***Puerto Rico Industrial Development Company***
***(A Component Unit of the Commonwealth of Puerto Rico)***
*Basic Financial Statements and Other Supplementary Information for the Year Ended June 30, 2015, and Independent Auditors' Report*

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HLB PARISSI
Certified Public Accountants, Tax & Business Advisors

# INDEPENDENT AUDITORS' REPORT

To the Board of Directors of the
Puerto Rico Industrial Development Company
San Juan, Puerto Rico

## Report on the Financial Statements

We have audited the accompanying basic financial statements of the ***Puerto Rico Industrial Development Company*** (PRIDCO) (a component unit of the Commonwealth of Puerto Rico), as of and for the year ended June 30, 2015, and the related notes to basic financial statements, which collectively comprise PRIDCO'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 misstatements, whether due to fraud or error.

### *Auditors' 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. 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 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 controls. 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 that we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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### *Basis for Qualified Opinion and Note Disclosure Regarding Pensions*

As discussed in Notes 1 and 11 to the basic financial statements, PRIDCO has not implemented the requirements of Statement No. 68 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27 (Statement 68)*. Accordingly, PRIDCO has not been able to determine and account for its proportionate share of net pension liability, deferred inflow of resources and deferred outflow of resources related to pension costs, and has not recognized the effect of current period changes in net pension liability, deferred outflow of resources and deferred inflow of resources as these relate to pension costs.

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

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

### *Qualified Opinion*

In our opinion, except for the possible effects of the matter described above in the Basis for Qualified Opinion and Note Disclosure Regarding Pensions paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the ***Puerto Rico Industrial Development Company*** as of June 30, 2015 and the changes in its financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### *Emphasis of Matter*

*Financial Deterioration of the Commonwealth of Puerto Rico (Commonwealth) and of the Government Development Bank for Puerto Rico (GDB)*

As discussed in Notes 2, 9 and 10 to the basic financial statements, PRIDCO has significant balances and transactions with the Commonwealth and GDB. As of June 30, 2015, the financial condition and liquidity of the Commonwealth and GDB has deteriorated and, therefore, the collectability of amounts receivable from the Commonwealth for the payments to be made to GDB may be affected. Considering the relationship of PRIDCO with the Commonwealth and GDB, PRIDCO's financial condition and liquidity could be similarly affected. PRIDCO has evaluated the possible effects of the budgetary constraints and liquidity risks being faced by the Commonwealth and GDB on its basic financial statements and operations, and has concluded that, as of June 30, 2015, PRIDCO will continue to operate as a going concern for a period not less than twelve months after such date.

***Other Matters***

*Required Supplementary Information Omitted*

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

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 to 7 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 inquires 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 comprise the ***Puerto Rico Industrial Development Company's*** basic financial statements. The schedule of changes in cash and sinking fund per trust indenture for the year ended June 30, 2015, included on page 30 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

H.B. Parissi PSC

San Juan, Puerto Rico
March 31, 2016

Stamp No. E195835 was affixed
to the original of this report
License No. 88 expires December 1, 2017

The ***Puerto Rico Industrial Development Company*** (PRIDCO) management provides annual financial report and the discussion and analysis of PRIDCO's financial performance during the fiscal year ended June 30, 2015. This report includes management's discussion and analysis, the independent auditors' report, the basic financial statements, the notes that explain in more detail the information contained in the financial statements, and a supplemental schedule, which is not a required part of the basic financial statements.

***Financial Analysis***

*The Statement of Net Position and the Statement of Revenue, Expenses and Changes in Net Position*

The Statement of Net Position and the Statement of Revenue, Expenses and Changes in Net Position report information about PRIDCO and about its activities in a way that helps financial statements users to understand whether PRIDCO's financial health is improving or deteriorating. These statements include all assets and liabilities, using the accrual basis of accounting, which is similar to the accounting method used by private sector companies. All revenues and expenses are taken into account, regardless of when cash was received or paid. The statement of net position present the value of PRIDCO's assets and liabilities, with the difference between them reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of changes in PRIDCO's financial position. However, one will need to consider other nonfinancial factors such as changes in economic conditions and new or ammendments to government legislation. The condensed net position information for PRIDCO is presented as follows (in thousands):

| | June 30, | | Change | |
|---|---|---|---|---|
| | 2015 | 2014 | In dollars | Percent |
| Current assets | $ 63,825 | $ 77,433 | $ (13,608) | (18)% |
| Capital assets, net | 661,771 | 659,891 | 1,880 | - % |
| Other noncurrent assets | 67,751 | 67,746 | 5 | - % |
| Total assets | $ 793,347 | $ 805,070 | $ (11,723) | (1)% |
| Current liabilities | $ 75,271 | $ 160,726 | $ (85,455) | (53)% |
| Noncurrent liabilitities | 343,047 | 265,428 | 77,619 | 29 % |
| Total liabilities | 418,318 | 426,154 | (7,836) | (2)% |
| Net position: | | | | |
| Net investment in capital assets | 389,246 | 393,732 | (4,486) | (1)% |
| Restricted | 13,690 | 19,577 | (5,887) | (30)% |
| Deficit | (27,907) | (34,393) | 6,486 | (19)% |
| Total net position | 375,029 | 378,916 | (3,887) | (1)% |
| Total liabilities and net position | $ 793,347 | $ 805,070 | $ (11,723) | (1)% |

In addition, the condensed changes in net position information is presented below (in thousands):

| | June 30, | | Change | |
|---|---|---|---|---|
| | 2015 | 2014 | Amount | Percent |
| **Operating revenues:** | | | | |
| Rental income, net | $ 61,832 | $ 61,717 | $ 115 | - % |
| **Nonoperating revenues:** | | | | |
| Net gain on sale of properties | 6 | 1,604 | (1,598) | (100)% |
| Net investment income, interest and other | 559 | 1,340 | (781) | (58)% |
| Total nonoperating revenues | 565 | 2,944 | (2,379) | (81)% |
| Total revenues | 62,397 | 64,661 | (2,264) | (4)% |
| **Operating expenses:** | | | | |
| Salaries and wages | 16,410 | 18,304 | (1,894) | (10)% |
| Administrative, general and other expenses | 30,239 | 26,128 | 4,111 | 16 % |
| Depreciation and amortization | 20,600 | 20,600 | - | - % |
| Total operating expenses | 67,249 | 65,032 | 2,217 | 3 % |
| **Nonoperating expenses - interest** | 18,787 | 20,550 | (1,763) | (9)% |
| Total expenses | 86,036 | 85,582 | 454 | 1 % |
| Loss before capital contributions and special item | (23,639) | (20,921) | (2,718) | 13 % |
| **Capital contributions** | 19,752 | 44,405 | (24,653) | (56)% |
| Change in net position | (3,887) | 23,484 | (27,371) | (117)% |
| **Net position, beginning of year** | 378,916 | 355,432 | 23,484 | 7 % |
| **Net position, end of year** | $ 375,029 | $ 378,916 | $ (3,887) | (1.03)% |

