



Progress Report

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

July 2009

Progress Report, Number IV

SUMMARY

- **The Government of Puerto Rico approved a General Fund expenditure budget of \$7.67 billion for fiscal year 2009-2010, down 19% from fiscal year 2008-2009.**
- **The budget includes a payment schedule of \$893.7 million to service debt that does not have a dedicated source of payment.**
- **The Government also approved a Stabilization Fund of \$2.5 billion that will facilitate the implementation of expense reduction measures adopted by Act No. 7 of 2009.**
- **The Public-Private Partnerships Act is being implemented; a Project Investor Conference will be held in Puerto Rico on October 15-16, 2009.**

Introduction

The Government of Puerto Rico approved a spending budget of \$7.67 billion for fiscal year 2009-2010, which began July 1. The budget is 19% lower than the \$9.48 billion approved for fiscal year 2008-2009. The Government action represents a commitment to achieve fiscal balance in Puerto Rico and comes at a time when 48 mainland states are facing budget shortfalls estimated to total \$166 billion¹. The approval also sets Puerto Rico apart from states that failed to enact budgets by July 1, 2009 (California, Arizona, Pennsylvania and Illinois) or states that resorted to temporary budget extensions (Connecticut, North Carolina and Ohio).

In addition, the Government has approved amendments to Act No. 7 that resolve technical shortcomings and clarify specific legal language, but do not alter revenue forecast or expense reduction measures in the new fiscal budget.

Implementation of the Public-Private Partnerships Act is on track with specific targets and milestones over the next four months.

General Fund Budget of \$7.67 Billion Approved for Fiscal Year 2009-2010

The Government of Puerto Rico approved its General Fund budget for fiscal year 2009-2010. The approved budget of \$7.67 billion compares to \$9.48 billion for the previous fiscal year 2008-2009, a 19% reduction. The budget contains several notable features for achieving fiscal balance: 1) it is based on attainable revenue forecasts, 2) there is a Stabilization Fund to facilitate expense reduction measures in an orderly fashion, and 3) a payment schedule was enacted for existing debt that did not have dedicated sources of payment.

The Puerto Rico Treasury Department estimates General Fund net revenues for fiscal year 2008-2009 of \$7.60 billion, down 10% relative to the original net revenue forecast of \$8.48 billion (the \$9.48 billion budget approved for fiscal year 2008-2009 included \$1.0 billion of extraordinary revenue on top of the net revenue forecast). The fiscal year 2009-2010 budget is based on a forecast of a 0.92% increase in General Fund net revenues for fiscal 2009-2010. In other words, the budget for fiscal year 2009-2010 is based on total net revenues of \$7.67 billion for the General

Fund, only \$70 million higher than the most recent estimates for fiscal year 2008-2009.

Estimated GF Net Revenues for FY 2009 and FY 2010 (\$ millions)				
Revenue Categories	Estimate FY 2009	Budget FY 2010	\$ Change	% Change
Individuals	\$2,555	\$2,614	\$59	2.3%
Corporations	\$1,412	\$1,541	\$129	9.1%
Non-Resident Withholdings	\$891	\$836	(\$55)	-6.2%
Sales and Use Tax	\$911	\$606	(\$305)	-33.5%
Motor Vehicles	\$339	\$334	(\$5)	-1.5%
Alcoholic Beverages	\$282	\$288	\$6	2.1%
Permits Fees and Penalties	\$94	\$94	\$0	0.0%
Off-Shore Shipments of Rum	\$394	\$356	(\$38)	-9.6%
Temporary State Property Tax	\$0	\$230	\$230	
Other	\$722	\$771	\$49	6.8%
Total	\$7,600	\$7,670	\$70	0.9%

Source: PR Treasury Department.

The \$2.5 billion Stabilization Fund allows for an orderly implementation of the expense reduction measures adopted by Act No. 7 of 2009. The fund provides (1) \$1.0 billion to finance the cost of transitioning public employees to non-governmental sectors and providing vouchers for re-training, self-employment, relocation and salary subsidy alternatives, and (2) \$1.5 billion to cover payroll and operating expenses that will be reduced throughout fiscal year 2009-2010, but whose savings will not be realized in such fiscal year. Based on the budget of fiscal year 2008-2009, reducing Government payroll expenses by 10% could represent \$552.3 million in annual savings.

