GOBIERNO DE PUERTO RICO
AUTORIDAD DE LOS PUERTOS

RECIBIDO FEB 2'22 AM 9:15

PRESIDENCIA DEL SENADO

1ro de febrero de 2022

**VÍA MENSAJERO**

Honorable José L. Dalmau Santiago
Presidente
Senado de Puerto Rico
Capitolio Núm. 1
Plaza de la Democracia
San Juan, Puerto Rico 00901

Estimado señor Presidente:

**ESTADOS FINANCIEROS AUDITADOS AL AÑO FISCAL 2015-2016**

Por omisión involuntaria no se remitieron los estados de referencia en la fecha de su emisión. Sin embargo, subsanando esta situación y en cumplimiento con los estatutos aplicables, se remite un disco compacto que contiene los Estados Financieros Auditados de la Autoridad de los Puertos, para el año fiscal que comprende el periodo del 1 de julio de 2015 al 30 de junio de 2016.

Estamos a sus órdenes de necesitar información adicional al respecto.

Cordialmente,

Luis A. De Jesús Clemente
Director Ejecutivo Auxiliar
en Desarrollo Económico y Finanzas

/mvr

Anejo

# PUERTO RICO PORTS AUTHORITY

(A Component Unit of the Commonwealth of Puerto Rico)

*Basic Financial Statements With Independent Auditors' Reports Thereon*

*For the Fiscal Year Ended June 30, 2016*

# PUERTO RICO PORTS AUTHORITY
(A Component Unit of the Commonwealth
of Puerto Rico)

*Basic Financial Statements With*
*Independent Auditors' Report There On*
*For the Fiscal Year Ended June 30, 2016*

**Page**

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
the Puerto Rico Ports Authority
San Juan, Puerto Rico

**Report on the Financial Statements**

We have audited the accompanying financial statements of the Puerto Rico Ports Authority (The Authority), a component unit of the Commonwealth of Puerto Rico as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the Table of Contents.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Accounting Principles Generally Accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Auditing Standards Generally Accepted in the United States of America 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 material misstatement.

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

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

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**Basis for Qualified Opinion on Governmental Activities and Note Disclosure Regarding Pensions**

As discussed in Notes 1 and 14 to the basic financial statements, the Authority has not implemented the requirements of Statement No. 68 of the Governmental Accounting Standards Board, Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27. Accordingly,

1. The Authority still has not been able to determine and account for its proportionate share of net pension obligation, deferred inflow of resources and deferred outflow of resources related to pension costs and,

2. The Authority has not recognized the effect of current period changes in net pension obligation, deferred outflow of resources and deferred inflow of resources as these relate to pension costs.

Accounting Principles Generally Accepted in the United States of America require that pension related liability, deferred outflow of resources, deferred inflow of resources, as applicable, be recognized in accordance with the parameters established by GASB Statement No. 68, as well as the effect of current period changes of the aforementioned amounts that must be recognized in pension expense during the current period. Recognition of these amounts would increase liabilities, increase deferred outflow of resources, increase deferred inflow of resources, increase the deficit, and change the pension expenses of the governmental activities. The amounts by which this departure would affect liabilities, deferred outflow of resources, deferred inflow of resources, deficit, and expenses of the governmental activities has not been determined.

The accompanying notes to the basic financial statements do not disclose the pension cost information required by GASB Statement No. 68. In our opinion, disclosure of this information is required by Accounting Principles Accepted in the United States of America.

**Qualified Opinion**

In our opinion, except for the possible effects of the matter described above in the Basis for Qualified Opinion on Government Activities and Note Disclosure Regarding Pensions paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities of the Authority as of June 30, 2016, the respective changes in financial position and its cash flows for the year then ended in accordance with Accounting Principles Generally Accepted in the United States of America.

**The Authority's ability to continue as a going concern**

The accompanying financial statements have been prepared assuming that the Authority will continue as a going concern. As discussed in Note 3 to the financial statements the indicators such as negative trend in operating losses sustancial decrease in net position, work a capital deficiency and negative cash flow; possible financial difficulties such as non payment or default of debt and/or restructuring or non compliance with capital or reserve requirements; and internal or external matters impacting the governmental entity's ability to meet its obligation as they become due, are factors that are considered in this evaluation.

Management's plans in regard to these matters are also described in Note 3. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

## Other Matters

*Emphasis of Matters*

*Airport Operations*

As discussed in Note 3 and further discussed in Note 21 to the basic financial statements, on February 28, 2013, the Authority entered into a significant transaction involving the operations of the Luis Muñoz Marín International Airport.

*Lines of Credit*

As discussed in Notes 3 and 10, most of the Lines of Credit owed to Government Development Bank (GDB), which approximate $255 million, remain unpaid since the date of the significant transaction indicated above. Therefore, the Authority is seeking to enter into a restructuring or payment plan with GDB. Some of the payments are contingent on the availability of funds from the Commonwealth to appropriate in its annual budget process.

***Required Supplementary Information Omitted***

The Authority has omitted the Schedule of the Authority's Proportionate Share of the Net Pension Liability, and the Schedule of Authority's Contributions to the Employees' Pension Plan, information that Accounting Principles Generally Accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Boards who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Our opinion on the basic financial statements is not affected by this missing information.

***Required Supplementary Information***

Accounting Principles Generally Accepted in the United States of America require that the Required Supplementary Information, such as Management's Discussion and Analysis on pages 4 through 11 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 22, 2016, on our consideration of the Authority'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 or on compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

**Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance**

We have audited the financial statements of The Authority for the year ended June 30, 2016 and have issued our report thereon dated December 22, 2016, which contain a modified opinion on those financial statements. Our audit was conducted for the purpose of forming opinion on the financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the Uniform Guidance, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with Auditing Standards Generally Accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the basic financial statements as whole.

Nieves Velázquez & Co., P.S.C.

**NIEVES VELAZQUEZ & CO., P.S.C.**
San Juan, Puerto Rico
December 22, 2016

Stamp No. 02739468 of the Puerto Rico Society of Certified Public Accountant has been affixed to the original of this report.

NIEVES VELAZQUEZ & CO., P.S.C.
LIC. NO. 7
PUERTO RICO
Certified Public Accountants

# MANAGEMENT'S DISCUSSION AND ANALYSIS
# JUNE 30, 2016

## *Introduction*

The following Management's Discussion and Analysis of the financial performance and activity of the Authority is intended to provide an introduction to its financial statements for the fiscal year ended June 30, 2016, with selected comparative information from the fiscal year ended June 30, 2015. This section has been prepared by the Authority's management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

## *Overview of Financial Results*

The Authority's net position totaled ($19.2) million at June 30, 2016, representing a ($10.1) million decrease, as compared to June 30, 2015, due principally to a $21.3 impairment loss recognized for restricted deposits held at the Government Development Bank (GDB), a reduction in net investment in capital assets of approximately $14.7 million and an additional reduction in net assets restricted for construction of approximately $10 million; offset by an increase in unrestricted net position of approximately $34 million.

This decrease in net position for 2016 (approximately $10.1 million) is approximately $53 million lower than the decrease experienced during fiscal year 2015 of approximately $63 million. This change responds principally to the $53.4 million provision for uncollectible balances made during fiscal year 2015 to the receivables from the Commonwealth OMB (approximately $14.7 million) and the Puerto Rico and Municipality Islands Maritime Transportation Authority ("PRMIMTA") (approximately $38.6 million), which did not recur in 2016. The net operating income before provisions for bad debt, the depreciation and amortization of capital assets and a 2016 favorable legal reserve adjustment of $18 million (all having no cash impact on the Authority) resulted in $32.2 million in fiscal year 2016, $21.5 million in fiscal year 2015 and $17.5 million in fiscal year 2014, thus, evidencing the consistent improvement in operations of the Authority for the past three years.

Net operating revenues totaled $103.2 million in 2016 and $103.1 million in 2015. These figures include $78.1 million of gross maritime revenues and $31.0 million of gross airport revenues, reduced by $5.5 million of provision for bad debts and $402 thousands of discounts and incentives in 2016; and $78.4 million of gross maritime revenues and $28.1 million of gross aviation revenues reduced by $2.8 million of bad debt provision and $697 thousands of discounts and incentives for 2015. The net increase of $640 thousands in maritime operating revenue is primarily due to an improvement and growth of the cruise ship traffic to Puerto Rico during fiscal year 2016. The airport operating net revenues remained relatively stable during 2016.

Operating expenses, excluding depreciation, amortization and the provisions for bad debt, totaled $53 million in 2016, which is approximately a $28.6 million improvement over 2015. This improvement resulted principally from a favorable legal reserve adjustment of $18 million made during 2016 and net reductions in salaries and general and administrative exenses in the aggregate of approximately $13.2 million.

Other notable non-operating activities during 2016 consisted of a $21.3 impairment loss on deposits held with the Government Development Bank (GDB) and gains on sale and exchange of certain real estate of approximately $7.4 million.

**Other Highlights**

The effects of the LMMIA lease and use agreements entered into with Aerostar in February 2013, continues to be seen during 2016, as the Authority recognized almost $32.8 million of additions to capital assets as a result of improvement and construction work already completed and placed in operations at the LMMIA by Aerostar.

## *Overview of the Financial Statements*

Management's Discussion and Analysis is intended to serve as an introduction to the Authority's basic financial statements, including the notes to the financial statements. The basic financial statements comprise the following: the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, the Statement of Cash Flows and the Notes to Basic Financial Statements.

### Statement of Net Position

The Statement of Net Position presents the financial position of the Authority at the end of the fiscal year and includes all of its assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position. Net position equals total assets, plus total deferred outflows of resources, less total liabilities, less total deferred inflows of resources.

A summarized comparison of the Authority's assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position follows:

| | 2016 | 2015 | Change | |
|---|---|---|---|---|
| | (In Thousands) | | In Dollars | Percentage |
| Assets: | | | | |
| Current assets | $ 32,347 | $ 35,695 | $ (3,348) | -9% |
| Non-current assets: | | | | |
| Capital assets, net | 1,284,080 | 1,254,462 | 29,618 | 2% |
| Other noncurrent assets | 47,123 | 76,617 | (29,494) | -38% |
| Total assets | 1,363,550 | 1,366,774 | (3,224) | 0% |
| Deferred outflows of resources | 12,506 | 13,589 | (1,083) | -8% |
| Total assets and deferred outflows | $ 1,376,056 | $ 1,380,363 | $ (4,307) | 0% |
| Liabilities: | | | | |
| Current liabilities | $ 228,322 | $ 191,158 | $ 37,164 | 19% |
| Non-current liabilities: | | | | |
| Loans and notes payable | 346,670 | 392,105 | (45,435) | -12% |
| Other non-current liabilities | 125,525 | 126,219 | (694) | -1% |
| Total liabilities | 700,517 | 709,482 | (8,965) | -1% |
| Deferred inflows of resources | 694,734 | 680,023 | 14,711 | 2% |
| Net position: | | | | |
| Net investment in capital assets | 636,346 | 651,009 | (14,663) | -2% |
| Restricted | 34,206 | 63,188 | (28,982) | -46% |
| Unrestricted | (689,747) | (723,339) | 33,592 | -5% |
| Total net position | (19,195) | (9,142) | (10,053) | 110% |
| Total liabilities, deferred inflows and net position | $ 1,376,056 | $ 1,380,363 | $ (4,307) | 0% |

### *Analysis of Net Position at June 30, 2016 and 2015*

The Authority's net position at June 30, 2016 includes assets of $1.36 billion, deferred outflows of resources of $12.5 million, liabilities of $701 million and deferred inflows of resources of $694.7 million. Net capital assets increased by approximately $29.6 million from 2015, as a result of net additions to construction in progress and to assets under the service concession arrangement of approximately $52.6 million, offset by the depreciation for the year (net of retirements) of approximately $23 million. Most of the additions come from improvements and work completed and placed in operations by Aerostar in LMMIA for approximately $33 million.

Decrease of approximately $29.5 million in other noncurrent assets is mostly attributed to the approximate $10 million disbursements of restricted funds over the year for their intended use and the recognition of an impairment reserve of $21.3 million on funds held at GDB. Approximately $7.7 million of the restricted funds were used for capital improvements and payment of actuarial costs for various employees retired under Act No. 27. Decrease in deferred outflows of resources of approximately $1.1 million resulted from the scheduled amortization for the year of the underlying deferred refunding losses on the existing PRIFA Bond Series.

Increases in current liabilities are mostly tied to increases of $5.2 million in amounts due to the Commonwealth Treasury Department, the Puerto Rico Retirement System and the government utilities entities for unpaid income tax withholdings, employer contributions and unpaid invoices, respectively. The other significant portion of the increase in current liabilities responds to the additional accrual of approximately $16.4 million of interest expense on the unpaid lines of credit to GDB. Deferred inflows of resources had a net increase of almost $14.7 million, responding to the approximately $32.7 million addition for Aerostar completing and placing in operations work and improvements under the LMMIA lease and use agreement, offset by the scheduled amortization for the year of almost $18 million.

Net position totaled approximately ($19.2) million at June 30, 2016, a decrease of approximately ($10.1) million from 2015. Net investment in capital assets totaled $636 million at June 30, 2016, comprising the investment in capital assets (e.g., land, buildings piers, improvements, roads and parking areas, among others), less the related outstanding indebtedness incurred to acquire those capital assets (net of the related deferred outflows of resources) and less the related deferred inflow of resources attributed to the work and improvements completed by Aerostar and placed in operations. Net position also contains approximately $34 million of net resources restricted principally for airport and maritime facilities construction and the acquisition of assets. The residual net position consists of an unrestricted deficit of $689.7 million.

### Statement of Revenues, Expenses and Change in Net Position

The change in net position is an indicator of whether the overall fiscal condition of a government has improved or worsened during the year. Following is a summary of the Statement of Revenues, Expenses and Change in Net Position for the years ended on June 30, 2016 and 2015.

## Statement of Revenues, Expenses and Change in Net Position (Continued)

| | 2016 | 2015 | Change | |
|---|---|---|---|---|
| | (In Thousands) | | In Dollars | Percentage |
| Operating revenues: | | | | |
| Maritime operations | $ 75,995 | $ 75,355 | $ 640 | 1% |
| Airport operations | 27,633 | 28,419 | (786) | -3% |
| Less discount and incentives | (402) | (697) | 295 | -42% |
| Total operating revenues | 103,226 | 103,077 | 149 | 0% |
| Non operating revenues: | | | | |
| Federal financial assistance | 13,638 | 11,315 | 2,323 | 21% |
| Contribution from Commonwealth of Puerto Rico | 25 | 2,735 | (2,710) | -99.1% |
| Gain on sale of assets | 3,499 | 3,155 | 344 | 10.9% |
| Gain on exchange of land for debt cancellation | 3,899 | - | 3,899 | 0.0% |
| Gain on favorable settlement of litigation | - | 10,460 | (10,460) | -100.0% |
| Passenger facility charges | 13 | 705 | (692) | -98.2% |
| Penalties and other fees | 61 | 126 | (65) | -52% |
| Total non operating revenues | 21,135 | 28,496 | (7,361) | -26% |
| Total revenues | 124,361 | 131,573 | (7,212) | -5% |
| Operating expenses: | | | | |
| Salaries and employee benefits | 34,296 | 38,800 | (4,504) | -11.6% |
| General and administrative | 22,694 | 31,355 | (8,661) | -28% |
| Professional services | 6,982 | 5,314 | 1,668 | 31% |
| Insurance, rent, repairs and maintenance | 7,016 | 6,135 | 881 | 14% |
| Legal claims reserve adjustment | (18,012) | - | (18,012) | 0% |
| Operating expenses before depreciation, amortization and provision for bad debts | 52,976 | 81,604 | (28,628) | -35% |
| Provision for bad debt-governmental entities | 1,598 | 53,377 | (51,779) | 97% |
| Depreciation and amortization | 23,959 | 22,652 | 1,307 | 6% |
| Total operating expenses | 78,533 | 157,633 | (79,100) | -50% |
| Non operating expenses: | | | | |
| Interest expense, net | 31,247 | 31,366 | (119) | 0% |
| Impairment loss on deposits with governmental bank | 21,273 | - | 21,273 | 0.0% |
| Grant subsidies and awards | 2,912 | 5,260 | (2,348) | -45% |
| Total expenses | 133,965 | 194,259 | (60,294) | -31% |
| Decrease in net position before early termination expense | (9,604) | (62,686) | 53,082 | -85% |
| Early termination expense | (449) | (140) | (309) | 221% |
| Decrease in net position | (10,053) | (62,826) | 52,773 | -84% |
| Net position, at beginning of year | (9,142) | 53,684 | (62,826) | -117% |
| Net position, at end of year | $ (19,195) | $ (9,142) | $ (10,053) | 110% |

## Analysis of Changes in Net Position During Fiscal Year 2016

Net maritime operating revenues, totaled $76 million compared to $75.4 million in 2015, an increase of $640 thousands that resulted principally from a superior performance in 2016 of the cruise ship traffic to Puerto Rico. Net airport operating revenues, totaled $27.6 million compared to $28.4 million in 2015, a net decrease of $786 thousands, mostly resulting from additional bad debts provision recognized during 2016.

**Analysis of Changes in Net Position During Fiscal Year 2016 (Continued)**

Non-operating revenues consist principally of passenger facility charges ("PFC"), Federal Aviation Administration (FAA) approved programs, contributions from Commonwealth and other governmental entities, penalties and other revenue. Non-operating revenues present a decrease of approximately $7.4 million during 2016, as compared to 2015. During fiscal year 2016, there were two significant non-operating revenue events: a gain of $3.5 million on the sale by the Authority of two real properties located in Hato Rey; and a $3.9 million recognized gain on a transaction where land was exchanged for a debt cancellation from a services provider. These gains were offset by the non-recurrence in 2016 of the prior year gain on the settlement of a litigation that had been filed in the past by the Authority against two airlines for breach of their space rental contract at the LMMIA. The settlement gain for the Authority was for the amount of approximately $10.5 million in 2015.

Operating expenses, excluding depreciation, amortization and the provisions for bad debt, totaled $53 million in 2016, which is almost a $29 million improvement over 2015. This improvement resulted principally from a favorable legal reserve adjustment of $18 million made during 2016 (which did not ocurr in 2015) and net reductions in salaries and general and administrative exenses in the aggregate of approximately $13.2 million. Of these reductions, approximately $4.5 million relates to salaries and employee benefits, responding from the continued aftermath effects of customary attrition during the year and having deployed in prior years early retirement programs. General and administrative expenses represent the remaining reductions of approximately $8.7 million, mostly as a result of credits granted by the government utility entities on the Authority's utility billings.

Net non-operating expenses had a net increase of $18.8 million during 2016. The increase resulted as a net effect of the recognition of an impairment loss for $21.3 million on deposits held at GDB during fiscal year 2016, which is explained in further detail in Note 4 and a decrease attributed to grant subsidies, which went down by $2.4 million. These grant subsidies represent pass-through federal funds for the Maritime Transportation Authority.