## Analysis of Net Position

As of June 30, 2015, net position of $375 million is composed of $389 million of net investment in capital assets, $14 million restricted and a deficit of $28 million. Total net position changed from $379 million to $375 million, a decrease of approximately $4 million or 1.00%. Current assets decreased by approximately $14 million or 18%. The decrease in current assets is related to a decreased in cash and cash equivalents of approximately $3 million that were used to pay commitments related to Act 66, payments of retirement benefits, insurance and building repair and maintenance. Also, investments decreased by approximately $4 million. Investments were retired to be used for the payment of the construction of various facilities. In addition, the decrease in current assets is due to the decrease in accounts receivable related to a write-off of approximately $2 million and a decreased in sinking fund of approximately $3 million.

Restricted position is mainly composed of amounts deposited in the sinking fund for payments of bonds payable. Restricted position decreased by approximately $5.9 million or 30%, mostly as a result of an increase of $2 million paid as a deposit of principal of the debt, as required by debt agreements. The deficit decreased to $28 million in 2015 from $34.4 million in 2014 mostly as a result of a loss before capital contributions and special items of approximately $24 million partially offset by $20 million in contributions used to acquire capital assets. The decrease in investment in sinking fund is due to that monies were used to pay interest due on July 1, 2015.

**Year Ended June 30, 2015 versus June 30, 2014**

Net gain on sale of properties decreased approximately $1.6 million, or 100%, as a result of PRIDCO's decision to reduce its program to sell properties. Management has decided to modify this strategy by renting existing available facilities, under different arrangements, rather than selling the facilities.

Administrative, general and other expenses increased by approximately $4.1 million or 16%, due to an increase in expenses related to Act 66 of June 2014 of approximately $1.5 million, an increase in provision for environmental matters of approximately $1 million, and an increase in related to pension fund of approximately $2 million.

Interest expenses for the year ended June 30, 2015 amounted to approximately $18.8 million, a decrease of approximately $1.8 million (10%), related with the line of credits, bonds and with the notes payable to GDB. The decrease in interest expense was more related to the decrease on overall debt level, and rates.

Capital contributions for the year ended June 30, 2015, amounted to approximately $19.8 million from the Special Fund for Economic Development and from the Special Incentives Fund for building and improvements. The decrease results from loss availability of funds to provide incentives. During the prior year, capital contributions included $14.1 million from a project of the PRIDCO's building division, which was concluded during the prior year.

***Capital Assets***

PRIDCO's investment in capital assets as of June 30, 2015 and 2014 amounted to approximately $661.8 million and $659.9 million, respectively, net of accumulated depreciation. Capital assets include land, land held for improvement, construction in progress, industrial development buildings and improvements, administration buildings and improvements, machinery, equipment, furniture, and vehicles.

During the years ended June 30, 2015 and 2014, PRIDCO invested approximately $25.8 million and $12.7 million, respectively, mainly related to addition of building and construction of buildings that will be leased to private organizations, as part of the industrial development activities. This construction activity was mainly financed through lines of credit and special financing from commercial banks which are later refinanced on a long-term basis. Rent from the buildings is pledged for the payment of long term debt (See Debt Administration below).

As disclosed in Note 7 to basic financial statements, certain properties, with a book value of $4.2 million, are mortgaged with GDB as a collateral of a financing agreement provided by GDB to the Puerto Rico Ports Authority.

See Note 7 to the basic financial statements for additional details on capital assets at year end and activity during the fiscal year.

***Debt Administration***

At June 30, 2015 and 2014, PRIDCO had approximately $179.9 million and $189.4 million, respectively, in outstanding bonds payable, including the current portion of $12.9 million and $10.0 million at June 30, 2015 and 2014, respectively.

The credit rating of PRIDCO's public debt is "CCC-", as determined by Standards & Poor's in June 2015 and "Caa3", as determined by Moody's Investor Services in July 2015. Detailed information regarding long-term debt activity is included in Note 10 to the basic financial statements.

**Current Known Facts**

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

As disclosed in Note 11 to the basic financial statements, PRIDCO was not able to implement the requirements of Statement No. 68 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Pension*, (GASB 68). PRIDCO's inability to implement the requirements of GASB 68 resulted from the unavailability of the required information that was expected to be provided by The Employee Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS), a pension trust fund of the Commonwealth, which is not under the PRIDCO's management and control. Therefore, as of the date of this report, it is not known when the required information shall be provided to enable PRIDCO to implement the requirements GASB 68 and, therefore, PRIDCO is not able to determine the possible impact on its basic financial statements. This situation resulted in the expression of a qualified opinion from our external auditors.

*Financial Deterioration of the Commonwealth of Puerto Rico (Commonwealth) and the Government Development Bank for Puerto Rico (GDB)*

As disclosed in Note 2, the financial condition and liquidity of the Commonwealth and GDB has deteriorated and, therefore, the collectability of certain amounts due from the Commonwealth that are designated for the payment of certain amounts due to GDB may not be collected. (See Note 9). Considering the relationship of PRIDCO with the Commonwealth and GDB, PRIDCO's financial condition and liquidity could be similarly affected. PRIDCO has evaluated the possible effects of the budgetary constraints and liquidity risks being faced by the Commonwealth and GDB on its basic financial statements and operations, and has concluded that, as of June 30, 2015, PRIDCO will continue to operate as a going concern for a period not less than twelve months after such date.

***Contacting PRIDCO's Financial Management:***

This financial report is designed to provide our customers and creditors with a general overview of the PRIDCO's finances and to demonstrate PRIDCO's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Puerto Rico Industrial Development Company, P.O. Box 362530, San Juan, Puerto Rico, 00936-2530.

