

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

BASIC FINANCIAL STATEMENTS AND
REQUIRED SUPPLEMENTARY INFORMATION

FOR THE YEAR ENDED JUNE 30, 2018

(WITH INDEPENDENT AUDITOR'S REPORTS THEREON)



TORRES, HERNANDEZ & PUNTER, CPA, PSC
Certified Public Accountants

PUERTO RICO LAND AUTHORITY
(A Component Unit of The Commonwealth of Puerto Rico)

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INDEPENDENT AUDITOR'S REPORT

To the Management and
Board of Directors
Puerto Rico Land Authority
San Juan, Puerto Rico

Report on the Basic Financial Statements

We have audited the accompanying basic financial statements of Puerto Rico Land Authority (a component unit of the Commonwealth of Puerto Rico and from now on the Authority), which comprise the statement of net position as of June 30, 2018, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the basic financial statements, as listed in the table of contents.

Management's Responsibility for the Basic Financial Statements

Management is responsible for the preparation and fair presentation of these basic 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

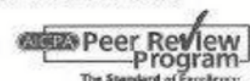
Our responsibility is to express an opinion on these basic financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards 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 basic financial statements are free from 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 basic 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 basic 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 basic financial statements.

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

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Basis for Qualified Opinion - Capital Assets Impaired

The Authority suffered damages to offices, warehouses, other structures and equipment, related to hurricanes Irma and Maria events, estimated at approximately \$28.8 millions. The Authority, as of basic financial statements date, is in the process of tracing the individual property and equipment items to a physical inspection damages detail, prepared by the Federal Emergency Management Agency (FEMA), to their capital assets details in order to dispose-off or adjust cost and accumulated depreciation related balances.

Given the effects of this natural disaster in the Authority, the Governmental Accounting Standards Board (GASB) Statement No. 42 "Accounting and Financial Reporting for Impairment of Capital Assets and For Insurance Recoveries", requires the recognition of capital asset impairments as soon as they occur. Losses from permanent impairments should be recognized in the Statement of Revenues, Expenses and Changes in Net Position in accordance with paragraphs 41-46, 55, 56, 101 and 102 of GASB No. 34. The restoration or replacement of the impaired capital asset should be reported as a separate transaction from the impairment loss and insurance recovery. Therefore, capital assets are overstated and the amount of loss from impairment and restoration or replacement of the impaired capital assets amounts is not available as of basic financial statements date.

Qualified Opinion

In our opinion, except for the effects of the matter described above in the "Basis for Qualified Opinion - Capital Assets Impaired" paragraph, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2018 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis - of - Matter

Restatement of Prior Year Basic Financial Statements

As discussed in Note 18, the 2017 basic financial statements has been restated to correct net position for the cumulative effect resulting from audited deferred outflows/inflows of resources, expenses and net liability balances provided by the Employee's Retirement System of the Commonwealth of Puerto Rico, for pension plan and other postemployment benefits other than pensions. Our opinion is not modified with respect to these matters.

Newly Adopted Standards

As discussed in Note 1(V) to the basic financial statements, the Authority adopted new guidance of GASB Statement No. 75 "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions", GASB Statement No. 81 "Irrevocable Split-Interests Agreements", GASB Statement No. 82 "Pension Issues - An Amendment of GASB Statement No. 67, No. 68 and No. 73", GASB Statement No. 84 "Fiduciary Activities", GASB Statement No. 85 "Omnibus 2017" and GASB Statement No. 86 "Certain Debt Extinguishment Issues". Our opinion is not modified with respect to these matters.

Emphasis - of - Matter (Continued)

Uncertainty about Ability to Continue as a Going Concern - Commonwealth of Puerto Rico

The Authority is an instrumentality of the Commonwealth of Puerto Rico (Commonwealth). The accompanying basic financial statements of the Authority have been prepared assuming that the Commonwealth will continue as a going concern. As discussed in Note 21 (c) to the basic financial statements, the Commonwealth and several component units recurring deficits, negative financial position, further deterioration of its economic condition, and inability to access the credit markets raises substantial doubt about the ability to continue as a going concern. The basic financial statements of the Authority do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

2010 Agriculture Department Reorganization Plan Number 4

As more explained on Note 17 (D) to the basic financial statements, Article 36 of the "Reorganization Plan number 4", discussed on Note 1 to the financial statements, amended laws number 165-2001 and 166-2001, requiring that funds received from coffee and sugar taxes be deposited in a new fund to be known as "Technological Innovation and Agricultural Promotion" ("Fondo de Innovacion"), to be transferred to the "Administration for the Development of Agricultural Enterprises" ("Administración para el Desarrollo de Empresas Agropecuarias" or ADEA). According to the Reorganization Plan, this fund can be administered by FIDA, through agreement with the Secretary of Agriculture, in order to promote the development of agriculture in Puerto Rico. However, the Reorganization Plan does not define how FIDA will cover its operational costs while promoting the agricultural and agro industrial development in Puerto Rico. It also comment that the Reorganization Plan does not establish which of the two entities will be finally be responsible for payment of FIDA credit lines through the GDB, and management of incentives already given to farmers. The Comptrollers Office of Puerto Rico (COPR) made recommendations to the Governor and the Legislative Assembly of Puerto Rico, to evaluate this concerns arising from Reorganization Plan Number 4, and the effect they will have on FIDA operations. The final outcome of COPR recommendations to the Governor and the Legislative Assembly of Puerto Rico cannot presently be determined and accordingly, no adjustments have been made in the accompanying financial statements.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America requires that the management's discussion and analysis, on pages 5 through 14, the schedule of proportionate share of the net pension liability and the related schedule of contributions, as part of employees' retirement systems information, on pages 85 to 87 respectively, and the schedule of proportionate share of the net other postemployment benefits other than pensions and the related schedule of contributions, on pages 88 to 90 respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by GASB, 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.

Other Matters (Continued)**Required Supplementary Information (Continued)**

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. We were unable to apply certain limited procedures to the required supplementary information related to employees' retirement systems information applicable to the Authority, in accordance with auditing standards generally accepted in the United States of America. We do not express an opinion or provide any assurance on the information.

Torres, Hernández & Punter, CPA, PSC

Torres, Hernández & Punter, CPA, PSC
Certified Public Accountants

Carolina, Puerto Rico

February 9, 2021

Stamp #EA39560 of the
College of CPA's of
Puerto Rico is affixed
to the original.

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

Management's Discussion and Analysis

June 30, 2018

This section of the Puerto Rico Land Authority ("the Authority") annual financial report, management discussion and analysis, presents our discussion of the Authority's financial performance and overview of financial activities during the fiscal year ended June 30, 2018. Please read it in conjunction with the Authority's basic financial statements and accompanying notes.

FINANCIAL HIGHLIGHTS

- The Authority's total assets decreased approximately by \$17.4 millions, \$169.8 millions in 2017, to \$152.4 millions in 2018, or 11%. Total Assets and Deferred Outflow of Resources decreased approximately \$18.8 millions, from \$184.5 millions in 2017 to \$165.7 millions in 2018,
- Total liabilities decreased approximately \$4.2 millions, from \$158.4 millions in 2017 to \$154.2 millions in 2018, or 4%. Basically, the decrease is due to net pension liability which amounted \$66.6 million in 2017 and \$58.6 million in 2018, for a decrease of \$7.9 million,
- Investment in capital assets and net capital assets amounted to \$94.2 million in 2017 and \$93.9 million in 2018, for a decrease of \$316,365. The decrease is mostly related to additions of \$291,470 less current depreciation expense of \$574,251,
- Total operating revenues decreased approximately \$420,635, from \$8.9 millions in 2017 to \$8.5 millions in 2018, or 5%. Total operating expenses amounted to \$29,303,619 in 2017 and \$26,442,694 in 2018, for a decrease of \$2.9 millions. Total operating expenses for 2018 includes an increase in bad debts expenses of \$13,089,324, when compared to 2017. Therefore, the Authority's operating expenses were reduced significantly during 2018, as explained below by the reduction in non operating revenues available to subsidize operations,
- Total net non - operating revenues and expenses decreased by approximately \$20.5 millions, \$19 millions in 2017 to \$(1.4) millions in 2018, or 14.36%, due mainly to the elimination of the coffee and sugar tax collections and a reduction in land sales. Other non operating revenues recorded in 2017, not available in 2018, were bad debt recoveries for \$999,249, sales of production of rice for \$128,076 and Commonwealth appropriations for \$740,176. Also, during 2018, there is an impairment loss from a bank account of FIDA with GDB for \$811,147, and a loss on investment on FIDA for \$1,714,495,
- Non - operating revenues "sales of land and exchange transactions related to land" decreased by approximately \$3.3 millions, from \$3.9 in 2017 to \$586,305 in 2018, a decrease of approximately 5.65%,
- Non - operating revenues "Coffee and Sugar Taxes" decreased by \$12.9 millions, from \$12.9 in 2017 to no revenue in 2018, a decrease of 100%, and
- Change in Net position amounted to \$(1,270,159) in 2017 and \$(19.3) millions in 2018, for a increase of \$(18.1) millions or .93%.

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

Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

New Significant Accounting Standards Implemented

During fiscal year 2016-2017, four new statements of financial accounting standards issued by the Governmental Accounting Standards Board (GASB), were adopted by the Authority:

1- GASB Statement No. 74, "Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans". The objective of this Statement is to improve the usefulness of information about postemployment benefits other than pensions (OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

2- GASB Statement No. 78, "Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans". The objective of this Statement is to address a practice issue regarding the scope and applicability of Statement No. 68, Accounting and Financial Reporting for Pensions. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. Prior to the issuance of this Statement, the requirements of Statement 68 applied to the financial statements of all state and local governmental employers whose employees are provided with pensions through pension plans that are administered through trusts that meet the criteria in paragraph 4 of that Statement.

3- GASB Statement No. 79, "Certain External Investment Pools and Pool Participants". This Statement addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes. An external investment pool qualifies for that reporting if it meets all of the applicable criteria established in this Statement. The specific criteria address (1) how the external investment pool transacts with participants; (2) requirements for portfolio maturity, quality, diversification, and liquidity; and (3) calculation and requirements of a shadow price. Significant noncompliance prevents the external investment pool from measuring all of its investments at amortized cost for financial reporting purposes. Professional judgment is required to determine if instances of noncompliance with the criteria established by this Statement during the reporting period, individually or in the aggregate, were significant.

4- GASB Statement No. 80, "Blending Requirements for Certain Component Units". This Statement establishes an additional presentation of component units. This Statement applies to all state and local governments. This Statement applies to component units that are organized as not-for-profit corporations in which the primary government is the sole corporate member. This Statement 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 amends Statement No. 14.

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

Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

During fiscal year 2017-2018, six new statements of financial accounting standards issued by the Governmental Accounting Standards Board (GASB), were adopted by the Authority:

1-GASB Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions". The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. This Statement replaces the requirements of Statements No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions", as amended, and 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.

2-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.

3-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 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.

PUERTO RICO LAND AUTHORITY
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Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

4-GASB Statement No. 84, "Fiduciary Activities". The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported.

This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities.

5-GASB Statement No. 85, "Omnibus 2017". The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]).

6-GASB Statement No. 86, "Certain Debt Extinguishment Issues". The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance.

Basic Financial Statements

This annual financial report consists of: the management's discussion and analysis (or MDA representing this section, which is required supplementary information) and:

- **Basic financial statements:** The Authority is a self-supporting entity and follows the enterprise fund reporting, accordingly, the basic financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Enterprise fund statements offer short-term and long-term financial information about the activities and the operations of the Authority. These statements are presented in a manner similar to a private business.

PUERTO RICO LAND AUTHORITY
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Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

- **Notes to the financial statements:** which provides more detailed information that is essential to a user's full understanding of the data provided in the statements.
- **Required Supplementary Information - Employee's Retirement System:** the annual financial report includes two required supplementary schedules after the notes to the basic financial statements, the Schedule of Proportionate Share of the Net Pension Liability and Schedule of Contributions, as the result of the implementation of GASB 68.
- **Required Supplementary Information - Postemployment Benefits Other Than Pensions (OPEB):** the annual financial report includes two new required supplementary schedules after the notes to the basic financial statements, the Schedule of Proportionate Share of the Other Postemployment Benefits Liability and Schedule of OPEB Contributions, as the result of the implementation of GASB 75.

Statement of Net Position

The change in net position serves, over time, as an useful indicator of the Authority's financial position. As of June 30, 2018, the Authority's assets and deferred outflows of resources exceeded its liabilities and deferred inflows of resources by \$2,832,914. As of June 30, 2017, the excess was \$23,468,860 as restated, representing a decrease of \$20,635,946, or 7.28%.

The largest portion of the Authority's net position represented its investment in capital assets, of \$93,893,002 and \$94,209,367 for the years ended June 30, 2018 and 2017 respectively.

Statement of Cash Flows

The statement of cash flows presents the sources and uses of cash flows divided in four categories: operating activities, non-capital financing activities, capital and related financing activities and investing activities. The statement reconciles net cash and cash equivalents at the beginning and end of year and reconciles the net income (loss) with the cash used in operating activities to provide an explanation of cash and non-cash activities within the statement of revenues, expenses and changes in net position.

The Authority's reporting structure includes the financial information of the Authority and a blended component unit - "Fondo Innovacion para el Desarrollo de la Agricultura" ("FIDA").

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

Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY

The following summarizes changes in the net position as of June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>	<u>\$ Changes</u>	<u>% Changes</u>
<u>Assets</u>				
Current assets	\$ 30,887,553	\$ 48,072,358	\$ (17,184,805)	(0.56)%
Non- Current Assets	<u>121,488,150</u>	<u>121,699,596</u>	<u>(211,446)</u>	<u>-</u> %
Total Assets	152,375,703	169,771,954	(17,396,251)	(0.11)
Deferred Outflow of Resources	<u>13,284,448</u>	<u>14,685,165</u>	<u>(1,400,717)</u>	<u>(0.11)%</u>
Total Assets and Deferred Outflow of Resources	<u>\$ 165,660,151</u>	<u>\$ 184,457,119</u>	<u>\$ (18,796,968)</u>	<u>(0.11)%</u>
<u>Liabilities</u>				
Current Liabilities	\$ 29,767,246	\$ 26,707,596	\$ 3,059,650	0.10 %
Net Pension Liability	58,641,397	66,554,910	(7,913,513)	(0.13)%
Termination Benefits	3,433,297	4,263,772	(830,475)	(0.24)%
Other Non - Current Liabilities	<u>62,344,595</u>	<u>60,889,449</u>	<u>1,455,146</u>	<u>0.02</u> %
Total Liabilities	<u>154,186,535</u>	<u>158,415,727</u>	<u>(4,229,192)</u>	<u>(0.03)%</u>
Deferred Inflows of Resources	<u>7,348,654</u>	<u>2,572,532</u>	<u>4,776,122</u>	<u>0.65</u> %
<u>Net Position</u>				
Invested in Capital Assets, Net	93,893,002	94,209,367	(316,365)	-
Unrestricted (Deficit)	<u>(89,768,040)</u>	<u>(70,740,507)</u>	<u>(19,027,533)</u>	<u>0.21</u> %
Total Net Position	<u>4,124,962</u>	<u>23,468,860</u>	<u>(19,343,898)</u>	<u>(4.69)%</u>
Total Liabilities, Deferred Inflows of Resources and Net Position	<u>\$ 165,660,151</u>	<u>\$ 184,457,119</u>	<u>\$ (18,796,968)</u>	<u>(0.11)%</u>

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

Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

Current Assets

Major components of current assets are as follows:

	<u>2018</u>	<u>2017</u>	<u>\$ Changes</u>	<u>% Changes</u>
Cash and Equivalents	\$ 17,883,006	\$ 16,281,041	\$ 1,601,965	0.09 %
Rent and Other				
Receivables	12,975,306	31,776,019	(18,800,713)	(1.45)%
Others	<u>29,241</u>	<u>15,298</u>	<u>13,943</u>	<u>0.48 %</u>
Totals	<u>\$ 30,887,553</u>	<u>\$ 48,072,358</u>	<u>\$ (17,184,805)</u>	<u>(0.56)%</u>

Decrease in rent and other receivable balances is mainly due to the write-off of FIDA's coffee and sugar taxes of \$12,772,208, which were uncollectible.

Other Major Components:

Capital Assets

Capital assets consists principally of land held for sale or for rent. During the year ended June 30, 2017, the Authority sold and exchange various land lots, generating a net gain on sales of \$3,904,620. During 2018, net gain on sales was \$586,305.

Non - Current Assets

The largest amount, which represents the amount that will not be collected during next fiscal year, consists mostly of the long - term portion of notes receivables and investments in private agricultural businesses. FIDA is authorized by law to provide credit lines to private and governmental entities, and to invest in private entities which are dedicated to agricultural activities in Puerto Rico. At fiscal year end, management evaluates the investments and valuation allowances.

PUERTO RICO LAND AUTHORITY
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Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

Current Liabilities

Major components of current liabilities are as follows:

	<u>2018</u>	<u>2017</u>	<u>\$ Changes</u>	<u>% Changes</u>
Accounts Payable, Accruals and Other Liabilities	\$ 27,990,660	\$ 24,855,202	\$ 3,135,458	0.11 %
Termination Benefits	747,419	860,761	(113,342)	(0.15)%
Advances for Farming Development	<u>1,029,167</u>	<u>991,633</u>	<u>37,534</u>	<u>0.04 %</u>
Totals	<u>\$ 29,767,246</u>	<u>\$ 26,707,596</u>	<u>\$ 3,172,992</u>	<u>0.11 %</u>

Other Major Components:

Non - Current Liabilities as June 30, 2018 consisted of long - tem financing related to the real estate program, through the Puerto Rico Public Financing Corporation (PFC), a component unit of the Commonwealth. The financing is repaid through appropriations made by the Commonwealth. In addition, FIDA has a non - revolving credit line with the Government Development Bank of Puerto Rico (GDB) with an outstanding balance for principal and accrued interests of \$28.1 millions. On November 29, 2018, through a Qualifying Modification under Title VI of PROMESA, an offset of this credit facility for \$22,971,172 was made. Borrowings under the credit line were repaid from coffee and sugar tax allocations and the credit facility is due on March 2027.

Also included is the net pension liability related to the employee's retirement system, which as of June 30, 2018 amounted to \$58,641,397, and decreased by \$7,913,513, or 13%. In addition, for the fiscal year ended June 30, 2018, the voluntary pre-retirement liability amounted to \$4,266,489, and decreased by \$858,044, or .20%. The Authority accrued \$1,657,962 and \$2,487,684, related to other post-employment benefits other than pension liability and pay-as-you-go liability, respectively.

Total liabilities decreased by \$5,160,370, or .04%.

PUERTO RICO LAND AUTHORITY
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Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

Operating Activities: The Authority entered into lease agreements on the land and properties it owns, with government and private entities. The agreements vary in prices offered and terms, depending on the intended public use and benefits to the Commonwealth of Puerto Rico's residents. The Authority also acquires and sells, to other government agencies and instrumentalities or private entities, land and property that have been determined to be used or developed for public interests. Operating expenses consists principally of payroll and related expenses, pension and pre-retirement expenses, program for the production of farming products and infrastructure and contracted services.

The following table summarizes the results of operations between fiscal years ended June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>	<u>\$ Changes</u>	<u>% Changes</u>
Operating Revenues	\$ 8,527,311	\$ 8,947,946	\$ (420,635)	(0.05)%
Operating Expenses	<u>26,442,694</u>	<u>29,303,619</u>	<u>(2,860,925)</u>	<u>(0.11)%</u>
Operating Loss	<u>(17,915,383)</u>	<u>(20,355,673)</u>	<u>2,440,290</u>	<u>(0.14)%</u>
Non - Operating Revenues (Expenses)				
Sales of Land and Exchange Transaction - Land	586,305	3,904,620	(3,318,315)	(5.66)%
Bad Debt Recovered	-	999,249	(999,249)	- %
Sales of Rice Production	-	128,076	(128,076)	- %
Coffee and Sugar Taxes Commonwealth	-	12,889,062	(12,889,062)	- %
Appropriations	-	740,176	(740,176)	- %
Federal Awards	647,371	435,170	212,201	0.33 %
Impairment Loss	(811,147)	-	(811,147)	1.00 %
Loss on Investments	(1,714,495)	-	(1,714,495)	1.00 %
Interest Expense	<u>(136,549)</u>	<u>(10,839)</u>	<u>(125,710)</u>	<u>0.92 %</u>
Non - Operating (Expense) / Revenues, Net	<u>(1,428,515)</u>	<u>19,085,514</u>	<u>(20,514,029)</u>	<u>14.36 %</u>
Change in Net Position	(19,343,898)	(1,270,159)	(18,073,739)	0.93 %
Net Position as of Beginning of Year, as Restated	<u>23,468,860</u>	<u>24,739,019</u>	<u>(1,270,159)</u>	<u>(0.05)%</u>
Net Position as of End of Year	<u>\$ 4,124,962</u>	<u>\$ 23,468,860</u>	<u>\$ (19,343,898)</u>	<u>(4.69)%</u>

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

Management's Discussion and Analysis (Continued)

June 30, 2018

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS (CONTINUED)

Total operating revenues decreased by \$420,635, mainly due to the decrease in the interest income charge to loans. Total operating expenses increased by \$145,618. Total operating expenses for 2018 includes an increase in bad debts expenses of \$13,089,324, when compared to 2017. Therefore, the Authority's operating expenses were reduced significantly during 2018, mostly due to the reduction in non - operating revenues available to subsidize operations,

Also, total non - operating revenues decreased by approximately \$21.1 millions, or 14.36%, mainly due to cancelation of the coffee and sugar tax collections, which were approximately \$12.8 million in 2017.