***Capital Activities***

The Authority's net costs for capital construction projects totaled approximately $19.9 million in 2016. Funding sources were as follows: $7.7 million was funded with federal contributions, $13 thousands was funded with PFC's and the balance of approximately $12 million was funded with the Authority's own monies and financing activities, including disbursements from the $25 million regional improvement fund set up in 2013 from the proceeds of the LMMIA APP Agreement described in Note 20.

***Loan and Notes Payable***

In December 2011, the Authority entered into a refinancing transaction by the issuance of Puerto Rico Infrastructure Financing Authority (PRIFA) (a component unit of the Commonwealth of Puerto Rico) bonds in a conduit debt transaction. The proceeds were used to pay various outstanding debts.

***Loan and Notes Payable (Continued)***

In February 2013, the Authority entered into a lease and use agreement with Aerostar for the LMMIA premises, receiving an advance leasehold fee of $615 million. A portion of this fee was used to pay the outstanding principal and interest balance of bonds, and partial payments of principal and interest on loans and notes payable to the GDB and other private entities. Some of the aforementioned bonds were repurchased by GDB upon the Authority's drawing of GDB letters of credit guaranteeing such bonds, as the Authority could not honor such bonds' scheduled debt service as they became due.

The outstanding principal balance of such PRIFA bonds was $197.4 million and $199.6 million at June 30, 2016 and 2015, respectively. The outstanding balance of the total notes payable amounted to $295.5 million and $296.1 million at June 30, 2016 and 2015, respectively. The reduction in the PRIFA bonds responds principally to the repayment of the amount due in 2016 of $1.6 million, while repayments of various notes amounted to approximately $1.4 million.

The Authority issued bonds at various times for the purpose of financing the construction of certain facilities and improvements for the airports and maritime facilities. There is no outstanding balance of these bonds as of June 2016.

**Failure to Implement Requirements of New Accounting Standard for Pensions**

As disclosed in Notes 2 and 14 to the basic financial statements, the Authority was not able to implement the requirements of GASB Statement No. 68, *Accounting and Financial Reporting for Pension (GASB No. 68)*. The Authority's inability to implement the requirements of GASB No. 68 resulted from the unavailability of the required information that was expected to be provided by the Employee Retirement System of the Commonwealth and its Instrumentalities (ERS), the pension trust of the Commonwealth, which is not under the Authority's management and control. Therefore, as of the date of this report, it is not known when the required information shall be provided to enable the Authority to implement the requirements of GASB No. 68 and, therefore, the Authority is not able to determine the possible impact on its basic financial statements. This situation resulted in the expression of a qualified opinion from our external auditors on the Authority.

**Liquidity Risks, Uncertainties and Recent Events**

Despite the multiple efforts undertaken by the Authority to improve its operating results, as described herein, it continues to face growing challenges and uncertainties. In relation to the lines of credit owed to GDB, most of them remain unpaid since the closing of the LMMIA lease and use agreements. Despite the fact that the Authority continues in conversations with GDB for the prospects of entering into restructuring or payment plan agreements for these balances due, the Authority still has significant lines of credit obligations to GDB, some of which have payments that are contingent on the availability of funds from the Commonwealth to appropriate in its annual budget process. These appropriations are contingent on the availability of funds from the Commonwealth and their legislative approval. The prospects of securing any Commonwealth appropriation or additional liquidity assistance from GDB have been significantly diminished by the

**Liquidity Risks, Uncertainties and Recent Events (Continued)**

passage of the Puerto Rico Emergency Moratorium and Rehabilitation Act (Act No. 21) and the Executive Order 2016-10, further described in Note 4. As a result of Act No. 21 and the Executive Order, and the issuance of the Circular Letter 1300-08-17 from the Secretary of the Treasury (see Note 21), the Authority recognized an impairment loss on all its deposits held with GDB, amounting to approximately $21 million. In addition, as discussed in Note 21 and pursuant the provisions of Act 21, the Authority has ceased to make, effective July 2016, the required monthly deposits to the trustee account needed to cover the debt service due on its PRIFA Bonds on Deceember 15, 2016. The Authority has also been designated as a covered entity under the PROMESA Act described in Note 21.

All these events described in the previous paragraph compile a trend of negative indicators defined in GASB Statement No. 56, that significantly impact the Authority's ability to fully satisfy its obligations as they become due and raises substantial doubt about the Authority's ability to continue as a going concern, as defined in GASB Statement No. 56.

***Requests for Information***

Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Department of the Puerto Rico Ports Authority, P.O. Box 362829, San Juan, Puerto Rico 00936-2829.

## PUERTO RICO PORTS AUTHORITY
## (A Component Unit of the Commonwealth of Puerto Rico)

## STATEMENT OF NET POSITION
## JUNE 30, 2016

| | 2016 (In thousands) |
|---|---|
| **Assets:** | |
| Current assets: | |
| Cash - unresctricted | $ 7,251 |
| Accounts receivable, net of allowance for doubtful accounts of $82.5 million | 20,869 |
| Prepaid expenses and other current assets | 4,227 |
| Total current assets | 32,347 |
| Non-current assets: | |
| Cash - restricted | 8,855 |
| Certificates of deposit - restricted (Note 4) | - |
| Deposits consigned in court-restricted | 25,351 |
| Due from governmental entities, net | 9,169 |
| Net pension asset | 3,748 |
| Capital assets: | |
| Non-depreciable | 955,500 |
| Depreciable, net | 328,580 |
| Total non-current assets | 1,331,203 |
| Total assets | 1,363,550 |
| **Deferred outflows of resources -** deferred loss on refunding | 12,506 |
| Total assets and deferred outflows of resources | $ 1,376,056 |

The accompanying notes are an integral part of these basic financial statements.

# PUERTO RICO PORTS AUTHORITY
## (A Component Unit of the Commonwealth of Puerto Rico)

## STATEMENT OF NET POSITION
## JUNE 30, 2016

| | | 2016 (In thousands) |
|---|---|---|
| **Liabilities:** | | |
| Current liabilities: | | |
| Loan payable, current portion | $ | 2,055 |
| Notes payable, current portion | | 144,153 |
| Accounts payable and accrued expenses | | 33,072 |
| Retainage and construction costs payable | | 4,839 |
| Termination benefits accrual, current portion | | 2,383 |
| Tenants deposits | | 1,393 |
| Interest payable | | 40,359 |
| Unearned revenues, current portion | | 68 |
| Total current liabilities | | 228,322 |
| Non-current liabilities: | | |
| Loan payable | | 195,349 |
| Notes payable | | 151,321 |
| Termination benefits accrual | | 19,258 |
| Unearned revenues | | 1,587 |
| Due to governmental entities | | 101,361 |
| Other post-employment benefits obligation | | 3,319 |
| Total non-current liabilities | | 472,195 |
| **Total liabilities** | | 700,517 |
| **Deferred inflows of resources -** | | |
| Deferred service concession arrangement receipts | | 694,734 |
| **Net position:** | | |
| Net investment in capital assets | | 636,346 |
| Restricted: | | |
| Acquisition of assets | | 25,351 |
| Construction, renewal and improvements | | 8,855 |
| Airport transaction guaranty and employees retirement (Note 4) | | - |
| Unrestricted - deficit | | (689,747) |
| **Total net position** | | (19,195) |
| Total liabilities, deferred inflows of resources and net position | $ | 1,376,056 |

*Concluded*

The accompanying notes are an integral part of these basic financial statements.

## PUERTO RICO PORTS AUTHORITY
## (A Component Unit of the Commonwealth of Puerto Rico)

## STATEMENT OF REVENUES, EXPENSES AND CHANGE IN NET POSITION
## YEAR ENDED JUNE 30, 2016

| | 2016 (In thousands) |
|---|---|
| Operating revenues: | |
| Maritime operations | $ 75,995 |
| Airport operations | 27,633 |
| Less: discount and incentives | (402) |
| Total operating revenues, net | 103,226 |
| Operating expenses: | |
| Salaries and employee benefits | 34,296 |
| General and administrative | 22,694 |
| Professional services | 6,982 |
| Insurance | 4,247 |
| Rent, repairs and maintenance | 2,769 |
| Legal claims reserve adjustment | (18,012) |
| Total operating expenses | 52,976 |
| Operating income before depreciation, amortization and provision for bad debt from governmental entities | 50,250 |
| Depreciation and amortization | (23,959) |
| Provision for bad debt from governmental entities | (1,598) |
| Operating income | 24,693 |
| Non operating revenues (expenses): | |
| Federal financial assistance | 13,638 |
| Contribution from Commonwealth of Puerto Rico | 25 |
| Passenger facility charges | 13 |
| Gain on sale of assets | 3,499 |
| Gain on exchange of land for debt cancellation | 3,899 |
| Penalties and others fees | 61 |
| Impairment loss on deposits with governmental bank | (21,273) |
| Grant subsidies and awards | (2,912) |
| Interest expense | (31,484) |
| Interest income | 237 |
| Total non operating loss, net | (34,297) |
| Decrease in net position before early termination expense | (9,604) |
| Early termination expense | (449) |
| Decrease in net position | (10,053) |
| Net position, at beginning of year | (9,142) |
| Net position, at end of year | $ (19,195) |

The accompanying notes are an integral part of these basic financial statements.

## PUERTO RICO PORTS AUTHORITY
## (A Component Unit of the Commonwealth of Puerto Rico)

## STATEMENT OF CASH FLOWS
## YEAR ENDED JUNE 30, 2016

| | 2016 (In thousands) |
|---|---|
| Cash flows from operating activities: | |
| Cash received from charges to customers | $ 86,173 |
| Cash payments to suppliers for goods and services | (33,901) |
| Cash payments to employees for services | (40,481) |
| Net cash provided by operating activities | 11,791 |
| Cash flows from capital and related financing activities: | |
| Acquisition and construction of capital assets | (21,613) |
| Proceeds from sale of capital assets | 3,570 |
| Capital contribution | 7,776 |
| Interest paid | (14,597) |
| Proceeds from notes payable | 852 |
| Repayment of loan payable | (1,650) |
| Principal payments on notes payable | (1,445) |
| Passenger facility charges received for capital expenditures | 13 |
| Net cash used in capital and related financing activities | (27,094) |
| Cash flows from non-capital and related financing activities: | |
| Penalties and other fees | 61 |
| Net change in due from (to) governmental entities | 5,903 |
| Net cash provided by non-capital and related financing activities | 5,964 |
| Cash flows provided by investing activities - | |
| Investment in certificates of deposit | 3,729 |
| Interest received | 237 |
| Net cash provided by investing activities | 3,966 |
| Net decrease in cash | (5,373) |
| Cash, beginning of year | 21,479 |
| Cash, end of year | $ 16,106 |

Continued

The accompanying notes are an integral part of these basic financial statements.

# PUERTO RICO PORTS AUTHORITY
## (A Component Unit of the Commonwealth of Puerto Rico)

## STATEMENT OF CASH FLOWS
## YEAR ENDED JUNE 30, 2016

| | 2016 (In thousands) |
|---|---|
| Reconciliation of cash: | |
| Unrestricted funds | $ 7,251 |
| Restricted funds: | |
| Construction | 8,091 |
| Renewal and replacements, maintenance and others | 764 |
| Total restricted funds | 8,855 |
| Total cash | $ 16,106 |
| Reconciliation of operating income to net cash used in operating activities: | |
| Operating income | $ 24,693 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | |
| Depreciation and amortization | 23,959 |
| Legal claims reserve adjustment | (18,012) |
| Amortization of deferred inflows of resources | (18,054) |
| Provision for due from governmental entities | 1,598 |
| Adjustment for increase in net pension asset | 164 |
| Early retirement termination expense | (449) |
| Net change in operating assets and liabilities: | |
| Decrease in accounts receivable | 1,035 |
| Decrease in prepaid expenses and other assets | 919 |
| Increase in accounts payable and accrued expenses | 837 |
| Increase in tenant deposits | 34 |
| Decrease in other employee benefits | (4,865) |
| Decrease in unearned revenues | (68) |
| Net cash provided by operating activities | $ 11,791 |
| Non-cash capital and financing activities | |
| Capital assets additions placed in operations by Aerostar credited to deferred inflows of resources | $ 32,765 |
| Exchange of land for debt cancellation | $ 3,900 |
| Impairment loss on deposits with governmental bank | $ 21,273 |

The accompanying notes are integral part of these basic financial statements.

## 1. REPORTING ENTITY

The Puerto Rico Ports Authority (the "Authority") is a component unit of the Commonwealth of Puerto Rico, (the "Commonwealth") created by Act No. 125 on May 7, 1942, as amended. The purpose of the Authority is to administer port and aviation transportation facilities of the Commonwealth and to render other related services. The Authority owns eleven airport facilities, including Luis Muñoz Marín International Airport ("LMMIA"), the main aviation port of entry into Puerto Rico, and most of government-owned maritime operations, including the Port of San Juan. The Authority's airport system consists of LMMIA, and other regional airports. Maritime operations consist principally of cargo and cruise ships with ports and docks all around Puerto Rico. See Note 20 for the Public-Private Partnership transaction regarding the administration and operations of the LMMIA (the APP or Lease and Use Agreements).

The Board of Directors is composed of five members as follows: the Secretary of Transportation and Public Works, Chairman; Secretary of Economic Development; the Executive Director of the Tourism Company of Puerto Rico, the Executive Director of Puerto Rico Industrial Development Company ("PRIDCO") and one private citizen appointed by the Governor with the consent of the Senate of Puerto Rico.

Act No. 82, approved on June 26, 1959, as amended, empowers the Authority to levy and collect a fee from the suppliers of aviation fuel and for the services and use of facilities in the Puerto Rico airports. This fee is currently two cents per gallon of aviation fuel supplied to airlines and other suppliers operating in the Puerto Rico airports.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America, as applicable to governmental units. The Authority follows Governmental Accounting Standard Board ("GASB") pronouncements under the hierarchy established by GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements. The following is a summary of the most significant accounting policies:

***Use of Estimates*** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

***Cash Equivalents*** - The Authority considers all highly liquid investments with maturities of three months or less, when purchased, to be cash equivalents. The Authority's cash composition as of June 30, 2016 is disclosed in Note 4.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

***Allowance for Doubtful Accounts*** - The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible losses on existing accounts receivable that may become uncollectible based on evaluations of collectability of accounts receivable and prior credit loss experience. Because of uncertainties inherent in the estimation process, management's estimate of credit losses in the existing accounts receivable and related allowance may change in the future.

***Prepaid Expenses*** - Prepaid expenses consist mostly of insurance policies and certain material and office supplies.

***Capital Assets -*** Capital assets are stated at cost or at estimated historical cost. The cost of property and equipment includes costs for infrastructure assets, equipment and other related costs, buildings, furniture and equipment. Costs for infrastructure assets include construction costs, design and engineering fees and other direct costs incurred during the construction period.

Capital assets are defined by the Authority as assets with an initial, individual cost of $500 or more and an estimated useful life over one year. Costs to acquire additional capital assets, which replace existing assets or otherwise prolong their useful lives, are generally capitalized. The costs of normal maintenance and repairs that do not add to the value of the assets or do not materially extend assets lives are not capitalized.

Interest cost is capitalized as part of the historical cost of acquiring certain assets. During the construction period, the interest costs related with specific assets qualify for interest capitalization.

Depreciation is computed using the straight-line method during the estimated useful lives of the related assets. The useful lives of assets are determined by the Authority's Engineering Department using past experience, standard industry expectations, and information from external sources such as consultants, manufacturers and contractors. Useful lives are reviewed periodically for each specific type of asset.

Asset lives used in the calculation of depreciation are generally as follows:

| | |
|---|---|
| Buildings, piers, improvements and other structures | 30 to 50 years |
| Other infrastructure | 5 to 25 years |
| Machinery, furniture and equipment | 3 to 10 years |
| Runways, roadways and other paving | 10 to 20 years |
| Utility infrastructure | 10 to 20 years |
| Automobile and service vehicles | 3 to 10 years |
| Infrastructure master plans | 5 years |

Those assets located at facilities leased by the Authority from others are depreciated over the lesser of the remaining term of the lease or the related asset lives.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *Capital Assets (Continued)*

Capital assets related to the LMMIA under the APP Agreements described in Note 20 are maintained at the Authority's books and also stated at cost or at estimated historical cost. Construction in progress made by Aerostar after the closing of the APP Agreements is not recorded by the Authority while such construction is still in progress and not ready for use and operation; at completion, such constructed assets and improvements will be recognized at their corresponding fair value. The capital assets related to the APP Agreements are not being depreciated since the closing date of the APP Agreements because the APP Agreements require Aerostar to return the related LMMIA facilities to the Authority in its original or enhanced condition. Such capital assets continued to apply existing capital asset guidance, including depreciation through February 27, 2013, the closing date of the APP Agreements. The carrying amount of capital assets, excluding construction in progress, under the APP Agreements amounted to approximately $599 million at June 30, 2016. This amount includes approximately $124.6 million of improvements and construction work already completed and placed in operations by Aerostar (approximately $32.8 million of which were completed and placed in operations during fiscal year 2016) therefore added to the carrying amount of capital assets under the APP Agreements.

During the year ended June 30, 2016, the Authority performed an assessment of impairment on capital assets under the provisions of Statement on Governmental Accounting Standard (GASB) No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries,* which establishes that, generally, an asset is considered impaired when its service utility has declined significantly and unexpectedly, and the event or change in circumstances is outside the normal life cycle of the asset. Management is then required to determine whether impairment of an asset has occurred. Impaired capital assets that will no longer be used by the Authority should be reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by the Authority should be measured using the method that best reflects the diminished service utility of the capital asset. Impairment of capital assets with physical damage generally should be measured using a restoration cost approach, an approach that uses the estimated cost to restore the capital asset to identify the portion of the historical cost of the capital asset that should be written off. During 2016, management did not identify any impairment of capital assets.

In addition, GASB Statement No. 49, "*Accounting and Financial Reporting for Pollution Remediation Obligations*," applicable for periods beginning after December 15, 2007, addresses accounting and financial reporting principles for pollution (including contamination) remediation obligations which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the statement excludes pollution prevention or control obligations with respect to current obligations, and future pollution activities that are required upon retirement of an asset, such as post-closure care. As of June 30, 2016, the Authority maintains an environmental reserve of approximately $3 million, which in the opinion of management is adequate to cover the

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

***Capital Assets (Continued)***

contingency exposure, if any. Such reserve is included as part of accounts payable and other accrued liabilities in the accompanying statement of net position. In establishing such reserve, management has evaluated its tenants' responsibilities in environmental and pollution exposures.

***Claims and Judgments*** - The estimated amount of the liability for claims and judgments is recorded on the accompanying statement of net position based on the Authority's evaluation of the probability of an unfavorable outcome in the litigation of such claims and judgments. The Authority consults with legal counsel upon determining whether an unfavorable outcome is expected. Refer to disclosures included in Note 15.