* * * * *

*Puerto Rico Industrial Development Company*
*(A Component Unit of the Commonwealth of Puerto Rico)*
*Statement of Net Position (In thousands)*
*June 30, 2015*

| | | |
|---|---|---|
| **ASSETS** | | |
| **Current assets:** | | |
| Cash and cash equivalents | $ | 13,454 |
| Investment in certificates of deposits | | 22,467 |
| Sinking fund, restricted | | 6,336 |
| Rent and accounts receivable, net | | 19,825 |
| Prepaid expenses and other assets | | 1,743 |
| Total current assets | | 63,825 |
| **Noncurrent assets:** | | |
| Sinking fund reserve accounts, at accreted cost, restricted | | 22,005 |
| Investment in equity securities, at cost | | 4,093 |
| Due from the Commonwealth of Puerto Rico | | 41,653 |
| Capital assets, net: | | |
| Land and construction in progress | | 271,784 |
| Buildings, improvements, machinery | | 389,987 |
| Total noncurrent assets | | 729,522 |
| Total assets | $ | 793,347 |
| **LIABILITIES AND NET POSITION** | | |
| **Current liabilities:** | | |
| Current portion of: | | |
| Loans and notes payable to commercial banks | $ | 14,659 |
| Bonds payable | | 12,865 |
| Obligations under capital leases | | 100 |
| Accounts payable and other accrued liabilities | | 26,428 |
| Due to the Commonwealth of Puerto Rico | | 14,987 |
| Environmental liabilities | | 2,440 |
| Accrued interest | | 1,971 |
| Termination benefits accrual, current portion | | 917 |
| Deposits | | 904 |
| Total current liabilities | | 75,271 |

*(continued)*

*Puerto Rico Industrial Development Company*
*(A Component Unit of the Commonwealth of Puerto Rico)*
*Statement of Net Position (In thousands)*
*June 30, 2015*

| | |
|---|---|
| **Noncurrent liabilities:** | |
| Bonds payable | $ 166,994 |
| Notes payable to Government Development Bank | 86,325 |
| Loans and notes payable to commercial banks | 64,101 |
| Termination benefits accrual | 7,319 |
| Rent and other deposits | 6,702 |
| Legal liabilities | 6,018 |
| Contract retention | 2,796 |
| Environmental liabilities | 2,567 |
| Obligations under capital leases | 225 |
| Total noncurrent liabilities | 343,047 |
| Total liabilities | 418,318 |
| **Net position:** | |
| Net investment in capital assets | 389,246 |
| Restricted | 13,690 |
| Deficit | (27,907) |
| Total net position | 375,029 |
| Total liabilities and net position | $ 793,347 |

*(concluded)*

See notes to basic financial statements.

***Puerto Rico Industrial Development Company***
***(A Component Unit of the Commonwealth of Puerto Rico)***
*Statement of Revenue, Expenses, and Changes in Net Position (In thousands)*
*For the Year Ended June 30, 2015*

| | |
|---|---|
| **Operating revenue:** | |
| Rental income, substantially from industrial properties, net | $ 61,832 |
| **Operating expenses:** | |
| Salaries and wages | 16,410 |
| Administrative and general | 23,307 |
| Depreciation and amortization | 20,600 |
| Maintenance and repairs, net | 6,932 |
| Total operating expenses | 67,249 |
| Operating loss | (5,417) |
| **Nonoperating revenues/(expenses):** | |
| Net gain on sale of properties | 6 |
| Net investment income | 211 |
| Interest income on loans | 348 |
| Interest expense | (18,787) |
| Total nonoperating expenses, net | (18,222) |
| Loss before capital contributions: | (23,639) |
| Capital contributions: | |
| Special Fund for Economic Development | 19,752 |
| Change in net position | (3,887) |
| **Net position, beginning of year** | 378,916 |
| **Net position, end of year** | $ 375,029 |

See notes to basic financial staements.

*Puerto Rico Industrial Development Company*
*(A Component Unit of the Commonwealth of Puerto Rico)*
*Statement of Cash Flows (In thousands)*
*For the Year Ended June 30, 2015*

| | |
|---|---|
| **Cash flows from operating activities:** | |
| Cash collected from rental income | $ 64,720 |
| Cash paid for salaries and benefits | (17,128) |
| Cash paid for supplies and services | (31,682) |
| Net cash provided by operating activities | 15,910 |
| **Cash flows from capital and related financing activities:** | |
| Collection of capital contributions | 19,752 |
| Payments for capital assets | (22,785) |
| Payments of obligations under capital leases | (280) |
| Payments of bonds payable | (10,020) |
| Proceeds from notes and loan payables | 14,862 |
| Payments of notes and loan payables | (15,284) |
| Interest paid | (19,701) |
| Net cash used in capital and related financing activities | (33,456) |
| **Cash flows from noncapital and related financing activities:** | |
| Net payments from Commonwealth of Puerto Rico | 7,296 |
| Payment of notes payable GDB | (1,000) |
| Net cash provided by noncapital and related financing activities | 6,296 |
| **Cash flows from investing activities:** | |
| Net change in sinking fund - redemption and bond service accounts | 3,377 |
| Investment in certificate of deposit | (125) |
| Interest collected on investments, loans and other nonoperating revenue | 559 |
| Collections from notes receivable | 29 |
| Net cash provided by investing activities | 3,840 |
| **Net decrease in cash and cash equivalents** | (7,410) |
| **CASH AND CASH EQUIVALENTS, beginning of year** | 20,864 |
| **CASH AND CASH EQUIVALENTS, end of year** | $ 13,454 |

*(continued)*

***Puerto Rico Industrial Development Company***
***(A Component Unit of the Commonwealth of Puerto Rico)***
*Statement of Cash Flows (In thousands)*
*For the Year Ended June 30, 2015*

| | | |
|---|---|---|
| **Reconciliation of operating Loss to net cash provided by operating activities:** | | |
| Operating loss | $ | (5,417) |
| Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization expense | | 20,600 |
| (Increase)/Decrease in accounts receivable and deposits | | 2,499 |
| (Increase)/Decrease in prepaid expenses and other assets | | 426 |
| Decrease in termination benefits accrual | | (718) |
| Increase in rent deposits and other assets | | 533 |
| Increase in accounts payable and accrued liabilities | | (2,013) |
| Net cash provided by operating activities | $ | 15,910 |
| **Supplemental cash flow information:** | | |
| Accretion of bonds payable | $ | 506 |
| Amortization of bond discount | | 14 |
| Capital contributions - Special Fund for Economic Development | | 19,752 |
| Capital additions through obligations under capital leases | | 384 |

See notes to basic financial statements.