CAPITAL ASSETS

The Authority acquires and or develops land and structures with agricultural potential for future development by farmers. Also, the Authority is authorized by law to sell surplus land and properties to other governmental entities and individuals. The following table summarizes the capital assets of the Authority as of June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>	<u>\$ Changes</u>	<u>% Changes</u>
Capital Assets Not Being Depreciated:				
Land	\$ 87,516,401	\$ 86,515,201	\$ 1,001,200	0.01 %
Construction in Progress	<u>628,466</u>	<u>1,669,531</u>	<u>(1,041,065)</u>	<u>(1.66)%</u>
Total Capital Assets Not Being Depreciated	<u>88,144,867</u>	<u>88,184,732</u>	<u>(39,865)</u>	<u>- %</u>
Capital Assets Being Depreciated	28,271,347	28,152,500	118,847	- %
Less: Accumulated Depreciation	<u>(22,523,212)</u>	<u>(22,127,865)</u>	<u>(395,347)</u>	<u>0.02 %</u>
Total Capital Assets, Net	<u>\$ 93,893,002</u>	<u>\$ 94,209,367</u>	<u>\$ (316,365)</u>	<u>- %</u>

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

The financial report has the purpose of informing the Commonwealth of Puerto Rico residents and taxpayers, and our clients with a general financial overview of the Authority's finances and to comply with the Authority's accountability of the assets, funds and appropriations it holds and receives. If you have any questions about this report or need additional information, contact, Finance Director, at Puerto Rico Land Authority, 1311 Fernandez Juncos Avenue, 19 1/2, San Juan, Puerto Rico.

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

Statement of Net Position

June 30, 2018

	<u>Puerto Rico Land Authority</u>	<u>FIDA</u>	<u>Eliminations</u>	<u>Totals</u>
<u>Assets</u>				
Current Assets:				
Cash	\$ 1,340,065	\$ 16,542,941	\$ -	\$ 17,883,006
Accounts Receivable:				
Rent Receivable and Others, Net	4,489,786	-	-	4,489,786
Land Sales Receivable	3,700,000	-	-	3,700,000
Internal Balance Due From - FIDA	-	1,911,132	(1,911,132)	-
Due From Sugar Corporation of Puerto Rico	<u>4,785,520</u>	<u>-</u>	<u>-</u>	<u>4,785,520</u>
Total Accounts Receivable	<u>12,975,306</u>	<u>1,911,132</u>	<u>(1,911,132)</u>	<u>12,975,306</u>
Other Assets	<u>12,365</u>	<u>16,876</u>	<u>-</u>	<u>29,241</u>
Total Current Assets	<u>14,327,736</u>	<u>18,470,949</u>	<u>-</u>	<u>30,887,553</u>
Non-Current Assets:				
Restricted Cash	1,338,634	-	-	1,338,634
Notes Receivable, Net	2,166,249	20,144,397	-	22,310,646
Investment in Privately - Held Entities, Net	-	3,945,868	-	3,945,868
Capital Assets, Net	<u>92,495,170</u>	<u>1,397,832</u>	<u>-</u>	<u>93,893,002</u>
Total Non - Current Assets	<u>96,000,053</u>	<u>25,488,097</u>	<u>-</u>	<u>121,488,150</u>
Deferred Outflows of Resources:				
Pension Related	13,152,307	-	-	13,152,307
Other Postemployment Benefits Related	<u>132,141</u>	<u>-</u>	<u>-</u>	<u>132,141</u>
Total Deferred Outflows of Resources	<u>13,284,448</u>	<u>-</u>	<u>-</u>	<u>13,284,448</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 123,612,237</u>	<u>\$ 43,959,046</u>	<u>\$ (1,911,132)</u>	<u>\$ 165,660,151</u>

See accompanying notes which are an integral part of the Basic Financial Statements.

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

Statement of Net Position - (Continued)

June 30, 2018

<u>Liabilities</u>	<u>Puerto Rico Land Authority</u>	<u>FIDA</u>	<u>Eliminations</u>	<u>Totals</u>
Current liabilities:				
Accounts Payable and Accrued Liabilities	\$ 3,227,484	\$ 1,089,126	\$ -	\$ 4,316,610
Due to Governmental Entities	21,417,040	328,731	-	21,745,771
Accrued Compensated Absences	521,604	122,122	-	643,726
Interests Payable	-	451,361	-	451,361
Termination Benefits Payable	747,419	85,773	-	833,192
Advances for Farming Development	1,029,167	-	-	1,029,167
Internal Balance Due To - Puerto Rico Land Authority	<u>1,911,132</u>	<u>-</u>	<u>(1,911,132)</u>	<u>-</u>
Total Current Liabilities	<u>28,853,846</u>	<u>2,077,113</u>	<u>(1,911,132)</u>	<u>29,019,827</u>
Non - Current liabilities:				
Notes Payable	17,051,349	-	-	17,051,349
Credit Line	-	27,674,033	-	27,674,033
Net Pension Liability	58,641,397	-	-	58,641,397
Other Post Employment Benefit Liability	1,657,962	-	-	1,657,962
Termination Benefits Payable	3,106,996	326,301	-	3,433,297
Deposits on Rent	2,482,321	-	-	2,482,321
Accrued Legal Claims	4,438,920	-	-	4,438,920
Deposits on Sales of Land	7,903,919	-	-	7,903,919
Unearned Revenue	-	1,127,868	-	1,127,868
Accrued Compensated Absences	<u>612,321</u>	<u>143,321</u>	<u>-</u>	<u>755,642</u>
Total Non - Current Liabilities	<u>95,895,185</u>	<u>29,271,523</u>	<u>-</u>	<u>125,166,708</u>
Total Liabilities	<u>124,749,031</u>	<u>31,348,636</u>	<u>(1,911,132)</u>	<u>154,186,535</u>
Deferred Inflows of Resources:				
Unamortized Investment in Employees Retirement System	<u>7,348,654</u>	<u>-</u>	<u>-</u>	<u>7,348,654</u>
Total Deferred Inflow of Resources	<u>7,348,654</u>	<u>-</u>	<u>-</u>	<u>7,348,654</u>
<u>Net Position:</u>				
Net Investment in Capital Assets Unrestricted	92,495,170 <u>(100,980,618)</u>	1,397,832 <u>11,212,578</u>	- <u>-</u>	93,893,002 <u>(89,768,040)</u>
Total Net Position	<u>(8,485,448)</u>	<u>12,610,410</u>	<u>-</u>	<u>4,124,962</u>
Total Liabilities, Deferred Inflows of Resources and Net Position	<u>\$ 123,612,237</u>	<u>\$ 43,959,046</u>	<u>\$ (1,911,132)</u>	<u>\$ 165,660,151</u>

See accompanying notes which are an integral part of the Basic Financial Statements.

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

Statement of Revenues, Expenses and Changes
in Net Position

For the Fiscal Year Ended June 30, 2018

	<u>Puerto Rico Land</u> <u>Authority</u>	<u>FIDA</u>	<u>Totals</u>
<u>Operating Revenues:</u>			
Rental Income	\$ 7,288,330	\$ -	\$ 7,288,330
Services to Farmers	110,580	-	110,580
Royalty Income	106,117	-	106,117
Interest Income	132,029	689,997	822,026
Other	<u>184,133</u>	<u>16,125</u>	<u>200,258</u>
Total Operating Revenues	<u>7,821,189</u>	<u>706,122</u>	<u>8,527,311</u>
<u>Operating Expenses:</u>			
Research Fund - Act # 26-2008	-	222,338	222,338
Specialty Crops	-	647,371	647,371
Infrastructure Program	-	87,200	87,200
Payroll and Personnel Costs	4,612,165	894,766	5,506,931
Pension Expense	4,776,229	-	4,776,229
Other Postemployment Benefits Expense (Credit)	(508,091)	-	(508,091)
Repairs and Maintenance	56,464	11,322	67,786
Utilities	358,602	-	358,602
Supplies and Materials	7,513	-	7,513
Contracted Services	185,570	351,934	537,504
Insurance	37,003	29,443	66,446
Travel, Representation and Meals	69,318	-	69,318
Fuel	39,630	-	39,630
Depreciation	529,453	44,798	574,251
Bad Debt Expense	917,116	12,772,208	13,689,324
Other - General and Administrative	<u>116,685</u>	<u>183,657</u>	<u>300,342</u>
Total Operating Expenses	<u>11,197,657</u>	<u>15,245,037</u>	<u>26,442,694</u>
Operating Income (Loss) Before Non - Operating Revenues (Expenses)	<u>(3,376,468)</u>	<u>(14,538,915)</u>	<u>(17,915,383)</u>

See accompanying notes which are an integral part of the Basic Financial Statements.

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

Statement of Revenues, Expenses and Changes
in Net Position - (Continued)

For the Fiscal Year Ended June 30, 2018

	<u>Puerto Rico Land</u> <u>Authority</u>	<u>FIDA</u>	<u>Totals</u>
<u>Non - Operating Revenues</u>			
<u>(Expenses):</u>			
Sales of Land	\$ 586,305	\$ -	\$ 586,305
Loss on Investments -			
Privately - Held Entities	-	(1,714,495)	(1,714,495)
Federal Awards	-	647,371	647,371
Impairment Loss - Deposits Held at			
Government Development Bank	-	(811,147)	(811,147)
Interest Expense	<u>(136,549)</u>	<u>-</u>	<u>(136,549)</u>
Total Non - Operating Revenues/ (Expenses), Net	<u>449,756</u>	<u>(1,878,271)</u>	<u>(1,428,515)</u>
Change in Net Position	<u>(2,926,712)</u>	<u>(16,417,186)</u>	<u>(19,343,898)</u>
Beginning Net Position, as Previously Reported	(5,047,955)	29,027,596	23,979,641
Prior Period Adjustments	<u>(510,781)</u>	<u>-</u>	<u>(510,781)</u>
Net Position, Beginning of Year, as Restated	<u>(5,558,736)</u>	<u>29,027,596</u>	<u>23,468,860</u>
Net Position at End of Year	<u>\$ (8,485,448)</u>	<u>\$ 12,610,410</u>	<u>\$ 4,124,962</u>

See accompanying notes which are an integral part of the Basic Financial Statements.

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

Statement of Cash Flows

For the Fiscal Year Ended June 30, 2018

	<u>Puerto Rico Land Authority</u>	<u>FIDA</u>	<u>Totals</u>
Cash Flows From Operating Activities:			
Collection of Rent	\$ 7,224,769	\$ -	\$ 7,224,769
Collection of Services to Farmers	110,580	-	110,580
Collection of Royalties	132,029	-	132,029
Collection of Interests	106,117	689,997	796,114
Miscellaneous Collections	184,133	16,125	200,258
Payments to Employees, Related Payroll Costs and Others	(6,245,139)	(977,375)	(7,222,514)
Payment for Goods and Services on Operating Activities	<u>(1,942,763)</u>	<u>(1,687,965)</u>	<u>(3,630,728)</u>
Net Cash Used in Operating Activities	<u>(430,274)</u>	<u>(1,959,218)</u>	<u>(2,389,492)</u>
Cash Flows for Capital and Related Financing Activities:			
Capital Expenditures Acquisition	(26,828)	(264,868)	(291,696)
Proceeds From Sales of Land	620,115	-	620,115
Cash Impairment Loss	<u>-</u>	<u>(811,147)</u>	<u>(811,147)</u>
Net Cash Provided by (Used in) Capital and Related Financing Activities	<u>593,287</u>	<u>(1,076,015)</u>	<u>(482,728)</u>
Cash Flows for Non-Capital Financing Activities:			
Repayment on Deposits on Sales and Rent of Land	(362,519)	-	362,519
Advances To Farming Development	-	(1,393,361)	(1,393,361)
Collection on Advances To Farming Development	37,534	-	37,534
Coffee and Sugar Tax Appropriations	-	6,200,000	6,200,000
Federal Awards Contributions	-	647,371	647,371
Interest Paid	(136,549)	-	(136,549)
Advances/(Repayments) to Other Related	<u>330,325</u>	<u>(438,259)</u>	<u>(107,934)</u>
Net Cash (Used in) Provided by Non-Capital Financing Activities	<u>(131,209)</u>	<u>5,015,751</u>	<u>4,884,542</u>
Cash Flows From Investing Activities:			
Collection of Principal on Notes Receivables	<u>310,910</u>	<u>-</u>	<u>310,910</u>
Net Cash Provided by Investing Activities	<u>310,910</u>	<u>-</u>	<u>280,759</u>
Net Change in Cash and Cash and Equivalents	342,714	1,980,518	2,323,232
Cash and Cash and Equivalents Beginning of Year	<u>2,335,985</u>	<u>14,562,423</u>	<u>16,898,408</u>
Cash and Cash and Equivalents at End of Year	<u>\$ 2,678,699</u>	<u>\$ 16,542,941</u>	<u>\$ 19,221,640</u>
Reconciliation of Cash and Cash Equivalents with the Statement of Net Position:			
Unrestricted Cash and Deposit Certificates	\$ 1,340,065	\$ 16,542,941	\$ 17,883,006
Restricted Cash	<u>1,338,634</u>	<u>-</u>	<u>1,338,634</u>
Total Cash and Cash Equivalents	<u>\$ 2,678,699</u>	<u>\$ 16,542,941</u>	<u>\$ 19,221,640</u>

See accompanying notes which are an integral part of the Basic Financial Statements

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

Statement of Cash Flows (Continued)

For the Fiscal Year Ended June 30, 2018

	<u>Puerto Rico Land Authority</u>	<u>FIDA</u>	<u>Totals</u>
Reconciliation of Operating Loss to Net Cash Used by Operating Activities:			
Operating Loss	\$ (3,376,468)	\$ (14,538,915)	\$ (17,915,383)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:			
Depreciation	529,453	44,798	574,251
Bad Debt	917,116	12,772,208	13,689,324
(Increase) in Rent Receivable	(980,677)	-	(980,677)
Increase (Decrease) in Accounts Payable and Accrued Liabilities	657,134	(465,874)	191,260
(Increase) in Other Assets	(2,511)	(11,432)	(13,943)
Increase in Due to Governmental Entities	845,077	328,731	1,173,808
(Decrease) in Pension Liability	(5,740,679)	-	(5,740,679)
Increase (Decrease) in Deferred Inflow	7,639,560	(212,439)	7,427,121
(Increase) in Deferred Outflow	(261,336)	-	(261,336)
Decrease (Increase) in Accrued Compensated Absences	(619,101)	123,705	(495,396)
Decrease in Accrued Legal Claims	<u>(37,842)</u>	<u>-</u>	<u>(37,842)</u>
Net Cash Used by Operating Activities	<u>\$ (430,274)</u>	<u>\$ (1,959,218)</u>	<u>\$ (2,389,492)</u>

See accompanying notes which are an integral part of the Basic Financial Statements.

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

Notes to the Basic Financial Statements

For the Fiscal Year Ended June 30, 2018

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(A) ORGANIZATION AND ACTIVITIES

The Puerto Rico Land Authority (from now on the Authority), is a public corporation and a component unit of the Commonwealth of Puerto Rico. The Authority was created by Act No. 26 approved on April 12, 1941, as amended, to carry out the provisions of the Land Law of Puerto Rico. By provision of Reorganization Plan No. 1 of May 4, 1994, the Land Authority became a programmatic and operational component of the Department of Agriculture (from now on DA).

On July 26, 2010, the Governor of Puerto Rico approved the “Reorganization Plan Number 4”, also known as “Plan for the 2010 DA Reorganization”. This Law provided for the reorganization of such Department and its programmatic and operational components, and was presented as part of Law Number 182 of December 17, 2009, known as “Reorganization and Modernization Law of the Executive Branch of Puerto Rico”. The purpose of this law was to provide DA and its components more administrative and legal flexibility in order to implement and carry out its responsibilities and obligations.

Through this plan, the Corporation for Rural Development and the Administration for Services and Agricultural Development (also known as ASDA) were eliminated. The tasks of this two entities were transferred to a new entity, the “Administration for the Development of Agricultural Enterprises” (“Administración para el Desarrollo de Empresas Agropecuarias” or ADEA). Also, the program for family farms was transferred to the Authority and the ownership of the land lots from the Corporation for Rural Development.

From the Reorganization Plan, DA is now composed of the following entities:

- The DA,
- The Authority and its affiliates,
- The Corporation for Agricultural Insurance (“Corporación de Seguros Agrícolas”), and
- ADEA.

The basic financial statements of the Authority are included as a component unit of the Commonwealth of Puerto Rico and substantially conform to the standards and practices established by the Governmental Accounting Standards Board (from now on GASB).

The Authority was created for the following purposes:

- Acquiring land with agricultural potential through purchase, transfer, exchange, bequest and donation or by the exercise of power of forceful expropriation,
- Selling land that has no agricultural use,
- Maintaining land with agricultural potential under lease,
- Leasing heavy agricultural machinery and equipment,
- Conducting all types of transactions related to land purchase, sale and leasing applications,
- Making appraisals of land to be sold,
- Preparing plans and control of land for sale and rent, and
- Negotiate the collection of rent from farmers through Legal and Finance Offices.

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(A) ORGANIZATION AND ACTIVITIES (CONTINUED)

The Authority operates one program, the Real Estate Program, which leases land owned by the Authority and held for agricultural purposes, principally to farmers, including farming services when requested by farmers. Moreover, the Authority is authorized by law to sell surplus land and properties to other governmental entities and individuals.

Also, the Authority manages infrastructure projects on behalf of the DA. Legislative funds were appropriated to create and improve drainage systems, water and sewer systems, bridges, roads, lakes, lighting systems and others. The basic financial statements do not reflect the effects of transactions related to managing such infrastructure projects and funds.

(B) FINANCIAL REPORTING ENTITY

The financial reporting entity included in this report consists of the basic financial statements of the Authority (primary government). To fairly present the financial position and the results of operations of the financial reporting entity, management must determine whether its reporting entity consists of only the legal entity known as the primary government or one or more organizations called component units. The inclusion of a potential component unit in the primary government's reporting entity depends on whether the primary government is financially accountable for the potential component unit or on whether the nature and significance of the relationship with the primary government is such that exclusion would cause the reporting entity's basic financial statements to be misleading or incomplete.

GASB Accounting Standards Codification Section 2100, "Defining the Financial Reporting Entity", describes the criteria for determining which organizations, functions, and activities should be considered part of the Authority for financial reporting purposes. Following GASB Sections 2100 and 2600 "Reporting Entity and Component Unit Presentation and Disclosure", there are two methods of presentation of the component unit in the basic financial statements: (a) blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Authority's balances and (b) discrete presentation of the component unit's financial data in columns separate from the Authority's balances and transactions.

The basic criteria for deciding financial accountability are any one of the following:

- Financial dependency of the potential component unit on the primary government, or
- The primary government appoint a voting majority of the potential component unit's governing body and,
 1. The primary government can impose its will on the potential component unit and/or,
 2. A financial benefit/burden exists between the primary government and the potential component unit.

In addition, a legally separate, tax exempt organization should be discretely presented as a component unit of a reporting entity if all of the following criteria are met:

- The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents,
- The primary government, or its component units, is entitled to, or has the ability to otherwise access a majority of the economic resources received or held by the separates organization, and

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(B) FINANCIAL REPORTING ENTITY (CONTINUED)

- The economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

Other organizations should be evaluated as potential component units if they are closely related to, or financially integrated with, the primary government. Professional judgment is applied in determining whether the relationship between a primary government and other organizations for which the primary government is not accountable and that do not meet these criteria is such that exclusion of the organization would render the financial statements of the reporting entity misleading or incomplete.

GASB Statement 61, "The Financial Reporting Entity: Omnibus an Amendment of GASB Statements No. 14 and No. 34", provides additional criteria for classifying entities as component units to better assess the accountability of elected officials by ensuring that the financial reporting entity includes only organizations for which the elected officials are financially accountable or that are determined by the government to be misleading to exclude.

Based on the above criteria, the basic financial statements of the Authority include the balances of one of its component units, the "Fondo de Innovacion para el Desarrollo Agrícola de Puerto Rico" (from now on "FIDA"). The primary purpose is to promote private investment in the general farming industry, by approving loans, warranties, direct and indirect investments, and other credit financing facilities, with favorable repayment conditions and interests rates to the agricultural industries. The Authority created FIDA during fiscal year 2001-2002 under the name "Integral Fund for the Agriculture Development of Puerto Rico". On December 16, 2010, the Authority's Board of Directors approved to change the name. All significant interfund transactions were eliminated.

Based also on the above criteria, the Sugar Corporation of Puerto Rico is not a component unit of the Authority and in accordance with Act. No. 189 named "Law of the Transfer of Assets and Liabilities for Negotiations of the Sugar Corporation and the Puerto Rico Land Authority", of September 5, 1996, is in the process of liquidation.

BASIS OF BASIC FINANCIAL STATEMENTS PRESENTATION

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America (US GAAP) applicable to governmental entities. The Authority follows 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.

(C) METHOD OF ACCOUNTING FOR PROPRIETARY FUNDS AND BASIC FINANCIAL STATEMENTS PRESENTATION

The Authority reports its financial position and results of operations as an enterprise fund. Financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Proprietary funds are used to account for business - type activities, which are financed mainly by fees and charges to users of the services provided by the funds operations. Proprietary funds distinguish operating revenues and expenses from non - operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non - operating revenues and expenses.

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BASIS OF BASIC FINANCIAL STATEMENTS PRESENTATION (CONTINUED)

Pursuant to GASB Statement No. 63, "Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position", and GASB Statement No. 65, "Items Previously Reported as Assets and Liabilities", the Authority recognized deferred outflows of resources in the basic financial statements. These items are a consumption of net position by the Authority that is applicable to a future reporting period. Previous financial reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities. The Authority has items that are reportable on the Statement of Net Position that are relates to outflows/inflows from changes in the Net Pension Liability (Note 14), items that relates to outflows/inflows from changes in the Other Postemployment pension liability (OPEB - Note 15) and items that relates to deferred inflows of resources from deposits on sales of land transactions (Note 9) as of basic financial statements date.

Note 13 provides details on deferred outflows of resources and deferred inflows of resources.

REQUIRED SUPPLEMENTARY INFORMATION - MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's discussion and analysis is required supplementary information that introduces the basic financial statements and provides an analytical overview of the Authority's financial activities. This analysis is similar to the analysis the private sector provides in their annual reports.