***Compensated Absences*** - Employees earn vacation benefits at a rate of 30 days per year, which is the maximum permissible accumulation. Employees accumulate sick leave at the rate of 20 days per year. Maximum permissible accumulation for sick leave is 60 days for managerial and clerical employees of which the excess was normally paid within the next fiscal year. Union employees were paid for accumulations over 26 days within the next fiscal year. However, effective with the approval of Act No. 66 of June 17, 2014, known as the Fiscal Operation and Sustainability Act, such excess has ceased to be paid to employees. The Authority records as a liability and as an expense the vested accumulated vacation and sick leave as benefits accrue to employees. Compensated absences as of June 30, 2016, amounted to approximately $6.2 million and are included as a component of accounts payable and accrued expenses in the accompanying statement of net position.

***Termination Benefits*** – The Authority accounts for termination benefits in accordance with the provisions of GASB No. 47, *Accounting for Termination Benefits*, which indicates that employers should recognize a liability and expense for *voluntary* termination benefits when the offer is accepted and the amount can be estimated. A liability and expense for *involuntary* termination benefits should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees, and the amount can be estimated. Refer to disclosure included in Note 13.

***Postemployment Benefits Other Than Pensions*** - The Authority accounts for postemployment benefits other than pensions ("OPEB") under the provisions of the GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This statement requires a systematic, accrual–basis measurement and recognition of OPEB cost (expense) over a period that approximates employees' years of service and provides information about actuarial accrued liabilities associated with OPEB and whether and to what extent progress is being made in funding the plan. GASB No. 45 allows employers to amortize the portion of the cost attributed to past service over a period not to exceed thirty (30) years. Refer to disclosure included in Note 12.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

***Retirement Benefits under the Employees' Retirement System of the Government of the Commonwealth* -** The employees of the Authority participate in the Employees' Retirement System of the Government of the Commonwealth (ERS), which was created pursuant Act No. 447 of May 15, 1951, as amended. This retirement system is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by and reported as a component unit of the Commonwealth. This retirement system consists of different benefit structures, including a cost-sharing, multiple-employer defined benefit program; a defined contribution program and a defined contribution hybrid program. As further discussed in Note 14, the ERS did not provide the Authority the information needed to adopt in prior year, GASB Statement No. 68, *Accounting and Financial Reporting for Pension-an amendment of GASB Statement No. 27* and GASB Statement No.71, *Pension Transition for Contributions made Subsequent to the Measurement Date*. Such required information has not been provided either for the current year; therefore the Authority has been unable to adopt this accounting pronouncement that would have required a different set of rules and provisions to account for the Authority's allocated share of the Comonwealth's resulting net pension liability and related accounts. Consequently, the Authority has maintained the accounting for pension costs in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers (GASB No. 27)*. This statement establishes standards for the measurement, recognition and display of pension expense and related liabilities in financial statements of state and local governmental employers, mostly based on funding requirements.

***Other Retirement Benefits under a Collective Bargaining Agreement*** - The Authority accounts for the pension costs resulting from a specific collective bargaining agreement pension plan, pursuant the provisions of GASB No. 27. As further discussed in the Accounting Principles Adopted paragraph, the accounting and financial reporting for the pension costs pertaining to this particular plan, would fall under the provisions of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Certain provisions of GASB Statement No. 73, became effective July 1, 2015; however, the specific provisions requiring the application of the accounting and financial reporting concepts similar to those of GASB Statement No. 68 are not effective until fiscal year 2017.

***Deferred Outflows of Resources*** – The deferred outflow of resources represent the consumption of net assets by the Authority that is applicable to a future reporting period. Deferred outflows of resources for the Authority is specifically related to a refunding loss associated to an issuance of PRIFA bonds and a swap agreement cancellation. This refunding loss is being amortized over the life of the PRIFA bonds that remain outstanding. The amortized amount during fiscal year 2016 is reported as a component of interest expense in the accompanying statement of revenues, expenses and change in net position.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

***Deferred Inflows of Resources*** – Deferred inflows of resources represent the acquisition of net assets by the Authority that is applicable to a future reporting period. In relation to the APP Agreements described in Note 20, on February 27, 2013, the Authority received an upfront fee of $615 million, the promise of annual payments of $2.5 million for the next five years, present valued at approximately $10.5 million; and also recognized a contractual obligation of $3.068 million to perform certain capital improvements. These resources were received in exchange for awarding Aerostar the right to operate, manage, maintain, develop and rehabilitate the LMMIA for a term of 40 years. The upfront fee and the promise of annual payments are considered deferred inflows of resources, which are recognized into revenue under the straight-line method over the APP Agreements term of 40 years. The amount recognized into revenue during fiscal year 2016 amounted to approximately $18.1 million and is recognized within operating revenues-airport in the accompanying Statement of Revenues, Expenses and Change in Net Position.

***Net Position*** - Net position is classified in the following components:

***Net Investment in Capital Assets*** - This component of net position consists of capital assets net of accumulated depreciation and reduced by the outstanding balance of any bonds, mortgages, notes, or other borrowings that are directly attributable to the acquisition, construction or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds or deferred inflows of resources at year-end, the portion of the debt or deferred inflows of resources attributable to the unspent amount is not included in the calculation of this component of net position. Rather, that portion of the debt or deferred inflows of resources is included in the same net position component (restricted or unrestricted) as the unspent amount.

***Restricted*** – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported. Restricted assets result when contraints placed on those assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

***Unrestricted*** – This component of net position is the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

As of June 30, 2016, the reconciliation of net position was as follows:

| | | 2016 (In thousands) |
|---|---|---|
| Net capital assets | $ | 1,284,080 |
| Liabilities directly attributable to capital assets: | | |
| Loan payable | | (197,404) |
| Notes payable | | (295,474) |
| Retainage payable to contractors | | (4,839) |
| Accrued interest | | (40,359) |
| Deferred inflows of resources - related to assets improvement | | (122,164) |
| Deferred outflow of resources - deferred loss on refunding | | 12,506 |
| Net investment in capital assets | $ | 636,346 |
| | | |
| Restricted funds, including certificates of deposit | $ | 8,855 |
| Deposit consigned with court restricted for capital asset | | 25,351 |
| Restricted net position | $ | 34,206 |

***Revenue Recognition*** - The Authority distinguishes operating revenues and expenses from non-operating items. Revenues associated with maritime and airport operations are recorded as operating revenues. Expenses related to the administration and maintenance of piers and airports, repairs and maintenance of corresponding roads and equipment, and the Authority's administrative expenses are recorded as operating expenses. All other revenues and expenses are considered non-operating.

***Non-Operating Revenues*** - Non-operating revenues consist principally of federal financial assistance, Commonwealth of Puerto Rico appropriations, favorable legal claims reserve adjustment, passenger facility charges, fuel flowage fee, interest and penalties, gain on sale of assets, and other fees. Federal financial assistance and Commonwealth of Puerto Rico appropriations are funds assigned by federal and local government entities such as the Federal Aviation Administration ("FAA"), Federal Transit Administration ("FTA"), and the Transportation Security Administration ("TSA") to the Authority for the exclusive purpose of the construction of specific projects or infrastructure, repairs and maintenance. Capital grants of the Authority are reported as non-operating revenues.

***New Accounting Principles Adopted -*** Several new accounting principles became effective July 1, 2015; however, only the following new accounting principles were of relevance and applicability to the Authority:

- GASB Statement No. 72, *Fair Value Measurement and Application*. This Statement requires a government to use valuation techniques that are appropriate under the circumstances and for which sufficient data are available to measure fair value. The techniques should be consistent with one or more of the following approaches; the market approach, the cost approach, or the income approach. This Statement also establishes a hierarchy of inputs to valuation techniques used to measure fair value. That hierarchy has three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the assets or liability, either directly or indirectly. Finally, Level 3 inputs are unobservable inputs, such as management's assumptions of the default rate among underlying mortgages of a mortgage-backed security.

**2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***New Accounting Principles Adopted (Continued)***

This Statement requires all investments, with certain exceptions, to be measured at fair value, using the valuation techniques described in the previous paragraph. Accordingly, the Statement defines an investment as a security or other asset that: a) a government holds primarily for the purpose of income or profit and b) has present service capacity based solely on its ability to generate cash or to be sold to generate cash. Other than cash and certificates of deposits with carrying amounts approximating their fair value, the Authority also holds income-producing real estate property that may appear to meet the aforementioned definition of an investment; however, the Authority's existing real estate property, although income-generating, are essentially held since acquisition as capital assets needed to provide port and aviation services to the Commonwealth's constituency. Accordingly, these capital assets are not considered investments, hence not carried at fair value, but rather at cost. There was no material impact on the Authority's financial statements as a result of the implementation of this Statement.

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. This Statement extends the approach to accounting and financial reporting established in Statement No. 68 to the Authority's retirement benefit plan existing under a collective bargaining agreement, to reflect that for accounting and financial reporting purposes, any assets accumulated for pensions that are provided through pension plans that are not administered through trusts that meet the criteria specified in Statement No. 68, should not be considered pension plan assets. It also requires that information similar to that required by Statement No. 68 be included in the notes to the financial statements and required supplementary information by all similarly situated employers and nonemployer contributing entities. The requirements of this Statement that address financial reporting for assets accumulated for purposes of providing those pensions are effective July 1, 2015, and such have been applied by the Authority since the assets that the Authority accumulates for the payment of benefits as they come due come from the Authority's own funding and are kept, if any, as assets of the Authority and not the plan. In addition, such collective bargaining plan is currently unfunded and holds no plan assets that could have otherwise be required to be presented as assets of the Authority. Therefore, there was no impact on the Authority's financial statements as a result of the implementation of this particular Statement requirement. On the other hand, the requirements of this Statement that address the accounting and financial reporting by employers similar to that required by Statement No. 68 are not effective until fiscal year 2017.

**2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***New Accounting Principles Adopted (Continued)***

- GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The "GAAP hierarchy" consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and non-authoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. There was no material impact on the Authority's financial statements as a result of the implementation of this Statement.

***Future Adoption of Accounting Principles -*** The GASB has issued the following accounting principles that have effective dates for the Authority after its June 30, 2016 year end:

- GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. This Statement replaces Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, as amended, Statement No. 43, and Statement No. 50, *Pension Disclosures*. The scope of this Statement includes OPEB plans—defined benefit and defined contribution—administered through trusts that meet the following criteria:

  - ✓ Contributions from employers and non-employer contributing entities to the OPEB plan and earnings on those contributions are irrevocable.

  - ✓ OPEB plan assets are dedicated to providing OPEB to plan members in accordance with the benefit terms.

  - ✓ OPEB plan assets are legally protected from the creditors of employers, non-employer contributing entities, and the OPEB plan administrator. If the plan is a defined benefit OPEB plan, plan assets also are legally protected from creditors of the plan members.

  This Statement also includes requirements to address financial reporting for assets accumulated for purposes of providing defined benefit OPEB through OPEB plans that are not administered through trusts that meet the specified criteria. The provisions of this statement are effective for fiscal years beginning after June 15, 2016.

**2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Future Adoption of Accounting Principles (Continued)***

Management is evaluating the impact that this Statement will have on the Authority's basic financial statements.

- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This Statement replaces the requirements of Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for OPEB. Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, establishes new accounting and financial reporting requirements for OPEB plans. The scope of this Statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed. In addition, this Statement details the recognition and disclosure requirements for employers with payables to defined benefit OPEB plans that are administered through trusts that meet the specified criteria and for employers whose employees are provided with defined contribution OPEB. This Statement also addresses certain circumstances in which a non-employer entity provides financial support for OPEB of employees of another entity. The provisions of this statement are effective for fiscal years beginning after June 15, 2017. Management is evaluating the impact that this Statement will have on the Authority's basic financial statements.

- GASB Statement No. 77, *Tax Abatement Disclosures*. This Statement establishes financial reporting standards for tax abatement agreements entered into by state and local governments. The disclosures required by this Statement encompass tax abatements resulting from both (a) agreements that are entered into by the reporting government and (b) agreements that are entered into by other governments and that reduce the reporting government's tax revenues. The provisions of this Statement should be applied to all state and local governments subject to such tax abatement agreements. For financial reporting purposes, a tax abatement is defined as a reduction in tax revenues that results from an agreement between one or more governments and an individual or entity in which (a) one or more governments promise to forgo tax revenues to which they are otherwise entitled and (b) the individual or entity promises to take a specific action after the agreement has been entered into that contributes to economic development or otherwise benefits the governments or the citizens of those governments. A transaction's substance, nor its form or title, is a key factor in determining whether the transaction meets the definition of a tax abatement for the purpose of this Statement. The provisions of this Statement are effective for financial

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *Future Adoption of Accounting Principles (Continued)*

statements for periods beginning after December 15, 2015. This Statement is not expected to be applicable to the Authority.

- GASB Statement No. 80, *Blending Requirements for Certain Component Units*. This Statement improves financial reporting by clarifying the financial statement presentation requirements for certain component units. This Statement amends the blending requirements established in paragraph 53 of Statement No. 14, *The Financial Reporting Entity*, as amended. This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary goverment is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. This Statement is not expected to be applicable to the Authority.

- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*. This Statement improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. Split-interest agreements are a type of giving agreement used by donors to provide resources to two or more beneficiaries, including governments. Split-interest agreements can be created through trusts, or other legally enforceable agreements with characteristics that are equivalent to split-interest agreements, in which a donor transfers resources to an intermediary to hold and administer for the benefit of a government and at least one other beneficiary. Examples of these types of agreements include charitable lead trusts, charitable remainder trusts, and life-interests in real estate. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period. This Statement is not effective until fiscal year 2018. This Statement is not expected to be applicable to the Authority.

- GASB Statement No. 82, *Pension Issues- an Amendment of GASB Statements No 67, No. 68 and No. 73*. This Statement addresses certain issues that have been raised with respect to GASB Statements No. 67, No. 68, and No. 73. The Statement is designed to improve consistency in the application of the pension standards by clarifying or amending related areas of existing guidance. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of

## 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *Future Adoption of Accounting Principles (Continued)*

deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. Prior to the issuance of this Statement, GASB Statements No. 67 and No. 68 required presentation of covered-employee payroll, which is the payroll of employees that are provided with pensions through the pension plan, and ratios that use that measure, in schedules of required supplementary information. This Statement amends GASB Statements No. 67 and No. 68 to instead require the presentation of covered payroll, defined as the payroll on which contributions to a pension plan are based, and ratios that use that measure. This Statement clarifies that a deviation, as the term is used in Actuarial Standards of Practice issued by the Actuarial Standards Board, from the guidance in an Actuarial Standard of Practice is not considered to be in conformity with the requirements of GASB Statement No. 67, GASB Statement No. 68, or GASB Statement No. 73 for the selection of assumptions used in determining the total pension liability and related measures. This Statement clarifies that payments that are made by an employer to satisfy contribution requirements that are identified by the pension plan terms as plan member contribution requirements should be classified as plan member contributions for purposes of GASB Statement No. 67 and as employee contributions for purposes of GASB Statement No. 68. It also requires that an employer's expense and expenditures for those amounts be recognized in the period for which the contribution is assessed and classified in the same manner as the employer classifies similar compensation other than pensions (for example, as salaries and wages or as fringe benefits). This Statement is not effective until fiscal year 2017, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. Management is evaluating the impact that this Statement will have on the Authority's basic financial statements.

## 3. FINANCIAL CONDITION AND MANAGEMENT PLANS – LIQUIDITY RISKS AND UNCERTAINTIES

The ensuing discussion on the following paragraphs about the Authority's liquidity risks, uncertainties and their remediation plans provide the necessary background and support for management's evaluation, as required by GASB Statement No. 56, as to whether there is a substantial doubt about the Authority's ability to continue as a going concern for 12 months beyond the financial statements date or for an extended period, if there is currently known information that may raise substantial doubt shortly thereafter. Statement No. 56 establishes that the continuation of a legally separate governmental entity as a going concern is assumed in financial reporting in the absence of significant information to the contrary. Information that may significantly contradict the going concern assumption would relate to a governmental entity's inability to continue to meet its obligations as they become due without substantial disposition of assets outside the ordinary course of governmental operations, restructuring of debt, submission to the oversight of a separate fiscal assistance authority or financial review

## 3. FINANCIAL CONDITION AND MANAGEMENT PLANS – LIQUIDITY RISKS AND UNCERTAINTIES (Continued)

board, or similar actions. Indicators such as negative trends in operating losses and negative cash flows; possible financial difficulties such as nonpayment or default of debt and/or restructurings or noncompliance with capital or reserve requirements; and internal or external matters impacting the governmental entity's ability to meet its obligations as they become due, are factors that are considered in this evaluation.

Over the past years since 2010, the Authority has seen its net position decrease from $337 million at June 30, 2010 to the current level of ($19.2) million at June 30, 2016. The Authority's net position decreased by $10.1 million during the year ended June 30, 2016 and had a working capital deficiency of approximately $195 million at June 30, 2016. The Authority also has over $285 million in lines of credit payable to GDB, most of them as a result of the drawing of certain letters of credit from GDB guaranteeing certain bonds, which the Authority could not honor.

In order to reverse this trend and instill some stability in the Authority's operations, management entered in 2013 into the LMMIA lease and use agreements, as further described in Note 20. This transaction became the centerpiece strategy around which certain cost cutting measures and revenue-base enhancing activities for regional airports and maritime operations have been implemented, while others are in progress, all of which are expected to improve the Authority's financial condition and refocus the objectives of the Authority into the future.

As further described in Notes 9, 10 and 20, the Authority refinanced during fiscal year 2012 the majority of its long-term debt through a Puerto Rico Infrastructure Financing Authority's (PRIFA) conduit debt issuance of $678.4 million, in anticipation of the LMMIA lease and use agreements. The lease and use agreements involving the LMMIA generated an upfront leasehold fee of $615 million for the Authority, $500 million of which were used to cancel and fully redeem certain outstanding debt and related interests, relieving the Authority from the corresponding applicable debt service requirements. That is, the Authority's then existing debt was reduced by more than half as a result of the LMMIA lease and use agreements. Consequently, interest expense has already seen a reduction from approximately $63 million in 2013 to approximately $31 million during the past two years. Another $50 million from the aforementioned leasehold fee were reserved and set aside for the early termination of several employees, commencing effective June 30 and July 15, 2013, which provided payroll savings past two years. For instance, basic salary expenses have gone down from approximately $27 million in 2013 to approximately $15.7 million and $17 million during 2016 and 2015, respectively; while total salaries expense including benefits and bonuses have decreased from approximately $58 million to $34.3 million, as a result of the various early retirement plans adopted since 2011. In addition, $25 million were also set aside for improvements to the regional airports in order to attract visitors and increase demand and revenues. One of such improvements covered the Aguadilla regional airport for the establishment of the Lufthansa's central operations of its fleet maintenance hub. For instance, since the closing of the LMMIA lease and use agreements, expenditures for the improvements and expansion of regional airports have created an additional rental revenue base at these airports that has materialized into an increase in rental revenue base of approximately $1 million since 2014, even though further projects continue in development. Future completion of the established development plans for the regional airports is expected to add more space rental room opportunities and increase passenger flow.

