OC-DA-123

jun. 16 (Rev.)
OC-16-18

Estado Libre Asociado de Puerto Rico
**OFICINA DEL CONTRALOR**
San Juan, Puerto Rico

**Certificación de Cumplimiento con la *Ley 273-2003*, según enmendada; y de Notificación de Envío de Cartas de Recomendaciones (*Management Letters*), Informes de Auditoría, Estados Financieros Auditados y Otros**[1]

Yo, Alberto Bacó Bagué (nombre del funcionario principal) Funcionario Principal de Fondo Rotatorio Estatal para Aquas Limpias (WP) (nombre de la entidad)

3085 (número de entidad) certifico a la Oficina del Contralor de Puerto Rico (Oficina) que relacionado con el año fiscal terminado al 30 de junio de 2015 :

1. Recibimos fondos públicos por $433,934 .
2. Efectuamos desembolsos de fondos federales por $ 68,166,864 . No aplica ☐.
3. Tenemos la obligación de cumplir con ☒ la *Ley 273-2003, Ley de Normas Contractuales sobre Independencia en las Auditorías Externas de Entidades Gubernamentales*[2], según enmendada, y con ☐ el *Single Audit Act*. En cumplimiento de estos:

   a. El 31 de marzo de 2015 formalizamos el contrato número 2015-BGF132 para realizar la auditoría de los ☒ Estados Financieros y/o el ☒ *Single Audit Report*.

   b. El 28 de marzo de 2016 recibimos el *Informe de Auditoria* del 30 de junio de 2015 de los auditores externos.

   c. El 16 de marzo de 2016 los auditores externos comparecieron para presentar el informe final y comunicar los hallazgos y las recomendaciones.

   d. Relacionado con las cartas finales de recomendaciones (*Management Letters*):

[1] La entidad deberá remitir a esta Oficina, en formato **PDF** y no más tarde del 31 de mayo siguiente al año fiscal auditado, el *Formulario OC-DA-123* firmado por el funcionario principal, con los documentos que se especifican en el Apartado 3-e y f del mismo. Esto, a través de la aplicación *Certificaciones Anuales de la Oficina del Contralor*. La aplicación está disponible en la Sección de Contraloría Digital en nuestra página en Internet: www.ocpr.gov.pr.

[2] En el Artículo 1 de la *Ley 273-2003* se establece que, para propósitos de dicha *Ley*, la frase "cualquier entidad de gobierno" incluye todos los organismos, con facultad de contratar, de las ramas Ejecutiva, Legislativa y Judicial tales como: departamentos, dependencias, municipios, corporaciones públicas y sus subsidiarias, afiliadas o cualesquiera entidades gubernamentales que tengan personalidad jurídica propia.

☒ El 2 de mayo de 2016 recibimos las cartas finales de recomendaciones (*Management Letters*) emitidas por los auditores externos el 8 de febrero de 2016. El archivo electrónico, en formato **PDF**, de las mismas fue remitido a su Oficina el 30 de agosto de 2016.

☐ Los auditores externos no emitieron las cartas finales de recomendaciones (*Management Letters*).

e. Se incluye el archivo electrónico, en formato **PDF**, de los siguientes documentos e informes:

☒ Informes de auditorías emitidos en forma final

☒ Estados financieros auditados

☐ Informes de Control Interno sobre Cumplimiento y la Opinión sobre Cumplimiento

☒ *Single Audit Report*

☐ Copia del *Form SF-SAC, Data Collection Form for Reporting on Audits of States, Local Governments, and Non-Profit Organizations*, y del recibo de envío al *Federal Audit Clearinghouse*.

☐ Otros (especifique): _____

f. Relacionado con el *Informe Especial Sobre el Cumplimiento de las Recomendaciones Contenidas en los Informes de Auditoría de la Oficina del Contralor de Puerto Rico y la Corrección de las Situaciones Comentadas en sus Informes Previos (Informe Especial)*:

☐ Se incluye el archivo electrónico, en formato **PDF**, del *Informe Especial* emitido por los auditores externos el ____ de _____ de _____.

☒ No aplica, ya que no tenemos recomendaciones pendientes de cumplimentar relacionadas con los informes publicados al 28 de febrero del año fiscal auditado.

4. ☐ No tenemos la obligación por ley, reglamento o acuerdo financiero, de contratar auditores externos para realizar la auditoría de los estados financieros del año fiscal terminado al ____ de _____ de _____.

En San Juan, Puerto Rico, hoy 30 de septiembre de 2016.

_____
Firma del Funcionario Principal

**LLM&D, PSC**
165 Ponce de León Ave.,
Second Floor
San Juan, Puerto Rico
00917-1233

# Puerto Rico Water Pollution Control Revolving Fund

Single Audit Package
June 30, 2015

(With Independent Auditors' Report Thereon)

CERTIFIED PUBLIC ACCOUNTANTS • BUSINESS AND TAX CONSULTANTS
Member Firm of The American Institute and the Puerto Rico Society of Certified Public Accountants

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# PUERTO RICO WATER POLLUTION CONTROL REVOLVING FUND

## TABLE OF CONTENTS


| | Page |
|---|---|
| INDEPENDENT AUDITORS' REPORT | 1–3 |
| MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) | 4–6 |
| BASIC FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2015: | |
| Statement of Net Position | 7 |
| Statement of Revenues, Expenses and Changes in Net Position | 8 |
| Statement of Cash Flows | 9 |
| Notes to Basic Financial Statements | 10–20 |
| Schedule of Expenditures of Federal Awards | 21 |
| Notes to Schedule of Expenditures of Federal Awards | 22 |
| INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS | 23-24 |
| INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133 | 25-26 |
| SCHEDULE OF FINDINGS AND QUESTIONED COSTS | 27-28 |
| SCHEDULE OF PRIOR YEAR AUDIT FINDINGS | 29 |

LLM&D, PSC
165 Ponce de León Ave.,
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San Juan, Puerto Rico
00917-1233

# Independent Auditors' Report

To the Board of Directors of
Puerto Rico Water Pollution
Control Revolving Fund

## Report on the Financial Statements

We have audited the accompanying statement of net position of the Puerto Rico Water Pollution Control Revolving Loan Fund ("the Revolving Fund") as of June 30, 2015 and the statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the basic financial statements, which collectively comprise the Revolving Fund'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 basic financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' Responsibility

Our responsibility is to express an opinion on these basic 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 auditors' 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 Revolving Fund'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 Revolving Fund'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.

