PUERTO RICO PORTS AUTHORITY

(A Component Unit of the Commonwealth
Of Puerto Rico)

*Basic Financial Statements With
Independent Auditors' Reports Thereon*

For the Fiscal Year Ended June 30, 2014

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(A Component Unit of the Commonwealth
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Basic Financial Statements With
Independent Auditors' Report There On
For the Fiscal Year Ended June 30, 2014

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

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INDEPENDENT AUDITORS' REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of the Puerto Rico Ports Authority (The Authority), a component unit of the Commonwealth of Puerto Rico as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

421 Muñoz Rivera Avenue, Suite 314, San Juan, Puerto Rico 00919 • Telephone (787) 250-1712 • Tel/Fax:(787) 250-1713
http://www.nievelaz.com • E-Mail: nievelaz@coqui.net

INDEPENDENT AUDITORS' REPORT
(Continued)

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2014, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters – Airport Operations

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

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Required Supplementary Information, such as Management's Discussion and Analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Nieves Velázquez & Co., P.S.C.

Nieves Velázquez & Co., P.S.C.
San Juan, Puerto Rico

November 7, 2014

Stamp No. 02710453 of the Puerto Rico Society of Certified Public Accountant has been affixed to the original of this report.

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Introduction

The following discussion and analysis of the financial performance and activity of the Authority is intended to provide an introduction to its financial statements for the fiscal year ended June 30, 2014, with selected comparative information from the fiscal year ended June 30, 2013. This section has been prepared by the Authority's management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Overview of Financial Results

The Authority's net position totaled $53.7 million at June 30, 2014, representing a $61.5 million decrease as compared to June 30, 2013 due to a reduction principally in net investment in capital assets and unrestricted net position. This decrease in net position for 2014 is approximately $30 million under the $91.5 million decrease in net position for 2013. This change resulted from a net effect of: reduction in operating revenues of $40 million, decrease in operating expenses of $83.5 million, decrease in depreciation and amortization of $7 million, net decrease in non-operating revenues of $26 million, decrease in non-operating expenses of $21 million and a net increase in early termination benefits expense of $8.6 million.

Net operating revenues totaled $100.1 million in 2014 and $140.2 million in 2013. These figures include $76.5 million of gross maritime revenues and $27.2 million of gross aviation revenues, reduced by $3.1 million of provision for bad debts and $461 thousands of discounts and incentives in 2014; and $84.4 million of gross maritime revenues and $70.9 million of gross aviation revenues reduced by $4.9 million bad debt provision and $10.2 million of discounts and incentives for 2013. The net decrease of $11.4 million in maritime operating revenue is primarily due to a reduction during 2014 (approximately $5 million) in the enhanced security fees that began to be charged last year as a result of the implementation of a new rapid scan services program with its new related equipment. In response to legal cases filed in opposition to these new security fees, the Federal Court ordered a prohibition from charging these fees under certain circumstances, although the essence of the security program was upheld and continues to generate revenues. The net decrease of $38.4 million in airport operating revenues resulted principally from the transfer, through the establishment of a Public Private Partnership (PPP) with Aerostar Airport Holdings, LLC (Aerostar), of the right to operate, manage, develop and maintain the Luis Muñoz Marín International Airport (LMMIA) at the end of February 2013; therefore reflecting the related LMMIA operating revenue for eight months in 2013 until such transfer versus none during 2014.

Operating expenses excluding depreciation and amortization totaled $82.6 million in 2014, which is $76.5 million lower than in 2013. This decrease was seen across all its categories: salaries and employee benefits ($19.2 million), general and administrative ($27.4 million), professional services ($24.8 million) and insurance, rent and maintenance ($5.1 million). The decrease responded principally to the reduction in the operating costs of the LMMIA, which operations were transferred to Aerostar during February 2013; therefore reflecting eight months of operating costs during 2013 versus none during 2014. Reductions in salaries and related benefits also respond to a lower employee base stemming from the early termination programs executed during previous years.

The depreciation and amortization decreased $7 million during 2014, as compared to 2013. This change resulted principally from the depreciation discontinuance, after February 2013, of the assets related to the LMMIA, as required by the applicable accounting pronouncements.

Overview of Financial Results **(Continued)**

Non-operating revenues consist of passenger facility charges ("PFC"), Federal Aviation Administration (FAA) approved programs, contributions from Commonwealth and other governmental entities, fuel flowage fees, penalties and other fees. Total non-operating revenues had a net decrease of approximately $26 million during 2014, as compared to 2013. This net decrease resulted principally from reductions in: passenger facility charges of approximately $9.6 million, contributions from Commonwealth and other governmental entities of approximately $8.2 million, federal financial assistance from the FAA of approximately $6.7 million and fuel flowage fees of approximately $1.5 million. These decreases are also caused by the transfer of the LMMIA operations to Aerostar since, after the transfer, such revenues belong to Aerostar.

Net non-operating expenses (consisting of grant subsidies and awards and interest expense) decreased by $21.1 million during 2014 as compared to 2013. The repayment during February 2013 of over $500 million in then existing debt from the proceeds received from the LMMIA transaction with Aerostar is the principal reason for the reduction of approximately $25.3 million in interest expense. This reduction was slightly offset with grants and subsidies provided to the Maritime Transportation Authority of Puerto Rico and Municipality Islands during 2014 in the amount of $4.2 million (none during 2013), as a result of resuming its federal funding through the Authority as a pass-through entity for the Federal Transit Administration.

Other Highlights

The effects of the LMMIA lease and use agreements entered into with Aerostar in February 2013, continues to be seen during 2014, as the Authority reflected eight months of operations of the LMMIA under its control during 2013 while containing none during 2014. Also, most of the $50 million fund created in 2013 from the LMMIA transaction with Aerostar, set aside to support the early retirement of certain of the Authority's employees, were ultimately disbursed during 2014, of which close to $30 million were expensed in fiscal year 2014.

Overview of the Financial Statements

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

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Statement of Net Position

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

	2014	2013 (As restated)	Change In Dollars	Change Percentage
	(In Thousands)			
Assets:				
Current assets	$ 40,633	$ 50,994	$ (10,361)	-20%
Non-current assets:				
Capital assets, net	1,131,500	1,137,533	(6,033)	-1%
Other noncurrent assets	153,164	193,740	(40,576)	-21%
Total assets	1,325,297	1,382,267	(56,970)	-4%
Deferred outflows of resources	14,623	25,997	(11,374)	-44%
Total assets and deferred outflows	$ 1,339,920	$ 1,408,264	$ (68,344)	-5%
Liabilities:				
Current liabilities	$ 160,646	$ 284,151	$ (123,505)	-43%
Non-current liabilities:				
Loans and notes payable	407,986	296,673	111,313	38%
Other non-current liabilities	112,200	92,821	19,379	21%
Total liabilities	680,832	673,645	7,187	1%
Deferred inflows of resources	605,404	619,416	(14,012)	0%
Net position:				
Net investment in capital assets	653,548	681,878	(28,330)	-4%
Restricted	87,917	47,396	40,521	85%
Unrestricted	(687,781)	(614,071)	(73,710)	12%
Total net position	53,684	115,203	(61,519)	-53%
Total liabilities, deferred inflows and net position	$ 1,339,920	$ 1,408,264	$ (68,344)	-5%

Analysis of Net Position at June 30, 2014 and 2013

The Authority's net position at June 30, 2014 includes assets of $1.33 billion, deferred outflows of resources of $14.6 million (new as a result of adopting GASB No. 65, which required a separate presentation of deferred losses on debt refunding as deferred outflows), liabilities of $680.8 million and deferred inflows of resources of $605.4 million. Net capital assets decreased by approximately $6 million from 2013, as a result of capital assets depreciation exceeding its additions by such amount. Decrease of approximately $40.6 million in other noncurrent assets is mostly attributed to the near full disbursement during 2014 of the early retirement fund of $50 million set up in 2013 from the proceeds received on the LMMIA transaction. Decrease in deferred outflows of resources of approximately $11.4 million resulted from the scheduled amortization of the year and the write-off of the portion tied to the PRIFA Series C Bonds tendered during 2014. Increases in liabilities are mostly tied to increases in amounts due to the Commonwealth Treasury Department and the Puerto Rico Retirement System for unpaid income tax withholdings and employer contributions. Deferred inflows of resources decreased principally as a result of the scheduled amortization for the year.

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Analysis of Net Position at June 30, 2014 and 2013 - Continued

Net position totaled approximately $53.7 million at June 30, 2014, a decrease of approximately $61.5 million from 2013. Net investment in capital assets, net of related debt, totaled $653.5 million at June 30, 2014, comprising the net investment in capital assets (e.g., land, buildings piers, improvements, roads and parking areas, among others), less the related outstanding indebtedness incurred to acquire those capital assets (net of the related deferred outflows of resources). Net position also contains approximately $88 million of net resources restricted principally for airport and maritime facilities construction. The residual net position consists of an unrestricted deficit of $687.8 million.

Statement of Revenues, Expenses and Change in Net Position

The change in net position is an indicator of whether the overall fiscal condition of a government has improved or worsened during the year. Following is a summary of the Statement of Revenues, Expenses and Change in Net Position for the years ended on June 30, 2014 and 2013.