**3. FINANCIAL CONDITION AND MANAGEMENT PLANS – LIQUIDITY RISKS AND UNCERTAINTIES (Continued)**

On June 17, 2014, the Governor of the Commonwealth signed into law Act No. 66, known as the *Fiscal Operation and Sustainability Act*. This Act requires that all instrumentalities, entities, agencies and public corporations of the Commonwealth reduce their operating expenses, specifically those related to payroll and related benefits, professional services, contracted services and leases, among others. During the effective term of this Act, the excess accumulation of vacation and sick leave will not be paid to employees; instead, the Act requires that employees exhaust such excess accumulation by the end of each fiscal year. This Act will remain in effect until July 1, 2017 or before that date if certain financial metrics are achieved by the Commonwealth. As a result of the Authority's execution of the provisions of Act No. 66, the 2015 operating budget for the expense categories identified above presented an approximately $10.3 million savings when compared to the 2014 actual amounts and the 2016 and 2017 operating budgets have remained relatively stable when compared to 2015.

Management of the Authority has also reacted responsibly with respect to its delinquent obligations by actively pursuing feasible payment plans for balances due to the Commonwealth's Treasury Department and the Puerto Rico Retirement Systems (see Note 6), as well as with the government utilities and most suppliers. These special payment arrangements have maintained an organized and steady cash flow strategy for the Authority while meeting its obligations.

Despite the aforementioned efforts undertaken by the Authority, it continues to face growing challenges and uncertainties. In relation to the lines of credit owed to GDB, most of them remain unpaid since the closing of the LMMIA lease and use agreements. Despite the fact that the Authority continues in conversations with GDB for the prospects of entering into restructuring or payment plan agreements for these balances due, the Authority still has significant lines of credit obligations to GDB, some of which have payments that are contingent on the availability of funds from the Commonwealth to appropriate in its annual budget process. These appropriations are contingent on the availability of funds from the Commonwealth and their legislative approval. The prospects of securing any Commonwealth appropriation or additional liquidity assistance from GDB have been significantly diminished by the passage of the Puerto Rico Emergency Moratorium and Rehabilitation Act (Act No. 21) and the Executive Order 2016-10, further described in Note 4. As a result of Act No. 21 and the Executive Order, and the issuance of the Circular Letter 1300-08-17 from the Secretary of the Treasury (see note 21), the Authority recognized an impairment loss on all its deposits held with GDB, amounting to approximately $21 million. In addition, as discussed in Note 21 and pursuant the provisions of Act 21, the Authority has ceased to make, effective July 2016, the required monthly deposits to the trustee account needed to cover the debt service due on its PRIFA Bonds on December 15, 2016. The Authority has also been designated as a covered entity under the PROMESA Act described in Note 21.

All these events described in the previous paragraph compile a trend of negative indicators defined in GASB Statement No. 56, that significantly impact the Authority's ability to fully satisfy its obligations as they become due and raises substantial doubt about the Authority's ability to continue as a going concern, as defined in GASB Statement No. 56.

## 4. CASH AND CERTIFICATES OF DEPOSIT

At June 30, 2016, cash amounted to approximately $16.1 million. There were no cash equivalents at June 30, 2016. Cash balances are detailed as follows:

| | 2016 (In thousands) |
|---|---|
| Restricted funds: | |
| For construction | $ 8,091 |
| Renewal and replacements, maintenance and other | 764 |
| Total restricted | 8,855 |
| Unrestricted fund | 7,251 |
| Total cash | $ 16,106 |

At June 30, 2016, the Authority also had two (2) certificates of deposit at GDB amounting to approximately $19.2 million in the aggregate. These certificates of deposit, bear interest from 0.9% to 1.25%, are restricted as a guaranty fund for the LMMIA transaction (approximately $15.3 million) and for regional airports improvements (approximately $3.9 million), and mature on May 19, 2017 and July 11, 2016, respectively.

The Authority is restricted by law to deposit funds only in institutions approved by the Puerto Rico Treasury Department, and such deposits are required to be kept in separate accounts in the name of the Authority. Pursuant to the Investment Guidelines for the Commonwealth of Puerto Rico adopted by the Government Development Bank ("GDB"), the Authority may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, banker's acceptances, or in pools of obligations of the municipalities of Puerto Rico, among others. Monies in the sinking fund, if any, can only be invested in direct obligations of the United States government, or obligations unconditionally guaranteed by the United States government, and/or interest-bearing time deposits, or other similar arrangements, as provided by bond resolutions, as applicable.

### Custodial Credit Risk and Impairment Loss on Deposits with GDB

For deposits, custodial credit risk is the risk that in the event of bank failure, the Authority's deposits may not be recovered by the Authority. However, under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. The bank balance and carrying amount of the Authority's accounts with commercial banks at June 30, 2016, amounted to $13.4 million and $12.0 million, respectively.

As of June 30, 2016, the Authority's custodial credit risk was approximately $25.3 million, which is the bank balance of cash and certificates of deposit with GDB and Economic Development Bank for Puerto Rico ("EDB"). These deposits are exempt from the collateral requirements established by the Commonwealth. GDB faces significant risks and uncertainties and it currently does not have sufficient liquid financial resources to meet obligations when they come due, as further described below. Pursuant to recently enacted legislation, the Governor of the Commonwealth has ordered the suspension of loan disbursements by GDB and imposed restrictions on the withdrawal and transfer of deposits from GDB, among other measures.

## 4. CASH AND CERTIFICATES OF DEPOSIT (Continued)

On April 6, 2016, the Governor signed into law the Puerto Rico Emergency Moratorium and Rehabilitation Act (Act No 21). Among other objectives, Act No. 21 allows the Governor to declare a moratorium on debt service payments and to stay related creditor remedies for a temporary period for the Commonwealth, the GDB, the EDB, and certain additional government instrumentalities in Puerto Rico. The temporary period set forth in Act No. 21 lasts until January 31, 2017, with a possible two-months extension in the Governor's discretion.

On April 8, 2016, the Governor signed Executive Order 2016-010 (EO 10), which declares an economic emergency in GDB. EO 10, in accordance with the emergency powers provided for in Act No. 21, implemented a regulatory framework governing GDB's operations and liquidity, including prohibiting loan disbursements by GDB and establishing a procedure with respect to governmental withdrawals, payments, and transfer requests with respect to funds held on deposit at GDB to that effect. EO 10 restricts the withdrawal, payment and transfer of funds held on deposit at GDB to those reasonable and necessary to ensure the provision of essential services and authorizes GDB to establish weekly limits on the aggregate amount of such disbursements. Moreover, EO 10 prohibits GDB's depositors from printing or writing checks creditable against their accounts at GDB, unless they obtain a temporary waiver from GDB. In addition, as further described in Note 21, on October 18, 2016, the Secretary of the Treasury issued Circular Letter 1300-08-17 (CC 1300-08-17) alerting all agencies and public corporations of the Commonwealth about the conditions affecting GDB as previously described and that as a result of such conditions, management of GDB believes there is significant doubt about GDB's ability to continue as a going concern. Accordingly, CC 1300-08-17 advises all such agencies and public corporations with deposits held at GDB to perform the necessary impairment analysis on the realizability of these deposits as it is probable that GDB will not be able to honor them and all its other remaining debt obligations beyond a reasonable period of time.

As GDB serves as the depositary of some of the Authority's funds, the Authority's cash and time deposits with GDB, pursuant EO 10, will be subject to strict restrictions and limitations, as described herein; therefore, an impairment loss on these deposits has been recorded on the Authority's financial statements as follows (expressed in thousands):

| | | Deposits Held with GDB at June 30, 2016 | | |
|---|---|---|---|---|
| **Type of Deposit** | | **Deposit Balance** | **Impairment Loss** | **Book Balance** |
| Cash | $ | 2,088 | (2,088) | – |
| Certificates of deposit | | 19,185 | (19,185) | – |
| **Total** | $ | 21,273 | (21,273) | – |

## 5. DEPOSITS CONSIGNED IN COURT - RESTRICTED

During November 2011, pursuant the objectives of the LMMIA Project, the Authority entered into certain expropriations proceedings through the Puerto Rico First Instance Court (the “Court”), to acquire certain properties and concessions owned by third parties within the LMMIA complex. In connection with such proceedings, on December 27, 2011, the Authority obtained a $30 million non-revolving credit facility with the GDB, out of which $25.4 million were consigned with the Court to start the expropriation process (this facility is known as the Caribbean Airport Facilities). The credit facility was fully repaid with the proceeds from the LMMIA concession agreement. At June 30, 2016, the $25.4 million deposited in Court is presented as restricted in a separate line item in the accompanying Statement of Net Position.

## 6. DUE FROM/DUE TO GOVERNMENTAL ENTITIES

Due from governmental entities as of June 30, 2016 consists of:

| | 2016 (In thousands) |
|---|---|
| Office of Management and Budget | $ 14,750 |
| Puerto Rico and Municipality Islands Maritime Transportation Authority (PRMIMTA) | 38,710 |
| Puerto Rico Highways and Transportation Authority (PRHTA) | 6,194 |
| Puerto Rico Tourism Company (PRTC) | 1,515 |
| Federal Aviation Administration (FAA) | 2,975 |
| Subtotal | 64,144 |
| Less: allowance for doubtful receivable | (54,975) |
| | $ 9,169 |

***Office of Management and Budget ("OMB")*** - Balance due from the OMB relates to $14.7 million incentives given by the Authority to certain cruise lines, which should be reimbursed by the OMB. The balance does not bear interest and has no formal repayment terms, since the terms and conditions have not been established. Although the Authority has established a reserve for this balance, management is evaluating alternative courses of actions in order to continue pursuing the collection of this outstanding balance.

***Puerto Rico and Municipality Islands Maritime Transportation Authority (“PRMIMTA”)*** - Balance due from PRMIMTA of $38.7 million mainly relates to expenses incurred by the Authority, such as payroll, on behalf of the PRMIMTA from 2000 to 2006. The balance does not bear interest and has no formal repayment terms at June 30, 2016. Although the Authority has established a reserve for this balance, management is evaluating alternative courses of actions, which will entail the combination of various transactions and administrative proceedings that would go in line with the already approved restructuring and merger of PRMIMTA’s operations into the new *Integrated Transport Authority of Puerto Rico (ITAPR),* created by Act No. 123 of August, 3, 2014. In addition, the Puerto Rico Public Private Partnership Authority (the PPPA) has already published requests for proposal for the establishment of a service concession arrangement for the operation and maintenance of the collective transportation services administered by ITAPR. The Authority will be actively pursuing the introduction of some action plan within the context of this expected public private partnership arrangement that would facilitate or create the conditions conducive to a potential repayment of ITAPR’s debt with the Authority.

## 6. DUE FROM/DUE TO GOVERNMENTAL ENTITIES (Continued)

***Puerto Rico Highways and Transportation Authority ("PRHTA")*** - Balance due from PRHTA relates to $6.2 million mainly associated with the rental of a hangar, a warehouse and land for which there are written agreements. These balances do not bear interest and have no formal repayment terms, since the terms and conditions have not been established. Authority's management is working with the government entity for the collection of this outstanding balance; therefore, management believes no allowance for bad debt is needed at this time.

***Puerto Rico Tourism Company ("PRTC")*** - Amount due from PRTC relates principally to a remaining balance from PRTC's contribution for the Special Incentive Funds of Cruise Ships under Act 113 of 2011. Although the Authority has established a reserve for this balance during 2016, management is evaluating alternative courses of actions in order to continue pursuing the collection of this outstanding balance.

***Federal Aviation Administration ("FAA")*** – Amounts due from the FAA of approximately $2.9 million as of June 30, 2016 consisted of pending reimbursements to be received related to certain capital projects.

Due to governmental entities as of June 30, 2016, consists of:

| | 2016 (In thousands) |
|---|---|
| Commonwealth of Puerto Rico | $ 43,640 |
| Due to other governmental entities: | |
| Puerto Rico Electric Power Authority ("PREPA") | 29,982 |
| Puerto Rico Aqueduct and Sewer Authority ("PRASA") | 21,420 |
| State Insurance Fund Corporation ("SIFC") | 4,476 |
| Puerto Rico Highways and Transportation Authority | 1,832 |
| Others | 11 |
| | $ 101,361 |

***Commonwealth of Puerto Rico*** **-** Balance due to the Commonwealth of Puerto Rico consists mainly of public insurance amounting to $19 million, income tax withheld amounting to $3.8 million owed to the Treasury Department, and $19.1 million to the Puerto Rico Retirement System ("PRRS") for employer contributions not fully paid since fiscal year 2012. The balance owed to the Treasury Department for the unpaid employer contributions (approximately $3.8 million) is subject to a formal payment plan that provides for consecutive monthly payments ranging from $50,000 to $100,000 during the next 57 months and a final payment of $5.110 million during the 58th month. The Authority has been complying with the established repayment plan. During August 2014, the Authority and PRRS also approved a new payment plan for a pre-2015 debt amounting to $12.5 million, that provides for consecutive monthly payments ranging from $100,000 to $300,000 during the next 47 months and a final payment of $2.374 million during the 48th month. The Authority has been complying with the established repayment plan.

## 6. DUE FROM/DUE TO GOVERNMENTAL ENTITIES (Continued)

***Due to Other Governmental Entitie*s** balances consist mainly of utilities or services provided by such entities. The non-current amounts due to Commonwealth of Puerto Rico and due to other governmental entities activity for the year ended June 30, 2016, was as follows (in thousands):

| | 2015 | Charges | Payments | 2016 |
|---|---|---|---|---|
| Due to Commonwealth of PR | $ 41,243 | $ 14,771 | $ (12,374) | $ 43,640 |
| Due to other governmental entities | 55,940 | 9,269 | (7,488) | 57,721 |
| | $ 97,183 | $ 24,040 | $ (19,862) | $ 101,361 |

## 7. CAPITAL ASSETS

The following schedule summarizes the capital assets held by the Authority as of June 30, 2016 (in thousands):

| | Balance June 30, 2015 | Increases | Decreases | Balance June 30, 2016 |
|---|---|---|---|---|
| Assets not being depreciated: | | | | |
| Land and land improvements | $ 211,873 | $ - | $ (71) | $ 211,802 |
| Construction in progress | 171,497 | 20,768 | (47,792) | 144,473 |
| Service concession arrangement (SCA) assets: | | | | |
| Land and land improvements | 82,221 | - | - | 82,221 |
| Building, improvements and structures | 332,659 | 32,765 | - | 365,424 |
| Machinery, furniture and equipment | 3,588 | - | - | 3,588 |
| Other infrastructure | 25,764 | - | - | 25,764 |
| Roads and parking areas | 122,228 | - | - | 122,228 |
| Total SCA assets | 566,460 | 32,765 | - | 599,225 |
| Total assets not being depreciated | 949,830 | 53,533 | (47,863) | 955,500 |
| Assets being depreciated: | | | | |
| Building, piers, improvements and structures | 514,691 | 46,476 | - | 561,167 |
| Other infrastructure | 134,479 | 431 | (105) | 134,805 |
| Roads and parking areas | 169,748 | - | - | 169,748 |
| Machinery, furniture and equipment | 104,155 | 1,010 | (876) | 104,289 |
| Automobiles and service vehicles | 11,099 | 678 | (666) | 11,111 |
| Infrastructure Master Plans | 11,621 | - | - | 11,621 |
| Total | 945,793 | 48,595 | (1,647) | 992,741 |
| Less: accumulated depreciation and amortization | (641,161) | (23,959) | 959 | (664,161) |
| Net total assets being depreciated | 304,632 | 24,636 | (688) | 328,580 |
| Total capital assets, net | $ 1,254,462 | $ 78,169 | $ (48,551) | $ 1,284,080 |

## 8. UNEARNED REVENUES

The Authority entered into an agreement with Puerto Rico Industrial Development Company (PRIDCO) in December 1989 for a tract of land at the Rafael Hernández Airport in Aguadilla, in which PRIDCO constructed some facilities and leased them to a tenant. Under the agreement, the Authority is the ultimate owner of the improvements. Accordingly, the Authority capitalized $3.2 million in 1997 and recognized unearned revenue, which is amortized through the term of the lease.

Unearned revenues balance at June 30, 2016 consists of:

| | 2016 (In thousands) |
|---|---|
| Carrying amount of unamortized portion of construction costs, amortized by equivalent credits to the minimum fixed rental through December 2019 | $ 1,655 |
| Less: current portion | (68) |
| Unearned revenues, long-term | $ 1,587 |

## 9. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS)

On December 28, 2011, the Authority entered into a refinancing transaction in the amount of $678,451,920, by issuing bonds through the Puerto Rico Infrastructure Finance Authority ("PRIFA") as conduit. The issuance was structured as follows:

| Series | Amount (In Thousands) |
|---|---|
| PRIFA Series 2011 A | $340,000 |
| PRIFA Series 2011 B | 202,066 |
| PRIFA Series 2011 C | 136,385 |
| | $678,451 |

The proceeds of these bonds (the PRIFA Bonds) were provided to the Authority pursuant to a Loan and Trust Agreement (the Loan Agreement) between the Authority, PRIFA and the trustee of the PRIFA Bonds (the Trustee). Pursuant to the terms of the Loan Agreement, the Authority has unconditionally agreed to repay the loan in the amounts and at times necessary to pay the principal of, premium, if any, and interests on the PRIFA Bonds when due. Therefore, the Authority has recognized a mirror effect of the PRIFA Bonds in its own debt as loans payable. The proceeds from the PRIFA Bonds were used for the most part to repay and cancel certain loans obligations and swap agreements existing then.

A refunding loss of $61.8 million resulted from this transaction, attributed to the write-off of the then existing deferred outflow for the same amount associated with a swap agreement cancellation. The notional amount of the swap agreement cancelled ($396 million) exceeded the outstanding principal balance of a hedged Wells Fargo loan being cancelled ($363.9 million); therefore, the proportion of that excess amount (unhedging portion) applied to the resulting refunding loss was recognized as a realized loss of approximately $5 million, which was charged to the result of operations for fiscal year 2012. The rest of the refunding loss ($56.8 million) was deferred and is amortized into interest expense over the life of the PRIFA Bonds based on the effective interest method. As of June 30, 2016, the unamortized deferred loss on refunding balance was $12.5 million and is included as deferred outflows of resources in the accompanying statement of net position, as required by GASB No 65.