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Puerto Rico Industrial Development Company (PRIDCO) is a component unit of the Commonwealth of Puerto Rico (the Commonwealth), created in 1942 by Law No. 188, as amended. PRIDCO is engaged in promoting the development of new local enterprises and encouraging U.S. and foreign investors to establish and expand business operations in Puerto Rico. To accomplish its mission, PRIDCO, among its many programs, constructs industrial facilities for lease or sale to qualified enterprises.

*a.* ***Reporting Entity*** – The basic financial statements include all funds and activities administered by PRIDCO.

*b.* ***Measurement Focus, Basis of Accounting and Financial Statement Presentation*** – The accompanying basic financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses when incurred, regardless of when cash is received or paid.

*c.* ***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 reporting periods. Actual results could differ from those estimates.

*d.* ***Concentration of Credit Risk*** – PRIDCO maintains cash on deposit with high rated financial institutions and with the Government Development Bank in Puerto Rico (GDB), another component unit of the Commonwealth. The laws of the Commonwealth require from commercial banks to fully collateralize all public funds deposited with them in excess of the amount insured by the Federal Government. The securities pledged by the banks as collateral for those deposits are under the custody of the Secretary of the Treasury in the name of the Commonwealth. Deposits with GDB and Economic Development Bank for Puerto Rico (EDB), are exempt from the collateralization requirement and represent a custodial credit risk, since in case of bankruptcy of the bank, PRIDCO would not recover its deposits. At June 30, 2015, there were no concentrations of credit risk.

*e.* ***Cash Equivalents*** – PRIDCO considers all highly liquid investments with original maturity of three months or less to be cash equivalents. As of June 30, 2015, cash equivalents amounted to $4.5 million.

*f.* ***Investments*** – PRIDCO is authorized to invest in Puerto Rico and U.S. government obligations or in obligations guaranteed by the Puerto Rico or U.S. governments, its agencies or instrumentalities, including mortgage loans secured or guaranteed under federal housing laws. The investment in certificates of deposit is restricted for the payment of construction works performed on one of the PRIDCO's industrial facilities. Investments in equity securities are stated at amortized cost and are mostly composed of common and preferred stock shares in private entities.

g. ***Rent Receivable, Notes and Lease Financing Receivable and Allowance for Doubtful Accounts*** – PRIDCO's rent receivable arises from the leasing of industrial facilities to its customers. Rent is calculated based on agreed rates on executed contracts. The allowance for doubtful accounts is established through provisions recorded as an offset of rental income. PRIDCO provides for an allowance for doubtful accounts, notes receivable and lease financing receivable upon an evaluation of the risks characteristics of those accounts, loss experience, economic conditions and other pertinent factors. Charge-offs is recorded against the allowance when management believes that the collectability of the principal is unlikely. Recoveries of amounts previously charged-off are credited to the allowance. Notwithstanding this, the allowance is subject to and may be adjusted in the future because of changes in the economic or market conditions.

Notes and lease financing receivables are presented at the outstanding unpaid principal balance reduced by the allowance for losses. These are measured for impairment when it is probable that all amounts, including principal and interest, will not be collected in accordance with the contractual terms of the loan agreement. No impairment was deemed necessary for the year ended June 30, 2015.

h. ***Restricted Assets*** – Restricted assets at June 30, 2015, consist of sinking fund to be used for the payment of debt service and sinking fund requirements, and investments in certificate of deposit restricted for the construction in Juana Díaz, and are composed of the following (in thousands):

| | |
|---|---|
| Debt service and sinking fund balance with Trustee | $ 28,341 |
| Liabilities payable from restricted assets consists of the following: | |
| Bonds payable within one year | 12,865 |
| Interest payable | 1,786 |
| Total liabilities payable from restricted assets | 14,651 |
| Net restricted assets | $ 13,690 |

i. ***Capital Assets*** – Capital assets are stated at cost, net of accumulated depreciation. Cost of construction includes, among other things, interest costs, indirect costs consisting of payroll taxes, and other fringe benefits. Depreciation is computed on the straightline method at rates considered adequate to allocate the cost of the various type of property over their estimated useful lives. Expenditures for maintenance and repair costs that do not improve or extend the life of the respective assets are charged to operations as incurred. Additions, renewals, and betterments, unless of relatively minor amounts, are capitalized. Estimated useful lives and capitalization thresholds are as follows:

| | Years | Capitalization Threshold (In thousands) |
|---|---|---|
| Buildings and buildings improvements | 50 | $ 1 |
| Machinery and equipment | 15 | $ 1 |
| Furniture and vehicles | 5-15 | $ 1 |

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. Impaired capital assets that will no longer be used by PRIDCO should be reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by PRIDCO 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.

*j.* ***Operating Revenue and Expenses*** – PRIDCO distinguishes operating revenue and expenses from non-operating items. Operating revenue and expenses generally result from providing services in connection with the principal ongoing operations. Revenue and expenses not meeting this definition are reported as non-operating revenue and expenses.

*k.* ***Revenue Recognition*** – Revenue from rental activities related to industrial properties is reported as revenue on the accrual basis over the term of the leases based on the monthly rental fees established by each lease agreement. Most of the leases in effect are cancelable, subject to penalty in case of early termination. Revenue from non-exchange transactions consists of intergovernmental grants, including contributions in aid for construction, mainly from two funds of the Commonwealth. These are recorded as revenue as soon as all eligibility requirements are met. Contributions received by PRIDCO for construction and improvements of capital assets during the years ended June 30, 2015, amounted to $19.7 million received from the Special Fund for Economic Development.

*l.* ***Compensated Absences*** – Employees earn 30 days of vacation and 18 days of sick leave annually. Vacation and sick leave may be accumulated at a maximum of 60 days and 90 days, respectively. The excess of 60 days in vacation and of 90 days of sick leave, until December 31st of each year, should be paid to the employee before March 31st of the following year. For employees under collective bargaining agreement, the excess of 60 days in vacation and of 90 days of sick leave, until June 30 of each year, should be paid to the employee before July 31st of the following year.