	2014	2013 (As restated)	Change	
	(In Thousands)		In Dollars	Percentage
Operating revenues:				
Maritime operations	$ 74,534	$ 85,945	$ (11,411)	-13%
Airport operations	26,057	64,429	(38,372)	-60%
Less discount and incentives	(461)	(10,206)	9,745	-95%
Total operating revenues	100,130	140,168	(40,038)	-29%
Non operating revenues:				
Federal financial assistance	17,018	23,712	(6,694)	-28%
Contribution from Commonwealth of Puerto Rico	2,726	6,942	(4,216)	-61%
Contribution from Puerto Rico Tourism Company	-	4,000	(4,000)	-100%
Passenger facility charges	852	10,498	(9,646)	-92%
Fuel flowage fees	109	1,630	(1,521)	-93%
Penalties and other fees	815	718	97	13%
Total non operating revenues	21,520	47,500	(25,980)	-55%
Total revenues	121,650	187,668	(66,018)	-35%
Operating expenses:				
Salaries and employee benefits	38,732	57,886	(19,154)	-33%
General and administrative	30,377	57,733	(27,356)	-47%
Professional services	7,976	32,770	(24,794)	-76%
Insurance, rent, repairs and maintenance	5,561	10,716	(5,155)	-48%
Depreciation and amortization	28,745	35,774	(7,029)	-20%
Total operating expenses	111,391	194,879	(83,488)	-43%
Non operating expenses:				
Interest expense, net	37,347	62,653	(25,306)	-40%
Grant subsidies and awards	4,168	-	4,168	-
Total expenses	152,906	257,532	(104,626)	-41%
Decrease in net position before early termination expense	(31,256)	(69,864)	38,608	-55%
Early termination expense	(30,263)	(21,653)	(8,610)	40%
Decrease in net position	(61,519)	(91,517)	29,998	-33%
Net position, at beginning of year (as restated)	115,203	206,720	(91,517)	-44%
Net position, at end of year	$ 53,684	$ 115,203	$ (61,519)	-53%

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Analysis of Fiscal Years 2014 and 2013

Net maritime operating revenues, totaled $74.5 million compared to $85.9 million in 2013, a decrease of $11.4 million that resulted principally from a reduction during 2014 in the enhanced security fees that began to be charged last year as a result of the implementation of a new rapid scan services program with its new related equipment. In response to legal cases filed in opposition to these new security fees, the Federal Court ordered a prohibition from charging these fees under circumstances of loose cargo shipments and/or on locations where the new equipment is not installed. However, the essence of the security program was upheld and continues to generate revenues. Net airport operating revenues, totaled $26 million compared to $64.4 million in 2013, a decrease of $38.4 million, mostly resulting from the transfer of the LMMIA operations to Aerostar in February 2013; reflecting eight months of LMMIA airport operations in 2013 against none during 2014.

Non-operating revenues consisting of passenger facility charges ("PFC"), Federal Aviation Administration (FAA) approved programs, contributions from Commonwealth and other governmental entities, fuel flowage fees, penalties and other fees, sustained a decrease of approximately $26 million during 2014, which, as explained in more detail on the overview section above, was mostly caused by the transfer of the LMMIA operations to Aerostar since, after the transfer, such revenues belong to Aerostar.

Capital Activities

The Authority's net costs for capital construction projects totaled $24.3 million in 2014. Funding sources were as follows: $12.9 million was funded with federal contributions, $852 thousands was funded with PFC's; and the balance of approximately $10.5 million was funded with the Authority's own monies and financing activities.

Loan and Notes Payable

In December 2011, the Authority entered into a refinancing transaction by the issuance of Puerto Rico Infrastructure Financing Authority (PRIFA) (a component unit of the Commonwealth of Puerto Rico) bonds in a conduit debt transaction. The proceeds were used to pay various outstanding debts. The outstanding balance of such PRIFA bonds was $200.8 million at June 30, 2014.

In February 2013, the Authority entered into a lease and use agreement with Aerostar for the LMMIA premises, receiving an advance leasehold fee of $615 million. A portion of this fee was used to pay the outstanding principal and interest balance of bonds, and partial payments of principal and interest on loans and notes payable to the Government Development Bank and other private entities. The outstanding balance of the loan and notes payable amounted to $277.1 million and $234 million at June 30, 2014 and 2013, respectively. Most of this increase was caused by the drawing of a letter of credit from Government Development Bank (GDB) in the amount of $39.6 million for the mandatory tender of the PRIFA Series C2 Bonds.

The Authority issued bonds at various times for the purpose of financing the construction of certain facilities and improvements for the airports and maritime facilities. There is no outstanding balance of these bonds as of June 2014.

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Requests for Information

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

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

STATEMENT OF NET POSITION
JUNE 30, 2014

	2014 (In thousands)
Assets:	
Current assets:	
Cash - unresctricted	$ 4,611
Accounts receivable, net of allowance for doubtful accounts of $74.1 million	31,014
Prepaid expenses and other current assets	5,008
Total current assets	40,633
Non-current assets:	
Cash - restricted	32,544
Certificates of deposit - restricted	30,022
Deposits consigned in court-restricted	25,351
Due from Commonwealth of Puerto Rico - OMB	14,750
Due from other governmental entities, net	46,419
Net pension asset	4,078
Capital assets, net	1,131,500
Total non-current assets	1,284,664
Total assets	1,325,297
Deferred outflows of resources - deferred loss on refunding	14,623
Total assets and deferred outflows of resources	$ 1,339,920

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

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

STATEMENT OF NET POSITION
JUNE 30, 2014

	2014 (In thousands)
Liabilities:	
Current liabilities:	
Loan payable, current portion	$ 550
Notes payable, current portion	69,297
Accounts payable and accrued expenses	72,086
Retainage and construction costs payable	5,295
Termination benefits accrual, current portion	2,522
Tenants deposits	1,381
Interest payable	9,447
Unearned revenues, current portion	68
Total current liabilities	160,646
Non-current liabilities:	
Loan payable	200,192
Notes payable	207,794
Termination benefits accrual	26,534
Unearned revenues	1,722
Due to Commonwealth of Puerto Rico	37,483
Due to governmental entities	43,765
Other post-employment benefits obligation	2,696
Total non-current liabilities	520,186
Total liabilities	680,832
Deferred inflows of resources -	
Deferred service concession arrangement receipts	605,404
Net position:	
Net investment in capital assets	653,548
Restricted:	
Acquisition of assets	25,351
Construction	62,566
Unrestricted - deficit	(687,781)
Total net position	53,684
Total liabilities, deferred inflows of resources and net position	$ 1,339,920

Concluded

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

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

STATEMENT OF REVENUES, EXPENSES AND CHANGE IN NET POSITION
YEAR ENDED JUNE 30, 2014

	2014 (In thousands)
Operating revenues:	
Maritime operations	$ 74,534
Airport operations	26,057
Less: discount and incentives	(461)
Total operating revenues, net	100,130
Operating expenses:	
Salaries and employee benefits	38,732
General and administrative	30,377
Professional services	7,976
Insurance	3,765
Rent, repairs and maintenance	1,796
Total operating expenses	82,646
Operating income before depreciation and amortization	17,484
Depreciation and amortization	28,745
Operating loss	(11,261)
Non operating revenues (expenses):	
Federal financial assistance	17,018
Contribution from Commonwealth of Puerto Rico	2,726
Passenger facility charges	852
Fuel flowage fees	109
Penalties and other fees	815
Grant subsidies and awards	(4,168)
Interest expense	(37,410)
Interest income	63
Total non operating loss, net	(19,995)
Decrease in net position before early termination expense	(31,256)
Early termination expense	(30,263)
Decrease in net position	(61,519)
Net position, at beginning of year - as previously reported	133,316
Restatement adjustment (Note 4)	(15,319)
Effect of adoption of GASB No. 65 (Note 4)	(2,794)
Net position, at beginning of year - as restated	115,203
Net position, at end of year	$ 53,684

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

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

STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2014

	2014 (In thousands)
Cash flows from operating activities:	
Cash received from charges to customers	$ 93,712
Cash payments to suppliers for goods and services	(43,902)
Cash payments to employees for services	(93,851)
Net cash used in operating activities	(44,041)
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(24,252)
Capital contributions	15,305
Interest paid	(18,346)
Proceeds from notes payable	50,960
Repayment of loans payable	(39,600)
Principal payments on notes payable	(7,830)
Passenger facility charges received for capital expenditures	852
Net cash used in capital and related financing activities	(22,911)
Cash flows from non-capital and related financing activities:	
Penalties and other fees	815
Fuel flowage fees	109
Net change in due from (to) government agencies	17,973
Net cash provided by non-capital and related financing activities	18,897
Cash flows provided by investing activities -	
Investment in certificates of deposit	(30,022)
Interest received	63
Net cash used in investing activities	(29,959)
Net decrease in cash	(78,014)
Cash, beginning of year	115,169
Cash, end of year	$ 37,155

Continued

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

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

STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2014

		2014 (In thousands)
Reconciliation of cash:		
Unrestricted funds	$	4,611
Restricted funds:		
Construction		16,156
Employees retirement		4,257
Regional airports improvements		24,598
LMMIA transaction guarantee		15,029
Federal		27
Renewal and replacements, maintenance and others		2,499
Total restricted funds		62,566
Total cash and certificates of deposits		67,177
Less: certificates of deposit - restricted, non cash equivalents		(30,022)
Total cash	$	37,155
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$	(11,261)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Capital assets impairment		3,177
Depreciation and amortization		28,745
Amortization of deferred inflows of resources		(15,615)
Adjustment increase in net pension asset		(4,004)
Early retirement termination expense		(30,263)
Prior year restatement in retirement accrual disbursed during 2014		(15,319)
Net change in operating assets and liabilities:		
Decrease in accounts receivable		9,284
Increase in prepaid expenses and other assets		(1,124)
Decrease in accounts payable and accrued expenses		(7,787)
Decrease in tenant deposits		(18)
Increase in other employee benefits		212
Decrease in unearned revenues		(68)
Net cash used in operating activities	$	(44,041)
Non-cash capital and financing activity- capital assets additions placed in operations by Aerostar credited to deferred inflows of resources	$	1,603

Concluded

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

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1. REPORTING ENTITY

The Puerto Rico Ports Authority (the "Authority") is a component unit of the Commonwealth of Puerto Rico, (the "Commonwealth") created by Act No. 125 on May 7, 1942, as amended. The purpose of the Authority is to administer port and aviation transportation facilities of the Commonwealth and to render other related services. The Authority owns eleven airport facilities, including Luis Muñoz Marín International Airport ("LMMIA"), the main aviation port of entry into Puerto Rico, and most of government-owned maritime operations, including the Port of San Juan. The Authority's airport system consists of LMMIA, and other regional airports. Maritime operations consist principally of cargo and cruise ships with ports and docks all around Puerto Rico. See Note 21 for the Public-Private Partnership transaction regarding the administration and operations of the LMMIA (the APP or Lease and Use Agreements).