## 9. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS) (Continued)

The PRIFA Series 2011 A Bonds were issued as fixed rate bonds carrying interest at 2.990%, payable on each June 15 and December 15, commencing on June 15, 2012. This series matured on June 15, 2013. The PRIFA Series 2011 B Bonds were also issued as fixed rate bonds and mature at different repayment periods from 2014 to 2026, with each maturity period carrying its own fixed interest rates ranging from 3.00% to 6.00%, payable in each June 15 and December 15, commencing on June 15, 2012. The PRIFA Series 2011 C Bonds (two series) were issued initially in a Term Rate Mode bearing interest at 2.75% and 3.00% (the initial term rates), convertible at June 14, 2013 and December 14, 2013, proportionally, to another term rate period or to a fixed term mode. Interest is payable each June 15 and December 15, commencing on June 15, 2012. The Series C Bonds were subject to redemption from sinking funds installment payments beginning in 2014 through 2026; however, under certain circumstances, one of the Series C segments amounting to $39.6 million was subject to a mandatory repurchase through one of the GDB Letters of Credit described in the paragraph below.

The Loan Agreement is payable solely from revenues of the Authority, such as all rates, rents, fees, charges and other income and receipts. The Loan Agreement is also secured by drawings from two irrevocable transferable direct-pay letters of credit issued by GDB (collectively referred as the GDB Letters of Credit). One letter of credit is for the maximum amount of $543.1 million to cover ultimately the PRIFA Series 2011 A and B Bonds, while the second letter of credit is for the maximum amount of $138.3 million to cover ultimately the PRIFA Series 2011 C Bonds. These letters of credit carry an annual fee of 1% on their outstanding amounts, payable semiannually, commencing on December 15, 2011. The Authority was charged during fiscal year 2016 for $1.9 million as fees related to the remaining letter of credit outstanding.

During fiscal year 2013, the Authority used $266.9 million from the proceeds of the APP Agreement (described in Note 20) and drew $74.6 million from the GDB Letters of Credit for the full redemption of PRIFA Series A Bonds. In addition, $96.8 million from the GDB Letters of Credit were also drawn for the mandatory partial redemption of a portion of the PRIFA Bonds Series C. Later during fiscal year 2014, the remaining balance of $39.6 million of PRIFA Bonds Series C was also repaid through the use of the corresponding GDB Letters of Credit. By having drawn on the GDB Letters of Credit, new notes payable to GDB have been issued and included in the accompanying statement of net position. See description of these notes payable to GDB in Note 10.

**9. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS) (Continued)**

Principal repayments under the Loan Agreement for the next five years and thereafter, are as follows (in thousands):

| Fiscal Year Ending June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2017 | $ 2,055 | $ 10,221 | $ 12,276 |
| 2018 | 1,125 | 10,160 | 11,285 |
| 2019 | 1,100 | 10,104 | 11,204 |
| 2020 | - | 10,059 | 10,059 |
| 2021 | - | 10,059 | 10,059 |
| 2022 through 2026 | 39,895 | 45,436 | 85,331 |
| 2027 | 146,455 | 8,139 | 154,594 |
| | 190,630 | $ 104,178 | $ 294,808 |
| Add: unamortized premium | 6,774 | | |
| | $ 197,404 | | |

At June 30, 2016, the loans principal outstanding consist of the PRIFA Bonds Series 2011B amounting to $190.6 million.

## 10. NOTES PAYABLE

Notes payable as of June 30, 2016 consist of (in thousands):

| | Amount |
|---|---|
| Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series C1 Bonds, converted into 5 years term loan payable in monthly principal installments of $1.608 million, bearing interest at prime rate plus 150 basis points with a minimum rate of 6%, due in February 2019. | $ 96,785 |
| Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series A Bonds, converted into 5 years term loan payable in monthly principal installments of $1.243 million, bearing interest at prime rate plus 150 basis points with a minimum rate of 6%, due in December 2018. | 74,589 |
| Borrowing under line of credit agreement with GDB, bearing interest at 90 days LIBOR rate plus 50 basis points with a minimum rate of 6%, due in June 2023. Collateralized by the San Juan Water Front (SJWF) Project. | 44,000 |
| Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series C2 Bonds, converted into 5 years term loan payable in monthly principal installments of $658 thousand, bearing interest at prime rate plus 150 basis points with a minimum rate of 6% due in March 2019. | 39,600 |
| Borrowing under line of credit agreement with GDB, bearing interest at prime rate plus 150 basis points with a minimum rate of 7% , due in December 2044 (with a 5 years grace period); used for deposit in the Special Incentives Fund administered by PRIDCO; collateralized with funds maintained at GDB for improvements to regional airports, legislative assignments, certain PRIDCO's properties and limited guarantee of Lufthansa AG, among other guarantees. | 31,513 |
| Promissory note payable to Carnival Corporation, bearing interest at 7.50%, due through May 2024. Collateralized by tariff income from Carnival Corporation. | 7,772 |
| Promissory note payable to International Shipping, bearing and interest at 6.00%, due through December 2017. Collateralized by rent income from International Shipping. | 1,215 |
| Total notes payable | 295,474 |
| Less: current portion | (144,153) |
| Long-term portion | $151,321 |

## 10. NOTES PAYABLE (Continued)

### Government Development Bank (GDB)

In February 2014, the line of credit of $96.8 million payable to GDB, used for the mandatory partial tender of the PRIFA Series C1 Bonds, was converted into a five (5) years term loan. The term loan is to be repaid by the Authority in monthly principal payments of approximately $1.608 million, plus interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 6%. The outstanding balance of the term loan at June 30, 2016 is $96.8 million. The Authority has not made the scheduled principal and interest payments since the inception of this credit facility and awaits for conversations with GDB in continuing to pursue a restructuring plan.

In December 2013, the line of credit of $74.6 million payable to GDB, used for the mandatory partial tender of the PRIFA Series A Bonds, was converted into a five (5) years term loan. The term loan is to be repaid by the Authority in monthly principal payments of approximately $1.243 million, plus interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 6%. The outstanding balance of the term loan at June 30, 2016 is $74.6 million. The Authority has not made the scheduled principal and interest payments since the inception of this credit facility and awaits for conversations with GDB in continuing to pursue a restructuring plan.

On July 1, 2008, the Authority entered into a $180 million line of credit for the development of the San Juan Water Front (SJWF) project (now Bahía Urbana) authorized by an executive order signed on February 20, 2008. Borrowings under this line of credit bear interest at 90 day Libor plus 50 basis points with a minimum rate of 6%, due through June 20, 2023. This line of credit is collateralized with the SJWF project. At June 30, 2016, $44 million were outstanding. The Authority has not made the scheduled principal and interest payments since the inception of this credit facility. However, on September 6, 2014, Joint Resolution #88 was approved authorizing annual Legislative Appropriations of $5 million, commencing on fiscal year 2015 through fiscal year 2023, to repay the balance outstanding under this line of credit. The appropriations for fiscal years 2015 and 2016 were not made and there is no assurance that such appropriation and the remaining ones until fiscal year 2023 will be made.

In March 2014, the line of credit of $39.6 million payable to GDB, used for the mandatory partial tender of the PRIFA Series C2 Bonds, was converted into a five (5) years term loan. The term loan is to be repaid by the Authority in monthly principal payments of approximately $658 thousand, plus interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 6%. The outstanding balance of the term loan at June 30, 2016 is $39.6 million. The Authority has not made the scheduled principal and interest payments since the inception of this credit facility and awaits for conversations with GDB in continuing to pursue a restructuring plan.

In December 2014, the Authority entered into a $41.4 million line of credit with GDB, the proceeds of which were deposited in the Special Incentives Fund administered by PRIDCO, for the development maintenance, repairs and overhaul operations at the regional airport of Aguadilla, Puerto Rico. The line of credit is due on December 5, 2044 with a grace period of five years for the payment of principal. This loan bears interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 7% and is payable in December of every

## 10. NOTES PAYABLE (Continued)

### Government Development Bank (GDB) (Continued)

year. The loan will be payable from the future rental revenue of the related facilities developed. The balance outstanding at June 30, 2016 amounted to $31.5 million, which is the amount drawn on the line of credit through that date. A previous existing line of credit with GDB for $8 million for the same purposes was repaid during fiscal year 2015.

### Carnival Cruise Lines

On June 7, 2001, the Authority entered into a Master Development Agreement with Carnival Corporation for the performance of certain improvements to Terminal 4 of the Port of San Juan. Total financed costs amounted to approximately $13.5 million, and will be payable to Carnival by 240 monthly deductions of $108,735 (including principal and interest at 7.50%) from the tariffs payable from Carnival to the Authority, commencing in May 2004, until May 2024. As of June 30, 2016, such note had an outstanding balance of $7.8 million.

### International Shipping

During November 2011, the Authority entered into an agreement with International Shipping for the performance of certain improvements to piers M, N and O. Total financed costs amounted to approximately $5.4 million, bearing an interest of 6% and payable to International Shipping by seven monthly payments of $36,000, commencing on December 31, 2011; followed by 70 consecutive monthly payments (including interests) of $71,000 and a final payment of $9,908. Payment will be made through the rent income from International Shipping. As of June 30, 2016, the outstanding balance of the note was approximately $1.2 million.

### Summarized Notes Payable Activity

The summarized notes payable activity for the fiscal year ended June 30, 2016, was as follows (in thousands):

| | June 30, 2015 | Borrowings | Payments | June 30, 2016 |
|---|---|---|---|---|
| Notes payable | $ 296,067 | $ 853 | $ (1,446) | $ 295,474 |

Principal repayments on notes payable for the next five years and thereafter, are as follows (in thousands):

| Fiscal Year Ending June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2017 | $ 144,153 | $ 48,686 | $ 192,839 |
| 2018 | 43,339 | 8,297 | 51,636 |
| 2019 | 27,118 | 5,851 | 32,969 |
| 2020 | 935 | 5,216 | 6,151 |
| 2021 | 1,008 | 5,143 | 6,151 |
| 2022 and there-on | 78,921 | 57,515 | 136,436 |
| | $ 295,474 | $ 130,708 | $ 426,182 |

## 11. SPECIAL FACILITY REVENUE BONDS

The Authority has issued $39,810,000 in Special Facility Revenue Bonds, under the provisions of a Trust Agreement, dated as of June 1, 1993, and $115,600,000 in Special Facility Revenue Bonds, under the provisions of a Trust Agreement dated May 1, 1996, between the Authority and The Chase Manhattan Bank (National Association), New York, as Trustee (now JP Morgan Chase Bank). These bonds are limited obligations of the Authority, and are payable solely from and secured by a pledge of certain payments made under Special Facilities Agreements with American Airlines, Inc. (American) and certain other monies. Neither the credit of the Commonwealth of Puerto Rico, nor that of any of its political subdivisions is pledged for the repayment of these bonds. In addition, all of the Special Facility Revenue Bonds are unconditionally guaranteed by American's Parent Company, AMR Corporation. The proceeds were used for the construction, acquisition of equipment and improvement of certain facilities at the LMMIA for the benefit of American Airlines. The property is owned by the Authority and leased to AMR Corporation. Therefore, the liability related to these bonds is not recorded in the accompanying financial statements.

Pursuant to the Special Facilities Agreements between the Authority and American, American has agreed to pay amounts sufficient to cover the principal of and premium, if any, and interest on the above bonds. The bonds are not collateralized by any property, but are payable solely from certain pledged payments by American under the Special Facilities Agreements or by AMR Corporation under its unconditional guarantee. Payments under the Special Facility Revenue Bond remain current at June 30, 2016.

## 12. OTHER POST-EMPLOYMENT BENEFITS OBLIGATION

The Authority follows GASB Statement No. 45, "*Accounting and Financial Reporting for Employers for Postemployment Benefits Other Than Pensions*" ("GASB No. 45"). This Statement establishes the standards for the measurement, recognition, and disclosure of Other Post-employment Benefits ("OPEB") expense/expenditures and related liabilities (assets), disclosures, and, if applicable, required supplementary information ("RSI") in the financial reports of state and local governmental employers.

Postemployment benefits are part of an exchange of salaries and benefits for employee services rendered. Most OPEB have been funded on a pay-as-you-go basis and have been reported in financial statements when the promised benefits are paid. GASB No. 45 requires state and local governments' financial reports to reflect systematic, accrual-basis measurement and recognition of OPEB cost (expense) over a period that approximates employees' years of service and provides information about actuarial accrued liabilities associated with the OPEB and whether and to what extent progress is being made in funding the Plans.

### Plan Description

The Authority agreed to provide medical prescription, dental and vision medical insurance coverage to eligible retirees, its spouses and dependents, for a period of four and five years, for union and non-union personnel, respectively (the "Plan").

The Plan can be amended by action of the Authority subject to applicable collective bargaining and employment agreements. The Plan does not issue a stand-alone financial report since there are no assets legally segregated for the sole purpose of paying benefits under the Plan.

## 12. OTHER POST-EMPLOYMENT BENEFITS OBLIGATION (Continued)

### Funding Policy

The obligations of the employer are established by action of the Authority pursuant to applicable collective bargaining and employment agreements. The required contribution rates of the employer vary depending on the applicable agreement. There is no participants' contribution. The Authority currently contributes enough money to the Plan to satisfy current obligations on a pay-as-you-go basis. The costs of administering the Plan are paid by the Authority.

### Annual OPEB Cost and Net OPEB Obligation

The Authority's annual OPEB expense is calculated based on the Annual Required Contribution of the employer ("ARC"). The Authority engaged an actuary to calculate the ARC and related information per the provisions of GASB No. 45 for employers with more than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

The following table shows the Authority's annual OPEB cost for the year ended June 30, 2016, the amount actually contributed to the Plan and the change in the Authority's net OPEB obligation to the Plan at June 30, 2016:

| | 2016 (In thousands) |
|---|---|
| Annual required contribution ( "ARC") | $ 1,587 |
| Interest on the net OPEB obligation | 196 |
| Adjustments to the ARC | (287) |
| Annual OPEB cost | 1,496 |
| Authority's contribution | (1,205) |
| Increase in net OPEB obligation | 291 |
| Net OPEB obligation, beginning of fiscal year | 3,028 |
| Net OPEB obligation, end of fiscal year | $ 3,319 |

As of June 30, 2016, the actuarial accrued liability for benefits amounted to $12.1 million, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the Plan) was $15.7 million during the year ended June 30, 2016, and the ratio of the unfunded actuarial accrued liability to the covered payroll was 77.1%.

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Plan and the ARC of the employer are subject to continuous revisions as actual results are compared with past experience and new estimates are made about the future.

## 12. OTHER POST-EMPLOYMENT BENEFITS OBLIGATION (Continued)

### Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the Substantive Plan (the Plan as understood by the employer and plan members) and include the types of benefits provided at the time of valuation and the historical pattern of benefit costs paid by the employer to date. The methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

The valuation date was July 1, 2015, and the Projected Unit Credit Cost Method was used. The actuarial assumptions were based on a set of assumptions supplied by the Authority. Turnover rates were based on service and age-related turnover. A discount rate of 6.5% was used. This rate is the best actuarial estimate of expected long-term experience and is in accordance with guidelines for selection of these rates under GASB No. 45. The healthcare trend rates are based on the actuarial knowledge of the general healthcare environment and the specific coverage offered by the Authority.

## 13. TERMINATION BENEFITS

During the fiscal year ended June 30, 2011, the Legislature of the Commonwealth of Puerto Rico approved a one-time retirement incentive plan for all regular employees of Central Government Agencies and certain Public Corporations, known as Act #70 of July 2, 2010. The program included early retirement incentives for certain eligible employees. Under the plan, employees could select one of three options as follows:

Article 4(a) provides economic incentive based on the following parameters:

| Years of Services in Public Sector | Incentive Gross Amount |
|---|---|
| Up to 1 year | 1 month of salary |
| From 1 year and 1 day up to 3 years | 3 months of salary |
| From 3 years and 1 day and up | 6 months of salary |

Article 4(b) provides, employees meeting certain years of service criteria (between 15 and 29 years) and opting for early retirement, to receive a higher pension benefit rate than they would otherwise be entitled to receive based on their current years of service, but such pension rate is lower than what they would have been entitled to if they had waited to meet the full vesting requirements. Annuity pension payments are based on the following parameters:

| Credited Years of Service | Pension Payment (As a % of salary) |
|---|---|
| 15 | 37.5% |
| 16 | 40.0% |
| 17 | 42.5% |
| 18 | 45.0% |
| 19 | 47.5% |
| 20 to 29 | 50.0% |

## 13. TERMINATION BENEFITS (Continued)

The Authority will be responsible for making the applicable employer contributions to the Employees Retirement System, as well as making the payments to cover the annuity payments to the employees opting for the early retirement window, until both; the years of service and age requirements for full vesting would have occurred, at which time the applicable Retirement System will continue making the annuity payments.

Employees selecting options 4(a) or (b) will be entitled to receive full payment of healthcare plan benefits for a period of up to 12 months or the date that the employee is eligible for a healthcare plan benefit offered by another employer, whichever occurs first.

Article 4(c) provides eligible employees that have 30 years of credited services contributing to the Commonwealth of Puerto Rico Retirement System and request to start receiving their pension benefits, will be entitled to receive the economic incentive disposed on article 4(a) but not entitled to the incentives provided on article 4(b). Employees that have the required retirement age but have not achieved the years of credited services contributing to the Commonwealth of Puerto Rico Retirement System will be entitled to an economic incentive of up to 6 months of salary to cover for the years of service not credited.

At June 30, 2016, the present value of future incentive payments reported as a liability amounted to approximately $21.6 million. Total expense recorded for the year ended June 30, 2016, for future incentive payments amounted to $449 thousands, presented as early termination expenses in the statement of revenues, expenses and changes in net position. The total aggregate liability of the program as of June 30, 2016 amounted to $21.6 million, of which $2.4 million should be funded during the next fiscal year. The long-term portion of the early termination obligation amounted to $19.2 million. Such amounts are disclosed respectively, as short-term and long-term liabilities in the accompanying statement of net position.

## 14. RETIREMENT PLANS

The Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (the Retirement System), created pursuant to Act No. 447 of May 15, 1951, as amended, is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by and reported as a fiduciary component unit of the Commonwealth. The Retirement System consists of different benefit structures, including a cost-sharing, multi-employer, defined benefit program; a defined contribution program; and a defined contribution hybrid program.

### *a. Cost-Sharing, Multiple-Employer,Defined Benefit Program*

Pursuant to Act No. 447 of May 15, 1951, as amended, all regular employees of the Authority hired before January 1, 2000 and less than 55 years of age at the date of employment became members of the Retirement System, under the Defined Benefit Program, as a condition of their employment. No benefits are payable if the participant receives a refund of their accumulated contributions.

**14. RETIREMENT PLANS (Continued)**

*a. Cost-Sharing, Multiple-Employer,Defined Benefit Program (Continued)*

The Defined Benefit Program provides retirement, death, and disability benefits pursuant to legislation enacted by the Legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after 10 years of plan participation. Disability benefits are available to members for occupational and non occupational disabilities. However, a member must have at least 10 years of service to receive non occupational disability benefits.