*m.* ***Termination Benefits*** – PRIDCO recognize a liability and expense for voluntary termination benefits when the offer is accepted and the amount can be estimated.

## 2. SIGNIFICANT DEPENDENCY ON COMMONWEALTH OF PUERTO RICO

As part of its normal operating activities, and as disclosed in Notes 9 and 10 to the basic financial statements, PRIDCO has significant balances and transactions with the Commonwealth of Puerto Rico (the Commonwealth) and with the Government Development Bank for Puerto Rico (GDB). As of June 30, 2015, the Commonwealth and GDB face significant uncertainties, including liquidity risk, which is the risk of not having sufficient liquid financial resources to meet their obligations when they come due. Because of these uncertainties, the amounts due from Commonwealth, disclosed in Note 9, may not be collected in the near future, and PRIDCO's management is unable to determine when such amounts will be appropriated by the Legislature of the Commonwealth. Concurrently, these amounts due from Commonwealth are the sole source for the payment of the note payable to GDB, as disclosed in Note 10 to the basic financial statements.

PRIDCO has evaluated the possible effects of the uncertainties and liquidity risks being faced by the Commonwealth and GDB, on its basic financial statements and operations, and has concluded that, as of June 30, 2015, PRIDCO will continue to operate as a going concern for a period not less than twelve months after such date.

## 3. SINKING FUND

As of June 30, 2015, PRIDCO held a sinking fund with U.S. Bank (the Trustee), to be used for the payment of bonds payable debt service and sinking fund requirements. At June 30, 2015, investments held by said sinking fund are all due within one year and consist of $28.3 million of money market funds held at U.S. Bank Trust National Association.

Expected maturities may differ from contractual maturities because borrowers may have the right to call or repay obligations with or without call or prepayment penalties.

The credit ratings for the investments held in sinking fund as of June 30, 2015, were BB- by Standards & Poors, and Ba3 by Moody's Investor Services.

## 4. INVESTMENT IN AND ADVANCES TO PUERTO RICO SOUTHERN INDUSTRIAL DEVELOPMENT COMPANY

Puerto Rico Southern Industrial Development Company (SIDCO) is a related organization engaged in promoting the development of the economy of Puerto Rico, with its sole facility in Guayama, Puerto Rico that is currently leased to a pharmaceutical company. The agreement calls for an annual rent equal to the amounts due and payable by SIDCO under various notes payable agreements and any other expenses incurred by SIDCO related to the facility's construction. During the term of the lease, the pharmaceutical company may exercise, at any time, an option to purchase the plant at a price equal to the outstanding amount of the notes and other plant-related obligations plus $750 thousand. Pursuant to the terms of the agreement, the pharmaceutical company exercised the right to extend the initial term of the lease for two successive renewal periods, the first renewal for a time ending 20 years (2017) after the date of commencement of operations of the pharmaceutical company's tax-exemption grant, whichever date is later and the second renewal for an additional period of 7 years commencing upon the expiration of the first renewal period.

At June 30, 2015, summarized information regarding SIDCO's assets follows (in thousands):

| | |
|---|---|
| Current assets | $ 678 |
| Land and plant | 90,118 |
| Total assets | 90,796 |
| Contribution by pharmaceutical company | (89,911) |
| Other liabilities | (444) |
| Investment in SIDCO, net | $ 441 |

SIDCO's only activity is the leasing of this facility. During 2001, SIDCO acquired a land facility by entering into a promissory note in the amount of $1.6 million. Pursuant to the terms of the promissory note, the parties agreed upon as follows:

- SIDCO shall not be obligated to pay the unpaid balance of principal hereunder, and this obligation shall become null and void, in the event the pharmaceutical company terminates early the lease and option agreement entered within.

- In the event the pharmaceutical company or the successor lessor under the lease exercises the option to purchase the plant pursuant to the lease, then the unpaid principal balance due on the promissory note shall be automatically accelerated and become due and payable in accordance with the lease agreement.

It is management's opinion that the pharmaceutical company will exercise its purchase option in the future. Accordingly, the assets of SIDCO have not been blended within PRIDCO's financial statements.

## 5. RENT AND ACCOUNTS RECEIVABLE

Rent and accounts receivable as of June 30, 2015, consist of the following (in thousands):

| | | |
|---|---|---|
| Rent receivable | $ | 21,550 |
| Loans receivable | | 11,684 |
| Others | | 7,111 |
| Total | | 40,345 |
| Less: Allowance for doubtful accounts | | (20,520) |
| Rent and accounts receivable, net | $ | 19,825 |

Changes in the allowance for doubtful accounts during the year ended June 30, 2015 is as follows (in thousands):

| | | |
|---|---|---|
| Allowance for doubtful accounts beginning of year | $ | 23,768 |
| Plus: Provision of doubtful accounts | | 3,900 |
| Less: Accounts written-off | | (7,148) |
| Allowance for doubtful accounts, end of year | $ | 20,520 |

## 6. NOTES RECEIVABLE

Notes receivable mostly represent the principal amount of various non-revolving promissory notes issued by PRIDCO to qualifying exempt businesses and to one Municipality of Puerto Rico for the purpose of partially financing the acquisition of machinery and land premises and working capital needs. Notes receivable as of June 30, 2015 consist of the following (in thousands):

| | |
|---|---|
| Non-revolving note receivable to qualified exempt business for the purpose of partially financing the acquisition of machinery and working capital needs, bearing interest at 4.25% during the term of the loan. This note is due in monthly installments of $5 thousand commencing on March 1, 2010 to September 1, 2023 and a final monthly payment of $4 thousand due on October 1, 2023 and is collateralized by a lien on machinery and equipment and insurance policies covering the replacement value of equipment and machinery. | $ 439 |
| Non-revolving note receivable to qualified exempt business for the purpose of partially financing the acquisition of machinery and working capital needs, bearing interest at 8% during the term of the loan. This note is due in monthly installments of $2 thousand commencing on December 1, 2004 over a 20-year period, and is collateralized by a lien on machinery and equipment and insurance policies covering the replacement value of equipment and machinery. | 452 |
| Total | 891 |
| Less allowance for doubtful accounts | (891) |
| Total, net of allowance for doubtful accounts | $ - |

Under these credit facilities, the outstanding principal balance may be prepaid without penalty.

