237,481**	1,181,499
Accrued expenses	**784,453**	1,717,360
Total current liabilities	**48,711,744**	47,149,186
Long-term debt, net of current portion	**1,632,389**	1,632,389
Due to related parties	**35,940,772**	34,800,479
Accrued claim losses	**1,015,551**	480,000
Total liabilities	**87,300,456**	84,062,054
Deficiency in unrestricted net assets	**(65,337,535)**	(64,013,858)
Total liabilities and deficiency in unrestricted net assets	**$ 21,962,921**	$ 20,048,196

See accompanying notes.

Discretely Presented Component Unit
Servicios Médicos Universitarios, Inc.
(A Not-for-Profit Organization)
Statements of Operations and Deficiency in Unrestricted Net Assets

	Year Ended June 30 2008	2007
Unrestriced revenues and other support		
Net patient service revenue	**$ 47,202,698**	$ 39,888,022
Contributions	**592,000**	–
Other revenue	**1,247,311**	1,705,766
Total revenues and other support	**49,042,009**	41,593,788
Expenses		
Salaries and benefits	**15,954,944**	17,379,152
Contracted services	**5,382,947**	3,238,090
Professional services	**1,333,232**	1,123,287
Supplies	**12,902,106**	12,853,696
Utilities	**2,493,003**	2,509,198
Interest	**1,160,177**	1,254,105
Provision for bad debts	**7,779,349**	8,434,671
Provision for claim losses	**650,000**	480,000
Depreciation and amortization	**1,005,093**	865,812
Other	**1,704,835**	1,826,988
Total expenses	**50,365,686**	49,964,999
Excess of expenses over revenue	**(1,323,677)**	(8,371,211)
Deficiency in unrestricted net assets, at beginning of year	**(64,013,858)**	(55,642,647)
Deficiency in unrestricted net assets, at end of year	**$ (65,337,535)**	$ (64,013,858)

See accompanying notes.

Discretely Presented Component Unit
Servicios Médicos Universitarios, Inc.
(A Not-for-Profit Organization)
Statements of Cash Flows

	Year Ended June 30	
	2008	**2007**
Cash flows from operating activities		
Change in unrestricted net assets	**$ (1,323,677)**	$ (8,371,211)
Adjustments to reconcile change in unrestricted net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	**1,005,093**	865,812
Provision for bad debts	**7,779,349**	8,434,671
Provision for claim losses	**650,000**	480,000
Increase in patient accounts receivable	**(7,937,317)**	(8,801,514)
(Increase) decrease in inventory of supplies	**(49,276)**	264,532
Decrease in prepaid expenses	**286,100**	465,483
Decrease (increase) in accounts receivable-other	**43,573**	(388,054)
Increase in accounts payable	**1,596,996**	3,041,995
Increase in estimated third-party payor settlements-Medicare	**(372,180)**	(777,510)
(Decrease) increase in accrued expenses, payroll taxes and employee benefits	**(876,925)**	1,563,238
Increase in accrued interest	**933,061**	1,086,300
Decrease in accrual claim	**(114,449)**	–
Total adjustments	**2,944,025**	6,234,953
Net cash provided by (used in) operating activities	**1,620,348**	(2,136,258)
Cash flows from investing actitivies		
Purchase of property and equipment	**(2,022,319)**	(657,968)
Cash flows from financing activities		
Net advances from University of Puerto Rico and other related parties	**1,044,625**	2,245,668
Net cash provided by financing activities	**1,044,625**	2,245,668
Net increase (decrease) in cash	**642,654**	(548,558)
Cash and cash equivalents, at beginning of year	**32,062**	580,620
Cash and cash equivalents, at end of year	**$ 674,716**	$ 32,062
Supplemental disclosures of cash flows information		
Cash paid for interest	**$ 91,395**	$ 78,762

See accompanying notes.

Discretely Presented Component Unit
Desarrollos Universitarios, Inc.
(A Not-for-Profit Organization)
Statements of Financial Position

	Year Ended March 31	
	2008	2007
Assets		
Current assets:		
Cash	**$ 971,892**	$ 2,013,630
Restricted cash	**320,790**	65,805
Restricted funds held by trustee	**9,814,784**	10,369,384
Net investment in direct financing lease	**70,165,021**	71,030,863
Due from the University of Puerto Rico	**3,397,623**	1,558,351
Prepaid expenses	**9,618**	95,579
Bond issuance costs, net of accumulated amortization of $31,656 and $451,765 in 2008 and 2007, respectively	**2,257,568**	2,337,459
Other assets	**24,163**	60,224
Total assets	**$ 86,961,459**	$ 87,531,295
Liabilities and net assets		
Liabilities:		
Construction contract, project management fee and other payables, including retaineage of $1,601,176 amd $1,663,995	**$ 1,784,507**	$ 2,497,062
Operating trade accounts payable	**137,370**	68,089
Accrued interest payable	**1,051,395**	1,066,245
Accrued expenses	**1,024,221**	797,452
Unearned student dormitories rental income	**23,101**	6,970
Student dormitories security deposits	**120,045**	29,345
Bonds payable, net of discount of $299,310 and $320,850 in 2008 and 2008, respectively	**80,880,690**	82,344,150
Total liabilities	**85,021,329**	86,809,313
Net assets	**1,940,130**	721,982
Total liabilities and net assets	**$ 86,961,459**	$ 87,531,295

See accompanying notes.

University of Puerto Rico
Desarrollos Universitarios, Inc.
(A Not-for-Profit Organization)
Statements of Activities and Changes in Net Assets

	Year Ended March 31	
	2008	2007
Revenues:		
Income from investment in direct financing lease	**$ 4,644,540**	$ 2,353,057
Fixed management fee	**758,000**	379,000
Reimbursable expenditures fee	**1,498,264**	1,209,366
Total revenues	**6,900,804**	3,941,423
Expenses:		
Project operation and maintenance	**1,593,647**	1,045,402
General and administrative	**324,626**	138,678
Total expenses	**1,918,273**	1,184,080
Other income (expenses):		
Interest and other financing, related expenses	**(4,287,033)**	(2,120,625)
Interest income	**522,650**	357,082
Total other expenses	**(3,764,383)**	(1,763,543)
Change in unrestricted net assets	**1,218,148**	993,800
Unrestricted net assets (deficiency) at beginning of year	**721,982**	(271,818)
Unrestricted net assets at end of year	**$ 1,940,130**	$ 721,982

See accompanying notes.

Statements of Cash Flows

	Year Ended March 31 2008	2007
Cash flows from operating activities		
Increase in net assets	**$ 1,218,148**	$ 993,800
Adjustments to reconcile excess of expenses over revenues to net cash used in operating activities:		
Bond discount amortization	**21,540**	22,842
Amortization of bond issuance cost	**79,891**	80,604
Adjustment to project cost transferred to the University of Puerto Rico under direct financing lease	**(191,087)**	–
Changes in operating assets and liabilities:		
Increase in restricted cash	**(254,985)**	(65,805)
Principal collected from direct financing lease	**1,056,929**	497,453
(Increase) decrease in due from University of Puerto Rico	**(1,839,272)**	(1,558,351)
Increase in project in process	**–**	(4,915,102)
(Increase) decrease in prepaid expenses	**85,961**	(587)
(Increase) decrease in other assets	**36,061**	(60,224)
Decrease in construction contract, project management fee and other payables	**(643,274)**	(679,834)
Decrease in accrued interest payable	**(14,850)**	(17,688)
Increase in accrued cost and expenses	**226,769**	392,816
Increase in unearned student dormitories rental income	**16,131**	6,970
Increase in student dormitories security deposits	**90,700**	29,345
Increase in unearned revenue	**–**	2,171,850
Net cash used in operating activities	**(111,338)**	(3,101,911)
Cash flows from investing activities		
Net proceeds from release of restricted funds held by trustee	**554,600**	4,097,134
Cash flows from financing activities		
Principal payments on bonds payable	**(1,485,000)**	(1,415,000)
Net change in cash	**(1,041,738)**	(419,777)
Cash at beginning of year	**2,013,630**	2,433,407
Cash at end of year	**$ 971,892**	$ 2,013,630

See accompanying notes.