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

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

Act No. 113, approved on July 4, 2011, created a fund called the Port Authority Cruise Ships Incentives Fund. This fund receives funding from the Puerto Rico Tourism Company ("PRTC") and the Puerto Rico Office of Management and Budget ("OMB") in order to provide incentives to cruise ship companies for making Puerto Rico ports a destination for their cruise ships. During fiscal year 2014, the administration of this fund was transferred to the PRTC pursuant to Act No. 80 of July 24, 2013.

2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America, as applicable to governmental units. The Authority follows Governmental Accounting Standard Board ("GASB") pronouncements under the hierarchy established by GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements. The following is a summary of the most significant accounting policies:

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

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Cash Equivalents - The Authority considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents. The Authority's cash composition as of June 30, 2014 is disclosed in Note 5.

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

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

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

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

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

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

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

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

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

Capital assets related to the LMMIA under the APP Agreements described in Note 21 are maintained at the Authority's books and also stated at cost or at estimated historical cost. Construction in progress made by Aerostar after the closing of the APP Agreements is not recorded by the Authority while such construction is still in progress and not ready for use and operation; at completion, such constructed assets and improvements will be recognized at their corresponding fair value. The capital assets related to the APP Agreements are not being depreciated since the closing date of the APP Agreements because the APP Agreements require Aerostar to return the related LMMIA facilities to the Authority in its original or enhanced condition. Such capital assets continued to apply existing capital asset guidance, including depreciation through February 27, 2013, the closing date of the APP Agreements. The carrying amount of capital assets, excluding construction in progress, under the APP Agreements amounted to approximately $476 million at June 30, 2014. This amount includes approximately $1.6 million of improvements and construction work already completed and placed in operations by Aerostar, therefore added to the carrying amount of capital assets under the APP Agreements.

During the year ended June 30, 2014, the Authority performed an assessment of impairment on capital assets under the provisions of Statement on Governmental Accounting Standard (GASB) No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries,* which establishes that, generally, an asset is considered impaired when its service utility has declined significantly and unexpectedly, and the event or change in circumstances is outside the normal life cycle of the asset. Management is then required to determine whether impairment of an asset has occurred. Impaired capital assets that will no longer be used by the Authority should be reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by the Authority should be measured using the method that best reflects the diminished service utility of the capital asset. Impairment of capital assets with physical damage generally should be measured using a restoration cost approach, an approach that uses the estimated cost to restore the capital asset to identify the portion of the historical cost of the capital asset that should be written off. During 2014, management identified certain assets as fully impaired and wrote-off accordingly such assets' carrying value amounting to $3.2 million. Such impairment loss is presented within general and administrative expenses in the accompanying statement of revenues, expenses and change in net position.

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

In addition, GASB Statement No. 49, "*Accounting and Financial Reporting for Pollution Remediation Obligations*," applicable for periods beginning after December 15, 2007, addresses accounting and financial reporting principles for pollution (including contamination) remediation obligations which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the statement excludes pollution prevention or control obligations with respect to current obligations, and future pollution activities that are required upon retirement of an asset, such as post-closure care. As of June 30, 2014, the Authority maintains an environmental reserve of approximately $3 million, which in the opinion of management is adequate to cover the contingency exposure, if any. Such reserve is included as part of accounts payable and other accrued liabilities in the accompanying statement of net position. In establishing such reserve, management has evaluated its tenants' responsibilities in environmental and pollution exposures.

Claims and Judgments - The estimated amount of the liability for claims and judgments is recorded on the accompanying statement of net position based on the Authority's evaluation of the probability of an unfavorable outcome in the litigation of such claims and judgments. The Authority consults with legal counsel upon determining whether an unfavorable outcome is expected. Refer to disclosures included in Note 16.

Compensated Absences - Employees earn vacation benefits at a rate of 30 days per year, which is the maximum permissible accumulation. Employees accumulate sick leave at the rate of 20 days per year. Maximum permissible accumulation for sick leave is 60 days for managerial and clerical employees of which the excess was normally paid within the next fiscal year. Union employees were paid for accumulations over 26 days within the next fiscal year. However, effective with the approval of Act No. 66 of June 17, 2014, known as the Fiscal Operation and Sustainability Act, such excess will cease to be paid to employees. The Authority records as a liability and as an expense the vested accumulated vacation and sick leave as benefits accrued to employees. Compensated absences as of June 30, 2014, amounted to approximately $6.4 million and are included as a component of accounts payable and accrued expenses in the accompanying statement of net position.

Termination Benefits – The Authority accounts for termination benefits in accordance with the provisions of GASB No. 47, *Accounting for Termination Benefits,* which indicates that employers should recognize a liability and expense for *voluntary* termination benefits when the offer is accepted and the amount can be estimated. A liability and expense for *involuntary* termination benefits should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees, and the amount can be estimated. Refer to disclosure included in Note 14.

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

Other Retirement Benefits - The Authority accounts for pension costs under the provisions of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*. This statement establishes standards for the measurement, recognition and display of pension expense and related liabilities in financial statements of state and local governmental employers.

Derivative Instruments - The Authority follows GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* ("GASB 53"). This Statement enhances the usefulness and comparability of derivative instrument information reported by state and local governments by providing a comprehensive framework for the recognition, measurement, and disclosure of derivative instrument transactions.

Derivative instruments such as interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), swaps, forward contracts, and futures contracts are entered into by governments as investments; as hedges of identified financial risks associated with assets or liabilities, or expected transactions (i.e., hedge able items) to lower the costs of borrowings, to effectively fix cash flows or synthetically fix prices, or to offset the changes in fair value of hedge able items. At June 30, 2014, the Authority has no derivative instruments.

Deferred Outflow of Resources – The deferred outflow of resources represent the consumption of net assets by the Authority that is applicable to a future reporting period. Deferred outflows of resources for the Authority is specifically related to a refunding loss associated to an issuance of PRIFA bonds and a swap agreement cancellation. This refunding loss is being amortized over the life of the PRIFA bonds that remain outstanding. The amortized amount during fiscal year 2014 is reported as a component of interest expense in the accompanying statement of revenues, expenses and change in net position.

Deferred Inflows of Resources – Deferred inflows of resources represent the acquisition of net assets by the Authority that is applicable to a future reporting period. In relation to the APP Agreements described in Note 21, on February 27, 2013, the Authority received an upfront fee of $615 million, the promise of annual payments of $2.5 million for the next five years, present valued at approximately $10.5 million; and also recognized a contractual obligation of $3.068 million to perform certain capital improvements. These resources were received in exchange for awarding Aerostar the right to operate, manage, maintain, develop and rehabilitate the LMMIA for a term of 40 years. Upfront fee is considered a deferred inflow of resources, which is recognized into revenue under the straight-line method over the APP Agreements term of 40 years. The amount recognized into revenue during fiscal year 2014 amounted to approximately

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Deferred Inflows of Resources- Continued

$15.6 million and is recognized within operating revenues-airport in the accompanying statement of revenues, expenses and change in net position.

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

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

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

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

As of June 30, 2014, the reconciliation of net position was as follows:

Net capital assets	$	1,131,500
Liabilities directly attributable to capital assets:		
Loan payable		(200,742)
Notes payable		(277,091)
Retainage payable to contractors		(5,295)
Accrued interest		(9,447)
Deferred outflows of resources - deferred loss on refunding		14,623
Net investment in capital assets	$	653,548

Restricted funds, including certificates of deposit	$	62,566
Deposit consigned with court restricted for capital asset		25,351
Restricted net position	$	87,917

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

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

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

New Accounting Principles Adopted - The following new accounting principles were adopted by the Authority effective July 1, 2013:

- GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. For a detailed description of the nature of this Statement and the effect of its adoption on July 1, 2013, please refer to Note 4.
- GASB Statement No. 66, *Technical Corrections 2012*. The objective of this Statement was to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This Statement amended Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type. As a result, governments should base their decisions about fund type classification on the nature of the activity to be reported, as required in Statement No. 54 and Statement No. 34, *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments*. This Statement also amended Statement No. 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. These changes clarify how to apply Statement No. 13, *Accounting for Operating Leases with Scheduled Rent Increases*, and result in guidance that is consistent with the requirements in Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, respectively. The adoption of this Statement on July 1, 2013, had no impact in the Authority's financial reporting.

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement resulted from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This Statement replaced the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures,* as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements No. 25 and No. 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions. The major fundamental change, among others related to the application and determination of certain measurement assumptions in valuing pension plans, is switching from the existing "funding-based" accounting model, where currently the Annual Required Contribution (ARC) is compared to the actual payments made and that difference determines the Net Pension Obligation; to an "accrual basis" model, where the Total Pension Obligation (Actuarially determined) is compared to the Net Plan Position (or assets) and the difference represents the Net Pension Liability. This particular Statement affects the reporting of the three Retirement Systems of the Commonwealth, not to the Authority or any of the Commonwealth's Component Units. The impact of this Statement will be establishing its new Net Pension Liability, to be disclosed for the three Retirement Systems of the Commonwealth, to an amount resembling the existing actuarial deficiency in the aforementioned Retirement Systems, which might exceed approximately $36 billion, at June 30, 2014.

- GASB Statement No. 70, Accounting and Financial Reporting for Nonexchange Financial *Guarantees*. The objective of this Statement is to require a governmental entity guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement. Certain qualitative factors should be considered when evaluating the likelihood of a guaranty payment, such as: initiation of a bankruptcy process, breach of a debt contract in relation to the guaranteed obligation and indications of significant financial difficulty to pay agents or trustees. This Statement had no impact on the Authority, as the Authority currently has no financial guarantees outstanding at June 30, 2014.