NOTES TO THE BASIC FINANCIAL STATEMENTS

The notes to the basic financial statements provide information that is essential to a user's full understanding of the data provided in the basic financial statements

REQUIRED SUPPLEMENTARY INFORMATION - EMPLOYEES RETIREMENT SYSTEM

GASB Statement No. 68, "Accounting and Financial Reporting for Pensions", that is effective for the Authority's fiscal year beginning July 1, 2014, revises existing standards for measuring and reporting pension liabilities for pension plans provided by the Authority to its employees, and required supplementary information that include the Schedule of Proportionate Share of the Net Pension Liability and Schedule of Contributions.

REQUIRED SUPPLEMENTARY INFORMATION - POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEB)

The Authority provides post-employment benefits other than pension for its retired employees (the "OPEB Program"). In accordance with GASB Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pension"s, that replaces GASB Statement No. 45 "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions", changes similar to those implemented on GASB Statement No. 67, "Financial Reporting for Pension Plans", and Statement No. 68, "Accounting and Financial Reporting for Pensions" should be made. The Statement requires supplementary information that include the Schedule of Proportionate Share of the Net OPEB Liability and Schedule of Contributions.

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(D) USE OF ESTIMATES

The preparation of basic financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from those estimates.

(E) CASH AND CASH EQUIVALENTS

Cash includes demand deposits in commercial banks, demand deposits in the Governmental Development Bank of Puerto Rico (from now on GDB), and cash equivalents in commercial banks, on hand and short-term investments with maturities of three months or less.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies is presented to assist in understanding that the basic financial statements and notes are representations of management, who is responsible for their integrity and objectivity. These accounting policies conform to US GAAP.

(F) INVESTMENTS IN AGRICULTURAL BUSINESSES

Investments in private entities are reported at cost, since these are not intended to obtain profit, but rather to promote agricultural and related businesses. During the year ended June 30, 2018, the Authority evaluated its investments in agricultural businesses for impairment and determined a loss on investments of \$1,714,495.

(G) INTERFUND BALANCES

Interfund receivables and payables balances, between the Authority and its component unit FIDA have been eliminated from the statement of net position.

(H) RECEIVABLES AND ALLOWANCE FOR DOUBTFUL ACCOUNTS

The allowance for uncollectible notes and other receivables is an amount that the Authority believes will be adequate to absorb possible losses on existing receivables that are identified as to be remote collectibles and others that may become collectible based on collection analysis and prior credit loss experience. Because of uncertainties inherent in the estimation process, the related allowance may change in the future.

(I) CAPITAL ASSETS AND DEPRECIATION POLICY

The Authority defines capital assets as assets with an individual cost of more than \$100 and a useful life of three (3) years or more. Assets to be depreciated were assigned a residual value of 10% of original cost. Capital assets are stated at cost. The costs of normal maintenance and repairs that do not add to the asset's value or materially extend the asset's useful life are not capitalized.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(I) CAPITAL ASSETS AND DEPRECIATION POLICY (CONTINUED)

Depreciation expense is computed using the straight-line method over the estimated useful lives of the respective assets, as follows:

<u>Description</u>	<u>Estimated Useful Lives</u>
Building and Improvements	20 - 40
Infrastructure	10 - 20
Industrial Equipment, Machinery and Equipment and Others	5 - 20
Furniture and Fixtures, Vehicles	3 - 7

At the time capital assets are sold or otherwise disposed, the cost and related accumulated depreciation is removed from books and the resulting gain or loss, if any is credited or charged to operations.

(J) ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG - LIVED ASSETS

The Authority follows GASB Statement No. 42, "Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries". This Statement establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This Statement also clarifies and establishes accounting requirements for insurance recoveries. During the year ended June 30, 2018, the Authority evaluated its capital assets for impairment under the guidance of this Statement and determined that the possible impairment amount, if any, would not have a material impact in the Authority's basic financial statements.

(K) LAND AND PROPERTIES COST

When portions of land parcels are sold, the cost of land is determined by computing an average area unit cost at the date in which land was acquired, which is then applied to the total area sold. Sale of air and surface rights to land is recognized as sale of land.

(L) ACCOUNTING FOR PENSION COSTS

In June 2012, GASB issued two new pronouncements related to the accounting and financial reporting requirements for pension related expenses and liabilities. GASB Statement No. 67, "Financial Reporting for Pension Plans" an amendment of GASB Statement No. 25, replaces the requirements of GASB Statement No's. 25 and 50 for plans administered by pension systems through trusts or equivalent arrangements, and was implemented by the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (from now on ERS) as of June 30, 2014.

In addition, GASB issued Statement No. 68, "Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27", effective for the Authority's' fiscal year beginning July 1, 2014. This Statement revises existing standards for measuring and reporting pension liabilities for pension plans provided by the Authority to its employees. This Statement requires recognition of a liability equal

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(L) ACCOUNTING FOR PENSION COSTS (CONTINUED)

to the net pension liability, which is measured as the total pension liability, less the amount of the pension plan's fiduciary net position. The total pension liability is determined based upon discounting projected benefit payments based on the benefit terms and legal agreements existing at the pension plan's fiscal year-end. Projected benefit payments are required to be discounted using a single rate that reflects the expected rate of return on investments, to the extent that plan assets are available to pay benefits, and a tax-exempt, high-quality municipal bond rate when plan assets are not available.

This Statement requires that most changes in the net pension liability be included in pension expense in the period of the change. To the extent practical, the basic financial statements presented for the periods affected should be restated. Also, GASB Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date, an amendment to GASB 68", was required to be implemented simultaneously with the provisions of GASB 68.

The Authority accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing multi-employers plan. During fiscal year ended June 30, 2015, the Authority implemented GASB Statement No. 68, Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27. This statement establishes accounting and financial reporting for pensions provided to the employees of state and local government employers through pension plans that are administered through trusts that have the following characteristics:

- Contributions from employers and nonemployer contributing entities to the pension plan and earnings on those contributions are irrevocable,
- Pension plan assets are dedicated to providing pensions to plan members in accordance with the benefit terms, and
- Pension plan assets are legally protected from the creditors of employers, nonemployer contributing entities, and the pension plan administrator. If the plan is a defined benefit pension plan, plan assets also are legally protected from creditors of the plan members.

For the purpose of applying the requirements of GASB No. 68, as amended, the state government of the Commonwealth is considered to be the sponsor of the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (ERS), a cost-sharing multi-employer Defined Benefit Pension Plan, and Defined Contribution Hybrid Program, in which the employees of the Authority participate. The Authority is considered a participant of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Commonwealth and the basic financial statements of such retirement systems are part of the financial reporting entity of the Commonwealth. Act No. 3 was enacted on April 4, 2013, amended the Act No. 447 for the purpose of establishing a major reform of the ERS effective on July 1, 2013. After that, and based on the fiscal crisis of the Commonwealth, was enacted the Act No. 106 of 2107 to establish a New Define Contribution Plan and create the pay-as-you-go scheme for payment of pensioners of the ERS and the other two retirement systems (See also Note 14).

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(L) ACCOUNTING FOR PENSION COSTS (CONTINUED)

For purposes of measuring the Net Pension Liability and Deferred Outflows/Inflows of Resources related to pensions, and pension expense, information about the fiduciary net position of the ERS and additions to/deductions from the ERS's fiduciary net position have been determined on the same basis as they are reported by Commonwealth of Puerto Rico. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

(M) POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEB)

Other postemployment benefits ("OPEB") expense is recognized and disclosed using the accrual basis of accounting. The Authority recognizes the total OPEB liability since the Authority's OPEB program is funded on a pay-as-you-go basis. Changes in the total OPEB liability during the period are recorded as OPEB expense, or as deferred inflows of resources or deferred outflows of resources depending on the nature of the change, in the period incurred. Those changes in total OPEB liability that are recorded as deferred inflows of resources or deferred outflows of resources that arise from changes in actuarial assumptions or other inputs and differences between expected or actual experience are amortized over the average of the remaining service life of all participants including retirees and recorded as a component of OPEB expense beginning with the period in which they arose. The Authority accounted for postemployment benefits other than pensions (OPEB) under the provisions of GASB Statement No. 75 "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions". See also Note 15.

(N) TERMINATION BENEFITS

The Authority accounts for termination benefits in accordance with the provisions of GASB Statement No. 47, "Accounting for Termination Benefits". This Statement establishes accounting standards for termination benefits. Pursuant to this Statement, the Administration should recognize a liability and expense for voluntary termination benefits (for example, early retirement incentives) when the offer is accepted, and the amount can be estimated. See also Note 20.

(O) COMPENSATED ABSENCES

Law No. 8 of February 4, 2017 for the "Administration and Transformation of Human Resources in the Government of Puerto Rico" (Law No. 8-2017) and Law 26 of April 29, 2017 issued for compliance with Act No. 26-2017, named "Law for Compliance with Fiscal Plan" establishes new parameters for the accrual of vacations and sick leave. Every government employee shall be entitled to accrue one and one-fourth (1¼) day of vacation leave for every month of service, for a total of 15 days per year. The employees shall begin to accrue the vacation leave upon completion of a three (3)-month period and said leave shall be retroactive to the employment commencement date. Furloughed or part-time employees shall accrue vacation leave proportionately to the number of hours regularly worked. The vacation leave may be accrued up to a maximum of sixty (60) workdays at the end of any calendar year. Vacation leave is granted to employees in order to allow them a reasonable annual rest period. As a general rule, said leave shall be used during the calendar year in which it was accrued. Every agency or public instrumentality is required to devise a vacation plan for every calendar year, in collaboration with supervisors and employees, establishing the period during which employees shall enjoy their vacation time in the manner that is more compatible with the needs for service. Said plan shall be completed no later than on December 31st of every year, so that it takes effect on January 1st of the following year.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(O) COMPENSATED ABSENCES (CONTINUED)

The Authority accrued a liability for compensated absences, which meet the following criteria: (1) the Authority's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered; (2) the obligation relates to rights that vest or accumulate; (3) payment of the compensation is probable; and (4) the amount can be reasonably estimated.

In accordance with the above criteria and requirements in conformance with GASB Accounting Standards Codification Section C60, "Compensated Absences", the Authority has accrued a liability for compensated absences, which has been earned but not taken by the Authority's employees, including its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay using salary rates effective as of June 30, 2018. All vacation pay is accrued when incurred. The current portion is the amount estimated to be used in the following year.

In addition, employees accumulate sick leave at a rate of 18 days per year, with a maximum permissible accumulation of 90 days at the end of any natural year.

As of June 30, 2018, the Authority accrual for compensated absences amounts to \$1,399,368 which represents the Authority's commitment to fund such compensated absences for future operations. Of this amount, the Authority estimates that approximately \$643,726 are due during the next fiscal year.

(P) ACCRUAL FOR LEGAL CLAIMS

The estimated amount of the liability for legal claim 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 legal claims. The Authority consulted with legal counsel to determine whether an unfavorable outcome is probable. Because of uncertainties inherent in the estimation process, management's estimate of the liability for legal claims may change in the near term.

(Q) NET POSITION CLASSIFICATION

Net position represent the difference between assets and liabilities and are presented in three components as follows:

- **Net Investment in Capital Assets** - consist of capital assets net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or borrowings that are attributable to the acquisition, construction, or improvements of those assets.

Net position invested in capital assets, net of related debt, is composed of the following:

Capital Assets, Net of Accumulated Depreciation	\$ 93,893,002
Outstanding Balance on Related Debt	<u>-</u>
Total Invested in Capital Assets, Net of Related Debt	<u>\$ 93,893,002</u>

- **Restricted Net Position** - consist of net position with constraint placed on the use either by: (1) external groups such as creditors, grantors, contributions, or law or regulations of other government; (2) law through constitutional provisions or enabling legislation. As of June 30, 2018 there is no restrictions imposed, and therefore, no restricted net position has been presented, and

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(Q) NET POSITION CLASSIFICATION (CONTINUED)

- **Unrestricted Net Position** - consist of all other assets that do not meet the definitions of "restricted" or "invested in capital assets, net of related debts".

(R) OPERATING REVENUES AND EXPENSES

The Authority distinguishes between operating and non - operating revenues and expenses in its statement of revenues, expenses and changes in net position. The principal revenues of the Authority are charges for land rental and services to farmers. The Authority also recognizes as operating revenues interest income generated on loans granted by FIDA. Operating expenses for the Authority include the costs of developing farming products, payroll and fringe benefits, and other administrative expenses such as utilities, repairs, contracted services and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non - operating revenues and expenses.

The Authority receives contributions from the Commonwealth. These contributions, which are subject to annual appropriations, are used to partially finance the operations of the Real Estate Program. Amounts received are recorded as a non - operating revenue in the period stated in the grant.

(S) REVENUE RECOGNITION

The following represents the Authority's policy for revenue recognition:

- All leases are deemed operating leases, therefore rental income is recognized as operating revenue over the term of the lease. Advance lease payments are recorded as deferred revenue and recognized as rental revenue when earned over the lease period.
- Rental income is composed of the lease canon and estimated property tax, using The Municipal Revenues Collection Center (from now on CRIM) tax rate, and multiplied by the number of lots leased.
- For services provided to farmers, revenue is recognized at the time the service was rendered.
- For land and property sales, revenues are recognized when title is conveyed to buyers. Funds received from infrastructure program and federal assistance are recognized when disbursement of the funds are made.
- Income from coffee and sugar taxes is recognized when the Commonwealth of Puerto Rico notifies FIDA. Coffee taxes imposed and collected by Federal U.S. Agencies are deposited at the Commonwealth, commingled with sugar taxes collections. Pending bills and undeclared taxes are not recorded in FIDA books. For the fiscal year ended June 30, 2018, such income ceased and was not received.

(T) PROPERTY TAXES

On September 9, 2010, the Superior Court in San Juan, Court of First Instance, decided that the Authority should paid to CRIM \$12,117,630 for property taxes accrued as of June 30, 2010. Total outstanding debt as of June 30, 2018 is \$11,704,721, net of credits, and is applied to "bonafide farmers" (Law number 225) against their accounts receivable (See Note 12). This amount is reported as part of due to governmental entities as of June 30, 2018.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(U) RISK MANAGEMENT

To minimize its risk of loss, the Authority purchases insurance coverage for public liability, automobile, crime, inland marine, commercial property and garage, as well as medical and workmen's insurance for employees. The selection of the insurer has to be approved by the Public Insurance Office of the Puerto Rico Treasury Department. Insurance coverage is updated annually to account for changes in operating risk. For the last three years, insurance settlements have not exceeded the amount of coverage.

(V) NON-EXCHANGE TRANSACTIONS

GASB Statement No. 33, "Accounting and Financial Reporting for Non-exchange Transactions", establishes accounting and financial reporting standards for non-exchange transactions involving financial or capital resources (for example, most taxes, grants, and private donations). In non-exchange transactions, a government gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal values. Under the provisions of this statement, the provider and the recipient should recognize the non-exchange transaction as an expense and revenue, respectively, when all eligibility requirements are satisfied.

(W) NEW ACCOUNTING STANDARDS

A. Implementation of GASB Statements

The provisions of the following GASB Statements are effective for financial statements for periods beginning after June 15, 2016 (FY 2016-2017) and have been implemented, when applicable, during the year ended June 30, 2018:

- **GASB Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions"**. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

This Statement replaces the requirements of Statements No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended, and 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

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

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 nonemployer entity provides financial support for OPEB of employees of another entity. In this Statement, distinctions are made regarding the particular requirements depending upon whether the OPEB plans through which the benefits are provided are administered through trusts that meet the following criteria:

- a. Contributions from employers and nonemployer contributing entities to the OPEB plan and earnings on those contributions are irrevocable,
 - b. OPEB plan assets are dedicated to providing OPEB to plan members in accordance with the benefit terms, and
 - c. OPEB plan assets are legally protected from the creditors of employers, nonemployer contributing entities, the OPEB plan administrator, and the plan members.
- **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.

GASB No. 81 does not have any impact on the Authority's financial statements.

- **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

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

measures in required supplementary information, (2) the selection of assumptions and the treatment of 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). The requirements of this Statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of paragraph 7 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 the circumstance, the requirements of paragraph 7 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 (FY 2017-2018).

- **GASB Statement No. 84, "Fiduciary Activities"**. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported.

This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities.

An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. An exception to that requirement is provided for a business-type activity that normally expects to hold custodial assets for three months or less.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

This Statement describes four fiduciary funds that should be reported, if applicable, (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria.

A fiduciary component unit, when reported in the fiduciary fund financial statements of a primary government, should combine its information with its component units that are fiduciary component units and aggregate that combined information with the primary government's fiduciary funds.

This Statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.

The requirements of this Statement are effective for reporting periods beginning after December 15, 2018 (FY 2018-2019). Earlier application is encouraged.

- **GASB Statement No. 85, "Omnibus 2017"**. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). Specifically, this Statement addresses the following topics:
 1. Blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation.
 2. Reporting amounts previously reported as goodwill and "negative" goodwill.
 3. Classifying real estate held by insurance entities.
 4. Measuring certain money market investments and participating interest-earning investment contracts at amortized cost.
 5. Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus.
 6. Recognizing on-behalf payments for pensions or OPEB in employer financial statements.
 7. Presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans and employers that provide OPEB.
 8. Classifying employer-paid member contributions for OPEB.
 9. Simplifying certain aspects of the alternative measurement method for OPEB

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

10. Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans.

- **GASB Statement No. 86, "Certain Debt Extinguishment Issues"**. The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources other than the proceeds of refunding debt are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance.

GASB No. 86 does not have any impact on the Authority's financial statements.

B. Future Adoption of GASB Statements

The Governmental Accounting Standards Board issued the following pronouncements that have effective dates after June 30, 2018. The Authority is currently evaluating its accounting practices to determine the potential impact on the financial statements for the GASB Statements.

- **GASB Statement No. 83, "Certain Asset Retirement Obligations"**. This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement.

This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs. This Statement requires that recognition occur when the liability is both incurred and reasonably estimable. The determination of when the liability is incurred should be based on the occurrence of external laws, regulations, contracts, or court judgments, together with the occurrence of an internal event that obligates a government to perform asset retirement activities. Laws and regulations may require governments to take specific actions to retire certain tangible capital assets at the end of the useful lives of those capital assets, such as decommissioning nuclear reactors and dismantling and removing sewage treatment plants. Other obligations to retire tangible capital assets may arise from contracts or court judgments. Internal obligating events include the occurrence of contamination, placing into operation a tangible capital asset that is required to be retired, abandoning a tangible capital asset before it is placed into operation, or acquiring a tangible capital asset that has an existing ARO.

This Statement requires the measurement of an ARO to be based on the best estimate of the current value of outlays expected to be incurred. The best estimate should include probability weighting of all potential outcomes, when such information is available or can be obtained at reasonable cost. If probability weighting is not feasible at reasonable cost, the most likely amount should be used. This Statement requires that a deferred outflow of resources associated with an ARO be measured at the amount of the corresponding liability upon initial measurement.

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(A Component Unit of the Commonwealth of Puerto Rico)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS (CONTINUED)

This Statement requires the current value of a government's AROs to be adjusted for the effects of general inflation or deflation at least annually. In addition, it requires a government to evaluate all relevant factors at least annually to determine whether the effects of one or more of the factors are expected to significantly change the estimated asset retirement outlays. A government should remeasure an ARO only when the result of the evaluation indicates there is a significant change in the estimated outlays. The deferred outflows of resources should be reduced and recognized as outflows of resources (for example, as an expense) in a systematic and rational manner over the estimated useful life of the tangible capital asset.

A government may have a minority share (less than 50 percent) of ownership interest in a jointly owned tangible capital asset in which a nongovernmental entity is the majority owner and reports its ARO in accordance with the guidance of another recognized accounting standards setter. Additionally, a government may have a minority share of ownership interest in a jointly owned tangible capital asset in which no joint owner has a majority ownership, and a nongovernmental joint owner that has operational responsibility for the jointly owned tangible capital asset reports the associated ARO in accordance with the guidance of another recognized accounting standards setter. In both situations, the government's minority share of an ARO should be reported using the measurement produced by the nongovernmental majority owner or the nongovernmental minority owner that has operational responsibility, without adjustment to conform to the liability measurement and recognition requirements of this Statement.

In some cases, governments are legally required to provide funding or other financial assurance for their performance of asset retirement activities. This Statement requires disclosure of how those funding and assurance requirements are being met by a government, as well as the amount of any assets restricted for payment of the government's AROs, if not separately displayed in the financial statements.

This Statement also requires disclosure of information about the nature of a government's AROs, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. If an ARO (or portions thereof) has been incurred by a government but is not yet recognized because it is not reasonably estimable, the government is required to disclose that fact and the reasons therefor. This Statement requires similar disclosures for a government's minority shares of AROs.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (FY 2018-2019). Earlier application is encouraged. As per GASB Statement No. 95 the effective date is postponed by additional one year.

- **GASB Statement No. 87, "Leases"**. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset.

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS (CONTINUED)

Under this Statement, a lessee is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

Definition of a Lease

A lease is defined as a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Any contract that meets this definition should be accounted for under the leases guidance, unless specifically excluded in this Statement.

Lease Term

The lease term is defined as the period during which a lessee has a noncancelable right to use an underlying asset, plus the following periods, if applicable:

1. Periods covered by a lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option
2. Periods covered by a lessee's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option
3. Periods covered by a lessor's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessor will exercise that option
4. Periods covered by a lessor's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessor will not exercise that option. A fiscal funding or cancellation clause should affect the lease term only when it is reasonably certain that the clause will be exercised.

Lessees and lessors should reassess the lease term only if one or more of the following occur:

1. The lessee or lessor elects to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would not exercise that option.
2. The lessee or lessor elects not to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would exercise that option.
3. An event specified in the lease contract that requires an extension or termination of the lease takes place.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

Short - Term Leases

A short-term lease is defined as a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Lessees and lessors should recognize short-term lease payments as outflows of resources or inflows of resources, respectively, based on the payment provisions of the lease contract.