## Opinion

In our opinion, based on our audit, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Revolving Fund, as of June 30, 2015, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## Other Matters

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Revolving Fund's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The schedule of expenditures of federal awards is responsibility of management and was derived from and relate to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated February 8, 2016, on our consideration of the Revolving Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Revolving Fund's internal control over financial reporting and compliance.

LLH&D, PSC

San Juan, PR
February 8, 2016

License No. 90
Expiration Date: December 1, 2016

Stamp No. E191234 of Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report

As financial management of the Puerto Rico Water Pollution Control Revolving Fund (the "Revolving Fund"), we offer readers of the Revolving Fund's financial statements this narrative overview and analysis of the Revolving Fund's financial performance during fiscal year ended June 30, 2015. This discussion and analysis is designed to assist the reader in focusing on the significant financial matters and activities and to identify any significant changes in the net position of the Revolving Fund. We encourage readers to consider the information presented here in conjunction with the basic financial statements as a whole, which follow this section.

## 1. FINANCIAL HIGHLIGHTS

- The Revolving Fund's restricted net position increased approximately $67.5 million or 15% over the course of the year's operations mainly resulting from an increase in the loans portfolio of approximately $52.8 million and from an increase in cash of approximately $13 million.

- Operating income was approximately $5.4 million for fiscal year 2015, a decrease of approximately $224 thousands when compared to the prior year.

- Grants and contributions received increased by approximately $41.6 million or 153.9% when compared to prior year. Grants received from the U.S. Environmental Protection Agency ("EPA") were $68.2 million while contributions from the Commonwealth of Puerto Rico (the "Commonwealth") amounted to approximately $434 thousands, during the year ended June 30, 2015.

- Loan disbursements made by the Revolving Fund to the Puerto Rico Aqueduct and Sewer Authority ("PRASA") to finance its capital improvement program amounted to approximately $72.3 million, an increase of approximately $41.1 million, or 131.7% from the $31.2 million disbursed during fiscal year 2014.

## 2. OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Revolving Fund's basic financial statements, which are comprised of the basic financial statements and the notes to the basic financial statements. Since the Revolving Fund is comprised of a single enterprise fund, no fund level financial statements are shown.

***Basic Financial Statements*** – The basic financial statements are designed to provide readers with a broad overview of the Revolving Fund's finances, in a manner similar to a private-sector business.

The statement of net position presents information on all of the Revolving Fund's assets and liabilities, with the difference between the two reported as net position. Net position increases when revenues exceed expenses. Increases in assets without a corresponding increase to liabilities result in increased net position, which indicate an improved financial position.

The statement of revenues, expenses, and changes in net position presents information showing how an entity's net position changed during the fiscal year. All changes in net position are reported as soon as the underlying event occurs, regardless of timing of related cash flows.

The last of the required financial statements is the statement of cash flows. This statement reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, and capital and non-capital financing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

***Notes to the Basic Financial Statements*** – The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

## 3. FINANCIAL ANALYSIS

Net position may serve, over time, as a useful indicator of whether a governmental entity's financial position is improving or deteriorating. In the case of the Revolving Fund, assets exceeded liabilities by approximately $518 million as of June 30, 2015. This represents an increase of $67.5 million or 15% over net position as of June 30, 2014. The total amount of net position is restricted as it only serves the purpose provided by the enabling legislation of providing loans and financing for drinking water infrastructure facilities. As of June 30, 2015, most of the outstanding loans have been granted to PRASA.

Pursuant to Act 96 of June 30, 2015 (the "Act 96"), the Commonwealth guarantees the payment of principal and interest on outstanding Revolving Fund loans granted to PRASA on or before June 30, 2020. Loans covered by Act 96 include a statement of such guarantee in the loan agreement. As of June 30, 2015, principal in the amount of approximately $337.7 million, plus any interest accrued on it, out of the $385.8 million in outstanding loans are guaranteed by the Commonwealth. The Revolving Fund's management believes that all loans are fully collectible, and has not established an allowance for loan losses.

The operation of the Revolving Fund is subject to the capital financing requirements of PRASA, and/or any other qualifying entity, and therefore, loan origination activity will be determined on an annual basis, depending upon PRASA's and/or any other qualifying entity's needs.

Condensed financial information on assets, liabilities, and restricted net position is presented below (in thousands):

| | June 30, | | Change | |
|---|---|---|---|---|
| | 2015 | 2014 | Amount | Percent |
| **Assets:** | | | | |
| Cash | $ 129,525 | $ 116,544 | $ 12,981 | 11.1% |
| Loans | 385,761 | 332,939 | 52,822 | 15.9% |
| Accrued interest receivable | 3,613 | 3,255 | 358 | 11.0% |
| Total assets | 518,899 | 452,738 | 66,161 | 14.6% |
| **Liabilities** - Accounts payable | 820 | 2,124 | (1,304) | (61.39%) |
| **Net position** - Restricted | $ 518,079 | $ 450,614 | $ 67,465 | 15.0% |

Cash increased to approximately $130 million as of June 30, 2015, from approximately $117 million as of June 30, 2014, for an increase of approximately $13 million, or 11.1%; and loans increased to approximately $385.8 million, for a net positive variance of approximately $52.8 million over 2014 figures. The $67.5 million growth in net position-restricted was primarily the result of the receipt of approximately $62.1 million in contributions from EPA during the year net of contributions to PRASA, and from approximately $7 million in interest income earned by the loan portfoli during the year ended June 30, 2015 and approximately $1.7 million in operating expenses.