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Future Adoption of Accounting Principles - The GASB has issued the following accounting principles that have effective dates for the Authority after its June 30, 2014 year ended:

- GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers,* as well as the requirements of Statement No. 50, *Pension Disclosures,* as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements No. 27 and No. 50 remain applicable for pensions that are not covered by the scope of this Statement. This Statement will bring the effect of Statement No. 67 summarized in the previous paragraph, into the accounting records of the individual agencies, component units and municipalities, whose employees participate in the Retirement Systems.

  The Authority, as well as the other component units of the Commonwealth and the municipalities, are considered "cost-sharing" employers of the Retirement Systems; therefore, the Authority would report its allocated share of the Commonwealth's resulting Net Pension Liability, pension expense and corresponding deferred inflows and outflows of resources from Statement No. 67 as follows:

  - ✓ Based on the Authority's individual proportion to the collective net pension liability of all the governments participating.
  - ✓ The proportion should be consistent with the method used to assess contributions (percentage of payroll). The use of the Authority's long term expected contribution effort to Retirement Systems divided by those of all governments in the plan, is encouraged.

  This Statement is not effective until the Authority's fiscal year 2015. The Commonwealth and the Retirement Systems are in the process of evaluating the exact impact of this Statement on its agencies and component units and also on the municipalities of the Commonwealth. The information to adopt this Statement will be based on the new actuarial reports to be prepared under the new Statement No. 67 described on the previous page.

- GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*. This Statement establishes accounting and financial reporting principles related to government combinations and disposals of government operations. As used in this Statement, the term government combinations includes a variety of transactions referred to as mergers, acquisitions, and transfer of operations. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.

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2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. This Statement amends paragraph 137 of Statement No. 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement No. 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts. The provisions of this Statement should be applied simultaneously with the provisions of Statement No. 68.

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

Over the past years since 2010, the Authority has seen its net position decrease from $337 million at June 30, 2010 to the current level of $54 million at June 30, 2014. In order to start reversing this trend and instill some stability in the Authority's operations, management entered in 2013 into the LMMIA lease and use agreements, as further described in Note 21. This transaction became the centerpiece strategy around which certain cost cutting measures and revenue-base enhancing activities for regional airports and maritime operations have been implemented, while others are in progress, all of which are expected to improve the Authority's financial condition and refocus the objectives of the Authority into the future.

As further described in Notes 10, 11 and 21, the Authority refinanced during fiscal year 2012 the majority of its long-term debt through a Puerto Rico Infrastructure Financing Authority's (PRIFA) conduit debt issuance of $678.4 million, in anticipation of the LMMIA lease and use agreements. The lease and use agreements involving the LMMIA generated an upfront leasehold fee of $615 million for the Authority, $500 million of which were used to cancel and fully redeem certain outstanding debt and related interests, relieving the Authority from the corresponding applicable debt service requirements. That is, the Authority's then existing debt was reduced by more than half as a result of the LMMIA lease and use agreements. Consequently, interest expense has already seen a reduction from approximately $63 million in 2013 to approximately $37 million in 2014. Another $50 million from the aforementioned leasehold fee were reserved and set aside for the early termination of several employees, commencing effective June 30 and July 15, 2013, which provided payroll savings from fiscal year 2014 going forward. For instance, basic salary expenses have gone down from approximately $27 million in 2013 to approximately $16 million during 2014; while total salaries expense including benefits and bonuses have decreased from approximately $58 million to $39 million, as a result of the various early retirement plans adopted since 2011. In addition, $25 million were also set aside for improvements to the regional airports in order to attract visitors and increase demand and revenues. One of such improvements will eventually cover the Aguadilla regional airport for the establishment of the upcoming Lufthansa's central operations of its fleet maintenance hub. For instance, since the closing of the LMMIA lease and use agreements, expenditures for the improvements and expansion of regional airports have created an additional rental revenue base at these airports that is expected to materialize into an increase in rental revenue of approximately $1.3 million or 32% for fiscal year 2015, even though not all projects have been completed yet. Future completion of the established development plans for the regional airports is expected to add more space rental room opportunities and increase passenger flow.

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3. FINANCIAL CONDITION AND MANAGEMENT PLANS – LIQUIDITY RISKS AND UNCERTAINTIES - Continued

A valuation for all properties owed by the Authority is also being prepared in order to verify (1) if the rent collected for all lease property is in accordance with the market value and (2) if the unused property is tagged at the correct market value in the eventuality of a potential sale.

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

Management of the Authority has also reacted responsibly with respect to its delinquent obligations by actively pursuing feasible payment plans for balances due to the Commonwealth's Treasury Department and the Puerto Rico Retirement Systems (see Note 7), as well as with the government utilities and most suppliers. These special payment arrangements have maintained an organized and steady cash flow strategy for the Authority while meeting its obligations. In relation to the lines of credit owed to GDB described in Note 11, most of them remain unpaid since the closing of the LMMIA lease and use agreements and the drawings of the existing GDB Letters of Credit for the PRIFA Series A and C Bonds. However, the Authority continues in conversations with GDB for the prospects of entering into restructuring or payment plan agreements for these balances due. These conversations are taking place in connection with the provisions of Act No. 24 of February 13, 2014, which calls for more prudent lending practices to be undertaken by GDB, supplemented by a stricter monitoring and oversight of funds lent to Commonwealth's agencies and instrumentalities. Among the many provisions of this Act, one provides for the potential restructuring of certain GDB's lines of credit beginning on 2017, which might include those provided to the Authority. Some of these restructuring plans could be potentially backed by the guaranty of the Commonwealth, according to Act No. 24, which increases from $550 million to $2 billion the amount of the GDB obligations that can be guaranteed by the full faith and credit of the Commonwealth to provide the GDB with greater flexibility in its role of granting interim financing to public corporations and agencies.

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3. FINANCIAL CONDITION AND MANAGEMENT PLANS – LIQUIDITY RISKS AND UNCERTAINTIES - Continued

It is also noteworthy to point out that of the approximately $62 million decrease in net position sustained in 2014, approximately $30 million are attributed to one time charges of early termination restructuring events that should not recur and approximately $27 million are attributed to net depreciation, amortization and impairment charges (including approximately $11.4 million in deferred refunding losses amortization) that do not consume cash flows. Therefore, the real results of 2014 might have otherwise show a near breakeven in operating cash flows, and it is management's belief that with the action plans referred to above, the additional savings expected from the execution of the Act No. 66 measures and potential additional revenue base at the regional airports, complemented with a more thoroughly monitored cash flow management techniques and continued feasible payment restructuring plans, the Authority would be able to continue operating satisfactorily and meeting its obligations as they become due.

The Authority's ability to reverse the loss trends of the past years and successfully execute the action plans referred to above, depend on a number of factors, some of which are not wholly within its control, including the performance of the Commonwealth's economy, the materialization of the regional airports expanded revenue base, the Authority's ability to reduce and control its costs and GDB's selection of the lines of credit to be restructured pursuant Act No. 24.

4. RESTATEMENT OF NET POSITION

During the year ended June 30, 2014, the Authority adjusted the beginning net position to reflect the effect of $15.3 million of voluntary termination expense incurred by certain employees in the prior year but that had inadvertently remained unaccrued.

Effective July 1, 2013, the Authority also adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities and viceversa. This Statement also requires the write-off of any existing deferred debt issuance costs at the time of adoption against beginning net position, and prospectively, any new debt issue costs on bonds or debt issuance will require immediate expensing. At transition, the impact of Statement No. 65 at the Authority was as follows:

Debt Issuance Costs— The Authority charged-off its existing unamortized debt issuance costs of approximately $2.8 million against its beginning net position.

Refunding of Bonds—The unamortized deferred loss on refunding bonds is now required to be presented as a deferred outflow of resources. The Authority reclassified the beginning unamortized deferred loss on refunding bonds of approximately $26 million as a deferred outflow of resources, which had previously been reported as a reduction of debt.

4. RESTATEMENT OF NET POSITION - Continued

The Authority also made restatements among the beginning net position classifications at July 1, 2013, as a result of having attributed incorrectly $532 million of the $619 million of deferred inflows resulting from the LMMIA lease and use agreements, to the net investment in capital asset category when such amount should have been presented within the unrestricted net position category. The total net position, though, sustained no restatements as a result of this adjustment.

5. CASH AND CERTIFICATES OF DEPOSIT

At June 30, 2014, cash amounted to approximately $37.2 million. There were no cash equivalents at June 30, 2014. Cash balances are detailed as follows:

	2014 (in thousands)
Restricted funds:	
For construction	$ 16,156
Federal	27
Renewal and replacements, maintenance and other	2,500
For employees retirement	4,257
For regional airports improvement	9,586
As guaranty fund for LMMIA transaction	18
Total restricted	32,544
Unrestricted fund	4,611
Total cash	$ 37,155

At June 30, 2014, the Authority also had two (2) certificates of deposit at GDB amounting to $30,022, in the aggregate. These certificates of deposit, bear interest at 0.9%, are restricted for regional airports improvements ($15,012) and as a guaranty fund for the LMMIA transaction ($15,010), and mature on December 17, 2014 and May 20, 2015, respectively.

The Authority is restricted by law to deposit funds only in institutions approved by the Puerto Rico Treasury Department, and such deposits are required to be kept in separate accounts in the name of the Authority.

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

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5. CASH AND CERTIFICATES OF DEPOSIT - Continued

Custodial Credit Risk

For deposits, custodial credit risk is the risk that in the event of bank failure, the Authority's deposits may not be recovered by the Authority. However, under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. The bank balance and carrying amount of the Authority's accounts with commercial banks at June 30, 2014, amounted to $10.2 million and $8.5 million, respectively.