1. Reporting Entity and Summary of Significant Accounting Policies

A. Reporting Entity

The University of Puerto Rico (the University) is a public corporation of the Commonwealth of Puerto Rico (the Commonwealth) governed by a thirteen-member Board of Trustees, of which ten are appointed by the Governor of Puerto Rico and confirmed by the Senate of Puerto Rico. The remaining members of the Board consist of one full-time student and two tenured professors. The Governor appointed the original members for terms from four to eight years. Upon expiration of their terms, the new members will be appointed for a period of six years. The terms for the student and professors are for one year.

The University is exempt from the payment of taxes on its revenues and properties. The University is a component unit of the Commonwealth.

The financial reporting entity of the University consists of the campuses at Río Piedras, Mayagüez, Medical Sciences, Cayey, Humacao, Ponce, Bayamón, Aguadilla, Arecibo, Carolina and Utuado, and the Central Administration.

Appropriations from the Commonwealth are the principal source of revenues of the University and are supported by Act No. 2 of January 20, 1966, as amended. Under the Act, the Commonwealth appropriates for the University an amount equal to 9.60% of the average total amount of annual general funds revenues collected under the laws of the Commonwealth in the two fiscal years immediately proceeding the current fiscal year. In addition, the Commonwealth has appropriated amounts for general current obligations, for capital improvement programs, and for loans and financial assistance to students.

Discretely Presented Component Unit Disclosures: A discretely presented component unit is an entity whose operations are separate from the University's but over whom the University has significant accountability. The University has two discretely presented component units as follows:

Servicios Médicos Universitarios, Inc.

Servicios Médicos Universitarios, Inc. (the Hospital) is legally separated entity from the University and is governed by a separate board. The Hospital is a not-for-profit acute care corporation, organized under the Laws of the Commonwealth of Puerto Rico, on February 11, 1998, to operate and administer healthcare units. The principal objectives of the Hospital are to constitute it as the principal medical education, institution of the University and to offer care services to the residents of Puerto Rico. The University appoints a voting majority of the Hospital board and is also financially accountable for the Hospital. Complete financial statements of the Hospital can be obtained directly by contacting the Hospital's administrative offices.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Desarrollos Universitarios, Inc.

Desarrollos Universitarios, Inc. (the Company) is a legally separated entity from the University and is governed by a separate board. The Company was organized on January 22, 1997, under the laws of the Commonwealth of Puerto Rico, as a not-for-profit organization. The Company was organized to develop, construct, and operate academic, residential, administrative, office, commercial, and maintenance facilities for the use of students and other persons or entities conducting business with the University of Puerto Rico (the University). The Company developed the Plaza Universitaria Project, which consist of a student housing facility, a multi-story parking building and an institutions building to house administrative, student service and support functions and to a lesser extent to lease commercial space. The financing for the Projects is being provided by the issuance of $86,735,000 in Educational Facilities Revenue Bonds through the Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority (AFICA) on December 20, 2000. In 2007 the University entered into a capital lease agreement with the Company for the Plaza Universitaria project. The Company is fiscally dependent on the University. Complete financial statements of the Company can be obtained directly by contacting the Company's administrative offices.

The following is a summary of the significant accounting policies followed by the University:

B. Measurement Focus and Basis of Accounting

For financial reporting purposes, the University is considered a special purpose governmental agency engaged only in business type activities, as defined by GASB Statement No. 34. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant transactions related to internal service activities such as publications, telecommunications and institutional computing have been eliminated where appropriate.

The University has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB pronouncements conflict with GASB pronouncements. The University has elected to not apply FASB pronouncements issued after the applicable date.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

C. Reclassifications

Reclassifications of prior year balances have been made to conform to the current year presentation.

D. Cash Equivalents

The University considers all highly liquid debt instruments with maturities of three months or less when purchased to be cash equivalents.

E. Investments

Investments are reported at fair value in the statements of net assets. Fair value is based on quoted market prices. The changes in the fair value of investments are reported in the statements of revenues, expenses and changes in net assets as a component of net investment income.

Donated investments are recorded at their fair value at the date of donation. Investments of the Deferred Compensation Plan are valued at fair value in order to measure the current liability attributable to plan participants.

F. Restricted Funds Held by Trustee – Discretely Presented Component Unit

Restricted funds of Desarrollos Universitarios, Inc. held by trustee at March 31, 2008 and 2007, consist of money market funds and zero coupon bonds purchased with remaining maturities of six months or less.

G. Capital Assets

All capital expenses of $1,000 or more and having a useful life of two or more years are capitalized at cost at the date of acquisition. Donated assets are recorded at estimated fair value at the date of donation. Depreciation is recorded using the straight-line method over the estimated useful lives of the assets, generally 25 to 50 years for buildings and infrastructure, 5 to 20 years for equipment and library materials, and 7 to 30 years for land improvements. Renovations to buildings and other assets that significantly increase the value or extend the useful life of the asset capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense has been incurred.

H. Inventories

Inventories are valued at the lower of first-in, first-out, cost or market and consist primarily of books.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

I. Classification of Net Assets

The University's net assets are classified as follows:

Invested in capital assets, net of related debt represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted, nonexpendable net assets consist of endowment and similar type funds which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

Restricted, expendable net assets include resources that the University is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, hospital revenues, sales and services of educational activities and auxiliary enterprises. Auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty and staff. While unrestricted net assets may be designated for specific purposes by action of management or the Board of Trustees, they are available for use, at the discretion of the governing board, to meet current expenses for any purpose. Substantially all unrestricted net assets are designated for academic and research programs and initiatives, and capital programs.

J. Scholarship Allowances and Student Financial Aid

Student tuition and fees, and certain other revenues from students, are recorded net of scholarship discounts and allowances in the statement of revenues, expenses and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants and other federal, state or nongovernmental programs, are recorded as operating revenues in the University's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and certain other student charges, the University has recorded a scholarship discount and allowance.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

K. Bond Premium/Discount, Deferred Issuance Costs and Deferred Refunding Loss

Bond premium and/or discount and deferred issuance costs are amortized using the effective interest method. Deferred refunding loss is amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter.

L. Deferred Compensation Plan

The University offers certain employees a non-qualified deferred compensation plan which was created pursuant to Certification No. 94 of the Council of Higher Education, dated February 13, 1984. The plan, managed by independent plan administrators, permits employees to defer a portion of their salary until future years. At the employee's election, such amounts may be invested in mutual funds, which represent varying levels of risk and return. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency. All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to these amounts, are (until paid or made available to the employee or other beneficiary) solely the property and rights of the University (without being restricted to the provisions of benefits under the plan), subject only to the claims of the University's general creditors. Participants' rights under the plan are equal to that of general creditors of the University in an amount equal to the fair market value of the deferred account for each participant. It is the opinion of the University's legal counsel that the University has no liability for the losses under the plan but does have the duty of care that would be required of an ordinary prudent investor. The University believes that it is unlikely that it will use the assets of the plan to satisfy the claims of general creditors in the future.

M. Compensated Absences

The vacation policy of the University generally provides for the accumulation of 2.5 days per month. Unpaid vacation time accumulated is fully vested to the employees from the first day of work.

Employees accumulate sick leave generally at a rate of 1.5 days per month up to a maximum of 90 days. The University pays, annually, the excess of 90 days of accumulated sick leave to the employees. Upon retirement, an employee receives compensation for all accumulated unpaid sick leave at the then current rate, provided the employee has at least 10 years of service with the University. During the years ended June 30, 2008 and 2007, the cost of the excess of 90 days of the accumulated sick leave was $10,748,463 and $10,208,075, respectively.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

N. Net Patient Service Revenue (Discretely Presented Component Unit)

Servicios Médicos Universitarios, Inc. has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

O. Classification of Revenues

The University has classified its revenues as either operating or nonoperating revenues.

Operating revenues include activities that have the characteristics of exchange transactions such as student tuition and fees, net of scholarship discounts and allowances; sales and services of auxiliary enterprises, net of scholarship allowances; most federal, state and local grants and contracts; and, hospital patient service revenues, net of allowances for contractual adjustments and doubtful accounts.

Non-operating revenues include activities that have the characteristics of no exchange transactions, such as gifts and contributions, Federal Pell Grants and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as state appropriations, investment income and gifts. Gifts to the endowment fund are classified as other nonoperating revenues.