Lessee Accounting

A lessee should recognize a lease liability and a lease asset at the commencement of the lease term, unless the lease is a short-term lease, or it transfers ownership of the underlying asset. The lease liability should be measured at the present value of payments expected to be made during the lease term (less any lease incentives), the lease liability, plus any payments made to the lessor at or before the commencement of the lease term and certain direct costs.

A lessee should reduce the lease liability as payments are made and recognize an outflow of resources (for example, expense) for interest on the liability. The lessee should amortize the lease asset in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset. The notes to financial statements should include a description of leasing arrangements, the amount of lease assets recognized, and a schedule of future lease payments to be made.

Lessor Accounting

A lessor should recognize a lease receivable and a deferred inflow of resources at the commencement of the lease term, with certain exceptions for leases of assets held as investments, certain regulated leases, short-term leases, and leases that transfer ownership of the underlying asset. A lessor should not derecognize the asset underlying the lease. The lease receivable should be measured at the present value of lease payments expected to be received during the lease term. The deferred inflow of resources should be measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relate to future periods.

A lessor should recognize interest revenue on the lease receivable and an inflow of resources (for example, revenue) from the deferred inflows of resources in a systematic and rational manner over the term of the lease. The notes to financial statements should include a description of leasing arrangements and the total amount of inflows of resources recognized from leases.

Contracts with Multiple Components and Contract Combinations

Generally, a government should account for the lease and nonlease components of a lease as separate contracts. If a lease involves multiple underlying assets, lessees and lessors in certain cases should account for each underlying asset as a separate lease contract. To allocate the contract price to different components, lessees and lessors should use contract prices for individual components as long as they do not appear to be unreasonable based on professional judgment, or use professional judgment to determine their best estimate if there are no stated prices or if stated prices appear to be unreasonable.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

If determining a best estimate is not practicable, multiple components in a lease contract should be accounted for as a single lease unit. Contracts that are entered into at or near the same time with the same counterparty and that meet certain criteria should be considered part of the same lease contract and should be evaluated in accordance with the guidance for contracts with multiple components.

Lease Modifications and Terminations

An amendment to a lease contract should be considered a lease modification, unless the lessee's right to use the underlying asset decreases, in which case it would be a partial or full lease termination. A lease termination should be accounted for by reducing the carrying values of the lease liability and lease asset by a lessee, or the lease receivable and deferred inflows of resources by the lessor, with any difference being recognized as a gain or loss. A lease modification that does not qualify as a separate lease should be accounted for by remeasuring the lease liability and adjusting the related lease asset by a lessee and remeasuring the lease receivable and adjusting the related deferred inflows of resources by a lessor.

Subleases and Leaseback Transactions

Subleases should be treated as transactions separate from the original lease. The original lessee that becomes the lessor in a sublease should account for the original lease and the sublease as separate transactions, as a lessee and lessor, respectively.

A transaction qualifies for sale-leaseback accounting only if it includes a sale. Otherwise, it is a borrowing. The sale and lease portions of a transaction should be accounted for as separate sale and lease transactions, except that any difference between the carrying value of the capital asset that was sold and the net proceeds from the sale should be reported as a deferred inflow of resources or a deferred outflow of resources and recognized over the term of the lease. A lease-leaseback transaction should be accounted for as a net transaction. The gross amounts of each portion of the transaction should be disclosed.

The requirements of this Statement are effective for reporting periods beginning after December 15, 2019 (FY 2020-2021). Earlier application is encouraged.

- **GASB Statement No. 88, "Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements"**. The primary objective of this Statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt.

This Statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specifies in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses.

For notes to financial statements related to debt, this Statement also requires that existing and additional information be provided for direct borrowings and direct placements of debt separately from other debts.

The requirements of this Statement will improve financial reporting by providing users of financial statements with essential information that currently is not consistently provided. In addition, information about resources to liquidate debt and the risk associated with changes in terms associated with debt will be disclosed. As a result, users will have better information to understand the effects of debt on a government's future resources flows.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (FY 2018-2019). Earlier application is encouraged.

The Authority has not yet determined the effect these statements will have on the basic financial statements.

- **GASB Statement No. 89, "Accounting for Interest Cost Incurred Before the end of a Construction"**. The objectives of this Statement are (1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) to simplify accounting for interest cost incurred before the end of a construction period.

This Statement establishes accounting requirements for interest cost incurred before the end of a construction period. Such interest cost includes all interest that previously was accounted for in accordance with the requirements of paragraphs 5-22 of Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements, which are superseded by this Statement. This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest cost incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund.

This Statement also reiterates that in financial statements prepared using the current financial resources measurement focus, interest cost incurred before the end of a construction period should be recognized as an expenditure on a basis consistent with governmental fund accounting principles.

The requirements of this Statement are effective for reporting periods beginning after December 15, 2019 (FY 2020-2021). Earlier application is encouraged. The requirement of this Statement should be applied prospectively.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

- **GASB Statement No. 90, "Majority Equity Interest - An Amendment of GASB Statements No. 14 and No. 61"**. The primary objectives of this Statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. It defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment (including permanent and term endowments) or permanent fund. Those governments and funds should measure the majority equity interest at fair value.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (FY 2018-2019). Earlier application is encouraged.

The Authority has not yet determined the effect these statements will have on the basic financial statements.

- **GASB Statement No. 91, "Conduit Debt Obligations"**. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation establishing that a conduit debt obligation is not a liability of the issuer, establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations, and improving required note disclosures.

A conduit debt obligation is defined as a debt instrument having all of the following characteristics:

1. There are at least three parties involved: (1) an issuer. (2) a third-party obligor, and (3) a debt holder or a debt trustee.
2. The issuer and the third-party obligor are not within the same financial reporting entity.
3. The debt obligation is not a parity bond of the issuer, nor is it cross-collateralized with other debt of the issuer.
4. The third-party obligor or its agent, not the issuer, ultimately receives the proceeds from the debt issuance.
5. The third-party obligor, not the issuer, is primarily obligated for the payment of all amounts associated with the debt obligation (debt service payments).

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

All conduit debt obligations involve the issuer making a limited commitment. Some issuers extend additional commitments or voluntary commitments to support debt service in the event the third party is, or will be, unable to do so.

An issuer should not recognize a conduit debt obligation as a liability. However, an issuer should recognize a liability associated with an additional commitment or a voluntary commitment to support debt service if certain recognition criteria are met. As long as a conduit debt obligation is outstanding, an issuer that has made an additional commitment should evaluate at least annually whether those criteria are met. An issuer that has made only a limited commitment should evaluate whether those criteria are met when an event occurs that causes the issuer to reevaluate its willingness or ability to support the obligor's debt service through a voluntarily commitment.

This Statement also addresses arrangements—often characterized as leases—that are associated with conduit debt obligations. In those arrangements, capital assets are constructed or acquired with the proceeds of a conduit debt obligation and used by third-party obligors in the course of their activities. Payments from third-party obligors are intended to cover and coincide with debt service payments. During those arrangement, issuers retain the titles to the capital assets. Those titles may or may not pass to the obligors at the end of the arrangements.

Issuers should not report those arrangements as leases, not should they recognize a liability for the related conduit debt obligations or a receivable for the payments related to those arrangements. In addition, the following provisions apply:

1. If the title passes to the third-party obligor at the end of the arrangement, an issuer should not recognize a capital asset.
2. If the title does not pass to the third-party obligor and third party has exclusive use of the entire capital asset during the arrangement, the issuer should not recognize a capital asset until the arrangement ends.
3. If the title does not pass to the third-party obligor and the third party has exclusive use of only portions of the capital asset during the arrangement, the issuer, at the inception of the arrangement, should recognize the entire capital asset and a deferred inflows of resources. The deferred inflow of resources should be reduced, and an inflow recognized, in a systematic and rational manner over the term of the arrangement.

This Statement requires issuers to disclose general information about their conduit debt obligations, organized by type of commitment, including the aggregate outstanding principal amount of the issuers' conduit debt obligations and a description of each type of commitment. Issuers that recognize liabilities related to supporting the debt service of conduit debt obligations also should disclose information about the amount recognized and how the liabilities changed during the reporting period.

The requirements of this Statement are effective for reporting periods beginning after December 15, 2020 (FY 2021-2022). Early application is encouraged. As per GASB Statement No. 95 the effective date is postponed by additional one year.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

- **GASB Statement No. 92, "Omnibus 2020"**. The objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the following:
 1. The requirements related to the effective date of Statement 87 and Implementation Guide 2019-3, reinsurance recoveries, and terminology used to refer to derivative instruments are effective upon issuance. As per GASB Statement No. 95 the effective date is postponed by additional 18 months.
 2. Reporting of intra-entity transfers of assets between a primary government employer and a component unit defined benefit pension plan or defined benefit other postemployment benefit (OPEB) plan are effective for fiscal years beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 3. The applicability of Statements 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, as amended, and No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended, to reporting assets accumulated for postemployment benefits are effective for fiscal years beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 4. The applicability of certain requirements of Statement No. 84, Fiduciary Activities, to postemployment benefit arrangements and those related to nonrecurring fair value measurements of assets or liabilities are effective for reporting periods beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 5. The requirements related to the measurement of liabilities (and assets, if any) associated with AROs in a government acquisition are effective for government acquisitions occurring in reporting periods beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 6. Reporting by public entity risk pools for amounts that are recoverable from reinsurers or excess insurers are effective for reporting periods beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 7. Reference to nonrecurring fair value measurements of assets or liabilities in authoritative literature are effective for reporting periods beginning after June 15, 2020. As per GASB Statement No. 95 the effective date is postponed by additional one year.
 8. Terminology used to refer to derivative instruments are effective for reporting periods beginning after June 15, 2020.

As per GASB Statement No. 95 the effective date is postponed by additional one year.

- **GASB Statement No. 93, "Replacement of Interbank Offered Rates"**. Some governments have entered into agreements in which variable payments made or received depend on an interbank offered rate (IBOR)—most notably, the London Interbank Offered Rate (LIBOR). As a result of global reference rate reform, LIBOR is expected to cease to exist in its current form at the end of 2021,

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

prompting governments to amend or replace financial instruments for the purpose of replacing LIBOR with other reference rates, by either changing the reference rate or adding or changing fallback provisions related to the reference rate.

Statement No. 53, Accounting and Financial Reporting for Derivative Instruments, as amended, requires a government to terminate hedge accounting when it renegotiates or amends a critical term of a hedging derivative instrument, such as the reference rate of a hedging derivative instrument's variable payment. In addition, in accordance with Statement No. 87, Leases, as amended, replacement of the rate on which variable payments depend in a lease contract would require a government to apply the provisions for lease modifications, including remeasurement of the lease liability or lease receivable.

The objective of this Statement is to address those and other accounting and financial reporting implications that result from the replacement of an IBOR. This Statement achieves that objective by:

1. Providing exceptions for certain hedging derivative instruments to the hedge accounting termination provisions when an IBOR is replaced as the reference rate of the hedging derivative instrument's variable payment
2. Clarifying the hedge accounting termination provisions when a hedged item is amended to replace the reference rate
3. Clarifying that the uncertainty related to the continued availability of IBORs does not, by itself, affect the assessment of whether the occurrence of a hedged expected transaction is probable
4. Removing LIBOR as an appropriate benchmark interest rate for the qualitative evaluation of the effectiveness of an interest rate swap
5. Identifying a Secured Overnight Financing Rate and the Effective Federal Funds Rate as appropriate benchmark interest rates for the qualitative evaluation of the effectiveness of an interest rate swap
6. Clarifying the definition of reference rate, as it is used in Statement 53, as amended
7. Providing an exception to the lease modifications guidance in Statement 87, as amended, for certain lease contracts that are amended solely to replace an IBOR as the rate upon which variable payments depend.

The removal of LIBOR as an appropriate benchmark interest rate is effective for reporting periods ending after December 31, 2021. All other requirements of this Statement are effective for reporting periods beginning after June 15, 2020. Earlier application is encouraged. As per GASB Statement No. 95 the effective date is postponed by additional one year.

- **GASB Statement No. 94, "Public-Private and Public -Public Partnerships and Availability Payment Arrangements"**. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements (PPPs). As used in this Statement, a PPP is an arrangement in which a government (the transferor) contracts with an operator (a governmental or nongovernmental entity) to provide public services by conveying control of the right to operate or use a nonfinancial asset, such as infrastructure or other capital asset (the underlying PPP asset), for a period of time in an exchange or exchange-like transaction.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

Some PPPs meet the definition of a service concession arrangement (SCA), which the Board defines in this Statement as a PPP in which (1) the operator collects and is compensated by fees from third parties; (2) the transferor determines or has the ability to modify or approve which services the operator is required to provide, to whom the operator is required to provide the services, and the prices or rates that can be charged for the services; and (3) the transferor is entitled to significant residual interest in the service utility of the underlying PPP asset at the end of the arrangement.

This Statement also provides guidance for accounting and financial reporting for availability payment arrangements (APAs). As defined in this Statement, an APA is an arrangement in which a government compensates an operator for services that may include designing, constructing, financing, maintaining, or operating an underlying nonfinancial asset for a period of time in an exchange or exchange-like transaction.

PPPS

This Statement requires that PPPs that meet the definition of a lease apply the guidance in Statement No. 87, Leases, as amended, if existing assets of the transferor that are not required to be improved by the operator as part of the PPP arrangement are the only underlying PPP assets and the PPP does not meet the definition of an SCA. This Statement provides accounting and financial reporting requirements for all other PPPs: those that either (1) meet the definition of an SCA or (2) are not within the scope of Statement 87, as amended (as clarified by this Statement). The PPP term is defined as the period during which an operator has a noncancelable right to use an underlying PPP asset, plus, if applicable, certain periods if it is reasonably certain, based on all relevant factors, that the transferor or the operator either will exercise an option to extend the PPP or will not exercise an option to terminate the PPP.

A transferor generally should recognize an underlying PPP asset as an asset in financial statements prepared using the economic resources measurement focus. However, in the case of an underlying PPP asset that is not owned by the transferor or is not the underlying asset of an SCA, a transferor should recognize a receivable measured based on the operator's estimated carrying value of the underlying PPP asset as of the expected date of the transfer in ownership. In addition, a transferor should recognize a receivable for installment payments, if any, to be received from the operator in relation to the PPP. Measurement of a receivable for installment payments should be at the present value of the payments expected to be received during the PPP term. A transferor also should recognize a deferred inflow of resources for the consideration received or to be received by the transferor as part of the PPP. Revenue should be recognized by a transferor in a systematic and rational manner over the PPP term.

This Statement requires a transferor to recognize a receivable for installment payments and a deferred inflow of resources to account for a PPP in financial statements prepared using the current financial resources measurement focus. Governmental fund revenue would be recognized in a systematic and rational manner over the PPP term.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

This Statement also provides specific guidance in financial statements prepared using the economic resources measurement focus for a government that is an operator in a PPP that either (1) meets the definition of an SCA or (2) is not within the scope of Statement 87, as amended (as clarified in this Statement). An operator should report an intangible right-to-use asset related to an underlying PPP asset that either is owned by the transferor or is the underlying asset of an SCA. Measurement of the right-to-use asset should be the amount of consideration to be provided to the transferor, plus any payments made to the transferor at or before the commencement of the PPP term, and certain direct costs. For an underlying PPP asset that is not owned by the transferor and is not the underlying asset of an SCA, an operator should recognize a liability measured based on the estimated carrying value of the underlying PPP asset as of the expected date of the transfer in ownership. In addition, an operator should recognize a liability for installment payments, if any, to be made to the transferor in relation to the PPP. Measurement of a liability for installment payments should be at the present value of the payments expected to be made during the PPP term. An operator also should recognize a deferred outflow of resources for the consideration provided or to be provided to the transferor as part of the PPP. Expense should be recognized by an operator in a systematic and rational manner over the PPP term.

This Statement also requires a government to account for PPP and non-PPP components of a PPP as separate contracts. If a PPP involves multiple underlying assets, a transferor and an operator in certain cases should account for each underlying PPP asset as a separate PPP. To allocate the contract price to different components, a transferor and an operator should use contract prices for individual components as long as they do not appear to be unreasonable based on professional judgment or use professional judgment to determine their best estimate if there are no stated prices or if stated prices appear to be unreasonable. If determining the best estimate is not practicable, multiple components in a PPP should be accounted for as a single PPP.

This Statement also requires an amendment to a PPP to be considered a PPP modification, unless the operator's right to use the underlying PPP asset decreases, in which case it should be considered a partial or full PPP termination. A PPP termination should be accounted for by a transferor by reducing, as applicable, any receivable for installment payments or any receivable related to the transfer of ownership of the underlying PPP asset and by reducing the related deferred inflow of resources. An operator should account for a termination by reducing the carrying value of the right-to-use asset and, as applicable, any liability for installment payments or liability to transfer ownership of the underlying PPP asset. A PPP modification that does not qualify as a separate PPP should be accounted for by remeasuring PPP assets and liabilities.

APAS

An APA that is related to designing, constructing, and financing a nonfinancial asset in which ownership of the asset transfers by the end of the contract should be accounted for by a government as a financed purchase of the underlying nonfinancial asset. This Statement requires a government that engaged in an APA that contains multiple components to recognize each component as a separate arrangement. An APA that is related to operating or maintaining a nonfinancial asset should be reported by a government as an outflow of resources in the period to which payments relate.

PUERTO RICO LAND AUTHORITY
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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

The requirements of this Statement are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter. Earlier application is encouraged. As per GASB Statement No. 95 the effective date is postponed by additional one year.

- **GASB Statement No. 95, "Postponement of the Effective Dates of Certain Authoritative Guidance"**. The primary objective of this Statement is to provide temporary relief to governments and other stakeholders in light of the COVID-19 pandemic. That objective is accomplished by postponing the effective dates of certain provisions in Statements and Implementation Guides that first became effective or are scheduled to become effective for periods beginning after June 15, 2018, and later.

The effective dates of certain provisions contained in the following pronouncements are postponed by one year:

1. Statement No. 83, Certain Asset Retirement Obligations,
2. Statement No. 84, Fiduciary Activities,
3. Statement No. 88, Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements,
4. Statement No. 89, Accounting for Interest Cost Incurred before the End of a Construction Period,
5. Statement No. 90, Majority Equity Interests,
6. Statement No. 91, Conduit Debt Obligations,
7. Statement No. 92, Omnibus 2020,
8. Statement No. 93, Replacement of Interbank Offered Rates,
9. Implementation Guide No. 2017-3, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (and Certain Issues Related to OPEB Plan reporting),
10. Implementation Guide No. 2018-1, Implementation Guidance Update - 2018,
11. Implementation Guide No. 2019-1, Implementation Guidance Update - 2019, and
12. Implementation guide No. 2019-2, Fiduciary Activities.

The effective dates of the following pronouncements are postponed by 18 months:

1. Statement No. 87, Leases, and
2. Implementation Guide No. 2019-3, Leases.

Earlier application of the provisions addressed in this Statement is encouraged and is permitted to the extent specified in each pronouncement as originally issued.

The requirement of this Statement are effective immediately.

- **GASB Statement No. 96, "Subscription-Based Information Technology Arrangements"**. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset -and a corresponding subscription liability; (3) provides the capitalization

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. To the extent relevant, the standards for SBITAs are based on the standards established in Statement No. 87, *Leases*, as amended.

A SBITA is defined as a contract that conveys control of the right to use another party's (a SBITA vendor's) information technology (IT) software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a period of time in an exchange or exchange-like transaction.

The subscription term includes the period during which a government has a noncancelable right to use the underlying IT assets. The subscription term also includes periods covered by an option to extend (if it is reasonably certain that the government or SBITA vendor will exercise that option) or to terminate (if it is reasonably certain that the government or SBITA vendor will *not* exercise that option).

Under this Statement, a government generally should recognize a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability. A government should recognize the subscription liability at the commencement of the subscription term, which is when the subscription asset is placed into service. The subscription liability should be initially measured at the present value of subscription payments expected to be made during the subscription term. Future subscription payments should be discounted using the interest rate the SBITA vendor charges the government, which may be implicit, or the government's incremental borrowing rate if the interest rate is not readily determinable. A government should recognize amortization of the discount on the subscription liability as an outflow of resources (for example, interest expense) in a subsequent financial reporting periods.

The subscription asset should be initially measured as the sum of (1) the initial subscription liability amount, (2) payments made to the SBITA vendor before commencement of the subscription term, and (3) capitalizable implementation costs, less any incentives received from the SBITA vendor at or before commencement of the subscription term. A government should recognize amortization of the subscription asset as an outflow of resources over the subscription term.

Activities associated with a SBITA, other than making subscription payments, should be grouped into the following three stages, and their costs should be accounted for accordingly:

1. Preliminary Project Stage, including activities such as evaluating alternatives, determining needed technology, and selecting a SBITA vendor. Outlays in this stage should be expensed as incurred.
2. Initial Implementation Stage, including all ancillary charges necessary to place the subscription asset into service. Outlays in this stage generally should be capitalized as an addition to the subscription asset.
3. Operation and Additional Implementation Stage, including activities such as subsequent implementation activities, maintenance, and other activities for a government's ongoing operations related to a SBITA. Outlays in this stage should be expensed as incurred unless they meet specific capitalization criteria.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

In classifying certain outlays into the appropriate stage, the nature of the activity should be the determining factor. Training costs should be expensed as incurred, regardless of the state in which they are incurred.

If a SBITA contract contains multiple components, a government should account for each component as a separate SBITA or no subscription component and allocate the contract price to the different components. If it is not practicable to determine a best estimate for price allocation for some or all components in the contract, a government should account for those components as a single SBITA.

This Statement provides an exception for short-term SBITAs. Short-term SBITAs have a maximum possible term under the SBITA contract if 12 months (or less), including any options to extend, regardless of their probability of being exercised. Subscription payments for short-term SBITAs should be recognized as outflows of resources.

This Statement requires a government to disclose descriptive information about its SBITAs other than short-term SBITAs, such as the amount of the subscription asset, accumulated amortization, other payments not included in the measurement of a subscription liability, principal and interest requirements for the subscription liability, and other essential information.