Members who have attained 55 years of age and have completed at least 25 years of creditable service, or members who have attained 58 years of age and have completed 10 years of creditable service, are entitled to an annual benefit payable monthly for life. The amount of the annuity shall be 1.5% of the average compensation, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. The annuity for which the participant is eligible, is limited to a minimum of $500 per month and a maximum of 75% of the average compensation, as defined.

Participants who have completed 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65% of the average compensation, as defined; otherwise, they will receive 75% of the average compensation, as defined.

Commonwealth's legislation requires employees to contribute 10% of their monthly gross salary.

Act No. 1 of February 16, 1990, made certain amendments applicable to new participating employees joining the Retirement System effective April 1, 1990. These changes consist principally of an increase in the retirement age from 55 to 65, a decrease in the benefit percentage of the average compensation in the occupational disability and occupational death benefits annuities from 50% to 40%, and the elimination of the Merit Annuity for participating employees who have completed 30 years of creditable service.

On September 24, 1999, the Legislature enacted Act. No. 305, which amended Act No. 447 to establish a new retirement program. In addition, on April 4, 2013, the Legislature enacted Act No. 3, which amended the provisions of the different benefit structures under the Retirement System, including the Defined Benefit Program.

*b. System 2000 Program*

The Legislature enacted Act No. 305 on September 24, 1999, which amended Act No. 447 to create, among other things the System 2000 Program, a new benefit structure, similar to a cash balance plan (defined contribution plan). All regular employees hired for the first time on or after January 1, 2000, and former employees who participated in the Defined Benefit Program, received a refund of their contributions, and were rehired on or after January 1, 2000, and became members of the System 2000 Program as a condition to their employment. In addition, employees who at December 31, 1999 were participants of the Defined Benefit Program had the option, up to March 31, 2000, to irrevocably transfer their prior

**14. RETIREMENT PLANS (Continued)**

***b. System 2000 Program (Continued)***

contributions to the Defined Benefit Program plus interest thereon to the System 2000 Program.

Commonwealth's legislation requires employees to contribute 10% of their monthly gross salary to the System 2000 Program. Employee contributions are credited to individual accounts established under the System 2000 Program. Participants have three options to invest their contributions to the system 2000 Program. Investment income is credited to the participant's account semiannually.

Under System 2000 Program, contributions received from participants are pooled and invested by the Retirement System, together with the assets corresponding to the Defined Benefit Program. Future benefit payments under the Defined Benefit Program and the System 2000 Program will be paid from the same pool of assets. As a different benefit structure, the System 2000 Program is not a separate plan and the Commonwealth does not guarantee benefits at retirement age.

Corresponding employers' contributions will be used by the Retirement System to reduce the unfunded status of the Defined Benefit Program.

The System 2000 Program reduced the retirement age from 65 years to 60 years for those employees who joined this plan on or after January 1, 2000.

Upon retirement, the balance in each participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefit to the participant's spouse in case of the participant's death. Participants with a balance of $10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in each participant's account will be paid in a lump sum to the participant's beneficiaries. Participants have the option of receiving a lump sum or purchasing an annuity contract in case of permanent disability.

On April 4, 2013, the Legislature enacted Act No. 3, which amended the provisions of the different benefit structures under the Retirement System, including the System 2000 Program.

***c. Defined Contribution Hybrid Program***

On April 4, 2013, the Legislature enacted Act. No. 3, which amended Act No. 447, Act No. 1 and Act. No. 305 to establish, among other things, a defined contribution program similar to the System 2000 Program (the Defined Contribution Hybrid Program) to be administered by the Retirement System. All regular employees hired for the first time on or after July 1, 2013, and former employees who participated in the Defined Benefit Program and the System 2000 Program, and were rehired on or after July 1, 2013, become members of the Defined Contribution Hybrid Program as a condition to their employment. In addition, employees who at June 30, 2013, were participants of previous plans will become part of the Defined Contribution Hybrid Program. Act No. 3 froze all retirement benefits accrued through June 30, 2013 under the Defined Benefit Program, and thereafter, all future benefits

## 14. RETIREMENT PLANS (Continued)

### *c. Defined Contribution Hybrid Program (Continued)*

will accrue under the defined contribution formula used for the 2000 System Program participants.

Participants in the Defined Benefit Program who as of June 30, 2013, were entitled to retire and receive some type of pension, may retire on any later date and will receive the annuity corresponding to their retirement plan, as well as the annuity accrued under the Defined Contribution Hybrid Program. Participants who as of June 30, 2013, have not reached the age of 58 and completed 10 years of service or have not reached the age of 55 and completed 25 years of service can retire depending on the new age limits defined by the Defined Contribution Hybrid Program and will receive the annuity corresponding to their retirement plan, as well as the annuity accrued under the Defined Contribution Hybrid Program.

Participants in the System 2000 Program who as of June 30, 2013, were entitled to retire because they were 60 years of age may retire on any later date and will receive the annuity corresponding to their retirement plan, as well as the annuity accrued under the Defined Contribution Hybrid Program. Participants in the System 2000 Program who as of June 30, 2013, have not reached the age of 60 can retire depending on the new age limits defined by the Defined Contribution Hybrid Program and will receive the annuity corresponding to their retirement plan, as well as the annuity accrued under the Defined Contribution Hybrid Program.

In addition, Act No. 3 amended the provisions of the different benefit structures under the Retirement System, including, but not limited to, the following:

1. Increased the minimum pension for current retirees from $400 to $500 per month.
2. The retirement age for the Act No. 447 participants will be gradually increased from age 58 to age 61.
3. The retirement age for the active System 2000 Program participants will be gradually increased from age 60 to age 65.
4. Eliminated the “merit annuity” available to participants who joined the retirement System prior to April 1, 1990.
5. The retirement age for new employees was increased to age 67.
6. The employee contribution rate was increased from 8.275% to 10%.
7. For the System 2000 Program participants, the retirement benefits will no longer be paid as a lump sum distribution, instead, they will be paid through a lifetime annuity.
8. Eliminated or reduced various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees was reduced from $600 to $200 and was eliminated for future retirees. The summer bonus was eliminated. Resulting employer contribution savings will be contributed to the Retirement System.
9. Disability benefits were eliminated and substituted for a mandatory disability insurance policy.
10. Survivor benefits were modified.

**14. RETIREMENT PLANS (Continued)**

***c. Defined Contribution Hybrid Program (Continued)***

Employee contributions are credited to individual accounts established under the Defined Contribution Hybrid Program. In addition, a mandatory contribution equal to or less than point twenty five percent (0.25%) is required for the purchase of disability insurance.

Upon retirement, the balance in each participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life. In case of the pensioner's death, the designated beneficiaries will continue receiving the monthly benefit until the contributions of the participant are completely consumed. In case of the participants in active service, a death benefit will be paid in one lump sum in cash to the participant's beneficiaries. Participants with a balance of less than $10,000 or less than five years of computed services at retirement will receive a lump-sum payment. In case of permanent disability, the participants have the option of receiving a lump sum or purchasing an annuity contract.

For the year ended June 30, 2016, the Authority was required to contribute 14.275% of each participant's gross salary under the different benefit structures. The Retirement System will use these contributions to increase its level of assets and to reduce the actuarial deficit. Beginning on July 1, 2013, and up until June 30, 2016, the employer's contribution rate shall be annually increased by one percent (1%). Beginning July 1, 2016, and up until June 30, 2021, the employer's contribution rate that is in effect on June 30 of every year shall be annually increased on every successive July 1 by one point twenty-five percent (1.25%).

Total employee contributions for the defined contribution plan and the defined contribution hybrid program during the year ended June 30, 2016, amounted to approximately $48 thousands and $1.9 million, respectively. There were no contributions to the defined benefit plan during fiscal year 2016. The Authority's contributions (either paid or accrued) during the year ended June 30, 2016, 2015 and 2014 amounted to approximately $2.8 million, $2 million, and $1.1 million, respectively. These amounts represented 100% of the required contribution for the corresponding year. Total payroll subjected to retirement contributions amounted to approximately $15.7 million for the year ended June 30, 2016. Individual information for each option is not available since the allocation is performed by the Retirement System itself.

The Retirement System also administers benefits granted under various special laws that have provided additional benefits for the retirees and beneficiaries, referred to as System Administered Pension Benefits. The System Administered Pension Benefits include, among others, additional minimum pension, death and disability benefits, ad-hoc cost-of-living adjustments and summer and Christmas bonuses. Act No. 3 and Act No. 160 amended various laws providing some of these System Administered Pension Benefits to reduce some of the amounts payable to existing retirees while eliminating the benefits for all future retirees (those retiring after June 30, 2013 and July 31, 2014). The System Administered Pension Benefits are funded on a pay-as-you-go basis by the participating employers, including the Authority. The System Administered Pension Benefits corresponding to former employees of the Authority are obligations of the Authority. Most of the funds used to cover the System Administered Pension Benefits for other covered employees are required to be paid by the Commonwealth.

**14. RETIREMENT PLANS (Continued)**

***c. Defined Contribution Hybrid Program (Continued)***

The ERS actuarial valuation report as of June 30, 2015 (most recently available) reflects a fiduciary net deficiency of ($578.6) million, total pension liability of $32.7 billion, and a net pension liability of $33.2 billion.

As disclosed in Note 2, GASB No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB 27,* became effective for the year ended June 30, 2015. This Statement replaces the requirements of GASB No. 27 as well as the requirements of GASB No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements that meet certain criteria as is the case of the Retirement System. As of the date of our report, the Retirement System has not issued its 2015 basic financial statements, nor has it provided the Authority with the required information to implement the requirements of GASB No.68 as of both June 30, 2016 and 2015. Therefore, the accompanying financial statements do not have any adjustments that will be necessary for the Authority to account for its proportionate share of the net pension liability, deferred inflow of resources and deferred outflow of resources in the statement of net position as of July 1, 2015 and June 30, 2016, as well as the effect in the recorded pension expense in the statement of revenues, expenses and changes in net position for the year ended June 30, 2016. Also, additional disclosures required by GASB No. 68 as well as required supplementary information have been omitted from these basic financial statements. The pension costs recognized in the accompanying financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions, which is not in accordance with accounting principles generally accepted in the United States of America.

Additional information on the Retirement System is provided on its stand-alone financial statements for the year ended June 30, 2014, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico, P.O. Box 42004, San Juan PR 00940-2004.

**Other Retirement Benefit**

The Authority has certain collective bargaining agreements that provide all union employees who work for the Authority upon retirement with a lump-sum bonus payable at the retirement date of $900 per year of service up to a maximum of $27,000. In addition, non-union employees have similar benefits under the same conditions granted to labor union personnel.

This particular collective bargaining plan can be amended by action of the Authority subject to applicable collective bargaining and employment agreements. The collective bargaining plan does not issue a stand-alone financial report since there are no assets legally segregated for the sole purpose of paying benefits under such plan.

**14. RETIREMENT PLANS (Continued)**

**Funding Policy**

The obligations of the employer are established by action of the Authority pursuant to applicable collective bargaining and employment agreements. There is no participants' contribution, and benefits, under this plan, are funded on a pay-as-you-go basis. The costs of administering the collective bargaining plan are paid by the Authority.

**Annual Pension Cost and Net Pension Obligation/(Asset)**

The Authority's annual pension expense is calculated based on the ARC. The Authority engaged an actuary to calculate the ARC and related information per the provisions of GASB Statement No. 27 "*Accounting for Pensions by State and Local Governmental Employer*s" ("GASB No. 27") for employers with more than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. At June 30, 2016, the actual funding excess over the ARC amounted to $3.8 million and is presented as a net pension asset in the accompanying statement of net position.

The following table shows the Authority's annual pension cost for the year ended June 30, 2016 and the amount actually contributed at June 30, 2016 (in thousands):

| | | |
|---|---|---|
| Annual Pension Cost | $ | 432 |
| Actual Funding Contribution | $ | - |

As of June 30, 2016, the actuarial accrued liability for benefits amounted to $2.8 million, all of which was unfunded.

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment and mortality. Amounts determined regarding the funded status of the Plan and the ARC of the employer are subject to continuous revisions as actual results are compared with past expectations and new estimates are made about the future.

**Methods and Assumptions**

Projections of benefits for financial reporting purposes are based on the Substantive Plan (the Plan as understood by the employer and plan members) and include the types of benefits provided at the time of valuation and the historical pattern of benefit costs paid by the employer to date.

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

The valuation date was July 1, 2015 and the Projected Unit Credit Cost Method was used. The actuarial projections were based on a set of assumptions supplied by the Authority. Turnover rates were based on service and age-related turnover. A discount rate of 6.5% was used. This rate is the best actuarial estimate of expected long-term experience and is in accordance with guidelines for selection of these rates under GASB No. 27.

## 15. COMMITMENTS AND CONTINGENCIES

### Construction

As of June 30, 2016, the Authority had commitments for approximately $11.3 million, related to construction contracts.

### Litigation

The Authority is defendant or co-defendant in various lawsuits, with claims amounting to approximately $262 million, as a result of the normal course of operations and also for alleged damages in cases principally related to its concessionaries. As of June 30, 2016, the Authority has reserves amounting to approximately $4.5 million to cover the aggregate exposure assessment. In the opinion of the Authority's management, based on legal advice, any liability in excess of insurance coverage and/or of the recorded reserves that may arise from final judgments would not affect significantly the Authority's financial position or result of operations.

### Human Resources

The Authority is defendant in various separate class action suits brought by employees, which are requesting the payment of overtime, accrued compensated absences, fringe benefits and increase in salaries. Due to the complexity of some of the claims, the total amount to be paid, if any, by the Authority cannot be determined, and as a result were not accrued as of June 30, 2016.

### Environmental Remediation

On May 23, 2002, the Authority, as well as other oil companies (the members), was contacted by the United States Environmental Protection Agency ("EPA") regarding certain alleged environmental conditions at the LMMIA related to the Hydrant Fuel System ("HFS"). The Authority and the other members entered into an Administrative Order Consent ("AOC") with EPA to perform a subsurface investigation and certain other tasks in connection with the HFS, with the exception of the assessment of the HFS, which will be undertaken by the Authority. In March 2003, the Authority and the other members entered into a Joint Defense, Participation and Cost Sharing Agreement to jointly conduct the subsurface investigation established in the AOC, constitute a Steering Committee and share the underlying costs. The Steering Committee established a budget for the sampling stage of the works for which the Authority is responsible for $3 million, which is included as part of the accounts payable and accrued expenses in the accompanying statement of net position as of June 30, 2016. The budget established by the Steering Committee covers only the sampling stage of the works in which they are currently on. Subsequent remediation and responsibility actions will be renegotiated in the future.

## 15. COMMITMENTS AND CONTINGENCIES (Continued)

### Tenant Lease Agreements

The Authority entered in two lease agreements with a tenant for a tract of land at LMMIA. The lease agreements are for twenty-five (25) years with options to renew for two (2) additional five (5) year terms. One of the agreements was effective in September 1988 and the other in June 1995. Under the terms of the agreements, the Authority will charge a fixed monthly rent, plus an additional rent based on sales volume. The Authority also agreed to grant rental credits to reimburse the lessee for the permanent improvements to the leased property. The title to such improvements will revert to the Authority at no further cost at the end of the lease term or at a prior date in case of default. The rental credit to be granted is limited to the amount invested by the lessee, which is required to submit evidence of the amount invested, in the leased property. Also, as of June 30, 2016, the tenant and the Authority are under litigation of certain aspects of the lease agreements, as described in the ensuing paragraph.

Pursuant to the objectives of the LMMIA *Project (see* Note 20), during December 2011, the Authority entered into certain expropriations proceedings through the Puerto Rico First Instance Court (the "Court"), to acquire certain properties and concessions owned by third parties within the LMMIA complex. In connection with such proceedings, on December 27, 2011, the Authority obtained a $30 million non-revolving credit facility with the GDB, out of which $25.4 million were consigned with the Court to start the expropriation process. The consigned amount was based on the Authority's determination of the properties' fair value, and it is included in a separate line item in the accompanying statement of net position. The counterparties have the right to contest the amount deposited, pursuant to the presentation of acceptable evidence indicating a higher fair value. As of the date of issuance of the financial statements, it is uncertain if the final settlement will be for the consigned amount, or for a higher consideration.

### AMR Bankruptcy and Other Related Litigation

On November 28, 2011, AMR Corp. ("AMR"), the parent company of American Airlines, filed for bankruptcy under Chapter 11 of the US Bankruptcy Law. The Authority derived over 20% of its rental revenues and landing and other fees from AMR during the fiscal year 2012. Prior to the closing of lease and use agreements with respect to the LMMIA, as described in Note 20, the Authority's collection of revenues could have been affected if AMR's bankruptcy proceedings caused delays or suspension of payments, or if AMR's operations were modified as part of the underlying corporate reorganization. However, pursuant to the lease and use agreement closed on February 27, 2013, referred to in Note 20, this potential risk was transferred to Aerostar, which is managing and monitoring such risk as part of the lease and use agreements.

### Trocadero-Diverplex Federal Funds Finding

During the 1980's, a water taxi terminal station was constructed in Hato Rey, as part of a water transportation system running from Hato Rey to Old San Juan. This project, also known as the "Aqua Express Project", was funded with approximately $30 million of federal financial assistance from the Federal Transit Administration (FTA) channeled through the Department of Transportation and Public Works (DTOP), as grantee, and various other governmental entities as participants in the project, including the Authority, the Maritime Transportation Authority of Puerto Rico (MTA) and the Puerto Rico Highways and Transportation Authority (PRHTA). During the early years of the 2000 decade, the water transportation service through Aqua Express was

**15. COMMITMENTS AND CONTINGENCIES (Continued)**

**Trocadero-Diverplex Federal Funds Finding (Continued)**

suspended principally due to high sedimentation on the maritime channel of the system and frequent technical problems with the water vessels of the system. During 2011, in an attempt to find an alternate productive use to the water terminal area that was otherwise being wasted, the Commonwealth administration then announced the conversion of the area into a restaurant and shopping center complex to be known as Trocadero-Diverplex, where at the present time several businesses operate.

The FTA learned about the new utilization of the federally funded water terminal area and confirmed that these changes were not consulted with them, which might expose the DTOP to a potential exposure of having to return the $30 million funding to the FTA, unless FTA and the DTOP can find a way to alleviate this apparent violation. The FTA has already frozen other $30 million in federal funding that could have been used for improvements to existing transportation systems elsewhere in Puerto Rico. The FTA has continued with its investigation of all the events and activities surrounding the change in the original purpose of the water terminal area and the DTOP, along with PRMIMTA and PRHTA, are evaluating who would bear the ultimate responsibility or how to share it in the eventuality of having to return the funds to FTA. The Authority's management has not considered necessary, at the moment, to recognize any reserve to cover this potential exposure.