Condensed financial information on revenues, expenses, and changes in net position is presented below (in thousands):

| | June 30, | | Change | |
|---|---|---|---|---|
| | 2015 | 2014 | Amount | Percent |
| Operating revenues - interest | $ 7,089 | $ 6,482 | $ 607 | 9.4% |
| Operating expenses - general and administrative | (1,723) | (892) | (831) | 93.2% |
| Operating income before grants and contributions, and transfers | 5,366 | 5,590 | (224) | (4.0%) |
| Grants and contributions | 68,601 | 27,023 | 41,578 | 153.9% |
| Contributions to PRASA and Other governmental entities | (6,502) | (291) | (6,211) | 2134.4% |
| Change in restricted net position | 67,465 | 32,322 | 35,143 | 108.7% |
| NET POSITION - Beginning of year | 450,614 | 418,292 | 32,322 | 7.7% |
| NET POSITION - End of year | $ 518,079 | $ 450,614 | $ 67,465 | 15.0% |

Change in net position increased by approximately $35 million when compared to prior year. Grants and contributions increased by approximately $41.6 million when compared to grants received during prior year. Note that grants are received to the extent disbursements are required under outstanding loans commitments.

## 4. REQUESTS FOR INFORMATION

This financial report is designed to provide those interested with a general overview of the Revolving Fund's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Puerto Rico Water Pollution Control Revolving Fund, at Government Development Bank for Puerto Rico, PO Box 42001, San Juan, Puerto Rico, 00940-2001.

# PUERTO RICO WATER POLLUTION CONTROL REVOLVING FUND

## STATEMENT OF NET POSITION
## JUNE 30, 2015

| | |
|---|---|
| **ASSETS:** | |
| **CURRENT ASSETS:** | |
| Cash | $ 129,525,232 |
| Accrued interest receivable | 3,613,383 |
| Loans receivable from Puerto Rico Aqueduct and Sewer Authority | 17,572,217 |
| Loans receivable from municipalities | 127,982 |
| Total current assets | 150,838,814 |
| **NON-CURRENT ASSETS:** | |
| Loans receivable from Puerto Rico Aqueduct and Sewer Authority | 367,307,031 |
| Loans receivable from municipalities | 753,693 |
| Total non-current assets | 368,060,724 |
| Total assets | 518,899,538 |
| **LIABILITIES** - Accounts payable | 820,299 |
| **NET POSITION** - Restricted | $ 518,079,239 |

See notes to the basic financial statements.

# PUERTO RICO WATER POLLUTION CONTROL REVOLVING FUND

## STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
## FOR THE YEAR ENDED JUNE 30, 2015

| | |
|---|---|
| **OPERATING REVENUES:** | |
| Interest income on loans | $ 6,958,162 |
| Interest income on deposits | 131,619 |
| Total interest earned | 7,089,781 |
| **OPERATING EXPENSES** - General and administrative | 1,723,220 |
| **OPERATING INCOME** | 5,366,561 |
| **NON-OPERATING REVENUES / (EXPENSES):** | |
| Contributions from Environmental Protection Agency | 68,166,864 |
| Contributions from Commonwealth of Puerto Rico | 433,934 |
| Contributions to Puerto Rico Aqueduct and Sewer Authority and Other Governmental Entities | (6,502,152) |
| Total non-operating revenues, net | 62,098,646 |
| **CHANGE IN NET POSITION** | 67,465,207 |
| **NET POSITION** - Beginning of year | 450,614,032 |
| **NET POSITION** - End of year | $ 518,079,239 |

See notes to the basic financial statements.

# PUERTO RICO WATER POLLUTION CONTROL REVOLVING FUND

## STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED JUNE 30, 2015

| | |
|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES:** | |
| Cash paid for general and administrative expenses | $ (3,026,877) |
| **CASH FLOWS FROM INVESTING ACTIVITIES:** | |
| Loans disbursements | (72,257,769) |
| Principal collected on loans | 19,435,486 |
| Interest received on loans | 6,602,591 |
| Interest received on deposits | 129,304 |
| Net cash used in investing activities | (46,090,388) |
| **CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:** | |
| Contributions received from Environmental Protection Agency | 68,166,864 |
| Contributions received from Commonwealth of Puerto Rico | 433,934 |
| Contributions paid to Puerto Rico Aqueduct and Sewer Authority and Other Governmental Entities | (6,502,152) |
| Net cash provided by non-capital financing activities | 62,098,646 |
| **NET CHANGE IN CASH** | 12,981,381 |
| **CASH** - Beginning of year | 116,543,851 |
| **CASH** - End of year | $ 129,525,232 |

| | |
|---|---|
| **RECONCILIATION OF OPERATING INCOME TO NET CASH USED IN OPERATING ACTIVITIES:** | |
| Operating income | $ 5,366,561 |
| Adjustments to reconcile operating income to net cash used in operating activities: | |
| Interest income on loans | (6,958,162) |
| Interest income on deposits | (131,619) |
| Decrease in accounts payable | (1,303,657) |
| Net cash used in operating activities | $ (3,026,877) |

See notes to the basic financial statements.

## 1. REPORTING ENTITY

Puerto Rico Water Pollution Control Revolving Fund (the "Revolving Fund") was created by Act 44 of the Legislature of the Commonwealth of Puerto Rico (the "Commonwealth") on June 21, 1988, as amended. The Revolving Fund was constituted separately and independently from any other funds or resources of the Commonwealth. It is presented as an enterprise fund of the Commonwealth.