The requirements of this Statement are effective for fiscal years beginning after June 15, 2022, and all reporting period thereafter. Earlier application is encouraged. Assets and liabilities resulting from SBITAs should be recognized and measured using the facts and circumstance that existed at the beginning of the fiscal year in which this Statement is implemented. Governments are permitted, but are not required, to include in the measurement of the subscription asset capitalizable outlays associated with the initial implementation stage and the operation and additional implementation stage incurred prior to the implementation of this Statement.

- **GASB Statement No. 97, "Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans - and amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32"**. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans, and employee benefit plans other than pension plans or OPEB plans (other employee benefit plans) as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(W) NEW ACCOUNTING STANDARDS (CONTINUED)

This Statement requires that for purposes of determining whether a primary government is financially accountable for a potential component unit, except for a potential component unit that is defined contribution pension plan, a defined contribution OPEB plan, or another employee benefit plan (for example, certain Section 457 plans), the absence of a governing board should be treated the same as the appointment of a voting majority of a governing board if the primary government performs the duties that a governing board typically would perform.

This Statement also requires that the financial burden criterion in paragraph 7 of Statement No. 84, Fiduciary Activities, be applicable to only defined benefit pension plans and defined benefit OPEB plans that are administered through trusts that meet the criteria in paragraph 3 of Statement No. a67, Financial Reporting for Pension Plans, or paragraph 3 of Statement No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, respectively

This Statement (1) requires that a Section 457 plan be classified as either a pension plan or another employee benefit plan depending on whether the plan meets the definition of a pension plan and (2) clarifies that Statement 84, as amended, should be applied to all arrangements organized under IRC Section 457 to determine whether those arrangements should be reported as fiduciary activities.

This Statement supersedes the remaining provisions of Statement No. 32, Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans, as amended, regarding investment valuation requirements for Section 457 plans. As a result, investments of all Section 457 plans should be measured as of the end of the plan's reporting period in all circumstances.

The requirements of this Statement that (1) exempt primary governments that perform the duties that a governing board typically performs from treating the absence of a governing board the same as the appointment of a voting majority of a governing board in determining whether they are financially accountable for defined contribution pension plans, defined contribution OPEB plans, or other employee benefit plans and (2) limit the applicability of the financial burden criterion in paragraph 7 of Statement 84 to defined benefit pension plans and defined benefit OPEB plans that are administered through trusts that meet the criteria in paragraph 3 of Statement 67 or paragraph 3 of Statement 74, respectively, are effective immediately.

The requirements of this Statement that are related to the accounting and financial reporting for Section 457 plans are effective for fiscal years beginning after June 15, 2021. For purposes of determining whether a primary government is financially accountable for a potential component unit, the requirements of this Statement that provide that for all other arrangements, the absence of a governing board be treated the same as the appointment of a voting majority of a governing board if the primary government performs the duties that a governing board typically would perform, are effective for reporting periods beginning after June 15, 2021. Earlier application of those requirements is encouraged and permitted by requirement as specified within this Statement.

The Board considered the effective dates for the requirements of this Statement in light of the COVID-19 pandemic and in concert with Statement No. 95, Postponement of the Effective Dates of Certain Authoritative Guidance.

The Authority has not yet determined the effect these statements will have on the Authority's basic financial statements.

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NOTE 2 - CASH AND CASH EQUIVALENTS

The Authority is restricted, by law, to deposit funds only in institutions approved by the Puerto Rico Treasury Department (from now on PRTD), and such deposits are required to be maintained in separate accounts in the Authority's name.

Under the laws and regulations of the Government, public funds deposited by the Authority in commercial banks must be fully collateralized for the amounts deposited in excess of the Federal Deposit Insurance Corporation (from now on FDIC) coverage. All securities pledged as collateral are held by agents designated by the Government's Secretary of the PRTD, but not in the Authority's name.

Credit Risk

This is the risk that an issuer or other counterpart to an investment will not fulfill its obligations. As of June 30, 2018, the Authority has invested only in cash in commercial banks approximately \$14.5 millions which are insured by the FDIC, generally up to a maximum of \$250,000. As mentioned before, public funds deposited by the Authority in commercial banks must be fully collateralized for the amounts deposited in excess of the FDIC coverage. Also, all securities pledged as collateral are held by the Secretary of the PRTD of the Commonwealth. Funds deposited with the Economic Development Bank for Puerto Rico (from now on "EDB"), a component unit of the Commonwealth, are not covered by this Commonwealth requirement. Therefore, the Authority's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Authority's deposits is considered low as of June 30, 2018.

Deposits placed with government banks include certificates of deposits, issued by EDB, amounting to approximately \$2.1 millions. These deposits are unsecured and uncollateralized. However, no losses related to defaults by EDB on deposit transactions have been incurred by the Authority through June 30, 2018.

Impairment Loss on Deposits with Governmental Development Bank of Puerto Rico (GDB)

The Commonwealth and the GDB face significant uncertainties, including liquidity risks, which is the risk of not having sufficient liquid financial resources to meet their obligations when they come due. Pursuant to enacted legislation, the Governor of the Commonwealth ordered the suspension of loan disbursements by GDB, imposed restrictions on the withdrawal and transfer of deposits from GDB, and imposed a moratorium on debt obligations of GDB, among other measures.

As a result of the reductions in liquidity experienced subsequent to June 30, 2014, GDB took a number of liquidity enhancing and conservation measures, and explored the sale of assets and other alternatives to address its liquidity needs. In light of GDB's significant debt service obligations during year 2016, these measures, however, are not expected to be sufficient to maintain GDB's operations in the ordinary course absent the completion of a capital market transaction, a restructuring of GDB's debt, and the payment by the Commonwealth of debt service on GDB's public sector loans payable from annual appropriations. As a result of the non-payment by the Commonwealth of the appropriation to GDB and GDB's inability to restructure its debt in light of the broader crisis faced by the Commonwealth, GDB was not in a position to pay principal on its debt obligations due on May 1, 2016 and continue operations in the ordinary course.

Due to the conditions and events described above, substantial doubt exists as to the GDB's ability to continue as a going concern.

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NOTE 2 - CASH AND CASH EQUIVALENTS (CONTINUED)

On October 18, 2016, the Secretary of the Treasury Department (from now on "the Department") of the Commonwealth issued its Circular Letter 1300-08-17 confirming that there is substantial doubt that GDB may be able to continue operating as a going concern, and that GDB is currently without financial liquidity. Based on this information, the Secretary recommended to all component units and other entities with deposits at GDB to evaluate the possibility of recognizing an impairment loss. The Authority recorded an impairment loss on all bank accounts and certificates of deposit with the GDB on 2016, and in 2018 recorded an additional impairment of \$811,147 for the remaining of the FIDA accounts with GDB. The Authority does not has any cash balances as of June 30, 2018 with GDB. See also Note 21 (a) on subsequent events, regarding the Restructuring Support Agreement (the RSA) entered between the Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA) and GDB, with a significant portion of the GDB's creditors, and the financial restructuring of the GDB pursuant to a Qualifying Modification under Title VI of PROMESA (the "Qualifying Modification").

Interest Rate Risk

This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Authority manages its exposure to declines in fair values by: (1) not including debt or equity investments in its investments portfolio at June 30, 2018, (2) limiting the weighted average maturity of its investments in certificates of deposit to periods of three months or less, and (3) keeping most of its banks deposits and certificates of deposit in interest bearing accounts generating interests at prevailing market rates. Therefore, as of June 30, 2018, the interest risk associated with the Authority's cash and cash equivalent is considered low.

Foreign Exchange Risk

This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Authority, the Authority is prevented from investing in foreign securities or any other types of investments for which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Authority's deposits is considered low as of June 30, 2018.

NOTE 3 - RESTRICTED CASH - PUERTO RICO LAND AUTHORITY

The Authority has as restricted \$912,212 of escrow accounts related to deposits of land sales. As of June 30, 2018, the Authority maintains unused funds amounted to \$1,338,634 as restricted cash from such sources.

NOTE 4 - INVESTMENTS IN PRIVATELY - HELD ENTITIES

FIDA

FIDA is authorized by law to invest in private entities which are dedicated to agricultural activities in Puerto Rico. The activity of such investments during the year ended June 30, 2018 is summarized below:

Balance, July 1, 2017	\$ 5,660,363
Decrease in Investments	<u>(1,714,495)</u>
Balance, June 30, 2018	<u>\$ 3,945,868</u>

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NOTE 4 - INVESTMENTS IN PRIVATELY - HELD ENTITIES (CONTINUED)

The investments are in convertible preferred stock. Under the terms of the investment contracts FIDA will receive the investment par value plus any accrued and unpaid dividends plus a premium depending on the year the stocks are redeemed as defined in investment contracts. Generally, the redemption premiums range from 2.5% to 30%.

During each year, the Authority's management evaluates the recoverability of the investments and records a valuation allowance for investments which are deemed as doubtful of realization. As of June 30, 2018, the balance of the investments is net of an allowance of \$4,784,730 for investments considered doubtful of realization.

NOTE 5 - RENT RECEIVABLE

Puerto Rico Land Authority

As of June 30, 2018, the Authority's rent receivable was as follows:

Rent and Other Receivables From Commonwealth Agencies and Municipalities	\$ 2,519,677
Rent and Land Leases From Third Parties	<u>17,643,805</u>
	20,163,482
Less Allowance for Doubtful Accounts	<u>(15,673,696)</u>
Net Rent Receivable	<u>\$ 4,489,786</u>

The Authority has a policy of including in the allowance for doubtful accounts all balances over one year old, except for certain balances, principally with governmental entities, that the Authority's management believes will be collectible.

NOTE 6 - NOTES AND INTERESTS RECEIVABLE

As of June 30, 2018, the Authority's notes and interests receivable were as follows:

Puerto Rico Land Authority:	
Family Farms Program	\$ <u>2,166,249</u>
FIDA:	
Private Entities	\$ 17,117,590
Governmental Entities	<u>3,026,807</u>
	<u>20,144,397</u>
Total	<u>\$ 22,310,646</u>

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NOTE 6 - NOTES AND INTERESTS RECEIVABLE (CONTINUED)

Family Farms Program

The Family Farms Program (from now on "the Program") was the main program of the Corporation for Rural Development (from now on "CDR"), a component unit of the DA of the Commonwealth. The Program was created for the purpose of stimulating the use of agricultural land by individuals who meet certain requirements. The land, transferred to qualified individuals under the program, is granted in usufruct. The usufructuary is under obligation to use the land for agricultural purposes only.

The value of the usufruct is the market value of the land and will be paid by the usufructuary over a period of 40 years, plus annual interest of 3% on the unpaid balance. In case the usufructuary does not comply with the payment requirements or with other conditions specified in the program, the usufruct is considered terminated.

During 2010, the Legislature of the Commonwealth approved Reorganization Plan No. 4 of the DA ("the Reorganization Plan"). Under the Reorganization Plan, the program was transferred from CDR to the Authority, which assumed all responsibilities and obligations under the program. The Reorganization Plan required CDR to transfer to the Authority all notes receivable and titles of all agricultural land under the Program.

As the result, during the year ended June 30, 2011, the Authority recorded notes receivables in the amount of \$3,722,000 under the program, which consisted of total notes receivable received from CDR of \$11,333,000, net of an allowance of, for notes receivable considered doubtful of collection, in the amount of \$7,611,000.

As of June 30, 2018, notes receivable outstanding balance of \$8,904,558 is presented net of an allowance for doubtful notes of \$6,738,309, for \$2,166,249. In addition, the Authority has not recorded the cost of any land available under the program or the land that should be recorded for terminated usufruct, as explained above.

FIDA

FIDA, as permitted by law, has entered into line of credit agreements with certain governmental entities and private agricultural businesses. The outstanding balances are unsecured and bear interest at rates ranging from 5% to 9% for governmental entities and from 7% to 10% for private agricultural businesses.

The outstanding balance of \$25,222,334\$ as of June 30, 2018, is presented net of an allowance for doubtful notes of \$5,077,937, for \$20,144,397.

During the year ended June 30, 2018, interest income recognized on notes receivable from governmental entities amounted to approximately \$144,938, included as part of interest income in operating revenues in the accompanying statement of revenues, expenses and changes in net position. Also, as of June 30, 2018, FIDA has a note receivable from a governmental entity with an outstanding balance of approximately \$2,405,141, for which no interest charged has been approved by FIDA's Board of Directors.

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NOTE 7 - CAPITAL ASSETS

Puerto Rico Land Authority

Capital assets consisted of the following:

<u>Description</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Adjustments/ Retirements</u>	<u>Ending Balance</u>
Capital Assets Not Being Depreciated:				
Land	\$ 86,515,201	\$ 12,474	\$ 988,726	\$ 87,516,401
Construction in Progress	<u>1,669,531</u>	<u>9,642</u>	<u>(1,050,707)</u>	<u>628,466</u>
	<u>88,184,732</u>	<u>22,116</u>	<u>(61,981)</u>	<u>88,144,867</u>
Capital Assets Being Depreciated:				
Building and Improvements	3,718,990	-	-	3,718,990
Infrastructure	14,892,347	-	2,497	14,894,844
Industrial Equipment	1,520,289	-	-	1,520,289
Machinery and Equipment	5,522,105	255,860	(279,163)	5,498,802
Vehicles	704,011	-	-	704,011
Furniture and Fixtures	<u>1,794,758</u>	<u>13,494</u>	<u>126,159</u>	<u>1,934,411</u>
	28,152,500	269,354	(150,507)	28,271,347
Less: Accumulated Depreciation	<u>(22,127,865)</u>	<u>(574,251)</u>	<u>178,904</u>	<u>(22,523,212)</u>
	<u>6,024,635</u>	<u>(304,897)</u>	<u>28,397</u>	<u>5,748,135</u>
Total Capital Assets, Net	<u>\$ 94,209,367</u>	<u>\$ (282,781)</u>	<u>\$ (33,584)</u>	<u>\$ 93,893,002</u>

From September 5, 2017 through September 7, 2017, Puerto Rico suffered the passing of Hurricane Irma, a Category 4 hurricane that severely affected the municipal islands and several municipalities located in the metro, north, east and south areas of the Island. It was declared a major disaster area by the President of the United States on September 10, 2017.

Just two weeks after Hurricane Irma, on September 20, 2017, Hurricane María hit Puerto Rico as a Category 4 hurricane, causing catastrophic damages to the infrastructure and the collapsing of the electric power grid and the telecommunications system of the entire Island. It was declared a major disaster area by the President of the United States on September 20, 2017. Many citizens lost their homes and the business sector suffered heavy losses due to infrastructure damages, looting during and after the hurricane, loss of inventory and the absence of electric power, which forced businesses to invest in power generators to operate, incurring in significant gasoline and diesel expenses. Several months after the incident, there were still many areas without energy and water service.

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NOTE 7 - CAPITAL ASSETS (CONTINUED)

Damages to offices, warehouses, other structures and equipment of the Authority, related to hurricane events, were estimated at approximately \$28.8 millions, as specified in a physical inspection detail prepared by FEMA. The report specifies the name of the facility or description of equipment, address or location, city located, a description of the damage, and amount of estimated damages. Although the Authority made arrangements to procure an insurance broker, the invoice for the insurance coverage was not paid previously to the hurricane events on September 2017, and therefore, no insurance coverage is available. Nevertheless, on January 2019, FEMA has provided assistance to the Authority in the amount of \$351,282, and agreed to provide additional further assistance for approximately \$266,065.

The Authority, as of basic financial statements report date, is in the process of tracing the individual property and equipment items in the physical inspection detail to their capital assets details, in order to dispose-off or adjust cost and accumulated depreciation related balances. Therefore, no adjustments to capital assets has been made in the accompanying basic financial statements for the year ended June 30, 2018.

Infrastructure Program

The infrastructure program is designed to improve water resource usage and fertilization of land dedicated to the production of fruits and vegetables, through the maintenance of risk pumps and other utilities. Currently, the majority of improvements made through the infrastructure funds are provided by the DA.

NOTE 8 - REAL ESTATE AND EQUIPMENT FOR FUTURE USE

By virtue of Act No. 189, described in Note 1(E), the Sugar Corporation of Puerto Rico and the Land Authority were authorized to transfer certain assets used in the production, marketing and selling of sugar to the sugarcane farmers (known as "colonos"). The Act imposed several restrictions upon the assets transferred to the sugarcane owners, in order to maintain the benefits of the Act. Because of the restrictions imposed by the Act and because of the infringement by the sugarcane growers of said restrictions, the assets were returned to the Corporation and the Land Authority. On September 2, 2004, the "Agroindustria Azucarera del Oeste, Inc." (known as "AGRASO") and Land Authority/Sugar Corporation agreed to return all assets, by virtue of Act. No. 189, in exchange of payments of certain obligations and release of debt owned to the Sugar Corporation.

The assets received have an estimated book value of \$4,090,000, detailed as follows:

Land	\$ 1,535,000
Buildings	873,000
Machinery and Equipment	<u>1,682,000</u>
Total	<u>\$ 4,090,000</u>

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NOTE 8 - REAL ESTATE AND EQUIPMENT FOR FUTURE USE (CONTINUED)

The Act established that in case of infringement, all assets transferred would be returned at cost or fair market value, whichever is lower. Due to significant adverse environmental damages, equipment becomes obsolete and unfit for industrial purposes, and a projection of future costs associated to clean up premises and legal actions involved, the Corporation considers this property as fully impaired, therefore, no value had been assigned in the accompanying financial statements. The Authority is trying to consolidate all impaired equipment and obsolete structures in sugar mills to convert into disposal material to be sold. As of financial statements date, the Authority cannot determine future losses or gains related to these impaired assets.

NOTE 9 - DEPOSITS ON SALE OF LAND

The Authority is authorized by the Land Law of Puerto Rico to sell surplus land and properties that have no agricultural use to other governmental entities and individuals. The liability for deposits reflected in the accompanying statement of net position, as deferred inflows of resources, represents amounts received in connection with land transactions in process. It also includes legal foreclosures and expropriations cases not finally executed by court.

NOTE 10 - NOTES PAYABLE

Notes payable as of June 30, 2018 consisted of the following:

Puerto Rico Land Authority:

Participation in Bonds Payable Issued by
 Puerto Rico Finance Corporation:

\$ 17,051,349

On December 27, 2001, the Authority entered into a loan agreement ("the Note") with the GDB to refinance certain debts, as authorized by Act No. 164 of December 17, 2001. The Puerto Rico Public Finance Corporation (from now on "PFC") acquired and restructured the Note through the issuance of its Commonwealth appropriations bonds ("PFC Bonds"). The PFC Bonds were issued under a trust indenture, whereby the PFC pledged and sold the Note, along with other notes, under Act No. 164, to certain trustees and created a first lien on the revenues of the notes sold.

During June 2004, the PFC issued PFC 2004 series A and B bonds, and advance refunded a portion of certain of its outstanding Commonwealth appropriation bonds issued in 2001 under Act No. 164. The Authority recognized a mirror effect of this advance refunding by the PFC in its own notes payable, in proportion to the portion of the Authority's notes payable included in the PFC refunding. The aggregate debt service requirements of the notes will be funded with annual appropriations from the Commonwealth.

During the fiscal year ended June 30, 2012, PFC issued PFC 2011 Series A and B and PFC 2012 Series A bonds, and refunded a portion of certain of its outstanding Commonwealth appropriation bonds issued in 2004 and before, under Act No.164, including \$15,099,000 of the Authority corresponding portion of the debt. The Authority recognized a mirror effect of these current refunding by the PFC in its own notes payable, in proportion to the portion of the Authority's notes payable included in the PFC refunding.

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NOTE 10 - NOTES PAYABLE (CONTINUED)

The Authority recorded a due from Commonwealth amounting to \$338,849 as of June 30, 2014, for an advance made to the bond trustee to cover future debt service requirements of the refunded notes. The aggregate debt service requirements of the refunded notes in excess of the advance already made to the bond trustee will be funded with annual appropriations from the Commonwealth.

In December 2011, the Puerto Rico Sales Tax Financing Corporation (from now on "COFINA"), issued bonds, and a portion of the proceeds from such bond issuance was used to cancel certain appropriation bonds of the Commonwealth and its agencies, departments and certain component units, including \$8,355,950 of the Authority's notes payable to PFC. As a result of this bond defeasance, the Authority recognized a contribution from COFINA of \$8,555,495 and recognized a loss on extinguishments of debt of \$54,886 during the year ended June 30, 2012.

The notes outstanding balance as of June 30, 2018, was \$17,051,349 and matures throughout August 1, 2032. Interest on the unpaid principal amount of the Note is equal to the applicable percentage of the aggregate interest payable on the PFC Bonds. Applicable percentage is the percentage representing the proportion of the amount paid by the PFC on the PFC Bonds serviced by the Note to the aggregate amount paid by the PFC on all the PFC Bonds issued by the PFC under Act No. 164.

The activity of the notes payable, during the year ended June 30, 2018, was as follows:

	<u>Balance</u> <u>6/30/2017</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance</u> <u>6/30/2018</u>
Notes Payable	\$ <u>17,051,349</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>17,051,349</u>

The estimated repayment schedule of the note payable during the next years follows:

<u>Fiscal Years</u> <u>Ending</u> <u>June 30,</u>	<u>Principal</u>	<u>Interests</u>	<u>Totals</u>
2019	\$ 1,330,416	\$ 2,775,629	\$ 4,106,045
2020	437,017	892,906	1,329,923
2021	454,516	874,274	1,328,790
2022	473,330	853,972	1,327,302
2023	493,943	831,812	1,325,755
2024-2029	10,684,572	4,676,445	15,361,017
2030-2032	<u>3,177,555</u>	<u>177,171</u>	<u>3,354,726</u>
Total	\$ <u>17,051,349</u>	\$ <u>11,082,209</u>	\$ <u>28,133,558</u>

FIDA - Credit Line

FIDA had a non - revolving credit line with GDB. When issued, FIDA had a ceiling on the line of \$94 millions. Proceeds from this credit line were used by FIDA to fund investments in agricultural businesses, loans to farmers and contributions, as were permitted by laws and regulations. Repayments of principal and interests were made from the collection of coffee and sugar taxes allocated by the Commonwealth.