**16. PASSENGER FACILITY CHARGE**

Pursuant to the Aviation Safety and Capacity Act of 1990 (the Act), airports may collect a Passenger Facility Charge (PFC) of up to $4.50 per ticket, out of which $0.11 belong to the airline companies for administrative expenses and $4.39 to the Authority. Under the Act, PFC revenues are restricted to be used for financing eligible airport-related projects that preserve or enhance safety, capacity or security of the air transportation system, subject to the approval of the Secretary of Transportation of the United States. The PFC income for the year ended June 30 2016, amounted to approximately $13 thousand. As of June 30, 2016, the Authority has unexpended resources amounting to approximately $5.7 million, which are restricted for PFC projects. PFC revenues are recognized as collected and are included in non-operating revenues. As part of the service concession arrangement for the LMMIA facilities signed with Aerostar (described in Note 20), after February 27, 2013, the PFC revenues related to the LMMIA operations are received and administered by Aerostar.

Under the provisions of the Act, the Authority is required to provide an annual independent audit of the PFC revenues, which expresses an opinion of the fairness and reasonableness of the Authority's procedures for receiving, holding and using PFC revenue. In addition, auditors are required to report whether the quarterly reports that must be filed by the Authority fairly represent the net transactions within the PFC accounts. After having performed no such independent audits since the inception of the PFC program in 1993, the Authority engaged one during fiscal year 2014 to cover compliance with the PFC requirements for the periods since inception through February 28, 2013. The resulting PFC audit report contained disclaimers of opinion for the first 10 years of the program and several noncompliance exceptions since 2003, mostly due to inadequate document retention policies that enabled the destruction and unavailability of supporting documentation to be inspected. The Authority had been following

## 16. PASSENGER FACILITY CHARGE (Continued)

the local seven-year retention policy regulations of the Commonwealth, rather than the ones prescribed by the PFC regulations. Also, the PFC audit report and certain other forensic report issued identified questioned costs of approximately $8.1 million and unsupported interest payments of approximately $6.6 million. Despite these results, management felt that such findings were not necessarily indicative of illegal or inappropriate expenditures outside the applicable PFC projects, as all PFC projects since inception of the program have been completed, in-process or accounted for. The FAA provided comments on the results of the audit report, which included requiring the Authority to prepare a detailed corrective action plan for remediating the findings noted and to identify the support for the aforementioned questioned costs and unsupported interest payments or in the alternative, to provide a credit to the PFC accounts for any unsupported amount. The Authority has identified most of the unsupported evidence and continues working in the identification of the remaining unsupported amounts and their reconciliation with the applicable projects; therefore, management believes no allowance for potential exposure is considered necessary at June 30, 2016.

## 17. RENTAL INCOME

The Authority leases its property to commercial airlines, car rental companies, concessionaires and to several fixed base operators who service the airline industry, the TSA, and other Federal and Commonwealth agencies.

Minimum future rentals to be received on non-cancelable operating leases are approximately as follows:

| Year Ending June 30, | Amount (In thousands) |
|---|---|
| 2017 | $ 18,692 |
| 2018 | 16,736 |
| 2019 | 16,187 |
| 2020 | 15,877 |
| 2021 | 15,454 |
| 2022-2026 | 71,120 |
| 2027-2031 | 47,085 |
| 2032-2036 | 7,697 |
| | $ 208,848 |

The Authority also has several leases that require the lessees to remit a percentage of their revenues or fuel consumption as their rental charges. Rental income under these leases is not included in future minimum rental amounts above.

## 18. FEDERAL ASSISTANCE PROGRAMS

The Authority 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 amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the Authority expects such amounts, if any, not to be significant.

Federal financial assistance and Commonwealth of Puerto Rico appropriations for the year ended June 30, 2016, consist of grants and donations as follows (in thousands):

## 18. FEDERAL ASSISTANCE PROGRAMS (Continued)

| | 2016 (In thousands) |
|---|---|
| **Federal financial assistance:** | |
| Federal grants received from: | |
| Federal Aviation Administration | $ 10,726 |
| Federal Transit Administration | 2,912 |
| Total grants | 13,638 |
| Less: pass - through grant program payments | (2,912) |
| | $ 10,726 |
| Commonwealth of Puerto Rico appropriations | $ 25 |

Pass-through grants program payments of approximately $2.912 million are included as grant subsidies and awards in the accompanying statement of revenues, expenses and change in net position.

## 19. OPERATING REVENUES

Operating revenues for the fiscal year ended June 30, 2016, consist of:

| | 2016 (In thousands) |
|---|---|
| Maritime operations: | |
| Wharfage, dockage and port services | $ 30,370 |
| Tourist ship fees | 18,155 |
| Equipment and property rental | 13,934 |
| Demurrage, utilities and other | 2,341 |
| Engagement security fee | 13,332 |
| Less: provision for doubtful accounts | (2,137) |
| | 75,995 |
| Airport operations: | |
| Landing fees | 1,575 |
| Passenger facilities fees | 659 |
| Space rentals | 26,889 |
| Utilities, gas sales and other | 1,895 |
| Less: provision for doubtful accounts | (3,385) |
| | 27,633 |
| Total revenues | 103,628 |
| Less: discounts and incentives | (402) |
| Total net operating revenues | $ 103,226 |

## 20. LEASE AND USE AGREEMENTS - LMMIA

On February 27, 2013, the Federal Aviation Administration (FAA) approved the closing of the Lease and Use Agreements (the APP Agreements) entered into on July 27, 2012 between the Authority and Aerostar Airport Holdings, LLC (Aerostar) with respect to the Luis Muñoz Marin International Airport Project ( the LMMIA Project). Aerostar is a partnership formed between Grupo Aeropuertuario de Sureste S.A.B de C.V. (ASUR), a New York Stock Exchange-listed Mexican airport management firm, and HighstarCapital L.P., a fourth-generation infrastructure investor and private equity funds manager. The Authority's objectives for entering into the APP agreements are discussed in Note 3.

The APP Agreements awarded Aerostar the right to operate, manage, maintain, develop and rehabilitate the LMMIA during a term of 40 years, subject to extension conditions as defined, in exchange for an upfront payment of a leasehold fee of $615 million to the Authority. In addition, upon the closing of the APP Agreements, the Authority receives from Aerostar annual rental payments for each of the first five full reporting years of $2.5 million; then from the sixth full reporting year through and including the thirtieth reporting year, the Authority will receive annual rental payments equal to 5% of the gross airport revenue earned by Aerostar in such years; and finally from the thirty-first reporting year and each succeeding year, the Authority will receive annual rental payments equal to 10% of the gross airport revenue earned by Aerostar in such years. Aerostar also funded with a $6 million deposit a separate escrow account called the *Puerto Rico Air Travel Promotion and Support Fund*, with the purpose of compensating airlines that increase their services to the LMMIA over certain established thresholds during the first three years of the APP Agreements. Under the APP Agreements, the Authority is responsible for certain capital improvements pursuant to the Airline Capital Improvement Program. The present value of these capital improvements was estimated at $3.068 million at the transaction date. Pursuant to the adoption of GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements,* the Authority recognized at February 27, 2013, the date of the closing of the APP Agreements, a resulting deferred inflow of resources amounting to $622.5 million and a liability of $3.068 million for the present value of the capital improvement commitments of the Authority; in exchange for the receipt of the $615 million upfront leasehold fee and the receivable of the annual payments of $2.5 million from Aerostar for the first 5 years since the closing, with a present value estimate of $10.5 million. Since the closing date through June 30, 2016, approximately $55.2 million of the deferred inflow of resources have been amortized into revenue, $18.1 of which belonged to fiscal year 2016 and recognized within operating revenues-airport in the accompanying statement of revenues, expenses and change in net position. As of June 30, 2016, the Authority has satisfied approximately $2.8 million (none during fiscal year 2016) of its capital improvement commitments, leaving a remaining obligation of approximately $313,000, recognized within accounts payable and accrued expenses in the accompanying statement of net position.

The right awarded to Aerostar to operate, manage and rehabilitate the LMMIA (following certain Operating Standards established by the FAA and the Authority) is accompanied with the assignment of all the revenues from the LMMIA facilities through the different lease agreements with airport concessionaries, including food and beverage providers, retailers, ground transportation providers, and other airport users, formerly belonging to the Authority. Aerostar will also be able to charge a maximum level of fees to the airlines at LMMIA, as established in the APP Agreements.

## 20. LEASE AND USE AGREEMENTS – LMMIA (Continued)

The APP Agreements also provide for a series of capital improvement expenditures on the LMMIA from Aerostar over the term of the APP Agreements, with certain required initial projects and general accelerated upgrades, as defined. This capital improvement program called for an investment in capital expenditures for the ensuing five years after the closing of the APP Agreements in amounts ranging from $246 million to $290 million, to be executed over three phases. Phase 1 would consist of "accelerated upgrades" ranging from $16 million to $24 million, including the acquisition of approximately 22 new boarding bridges, starting in September 2013. Phase 2 expected an investment of approximately $92 million extending through December 2014, mostly in the remodeling of Terminal B and the establishment of a new automated luggage management system. Phase 3 would require the investment of approximately $130 million to start in January 2015 through December 2015, principally in the remodeling and revamping of Terminal C. At June 30, 2016, approximately over $173 million have been invested in capital expenditures by Aerostar, $124.7 million of which have been completed and placed in operations; thus recognized by the Authority as an increase in its capital asset with the corresponding credit to deferred inflow of resources by the same amount. The amortized balance of deferred inflow of resources at June 30, 2016, after all the activities referred to in the paragraphs above amounts to $694.7 million.

The Authority is required to provide police and fire services to the LMMIA in exchange for annual compensation of $2.8 million, to be adjusted thereafter based on inflation. The APP Agreements also established certain compensation events, the occurrence of which from either party would trigger a compensation amount or activity from the defaulting party to the affected party, as defined. Finally, the Authority will be responsible to Aerostar, at the termination of the APP Agreements, for any capital related improvements not fully reimbursed to Aerostar from the Passenger Facility Charge (PFC) program or other airline charges. No such compensation events have occurred through June 30, 2016.

The LMMIA facilities leased to the Puerto Rico Air National Guard are excluded from the APP Agreements and upon the satisfaction of certain conditions, as defined, Aerostar will have option and negotiation rights for the use of such areas, potentially in exchange for additional leasehold fees and annual rental payments. The hotel property within the LMMIA and the cargo facilities leased to CAF and the ongoing related litigation, remain under the responsibility of the Authority, although the properties are included in the APP Agreements. If the litigation is resolved, Aerostar will have option and negotiation rights for the use of such areas, potentially in exchange for additional leasehold fees and annual rental payments.

Upon the closing of the APP Agreements, the Authority used $525 million of the $615 million upfront leasehold fee received to repay debt obligations to lenders and suppliers and to cover certain related transaction costs. The rest of the remaining upfront leasehold fee ($90 million) was used to establish the following supporting funds:

- A fund of $50 million for the early retirement of certain Authority's employees. At June 30, 2016, $774 thousands remain in this early retirement fund.
- A fund of $25 million for the development of the Authority's regional airports. At June 30, 2016, $4.2 million remain in the regional airports development fund.
- A fund of $15 million for the guaranty to cover the Authority's obligations in case of losses sustained on the APP Agreements. At June 30, 2016, including interest, $15.2 million remain in this guaranty fund.

## 20. LEASE AND USE AGREEMENTS – LMMIA (Continued)

The aforementioned supporting funds are maintained in a separate bank account and deposits with GDB. These funds would require GDB's authorization for release, following the Authority's submission of the supporting documentation for such expenditures and their validation by GDB. However, these funds have been included within the impairment loss on deposits placed with GDB, as further described in Note 4.

The APP Agreements also set the basis for the creation and establishment of a program for the supervision and monitoring of Aerostar's compliance with such agreements. Under this program, the Authority maintains offices inside the LMMIA's facilities, housing employees and consultants in charge of monitoring the APP Agreements' clauses related to Aerostar construction, environmental control and commercialization plan. Progress reports are being provided to top management of the Authority on a periodic basis.

## 21. SUBSEQUENT EVENTS

On June 30, 2016, the U.S. President signed the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA), which grants the Commonwealth and its component units access to an orderly mechanism to restructure their debts in exchange for significant federal oversight over the Commonwealth's finances. On August 31, 2016, the U.S. President announced the appointment of seven members to the Oversight Board, and on its first meeting held on September 30, 2016, the Oversight Board designated the Authority as one of the initial covered entities to be subject to the PROMESA Act. The Oversight Board expects to establish deadlines for the Authority and other covered entities that will require individual fiscal plans to be submitted.

Under the Loan and Trust Agreement for the PRIFA Bonds described in Note 9, the Authority used to set aside and deposit on a monthly basis at the trustee account approximately $1 million for the debt service of the PRIFA Bond outstanding. Effective July 2016, pursuant to the provisions of Act 21, the Authority ceased making such deposits to the trustee; consequently, the debt service of the PRIFA Bonds due on December 15, 2016 is not expected to be honored. The Authority has nevertheless contemplated in its fiscal year 2017 budget to resume the aforementioned monthly deposits after January 2017, assuming the moratorium under Act 21 wil not be extended.

On September 16, 2016, the Authority and Edgewater Port Caribe, LLC (Edgewater), a limited liability company organized under the laws of the state of Michigan, entered into a Development and Lease Agreement (the Agreement) whereas Edgewater will be in charge of the development and operation of the shipyard and mega yacht marina at the Port of San Juan, including the Isla Grande Dry Dock (IGDD) and the Marina Site. Under the Agreement, Edgewater specifically agrees to undertake (i) the financing, leasing, designing, construction, operation, rehabilitation and improvement of the IGDD located on Pier 15 and the necessary docks, piers and moorings located in the territorial waters of Puerto Rico and the lands submerged thereunder, which are necessary for the operation of the IGDD, in order to create a facility capable of servicing the

**21. SUBSEQUENT EVENTS (Continued)**

maintenance, repair and overhaul needs of yachts and mega yachts, commercial and military/government vessels (the MRO Services) and (ii) the leasing, design, construction, financing and development of a mega yacht marina complex, including a hotel and other long-term rental facilities located on or between Piers 6 and 9 (the Marina Parcels) and the necessary docks, piers and moorings located in the territorial waters of Puerto Rico and the lands submerged thereunder, which are necessary for the operation of such marina. The IGDD project will consist of three phases and such site lease term shall begin on the term commencement date, as defined, and shall last for 30 years. Edgewater will be charged monthly rent for the IGDD site ranging from approximately $8,000 to $24,000 depending on the particular phase in progress; offset with certain rent credits, as defined. The Marina Site project will carry a lease term that shall begin on the term commencement date, as defined, and shall last for 50 years. Edgewater shall pay upon commencement of operations of the Marina Site a minimum rent and a fee equal to 5% of the gross revenues of the Marina Site, and such minimum rent shall be the equivalent to 6% of the fair market value of the Marina Site at Pier 9. The annual rent for the Marina Site at Piers 6, 7 and 8 shall be a minimum of $54 per square feet, payable in equal installments. Following the term commencement date, as defined, Edgewater shall have an 18-month period to begin the construction of the entire project under the Agreement, during which time the Authority may negotiate with Edgewater a stabilization period during which Edgewater shall be allowed to pay an interim fee of at least 2% of the aforementioned minimum rent. Thereafter, Edgewater shall pay the minimum rent.

On October 7, 2016, the Authority and the Governor of Puerto Rico announced an $8 million agreement with Duty Free Americas for the construction of a two story building on Pier 3 to house a new duty free store and additional commercial space for shopping and entertainment. The facility is being developed by Duty Free Americas in coordination with Royal Caribbean and the Authority. Construction is slated to begin in the coming months, with completion planned in early 2018.

On October 18, 2016, the Secretary of the Treasury issued Circular Letter No. 1300-08-17 (CC 1300-08-17) alerting the Commonwealth's agencies and component units with funds deposited with GDB, about such deposits' exposure to credit risk as a result of GDB's liquidity shortage and corresponding insolvency situation. The CC 1300-08-17 also reminded that with the passage of Act No. 21 and EO 10 (discussed in Note 4), GDB believes there is substantial doubt about its ability to continue as a going concern. For all these reasons, CC 1300-08-17 urges all Commonwealth's agencies and component units with funds deposited with GDB to conduct an impairment analysis on such deposits at June 30, 2016 and 2015.

**21. SUBSEQUENT EVENTS (Continued)**

On October 31, 2016, the Puerto Rico Court of Appeals paralyzed the Authority's container inspection program at the various Puerto Rico's dock facilities as a result of the Authority's not renovating the underlying regulation in conformity with the applicable laws. The cease and desist order from the Court of Appeals covers also the related inspection fees that were being charged under such program. After evaluating its legal options, the continued performing the inspection, but without charging the related fees, as the Authority understood that the cease and desist order was only for the charging of the fees, and not for the inspection. However, effective December 19, 2016, the Authority resumed the charging of the inspection fees under the new emergency Regulation # 8837, approved by the Authority's Board of Directors on November 4, 2016. Upon resuming the aforementioned charging, the trade association representing the food distribution industry in Puerto Rico filed a lawsuit challenging the validity of the new emergency regulation. As of the date of these financial statements, the appropriate courts have not addressed such lawsuit.

In preparing these financial statements, the Authority has evaluated events and transactions for potential recognition or disclosure through December 22, 2016, the date in which the basic financial statements were available to be issued.

NIEVES VELAZQUEZ & CO., P.S.C.
Certified Public Accountants and Financial Consultants

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Directors
Puerto Rico Ports Authority
San Juan, Puerto Rico

We have audited, in accordance with the Auditing Standards Generally Accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Puerto Rico Ports Authority (the Authority) a component unit of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated December 22, 2016. Our report was qualified because The Authority does not have the information available to implement the requirements of Statement No. 68 of the Governmental Accounting Standards Board, *"Accounting and Financial Reporting for Pensions"*, an amendment of GASB Statement No. 27.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of Authority's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs 2016-002 to be a material weakness.

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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS* *(Continued)***

**Internal Control Over Financial Reporting (Continued)**

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. The results of our tests disclosed a significant deficiency identified as item 2016-001 that is required to be reported under *Government Auditing Standards*.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from 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 did not disclose any instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards*.

**Authority's Response to Findings**

Authority's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Nieves Velazquez & Co., P.S.C.

NIEVES VELAZQUEZ & CO., P.S.C.
San Juan, Puerto Rico
December 22, 2016

Stamp No. 02739469 of the Puerto Rico Society of Certified Public Accountant has been affixed to the original of this report.

NIEVES VELAZQUEZ & CO., P.S.C. LIC. NO. 7 PUERTO RICO Certified Public Accountants

# REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM, REPORT ON INTERNAL CONTROL OVER COMPLIANCE, AND REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS REQUIRED BY THE UNIFORM GUIDANCE

To the Board of Directors
Puerto Rico Ports Authority
San Juan, Puerto Rico

## Report on Compliance for Each Major Federal Program

We have audited the Puerto Rico Ports Authority (A Component Unit of the Commonwealth of Puerto Rico) (the Authority) compliance with the types of compliance requirements described in the OMB Uniform Guidance and *Compliance Supplement* that could have a direct and material effect on each of the Authority's major federal programs for the year ended June 30, 2016. The Authority's major federal programs are identified in the Summary of Auditor's Results Section of the accompanying Schedule of Findings and Questioned Costs.