The Revolving Fund is administered, pursuant to Act 416 of September 22, 2004, as amended, (the "Act 416") by the Puerto Rico Environmental Quality Board ("EQB"). Pursuant to the Act 416, EQB, on behalf of the Commonwealth, is authorized to enter into operating agreements and capitalization grant agreements with the U.S. Environmental Protection Agency ("EPA"). EQB, Puerto Rico Infrastructure Financing Authority ("PRIFA"), Puerto Rico Aqueduct and Sewer Authority ("PRASA"), and Government Development Bank for Puerto Rico (the "Bank") entered into a memorandum of understanding under which each party has agreed to assume specific responsibilities in connection with the operations of the Revolving Fund. Under the memorandum of understanding, the Bank provides assistance in maintaining the accounting records of the Revolving Fund.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Revolving Fund conform to Accounting Principles Generally Accepted in the United States of America ("GAAP"), for governments as prescribed by the Governmental Accounting Standards Board ("GASB").

During fiscal year ended on June 30, 2015, certain governmental accounting pronouncements became effective, none of which had any impact in the results of the operations or in the presentation of the financial statements of the Revolving Fund.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of changes in net position and revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Following is a description of the Revolving Fund's most significant accounting policies:

*Measurement Focus, Basis of Accounting, and Financial Statements Presentation* — The Revolving Fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when incurred, regardless of the timing of related cash flows.

The statement of net position and the statement of revenues, expenses, and changes in net position report information on all activities of the Revolving Fund. The Revolving Fund's activities are distinguished as proprietary activities. The Revolving Fund's activities generally are financed through intergovernmental revenues, other non-exchange revenues and interest income from loans and deposits. Following is a description of the Revolving Fund's financial statements.

The statement of net position presents the Revolving Fund's assets and liabilities, with the difference reported as net position. Net position may be reported as:

- Restricted component of net position consists of restricted assets reduced by liabilities related to those assets. Restricted net position result when constraints placed on net position use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

- Unrestricted component of net position consists of net amount of the assets and liabilities that do not meet the definition of the preceding category. Unrestricted component of net position often is designated in order to indicate that management does not consider them to be available for general operations. Unrestricted component of net position often has constraints on use that are imposed by management, but such constraints may be removed or modified.

As of June 30, 2015, the Revolving Fund net position is presented as restricted.

The statement of revenues, expenses, and changes in net position demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include interest income on loans and deposits. Operating expenses are those that relate to the administration of the Revolving Fund. Other items not meeting the definition of program revenues or operating expenses are reported as non-operating revenues or expenses.

*Loans Receivable and Allowance for Loan Losses* – Loans are presented at the outstanding unpaid principal balance. Management assesses the inherent risk of its loan portfolio and records an allowance for loan losses through provisions recorded in the financial statements. This allowance is based on management's evaluation of the risk characteristics of the loan including such factors as the nature of individual credits outstanding, past loss experience, known and inherent risks in the portfolios, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and general economic conditions. Loans charge-offs are recorded against the allowance when management believes that the collection of the principal is unlikely. Recoveries of amounts previously charged off are credited to the respective allowance. Management believes that the inherent risk of its loan portfolio is mitigated by the fact that there have been no historical losses in such portfolio. Accordingly, no allowance for loan losses has been recorded at June 30, 2015. Because of uncertainties inherent in the estimation process, management estimate of credit losses in the outstanding loans receivable portfolios and the related allowance may change in the near future.

The accrual of interest ceases only when management determines that all of the following characteristics are present, thus the mere existence of several but not all of these attributes does not warrant the discontinuance of interest income recognition: (a) a loan is six months past due; (b) it has no definitive source of repayment; (c) it is not covered by a formal commitment from the Commonwealth; and (d) it has no designated collateral or such collateral is insufficient. If a loan is placed in nonaccrual status, all accrued interest receivable is reversed from interest income. Interest income on nonaccrual loans is,

thereafter, recognized as income only to the extent actually collected. Nonaccrual loans are returned to an accrual status when management has adequate evidence to believe that the loans will be performing as contracted. The Revolving Fund does not have loans on nonaccrual status as of June 30, 2015.

Management considers current information and events regarding the borrowers' ability to repay their obligations, and considers a loan to be impaired when it is probable that the Revolving Fund will be unable to collect all amounts due according to the contractual terms of the loan agreement. Interest income and cash receipts on impaired loans are accounted for predominantly in the same manner as nonaccrual loans. If a loan is considered to be impaired, it will be generally reduced to the present value of expected future cash flows, discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral, if the loan is collateral dependent, by establishing a valuation allowance. The Revolving Fund does not have impaired loans as of June 30, 2015.

*Off-Balance Sheet Arrangements*— In the ordinary course of business, the Revolving Fund enters into off-balance sheet arrangements consisting of commitments to extend credit. Such financial arrangements are recorded in the financial statements when they are funded. The Revolving Fund periodically evaluates the credit risks inherent in these commitments and establishes loss allowances for such risks if and when these are deemed necessary. Management of the Revolving Fund periodically evaluates the credit risk inherent in the commitments to extend credit portfolio on the same basis as loans are evaluated. As of June 30, 2015, the Revolving Fund has approximately $150 million of undisbursed commitments to extend credit.

The GASB has issued the following accounting pronouncements that have effective date after June 30, 2015:

(a) GASB Statement No. 72, *Fair Value Measurement and Application.* This Statement addresses accounting and financial reporting issues related to fair value measurements. The definition of *fair value* is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2015.

(b) GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB 68, and Amendments to Certain Provisions of GASB Statements 67 and 68.* This Statement establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement No. 68. It also amends certain provisions of Statement No. 67, *Financial Reporting for Pension Plans*, and Statement No. 68 for pension plans and pensions that are within their respective scopes.