P. Gifts and Pledges

Pledges of financial support from organizations and individuals representing and unconditional promise to give are recognized in the financial statements once all eligibility requirements, including time requirements, have been met. In the absence of such promise, revenue is recognized when the gift is received. Endowment pledges generally do not meet eligibility requirements, as defined by GASB Statement No. 33, *Accounting and Financial Reporting for No exchange Transactions*, and are not recorded as assets until the related gift has been received.

Unconditional promises that are expected to be collected in future years are recorded at the present value of the estimated future cash flows.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Q. Grants and Contracts

The University has been awarded grants and contracts for which the funds have not been received or expenditures made for the purpose specified in the award. These awards have not been reflected in the financial statements, but represent commitments of sponsors to provide funds for specific research or training projects. For grants that have allowable cost provisions, the revenue will be recognized as the related expenditures are made. For grants with work completion requirements, the revenue is recognized as the work is completed and for grants without either of the above requirements, the revenue is recognized as it is received.

R. GASB Statement No. 45

During fiscal year 2008, the University adopted the provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement improves the relevance and usefulness of financial reporting by (a) requiring systematic, accrual-basis measurement and recognition of OPEB cost (expense) over a period that approximates employees' years of service and (b) providing information about actuarial accrued liabilities associated with OPEB and whether and to what extent progress is being made in funding the plan. The impact of the adoption on the financial statements of the University is considered not to be significant. Further details are disclosed in Note 12.

2. Deposits

All the operating cash of the University is pooled into one bank account. Cash balances by funds represent the cash that is allocated to each fund of the University.

The University is authorized to deposit only in institutions approved by the Department of the Treasury of the Commonwealth of Puerto Rico (Treasury), and such deposits are maintained in separate bank accounts in the name of the University. Such authorized depositories, except for the Government Development Bank for Puerto Rico (GDB) and the Economic Development Bank for Puerto Rico (EDB), collateralize the uninsured deposits with securities that are pledged with the Department of the Treasury.

No collateral is required to be maintained for deposits at the GDB and EDB, both public corporations of the Commonwealth of Puerto Rico.

As of June 30, 2008 and 2007, the carrying value of cash and cash equivalents amounted to $24,994,664 and $54,140,722, respectively, and the cash deposited in the banks amounted to $54,217,337 and $62,648,245, respectively.

3. Investments

The University's investments held at June 30, 2008 and 2007, are summarized in the following table:

	2008	2007
Certificates of deposit	$ 127,937	$ 5,909,686
Government agency securities	73,596,054	81,397,420
Guaranteed investment certificate	161,230,999	179,491,255
Corporate bonds and preferred stock	20,912,375	15,249,929
Common stock and convertibles	21,493,012	19,927,139
Mutual Funds	54,046,129	58,287,211
	$ 331,406,506	$ 360,262,640

The custody of these investments is held by the trust department of a commercial bank in the name of the University and the portfolio is managed by a brokerage firm.

The University is authorized to invest a percentage of total assets, with certain limitations, in the following types of investments; not less than 20% and no more than 80% in fixed income securities, not less than 20% and no more than 80% in equity securities. No international equity, private equity and non-U.S. income securities investments are held by the University.

Guaranteed Investment Certificate

The University maintains a Construction Fund account, related to the issuance of the Series Q University of Puerto Rico System Revenue Bonds. As of June 30, 2008 and 2007, the account balance amounted to approximately $161 and $179 million, respectively. The account is held under a guaranteed investment certificate (the certificate) whereas the financial institution guarantees the University a fixed rate of return equal to 4.772%. As established in the contract, the financial institution has invested such funds in predetermined securities such as cash, U.S. Treasury and U.S. Government Agency securities. These securities are pledged and serve as collateral for the account balance. The fair value of the guaranteed investment certificate is determined based on the fair value of the underlying investments based on quoted market prices and then adjusted to contract value. As of June 30, 2008 and 2007 the contract value, which represents amounts deposited plus interest credited less withdrawals, is equal to the fair value.

3. Investments (continued)

Credit Risk

Issuer credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. As of June 30, 2008, the University's credit quality distribution for securities is as follows:

	Carrying Value	Quality Rating AAA-A	AA	Unrated	No Risk
Government agency securities	$ 73,596,054	$ –	$ –	$ –	$ 73,596,054
Guaranteed investment certificate	161,230,999	–	161,230,999	–	–
Corporate Bonds and preferred stocks	20,912,375	20,912,375	–	–	–
Common Stocks and Convertibles	21,493,012	21,493,012	–	–	–
Mutual Funds	54,046,129	–	–	54,046,129	–
	$ 331,278,569	$ 42,405,387	$ 161,230,999	$ 54,046,129	$ 73,596,054

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value is to changes in market interest rates. As of June 30, 2008, the weighted average maturity by investment type in each fund follows:

Investment Type	Maturities	Amount
Corporate Bonds	25/Apr/10 - 15/May/40	$ 4,540,271
Corporate Bonds	15/Jul/09 - 15/May/44	1,257,566
Corporate Bonds	15/Jul/09 - 15/May/44	7,058,305
Corporate Bonds	29/Jul/10 - 15/May/44	152,698
Corporate Bonds	15/Jul/09 - 15/May/44	408,555
Corporate Bonds	15/Jul/09 - 15/May/44	7,477,443
Corporate Bonds	15/Mar/12 - 15/Oct/30	17,537
		$ 20,912,375

4. Accounts Receivable

Accounts receivable as of June 30 are as follows:

	2008	2007
Commonwealth of Puerto Rico appropriations grants and contracts	**$ 43,886,782**	$ 37,112,832
Other government agencies	**91,761,296**	92,984,383
Due from Federal Government	**23,799,975**	22,329,643
Due from medical plans	**67,311,384**	60,044,847
Due from Servicios Médicos Universitarios, Inc.	**33,296,756**	33,296,756
Other	**30,566,154**	20,268,354
	290,622,347	266,036,815
Less allowance for doubtful accounts	**(132,409,296)**	(106,514,050)
Accounts receivable, net	**$ 158,213,051**	$ 159,522,765

On September 7, 2004, the Commonwealth of Puerto Rico approved a resolution to pay $94,710,382 to the University on behalf of the Puerto Rico Department of Health and the Commonwealth of Puerto Rico, over the course of ten years. As of June 30, 2008, the University has received $54,280,255 from this amount. The remaining balance will be received as follows:

Fiscal Year	Amount
2008-2009	$ 7,570,127
2009-2010	7,570,127
2010-2011	7,570,127
2011-2012	8,000,000
2012-2013	8,000,000
2013-2014	1,719,746
	$ 40,430,127

5. Capital Assets

Changes in capital assets for the year ended June 30, 2008 and 2007, are as follows:

	2008				
	Beginning Balance	**Additions**	**Transfers**	**Reductions**	**Ending Balance**
Capital assets not being depreciated:					
Land	**$ 42,161,028**	**$ –**	**$ –**	**$ –**	**$ 42,161,028**
Construction - in progress	**97,985,272**	**60,199,286**	**(21,573,166)**	**(1,297,172)**	**135,314,220**
	140,146,300	**60,199,286**	**(21,573,166)**	**(1,297,172)**	**177,475,248**
Other capital assets:					
Land improvements	**31,593,642**	**–**	**67,040**	**–**	**31,660,682**
Building, fixed equipment, improvements and infrastructure	**722,924,139**	**–**	**20,111,537**	**–**	**743,035,676**
Equipment and library materials	**214,047,507**	**16,254,516**	**1,394,589**	**(7,086,998)**	**224,609,614**
Building and equipment under capital lease	**99,298,349**	**–**	**–**	**(100)**	**99,298,249**
	1,067,863,637	**16,254,516**	**21,573,166**	**(7,087,098)**	**1,098,604,221**
Less accumulated drepreciation for:					
Land improvements	**(13,626,245)**	**(1,160,150)**	**–**	**–**	**(14,786,395)**
Buildings, fixed equipment, improvements and infrastructure	**(240,932,843)**	**(17,920,705)**	**–**	**–**	**(258,853,548)**
Equipment and library materials	**(154,903,405)**	**(15,033,300)**	**–**	**6,768,128**	**(163,168,577)**
Building and equipment under capital lease	**(1,861,842)**	**(3,010,914)**	**–**		**(4,872,756)**
	(411,324,335)	**(37,125,069)**	**–**	**6,768,128**	**(441,681,276)**
Other capital assets, net of acumulated depreciation	**656,539,302**	**(20,870,553)**	**21,573,166**	**(318,970)**	**656,922,945**
Capital assets, net	**$ 796,685,602**	**$ 39,328,733**	**$ –**	**$ (1,616,142)**	**$ 834,398,193**