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NOTE 10 - NOTES PAYABLE (CONTINUED)

Nevertheless, the Authority has made no additional payments, of neither principal or interests, on the credit line since July 1, 2016. The credit line does not have a formal repayment schedule. Base rate on the credit line is the London Interbank Offered Rate or LIBOR, with a spread of 1.25%. The credit line matures on March 1, 2027.

GDB faced significant risks and uncertainties and it currently does not have (and is not expected to have) sufficient liquid financial resources to meet its obligations in full. Pursuant to enacted legislation and executive orders by two separate government administrations, GDB was ordered to suspend loan disbursements, to impose restrictions on the withdrawal and transfer of deposits from GDB and it is currently winding down in an orderly fashion under Title VI of PROMESA.

On November 29, 2018 through a Qualifying Modification under Title VI of PROMESA, an offset of this credit facility was made, by the amount of FIDA's deposits held at the GDB. FIDA has already recorded impairment losses, for the totality of the funds deposited in GDB, of \$12,000,000 as of June 30, 2016, and of \$11,661,192 as of June 30, 2017. The \$28,125,394 total outstanding amount of the credit line (\$27,674,032 plus accrued interests of \$451,361) was not completely offset. See Note 21 for further details of the offset of the credit facility transaction with GDB.

Outstanding interests payable related to this credit line amounted to \$451,361.

NOTE 11 - RELATED PARTY TRANSACTIONS

Intercompany transactions occurred during the fiscal year ended June 30, 2018 between Puerto Rico Land Authority and FIDA, because by request of FIDA, the Authority makes payments on behalf of FIDA and records the corresponding receivable or payable transaction, as applicable.

NOTE 12 - DUE TO OTHER GOVERNMENTAL ENTITIES

As of June 30, 2018 due to other governmental entities consisted of the following:

Municipal Revenues Collection Center (CRIM)	\$ 11,704,721
Puerto Rico Electric Power Authority	2,772,366
Retirement System Administration	6,827,271
Puerto Rico Aqueduct and Sewer Authority	389,901
Others	<u>51,512</u>
Total Due to Other Governmental Entities	<u>\$ 21,745,771</u>

NOTE 13 - DEFERRED OUTFLOWS AND INFLOW OF RESOURCES

Deferred outflows of resources and deferred inflows of resources are defined in GASB Concept Statement No. 4, "Elements of Financial Statements", as the acquisitions and consumption's of net assets by the government that is applicable to future periods. Pursuant to GASB Statement No. 63, "Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position," and GASB Statement No. 65, "Items Previously Reported as Assets and Liabilities," the Authority recognizes deferred outflows and inflows of resources.

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NOTE 13 - DEFERRED OUTFLOWS AND INFLOW OF RESOURCES (CONTINUED)

In addition to assets, the Statement of Net Position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then.

In addition to liabilities, the Statement of Net Position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

Based on this concept, the Authority reports the following as deferred outflows of resources and deferred inflows of resources:

- The deferred outflows of resources and deferred inflows of resources resulting from the implementation of GASB No. 68 and 75. Notes 14 and 15 presents additional information about the composition of these items, respectively.

NOTE 14 - PENSION PLAN

As described in Note 1(L), the Authority implemented GASB Statement No. 68, Accounting and Financial Reporting for Pension, during fiscal year 2017, and a new Required Supplementary Information schedules are included herein. Also, GASB Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date, an amendment to GASB No. 68", was implemented simultaneously with the provisions of GASB No. 68.

Description of the Plan

Prior to August 23, 2017, the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico (ERS) implemented a cost-sharing multi-employer defined benefit pension plan administered by the Puerto Rico Government Employees and Judiciary Retirement Systems Administration. Employees of the Municipality participate in the ERS. The ERS is a trust created by Act No. 447, approved on May 15, 1951, as amended (Act No. 447-1951) and began operation on January 1, 1952, at which date, contributions by employers and participating employees commenced. The ERS is a pension trust of the Commonwealth. All qualified permanent and probationary employees of the Commonwealth and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems are eligible to participate in the ERS.

As of June 30, 2015, there were 206 participating employers (73 Commonwealth agencies, 78 municipalities, and 55 public corporations, including the ERS). Membership is optional for the Governor, Government secretaries, head of public agencies, and instrumentalities, among others. The ERS, as a governmental retirement plan, is excluded from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

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NOTE 14 - PENSION PLAN (CONTINUED)

The employees of the House of Representatives are eligible to participate in the pension plan. Participation is optional for employees hired before January 1, 2000 and less than 55 years of age at the date of employment. No benefits are payable if the participant receives a refund of their accumulated contributions.

As of July 1, 2015, membership of the ERS consisted of the following:

Retirees and Beneficiaries Currently Receiving Benefits	108,035
Current Participating Employees - Defined Benefit	53,832
Current Participating Employees - System 2000 and Act No. 3	64,825
Disabled members, receiving benefits	<u>14,722</u>
 Total Membership	 <u><u>241,414</u></u>

Pension Benefits

Pension benefits provided to members of the System are established by Commonwealth law and may be amended only by the Legislature with the Governor's approval. Act No. 3-2013, in conjunction with other recent funding and design changes, provided for a comprehensive reform of the System. This summary details the provisions under Act No. 3-2013.

Certain provisions are different for the three groups of members who entered the ERS prior to July 1, 2013 as described below:

- Members of Act No. 447-1951 are generally those members hired before April 1, 1990 (Contributory, Defined Benefit Program)
- Members of Act No. 1 are generally those members hired on or after April 1, 1990 (Act No. 1-1990) and on or before December 31, 1999 (Contributory, Defined Benefit Program)
- Members of Act No. 305 are generally those members hired on or after January 1, 2000 and on or before June 30, 2013 (Define Contribution Hybrid Program). Each member has a no forfeitable right to the value of his/her account. Members have three options to invest their contributions. Investment income is credited to the member's account semiannually. The Commonwealth does not guarantee benefits at retirement age.

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 Defined Contribution Hybrid 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 programs will become part of the Defined Contribution Hybrid Program.

Each member has a no forfeitable right to the value of his/her account. Members have three options to invest their contributions. Investment income is credited to the member's account semiannually. The Commonwealth does not guarantee benefits retirement age.

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NOTE 14 - PENSION PLAN (CONTINUED)

The assets of the Define Benefit Program, the Defined Contribution Program and the Contributory Hybrid Program were pooled and invested by the ERS.

- a. **Retirement Annuity** - Plan members are eligible for a retirement annuity based on years of service, final average compensation and retirement age. Plan members are eligible for monthly benefit payments determined by the application of stipulated benefit ratios to the plan member's average compensation.
- b. **Average Compensation** - Is computed based on the highest 36 months of compensation recognized by the System. The annuity, for which a plan member is eligible, is limited to a minimum of \$400 per month and a maximum of 75% of the average compensation.
- c. **Merit Annuity** - Plan members are eligible for merit annuity with a minimum of 30 years or more of credited service. The annuity for which the plan member is eligible is limited to a minimum of 65% and a maximum of 75% of the average compensation.
- d. **Deferred Retirement Annuity** - A participating employee who ceases to be an employee of the Commonwealth after having accumulated a minimum of 10 years of credited service qualifies for retirement benefits provided his/her contributions to the System are not withdrawn until attainment of 58 years of age.
- e. **Coordinated Plan** - On this plan, the participating employee contributes a 5.775% of the monthly salary for the first \$550 and 8.275% for the excess over \$550. By the time the employee reaches 65 years old and begins to receive social security benefits, the pension benefits are reduced.
- f. **Non-Coordinated Plan** - On this plan, the participant employee contributes an 8.275% of the monthly salary and does not have any change on the pension benefits upon receiving social security benefits.
- g. **Reversionary Annuity** - A plan member, upon retirement, could elect to receive a reduced retirement annuity giving one or more benefit payments to his/her dependents. The life annuity payments would start after the death of the retiree for an amount not less the \$240 yearly or greater than the payments being received by the retiree.
- h. **Occupational Disability Annuity** - A participating employee, who as a direct result of the performance of his/her occupation is totally and permanently disabled, is eligible for a disability annuity of 50% of the compensation received at the time of the disability.
- i. **Non-Occupational Disability Annuity** - A participating employee totally and permanently disabled for causes not related to his/her occupation, and with no less than 10 years of credited service, is eligible for an annuity of 1.5% of the average compensation of the first 20 years of credited services increased by 2% for every additional year of credited service in excess of 20 years.
- j. **Death Benefits-Occupational** - The surviving spouse is eligible for an annuity equal to 50% of the participating employee's salary at the date of the death. Children are eligible for an annuity of \$10 per month for each child, minor or student, up to a maximum benefit per family of 100% of the participating employee's salary at the date of the death. If no spouse survives, or dies while receiving the annuity payments, each child, age 18 or under, is eligible to receive an annuity of \$20 per month up to the attainment of 18 years of age or the completion of his/her studies.
- k. **Death Benefits-Non-Occupational** - The beneficiary if eligible to receive the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of the death. Beneficiary with surviving spouse age 60 or over and child, age 18 or under, up to 50% (60%, if not covered under the Title II of the Social Security Act) of retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$1,000.

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NOTE 14 - PENSION PLAN (CONTINUED)

Other benefits granted by the Commonwealth to the System's retirees during fiscal years 2003 and 2007 included Christmas bonus, summer bonus, medication bonus and cost of living adjustment for pension benefits (COLA).

The Act No.1-1990 made certain amendments applicable to new participants joining the pension plan effective April 1, 1990. These changes consist principally of the establishment of contributions at 8.275% of their monthly gross salary, an increase in the retirement age to 65, a decrease in the annuity benefit to 1.5% of the average salary, as defined, and death benefits annuities from 50% to 40% of average salary, as defined, and the elimination of the Merit Annuity for participant who have completed 30 years of creditable service.

Adoption of Comprehensive Reform of Employees Retirement System

On April 4, 2013, the Governor of Puerto Rico signed into law Act No. 3 ("Act No. 3-2013"), which adopted a comprehensive reform of the Employees Retirement System of the Commonwealth (ERS System).

Act No. 3-2013, which is effective on July 1, 2013, provides the following:

- a. It freezes and grandfathers the benefits that have accrued through June 30, 2013 of those participants who are covered by the ERS System's defined benefit formula (those who joined the ERS System prior to January 1st, 2000, whose retirement benefits accrued at a rate of 1.5% or 2% per year of creditable service;
- b. It provides that, beginning on July 1st, 2013, the retirement benefits accruing on and after the Effective Date for defined benefit employees will be calculated based on a defined contribution formula, similar to the ERS System 2000 formula currently applicable to employees who joined the ERS System on or after January 1st, 2000, with all such benefits being paid in the form of a lifetime annuity rather than a lump sum payment (upon retirement). The employee will receive the benefits accrued through June 30, 2013 based on the defined benefit formula plus the contributions made by the employee after June 30, 2013;
- c. It provides that defined contribution benefits accrued pursuant to ERS System 2000 will also be paid in the form of a lifetime annuity rather than a lump sum payment;
- d. It eliminates the so called "merit pension" that provided to participants who joined the ERS System prior to April 1, 1990, after attaining 30 years of service, a retirement benefit of 65% (if less than 55 years of age) or 75% (if age 55 or greater) of the average salary earned during the highest 36 months of employment;
- e. It increases the retirement age for various groups as follows: (a) from 58 to age 61 for Act No. 447-1951 participants and: (b) from 60 to age 65 for active system 2000 participants;
- f. It increases the employee contributions to the ERS System from 8.275% to 10%;
- g. It eliminates or reduces various retirement benefits previously granted by special laws, including Christmas and summer bonus;

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NOTE 14 - PENSION PLAN (CONTINUED)

- h. It provides that, beginning on July 1st, 2013, the retirement benefits accruing on and after the Effective Date for defined benefit employees will be calculated based on a defined contribution formula, similar to the ERS System 2000 formula currently applicable to employees who joined the ERS System on or after January 1st, 2000, with all such benefits being paid in the form of a lifetime annuity rather than a lump sum payment (upon retirement). The employee will receive the benefits accrued through June 30, 2013 based on the defined benefit formula plus the contributions made by the employee after June 30, 2013;
- i. It provides that defined contribution benefits accrued pursuant to ERS System 2000 will also be paid in the form of a lifetime annuity rather than a lump sum payment;
- j. It eliminates the so called "merit pension" that provided to participants who joined the ERS System prior to April 1, 1990, after attaining 30 years of service, a retirement benefit of 65% (if less than 55 years of age) or 75% (if age 55 or greater) of the average salary earned during the highest 36 months of employment;
- k. It increases the retirement age for various groups as follows: (a) from 58 to age 61 for Act No. 447-1951 participants and: (b) from 60 to age 65 for active system 2000 participants;
- l. It increases the employee contributions to the ERS System from 8.275% to 10%;
- m. It eliminates or reduces various retirement benefits previously granted by special laws, including Christmas and summer bonus;
- n. It increases the minimum pension from \$400 to \$500 per month for current retirees, and
- o. It eliminates or modifies other benefits such as disability and survivor benefits.

Liquidity Risk and Uncertainties

ERS is a mature retirement system with a significant retiree population. Based on the statutory funding requirements, the annual benefit payments and administrative expenses paid by the ERS were significantly larger than the member and employer contributions made to the ERS. Thus, investment income must have had to be used to cover negative cash flow. If the increasing and additional contributions stipulated by law are not paid in full on an annual basis, the ERS will continue being rapidly defunded and gross assets will be exhausted. If measures are not taken to significantly increase the contributions, the ERS will become insolvent in fiscal year 2015. In addition, annual cash flow estimates for the foreseeable future are presently estimated to be insufficient to cover the ERS's obligations unless other measures are taken.

If the ERS's assets are exhausted it would be operating solely on a "pay-as-you-go" basis, which means that it would be unable to pay benefits that exceed the actual employer and employee contributions received (net of administrative and other expenses), unless the Government provides the funding required to meet the pay-as-you-go retirement benefits. Additionally, future employers' contributions have been pledged for the payment of debt service, further depletion of the ERS's assets could result in the inability to repay its bond obligations. Consequently, the ERS's funding requirements, together with the funding requirements of JRS and the Puerto Rico System of Annuities and Pensions for Teachers, could have a direct negative effect on the Government's General Funds, since the Government is the primary sponsor and is obligated to make contributions to fund each of the ERS.

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NOTE 14 - PENSION PLAN (CONTINUED)

The Government and the other participating employers have been facing several fiscal and economic challenges in recent years due, among other factors, to continued budget deficits, a prolonged economic recession, high unemployment, population decline, and high levels of debt and pension obligations. The widening of credit spreads for the Government's public-sector debt, the continued downgrading of the Government's credit ratings and those of many of its instrumentalities to noninvestment grade categories, and the lowered-than-projected revenues have put further stain on the Government liquidity and have affected its access to both the capital markets and private sources of financing, as well as the borrowing cost of any such funding.

If the Government's financial condition does not improve as a result of fiscal and budgetary measures it is taking, its ability to repay its obligations, including its regular employer contributions to the ERS and its additional contributions as provided by Act No. 32 of June 25, 2013 (Act No. 32-2013), for the upcoming years, may continue to be adversely affected, and could also affect the payment of benefits and the repayment of the ERS's bond payable.

To improve the liquidity and solvency of the ERS, the Government enacted Act No. 32-2013, as amended by Act No. 244-2014, which provides for incremental annual contributions (Additional Uniform Contribution) from the Government's General Fund, public corporations and municipalities beginning in fiscal year 2014 and up to the fiscal year 2033. The AUC determined for fiscal year 2014 was defined as \$120.0 million and subsequent annual amounts will be determined annually based on actuarial studies to be performed by the ERS's actuaries as necessary for the ERS's gross assets to remain above \$1.0 billion. An appropriation for such AUC of approximately \$98 million was included in the Government's budget for the fiscal year 2014. However, as a result of the Government's General Fund revenue shortfall, compared to budget, the Government made certain adjustments to the fiscal year 2014 budgetary appropriations following the "priority norms" for the disbursement of public funds that apply during any fiscal year in which the resources available to the Government are insufficient to cover the appropriations approved for such year. These adjustments included the reduction in full of the portion of the Act No. 32-2013 AUC by executive Order No. 29-2014.

For fiscal year 2015 and 2016, the certification of the AUC was not available at least 120 days before the commencement of the applicable fiscal year. ACT No. 32-2013, as amended, provides that in this situation, the AUC for fiscal year will be the AUC applicable for the preceding year. Thus, the AUC determined for fiscal years 2015 and 2016 was \$120 million.

Timely payment of the AUC is a critical component of the reform in order for the ERS to be able to make payments as they come due without depleting all its assets first. However, as a result of continued budget deficits in fiscal years 2014 and 2015, the Government and other participating employers have not been unable to make the AUC required in full for these fiscal years (other than \$34.4 million paid by such municipalities and public corporations for fiscal year 2014 and \$22.7 million paid by the Government and \$37.1 million paid by public corporations and municipalities for fiscal year 2015). In February 2016, the ERS's actuaries recalculated the AUC for fiscal year 2017 and subsequent years. Based on certain assumptions (which do not account for any fiscal adjustment that the Government may undertake to address its fiscal challenges), the projected AUC for fiscal year 2017 and subsequent years was approximately \$596.0 million (of which approximately \$370.0 million corresponds to the Government, to be funded from its General Fund, and the remaining portion corresponds to the participating public corporations and municipalities).

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NOTE 14 - PENSION PLAN (CONTINUED)

Pension Liabilities, Pension Expenses, and Deferred Outflows/Inflows of Resources Related to Pensions

1) Net Pension Liability

The Authority's Net Pension Liability for each plan program is measured as the proportionate share of the Net Pension Liability. The Net Pension Liability of each of the plan program was measured as of June 30, 2017, and the Total Pension Liability for each plan program used to calculate the Net Pension Liability was determined by an actuarial valuation as of June 30, 2017. The Authority's proportion of the Net Pension Liability was based on a projection of the Authority's long-term share of contributions to the pension plans program relative to the projected contributions of all participating employers, actuarially determined. As June 30, 2018, the Authority's used the proportional share of 0.171318%.

Proportion - June 30 2016	0.17078
Proportion - June 30, 2017	<u>0.17138</u>
Change - Increase	<u>0.00060</u>

As June 30, 2018, the Authority reported \$58,641,397 as Net Pension Liability for its proportionate shares of the Net Pension Liability of ERS, as follows:

	<u>Net Pension Liability</u>	<u>Total</u>	<u>Proportional Share</u> <u>(.17138%)</u>
Total Pension Liability	\$ 32,109,294,000		\$ 55,027,245
Fiduciary Net Position		<u>2,108,853,000</u>	<u>3,614,152</u>
Net Pension Liability		<u>\$ 34,218,147,000</u>	<u>\$ 58,641,397</u>
Plan's Fiduciary Net Pension (Deficit) of Total Pension Liability		-6.57%	-6.57%
Covered Payroll	\$ 3,344,197,000		\$ 5,728,609
Net Pension Liability as a % of Covered Payroll		1,023.21 %	1,023.66 %

2) Pension Expense

For the fiscal year ended June 30, 2018, the Authority recognized pension expense of \$4,776,229. Pension expense represents the change in the net pension liability during the measurement period, adjusted for actual contributions and the deferred recognition of changes in investment gain/loss, actuarial gain/loss, actuarial assumptions or method, and plan benefits.

3) Deferred Outflows/Inflow of Resources

As of June 30, 2018, the Authority reported Deferred Outflows of Resources and Deferred Inflows of Resources related to pensions from the following sources:

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NOTE 14 - PENSION PLAN (CONTINUED)

	<u>Deferred Outflows Of Resources</u>	<u>Deferred Inflows Of Resources</u>
Pension Contributions Subsequent to Measurement Date	\$ -	\$ -
Differences Between Actual and Expected Experience	39,616	1,037,820
Changes in Assumptions	7,666,012	5,968,292
Change in Employer's Proportion and Differences Between The Employer's Contributions and the Employer's Proportionate Share of Contributions	2,440,136	-
Net Differences Between Projected and Actual Earnings on Plan Investments	<u>3,006,543</u>	<u>342,542</u>
	<u>\$ 13,152,307</u>	<u>\$ 7,348,654</u>

Actuarial Methods and Assumptions

The census data collection date has changed from end-of-year to beginning-of-year. For this switchover year, the June 30, 2017 are based on projecting the System obligations determined as of the census data collection date of July 1, 2016 for one year, using roll-forward methods and assuming no liability gains or losses.

The actuarial valuation used the following actuarial assumptions:

Inflation Rate	Not applicable.
Municipal Bond Index	3.58%, based on Bond Buyer General Obligation 20 - Bond Municipal Bond Index
Salary increase	3.00% per year. No compensation increases are assumed until July 1, 2021, as a result of Act No. 3-2017, four year extension of Act No. 66-2014, and the current general economy.
Mortality	<u>Pre-Retirement Mortality</u> : for general employees not covered Under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on a generational basis. For members covered under Act 127, RP-2014 Employee Mortality Rates are assumed with blue collar adjustments for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on a generational basis. As generational tables, they reflect mortality improvements both before and after measurement date. 100% of deaths while in active service are assumed to be occupational for members covered under Act. No. 127.

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NOTE 14 - PENSION PLAN (CONTINUED)

Post-Retirement Healthy Mortality: Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994 Mortality Tables Males and 95% of the rates from UP-1994 Mortality Table Females, both projected from 1994 to 2010 using Scale AA. These base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

Post-Retirement Disabled Mortality: Rates which vary by gender are assumed for disabled retirees based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table Males and 115% of the rates from the UP-1994 Mortality Table Females, both projected from 1994 to 2010 using Scale AA. These base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after measurement date.

Most other demographic assumptions used in the June 30, 2017 valuation were based on the results of a 2009 actuarial experience study using data as of June 30, 2003, June 30, 2005 and June 30, 2007.