(c) This Statement also clarifies the application of certain provisions of Statements No. 67 and No. 68 with regard to the following issues:

- ✓ Information that is required to be presented as notes to the 10-year schedules of required supplementary information about investment-related factors that significantly affect trends in the amounts reported.
- ✓ Accounting and financial reporting for separately financed specific liabilities of individual employers and nonemployer contributing entities for defined benefit pensions.
- ✓ Timing of employer recognition of revenue for the support of nonemployer contributing entities not in a special funding situation.

The requirements of this Statement that address accounting and financial reporting by employers and governmental nonemployer contributing entities for pensions that are not within the scope of Statement No. 68 are effective for financial statements for fiscal years beginning after June 15, 2016, and the requirements of this Statement that address financial reporting for assets accumulated for purposes of providing those pensions are effective for fiscal years beginning after June 15, 2015. The requirements of this Statement for pension plans that are within the scope of Statement No. 67 or for pensions that are within the scope of Statement No. 68 are effective for fiscal years beginning after June 15, 2015.

(d) GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. This Statement replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, as amended, Statement No. 43, and Statement No. 50, *Pension Disclosures*. The objective of this Statement is to improve the usefulness of information about postemployment benefits other than pensions (other postemployment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. This Statement is effective for financial statements for fiscal years beginning after June 15, 2016.

(e) GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefit Other Than Pension*. This Statement replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for OPEB. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement is effective for fiscal years beginning after June 15, 2017.

(f) GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The "GAAP

hierarchy" consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2015, and should be applied retroactively.

(g) GASB Statement No. 77, *Tax Abatement Disclosures*. This Statement requires governments that enter into tax abatement agreements to disclose the following information about the agreements:

- ✓ Brief descriptive information, such as the tax being abated, the authority under which tax abatements are provided, eligibility criteria, the mechanism by which taxes are abated, provisions for recapturing abated taxes, and the types of commitments made by tax abatement recipients
- ✓ The gross dollar amount of taxes abated during the period
- ✓ Commitments made by a government, other than to abate taxes, as part of a tax abatement agreement

Governments should organize those disclosures by major tax abatement program and may disclose information for individual tax abatement agreements within those programs. Tax abatement agreements of other governments should be organized by the government that entered into the tax abatement agreement and the specific tax being abated. Governments may disclose information for individual tax abatement agreements of other governments within the specific tax being abated. For those tax abatement agreements, a reporting government should disclose:

- ✓ The names of the governments that entered into the agreements
- ✓ The specific taxes being abated
- ✓ The gross dollar amount of taxes abated during the period

The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2015.

(h) GASB No. 78, *Pensions Provided Through Certain Multiple-Employer Defined Benefit Plans*. This Statement addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. Prior to the issuance of this Statement, the requirements of Statement No. 68 applied to the financial statements of all state and local governmental employers whose employees are provided with pensions through pension plans that are administered through trusts that meet the criteria in paragraph 4 of that Statement. This Statement amends the scope and applicability of Statement No. 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees

of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2015.

(i) GASB No. 79, *Certain External Investment Pools and Pool Participants.* This Statement addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes. An external investment pool qualifies for that reporting if it meets all of the applicable criteria established in this Statement. The specific criteria address (1) how the external investment pool transacts with participants; (2) requirements for portfolio maturity, quality, diversification, and liquidity; and (3) calculation and requirements of a shadow price. Significant noncompliance prevents the external investment pool from measuring all of its investments at amortized cost for financial reporting purposes. Professional judgment is required to determine if instances of noncompliance with the criteria established by this Statement during the reporting period, individually or in the aggregate, were significant. If an external investment pool does not meet the criteria established by this Statement, that pool should apply the provisions in paragraph 16 of Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, as amended. If an external investment pool meets the criteria in this Statement and measures all of its investments at amortized cost, the pool's participants also should measure their investments in that external investment pool at amortized cost for financial reporting purposes. If an external investment pool does not meet the criteria in this Statement, the pool's participants should measure their investments in that pool at fair value, as provided in paragraph 11 of Statement No. 31, as amended. This Statement establishes additional note disclosure requirements for qualifying external investment pools that measure all of their investments at amortized cost for financial reporting purposes and for governments that participate in those pools. Those disclosures for both the qualifying external investment pools and their participants include information about any limitations or restrictions on participant withdrawals.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2015, except for certain provisions on portfolio quality, custodial credit risk, and shadow pricing. Those provisions are effective for reporting periods beginning after December 15, 2015. Earlier application is encouraged.

Management is evaluating the impact that these statements will have, if any, on the Revolving Fund financial statements.

## 3. CUSTODIAL CREDIT RISK

Custodial credit risk is the risk that in the event of a bank failure, the Revolving Fund's deposit may not be returned to it. The Revolving Fund does not have a policy for custodial credit risk. As of June 30, 2015, all of the Revolving Fund's bank balance, aggregating approximately $130,000,000, was exposed

to custodial credit risk since such deposits, all of which are maintained at the Bank, are uninsured and uncollateralized.

## 4. TRANSACTIONS WITH GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

Since the Revolving Fund has no employees, the Bank provided certain management services to the Revolving Fund at no cost during the year ended June 30, 2015.