	2007				
	Beginning Balance	**Additions**	**Transfers**	**Reductions**	**Ending Balance**
Capital assets not being depreciated:					
Land	$ 33,534,290	$ –	$ 8,626,738	$ –	$ 42,161,028
Construction - in progress	138,489,823	52,364,572	(91,876,089)	(993,034)	97,985,272
	172,024,113	52,364,572	(83,249,351)	(993,034)	140,146,300
Other capital assets:					
Land improvements	30,855,329	–	738,313	–	31,593,642
Building, fixed equipment, improvements and infrastructure	638,398,067	2,249,147	82,303,525	(26,500)	722,924,239
Equipment and library materials	202,446,186	18,649,056	207,513	(7,255,248)	214,047,507
Building and equipment under capital lease	–	99,298,249	–	–	99,298,249
	871,699,582	120,196,452	83,249,351	(7,281,748)	1,067,863,637
Less accumulated drepreciation for:					
Land improvements	(12,518,386)	(1,124,949)	–	17,090	(13,626,245)
Buildings, fixed equipment, improvements and infrastructure	(225,160,046)	(15,783,169)	–	10,372	(240,932,843)
Equipment and library materials	(146,718,735)	(15,004,950)		6,820,280	(154,903,405)
Building and equipment under capital lease	–	(1,861,842)	–	–	(1,861,842)
	(384,397,167)	(33,774,910)	–	6,847,742	(411,324,335)
Other capital assets, net of acumulated depreciation	487,302,415	86,421,542	83,249,351	(434,006)	656,539,302
Capital assets, net	$ 659,326,528	$ 138,786,114	$ –	$ (1,427,040)	$ 796,685,602

5. Capital Assets (continued)

Amortization expense of assets recorded under capital leases amounted to $3,010,914 and $1,861,842 in 2008 and 2007, respectively.

6. Lines of Credit

As of June 30, 2008, the University has available a non-revolving line of credit agreement with GDB for the total authorized amount of $60,000,000. This line of credit is guaranteed by the Commonwealth of Puerto Rico. As of June 30, 2008, the University had $36,061,717 outstanding under this line of credit.

7. Noncurrent Liabilities

Changes in noncurrent liabilities for the year ended June 30, 2008 and 2007, are as follows:

2008

	Beginning Balance	Additions	Reductions	Other	Ending Balance	Less Due Within One Year	Noncurrent Liabilities
Long-term debt:							
Notes payable	$ 20,271,404	$ 15,790,313		$ –	$ 36,061,717	$ –	$ 36,061,717
Bonds payable	655,507,668	2,752,336	(19,760,000)	(595,173)	637,904,831	21,455,000	616,449,831
Total long-term	$ 675,779,072	$ 18,542,649	$ (19,760,000)	$ (595,173)	$ 673,966,548	$ 21,455,000	$ 652,511,548
Other long-term liabilities:							
Deferred compensation payable	$ 58,287,211		$ (4,241,081)	$ –	$ 54,046,130	$ –	$ 54,046,130
Claims liability	22,060,285		(863,150)	(2,072,388)	19,124,747	863,150	18,261,597
Compensated absences	144,527,515	37,785,817	(21,531,924)	–	160,781,408	28,195,670	132,585,738
Capital lease obligation	70,775,930		(1,063,344)	–	69,712,586	1,063,344	68,649,242
Total other long-term liabilities	$ 295,650,941	$ 37,785,817	$ (27,699,499)	$ (2,072,388)	$ 303,664,871	$ 30,122,164	$ 273,542,707

2007

	Beginning Balance	Additions	Reductions	Other	Ending Balance	Less Due Within One Year	Noncurrent Liabilities
Long-term debt:							
Notes payable	$ 79,645,174	$ 23,209,527	$ (82,583,297)	$ –	$ 20,271,404	$ –	$ 20,271,404
Bonds payable	382,449,715	546,150,000	(320,048,872)	46,956,825	655,507,668	19,760,000	635,747,668
Total long-term	$ 462,094,889	$ 569,359,527	$ (402,632,169)	$ 46,956,825	$ 675,779,072	$ 19,760,000	$ 656,019,072
Other long-term liabilities:							
Deferred compensation payable	$ 51,995,435	$ 6,291,776	$ –	$ –	$ 58,287,211	$ –	$ 58,287,211
Claims liability	18,332,300	4,828,126	(1,100,141)	–	22,060,285	1,100,000	20,960,285
Compensated absences	135,075,173	29,454,465	(20,002,123)	–	144,527,515	24,919,842	119,607,673
Capital lease obligation	–	99,298,349	(28,522,419)	–	70,775,930	2,178,105	68,597,825
Total other long-term liabilities	$ 205,402,908	$ 139,872,716	$ (49,624,683)	$ –	$ 295,650,941	$ 28,197,947	$ 267,452,994

Bonds payable are further discussed in Note 8-A.

8. Bonds Payable

A. Bonds

The University has issued revenue bonds designated as "University System Revenue Bonds", the proceeds of which have been used mainly to finance new activities in connection with its educational facilities construction program and to cancel and refinance previous debts incurred. The following is the balance of bonds payable as of June 30, 2008 and 2007:

Series	Balance as of June 30, 2008	Anual Interest Rate (%)	Due Date
C - Serial	**$ 489,000**	3.00%	1972-2011
D - Serial	**633,000**	3.75%	1972-2011
F - Term	**8,700,000**	5.50%	1973-2012
M - Serial	**4,940,000**	4.35-5.45%	1996-2009
N - Capital Appreciation Serial Bonds	**51,980,000**	5.65-5.75%	1996-2013
O - Serial	**7,060,000**	4.5-3.75%	2001-2020
P - Serial	**238,860,000**	5.00%	2010-2026
P - Term	**47,645,000**	5.00%	2027-2030
Q - Serial	**123,065,000**	5.00%	2008-2026
Q - Term	**132,415,000**	5.00%	2027-2036
	615,787,000		
Less unamortized bond discount	**(4,316)**		
Plus unaccreted premium	**34,715,169**		
Less future appreciated principal	**(7,867,143)**		
Deferred loss on refunding	**(4,725,879)**		
	$ 637,904,831		

Series	Balance as of June 30, 2007	Anual Interest Rate (%)	Due Date
C - Serial	$ 639,000	3.00%	1972-2011
D - Serial	833,000	3.75%	1972-2011
F - Term	9,950,000	5.50%	2012
M - Serial	4,940,000	4.35-5.45%	1996-2009
N - Serial	9,840,000	4.35-5.45%	1996-2008
N - Capital Appreciation Serial Bonds	51,980,000	5.65-5.75%	2009-2013
O - Serial	11,215,000	4.5-3.75%	2001-2020
P - Serial	238,860,000	5.00%	2010-2026
P - Term	47,645,000	5.00%	2027-2030
Q - Serial	127,230,000	5.00%	2008-2026
Q - Term	132,415,000	5.00%	2027-2036
	635,547,000		
Less unamortized bond discount	(6,473)		
Plus unaccreted premium	35,310,342		
Less future appreciated principal	(10,339,329)		
Deferred loss on refunding	(5,003,872)		
	$ 655,507,668		

8. Bonds Payable (continued)

A. Bonds (continued)

Capital Appreciation Serial Bonds interest accrues semi-annually and is added to the principal.