As of June 30, 2014, the Authority's custodial credit risk was approximately $58.6 million, which is the bank balance of cash and certificates of deposit with GDB and Economic Development Bank for Puerto Rico ("EDB"). These deposits are exempt from the collateral requirements established by the Commonwealth.

6. DEPOSITS CONSIGNED IN COURT - RESTRICTED

During November 2011, pursuant the objectives of the LMMIA Project, the Authority entered into certain expropriations proceedings through the Puerto Rico First Instance Court (the "Court"), to acquire certain properties and concessions owned by third parties within the LMMIA complex. In connection with such proceedings, on December 27, 2011, the Authority obtained a $30 million non-revolving credit facility with the GDB, out of which $25.4 million were consigned with the Court to start the expropriation process (this facility is known as the Caribbean Airport Facilities). The credit facility was fully repaid with the proceeds from the LMMIA concession agreement. At June 30, 2014, the $25.4 million deposited in Court is presented as restricted in a separate line item in the accompanying statement of net position.

7. DUE FROM/DUE TO GOVERNMENTAL ENTITIES

Due from governmental entities as of June 30, 2014 consists of:

	(in thousands)
Office of Management and Budget	$ 14,750

	(in thousands)
Maritime Transportation Authority of Puerto Rico and Municipality Islands (MTA)	$ 38,545
Puerto Rico Highway and Transportation Authority (PRHTA)	6,088
Puerto Rico Tourism Company	1,515
Federal Aviation Administration	271
Total	$ 46,419

Office of Management and Budget ("OMB") - Balance due from the OMB relates to $14.7 million incentives given by the Authority to certain cruise lines, which should be reimbursed by the OMB. The balance does not bear interest and has no formal repayment terms, since the terms and conditions have not been established. Authority's management is working with the government entity for the collection of this outstanding balance.

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7. DUE FROM/DUE TO GOVERNMENTAL ENTITIES - Continued

Maritime Transportation Authority of PR and Municipality Islands - Balance due from Maritime Transportation Authority of PR and Municipality Islands (MTA) of $38.5 million mainly relates to expenses incurred by the Authority, such as payroll, on behalf of the MTA from 2000 to 2006. The balance does not bear interest and has no formal repayment terms at June 30, 2014. However, the Authority and MTA are currently involved in the process of executing a repayment plan for this balance, which will entail the combination of various transactions and administrative proceedings that would go in line with the already approved restructuring and merger of MTA's operations into the new *Integrated Transport Authority of Puerto Rico,* created by Act No. 123 of August, 3, 2014.

Puerto Rico Highway and Transportation Authority ("PRHTA") - Balance due from PRHTA relates to $6 million mainly associated with the rental of a hangar, a warehouse and land for which there are written agreements. These balances do not bear interest and have no formal repayment terms, since the terms and conditions have not been established. Authority's management is working with the government entity for the collection of this outstanding balance.

Puerto Rico Tourism Company ("PRTC") - Amount due from PRTC relates principally to a remaining balance from PRTC's contribution for the Special Incentive Funds of Cruise Ships under Act 113 of 2011.

Federal Aviation Administration ("FAA") - Amounts due from the FAA of approximately $270.4 thousand as of June 30, 2014 consisted of pending reimbursements to be received related to certain capital projects.

Due to governmental entities as of June 30, 2014, consists of:

	2014 (In thousands)
Commonwealth of Puerto Rico	$ 37,483
Due to other governmental entities:	
Puerto Rico Electric Power Authority ("PREPA")	24,760
Puerto Rico Aqueduct and Sewer Authority ("PRASA")	12,868
State Insurance Fund Corporation ("SIFC")	4,181
Puerto Rico Highway and Transportation Authority	1,833
Others	123
	$ 43,765

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7. DUE FROM/DUE TO GOVERNMENTAL ENTITIES - Continued

Commonwealth of Puerto Rico **-** Balance due to the Commonwealth of Puerto Rico consists mainly of public insurance amounting to $19 million, income tax withheld amounting to $3.5 million owed to the Treasury Department, and $12.5 million to the Puerto Rico Retirement System ("PRRS") for employer contributions not fully paid since fiscal year 2012. The balances owed to the Treasury Department for the unpaid employer contribution and public insurance charges do not bear interest and have no formal repayment terms; however, the Authority is currently in conversations to enter into a restructuring or payment arrangement plan for these balances. During August 2014, the Authority and PRRS approved a new payment plan that provides for consecutive monthly payments ranging from $100,000 to $300,000 during the next 47 months and a final payment of $2.374 million during the 48th month. Such plan was entered into upon an initial payment of approximately $1.3 million that reduced the balance owed to PRRS to $11.3 million from the $12.5 million referred to above.

***Due to other governmental entitie*s** balances consist mainly of utilities or services provided by such entities.

The non-current amounts due to Commonwealth of Puerto Rico and due to other governmental entities activity for the year ended June 30, 2014, was as follows (in thousands):

	2013	Charges	Payments	2014
Due to Commonwealth of PR	$ 25,804	$ 17,383	$ (5,704)	$ 37,483
Due to other governmental entities	36,200	10,314	(2,749)	43,765
	$ 62,004	$ 27,697	$ (8,453)	$ 81,248

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8. CAPITAL ASSETS

The following schedule summarizes the capital assets held by the Authority as of June 30, 2014 (in thousands):

	Balance June 30, 2013	Increases	Decreases	Balance June 30, 2014
Land and land improvements	$ 292,918	$ 4,140	$ (2,884)	$ 294,174
Construction in progress	134,102	51,430	(52,223)	133,309
Total assets not being depreciated	427,020	55,570	(55,107)	427,483
Assets being depreciated:				
Building, piers, improvements and structures	829,581	36,435	(21,767)	844,249
Other infrastructure	176,230	4,747	(2,379)	178,598
Roads and parking areas	354,125	7,986	-	362,111
Machinery, furniture and equipment	115,400	379	(2,379)	113,400
Automobiles and service vehicles	11,400	31	-	11,431
Infrastructure Master Plans	12,442	-	(821)	11,621
Total	1,499,178	49,578	(27,346)	1,521,410
Less accumulated depreciation and amortization	(788,665)	(28,745)	17	(817,393)
Net total assets being depreciated	710,513	20,833	(27,329)	704,017
Total capital assets, net	$ 1,137,533	$ 76,403	$ (82,436)	$ 1,131,500

Total capital assets presented in the statement of net position and in this note are segregated as follows:

Capital assets - net (excluding assets under concession agreement)	$ 655,314
Capital assets under service concession agreement	476,186
Total	$ 1,131,500

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9. UNEARNED REVENUES

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

Unearned revenues balance at June 30, 2014, consists of:

	2014 (In thousands)
Carrying amount of unamortized portion of construction costs, amortized by equivalent credits to the minimum fixed rental through December 2019	$ 1,790
Less: current portion	(68)
Unearned revenues, long-term	$ 1,722

10. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS)

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

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

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

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10. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS) – Continued

A refunding loss of $61.8 million resulted from this transaction, attributed to the write-off of the then existing deferred outflow for the same amount associated with a swap agreement cancellation. The notional amount of the swap agreement cancelled ($396 million) exceeded the outstanding principal balance of a hedged Wells Fargo loan being cancelled ($363.9 million); therefore, the proportion of that excess amount (unhedging portion) applied to the resulting refunding loss was recognized as a realized loss of approximately $5 million, which was charged to the result of operations for fiscal year 2012. The rest of the refunding loss ($56.8 million) was deferred and is amortized into interest expense over the life of the PRIFA Bonds based on the effective interest method. As of June 30, 2014, the unamortized deferred loss on refunding balance was $14.6 million and is included as deferred outflows of resources in the accompanying statement of net position, as required by GASB No 65.

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

The Loan Agreement is payable solely from revenues of the Authority, such as all rates, rents, fees, charges and other income and receipts. The Loan Agreement is also secured by drawings from two irrevocable transferable direct-pay letters of credit issued by GDB (collectively referred as the GDB Letters of Credit). One letter of credit is for the maximum amount of $543.1 million to cover ultimately the PRIFA Series 2011 A and B Bonds, while the second letter of credit is for the maximum amount of $138.3 million to cover ultimately the PRIFA Series 2011 C Bonds. These letters of credit carry an annual fee of 1% on their outstanding amounts, payable semiannually, commencing on December 15, 2011. The Authority was charged for $3.7 million as fees related to these letters of credit for the year ended June 30, 2014.

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10. LOAN AND TRUST AGREEMENT (THE PRIFA BONDS) - Continued

During fiscal year 2013, the Authority used $266.9 million from the proceeds of the APP Agreement (described in Note 21) and drew $74.6 million from the GDB Letters of Credit for the full redemption of PRIFA Series A Bonds. In addition, $96.8 million from the GDB Letters of Credit were also drawn for the mandatory partial redemption of a portion of the PRIFA Bonds Series C. Later during fiscal year 2014, the remaining balance of $39.6 million of PRIFA Bonds Series C was also repaid through the use of the corresponding GDB Letters of Credit. By having drawn on the GDB Letters of Credit, new notes payable to GDB have been issued and included in the accompanying statement of net position. See description of these notes payable to GDB in Note 11.

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

Fiscal Year Ending June 30,	Principal	Interest	Total
2015	$ 550	$ 10,315	$ 10,865
2016	1,650	10,304	11,954
2017	2,055	10,221	12,276
2018	1,125	10,160	11,285
2019	1,100	10,104	11,204
2020 through 2024	30,620	48,678	79,298
2025 through 2027	155,730	25,016	180,746
	192,830	$ 124,798	$ 317,628
Add: unamortized premium	7,912		
	$ 200,742		

At June 30, 2014, the loans principal outstanding consist of the PRIFA Bonds Series 2011B amounting to $192.8 million.