## 5. LOANS RECEIVABLE

Loans receivable as of June 30, 2015, consist of:

| Description | Amount |
|---|---|
| Permanent loans: | |
| PRASA | $ 232,049,511 |
| Municipalities | 881,675 |
| Total permanent loans | 232,931,186 |
| Construction loans — PRASA | 152,829,737 |
| Total loans receivable | $ 385,760,923 |

**Reconciliation to the statement of net position**

| | |
|---|---|
| Current portion: | |
| PRASA | $ 17,572,217 |
| Municipalities | 127,982 |
| Total current portion | 17,700,199 |
| Noncurrent portion: | |
| PRASA | 367,307,031 |
| Municipalities | 753,693 |
| Total noncurrent portion | 368,060,724 |
| Total loans receivable | $ 385,760,923 |

Permanent loans are due in semiannual installments, bearing interest at 2% per annum, maturing on various dates through December 31, 2035. Permanent loans receivable, as of June 30, 2015, mature as follows:

| Years Ending on June 30, | Amount |
|---|---|
| 2016 | $ 17,700,199 |
| 2017 | 17,556,982 |
| 2018 | 16,746,154 |
| 2019 | 15,279,046 |
| 2020 | 14,876,241 |
| Thereafter | 150,772,564 |
| | $ 232,931,186 |

Construction loans bear interest at 2% per annum and principal will be payable semiannually, commencing no later than one year after construction completion date. All loans are required to be paid in full in a period not to exceed 20 years. For construction loans, such period commences after the construction loan is converted to a permanent loan. Interest on construction loans are payable semiannually since inception of loan.

The Revolving Fund is operated as a direct loan program, whereby most of the loans made are funded by capitalization grants from the EPA and a Commonwealth match equaling 20% of the EPA capitalization grant. All of the outstanding loans were 100% funded with EPA capitalization grants or 100% funded with the results of the operations of the Revolving Fund.

Pursuant to Act 96 of June 30, 2015 (the "Act 96"), the Commonwealth guarantees the payment of principal and interest on outstanding Revolving Fund loans granted to PRASA on or before June 30, 2015. Loans covered by Act 96 include a statement of such guarantee in the loan agreement. As of June 30, 2015, principal in the amount of approximately $337.7 million, plus any interest accrued on it, out of the $385.8 million in outstanding loans are guaranteed by the Commonwealth. The Revolving Fund's management believes that all loans are fully collectible, and has not established an allowance for loan losses.

As of June 30, 2015, the Revolving Fund has approximately $150 million of undisbursed commitments to extend credit of which $27 million were granted to the Puerto Rico Electric Power Authority ("PREPA") for the construction of two water infrastructure program qualifying projects. PREPA and EQB have agreed that the projects comply with EPA requirements of the Clear Water Act, as amended (the "CWA"). EQB estimates that the construction phase of the projects will end between December 2016 and March 2017. The $27 million credit commitment, when ultimately disbursed, will be due in 20 years after completion of the projects. This credit agreement is subordinated to PREPA's Revenue Bonds and its debts with financial institutions.

PREPA has been facing liquidity issues and experiencing negative results of operations. On August 14, 2014, PREPA executed forbearance agreements with its creditors to be able to continue its efforts to reform its operations. These forbearance agreements were enabled to avoid a default on certain working capital lines of credit and to provide with incremental liquidity through the suspension of certain debt

service reserve payments and access to construction fund reserves. Further, PREPA's Board of Directors appointed on September 8, 2014 a Chief Restructuring Officer ("CRO") to develop an integrated plan to restructure PREPA operations. Although the final integrated plan to restructure PREPA's operations was ratified by the Commonwealth's Legislature, management of the Revolving Fund does not believe there is any exposure on this loan commitment at June 30, 2015, as it has yet to be funded. Management is of the opinion that once disbursed, PREPA will comply with its debt service requirements under the line of credit agreement and its performance will be evaluated consistently in light of the potential restructuring plan to be ultimately adopted by PREPA.

## 6. CAPITALIZATION GRANTS

The CWA is the main federal law that establishes the basic structure for regulating discharges of pollutants into waters of the United States and for regulating quality standards for surface waters. Under the CWA, EPA has implemented pollution control programs such as setting wastewater standards for industry and quality standards for all contaminants in surface waters. The CWA created the federal Clean Water State Revolving Fund to make funds available to finance water quality protection projects for wastewater treatment, nonpoint source pollution control, and watershed and estuary management that are needed to comply with the CWA water pollution requirements. The CWA authorizes the EPA to award capitalization grants to state which, in turn, provide low interest loans and other types of financial assistance to eligible systems. These grants are routinely subject to financial and compliance audits in accordance with the provisions of the U.S. Office of Management and Budget Circular A-133 and compliance audits by EPA. The latter has the authority to determine liabilities as well as to limit, suspend, or terminate the federal assistance. All funds drawn from EPA and the matching funds from the Commonwealth are recorded as non-operating revenues. As of June 30, 2015, EPA has awarded capitalization grants of $514,085,899 to the Revolving Fund of which $439,746,503 has been drawn for loans and administrative expenses.

The following summarizes the capitalization grant awarded, amounts drawn on each grant as of the statement of position date, and balances available for future draws:

| June 30, | Grant Amount | Total Draws at June 30, 2014 | Draws During 2015 | Total Draws at June 30, 2015 | Available at June 30, 2015 |
|---|---|---|---|---|---|
| 1989 | $ 12,302,136 | $ 12,302,136 | $ - | $ 12,302,136 | $ - |
| 1990 | 12,724,965 | 12,724,965 | - | 12,724,965 | - |
| 1991 | 26,767,224 | 26,767,224 | - | 26,767,224 | - |
| 1992 | 25,341,921 | 25,341,921 | - | 25,341,921 | - |
| 1993 | 25,068,780 | 25,068,780 | - | 25,068,780 | - |
| 1994 | 15,554,979 | 15,554,979 | - | 15,554,979 | - |
| 1995 | 16,064,829 | 16,064,829 | 102,679 | 16,167,508 | (102,679) |
| 1996 | 26,314,675 | 26,314,675 | - | 26,314,675 | - |
| 1997 | 8,110,800 | 8,110,800 | - | 8,110,800 | - |
| 1998 | 17,562,897 | 19,244,428 | - | 19,244,428 | (1,681,531) |
| 1999 | 17,564,382 | 16,532,547 | - | 16,532,547 | 1,031,835 |
| 2000 | 17,504,784 | 17,418,708 | 86,076 | 17,504,784 | - |
| 2001 | 31,349,156 | 30,770,851 | 578,305 | 31,349,156 | - |
| 2002 | 17,387,865 | 16,808,269 | 579,596 | 17,387,865 | - |
| 2003 | 18,322,900 | 15,006,151 | 3,316,749 | 18,322,900 | - |
| 2004 | 17,285,301 | 16,709,124 | 576,177 | 17,285,301 | - |
| 2006 | 25,475,868 | 14,560,592 | 10,066,082 | 24,626,674 | 849,194 |
| 2007 | 13,959,396 | 3,056,731 | 10,437,352 | 13,494,083 | 465,313 |
| ARRA | 51,114,200 | 51,114,200 | - | 51,114,200 | - |
| 2008 | 18,340,841 | 1,765,057 | 15,964,422 | 17,729,479 | 611,362 |
| 2010 | 26,575,000 | 342,672 | 21,641,531 | 21,984,203 | 4,590,797 |
| 2011 | 19,259,000 | - | 4,817,895 | 4,817,895 | 14,441,105 |
| 2012 | 18,434,000 | - | - | - | 18,434,000 |
| 2013 | 17,413,000 | - | - | - | 17,413,000 |
| 2014 | 18,287,000 | - | - | - | 18,287,000 |
| | $ 514,085,899 | $ 371,579,639 | $ 68,166,864 | $ 439,746,503 | $ 74,339,396 |

At June 30, 2015, the Revolving Fund has $18,287,000, $17,413,000 and $18,434,000 from grants awarded by EPA during the federal fiscal years ended September 30, 2014, 2013 and 2012, respectively, which are available to be drawn for loan commitments and/or administrative expenses once all the EPA requirements have been met. As of June 30, 2015, PRIFA, PRASA, and third parties have not executed financial agreements related to these awards. See Note 8 for subsequent events.

At June 30, 2015 the Revolving Fund contributed $6.5 million for different types of projects to the following entities:

| | Amount |
|---|---|
| • San Juan Bay Estuary | $ 209,761 |
| • Municipality of Vega Alta | 362,058 |
| • Puerto Rico Electric Power Authority | 1,478,801 |
| • Municipality of Arecibo | 1,265,541 |
| • Puerto Rico Aqueduct and Sewer Authority | 3,185.991 |
| | $6,502,152 |

## 7. ADMINISTRATIVE EXPENSES

As provided by federal laws and regulations, reasonable costs of administering the Revolving Fund are reimbursable under federal programs up to a maximum of 4% of the capitalization grant awarded each year. The federal government also reimburses expenses incurred in training and certifying personnel as well as technical matters. During the year ended June 30, 2015, total reimbursement of administrative expenses amounted to $3,040,318.

## 8. SUBSEQUENT EVENTS

On September 21, 2015, EPA awarded the Revolving Fund $18,193,000 for the federal fiscal year ended September 30, 2015, to be drawn for loan commitments and administrative expenses reimbursement once all EPA requirements have been met.

Subsequent events were evaluated through February 8, 2016, the date the financial statements were available to be issued, to determine if any such events should either be recognized or disclosed in the 2015 financial statements.

# PUERTO RICO WATER POLLUTION CONTROL REVOLVING FUND

## SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
### AS OF AND FOR THE YEAR ENDED JUNE 30, 2015

| Federal grantor/pass-through grantor/program title | Federal CFDA Number /pass-through | Expenditures |
|---|---|---|
| **U. S. Environmental Protection Agency** | | |
| **Pass-through from Puerto Rico Department of Health** | | |
| Capitalization Grants for Clean Water State Revolving Funds | 66.458 | $ 66,861,040 |
| Total expenditures of federal awards | | $ 66,861,040 |

See notes to schedule of expenditures of federal awards.

## NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2015

1. **Basis of Presentation and Summary of Significant Accounting Policies** – The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Puerto Rico Water Pollution Revolving Fund (the "Revolving Fund") for the year ended June 30, 2015 and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Because the schedule presents only a selected portion of the operations of the Revolving Fund, it is not intended to and does not present the financial position, changes in net position or cash flows of the revolving fund.

2. **Reporting Entity** – During the year ended June 30, 2015, loans originated with U.S. Environmental Protection Agency ("EPA) capitalization grants amounted to $72,257,769, of which, $60,214,806, and $12,042,963, represent the federal and state share, respectively, of loans originated. For the year ended June 30, 2015, grants paid amounted to $6,502,152 of which $5,418,460 and $1,083,692 represent the federal and state share, respectively. Grants are not subject to loan or interest charges. The balance of loans previously granted amounting to $385,760,923 is not included in the schedule since the Revolving Fund is not deemed to have continuing compliance with requirements.

3. **Reconciliation of the Schedule with the Statement of Revenues, Expenses and Changes in Net Position**-The following presents a reconciliation between the Schedule with the contributions received from the EPA per the statement of revenues, expenses and changes in net position:

| Description | Total |
|---|---|
| Expenditures per Schedule of Expenditures of Federal Awards | $ 66,861,040 |
| Expenditures incurred in prior years but claimed for reimbursement during the year ended June 30, 2015 | 2,051,123 |
| Expenditures incurred during the year ended June 30, 2015 that have not been claimed for reimbursement to the Federal government | (745,299) |
| Contributions received from the EPA per the Statement of Revenues, Expenses and Changes in Net Position | $ 68,166,864 |

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

To the Board of Directors of
Puerto Rico Water Pollution Revolving Fund

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of the Puerto Rico Water Pollution Revolving Fund ("the Revolving Fund"), as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Revolving Fund's basic financial statements and have issued our report thereon dated February 8, 2016.

## Internal Control over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We identified a deficiency in internal control, described in the accompanying schedule of findings and questioned costs as finding 2015-01 that we consider to be a significant deficiency.