B. Debt Service Requirement

At June 30, 2008, bonds payable require payments of principal and interest as follows:

Fiscal Year	Principal	Interest	Total
2009	$ 21,455,000	$ 28,217,053	$ 49,672,053
2010	20,825,000	27,644,555	48,469,555
2011	27,652,000	27,127,880	54,779,880
2012	27,040,000	26,281,245	53,321,245
2013 to 2017	107,990,000	117,467,000	225,457,000
2018 to 2022	121,635,000	91,136,000	212,771,000
2023 to 2027	130,715,000	58,127,500	188,842,500
2028 to 2032	97,665,000	28,380,000	126,045,000
2033 to 2036	60,810,000	7,786,000	68,596,000
	$ 615,787,000	$ 412,167,233	$ 1,027,954,233

C. Pledged Revenues

The bonds are general obligations of the University and are collateralized by the pledge of, and a first charge on, all revenues derived or to be derived by the University, except for appropriations and contributions, as defined in the Trust Agreement governing the bonds issued. In the event that the pledged revenues are insufficient to pay the principal of and the interest on, the bonds, the University agrees to provide any additional required monies from other funds available to the University for such purposes, including funds appropriated by the Commonwealth of Puerto Rico. The revenues pledged were as follows for the years ended June 30, 2008 and 2007:

8. Bonds Payable (continued)

C. Pledged Revenues (continued)

Pledged Revenues:		2008		2007
Tuition and other fees collected	$	**77,347,598**	$	72,973,464
Student fees collected		**6,431,462**		6,160,271
Rental and other charges received for the right of use and occupancy of the facilities in the University system		**1,289,912**		1,241,694
Bookstore receipts (gross sales less cost of books and supplies sold)		**464,502**		810,127
Interest on investment of University funds, excluding funds invested pursuant to Article VI of the Trust Agreement		**2,931,455**		4,665,763
Funds paid to the University in respect to overhead allowance on federal research projects		**16,260,829**		18,981,291
Other income		**30,028,753**		27,788,421
	$	**134,754,511**	$	132,621,031

Interest earned on investments in the sinking fund reserve account amounted to $2,884,891 and $1,766,873 for the years ended June 30, 2008 and 2007, respectively.

The University is required to maintain a sinking fund and construction fund as described in the following paragraphs:

The funds for retirement of indebtedness consist of a sinking fund which includes three separate accounts designated Bond Service Account, Redemption Account and Reserve Account. The Trustee shall, upon the receipt of the pledged revenues, make deposits to the credit of the following accounts in the amounts specified and in the following order:

Bond Service Account - such amount thereof as may be required to make the amount then to its credit equal to the interest then due, or to become due, within the next ensuing six (6) months on the bonds of each series then outstanding, and the amount of principal of the serial bonds of each series then due, or to become due, within the next ensuing twelve (12) months.

Redemption Account - such amount, if any, after making the deposit to the Bond Service Account, as may be required to make the amount then to its credit equal to the amortization requirements, if any, for the fiscal year in which such deposit is made for the term bonds of each series then outstanding plus redemption premiums, if any.

8. Bonds Payable (continued)

C. Pledged Revenues (continued)

Reserve Account - such amount, if any, after making the deposit to the above accounts as may be required to make the amount then to its credit equal to the maximum principal and interest (less any federal debt service grant payments) requirements for any year thereafter, on account of all bonds then outstanding.

Monies in the Bond Service Account and the Redemption Account shall, as nearly as may be practicable, be continuously invested and reinvested in direct obligations of, or obligations, the principal of and interest on which are unconditionally guaranteed by the United States Government. Monies in the Reserve Account may be invested in a broader range of investments including interest bearing bank accounts, federal agency obligations, repurchase agreements, commercial paper and other highly rated obligations.

D. Bonds Payable – Discretely Presented Component Unit

On December 21, 2000, AFICA issued, on behalf of Desarrollos Universitarios, Inc., Educational Facilities Revenue Bonds, 2000 Series A, in the amount of $86,735,000. The bonds were issued to (i) finance the development, construction and equipment of the Plaza Universitaria Project (the Projects), (ii) repay a portion of certain advances made by the Government Development Bank for Puerto Rico under a line of credit facility for the purpose of paying certain costs of the development and construction of the Projects, (iii) make a deposit to the Debt Service Reserve fund and, (iv) pay the costs and expenses incurred in connection with the issuance and sale of bonds. The principal and interest on the bonds are insured by a financial guaranty insurance policy issued by MBIA Insurance Corporation, and by the assignment of the lease agreement with the University.

8. Bonds Payable (continued)

D. Bonds Payable – Discretely Presented Component Unit (continued)

Bonds payable at March 31, 2008 and 2007, consist of:

Description	Interest Rate	Maturity	2008 Face Amount	2007 Face Amount
Serial Bonds	4.00%	July 1, 2007	**$ –**	$ 1,485,000
Serial Bonds	5.00%	July 1, 2008	**1,545,000**	1,545,000
Serial Bonds	4.13%	July 1, 2009	**1,620,000**	1,620,000
Serial Bonds	4.25%	July 1, 2010	**1,685,000**	1,685,000
Serial Bonds	5.63%	July 1, 2011	**1,760,000**	1,760,000
Serial Bonds	5.63%	July 1, 2012	**1,860,000**	1,860,000
Serial Bonds	5.63%	July 1, 2013	**1,960,000**	1,960,000
Serial Bonds	5.63%	July 1, 2014	**2,075,000**	2,075,000
Serial Bonds	5.63%	July 1, 2015	**2,190,000**	2,190,000
Serial Bonds	5.63%	July 1, 2016	**2,315,000**	2,315,000
Serial Bonds	5.63%	July 1, 2017	**2,445,000**	2,445,000
Serial Bonds	5.63%	July 1, 2018	**2,580,000**	2,580,000
Serial Bonds	5.63%	July 1, 2019	**2,725,000**	2,725,000
Serial Bonds	5.00%	July 1, 2020	**2,880,000**	2,880,000
Serial Bonds	5.00%	July 1, 2021	**3,020,000**	3,020,000
Serial Bonds	5.00%	July 1, 2033	**50,520,000**	50,520,000
			$ 81,180,000	$ 82,665,000

8. Bonds Payable (continued)

D. Bonds Payable – Discretely Presented Component Unit (continued)

Interest on the bonds is payable each January 1 and July 1, commencing on July 1, 2001, Bonds maturing after July 1, 2010 may be redeemed, at the option of the University in whole or in part, at a redemption price equal to 100% of the principal amount plus accrued interest, without premium. In addition, term bonds are subject to mandatory redemption in part commencing on July 1, 2022 to the extent of the sinking fund requirement for said bonds set forth below at a redemption price equal to 100% of the principal amount thereof plus accrued interest.

Redemption Period	Amount
July 1, 2022	$ 3,175,000
July 1, 2023	3,330,000
July 1, 2024	3,500,000
July 1, 2025	3,675,000
July 1, 2026	3,855,000
July 1, 2027	4,050,000
July 1, 2028	4,255,000
July 1, 2029	4,465,000
July 1, 2030	4,690,000
July 1, 2031	4,925,000
July 1, 2032	5,170,000
July 1, 2033	5,430,000
	$ 50,520,000

E. Compliance with the Loan Agreement with AFICA – Discretely Presented Component Unit

At March 31, 2008 and 2007, the Company was not in compliance with Section 3.04 of the Loan Agreement with AFICA regarding allowed uses of funds in the Construction Fund, which are restricted to the payment of Project Costs, as defined in the Trust Agreement. Management and the Board of Directors understand that this situation does not jeopardize the tax exempt status of the underlying bonds. However, the Trustee and/or AFICA may notify in writing the Company's failure to observe this provision of the Loan Agreement and demand that it be remedied within sixty (60) days or that corrective action be instituted and diligently pursued by the Company within such period.

On October 15, 2008, the Trustee issued a Notice of Event of Default. Thereafter, on November 10, 2008, the Company received a payment from the University covering substantially all amounts due under the reimbursable expenses fee through June 30, 2008.

9. Obligation under Capital Lease

In October, 2007, the University entered into a capital lease agreement with Desarrollos Universitarios, Inc. a nonprofit corporation and component unit of the University. The agreement is for the use of Plaza Universitaria a residential and commercial facility for the use of students and other persons or entities conducting business with the University. The agreement began on October 1, 2006 and expires on June 25, 2033. The outstanding liability at June 30, 2008 and 2007 on this capital lease is $69,712,586 and $70,775,930, respectively.