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11. NOTES PAYABLE

Notes payable as of June 30, 2014 consist of (in thousands):

	Amount
Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series C1 Bonds, converted into 5 years term loan payable in monthly principal installments of $1,608 million, bearing interest at prime rate plus 150 basis points with a minimum rate of 6%, due in February 2019.	$ 96,785
Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series A Bonds, converted into 5 years term loan payable in monthly principal installments of $1,243 million, bearing interest at prime rate plus 150 basis points with a minimum rate of 6%, due in December 2018.	74,589
Borrowing under line of credit agreement with GDB, bearing interest at 90 days LIBOR rate plus 50 basis points with a minimum rate of 6%, due in June 2023. Collateralized by the San Juan Water Front (SJWF) Proyect.	44,000
Borrowing under line of credit agreement with GDB, used for mandatory tender of PRIFA Series C2 Bonds, converted into 5 years term loan payable in monthly principal installments of $658 thousand, bearing interest at prime rate plus 150 basis points with a minimum rate of 6% due in March 2019.	39,600
Promissory note payable to Carnival Corporation, bearing interest at 7.50%, due through May 2024. Collateralized by tariff income from Carnival Corporation.	9,109
Borrowing under line of credit agreement with GDB, bearing interest at prime rate plus 150 basis points (4.75% at June 30, 2014), due in November 2014; used for deposit in the Special Incentives Fund administered by PRIDCO; collateralized with funds maintained at GDB for improvements to regional airports.	8,000
Promissory note payable to International Shipping, bearing and interest at 6.00%, due through December 2017. Collateralized by rent income from International Shipping.	2,675
Promissory note payable to First Insurance Funding for insurance premium financed, bearing interest at 4.75%, due through December 2014.	1,571
Line of credit of $5 million with Puerto Rico Convention Center District Authority; bearing interest at 5%, due in April 2016; collateralized with certain Authority's capital assets, located at Yabucoa, Puerto Rico.	762
Total notes payable	277,091
Less current portion	(69,297)
Long-term portion	$207,794

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11. NOTES PAYABLE - Continued

Government Development Bank (GDB)

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

In December 2013, the line of credit of $74.6 million payable to GDB, used for the mandatory partial tender of the PRIFA Series A Bonds, was converted into a five (5) years term loan. The term loan is to be repaid by the Authority in monthly principal payments of approximately $1.243 million, plus interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 6%. The outstanding balance of the term loan at June 30, 2014 is $74.6 million. The Authority has not made the scheduled principal and interest payments since the inception of this credit facility and is currently in conversations with GDB pursuing a possible restructuring plan.

On July 1, 2008, the Authority entered into a $180 million line of credit for the development of the San Juan Water Front (SJWF) project (now Bahía Urbana) authorized by an executive order signed on February 20, 2008. Borrowings under this line of credit bear interest at 90 day Libor plus 50 basis points with a minimum rate of 6%, due through June 20, 2023. This line of credit is collateralized with the SJWF project. At June 30, 2014, $44 million were outstanding.

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

In May 2013, the Authority entered into an $8 million line of credit with GDB, the proceeds of which were deposited in the Special Incentives Fund administered by PRIDCO, for the development maintenance, repairs and overhaul operations at the regional airport of Aguadilla, Puerto Rico. The line of credit is for a term of two (2) years, bearing interest at the rate of 150 basis points over the prevailing prime rate, but never to be less than 6%; and it is collateralized with funds deposited at GDB for the development of improvements to the regional airports, stemming from the APP Agreement described in Note 21.

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11. NOTES PAYABLE - Continued

Carnival Cruise Lines

On June 7, 2001, the Authority entered into a Master Development Agreement with Carnival Corporation for the performance of certain improvements to Terminal 4 of the Port of San Juan. Total financed costs amounted to approximately $13.5 million, and will be payable to Carnival by 240 monthly deductions of $108,735 (including principal and interest at 7.50%) from the tariffs payable from Carnival to the Authority, commencing in May 2004, until May 2024. As of June 30, 2014, such note had an outstanding balance of $9.1 million.

International Shipping

During November 2011, the Authority entered into an Agreement with International Shipping for the performance of certain improvements to piers M, N and O. Total financed costs amounted to approximately $5.4 million, bearing an interest of 6% and payable to International Shipping by seven monthly payments of $36,000, commencing on December 31, 2011; followed by 70 consecutive monthly payments (including interests) of $71,000 and a final payment of $9,908. Payment will be made through the rent income from International Shipping. As of June 30, 2014, the outstanding balance of the note was $2.7 million.

First Insurance Funding

This note payable is related to the financing of certain Authority's insurance policies. The note payable has an interest rate of 4.75%, and requires monthly payments of $265.5 thousand through December 2014. As of June 30, 2014, the note payable had an outstanding balance of $1.6 million.

Puerto Rico Convention Center District Authority

On April 28, 2014, the Authority and the Puerto Rico Convention Center District Authority (PRCCDA) entered into an Interagency Credit Agreement where PRCCDA granted a loan of up to $5 million to the Authority to finance the remodeling of certain piers of the port of San Juan, mainly Pier No. 3. The loan, payable in full on April 28, 2016, bears an interest rate of 5% payable on a monthly basis. These payments will be made from the additional maritime income expected from this remodeling. This loan is collateralized with certain Authority's property located in Yabucoa, Puerto Rico carrying an estimated value of $10.5 million.

Summarized Notes Payables Activity

The summarized notes payable activity for the fiscal year ended June 30, 2014, was as follows (in thousands):

	June 30, 2013	Borrowings	Payments	June 30, 2014
Notes payable	$ 233,961	$ 50,960	$ (7,830)	$ 277,091

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11. NOTES PAYABLE - Continued

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

Fiscal Year Ending June 30,	Principal	Interest	Total
2015	$ 69,297	$ 23,535	$ 92,832
2016	44,323	11,385	55,708
2017	43,662	8,720	52,382
2018	43,339	6,091	49,430
2019	27,118	3,645	30,763
2020 through 2024	49,352	11,623	60,975
	$ 277,091	$ 64,999	$ 342,090

12. SPECIAL FACILITY REVENUE BONDS

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

Pursuant to the Special Facilities Agreements between the Authority and American, American has agreed to pay amounts sufficient to cover the principal of and premium, if any, and interest on the above bonds. The bonds are not collateralized by any property, but are payable solely from certain pledged payments by American under the Special Facilities Agreements or by AMR Corporation under its unconditional guarantee. Payments under the Special Facility Revenue Bond remain current at June 30, 2014.

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13. OTHER POST-EMPLOYMENT BENEFITS OBLIGATION

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

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

Plan Description

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

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

Funding Policy

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

Annual OPEB cost and net OPEB obligation

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

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13. OTHER POST-EMPLOYMENT BENEFITS OBLIGATION - Continued

The following table shows the Authority's annual OPEB cost for the year ended June 30, 2014, the amount actually contributed to the Plan and the change in the Authority's net OPEB obligation to the Plan at June 30, 2014:

	June 30, 2014 (In thousands)
Annual required contribution ("ARC")	$ 1,639
Interest on the net OPEB obligation	175
Adjustments to the ARC	(247)
Annual OPEB cost	1,567
Authority's contribution	(5,352)
Decrease in net OPEB obligation	(3,785)
Net OPEB obligation, beginning of fiscal year	6,481
Net OPEB obligation, end of fiscal year	$ 2,696

As of June 30, 2014, the actuarial accrued liability for benefits amounted to $12.9 million, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the Plan) was $16.2 million during the year ended June 30, 2014, and the ratio of the unfunded actuarial accrued liability to the covered payroll was 79.6%.

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

Methods and Assumptions

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

The valuation date was July 1, 2014, and the Projected Unit Credit Cost Method was used. The actuarial assumptions were based on a set of assumptions supplied by the Authority. Turnover rates were based on service and age-related turnover. A discount rate of 6.5% was used. This rate is the best actuarial estimate of expected long-term experience and is in accordance with guidelines for selection of these rates under GASB No. 45. The healthcare trend rates are based on the actuarial knowledge of the general healthcare environment and the specific coverage offered by the Authority.

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14. TERMINATION BENEFITS

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

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

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

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

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

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

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

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14. TERMINATION BENEFITS - Continued

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

At June 30, 2014, the present value of future incentive payments reported as a liability amounted to approximately $29 million. Total expense recorded for the year ended June 30, 2014, for future incentive payments amounted to $1.7 million, presented as early termination expenses in the statement of revenues, expenses and changes in net position. The total aggregate liability of the program as of June 30, 2014 amounted to $29 million, of which $2.5 million should be funded during the next fiscal year. The long-term portion of the early termination obligation amounted to $26.5 million. Such amounts are disclosed respectively, as short-term and long-term liabilities in the accompanying statement of net position.

15. RETIREMENT PLANS

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

a. Defined Benefit Program

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

The Defined Benefit Program provides retirement, death, and disability benefits pursuant to legislation enacted by the Legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after 10 years of plan participation. Disability benefits are available to members for occupational and no occupational disabilities. However, a member must have at least 10 years of service to receive no occupational disability benefits.

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15. RETIREMENT PLANS - Continued

a. Defined Benefit Program -Continued

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

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

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

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

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

b. System 2000 Program

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

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

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15. RETIREMENT PLANS - Continued

b. System 2000 Program -Continued

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

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

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

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

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

c. Defined Contribution Hybrid Program

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

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15. RETIREMENT PLANS - Continued

c. Defined Contribution Hybrid Program -Continued

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

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

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

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

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15. RETIREMENT PLANS - Continued

c. Defined Contribution Hybrid Program -Continued

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

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

For the year ended June 30, 2014, the Authority was required to contribute 12.275% of each participant's gross salary under the different benefit structures. The Retirement System will use these contributions to increase its level of assets and to reduce the actuarial deficit. Beginning on July 1, 2013, and up until June 30, 2016, the employer's contribution rate shall be annually increased by one percent (1%). Beginning July 1, 2016, and up until June 30, 2021, the employer's contribution rate that is in effect on June 30 of every year shall be annually increased on every successive July 1 by one point twenty-five percent (1.25%).