Comparison and Detail of General Fund Budgets (\$ millions)			
General Fund Main Expense Categories	Budget FY 2008 A	Budget FY 2009 A	Budget FY 2010 E
Payroll & Related Expenses	\$5,088	\$5,526	\$3,068
Incentives and Subsidies	\$1,663	\$1,703	\$1,788
Debt Payment & Amortization	\$298	\$393	\$894
Utilities and Public Facilities	\$522	\$458	\$593
Purchased Services	\$339	\$298	\$275
Others	\$1,176	\$1,105	\$1,052
Total General Fund	\$9,087	\$9,484	\$7,670
Stabilization Fund	\$0	\$0	\$2,500
Gen. Fund + Stabilization Fund	\$9,087	\$9,484	\$10,170

A = Actual.
E = Estimate and subject to change.
Source: PR Treasury Department.

The Stabilization Fund has been financed through the proceeds of COFINA's highly successful sale of First Subordinate Series A and B bonds, which closed in June 2009, raising a total of \$5.34 billion.

The approved budget also includes a payment schedule to service existing debt that did not have a dedicated source of payment. This action alleviates the credit conditions of the different entities or public corporations that will be receiving debt payments.

The amount included in the budget for debt service is \$893.7 million for fiscal year 2009-2010, compared to \$392.9 million in fiscal year 2008-2009, and covers General Obligations bonds, interest on Tax Revenue Anticipation Notes (TRANs), and other debt payable from the Central Government. The table below presents a set of existing debt that has been included in the approved General Fund budget for fiscal year 2009-2010, but whose payment was not budgeted in previous years.

Selected Existing Debt Payable from General Fund (\$ millions)

Debt Payable from Central Government	Outstanding P+I Amount	Budgeted Payment Schedule
Payable to Public Corporations		
PREPA	\$189.7	\$38.0
PRASA	\$18.4	\$3.7
PBA	\$255.0	\$51.0
Total Public Corporations	\$463.1	\$92.7
Payable to Government Dev. Bank*	\$356.1	\$44.8
Total Budgeted Payment Schedule	\$819.2	\$137.5

* Debt payable to GDB from loans to several Central Government agencies.

Technical Amendments to Act No. 7 of 2009

The Government of Puerto Rico also approved a series of technical amendments to Act No. 7 of 2009, originally enacted on March 9, 2009. Act No. 7 declared a state of fiscal emergency in Puerto Rico and adopted a comprehensive plan for fiscal and economic stabilization. The amendments do not alter the forecast of net revenues for fiscal year 2009-2010 nor

do they affect the adoption of on-going expense reduction measures.

Key amendments include:

- Restoring the tax-exemption of certain securities that were being affected by recent changes under the Alternative Minimum Tax.
- Introducing a total cap of \$40 million to tax credits related to Act No. 212 of 2002 (Urban Renewal projects) and establishing specific limitations on the claim of such credits.
- Re-introducing the Sales and Use Tax Resale Exemption Certificate to retailers with a proven sales volume higher than \$500,000. Retailers with a lower sales volume are subject to approval from the Secretary of the Treasury. The Secretary retains the right to revoke any Exemption Certificate for the period of a year if a retailer fails to comply with filing requirements related to the Sales and Use Tax.
- Extending the temporary State property tax to commercial real estate. The applicable State property tax will be 0.591%. This temporary tax will be levied for three years or until an aggregated amount of \$690 million is collected from this tax, whichever event occurs first.

Progress on Implementation of Public-Private Partnerships Act

On June 8, 2009, the Government approved Act No. 29, establishing a clear public policy and legal framework for Public-Private Partnerships in Puerto Rico as a source of new and additional funding for infrastructure improvements and more efficient services.

GDB has taken on the responsibilities to conduct all the preparatory work to launch the Puerto Rico Public-Private Partnerships Authority, as mandated by the

legislation. The table below shows the estimated dates for each implementation milestone.

Milestones*	Completion Date*
Approval PPP Act	Jun-08-2009: completed
Letter requesting potential projects from Government Entities	Jun-19-2009: completed
Launch Official Website	Late July or early August 2009
Release Administrative By-laws	Week of Jul-31-2009
PPP Authority Board is constituted	Aug-2009
Governmental Entities submit Potential Projects	Sep-08-2009
1 st Puerto Rico PPP Project Conference	Oct-15 & 16-2009

* Preliminary and subject to change

Investors will have the opportunity to learn about specific Public-Private Partnership projects during a PPP Project Investor Conference to be held in San Juan on October 15 and 16. GDB will be providing details about the conference in July and August.

The 2008 Commonwealth CAFR expected to be released during August 2009

The Commonwealth Comprehensive Annual Financial Report (CAFR) for 2008 is expected to be released during the month of August of 2009. The CAFR will be posted in the GDB website and investors will be notified immediately after its release.

¹ “New Fiscal Year Brings Painful Spending Cuts, Continued Budget Gaps in Almost Every State”, June 29, 2009, Center on Budget and Policy Priorities.

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