The future minimum lease payments under the capital lease are as follows:

Future Minimun Lease Payments

Year	Amount
2009	$ 5,699,375
2010	5,697,550
2011	5,700,938
2012	5,701,938
2013	5,697,312
2014 to 2018	28,505,906
2019 to 2023	28,495,531
2024 to 2028	28,499,500
2029 to 2033	28,502,500
Total minimun lease payments	142,500,550
Less amount representing interest	(72,787,964)
Present value of net minimun lease payments	$ 69,712,586

10. Commitments and Contingent Liabilities

A. Insurance

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Through January 1993, the University was insured under claims-made insurance policies with respect to medical malpractice risks for $250,000 per occurrence up to an annual aggregate of $500,000. Subsequent to such date, the University was unable to obtain insurance at a cost it considered to be economically justifiable, consequently, the University is now self-insured for such risks. Under Law Number 98 of August 24, 1994, the responsibility of the University is limited to a maximum amount of $75,000 per person, or $150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Self-insured risk liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend upon such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. Changes in the claims liability amount in fiscal years 2008 and 2007 were:

		2008		2007
Claims payable - July 1	**$**	**22,060,285**	$	18,332,300
Incurred claims and changes in estimates		**29,300,132**		34,279,088
Payments for claims and adjustments expenses		**(32,235,670)**		(30,551,103)
Claims payable - June 30	**$**	**19,124,747**	$	22,060,285

The University continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

B. Federal Assistance Programs

The University participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations,* or to compliance audits by grantor agencies. The resolution of certain previously identified questioned costs has not occurred. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the University expects such amounts, if any, to be immaterial.

10. Commitments and Contingent Liabilities (continued)

C. Discretely Presented Component Units

Servicios Médicos Universitarios, Inc. (the Hospital) is a non-for-profit corporation organized to operate and administer healthcare unit locate in Carolina. This facility was acquired by the University and includes land, building and medical equipment.

The Hospital entered into a loan agreement (the Agreement) with the Government Development Bank of Puerto Rico (GDB) for an aggregate principal amount not to exceed $17,000,000. As part of the Agreement, the University (the Guarantor) agreed to guaranty payment obligations.

On July 18, 2001, the Board of Trustees approved to amend the Working Capital Loan to $15,367,611 and to decrease the Improvement Loan to $1,632,389. The amendment was effective on August 1, 2001. In addition, the Guarantor will pay GDB, on the first day of July and January of each year, the balance of interest due and outstanding by the Hospital.

Scheduled principal repayments of the long-term debt for the next five years and thereafter are as follows:

Fiscal Year	Amount
2009	$ 15,367,611
2010	–
2011	–
2012	–
2013	–
Thereafter	1,632,389
	$ 17,000,000

10. Commitments and Contingent Liabilities (continued)

C. Discretely Presented Component Units (continued)

Desarrollos Universitarios, Inc. (the Company) was incorporated on January 22, 1997. The Company is a non-for-profit corporation, with the sole purpose of developing, constructing and operating academic, residential, administrative, office, commercial and maintenance facilities (Plaza Universitaria) for use by students, faculty members, administrators, employees, visitors, invitees, and other members of or persons and entities related to or conducting business with the University community, or other activities conducted in such facility.

On May 11, 2000, the University's Board of Trustees ratified a Memorandum of Agreement (the Agreement) to establish a contractual agreement between the University and the Company. The Agreement, dated May 22, 1998, states among other things the following: (1) the University will lease to, or otherwise grant to, the Company the right for the long-term use of the land, for the sole purpose of developing, constructing and operating Plaza Universitaria, (2) the Company shall finance the development of Plaza Universitaria from AFICA Bond proceeds and/or line credit and/or any other structure or credit facility, (3) the Company will own the Plaza Universitaria improvements and will lease them exclusively to the University, during the life of the AFICA Bonds, (4) the University shall have the right to prepay or refinance the Bonds at any time, consistent with the restrictions on refinancing contained in the financing documents, (5) upon the payment or prepayment in full of all the AFICA Bonds, the lease on the land shall terminate and the University shall become, *ipso facto*, owner of all the Plaza Universitaria improvements, without the need or obligation to make any additional payment of any kind (other than any "bargain purchase" payment as may be required under the project documents), and (6) rental payments (lease payments) from the University shall have a fixed component and a variable component. The fixed component shall be in an amount sufficient to guarantee to bondholders the payment of principal and interest on the AFICA Bonds as may be established in the financing documents, and will be pledged to guarantee such payments. The variable component of the lease payments will be used to cover operating, maintenance, administrative, management, and other fees and costs, which will be established periodically and reviewed annually between the parties, as well as such amounts for reserves and special funds, which may be required under the financing documents related to the bond issue.

10. Commitments and Contingent Liabilities (continued)

C. Discretely Presented Component Units (continued)

In October 2003, Plaza Universitaria Project's general contractor submitted a claim for extended overhead (field and main office) and subsequently a Proposal for Settlement for an amount exceeding $10 million. It is the Company's legal counsel's opinion that some of the allegation are invalid under the terms of the contract and that the general contractor has already been compensated for some of the claimed amounts by Company approved change orders. Management of the Company believes, based on the advice of counsel, that there is a minimal financial exposure to the Company in connection with this claim.

11. University of Puerto Rico Retirement System

The University of Puerto Rico Retirement System (the System) is a single-employer, defined benefit pension plan that covers all employees of the University of Puerto Rico (the University) with the exception of hourly, temporary, part-time, contract and substitute employees, and visiting professors. It is qualified and exempt from Puerto Rico and United States taxes.

The System issues stand-alone audited financial statements and can be obtained from the System's administrative offices.

11. University of Puerto Rico Retirement System (continued)

Effective July 1, 2006, the System changed its method of amortizing the unfunded actuarial liability from the "Level Dollar Amount" method to the "Level Percentage of Payroll" method. The newly adopted method is an accepted method of amortizing the unfunded actuarial liability of defined benefit plans. The change has been accounted for prospectively in the financial statements.

Funding Policy and Annual Pension Cost

Contribution rates:	
University	10.9%
Plan members	7%
Annual pension cost	$59,245,691
Contributions made	$81,553,088
Actuarial valuation date	6/30/2008
Actuarial cost method	Entry age normal (traditional)
Amortization method	Level percentage of payroll
Remaining amortization period	30 years constant (open basis)
Asset valuation method	5-year smoothed market
Actuarial assumptions:	
Investment rate of return*	8.00%
Projected salary increases*	5%
*Includes inflation at	3.50%
Postretirement benefit increases	3% every two (2) years

Year Ending	Annual Pension Cost (APC)	Employer Contribution	Percentage of APC Contributed	Net Pension Obligation (Asset)
6/30/2008	$ 59,245,691	$ 81,553,088	137.7%	$ (22,307,397)
6/30/2007	$ 57,524,263	$ 78,310,774	136.1%	$ (20,786,511)
6/30/2006	$ 55,399,680	$ 73,658,083	133.0%	$ (18,258,403)
6/30/2005	$ 84,672,084	$ 69,291,395	81.8%	$ 15,380,689
6/30/2004	$ 70,244,365	$ 61,376,007	87%	$ 8,868,358

Pension asset has been recorded in prepaid expense and other assets.

12. Other Post-Employment Benefits (OPEB)

In addition to the pension benefits described in Note 11, the University provides post-employment health care benefits for its retired employees. Substantially all of the employees may become eligible for this benefit if they reach normal retirement age while working for the University. Health care benefits are provided through insurance companies whose premiums are paid by the retiree and by the University up to maximum of $125 per month for each retiree. The cost of providing such benefits are recognized when paid.

The Governmental Accounting Standards Board released Statement No. 45 (GASB No. 45) in 2004. This statement requires employers to accrue the cost of Postemployment Benefit Plans while employees who will receive these benefits are providing services to the employer.

The University does not pre-fund its postemployment benefit plan and retiree benefits are paid out of the University's general assets each year. Accordingly, the discount rate is based on the long-term rates of return that the University expects to earn on general assets which are used to pay plan benefits.