Long-Term Expected Rate of Return

The long-term expected rate of return on pension benefits investments was not applicable as of June 30, 2017. Net assets are negative as of June 30, 2017 and accordingly, it is not possible to determine a rate of return on net assets during the fiscal year. In addition, after June 30, 2017, due to the Pay-As-You-Go System by which the Government guarantees payment of pensions. The System assets were no longer necessary to generate investment returns to pay pension benefits. The approximate actual rate of return on gross assets was 8.74% as of June 30, 2017.

Before June 30, 2017, the pension plan's policy for allocation of invested assets has been established and may be amended by the System's Board of Trustees. Plan assets are managed on a total return basis with a long-term objective of achieving and maintaining a positive impact on the System's financial condition for the benefits provided through the pension programs. The following asset allocation policy as of June 30, 2017 was adopted by the System's Board of Trustees:

Asset Class	Target Allocation	Long-Term Expected Rate of Return
Domestic Equity	56%	N/A
International Equity	15%	N/A
Fixed Income	2%	N/A
Cash	1%	N/A
Total	100%	

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NOTE 14 - PENSION PLAN (CONTINUED)

In prior years, the long-term expected rate of return on pension benefits investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. This year, the long-term expected rate of return assumption is no longer applicable.

Discount Rate

The asset basis for the date of depletion projection is the ERS's fiduciary net position (the gross assets plus deferred outflows of resources less the gross liabilities, including the senior pension funding bonds payable, plus deferred inflows of resources). On this basis, the ERS's fiduciary net position was expected to be exhausted in the fiscal year 2015.

The ERS's fiduciary net position was not projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the tax free municipal bond index (Bond Buyer General Obligation 20-Bond Municipal Bond Index) was applied to all periods of projected benefits payments to determine the total pension liability. The discount rate was 3.58% as of June 30, 2017.

The June 30, 2017, actuarial valuation reflects a decrease of \$5,498 million in the net pension liability, rate as required by GASB Statement No. 67 from 2.85% in fiscal year 2016 to 3.58% in fiscal year 2017, and the effect of plan changes of approximately \$2,017 million.

The discount rate on June 30, 2016 and 2017 was as follow:

	June 30, 2016	June 30, 2017
Discount Rate	2.85%	3.58%
Long-term expected rate of return net of investment expense	6.55%	N/A
Municipal bond rate *	2.85%	3.58%

* Bond Buyer General Obligation 20-Bond Municipal Bond Index
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According to Paragraph 30 of Statement 68, the long-term discount rate should be determined without reduction for pension plan administrative expense. Using this lower discount rate has resulted in a slightly higher Total Pension Liability and Net Pension Liability.

Sensitivity of the Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the Authority's proportionate share of the Net Pension Liability on June 30, 2017, calculated using the discount rate of 3.58%, as well as what the Municipality's proportionate share of the Net Pension Liability would be if it were calculated using a discount rate that is 1 – percentage point lower or 1 – percentage point higher than the current rate:

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NOTE 14 - PENSION PLAN (CONTINUED)

	1% Decrease 2.58%	Current Discount Rate 3.58%	1% Increase 4.58%
Net Pension Liability as of June 30, 2018	\$64,526,122	\$58,641,397	\$53,666,152

Medical Insurance Plan for Retired Employees

There are no member or employer contributions on behalf of the Medical Insurance Plan Contribution. This benefit is financed on a pay-as-you-go basis from the General Fund of the Government of Puerto Rico. Since this benefit is not funded in advance, the Annual Required Contribution (ARC) for this benefit has been calculated based on an assumed investment return rate of 2.90% based on the asset allocation on the Government general assets that are used to pay this benefit.

As a cost-sharing multiple employer plan, ERS is not required to report a Net OPEB Liability. In accordance with paragraph 23 of GASB Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions", the employers that participate in the plan should recognize annual OPEB expense equal to their contractually required contributions to the plan. The employers do not have an ARC or a Net OPEB Liability.

Fiscal Plan for Puerto Rico

The last Fiscal Plan for Puerto Rico was approved by the Oversight Board of PROMESA on May 27, 2020. The approval was conditioned on the Puerto Rico government and the Board reaching an agreement to reduce benefit payments of the following systems by 8.5% for higher pensions in the aggregate:

- Puerto Rico Government Employees Retirement System,
- Puerto Rico Judiciary Retirement System, and
- Puerto Rico Teachers Retirement System.

The details of the reduction methodology, which will determine how the reductions impact each system, are not final at this time. A multi-year delay in implementation is also anticipated. These potential reductions are not reflected in the June 30, 2016 valuation. Also, note that the Fiscal Plan does not anticipate future payment of the Act 3-2013 AUC (shown earlier as \$776 million for fiscal year 2016-2017 and \$685 million per year for fiscal years 2017-2018 through 2032-2033) contained in current law. Rather, the Fiscal Plan anticipates that ERS will be funded on a pay-as-you-go basis once assets are exhausted.

Pay-As-You-Go Funding

On June 27, 2017, the Treasury Department issued Circular Letter No. 1300-46-17 in order to convey to the central government agencies, public corporations and municipalities the new implementation procedures to adopt, effective July 1, 2017, a new "pay-as-you-go" (Pay-Go) mechanism for the ERS.

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NOTE 14 - PENSION PLAN (CONTINUED)

Subsequently, on August 23, 2017, the Governor signed into law the “Act to Guarantee the Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants” (Act No. 106), which reformed the Commonwealth Retirement Systems. Act No. 106 terminated the previously existing pension programs for the ERS’s participants as of June 30, 2017. The members of the prior programs and new system members hired on and after July 1, 2017 are now enrolled in a new defined contributions program. Act No. 106 also established by law the Pay-Go mechanism for the payment of accumulated pension benefits and eliminated employers’ contributions and other analogous contributions. Approximately \$2 billion was allocated for the payment of Pay-Go benefits in each of the budgets for fiscal years 2018 and 2019.

Furthermore, Act No. 106 modified the ERS’s governance. Under Act No. 106, the ERS’ Board of Trustees was substituted with a new Retirement Board, which is currently responsible for governing all of the Commonwealth’s Retirement Systems.

Act No. 106 also ordered a suspension of the ERS’s loan programs and ordered a merger of the administrative structures of the retirement systems. At the Retirement Board’s discretion, the servicing of the ERS’s existing loan portfolio may be externalized. Pursuant to Act No. 106, the employees of the ERS that are not retained under the new administrative structure will be transferred to other public agencies in conformity with Act No. 8 of February 8, 2017.

At a basic level, ERS will need to hold some level of operating cash to account for any ongoing timing issues between receipt and disbursement of funds. The “pay-go” funding needed in a given year is the difference between actual contributions and actual disbursements:

- Contributions to ERS are primarily based on statutory percentage of payroll.
- Disbursements are comprised of benefit payments, administrative expenses, and Pension Obligation Bond debt service.

Contributions and disbursements will experience natural variation due to emerging demographic experience. Contributions and disbursements can also be greatly impacted by specific management decisions, such as an early retirement incentive program or other workforce reduction. A major issue that needs to be addressed by ERS and the Commonwealth is determining what the process of ERS budgeting for “pay-go” funding will be. While the ERS can set an expected “pay-go” amount at the time of budgeting for an upcoming fiscal year, both actual contributions and disbursements can vary from expectations during the fiscal year.

- If the budget is set based on expected contributions and disbursements, in the event of adverse experience during the fiscal year, should provide for additional funds from the sponsoring employers.
- If the ERS be permitted to develop a budget request of a “pay-go” amount for the fiscal year that includes a margin to provide a buffer against adverse outcomes.
- And how would the impacts of specific management decisions be handled.

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NOTE 14 - PENSION PLAN (CONTINUED)

There are certainly many more operational details to be considered. "Pay-go" operation is a complex issue that requires careful thought and planning, constant monitoring, and the ability to respond to emerging events quickly.

Pension Plan Fiduciary Net Position

As per June 30, 2017, Actuarial Valuation Report issued on November 9, 2020, the Actuaries state: "PRGERS net assets became negative in the 2014-2015 fiscal year PRGERS gross assets as June 30, 2017 are less than one year of expected benefit payments."

The Employee's Retirement System of the Government of the Government of Puerto Rico provides additional information of the Defined Benefit Program and Hybrid Program. They issue a publicly available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Government. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940-2003.

NOTE 15 - POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS ("OPEB")

Program Description and Membership

The Authority provides post-employment benefits other than pension for its retired employees (the "OPEB Program"). The plan is an unfunded, multi-employer defined benefit other postemployment healthcare benefit plan. The plan is administered on a pay-as-you-go basis. Accordingly, no assets are accumulated in a qualifying trust that meets the criteria in paragraph 4 of GASB Statement No. 75 "Accounting and Financial Reporting for the Postemployment Benefits Other Than Pensions".

The Plan covers a payment of up to \$100 per month to the eligible medical insurance plan selected by each member (\$1,200 annually) provided that the member retired prior to July 1, 2013 (Act No. 43, as amended by Act No. 3). The Plan is financed by the Commonwealth through legislative appropriations. However, the Commonwealth claims reimbursement from each employer on a monthly basis for the corresponding amount of the OPEB payments made by the Commonwealth in relation to the retirees associated with each employer. There is no payments made by the Commonwealth in relation to the retirees associated with each employer. There is no contribution requirement from the plan members during active employment. The retirees contribute the amount of the healthcare insurance premium not covered by the Commonwealth contribution. In addition, a bonus of \$100 is given to retirees annually (on July), for the purpose of acquiring medicines. These benefits are not provided to the retirees' spouse or any relatives.

Plan members were eligible for benefits upon reaching the applicable pension benefits retirement age. Act No. 3 of 2013 eliminated this healthcare benefit to the Plan members that retired after June 30, 2013.

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NOTE 15 - POST- EMPLOYMENT BENEFITS OTHER THAN PENSIONS ("OPEB") (CONTINUED)

Total OPEB Liability, Expense and Deferred Outflows/Inflows of Resources

As permitted by GASB, the Authority's unfunded total OPEB liability as of June 30, 2018 of approximately \$1,657,962 was measured at June 30, 2017 by an actuarial valuation as of that date. An expected total OPEB liability was determined as of June 30, 2016, the prior measurement date, using standard roll back techniques. The roll back calculation begins with the total OPEB liability, as of the measurement date, June 30, 2017, adds the expected benefit payments for the year, deducts interest at the measurement date, June 30, 2017, adds the expected benefit payments for the year, deducts interest at the discount rate for the year, and then subtracts the annual normal cost (also called the service cost).

Changes in the total OPEB liability for the year ended June 30, 2018 are as follows:

Balance at the Beginning of the Year	\$ 2,172,834
Charges for the Year:	
Interest on Total OPEB Liability	68,245
Effect of Economic/Demographic Gains and Losses	(24,912)
Effect of Assumptions Changes or Inputs	(419,283)
Benefit Payments	<u>(138,922)</u>
Net Changes	<u>(514,872)</u>
Balance at the End of Year	<u>\$ 1,657,962</u>

For the year ended June 30, 2018, the Authority recognized an OPEB (credit) expense of \$508,091.

As of June 30, 2018, the Authority reported deferred outflows of resources from OPEB activities as follows:

<u>Source</u>	
Payment of Benefits Subsequent to the Measurement Date	\$ 138,922
Differences Between Expected and Actual Experience	-
Changes in Assumptions or Other Inputs	<u>(6,780)</u>
Total Deferred Outflows	<u>\$ 132,142</u>

Deferred outflows of resources related to OPEB resulting from the Authority payment of benefits subsequent to the measurement date which amounted to \$138,922 as of June 30, 2018 is recognized as a reduction of the total OPEB liability in the year ending June 30, 2019.

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NOTE 15 - POST- EMPLOYMENT BENEFITS OTHER THAN PENSIONS ("OPEB") (CONTINUED)

Amounts reported as deferred outflows of resources from OPEB activities as of June 30, 2018 will be recognized in the OPEB expense as follows:

Years Ending June 30:

2019	\$ (1,356)
2020	(1,356)
2021	(1,356)
2022	(1,356)
2023	<u>(1,356)</u>
Total	\$ <u>(6,780)</u>

Actuarial Methods and Assumptions

The actuarial cost method used to measure the total OPEB liability at June 30, 2018 was the individual entry age normal cost method. The actuarial valuations used the following actuarial method and assumptions:

Measurement Date	June 30, 2017
Valuation Date	July 1, 2016
Inflation	Not Applicable
Payroll Growth	Not Applicable
Salary Increases	Current General Economy
Discount Rate - Municipal Bond Index	3.58%, based on Bond Buyer General Obligation 20-Bond Municipal Index
Mortality	<p><u>Pre-Retirement Mortality</u> - For general employees not covered under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on generational basis. For members covered under Act No. 127, RP-2014 Employee Mortality Rates are assumed with blue collar adjustments for males and adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on a generational basis. As generational tables, they reflect mortality improvements both before and after the measurement date.</p> <p><u>Post-Retirement Healthy Mortality</u> - Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of the ERS Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994 Mortality Table for Males and 95% of the rates from the UP-1994 Mortality Table for Females, both projected from 1994 to 2010 using Scale AA.</p>

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NOTE 15 - POST- EMPLOYMENT BENEFITS OTHER THAN PENSIONS ("OPEB") (CONTINUED)

The base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational basis, it reflects mortality improvements both before and after the measurement date.

Post-retirement Disable Mortality - Rates which vary by gender are assumed for disable retirees based on a study of the ERS Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table for Males and 115% of the rates from the UP-1994 Mortality Table for Females. The base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

Sensitivity of the Total OPEB Liability to Changes in the Discount Rate

The following presents the total OPEB liability calculated using the discount rate of 3.58%, as well as what it would be if it were calculated using a discount rate of 1 percent-point lower (2.58%) or 1 percent-point higher (4.58%) than the current rate:

	1% Decrease 2.58%	Current Discount Rate 3.58%	1% Increase 4.58%
Total OPEB Liability as of June 30, 2018	\$1,824,340	\$1,657,962	\$1,517,297

NOTE 16 - OPERATING LEASES

The Authority's land operating lease terms vary generally from one to five years. Minimum future rental revenues on non-cancelable operating lease with terms of one year or longer are as follows:

<u>Years</u>	<u>Amount</u>
2019	\$ 7,085,304
2020	4,896,486
2021	4,667,454
2022	4,463,176
2023	3,862,208
2024 - 2029	10,312,795
2030 - 2035	4,011,035
2036 - 2041	1,713,921
2042 - 2047	1,542,000
2048 - 2052	<u>813,833</u>
	<u>\$ 43,368,212</u>

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NOTE 16 - OPERATING LEASES (CONTINUED)

Real estates taxes, insurance and maintenance expenses are usually obligations of the lessees. Contracts provide, in certain cases, for rent increases during renewal periods to be based on fixed percentages. Usually, rent is collected six (6) months in advance, and is billed taking into consideration the rent of the parcel and property taxes estimated using the CRIM invoices sent to the Authority related the specific parcel of land. The lessee is responsible to provide a certificate of "bonafide farmer", in order to be released of such payment. In most cases, farmers need to pay in advance the total amount of the rent, and when condition is satisfied, an adjustment of such amount is credited to their account balance.

NOTE 17 - CONTINGENCIES

Puerto Rico Land Authority

(A) LITIGATIONS

The Authority is a defendant or a co-defendant in various lawsuits and complaints. The Authority's management, after consultation with legal counsel, has made a provision of \$4,438,920 for losses on these litigations. However, the ultimate amount payable in excess of the amount provided, if any, cannot be determined.

The Authority is a defendant in various claim most of them resulting form the closing of several sugar mills throughout the years and from events generally incidental to its operations. Also, it has various environmental claims and penalties imposed by The Environmental Protection Agency (EPA), mainly from the handling of pesticide warehouses. The Authority is in the process of litigating such claims. The accompanying statement of net position include a reserve in relation to this matter, but the ultimate outcome is uncertain at this time and accordingly, the ultimate liability, if any, cannot be presently determined.

In July 2004, the Land Authority deposited in the Superior Court in San Juan, the amount of \$5 million for expropriation of land form "Comunidad Agricola Bianchi". The case is still in court because "Comunidad Agricola Bianchi" does not consider the amount given as fair value of the property. The Authority's management believes that the case will be settled for an additional of \$4 millions, which was considered in the reserve for contingencies included in the accompanying, basic financial statements.

During 2006, the "Central Roig Company, Inc.", which is one of the two corporations organized by sugarcane farmers that received 50% of the transferred assets of the Sugar Corporation (the sugar mills known as Central Roig, Central Coloso, Central Plata and Central Mercedita, together with the "Refineria Mercedita"), in compliance with and according to the provisions of Public Law No. 189 of December 26, 1997, is suing, among other parties, the Authority, alleging all sorts of actions in damages against the different parties, based upon their inability to produce sugarcane as contemplated by Public Law No.1 189 at the time that the aforementioned assets were transferred to them. The plaintiffs are basically alleging that, because of the failure of the different governmental agencies and third parties involved, to comply with certain undefined and allegedly multiple obligations and commitments to which they were bound, they suffered economic damages in excess of \$100 million. This case is related to two other cases considered in the contingency reserve. Management, based on advice from legal counsel, believes that no potential loss is forecasted as of this date, other that attorney's fees and litigation expenses.

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NOTE 17 - CONTINGENCIES (CONTINUED)

(B) FEDERAL AWARDS

During the year ended June 30, 2015, the Authority received a grant fund from the Department of Education. The grant programs are subject to audit by agents of the granting authorities, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. For the year ended June 30, 2018 and as of the basic financial statements date, no audits have been conducted for this particular grant. Nevertheless, any liability for reimbursement which may arise as a result of the audits is not considered by management to have a significant effect in the accompanying financial statements.

(C) COMPTROLLER'S OFFICE OF PUERTO RICO REPORTS

The Authority is also audited by the Comptroller's Office of Puerto Rico (COPR), who has issued several reports on audits over operations of the Authority and FIDA. The oversight entities, such as the Puerto Rico Department of Justice, are evaluating actions to be taken against the Authority and its employees. The financial impact if any of the possible actions to be taken by the oversight entities can not be presently determined.

Innovation Fund for the Agriculture Development of Puerto Rico (FIDA)

(D) 2010 Agriculture Department Reorganization Plan Number 4

Article 36 of the Reorganization Plan number 4, discussed on Note 1 to the financial statements, amended laws number 165-2001 and 166-2001, requiring that funds received from coffee and sugar taxes be deposited in a new fund to be known as "Technological Innovation and Agricultural Promotion" ("Fondo de Innovacion"), to be transferred to the "Administration for the Development of Agricultural Enterprises" ("Administración para el Desarrollo de Empresas Agropecuarias" or ADEA). According to the Reorganization Plan, this fund can be administered by FIDA, through agreement with the Secretary of Agriculture, in order to promote the development of agriculture in Puerto Rico.

As of financial statement date, monies from such sugar and coffee taxes has not been deposited in such fund nor transferred to ADEA, and kept on FIDA accounts.

FIDA had received funds from sugar and coffee taxes, from 2011 (date in which the Reorganization Plan was to be implemented) to June 30, 2017 as follows:

<u>Years</u>	<u>Amount</u>
2011	\$ 14,784,002
2012	13,932,814
2013	15,301,865
2014	12,866,028
2015	12,685,288
2016	13,695,023
2017	<u>12,889,062</u>
Total	<u>\$ 96,154,082</u>

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NOTE 17 - CONTINGENCIES (CONTINUED)

During the year ended June 30, 2018, no funds were received.

On November 2015, COPR issued audit report number CP-16-03, covering FIDA operations from July 1, 2009 to December 31, 2013. In such report, COPR includes a special comment that the Reorganization Plan will impact FIDA operations and services that FIDA provides to farmers and agricultural activities, since monies that FIDA receives to fund their operations are to be transferred to the "Technological Innovation and Agricultural Promotion" fund of ADEA. Also, COPR comments that the Reorganization Plan does not define how FIDA will cover its operational costs while promoting the agricultural and agro industrial development in Puerto Rico. It also comment that the Reorganization Plan does not establish which of the two entities will be finally be responsible for payment of FIDA credit lines through the GDB, and management of incentives already given to farmers.

In his audit report, COPR makes a recommendation, to the Governor and the Legislative Assembly of Puerto Rico, to evaluate this concerns arising from Reorganization Plan Number 4, and the effect they will have on FIDA operations.

FIDA management has also raised these concerns and is in agreement with the COPR recommendations. In addition, on April 19, 2016, Project 2873 (P. de la C. 2873) was presented to the Legislature of Puerto Rico, and referred to the Governmental, Agriculture and Environmental and Natural Resources Commissions. Project 2873 propose to revitalize and restructure DA by including FIDA as a programatic and operational component of DA, separated from the Authority, for the purpose of promoting agricultural enterprises. According to Project 2873, the requirements of Reorganization Plan number 4 were never placed in operation, and are not in accordance with the present public policy of the Commonwealth of Puerto Rico, and that it is necessary to derogate the requirements of such Reorganization Plan.

The final outcome of COPR recommendations to the Governor and the Legislative Assembly of Puerto Rico, and the outcome of Project 2873, cannot presently be determined and accordingly, no adjustments have been made in the accompanying financial statements.

NOTE 18 - RESTATEMENT OF NET POSITION

Puerto Rico Land Authority

During the year ended June 30, 2018, the Authority identified certain accounting errors belonging to prior years and other adjustments required under new GASB standards. The effect of these prior period adjustments on the net position of the Authority as of July 1, 2017 is as follows:

Net Position, Beginning of Year, as Previously Presented		\$ 23,979,641
Restatement Adjustments:		
Deferred Outfloww GASB 68	\$ 1,523,131	
Deferred Outfloww GASB 75	138,922	
Net Other Postemployment Benefits Liability GASB 75	<u>(2,172,834)</u>	
Total Net Adjustment for the Authority	\$ <u>(510,781)</u>	<u>(510,781)</u>
Net Position, Beginning of Year, as Restated		\$ <u>23,468,860</u>

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NOTE 19 - DATE OF MANAGEMENT'S REVIEW

The Authority's management evaluated subsequent events until February 9, 2021, date in which the basic financial statements are available to be issued. See also Note 21.