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## 7. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2015 consists of the following (in thousands):

| | Beginning Balance | Additions | Reductions | Ending Balance |
|---|---|---|---|---|
| Capital assets not being depreciated: | | | | |
| Land held for improvement | $ 162,484 | $ 690 | $ - | $ 163,174 |
| Land on leased projects | 72,156 | - | - | 72,156 |
| Construction in progress | 17,095 | 21,965 | (2,606) | 36,454 |
| Total capital assets not being depreciated | 251,735 | 22,655 | (2,606) | 271,784 |
| Capital assets being depreciated: | | | | |
| Buildings and improvements | 773,767 | 2,612 | (689) | 775,690 |
| Machinery and equipment | 72,757 | 391 | - | 73,148 |
| Furniture and vehicles | 13,675 | 117 | - | 13,792 |
| Total capital assets being depreciated | 860,199 | 3,120 | (689) | 862,630 |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | (382,457) | (17,276) | - | (399,733) |
| Machinery and equpment | (58,326) | (2,541) | - | (60,867) |
| Furniture and vehicles | (11,260) | (783) | - | (12,043) |
| Total accumulated depreciation | (452,043) | (20,600) | - | (472,643) |
| Total capital assets being depreciated, net | 408,156 | (17,480) | (689) | 389,987 |
| Total capital assets, net | $ 659,891 | $ 5,175 | $ (3,295) | $ 661,771 |

PRIDCO evaluated its capital assets for impairment and no impairment charges were recorded during the year ended June 30, 2015.

On December 5, 2014, the Puerto Rico Ports Authority (Ports), another component unit of the Commonwealth, entered into an $8 million financing agreement with GDB and used the proceeds for the development of certain repair, maintenance and overhaul aerospace facilities, at Rafael Hernández Airport, in Aguadilla, Puerto Rico, a property of Ports. Also, the Special Development Economic Fund agreed to provide a $6.4 million incentive for the creation of new employment at that project, and the Special Incentives Fund, both fiduciary funds of the Commonwealth, agreed to provide $40 million to supplement the construction of the facilities at the Airport.

To secure the $8 million financing provided by GDB to Ports, on that same date, PRIDCO entered into a voluntary mortgage agreement with GDB, and mortgaged certain non-bonded properties, with a carrying value of $4.2 million, as collateral for this financing, for an amount not to exceed $10 million. This agreement establishes that PRIDCO is not a debtor or co-debtor for the Ports financing, and does not have any other responsibility, other than to provide these properties as collateral in case of default or noncompliance by Ports, up to $10 million. The mortgage note is due and payable on December 5, 2044.

## 8. ACCOUNTS PAYABLE AND OTHER ACCRUED LIABILITIES

Accounts payable and other accrued liabilities as of June 30, 2015 consist of the following (in thousands):

| | | |
|---|---|---|
| Accounts payable | $ | 13,701 |
| Compensated absences | | 5,284 |
| Accrued payroll related expenses | | 939 |
| Other accrued liabilities | | 6,504 |
| Total | $ | 26,428 |

## 9. DUE TO AND FROM THE COMMONWEALTH OF PUERTO RICO

Amounts due from the Commonwealth as of June 30, 2015 consist of funds provided for granting industrial incentives to the Special Incentives Fund, a fiduciary fund of the Commonwealth, for $41.7 million with maturity date June 30, 2040. Prior to June 30, 2004, the Fund received monies from a line of credit established with the GDB through an agreement between the bank and PRIDCO, the Fund's administrator. Therefore, the outstanding balance of the line of credit was recorded in PRIDCO's financial statements and amounted to approximately $41.7 million as of June 30, 2015. Repayments for these notes are to be provided by COFINA through legislative appropriations.

Amounts due to the Commonwealth as of June 30, 2015 consist of the following (in thousands):

| Payable to | Purpose | | Amount |
|---|---|---|---|
| Rums of Puerto Rico Fund | Operating advances | $ | 7,389 |
| Puerto Rico Department of Economic Development | Management Fees | | 7,298 |
| Special Fund for Economic Development | Advance for acquisition of investment securities | | 300 |
| | | $ | 14,987 |

Rums of Puerto Rico Fund, Special Incentives Fund, and Special Fund for Economic Development are administered by PRIDCO on behalf of the Commonwealth. Management has concluded that these do not constitute funds of PRIDCO. Accordingly, they are not presented in the accompanying basic financial statements.

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## 10. LINES OF CREDIT AND LONG-TERM DEBT ACTIVITY

Lines of credit and long-term debt activity for the year ended June 30, 2015 were as follows (in thousands):

| | Beginning Balance | Additions | Accretion | Reductions | Ending Balance | Due Within One year |
|---|---|---|---|---|---|---|
| Bonds payable | $ 189,643 | $ - | $ 506 | $ (10,020) | $ 180,129 | $ 12,851 |
| Less: bond discount | (284) | - | - | 14 | (270) | 14 |
| Bond payable, net | 189,359 | - | 506 | (10,006) | 179,859 | 12,865 |
| Notes payable to GDB | 87,325 | - | - | (1,000) | 86,325 | - |
| Loans and notes payable | 79,182 | 14,862 | - | (15,284) | 78,760 | 14,659 |
| Obligations under capital leases | 221 | 384 | - | (280) | 325 | 100 |
| Total | $ 356,087 | $ 15,246 | $ 506 | $ (26,570) | $ 345,269 | $ 27,624 |

Loans and notes payable consist of the following (in thousands):

| | |
|---|---|
| Term loan payable in 180 monthly installments of $268 thousand including interest with a balloon payment for the remainder balance including interest due in June 2022. The loan bears interest at 6.06%. | $ 18,590 |
| Term loan payable in 138 monthly installments of $208 thousand including interest with a balloon payment for the remainder balance including interest due in June 2022. The loan bears interest at 5.38%. | 14,650 |
| Term loan payable in 180 monthly installments of $137 thousand including interest and is due in March 2018. The loan bears interest at 6.98%. | 12,425 |
| Non-revolving line of credit with 24 interest only payments then converted into a term loan payable in 216 monthly installments of $110 thousand including interest and is due in December 2024. The loan bears interest at 6.06%. | 9,621 |
| Term loan payable in 179 monthly installments of $118 thousand including interest, bearing interest at 5.46% and a final balloon payment due in October 2019. The loan is jointly and severally guaranteed by PRIDCO. | 5,649 |
| Non-revolving line of credit with 24 interest only payments then converted into a term loan payable in 216 monthly installments of $72 thousand including interest and is due in December 2024. The loan bears interest at 6.061%. | 6,181 |
| Term loan payable in 119 monthly installments of $38 thousand including interest and a last balloon payment due in February 2020. The loan bears interest at 8.45%. | 3,868 |