The Annual OPEB Cost is calculated based on the Annual Required Contribution of the employer (ARC), an amount actuarially determined in accordance with the provisions of GASB Statement No. 45. The ARC represents a level of funding that, if paid on ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years. The following table shows the components of the University's annual OPEB cost for the fiscal year 2007-2008:

Annual OPEB cost (or ARC)	$ 9,681,698
Actuarial Accrued Liability (AAL)	$186,689,632
Unfunded AAL	$186,689,632
Funded Ratio	0%

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the Net OPEB Obligation on a funded and unfunded basis are as follow:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/2008	$9,681,698	85.6%	$1,394,231

12. Other Post-Employment Benefits (OPEB) (continued)

OPEB Actuarial Valuation – The University's other Post-Employment Benefits Program actuarial valuation was conducted by Deloitte Consulting, LLP as of July 1, 2007, members of the American Academy of Actuaries. The valuation was performed in accordance with GASB Statement No. 45 requirements.

Significant Actuarial Methods and Assumptions:

Actuarial Valuation Date	July 1, 2007
Actual Cost Method	Projected Unit Credit
Amortization Method	Level Dollar Amortization over 30 years
Medical Subsidy	85%
Tuition Remission	$460 per retiree in fiscal 2008, increasing 4.0% per year
Payroll Growth	4%
Discount Rate	4%

Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future.

The actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

13. Going Concern - Discretely Presented Component Unit

Since the Hospital commenced operations, it has experienced significant operating losses having an accumulated net assets deficiency of $65,337,535 as of June 30, 2008. The Hospital has received advances from the University to cover its cash needs from operations. Most of these accumulated losses are mainly related to the fact that, as a former public hospital operated by the Department of Health, it provides a significant amount of services to indigent population for which the Hospital does not obtain a payment. Most of these patients are indigent persons not subscribed to the Health Reform Program and aliens without medical insurance coverage. The medical services provided to these persons were supposed to be paid to the Hospital by the Puerto Rico Department of Health. However, since the beginning of the operations, the Department of Health has been unable to pay for such services. As shown in the accompanying financial statements, the Hospital has accumulated losses for uncollectible accounts receivable in the approximate amount of $21,260,231.

13. Going Concern - Discretely Presented Component Unit (continued)

The Hospital's management believes that all these factors had a material impact in the Hospital's results of operations during its years of operations and consequently in the accumulated deficit at June 30, 2008.

The Hospital's management with the assistance of the University of Puerto Rico's administration continues implementing a management plan toward its operational activities as well as the Hospital's ability to get cash to comply with its current obligations.

Among the matters included in such management plan are the following:

- Extension of the medical privileges in the Hospital to faculty members within the Hospital's primary and secondary market area.
- Development of new business within the Hospital's building, for example space rentals for physicians and others.
- Marketing of the Ob-Gyn and pediatrics services.
- Marketing of the ophthalmology services, including a new physician that has a specialization in cornea diagnosis and treatment.
- More aggressive negotiation with medical insurance companies and restructuring the billing and collection department, in order to reduce to a minimum, denied reimbursement for service provided, to increase the reimbursement rates.
- Increasing the Hospital operating cash flow by improving the reimbursement rate through more aggressive negotiations with medical insurance companies and restructuring the billing and collection department with the acquisition and implementation of a new accounting, billing and collection, and emergency room tracking and clinical documentation information systems, in order to reduce to at minimum denied reimbursement for services provided.
- Refurbishing pediatrics, Ob-Gyn, Surgery and other hospital general and common areas, improve hospital image and be able to attract insured patients sector.
- Expansion of the Intensive Care Unit area with twelve new beds. This will improve service provided to critical patients and as result of this an increase in patient days.

The Hospital's financial statements do not include any adjustments relating to the recoverability and classification of recorded assets amounts or the amounts and classifications of liabilities that might be necessary, should the Hospital be unable to continue as a going concern or in the event of any disposition of the Hospital's assets through a sale or by other means.

14. Functional Information

The University's operating expenses by functional classification during the years ended June 30, 2008 and 2007 were as follows:

2008

Functional classification	Salaries and benefits	Supplies and other services	Scholarship and fellowship	Utilities	Depreciation	Other Expenditures	Total
Instruction	$ 410,571,202	$ 17,610,881	$ 11,008,442	$ 1,174,161	$ –	$ 297,676	$ 440,662,362
Research	67,422,998	26,982,113	10,958,266	1,168,046	–	688,189	107,219,612
Public service	53,366,517	13,547,886	2,612,691	763,571	–	588,255	70,878,920
Academic support	79,961,708	17,280,054	4,361,716	134,338	–	124,113	101,861,929
Student service	45,669,139	10,339,543	954,213	3,251	–	36,852	57,002,998
Institutional support	125,970,369	36,992,224	531,730	1,920,365	–	1,427,314	166,842,002
Oper & Maintenance	78,109,943	29,214,526	29,990	43,853,045	–	3,989,007	155,196,511
Student Aid	2,401,587	666,013	129,685,290	1,116	–	9,700	132,763,706
Independent Operation	–	8,181	–	–	–	76,991	85,172
Patient Service	43,665,393	2,715,026	295,491	61,284	–	2,876	46,740,070
Auxiliary Enterprises	5,184,715	4,741,671	54,739	68,422	–	1,243,359	11,292,906
Depreciation	–	–	–	–	37,125,069	–	37,125,069
Other	–	–	–	–	–	23,612,308	23,612,308
	$ 912,323,571	$ 160,098,118	$ 160,492,568	$ 49,147,599	$ 37,125,069	$ 32,096,640	$ 1,351,283,567

2007

Functional classification	Salaries and benefits	Supplies and other services	Scholarship and fellowship	Utilities	Depreciation	Other Expenditures	Total
Instruction	$ 383,324,453	$ 18,945,647	$ 10,846,926	$ 1,126,143	$ –	$ 82,508	$ 414,325,677
Research	66,284,908	21,338,866	11,755,699	1,026,227	–	4,995,303	105,401,003
Public service	49,857,343	11,488,554	2,153,249	395,646	–	26,200	63,920,992
Academic support	79,270,040	17,460,444	4,118,524	123,684	–	36,300	101,008,992
Student service	43,680,136	9,838,406	924,629	461	–	24,010	54,467,642
Institutional support	120,318,861	41,876,263	507,043	1,762,543	–	184,187	164,648,897
Oper & Maintenance	77,452,882	16,516,950	16,569	39,970,471	–	273,708	134,230,580
Student Aid	2,161,073	612,771	119,897,505	344	–	–	122,671,693
Independent Operation	–	462	–	–	–	–	462
Patient Service	43,117,786	2,623,561	282,541	63,117	–	15,697	46,102,702
Auxiliary Enterprises	4,746,225	5,326,439	70,613	61,645	–	1,268,137	11,473,059
Depreciation	–	–	–	–	33,774,910	–	33,774,910
Other	–	–	–	–	–	14,496,756	14,496,756
	$ 870,213,707	$ 146,028,363	$ 150,573,298	$ 44,530,281	$ 33,774,910	$ 21,402,806	$ 1,266,523,365

15. Significant New Accounting Pronouncements

Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues

In September 2007, the GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues.* This Statement establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. Such transactions are likely to comprise the sale of delinquent taxes, certain mortgages, student loans, or future revenues such as those arising from tobacco settlement agreements.

In addition to clarifying guidance on accounting for sales and pledges of receivables and future revenues, the Statement:

- Requires enhanced disclosures pertaining to future revenues that have been pledged or sold,
- Provides guidance on sales of receivables and future revenues within the same financial reporting entity,
- Provides guidance on recognizing other assets and liabilities arising from the sale of specific receivables or future revenues.

The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2007.

Pollution Remediation Obligations

In November 2007, the GASB recently issued Statement No. 49, *Pollution Remediation Obligations.* The Statement identifies the circumstances under which a governmental entity would be required to report a liability related to pollution remediation. According to the Statement, a government would have to estimate its expected outlays for pollution remediation if it knows a site is polluted and any of the following recognition triggers occur:

- Pollution poses an imminent danger to the public or environment and a government has little or no discretion to avoid fixing the problem,
- A government has violated a pollution prevention-related permit or license,
- A regulator has identified (or evidence indicates a regulator will do so) a government as responsible (or potentially responsible) for cleaning up pollution, or for paying all or some of the cost of the clean up,
- A government is named in a lawsuit (or evidence indicates that it will be) to compel it to address the pollution,
- A government begins to clean up pollution or conducts related remediation activities (or the government legally obligates itself to do so).