Total employee contributions for the defined benefit pension plan, the defined contribution plan and the defined contribution hybrid program during the year ended June 30, 2014, amounted to approximately $18 thousands, $19 thousands and $2.2 million, respectively. The Authority's contributions (either paid or accrued) during the year ended June 30, 2014, 2013 and 2012 amounted to approximately $1.1 million, $7.4 million, and $6.6 million, respectively. These amounts represented 100% of the required contribution for the corresponding year. Total payroll subjected to retirement contributions amounted to approximately $16 million for the year ended June 30, 2014. Individual information for each option is not available since the allocation is performed by the Retirement System itself.

Additional information on the Retirement System is provided on its stand-alone financial statements for the year ended June 30, 2013, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico, P.O. Box 42004, San Juan PR 00940-2004.

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15. RETIREMENT PLANS - Continued

Other Retirement Benefit

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

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

Funding Policy

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

Annual pension cost and net pension obligation/ (asset)

The Authority's annual pension expense is calculated based on the ARC. The Authority engaged an actuary to calculate the ARC and related information per the provisions of GASB Statement No. 27 "*Accounting for Pensions by State and Local Governmental Employers*" ("GASB No. 27") for employers with more than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. At June 30, 2014, the actual funding excess over the ARC amounted to $4.1 million and is presented as a net pension asset in the accompanying statement of net position.

The following table shows the Authority's annual pension cost for the year ended June 30, 2014 and the amount actually contributed at June 30, 2014 (in thousands):

Annual Pension Cost	$ 491
Actual Funding Contribution	$ 532

As of June 30, 2014, the actuarial accrued liability for benefits amounted to $4.1 million, all of which was unfunded.

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

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15. RETIREMENT PLANS - Continued

Methods and Assumptions

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

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

The valuation date was July 1, 2012 and the Projected Unit Credit Cost Method was used. The actuarial projections were based on a set of assumptions supplied by the Authority. Turnover rates were based on service and age-related turnover. A discount rate of 5% was used. This rate is the best actuarial estimate of expected long-term experience and is in accordance with guidelines for selection of these rates under GASB No. 27.

16. COMMITMENTS AND CONTINGENCIES

Construction

As of June 30, 2014, the Authority had commitments for approximately $7.9 million, related to construction contracts.

Litigation

The Authority is defendant or co-defendant in various lawsuits, with claims amounting to approximately $305 million, as a result of the normal course of operations and also for alleged damages in cases principally related to its concessionaries. As of June 30, 2014, the Authority has reserves amounting to approximately $22.9 million to cover the aggregate exposure assessment. In the opinion of the Authority's management, based on legal advice, any liability in excess of insurance coverage and/or of the recorded reserves that may arise from final judgments would not affect significantly the Authority's financial position or result of operations.

Human Resources

The Authority is defendant in various separate class action suits brought by employees, which are requesting the payment of overtime, accrued compensated absences, fringe benefits and increase in salaries. Due to the complexity of some of the claims, the total amount to be paid, if any, by the Authority cannot be determined, and as a result were not accrued as of June 30, 2014.

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16. COMMITMENTS AND CONTINGENCIES - Continued

Environmental Remediation

On May 23, 2002, the Authority, as well as other oil companies (the members), was contacted by the United States Environmental Protection Agency ("EPA") regarding certain alleged environmental conditions at the LMMIA related to the Hydrant Fuel System ("HFS"). The Authority and the other members entered into an Administrative Order Consent ("AOC") with EPA to perform a subsurface investigation and certain other tasks in connection with the HFS, with the exception of the assessment of the HFS, which will be undertaken by the Authority. In March 2003, the Authority and the other members entered into a Joint Defense, Participation and Cost Sharing Agreement to jointly conduct the subsurface investigation established in the AOC, constitute a Steering Committee and share the underlying costs. The Steering Committee established a budget for the sampling stage of the works for which the Authority is responsible for $3 million, which is included as part of the accounts payable and accrued expenses in the accompanying statement of net position as of June 30, 2014. The budget established by the Steering Committee covers only the sampling stage of the works in which they are currently on. Subsequent remediation and responsibility actions will be renegotiated in the future.

Tenant Lease Agreements

The Authority entered in two lease agreements with a tenant for a tract of land at LMMIA. The lease agreements are for twenty-five (25) years with options to renew for two (2) additional five (5) year terms. One of the agreements was effective in September 1988 and the other in June 1995. Under the terms of the Agreements, the Authority will charge a fixed monthly rent, plus an additional rent based on sales volume. The Authority also agreed to grant rental credits to reimburse the lessee for the permanent improvements to the leased property. The title to such improvements will revert to the Authority at no further cost at the end of the lease term or at a prior date in case of default. The rental credit to be granted is limited to the amount invested by the lessee, which is required to submit evidence of the amount invested, in the leased property. Also, as of June 30, 2014, the tenant and the Authority are under litigation of certain aspects of the lease agreements, as described in the ensuing paragraph.

Pursuant to the objectives of the LMMIA *Project (see* Note 21), during December 2011, the Authority entered into certain expropriations proceedings through the Puerto Rico First Instance Court (the "Court"), to acquire certain properties and concessions owned by third parties within the LMMIA complex. In connection with such proceedings, on December 27, 2011, the Authority obtained a $30 million non-revolving credit facility with the GDB, out of which $25.4 million were consigned with the Court to start the expropriation process. The consigned amount was based on the Authority's determination of the properties' fair value, and it is included in a separate line item in the accompanying statement of net position. The counterparties have the right to contest the amount deposited, pursuant to the presentation of acceptable evidence indicating a higher fair value. As of the date of issuance of the financial statements, it is uncertain if the final settlement will be for the consigned amount, or for a higher consideration. See Note 22 for more information on subsequent developments related to this expropriation case.

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16. COMMITMENTS AND CONTINGENCIES - Continued

AMR Bankruptcy

On November 28, 2011, AMR Corp. ("AMR"), the parent company of American Airlines, filed for bankruptcy under Chapter 11 of the US Bankruptcy Law. The Authority derived over 20% of its rental revenues and landing and other fees from AMR during the fiscal year 2012. Prior to the closing of lease and use agreements with respect to the LMMIA, as described in Note 21, the Authority's collection of revenues could have been affected if AMR's bankruptcy proceedings caused delays or suspension of payments, or if AMR's operations were modified as part of the underlying corporate reorganization. However, pursuant to the lease and use agreement closed on February 27, 2013, referred to in Note 21, this potential risk was transferred to Aerostar, which is managing and monitoring such risk as part of the lease and use agreements.

Trocadero-Diverplex Federal Funds Finding

During the 1980's, a water taxi terminal station was constructed in Hato Rey, as part of a water transportation system running from Hato Rey to Old San Juan. This project, also known as the "Aqua Express Project", was funded with approximately $30 million of federal financial assistance from the Federal Transit Administration (FTA) channeled through the Department of Transportation and Public Works (DTOP), as grantee, and various other governmental entities as participants in the project, including the Authority, the Maritime Transportation Authority of Puerto Rico (MTA) and the Puerto Rico Highways and Transportation Authority (PRHTA). During the early years of the 2000 decade, the water transportation service through Aqua Express was suspended principally due to high sedimentation on the maritime channel of the system and frequent technical problems with the water vessels of the system. During 2011, in an attempt to find an alternate productive use to the water terminal area that was otherwise being wasted, the Commonwealth administration then announced the conversion of the area into a restaurant and shopping center complex to be known as Trocadero-Diverplex, where at the present time several businesses operate.

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

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16. COMMITMENTS AND CONTINGENCIES - Continued

Federal Funds Pass through Grants

During July 2007, the Commonwealth of Puerto Rico approved Joint Resolution No. 116, which authorized the Secretary of Treasury to transfer $9 million to the MTA for financing the acquisition of ferryboats. MTA used these funds to finance the acquisition of a ferryboat with a capacity of 600 passengers and a total cost of approximately $10.6 million. During fiscal years 2009 and 2010, MTA requested federal assistance from the FTA, through the Authority as grantee, to finance the same 600-passenger ferryboat. Approval from FTA was obtained, and the Authority received $6.8 million in federal assistance, and passed through to MTA. The excess funds between the federal assistance and the Commonwealth appropriation received by MTA were used for operational purposes, which was not an authorized use under the federal award, nor under the Joint Resolution No. 116. Therefore, the FTA had frozen $15,314,596 until this matter was resolved. After further discussions between MTA's management, the Authority and FTA, this matter has already been resolved, the FTA funds are no longer frozen and the precautionary reserve of $6.8 million had already been reversed.

17. PASSENGER FACILITY CHARGE

Pursuant to the Aviation Safety and Capacity Act of 1990 (the Act), airports may collect a Passenger Facility Charge (PFC) of up to $4.50 per ticket, out of which $0.11 belong to the airline companies for administrative expenses and $4.39 to the Authority. Under the Act, PFC revenues are restricted to be used for financing eligible airport-related projects that preserve or enhance safety, capacity or security of the air transportation system, subject to the approval of the Secretary of Transportation of the United States. The PFC income for the year ended June 30 2014, amounted to approximately $852 thousand. As of June 30, 2014, the Authority has unexpended resources amounting to approximately $5.1 million, which are restricted for PFC projects. PFC revenues are recognized as collected and are included in non-operating revenues. As part of the service concession arrangement for the LMMIA facilities signed with Aerostar (described in Note 21), after February 27, 2013, the PFC revenues related to the LMMIA operations are received and administered by Aerostar.