### *Management's Responsibility*

Management is responsible for compliance with federal statutes, regulations applicable to its federal programs and the terms and conditions of its federal awards.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on compliance for each of the Authority's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with Auditing Standards Generally Accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Costs Principles and Audit Requirements. Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority's compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Authority's compliance.

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***Opinion on Each Major Federal Program***

In our opinion, the Authority, a Component Unit of the Commonwealth of Puerto Rico's, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

***Other Matters***

The Authority's response to the noncompliance findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. The Authority's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

**Report on Internal Control Over Compliance**

Management of the Authority is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Authority's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We considered the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 2016-003 to be a significant deficiency.

**REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM;**
**REPORT ON INTERNAL CONTROL OVER COMPLIANCE;**
**AND REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**
**REQUIRED BY THE UNIFORM GUIDANCE**
**(Continued)**

**<u>Report on Internal Control Over Compliance</u> (Continued)**

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Purpose of this Report**

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Nieves Velazquez & Co., P.S.C.

**NIEVES VELAZQUEZ & CO., P.S.C.**
San Juan, Puerto Rico
December 22, 2016

Stamp No. 02739470 of the Puerto Rico Society of Certified Public Accountant has been affixed to the original of this report.

NIEVES VELAZQUEZ & CO., P.S.C.
LIC. NO. 7
PUERTO RICO
Certified Public Accountants

**PUERTO RICO PORTS AUTHORITY**
(A Component Unit of the Commonwealth of Puerto Rico)

## SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
## FOR THE YEAR ENDED JUNE 30, 2016

| *Federal Grantor/Pass-through Grantor/Program or Cluster Title* | *Federal CFDA Number* | *Pass-through Entity Identifying Number* | *Pass-through to Sub-recipients* | *Total Federal Expenditures* |
|---|---|---|---|---|
| **Department of Transportation** | | | | |
| Federal Aviation Administration (FAA): Airport Improvement Program | 20.106 | - | - | $11,244,480 |
| Federal Transit Administration: Urban Mass Transportation Capital and Operating Assistance Formula Grant | 20.507 | 660433854 | 660584953 | 2,790,660 |
| ARRA – Urban Mass Transportation Capital and Operating Assistance Formula Grant | 20.507 | 660433854 | 660584953 | 121,028 |
| Total Urban Mass Transportation | | | | 2,911,688 |
| **Total Expenditures of Federal Awards** | | | | $14,156,168 |

See Notes to Schedule of Expenditures of Federal Awards.

## NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2016

### 1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal grant activity of Puerto Rico Ports Authority under programs of the federal government for the year ended June 30, 2016. The The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of Puerto Rico Ports Authority, it is not intended to and does not present the financial position, changes in net assets, or cash flows of Puerto Rico Ports Authority.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

### 3. FEDERAL CFDA NUMBER

The Catalog of Federal Domestic Assistance (CFDA) Numbers is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence.

### 4. SUBRECIPIENT

For the fiscal year 2015-2016, the Authority assigned $2,911,688 federal awards to the sub-recipient.

## SCHEDULE OF FINDINGS AND QUESTIONED COSTS
## YEAR ENDED JUNE 30, 2016

**Section I - Summary of Auditor's Results**

***Financial Statements***

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP: **Qualified**

Internal control over financial reporting:

| | | |
|---|---|---|
| • Material weakness (es) identified? | x Yes | __ No |
| • Significant deficiency (ies) identified? | x Yes | __ No |
| Noncompliance material to financial statement noted? | ___Yes | x No |

***Federal Awards***

Internal control over major programs:

| | | |
|---|---|---|
| • Material weakness (es) identified? | ___Yes | x No |
| • Significant deficiency (ies) identified? | x Yes | ___ No |

Type of auditor's report issued on compliance for major programs: **Unmodified**

| | | |
|---|---|---|
| Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? | ___Yes | x No |

Identification of major programs:

| CFDA Numbers | Name of Federal Program or Cluster |
|---|---|
| 20.106 | Airport Improvement Program |
| 20.507 | Urban Mass Transportation Capital and Operating Assistance Formula Grant |

Dollar threshold used to distinguish between Type A and Type B programs: $750,000

| | | |
|---|---|---|
| Auditee qualified as low-risk auditee? | ___Yes | x No |

**Section II. Financial Statement Findings**

| | Finding Number | Findings/Non-Compliance | Questioned Costs |
|---|---|---|---|
| **Significant Deficiency** | **2016-001** | **Time Delays in Annual Accounting Closing** | |

*Condition*

The Authority has substantially improved the year-end accounting closing procedures and, accordingly, no auditing delay occurred in the current year. However, at date of the year-end closing certain accounts had not been analyzed, the impact of the GASB 68 application, capital assets and litigation accrual, among others.

*Criteria*

The annual accounting closing and the underlying verification of records and accounts should be performed, analyzed and adjusted during the year.

*Cause*

The Authority has not completed the establishment of an annual accounting closing workflow that may speed up the final closing procedures.

*Effect*

The interim financial statements prepared do not reflect clearly the results of operation and may affect management's financial decision.

*Recommendation*

We strongly recommend management to analyze such accounts during the year and not only at year-end.

**Section II. Financial Statement Findings**

| | Finding Number | Findings/Non-Compliance | Questioned Costs |
|---|---|---|---|
| **Significant Deficiency** | **2016-001** | **Time Delays in Annual Accounting Closing (Continued)**<br><br>*Management Comments*<br><br>We did not analize GASB 68 since information must be provided by the Employees' Retirement System of the Commonwealth of Puerto Rico. This account we will establish a monthly reconciliation once we implement an effective information flow with the department that needs to provide the information and/or Oracle Accounting System are corrected. | |
| **Material Weakness** | **2016-002** | **Capital Assets Recording Procedures**<br><br>*Condition*<br><br>There is no existing monthly reconciling procedures to allow the Properly Engineering and Accounting Departments to properly and effectively reconcile the capital assets subsidiaries with general ledger.<br><br>*Criteria*<br><br>Capital assets should be properly recorded and classified timely and accurately.<br><br>*Cause*<br><br>There is no formal and documented procedure for reconciling capital assets activity identified by the Accounting Department versus the activity reported by the Authority's Property Department.<br><br>*Effect*<br><br>Capital asset accounts could be overstated or understated. | — |

**Section II. Financial Statement Findings**

| | Finding Number | Findings/Non-Compliance | Questioned Costs |
|---|---|---|---|
| **Material Weakness** | **2016-002** | **Capital Assets Recording Procedures** (Continued) | |

*Recommendation*

Management should establish a monthly or quarterly reconciling procedure that allows the Property, Engineering and Accounting Departments to properly and effectively reconcile the capital assets subsidiaries and the period's activity.

*Management Comments*

Since year 2016, we started to fix errors and problem that we have with Oracle Accounting System Property Module. We programed the system to generate the Property, Plant and Equipment Report. We also hired an external consultant to help us reconcile books with Property, Plant and Equipment Report Module. This work will be completed for fiscal year 2017.

**Section III. Federal Award Findings and Questioned Costs**

| Program | Finding Number | Findings/Non-Compliance | Questioned Costs |
|---|---|---|---|
| **AIP & FTA** | **2016-003** | **Equipment and Real Property Management** | |

*Criteria and Conditions*

The OMB Uniform Guidance and the 2016 Compliance Supplement, establishes that equipment acquired with federal awards having a useful life of more than one year and an acquisition cost of $5,000 or more per unit, should maintain adequate equipment records. During our examination, we noted that all equipment acquired with federal funds are not kept separately by program and northeless, it is included together with all the Authority's capital assets. The physical inventory related to the equipment acquired with federal funds was taken during the fiscal year 2014-2015. However, it has not been reconciled with the subsidiary ledger. This finding was repeated in prior years.

*Cause*

A physical inventory of the equipment acquired with federal funds was taken during the current fiscal year but, related adjustments have not been determined nor recorded in the subsidiary ledger. Also, the Puerto Rico Ports Authority does not have adecuate internal control procedures.

*Effect*

The Authority's Management did not comply with the Federal Regulations.

*Recommendations*

We recommend to take a physical inventory for each federal program and reconciled it to the equipment records. The PRPA should establish internal control to ensure that the Equipment and Real Property are recorded properly.

*Management Comments*

See Corrective Action Plan Letter attached. (Page 82)

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS
## JUNE 30, 2016

### Section II. Financial Statement Findings

| Single Audit Report | | Finding No. | Finding |
|---|---|---|---|
| **06/30/2015** | **Significant Deficiency** | **15-001** | **Time Delays in Annual Accounting Closing**<br><br>Condition<br><br>The Authority has substantially improved the year-end accounting closing procedures and, accordingly, no auditing delay occurred in the current year. However, at date of the year-end closing certain accounts had not been analyzed; capital assets, litigation accrual, accounts payable and due from/to governmental entities, among others.<br><br>Criteria<br><br>The annual accounting closing and the underlying verification of records and accounts should be performed, analyzed and adjusted during the year.<br><br>Current Status<br><br>This finding still prevails. See Current Year Finding 2016-001. |
| **06/30/2015** | **Material Weakness** | **15-002** | **Capital Assets Recording Procedures**<br><br>Condition<br><br>There is no existing monthly reconciling procedures to allow the Properly Engineering and Accounting Departments to properly and effectively reconcile the capital assets subsidiaries with general ledger.<br><br>Criteria<br><br>Capital assets should be properly recorded and classified timely and accurately.<br><br>Current Status<br><br>This finding still prevails. See Current Year Finding 2016-002. |

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS
## JUNE 30, 2016

**Section III. Federal Award Findings and Questioned Costs**

| Single Audit Report | | Finding No. | Finding |
|---|---|---|---|
| **06/30/2015** | **Significant Deficiency** | **15-003** | **Cash Management**<br><br>Criteria and Condition<br><br>The A-102 Common Rule, 21OMB Circular A-110, (2 CFR Section 215.22) state that procedures must be implemented to minimize the time elapsed between the transfer of funds from the federal agency and the disbursement of funds by the grantee. During our cash management test, we found from 9 bank transfers examined for the programs AIP, FTA and Port Security, we noted that in 5 cases or 55% of the sample, the programs elapsed time of federal funds disbursement were made between 4 and 73 business days.<br><br>Current Status<br><br>This finding did not occure this year. |
| **06/30/2015** | **Significant Deficiency** | **15-004** | **Equipment and Real Property Management**<br><br>Criteria and Condition<br><br>The OMB Circular A-102, Common Rule, establishes that equipment acquired with federal awards having a useful life of more than one year and an acquisition cost of $5,000 or more per unit, should maintain adequate equipment records. During our examination, we noted that all equipment acquired with the federal funds are not kept separately by program and instead, it is included together with all the Authority's capital assets. The physical inventory related to the equipment acquired with federal funds has been taken during the fiscal year 2014-2015. However, it has not been reconciled with the subsidiary ledger.<br><br>Current Status<br><br>This finding still prevails. See Current Year Finding 2016-003. |

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS
## JUNE 30, 2016

**Section III. Federal Award Findings and Questioned Costs**

| Single Audit Report | | Finding No. | Finding |
|---|---|---|---|
| **06/30/2015** | **Significant Deficiency** | **15-005** | **Reporting** |

Criteria and Condition

As per Agreement Number EMW-2011-PU-K00380-501, Article VII – Federal Financial Report (FFR) establishes the final FFR is due 90 days after the end date of the performance period. The final Federal Financial Report was due on August 31, 2014. However, it was submitted on April 13, 2015.

Current Status

This finding did not occure this year.

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS
## JUNE 30, 2016

### Section II. Financial Statement Findings

| Single Audit Report | | Finding No. | Finding |
|---|---|---|---|
| **06/30/2014** | **Significant Deficiency** | **14-II-01** | **Time Delays in Annual Accounting Closing**<br><br>Condition<br><br>The Authority has substantially improved the year-end accounting closing procedures and, accordingly, no auditing delay occurred in the current year. However, at date of the year-end closing certain accounts had not been analyzed; capital assets, litigation accrual, accounts payable and due from/to governmental entities, among others.<br><br>Criteria<br><br>The annual accounting closing and the underlying verification of records and accounts should be performed, analyzed and adjusted during the year.<br><br>Current Status<br><br>This finding still prevails. See current year finding 2016-001.<br><br>**Capital Assets Differences** |
| **06/30/2014** | **Material Weakness** | **14-11-02** | Condition<br><br>Existing procedures for recording capital assets and related accumulated depreciation result in numerous misclassifications, adjustments, and the need for further time-consuming reconciliation procedures.<br><br>Criteria<br><br>Capital assets should be properly recorded and classified timely and accurately.<br><br>Current Status<br><br>This finding still prevails. See current year finding 2016-002. |

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS JUNE 30, 2016

### Section III. Federal Award Findings and Questioned Costs

| Single Audit Report | Program | Finding No. | Finding |
|---|---|---|---|
| **06/30/2014** | **AIP & FTA** | **14-III-01** | **Cash Management** |

Criteria and Conditions

The A-102 Common Rule, 21 OMB Circular A-110, (2 CFR Section 215.22) state that procedures must be implemented to minimize the time elapsed between the transfer of funds from the federal agency and the disbursement of funds by the grantee. During our Cash Management Test of the AIP Program, from a sample of five (5) electronic bank transfers, we noted that in three (3) cases the program disbursements delay was between five (5) days and eight (8) days. For the FTA program from a three (3) electronic bank transfers, we noted that in the three (cases) was between nine (9) and 74 delay days.

Current Status

This finding did not occure this year.

| Single Audit Report | Program | Finding No. | Finding |
|---|---|---|---|
| **06/30/2014** | **AIP & FTA** | **14-III-02** | **Equipment and Real Property Management** |

Criteria and Conditions

The OMB Circular A-102, Common Rule, establishes that equipment acquired with federal awards having a useful life of more than one year and an acquisition cost of $5,000 or more per unit, should maintain adequate equipment records. A physical inventory of equipment shall be taken at least once every two years and reconciled to the equipment records. Appropriate internal control system should be used to safeguard equipment. During our examination, we noted that all equipment acquired with federal funds are not kept separately by program and instead, it is included together with all the Authority's capital assets. Therefore, the equipment records were not adequately maintained.

Current Status

This finding still prevails. See Current Year Finding 2016-003.

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS JUNE 30, 2016

**Section II. Financial Statement Findings**

| Single Audit Report | Significant Deficiency | Finding No. | Finding |
|---|---|---|---|
| **06/30/2013** | | **13-II-01** | **Time Delays in Annual Accounting Closing** |

Condition

The performance of the auditing procedures were delayed because of the Authority's untimely yearly accounting closing. However, management entered into an analysis and reconciliation process in areas such as: capital assets, accounts receivable and reserve for doubtful accounts, account payable, accruals and due to/from governmental entities, among others. The complexity of the analysis and reconciliation procedures post-phoned the receipts of a pre-audit trial balance.

In addition, during the performance of our auditing procedures, the Authority's external consultant recommend more than 30 post-closing adjustments. We recommend ten audit adjustments related to the fiscal year ended June 30, 2013.

As a result of the above, the completion and issuance of the Authority's financial statements experienced some delays.

Criteria

The annual accounting closing and the underlying verification of records and accounts should be performed, analyzed and adjusted timely during the annual closing.

Current Status

This finding still prevails. See Current Year Finding 2016-001.

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS
## JUNE 30, 2015

**Section II. Financial Statement Findings**

| Single Audit Report | Significant Deficiency | Finding No. | Finding |
|---|---|---|---|
| **06/30/2013** | | **13-II-02** | **Capital Assets Differences** |

Condition

Existing procedures for recording capital assets and related accumulated depreciation result in numerous misclassifications, adjustments, and the need for further time-consuming reconciliation procedures.

Criteria

Capital assets should be properly recorded and classified timely and accurately.

Current Status

This finding still prevails. See Current Year Finding 2016-002.

## SUMMARY OF SCHEDULE OF PRIOR YEARS FINDINGS AND QUESTIONED COSTS JUNE 30, 2016

### Section III. Federal Award Findings and Questioned Costs

| Single Audit Report | Program | Finding No. | Finding |
|---|---|---|---|
| **06/30/2013** | **AIP** | **13-III-01** | **Cash Management**<br><br>Criteria and Conditions<br><br>The A-102 Common Rule, 21 OMB Circular A-110, (2 CFR Section 215.22) state that procedures must be implemented to minimize the time elapsed between the transfer of funds from the federal agency and the disbursement of funds by the grantee. During our Cash Management Test, from a sample of 10 electronic bank transfers we noted that in two (2) cases the program disbursements delay was five (5) days.<br><br>Current Status<br><br>This finding did not occure during this year. |
| **06/30/2013** | **AIP & PSGP** | **13-III-02** | **Equipment and Real Property Management**<br><br>Criteria and Conditions<br><br>The OMB Circular A-102, Common Rule, establishes that equipment acquired with federal awards having a useful life of more than one year and an acquisition cost of $5,000 or more per unit, should maintain adequate equipment records. A physical inventory of equipment shall be taken at least once every two years and reconciled to the equipment records. Appropriate internal control system should be used to safeguard equipment. During our examination, we noted that all equipment acquired with federal funds are not kept separately by program and instead, it is included together with all the Authority's capital assets. Therefore, the equipment records were not adequately maintained.<br><br>Current Status<br><br>This finding still prevails. See current fiscal year finding 2016-003. |

COMMONWEALTH OF PUERTO RICO
Ports Authority

# CORRECTIVE ACTION PLAN
# SINGLE AUDIT 2015-2016

## Federal Award Findings and Questioned Costs

**Finding 2016-003 Equipment and Real Property Management**

Criteria and Conditions

The OMB Uniform Guidance and the 2016 Compliance Supplement, establishes that equipment acquired with federal awards having a useful life of more than one year and an acquisition costs of $5,000 or more per unit, should maintain adequate equipment records. During our examination, we noted that all equipment records acquired with federal funds are not kept separately by program and instead, it is included together with all the Authority's assets. The physical inventory related to the equipment acquired with federal funds was taken during the fiscal year 2014-2015. However, it has not been reconciled with the subsidiary ledger. This finding was repeated in prior years.

Corrective Action for Finding 2016-003

An initiative has taken place by creating a team with the FAA and PRPA personnel. This effort resulted in the development of procedures to support and improve deficiencies outlined in this audit. The procedures included taking physical inventory and the manner of reconciliation. The reconciliation was completed but we are waiting for the Internal Auditor to authorize the transactions that have been recomended. Also we are conducting efforts in order to make system adjustments to identify in the Inventory Module the equipment buyed with the specific Federal Funds Program. The system already provides to segregate by Fereral Funds or PRPA funds.

Responsible Official,

Vanessa Tirado Rodríguez
Acting Finance Director