15. Significant New Accounting Pronouncements (continued)

Pollution Remediation Obligations (continued)

Liabilities and expenses would be estimated using an "expected cash flows" measurement technique, which will be employed for the first time by governments. Statement 49 also would require governments to disclose information about their pollution remediation obligations associated with clean-up efforts in the notes to the financial statements.

Statement 49 will be effective for financial statements for periods beginning after December 15, 2007.

Pension Disclosures

In May 2007, the GASB recently issued Statement No. 50, *Pension Disclosures*, which more closely aligns current pension disclosure requirements for governments with those that governments are beginning to implement for retiree health insurance and other post-employment benefits.

Specifically, Statement 50 amends GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27, *Accounting for Pensions by State and Local Governmental Employers*, by requiring:

- Disclosure in the notes to the financial statements of pension plans and certain employer governments of the current funded status of the plan—in other words, the degree to which the actuarial accrued liabilities for benefits are covered by assets that have been set aside to pay the benefits—as of the most recent actuarial valuation date.
- Governments that use the aggregate actuarial cost method to disclose the funded status and present a multi-year schedule of funding progress using the entry age actuarial cost method as a surrogate; these governments previously were not required to provide this information.
- Disclosure by governments participating in multi-employer cost-sharing pension plans of how the contractually required contribution rate is determined.

The provisions of Statement 50 generally are effective for periods beginning after June 15, 2007, with early implementation encouraged. The requirements relating to governments using the aggregate actuarial cost method are effective for financial statements and required supplementary information that contains information from actuarial valuations as of June 15, 2007, or later.

15. Significant New Accounting Pronouncements (continued)

Accounting and Financial Reporting for Intangible Assets

In June 2007, the GASB recently issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, to provide guidance regarding how to identify, account for, and report intangible assets.

The new standard characterizes an intangible asset as an asset that lacks physical substance, is nonfinancial in nature, and has an initial useful life extending beyond a single reporting period. Examples of intangible assets include easements, computer software, water rights, timber rights, patents, and trademarks.

Statement 51 requires that intangible assets be classified as capital assets (except for those explicitly excluded from the scope of the new standard, such as capital leases). Relevant authoritative guidance for capital assets should be applied to these intangible assets.

Statement 51 provides additional guidance that specifically addresses the unique nature of intangible assets, including:

- Requiring that an intangible asset be recognized in the statement of net assets only if it is considered identifiable
- Establishing a specified-conditions approach to recognizing intangible assets that are internally generated (for example, patents and copyrights)
- Providing guidance on recognizing internally generated computer software
- Establishing specific guidance for the amortization of intangible assets.

The requirements Statement 51 are effective for financial statements for periods beginning after June 15, 2009. The GASB made significant changes to the transition provisions, based on constituent response to the proposed version of the standards, to make it easier for governments to implement.

Land and Other Real Estate Held as Investments by Endowments

In November 2007, the GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. This Statement establishes consistent standards for the reporting of land and other real estate held as investments by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. Governments also are required to report the changes in fair value as investment income and to disclose the methods and significant assumptions employed to determine fair value, and other information that they currently present for other investments reported at fair value.

Statement 52 will be effective for financial statement periods beginning after June 15, 2008.

15. Significant New Accounting Pronouncements (continued)

Accounting and Financial Reporting for Derivative Instruments

In June 2008, the GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This Statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Derivative instruments are often complex financial arrangements used by governments to manage specific risks or to make investments. By entering into these arrangements, governments receive and make payments based on market prices without actually entering into the related financial or commodity transactions. Derivative instruments associated with changing financial and commodity prices result in changing cash flows and fair values that can be used as effective risk management or investment tools. Derivative instruments, however, also can expose governments to significant risks and liabilities. Common types of derivative instruments used by governments include interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), swaptions, forward contracts, and futures contracts.

Statement 53 will be effective for financial statement periods beginning after June 15, 2009.

Fund Balance Reporting and Governmental Fund Type Definitions

The GASB recently issued GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. Statement 54 is intended to improve the usefulness of information provided to financial report users about fund balance by providing clearer, more structured fund balance classifications, and by clarifying the definitions of existing governmental fund types.

The new standards also clarify the definitions of individual governmental fund types. It interprets certain terms within the definition of special revenue fund types, while further clarifying the debt service and capital projects fund type definitions. The final standard also specifies how economic stabilization or “rainy-day” amounts should be reported.

GASB Statement 54 is effective for financial statements for periods beginning after June 15, 2010. Governments that wish to implement earlier than that date are encouraged to do so.

Required Supplementary Information

Employees Retirement Plan

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Excess of Assets over AAL (b – a)	Funded Ratio (a / b)	Covered Payroll (c)	Excess as a Percentage of Covered ((b – a) / c)
6/30/2005	$ 820,501,000	$ 1,848,175,710	$ 1,027,674,710	44%	$ 460,956,060	222.90%
6/30/2006	$ 869,211,000	$ 1,930,131,983	$ 1,060,920,983	45%	$ 484,886,628	218.80%
6/30/2007	$ 933,197,000	$ 2,068,102,695	$ 1,114,905,695	45%	$ 513,486,180	217.10%

Post Employment Plan

Actuarial Valuation Date	Actual Value of Assets (a)	Actual Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (a – b)	Funded Ratio (a / b)
6/30/2007	$ 0	$ 184,232,820	$ (184,232,820)	0%
6/30/2008	$ 0	$ 186,689,632	$ (186,689,632)	0%

Other Financial Information

University of Puerto Rico
Schedules of Changes in Sinking Fund Reserve
(Unaudited)

	2008		
	Bond Service Account	Bond Reserve Account	Total
Additions:			
Transfer from Reserve Account	$ 2,198,378	$ –	$ 2,198,378
Transfer from unrestricted current funds	46,460,002	–	46,460,002
Net increase in fair marker value of investments	3,271	–	3,271
Interest Earned on Investments	608,274	2,276,617	2,884,891
Total receipts	49,269,925	2,276,617	51,546,542
Deductions:			
Payments of bond interest	29,308,028	–	29,308,028
Payments of bond principal	19,760,000	–	19,760,000
Net decrease in fair market value of investments	202,754	477,035	679,789
Transfer to Reserve Account	–	2,110,521	2,110,521
Total disbursements	49,270,782	2,587,556	51,858,338
Net decrease for the year	(858)	(310,939)	(311,796)
Balances at beginning of year	857	54,797,389	54,798,246
Balance at end of year	$ (1)	$ 54,486,450	$ 54,486,450

	2007		
	Bond Service Account	Bond Reserve Account	Total
Additions:			
Transfer from Reserve Account	$ 9,562,744	$ 16,589,826	$ 26,152,570
Transfer from unrestricted current funds	30,331,662	–	30,331,662
Net increase in fair market value of investments	1,481,868	734,124	2,215,992
Interest Earned on Investments	258,731	1,508,142	1,766,873
Total receipts	41,635,005	18,832,092	60,467,097
Deductions:			
Payments of bond interest	14,760,000	1,385,961	16,145,961
Payments of bond principal	25,230,881	–	25,230,881
Transfer to Reserve Account	1,642,113	1,861,855	3,503,968
Total disbursements	41,632,994	3,247,816	44,880,810
Net increase for the year	2,011	15,584,276	15,586,287
Balances at beginning of year	(1,154)	39,213,113	39,211,959
Balance at end of year	$ 857	$ 54,797,389	$ 54,798,246

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Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Trustees
University of Puerto Rico

We have audited the financial statements of the business-type activities and the aggregate discretely presented component units of the University of Puerto Rico (the University), as of and for the year ended June 30, 2008, which collectively comprise the University's basic financial statements and have issued our report thereon dated June 9, 2009. Our report was modified to include a reference to other auditors. One of the report of other auditors included an explanatory paragraph stating that it has experience recurring losses since it commenced operations and has a net capital deficiency that raise substantial doubt about its ability to continue as a going concern. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contain in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of Servicios Médicos Universitarios, Inc. (the Hospital) and Desarrollos Universitarios, Inc. (the Company), as described in our report on the University's financial statements. The financial statements of the Hospital and the Company were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Trustees, others within the entity, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

June 9, 2009

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