| | |
|---|---|
| Non-revolving line of credit and on conversion date will be converted into a term loan in a principal amount equivalent to the sum of outstanding balance of all advances made available under the line of credit up to $20 million. Payable in monthly installments including interest. Conversion date will be on the earlier to occur of the project has been substantially completed or October 6, 2015. The loan bears interest at 4.65%. | 6,742 |
| Note payable in monthly payments of $6 thousand and with due date of August 18, 2019. The note bears interest at 5.99%. | 262 |
| Term loan payable in monthly installments of $56 thousand including interest and is due in August 2016. The loan bears interest at 5.26% . | 772 |
| Total debt | 78,760 |
| Less current maturities | (14,659) |
| Loans and notes payable to commercial banks, noncurrent portion | $ 64,101 |

Notes payable to the Government Development Bank for Puerto Rico (GDB) are comprised as follows (in thousands):

| | |
|---|---|
| Non-revolving line of credit up to $75 million with GDB to provide for payment of expenses related to the voluntary separation and early retirement plans, bearing interest at 7%, due November 1, 2024. Meanwhile, PRIDCO has agreed with GDB to continue making monthly installments of principal and interest according to original terms. PRIDCO identified several properties to be disposed of for repayment of this debt and placed as collateral several other non-trusted properties. | $ 44,672 |
| Notes payable that were used to grant industrial incentives under the Special Incentives Fund, a fund of the Commonwealth, which is administered by PRIDCO. Repayments for these notes are provided by the Puerto Rico Sales Tax Financing Corporation (COFINA) and Commonwealth under legislative appropriation. The notes are due on June 30, 2040 and bear interest at 7%. Since these lines of credit are payable only from resources to be provided by COFINA and Commonwealth appropriations, PRIDCO has recorded an amount due from Commonwealth for the same amount. (See Note 2) | 41,653 |
| Total notes payable to GDB | $ 86,325 |

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Debt service requirements for the loans and notes payable to commercial banks and obligations under capital leases are as follows (in thousands):

| Year Ending | Due to Commercial Banks | | | Obligations under capital leases | | |
|---|---|---|---|---|---|---|
| June 30, | Principal | Interest | Total | Principal | Interest | Total |
| 2016 | $ 14,659 | $ 4,916 | $ 19,575 | $ 100 | $ 13 | $ 113 |
| 2017 | 7,831 | 3,910 | 11,741 | 82 | 9 | 91 |
| 2018 | 17,982 | 3,221 | 21,203 | 65 | 6 | 71 |
| 2019 | 7,699 | 2,156 | 9,855 | 71 | 2 | 73 |
| 2020 | 10,477 | 1,561 | 12,038 | 7 | - | 7 |
| 2021 to 2025 | 20,112 | 2,067 | 22,179 | - | - | - |
| Totals | $ 78,760 | $ 17,831 | $ 96,591 | $ 325 | $ 30 | $ 355 |

PRIDCO is subject to compliance with certain covenants on its loans and notes payable with three commercial banks. During the years ended June 30, 2015, PRIDCO did not comply with some of those covenants and the financial institutions waived the non-compliance as of March 31, 2016.

***Bonds Payable***

As required by the Trust Indenture dated July 1, 1964, as amended, PRIDCO has pledged and assigned to the Trustee the gross revenue from certain properties (known as trusteed properties) for the payment of the Refunding and General Purpose Revenue Bonds, Series 1991 to 1997. In the event that the gross revenue from trusteed properties and the amounts deposited with the Trustee are not sufficient, PRIDCO shall deposit with the Trustee such amounts as necessary to meet the debt service requirements.

During fiscal year 1998, PRIDCO issued approximately $150 million in refunding bonds and general purpose revenue bonds. The proceeds of the fiscal year 1998 bond issuance destined to refund the previous outstanding bonds were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments. As a result, all the Series prior to 1997, except for the Series 1991 serial and capital appreciation bonds were considered defeased and the liability for those bonds was considered extinguished and has been removed from the accompanying basic financial statements.

Revenue refunding and general purpose revenue bonds outstanding at June 30, 2015 are as follows (in thousands):

| | |
|---|---|
| Revenue Refunding Bonds and General Purpose Revenue Bonds: | |
| Series A 1997: | |
| Term bonds, 6.75%, due on July 1, 2021 | $ 22,815 |
| Series B 1997, 5.375%, due on july 1, 2016 | 16,910 |
| Series 2003 General Purpose Revenue Bonds: | |
| Series bonds, 5.10% to 5.15% due on July 1, 2017 and 2018 | 2,395 |
| Capital appreciation bonds, implicit interest rates of 5.15% to 5.20%, due on July 1, 2017 and July 1, 2018 | 9,904 |
| Term bonds, 5.20%, due on July 1, 2023 | 48,925 |
| Term bonds, 5.25%, due on July 1, 2028 | 78,910 |
| Total bonds payable | 179,859 |
| Less current maturities | (12,865) |
| Bonds payable - noncurrent | $ 166,994 |

Series 2003 of the capital appreciation bonds will accrete to a maximum of $11.6 million, through their corresponding maturity dates. The annual debt service requirements to maturity, including principal and interest, for bonds payable as of June 30, 2015 are as follows (in thousands):

| Year Ending June 30, | Principal | Interest | Total |
|---|---|---|---|
| 2016 | $ 12,865 | $ 9,119 | $ 21,984 |
| 2017 | 10,065 | 8,280 | 18,345 |
| 2018 | 7,333 | 10,783 | 18,116 |
| 2019 | 11,007 | 10,657 | 21,664 |
| 2020 | 11,135 | 7,012 | 18,147 |
| 2021-2025 | 65,785 | 24,967 | 90,752 |
| 2026-2028 | 57,301 | 6,172 | 63,473 |
| | 175,491 | $ 76,990 | $ 252,481 |
| Plus: Accreted discount | 4,638 | | |
| Less: Unamortized bond discount | (270) | | |
| Total | $ 179,859 | | |

***Obligations Under Capital Leases***

PRIDCO finances the acquisition of certain office equipment through capital leases from various financial institutions. Capital leases outstanding as of June 30, 2015, are payable in monthly installments of principal and interest ranging from $117 to $1,737 in 2015, through the year 2020. The obligations under capital leases are secured by the corresponding office equipment and bear interest rates ranging from 4.00% to 5.22% in 2015.