NOTE 20 - VOLUNTARY 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:

<u>Years of Services in Public Sector</u>	<u>Incentive Gross Amount</u>
Up to 1 Year	1 Month of Salary
From 1 Year and One Day Up to 3 Years	3 Months of Salary
from 3 Years and One 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:

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

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.

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NOTE 20 - VOLUNTARY TERMINATION BENEFITS (CONTINUED)

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.

The Authority has 18 participants in the plan, and termination benefits are measured at the discount present value of expected future benefit payments. Benefits are based on 60% of average pay (meaning the highest annual average salary of the participant during any of three years of credited services), in addition to social security computed at 7.65%, retirement benefits based on a percentage ranging from 25.5250% to 30.5250% from 2016 to 2025, and \$320 of medical plan up to fiscal year 2018 - 2019. Termination benefits will be completed during fiscal year 2024-2025.

As of June 30, 2018, the present value of future incentive payments reported as a liability amounted to approximately \$4,266,489. Of this amount, \$833,192 should be funded during the next fiscal year. The long - term portion of the early termination obligation amounted to \$3,433,297. Such amounts are disclosed respectively, as short - term and long - term liabilities in the accompanying statement of net position.

NOTE 21 - SUBSEQUENT EVENTS

The Authority has evaluated subsequent events and the basis for the date, whether it is the date the basic financial statements were issued or were available to be issued.

(a) Qualifying Modification Under Title VI of PROMESA

On May 15, 2017, the Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA) and GDB entered into a Restructuring Support Agreement (the RSA) with a significant portion of the GDB's creditors. The parties to the RSA agreed to undertake a financial restructuring of the GDB pursuant to a Qualifying Modification under Title VI of PROMESA (the "Qualifying Modification"). On August 9, 2018, the GDB commenced the solicitation of votes on the Qualifying Modification and on August 10, 2018 commenced an action to obtain court approval of the Qualifying Modification. Following the conclusion of voting on September 12, 2018, the GDB announced that it received the necessary

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NOTE 21 - SUBSEQUENT EVENTS (CONTINUED)

votes from holders of claims subject to the Qualifying Modification (the “Participating Bond Claims”) to approve the Qualifying Modification, as required under PROMESA. On November 6, 2018, the Qualifying Modification was approved by the Federal Court. On November 29, 2018, the FAFAA and the GDB announced the consummation of the Qualifying Modification. Under the Qualifying Modification, holders of Participating Bond Claims exchanged their Participating Bonds claims for bonds issued by a newly created public instrumentality, the GDB Debt Recovery Authority, and the GDB transferred to such entity its municipal loan portfolio, a portion of its public entity loan portfolio, its real estate owned assets and its unencumbered cash.

Pursuant to Act No. 109-2017, also known as the Government Development Bank for Puerto Rico Debt Restructuring Act (the “GDB Restructuring Act”), claims on account of deposits held by the Commonwealth and other public entities, including the Authority, will be exchanged for interest in the Public Entity Deed of Trust created pursuant to the GDB Restructuring Act. Specifically, pursuant to the GDB Restructuring Act, on the closing date of the Qualifying Modification (the “Closing Date”), the balance of liabilities owed between the Commonwealth and its agents, instrumentalities and affiliates, including the Authority (each a “Non-Municipal Government Entity”) and the GDB will be determined by applying the outstanding balance of any deposits held at GDB in a Non-Municipal Government Entity’s name against the outstanding balance of any loan of such Non-Municipal Government Entity owed to the GDB or of any bond or note of such Non-Municipal Government Entity held by the GDB as of such date. Those Non-Municipal Government Entities having net claims against the GDB, after giving effect to the foregoing adjustment will receive their pro rata share of interests in the Public Entity Trust (PET), which will be deemed to be full satisfaction of any and all claims such Non-Municipal Government Entity may have against GDB. The assets of the PET (the “PET Assets”) will consist of, among other items, a \$890 million claim against the Commonwealth, which is the subject of a proof of claim filed in the Commonwealth Title III case under PROMESA. A portion of the PET Assets will be transferred to the PET on the Closing Date and the remainder of the PET Assets, or any portion thereof, will be transferred to the PET in one or more transactions, as set forth in the Public Entity Deed of Trust (as defined in the GDB Restructuring Act). Under the GDB Restructuring Act, the transfer of the PET Assets by the GDB to the PET will be an irrevocable, non-voidable, and absolute transfer of all the GDB’s legal and equitable right, title, and interest in the PET Assets.

As a result of the qualifying Modification, on November 29, 2018, the credit facility of FIDA owed to the GDB of \$28,125,394 (\$27,674,033 plus accrued interests of \$451,361) was partially offset for \$22,971,172, leaving a balance outstanding of \$5,154,222 (\$4,702,861 plus accrued interests of \$451,361). As of financial statements date, an agreement has not been reached to cancel the remaining of the balance, or to determine how the remainder of the credit facility will be managed.

(b) Administrative Bulletin No. OE-2021-003

On January 2, 2021, the newly elected governor of the Commonwealth of Puerto Rico, issued Administrative Bulletin No. OE-2021-003 named "Executive Order to Issue Fiscal Responsibility and Expense Control Measures, and to repeal Administrative Bulletin No. OE-2017-001.

The executive order declares a fiscal emergency state in the government of Puerto Rico. It orders all governmental agencies in Puerto Rico to implement the necessary measures in order to reduce operational expenses, without adversely affect those services necessary to protect the citizens health, security and wellnes.

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NOTE 21 - SUBSEQUENT EVENTS (CONTINUED)

Among the most significant measures required by the executive order are:

- 1) **Vacancies** - All regular career, transitory and irregular positions, which are vacant at executive order's date, or which becomes vacant after the effective date of the executive order, will be subject to a need assessment. The governmental agencies are also not allowed to fill any vacant positions by any means (like promotion, merit, mobility, transfer and others), unless it is deemed necessary to offers the necessary services to the citizens, and only through a written authorization from the Management and Busdet Office (OGP),
- 2) **Prohibition to Create New Positions** - Governmental agencies are not allowed to create new regular career, transitory and irregular positions, unless it is deemed necessary to offers the necessary services to the citizens, and only through a written authorization from the Management and Busdet Office (OGP),
- 3) **Reduction in Positions of Confidence** - All governmental agencies are required a 20% reduction in posts of confidence,
- 4) **Reduction in Operational Expenses** - All governmental agencies are required reductions in operational expenses, as part of the expense reduction measures,
- 5) **Credit Cards** - The use of official credit cards, paid through with public funds, is prohibited, unless it is done is strict compliance with applicable and outstanding regulations,
- 6) **Traveling outside Puerto Rico** - The order prohibits the use, by officers and employees of the governmental agencies, of public funds for traveling outside Puerto Rico, unless they are strictly essential to perform the duties of the position, and only when authorized by the Secretary of the agency and the Secretary of the Commonwealth of Puerto Rico. Also, if authorized, should be done in strict compliance with applicable and outstanding regulations,
- 7) **Cellular Phones and Other Technological Services** - The order prohibits the use of public funds for payment of celullar phones, personal digital assistants (PDA's), personal internet service equipment and other technological services, for exclusive use of the Officers and employees of the agencies. OGP Director is allowed to offer waivers to thses requirements, considering, among other things, the service needs of public employees related to remote working. Agencies are required to obtain authorization from OGP and the Puerto Rico Innovation and Technology Service (PRITS), for any plan related to the acquisition of these technological equipments or services,
- 8) **Reduction in Energy and Water Consumption** - All agencies directors are required to reduce consumption of public utilities, like electric power and water. Regarding electric power, the agencies are required to implement all necessary measures to reach a minimum annual reduction of 5%. As for water consumption, those agencies, for which operational expenses are subsidized, in whole or in part, with funds from the Commonwealth's Central Government, must reduce water consumption by 5% annually, during years 2020-2021, 2021-22, and 2022-23, so it can reach a reduction of 15% in the three-year period. Percentage reduction will be measured from water consumption expense during year 2019-20 as base year,
- 9) **Reduction in Contract Amounts** - Each agency must reduce expenses for services (purchased and/or professional) by 10% annually,
- 10) **Contracting for Services** - It is prohibited to make a contract for purchased or professional services over \$10,000 (and below \$10,000,000) in the same fiscal year, without the written authorization from OGP. For this purpose, the Director of OGP will verify funds availability in the budget assigned to the agency. For contracts in excess of \$10,000,000, in the same fiscal year, must be authorized together by the Director of OGP and the the Secretary of the Commonwealth of Puerto Rico, or the person designated by him for such purpose, and

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NOTE 21 - SUBSEQUENT EVENTS (CONTINUED)

- 11) **Lease Contracts** - Agencies must submit to OGP, within 30 days after the effective date of this executive order, a list of all outstanding lease contracts, amount contracted, and the reasons to justify the contract. OGP is authorized to deny the renewal of these contracts, or to modify its terms when due, unless it is necessary for the services given to citizens. OGP can consolidate operations in various agencies in a single lease premise, and renegotiate monthly fees and other clauses, in order to attain better terms.

The executive order discloses that all these control measures are the first ones to be implemented to face the fiscal crisis, and that it should not be understood that they are the only ones to be implemented. All agencies must evaluate its operations in order to detect additional measures of control, savings and expense reduction.

The Authority has not yet determined the effects these measures will have on the basic financial statements and the results of operations.

(c) Effects of the Coronavirus Disease

During the month of December 2019, a respiratory disease started to spread, caused by a novel virus called "Coronavirus" or COVID-19. The World Health Organization (WHO) declared a global health emergency in January 2020 and in March 2020, it declared the spread of COVID-19 as a global pandemic.

The effects of the disease have been swift. The pandemic has transformed economic outlooks, health, and social norms around the globe. Government and health care providers are working around the clock to slow the spread of the disease. The whole world is affected by the pandemic. Travel restrictions are in place, and global trade, commerce, tourism, investment, and supply chains are in disarray.

The Governor of the Commonwealth of Puerto Rico issued a lockdown starting on March 15, 2020, which as of the Financial Statements issuance date has not been fully lifted. The economic damages to the Authority finance could not be estimated at this time.

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

Required Supplementary Information
Schedule of Proportionate Share
of the Net Pension Liability
(Unaudited)

For the Fiscal Year Ended June 30, 2018

<u>Last 10 Years (1)</u>	<u>June 30, 2015</u>	<u>June 30, 2016</u>	<u>June 30, 2017</u>	<u>June 30, 2018</u>
Proportion of the Net Pension Liability	<u>0.15986 %</u>	<u>0.17010 %</u>	<u>0.17078 %</u>	<u>0.17138 %</u>
Proportionate Share of the Net Pension Liability	<u>\$ 48,179,967</u>	<u>\$ 56,705,886</u>	<u>\$ 64,382,076</u>	<u>58,641,397</u>
Covered - Employee Payroll	<u>\$ 5,577,669</u>	<u>\$ 5,646,095</u>	<u>\$ 5,711,548</u>	<u>5,728,609</u>
Proportionate Share of the Net Pension Liability as a Percentage of Covered Payroll	<u>863.80 %</u>	<u>1,004.34 %</u>	<u>1,127.23 %</u>	<u>1,023.66 %</u>
Plan's Fiduciary Net Position	<u>\$ 128,953</u>	<u>\$ 1,136,709</u>	<u>\$ 2,161,883</u>	<u>3,614,152</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	<u>0.27 %</u>	<u>(2.05)%</u>	<u>(3.47)%</u>	<u>(6.57)%</u>

Notes to the Schedule:

Benefit Changes: In 2015, benefit terms were modified to base public safety employee pensions on a final three-year average salary instead of a final five-year average salary. Beginning on July 1, 2017, the pension benefits were paid through pay-as-you-go method.

Changes Assumptions: In 2015, amounts reported as changes in assumptions resulted primarily from adjustments to expected retirement ages of general employees.

Fiscal year 2015 was the first year of implementation, therefore only years 2015 and 2016 are shown. The amounts presented have a measurement date as of June 30, 2014. Total pension liability was obtained from the audited Puerto Rico Government Employees Retirement System (PRGERS) financial statements as of June 30, 2017, 2016 and 2015. These reports are the basis to determine the net pension liability for the year ended June 30, 2018 and 2017 respectively.

Date References: Employee's Retirement System of the Government of the Commonwealth of Puerto Rico: Actuarial Valuation Report.

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

Schedule of Contributions
(Unaudited)

For the Fiscal Year Ended June 30, 2018

<u>Last 10 Years (1)</u>	<u>June 30, 2015</u>	<u>June 30, 2016</u>	<u>June 30, 2017</u>	<u>June 30, 2018</u>
Contractually Required Contribution (Actuarially Determined)	\$ 973,613	\$ 1,050,308	\$ 1,114,753	\$ 1,099,505
Contributions in Relation to the Actuarially Required Contributions	<u>973,613</u>	<u>1,050,308</u>	<u>1,114,753</u>	<u>1,099,505</u>
Contributions Deficiency (Excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered - Employee Payroll	<u>\$ 5,358,205</u>	<u>\$ 5,646,095</u>	<u>\$ 5,711,548</u>	<u>\$ 5,711,548</u>
Contributions as a Percentage of Covered - Employee Payroll	<u>18.17 %</u>	<u>18.60 %</u>	<u>19.52 %</u>	<u>19.25 %</u>

Notes to the Schedule:

Unless otherwise noted above, the following actuarial methods and assumptions were used to determine contribution rates reported in the Pension Benefits Schedule of the Employers' Contributions:

Assets Valuation Method	Market Value of Assets
Inflation	Not Applicable
Investment Rate of Return	6.55% Net Pension Plan Investment, Including Inflation
Municipal Bond Index	3.58% as per Bond Buyer General Obligation 20 - Bond Municipal Index
Discount Rate	2.85%
Projected Salary increase	3.00% per year. No compensation increases are assumed until July 1, 2021, as a result of Act No. 3-2017, four year extension of Act No. 66-2014, and the current general economy.
Mortality	Pre-Retirement Mortality: for general employees not covered Under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the base year, and projected forward using MP-2017 on a generational basis. For members covered under Act 127, RP-2014 Employee Mortality Rates with blue collar adjustments for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on a generational basis. As generational tables, they reflect mortality improvements both before and after measurement date. 100% of deaths while in active service are assumed to be occupational for members covered under Act. No. 127.

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

Schedule of Contributions - Continued
(Unaudited)

For the Fiscal Year Ended June 30, 2018

Post-Retirement Healthy Mortality: Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994 Mortality Tables Males and 95% of the rates from UP-1994 Mortality Table Females, both projected from 1994 to 2010 using Scale AA. These base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

Post-Retirement Disabled Mortality: Rates which vary by gender are assumed for disabled retirees based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table Males and 115% of the rates from the UP-1994 Mortality Table Females, both projected from 1994 to 2010 using Scale AA. These base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after measurement date.

(1) Fiscal year 2015 was the first year of implementation. The schedule will be expanded to show 10 years once the information becomes available in the future.

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

Required Supplementary Information
Schedule of Proportionate Share
of the Net Other Postemployment Benefits (OPEB) Liability
(Unaudited)

For the Fiscal Year Ended June 30, 2018

<u>Last 10 Years (1)</u>	<u>June 30, 2017</u>	<u>June 30, 2018</u>
Proportion of the Net OPEB Liability	<u>0.18334</u> %	<u>0.17010</u> %
Proportionate Share of the Net Pension Liability	<u>\$ 2,172,834</u>	<u>\$ 1,657,962</u>
.17010		
Covered - Employee Payroll	N/A	N/A
Proportionate Share of the Net Pension Liability as a Percentage of Covered Payroll	N/A	N/A
Plan's Fiduciary Net Position	N/A	N/A

(1) Fiscal year 2018 was the first year of implementation. The schedule will be expanded to show 10 years once the information becomes available in the future.

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

Schedule of Other Postemployment Benefits (OPEB)
Contributions
(Unaudited)

For the Fiscal Year Ended June 30, 2018

<u>Last 10 Years (1)</u>	<u>June 30, 2017</u>	<u>June 30, 2018</u>
Contractually Required Contribution (Actuarially Determined)	\$ 146,304	\$ 138,922
Contributions in Relation to the Actuarially Required Contributions	<u>146,304</u>	<u>138,922</u>
Contributions Deficiency (Excess)	\$ <u>-</u>	\$ <u>-</u>
Covered - Employee Payroll	N/A	N/A
Contributions as a Percentage of Covered - Employee Payroll	N/A	N/A

Notes to the Schedule:

Measurement Date	June 30, 2017
Valuation Date	July 1, 2016
Inflation	Not Applicable
Payroll Growth	Not Applicable
Salary Increases	Current General Economy
Discount Rate - Municipal Bond Index	3.58%, based on Bond Buyer General Obligation 20-Bond Municipal Index
Mortality	<u>Pre-Retirement Mortality</u> - For general employees not covered under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on generational basis. For members covered under Act No. 127, RP-2014 Employee Mortality Rates are assumed with blue collar adjustments for males and adjusted to reflect Mortality Improvement Scale MP-2017 from the 2006 base year, and projected forward using MP-2017 on a generational basis. As generational tables, they reflect mortality improvements both before and after the measurement date.

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

Schedule of Other Postemployment Benefits (OPEB)
Contributions - Continued
(Unaudited)

For the Fiscal Year Ended June 30, 2018

Post-Retirement Healthy Mortality - Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of the ERS Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994 Mortality Table for Males and 95% of the rates from the UP-1994 Mortality Table for Females, both projected from 1994 to 2010 using Scale AA. The base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational basis, it reflects mortality improvements both before and after the measurement date.

Post-retirement Disable Mortality - Rates which vary by gender are assumed for disable retirees based on a study of the ERS Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table for Males and 115% of the rates from the UP-1994 Mortality Table for Females. The base rates are projected using Mortality Improvement Scale MP-2017 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

(1) Fiscal year 2018 was the first year of implementation. The schedule will be expanded to show 10 years once the information becomes available in the future.



**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**

INDEPENDENT AUDITOR'S REPORT

To the Management and
Board of Directors
Puerto Rico Land 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 Puerto Rico Land Authority (From now on the Authority), an enterprise fund of the commonwealth of Puerto Rico, as of and for the fiscal year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated February 9, 2021. Our report was qualified because the Authority was not able to perform the evaluation and recognition of capital asset impairments, and therefore, capital assets are overstated and the amount of loss from impairment and restoration or replacement of the impaired capital assets amounts are not available as of basic financial statements date.

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 basic 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 the Authority's internal control.

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 Authority's financial statements will not be prevented, or detected and corrected on a timely basis. 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.

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

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 the basic financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which we reported to the Authority's management in a separate letter dated February 9, 2021.

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 Authority'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 Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Torres, Hernández & Punter, CPA, PSC

Torres, Hernández & Punter, CPA, PSC
Certified Public Accountants

Carolina, Puerto Rico

February 9, 2021

Stamp #EA39561 of the
College of CPA's of
Puerto Rico is affixed
to the original.



TORRES, HERNANDEZ & PUNTER, CPA, PSC
Certified Public Accountants

To the clients and users of the financial statements
Reported upon by Torres, Hernández & Punter, CPA, PSC
Certified Public Accountants

The partners and staff of Torres, Hernández & Punter, CPA, PSC are pleased to announce the successful completion of the 2019 independent peer review of our accounting and auditing practice. This review was undertaken as a condition of membership in the American Institute of Certified Public Accountants (AICPA), the national organization of CPA's in public practice, industry, government and education. Our participation in the Peer Review Program demonstrates our firm's commitment and desire of maintaining and improving the quality of our practice.

After through study of our policies and procedures, the team conducting the review concluded our firm complies with the quality control standards established by the AICPA and the Puerto Rico Society of CPA's (PRSCPA). Our firm is committed to periodic peer review to foster quality performance.

Bankers, bonding agents, investors, suppliers, legal advisors and others use the financial statements our firm audits, reviews, or compiles. We think those people, our clients, and our own staff, deserve independent quality assurance that our firm provides quality services. We are proud of our peer review results and would be happy to answer any questions you might have.

Sincerely,

Torres, Hernández & Punter, CPA, PSC

Torres, Hernández & Punter, CPA, PSC

Added Value Services, Provided by Leading Professionals, Obtaining a Reasonable Return on Investment

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To the Stockholders of
Torres, Hernandez, & Punter, CPA, PSC
and the Peer Review Committee of the
Puerto Rico Society of Certified Public Accountants

REPORT ON THE FIRM'S SYSTEM OF QUALITY CONTROL

We have reviewed the system of quality control for the accounting and auditing practice of **Torres, Hernandez, & Punter, CPA, PSC** (the firm) in effect for the year ended December 31, 2018. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants.

A summary of the nature, objectives, scope, limitations of, and the procedures performed in a System Review as described in the Standards may be found at www.aicpa.org/prsummary. The summary also includes an explanation of how engagements identified as not performed or reported in conformity with applicable professional standards, if any, are evaluated by a peer reviewer to determine a peer review rating.

Firm's Responsibility

The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. The firm is also responsible for evaluating actions to promptly remediate engagements deemed as not performed or reported in conformity with professional standards, when appropriate, and for remediating weaknesses in its system of quality control, if any.

Peer Reviewer's Responsibility

Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review.

Required Selections and Considerations

Engagements selected for review included engagements performed under *Government Auditing Standards*, including compliance audit under Single Audit Act, and audits of *Employee Benefit Plans*.

As part of our peer review, we considered reviews by regulatory entities as communicated by the firm, if applicable, in determining the nature and extent of our procedures.

Opinion

In our opinion, the system of quality control for the accounting and auditing practice of **Torres, Hernandez, & Punter, CPA, PSC** in effect for the year ended December 31, 2018, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency(ies) or fail. **Torres, Hernandez, & Punter, CPA, PSC** has received a peer review rating of *pass*.

A handwritten signature in black ink that reads "J. Angel, CPA". The signature is written in a cursive style.

License No. LLC-317
Expires on December 1, 2020

San Juan, Puerto Rico
October 1, 2019
2019-10-52

Stamp Number
E-376178
was affixed to
original