**Compliance and Other Matters**

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

**The Revolving Fund's Response to Findings**

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

**Purpose of this Report**

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

LLMD PSC

San Juan, PR
February 8, 2016

License No, 90
Expiration Date: December 1, 2016

Stamp No. E191235 of Puerto Rico
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was affixed to the record copy of this report.

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# INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

To the Board of Directors of
Puerto Rico Water Pollution Revolving Fund

## Report on Compliance for Each Major Federal Program

We have audited the Puerto Rico Water Pollution Revolving Fund ("the Revolving Fund"), compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the Revolving Fund's major federal programs for the year ended June 30, 2015. The Revolving Fund's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

## Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

## Auditors' Responsibility

Our responsibility is to express an opinion on compliance each of the Revolving Fund's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Revolving Fund's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Revolving Fund's compliance.

## Opinion on Each Major Federal Program

In our opinion, the Revolving Fund complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2015.

**Report on Internal Control over Compliance**

Management of the Revolving Fund is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Revolving Fund's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Revolving Fund's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

LLMD PSC

San Juan, PR
February 8, 2016

License No. 90
Expiration Date: December 1, 2016

Stamp No. E191236 of Puerto Rico
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was affixed to the record copy of this report.

**Part I-Summary of Auditors' Results**

**Financial Statements**

| | |
|---|---|
| Type of auditors' report issued: | Unmodified |
| Internal control over financial reporting: | |
| • Significant deficiencies identified? | x yes ____ no |
| • Material weakness identified? | ____ yes x none reported |
| Noncompliance that is material to financial statements noted? | ____ yes x no |

**Federal Awards**

| | |
|---|---|
| Internal control over major programs: | |
| • Significant deficiencies identified? | ____ yes x no |
| • Material weakness identified? | ____ yes x none reported |
| Type of auditors' report issued on compliance for major programs: | Unmodified |
| Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133? | ____ yes x no |

**Identification of Major Programs**

| CFDA Number | Name of Federal Program |
|---|---|
| 66.458 | Capitalization Grants for Clean Water State Revolving Funds |

| | |
|---|---|
| Dollar threshold used to distinguish between Type A and Type B programs: | $2,045,006 |
| Auditee qualify as low-risk auditee? | ____ yes x no |

## Section II-Financial Statement Findings

### Finding No. 2015-1 Administrative expenses reported in the incorrect accounting period

#### Criteria

In accordance with U.S. Generally Accepted Accounting Principles (US GAAP) accrual basis of accounting, expenses should be recorded in the accounting books when incurred.

#### Condition and Context

We examined supporting documentation of all fund transfers performed during the current accounting period from the Revolving Fund to the Environmental Quality Board to reimburse administrative expenses paid on behalf of the Revolving Fund. We noted that prior year expenses amounting $972,653 were not previously accrued and were recorded as current expenses on the period under audit.

#### Cause and Effect

Prior years' expenses were not accurately estimated when recorded on accounting books. This cause may result in that expenses reported in the current accounting period are overstated and do not agree with the expenses incurred.

#### Recommendation

Management should establish procedures to ensure that expenses incurred during the fiscal year are recorded in the accounting books at year end.

#### Views of Responsible Officials and Planned Corrective Actions

For an extended period of time, most of the Revolving Fund's operating expenses were incurred by the EQB as program administrator. These expenses were estimated and accrued for financial statement purposes but were not being promptly reimbursed to the EQB, partly because of its High Risk designation by the EPA. As expected, a variance arose between the amounts that were being accrued as expenses and the actual expenses that were reimbursed to the EQB.

To make sure Revolving Fund expenses are actually recorded in a timely manner and to assure proper matching of revenues and expenses within every 12 month fiscal period, GDB and the EQB have been designing a mechanism by which expense payment will be drawn against Revolving Fund's cash on hand at the GDB instead of against federal funds. On May 2014, the EPA lifted the High Risk Designation and allowed the EQB approved fund request method to pay expenses in advance instead of by reimbursement. EQB is considering requesting advance payment of expenses to be incurred on behalf of the Revolving Fund, thereby virtually eliminating any possibility for the need of expense accrual estimation, except for some immaterial amounts on incurred but unpaid expenses as of the audited financial statements fiscal year closing date.

## Section III-Federal Award Findings and Questioned Costs

The audit report for the year ended June 30, 2015, dated February 8, 2016, has no federal award findings.

**Finding No. 2014-01 Federal Funding Accountability and Transparency Act-Sub award Reporting**

**Federal Program Name**

Capitalization Grants for Clean Water State Revolving Funds CFDA No. 64.458

**Name of Federal Agency**

U.S. Environmental Protection Agency

**Award Number and Year**

Various awards

**Program requirement:**

Reporting

**Questioned costs:**

None

**Criteria**

In accordance with the Federal Funding Accountability and Transparency Act (FFATA), a primary grantee must report each action that obligates $25,000 or more in Federal funds to other entity for a sub grant under a federal grant. A primary grantee must record the required information in the FFATA Sub-award Reporting System (FSRS). Also the grant agreement with the U.S. Environmental Protection Agency requires that the Revolving Fund comply with the sub award reporting under FFATA.

**Condition**

The Revolving Fund has not reported sub-awards in the FFATA Sub-award Reporting System.

**Cause and Effect**

Management has not developed procedures to report sub-awards in the FFATA Sub-award Reporting System.

**Recommendation**

Management must put in place procedures to ensure that sub-awards subject to FFATA reporting are reported in the FFATA Sub-award Reporting System.

**Views of Responsible Officials and Planned Corrective Actions**

On various occasions, EQB has requested (via e-mail and telephone calls) guidance and support from EPA as to the initial applicability of the FFATA reporting requirements with respect to the program. Such requests have not been answered. Therefore, EQB has not been able to establish FFATA reporting procedures or develop a work plan to submit FFATA reports.