Under the provisions of the Act, the Authority is required to provide an annual independent audit of the PFC revenues, which expresses an opinion of the fairness and reasonableness of the Authority's procedures for receiving, holding and using PFC revenue. In addition, auditors are required to report whether the quarterly reports that must be filed by the Authority fairly represent the net transactions within the PFC accounts. After having performed no such independent audits since the inception of the PFC program in 1993, the Authority engaged one during fiscal year 2014 to cover compliance with the PFC requirements for the periods since inception through February 28, 2013. The resulting PFC audit report contained disclaimers of opinion for the first 10 years of the program and several noncompliance exceptions since 2003, mostly due to inadequate document retention policies that enabled the destruction and unavailability of supporting documentation to be inspected. The Authority had been following the local seven-year retention policy regulations of the Commonwealth, rather than the ones prescribed by the PFC regulations. Despite these results, management felt that such findings were not necessarily indicative of illegal or inappropriate expenditures outside the applicable PFC projects, as all PFC projects since inception of the program have been completed, in-process

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17. PASSENGER FACILITY CHARGE - Continued

or accounted for. Also, the FAA has not provided any comments or feedback on the results of the audit report, not has a return of PFC funds being requested; therefore, management believes no allowance for potential exposure is considered necessary at June 30, 2014.

18. RENTAL INCOME

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

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

Year Ending June 30,	Amount (in thousands)
2015	$ 17,162
2016	16,993
2017	16,344
2018	16,336
2019	14,787
	$ 81,622

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

19. FEDERAL ASSISTANCE PROGRAMS

The Authority participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations,* or to compliance audits by grantor agencies.

Federal financial assistance and Commonwealth of Puerto Rico appropriations for the year ended June 30, 2014, consist of grants and donations as follows (in thousands):

Federal financial assistance:	**2014**
Federal grants received from:	
Federal Aviation Administration	$ 12,766
Federal Transit Administration	4,168
Federal Transit Administration - ARRA funds returned	(58)
Department of Home Land security	142
Total grants	17,018
Less: pass - through grant program payments	(4,168)
	$ 12,850
Commonwealth of Puerto Rico appropriations	$ 2,726

Pass-through grants program payments of approximately $4.168 million are included as grant subsidies and awards in the accompanying statement of revenues, expenses and change in net position.

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20. OPERATING REVENUES

Operating revenues for the fiscal year ended June 30, 2014, consist of:

	2014 (In thousands)
Maritime operations:	
Wharfage, dockage and port services	$ 29,056
Tourist ship fees	16,248
Equipment and property rental	13,504
Demurrage, utilities and other	1,104
Engagement security fee	16,561
Less: provision for doubtful accounts	(1,939)
	74,534
Airport operations:	
Landing fees	1,080
Passenger facilities fees	709
Space rentals	23,574
Utilities, gas sales and other	1,836
Less: provision for doubtful accounts	(1,142)
	26,057
Total revenues	100,591
Less: discounts and incentives	(461)
Total net operating revenues	$ 100,130

21. LEASE AND USE AGREEMENTS - LMMIA

The Puerto Rico Public-Private Partnerships Authority (the "PPP") was created by the Public-Partnership Act for the purpose of implementing the Commonwealth's public policy of favoring strategic alliances with the private sector. Among the priority projects was the establishment of a public-private partnership for the *Luis Muñoz Marín International Airport* (the "LMMIA Project"). On February 27, 2013, the Federal Aviation Administration (FAA) approved the closing of the Lease and Use Agreements (the APP Agreements) entered into on July 27, 2012 between the Authority and Aerostar Airport Holdings, LLC (Aerostar) with respect to the LMMIA Project. Aerostar is a partnership formed by between Grupo Aeropuertuario de Sureste S.A.B de C.V. (ASUR), a New York Stock Exchange-listed Mexican airport management firm, and Highstar Capital L.P., a fourth-generation infrastructure investor and private equity funds manager. The Authority's objectives for entering into the APP agreements are discussed in Note 3.

The APP Agreements awarded Aerostar the right to operate, manage, maintain, develop and rehabilitate the LMMIA during a term of 40 years, subject to extension conditions as defined, in exchange for an upfront payment of a leasehold fee of $615 million to the Authority. In addition, upon the closing of the APP Agreements, the Authority receives from Aerostar annual rental payments for each of the first five full reporting years of $2.5 million; then from the sixth full reporting year through and including the thirtieth reporting year, the Authority will receive annual rental payments equal to 5% of the gross airport revenue earned by Aerostar in such years; and finally from the thirty-first reporting year and each succeeding year, the Authority will receive annual rental payments equal to 10% of the gross airport revenue earned by Aerostar in such years. Aerostar also funded with a $6 million deposit a separate escrow account called the

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21. **LEASE AND USE AGREEMENTS – LMMIA -Continued**

Puerto Rico Air Travel Promotion and Support Fund, with the purpose of compensating airlines that increase their services to the LMMIA over certain established thresholds during the first three years of the APP Agreements. Under the APP Agreements, the Authority is responsible for certain capital improvements pursuant to the Airline Capital Improvement Program. The present value of these capital improvements was estimated at $3.068 million at the transaction date. Pursuant to the adoption of GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, the Authority recognized at February 27, 2013, the date of the closing of the APP Agreements, a resulting deferred inflow of resources amounting to $622.5 million and a liability of $3.068 million for the present value of the capital improvement commitments of the Authority; in exchange for the receipt of the $615 million upfront leasehold fee and the receivable of the annual payments of $2.5 million from Aerostar for the first 5 years since the closing, with a present value estimate of $10.5 million. Since the closing date through June 30, 2014, approximately $20.7 million of the deferred inflow of resources have been amortized into revenue, $15.6 of which belonged to fiscal year 2014 and recognized within operating revenues-airport in the accompanying statement of revenues, expenses and change in net position. As of June 30, 2014, the Authority has satisfied approximately $2.8 million of its capital improvement commitments, leaving a remaining obligation of approximately $313,000, recognized within accounts payable and accrued expenses in the accompanying statement of net position.

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

The APP Agreements also provide for a series of capital improvement expenditures on the LMMIA from Aerostar over the term of the APP Agreements, with certain required initial projects and general accelerated upgrades, as defined. This capital improvement program called for an investment in capital expenditures for the ensuing five years after the closing of the APP Agreements in amounts ranging from $246 million to $290 million, to be executed over three phases. Phase 1 would consist of “accelerated upgrades” ranging from $16 million to $24 million, including the acquisition of approximately 22 new boarding bridges, starting in September 2013. Phase 2 expected an investment of approximately $92 million extending through December 2014, mostly in the remodeling of Terminal B and the establishment of a new automated luggage management system. Phase 3 would require the investment of approximately $130 million to start in January 2015 through December 2015, principally in the remodeling and revamping of Terminal C. At June 30, 2014, approximately $42.4 million have been invested in capital expenditures by Aerostar, $1.6 million of which have been completed and placed in operations; thus recognized by the Authority as an increase in its capital asset with the corresponding credit to deferred inflow of resources by the same amount. The balance of deferred inflow of resources at June 30, 2014, after all the activities referred to in the paragraphs above amounts to $605.4 million.

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21. **LEASE AND USE AGREEMENTS – LMMIA -Continued**

The Authority is required to provide police and fire services to the LMMIA in exchange for annual compensation of $2.8 million, to be adjusted thereafter based on inflation. The APP Agreements also established certain compensation events, the occurrence of which from either party would trigger a compensation amount or activity from the defaulting party to the affected party, as defined. Finally, the Authority will be responsible to Aerostar, at the termination of the APP Agreements, for any capital related improvements not fully reimbursed to Aerostar from the Passenger Facility Charge (PFC) program or other airline charges. No such compensation events have occurred through June 30, 2014.

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

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

- A fund of $50 million for the early retirement of certain Authority's employees. At June 30, 2014, $4.3 million remain in this early retirement fund.
- A fund of $25 million for the development of the Authority's regional airports. At June 30, 2014, the entire amount remain in the regional airports development fund.
- A fund of $15 million for the guaranty to cover the Authority's obligations in case of losses sustained on the APP Agreements. At June 30, 2014, $15 million remain in this guaranty fund.

The aforementioned supporting funds are maintained in a separate bank account with GDB. These funds would require GDB's authorization for release, following the Authority's submission of the supporting documentation for such expenditures and their validation by GDB. In the case of the $25 million fund for the development of the Authority's regional airports, although no funds have been released through June 30, 2014 from the GDB account, the Authority has already made expenditures on this program from its own operational bank accounts with funds coming from applicable federal programs of the FAA and the local Authority's corresponding matching and related administrative costs. Through June 30, 2014, approximately $13 million from federal funds have been expended along with $5 million in local matching and administrative costs. The local funds expended from the Authority's operational bank accounts are expected to be recovered from the release of the supporting funds held with GDB within the following year.

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21. **LEASE AND USE AGREEMENTS – LMMIA -Continued**

With respect to the $50 million funds set aside to support the early retirement of certain Authority's employees, approximately $28 million were expensed and recognized during fiscal year 2014 for those employees who accepted the early retirement proposal and left the Authority during fiscal year 2014. This amount is presented within early retirement expense in the accompanying statement of revenues, expenses and change in net position. Another $15.3 million had been incurred during 2013, for which the Authority restated the beginning net position as further described in Note 4.

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

22. SUBSEQUENT EVENTS

On October 14, 2014, GDB reactivated a non-revolving line of credit that had been previously used by the Authority to consign with the Puerto Rico First Instance Court (the Court) $25.4 million to start the expropriation process of the Caribbean Airport Facilities at the LMMIA (See Note 6). This non-revolving credit facility, known as the CAF Loan (which had been fully repaid by the Authority in 2013 with the proceeds from the lease and use agreement described in Note 21), was reactivated for up to $6 million in order to consign with the Court such additional amount and resume the expropriation proceedings. Disbursements under the reactivated CAF Loan will bear interest at prime plus 150 basis points, but never lower than 7%, and will be due in one year after the closing of the transaction.

In preparing these financial statements, the Authority has evaluated events and transactions for potential recognition or disclosure through November 7, 2014, the date in which the basic financial statements were available to be issued.

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