## 11. RETIREMENT PLAN

Substantially all full-time employees of PRIDCO participate in the Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS). The Employees Retirement System is a statutory trust created by Act No. 447 of May 15, 1951, as amended (Act 447) and a component unit of the Commonwealth.

On April 4, 2013, the Governor of Puerto Rico signed into law Act No. 3 of 2013, which represents a comprehensive reform of the ERS, which became effective on July 1, 2013 and amended the provisions of the different benefit structures under the ERS as further discussed below.

Members that entered the ERS before January 1, 2000 participated in a defined benefit program. Members who began to participate prior to April 1, 1990 (Act 447 Participants) were entitled to the highest benefits structure, while those who began to participate on or after April 1, 1990 (Act 1 Participants) were subject to a longer vesting period and a reduced level of benefits, as provided by Act No. 1 of February 16, 1990 (Act 1 of 1990).

In 1999, Act 447 was amended to close the defined benefit program for new participants and, prospectively, establish a new benefit structure similar to a cash balance plan (this new benefit structure is referred to as System 2000). Members who entered the ERS on or after January 1, 2000 (System 2000 Participants) participate solely in System 2000. Act 3-2013 amended the law to eliminate the lump sum distribution alternative and substitute it for a life annuity payable to the System 2000 Participant. System 2000 Participants do not benefit from any employer contributions. Instead, employer contributions made on account of System 2000 Participants are used to reduce the accumulated unfunded pension benefit obligation of the ERS. System 2000 is not a separate plan as there are no separate accounts for System 2000 Participants. Contributions received from System 2000 Participants are pooled and invested by the ERS together with the assets corresponding to the defined benefit structure of Act 447 and Act 1 of 1990 and the defined contribution structure of System 2000, as amended by Act 3-2013, will be paid from the same pool of assets of the ERS.

Retirement and related benefits provided by the ERS, and required contributions to the ERS by employers and employees, are determined by law rather than by actuarial requirements. As of July 1, 2011, after the adoption of Act 116 of July 6, 2011 (Act 116), the statutory employer contribution for the ERS increased from a minimum of 9.275% to a minimum of 10.275% of covered payroll, and will continue to increase annually until fiscal year 2021. The employer contribution rate for fiscal year 2015 is 13.275%.

The ERS provides basic benefits under the defined benefit program principally consisting of a retirement annuity and death and disability benefits (collectively referred to herein as Basic System Pension Benefits). The ERS also administers benefits granted under various special laws that have provided additional benefits for the retirees and beneficiaries (collectively referred to herein as System Administered Pension Benefits). The System Administered Pension Benefits include, among others, additional minimum pension, death and disability benefits, ad-hoc cost-of-living adjustments and summer and Christmas bonuses. Act 3-2013 and Act 160-2013 amended the various laws providing some of these System Administered Pension Benefits to reduce some of the amounts payable to existing retirees while eliminating the benefits for all future retirees (those retiring after June 30, 2013 and July 31, 2014).

The actuarial valuation of the Basic System Benefits and System Administered Benefits as of June 30, 2014 (most recently available) reflects a fiduciary net position of $127 million, total pension liability of $30.2 billion and a net pension liability of $30.1 billion.

Statement No. 68 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* (GASB 68) became effective for the year ended June 30, 2015. 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 that meet certain criteria.

As of the date of the release of this report, the ERS has not issued its 2014 basic financial statements, nor has it provided PRIDCO with the required information to implement the requirements of GASB 68. Therefore, the accompanying financial statements do not have any adjustments that will be necessary for PRIDCO to account for its proportionate share of the net pension liability, deferred inflow of resources and deferred outflow of resources in the statement of net assets as of July 1, 2014 and June 30, 2015, as well as the effect in the recorded pension expense in the statement of revenue, expenses and changes in net position for the year ended June 30, 2015. Also, additional disclosures required by GASB 68 as well as required supplementary information have been omitted from these basic financial statements.

## 12. COMMITMENTS

***Construction Program***

As of June 30, 2015, PRIDCO estimates to invest approximately $10 million for construction, land acquisition, and development.

***Other Commitments***

PRIDCO has only administrative responsabilities with regards to the Special Incentives Fund, Special Fund Economic Development, and Rums of Puerto Rico Fund.

PRIDCO maintains a joint agreement with the University of Puerto Rico for the administration of the Bioprocess Development and Training Complex (BDTC) in Mayagüez. Under said agreement, PRIDCO constructed a modern building with state of the art facilities for rental by pharmaceutical and high end technological industries with research and development projects. PRIDCO is therefore renting the building to BDTC. For the year ended June 30, 2015, the BDTC has received funding solely from the Special Fund for Economic Development.

PRIDCO maintains a joint interagency agreement along with the Puerto Rico Tourism Company (PRTC). Both entities agreed to provide $1 million each for the Office of Land Use Planning. PRIDCO is responsible for the purchase of office equipment as well as professional services necessary for the operations of said office. PRIDCO received $1 million from PRTC and total expenditures amounted to $672 thousand. PRTC did not make any contribution during the years ended June 30, 2015.

PRIDCO leases office in New York City under an operating lease with a third party expiring in the year 2022. Rent expense including common area maintenance, taxes and other charges amounted to approximately $343 thousand for the year ended June 30, 2015. Said office space is shared with GDB and Rums of Puerto Rico aiming towards the presence of the Commonwealth of Puerto Rico in one of the most important cities of the world. PRIDCO charges rent back to the previously mentioned governmental agencies based on space occupancy allocation.

Future annual minimum lease payments under the operating lease agreement at June 30, 2015, are as follows (in thousands):

| Year Ending June 30, | Amount |
|---|---|
| 2016 | $ 883 |
| 2017 | 883 |
| 2018 | 905 |
| 2019 | 926 |
| 2020 | 926 |
| 2021-2024 | 2,317 |
| Total | $ 6,840 |

## 13. CONTINGENCIES

PRIDCO is a defendant in a number of legal proceedings arising in the normal course of business, including but not limited to labor, torts, and breach of contract. Management believes that it has a reasonable possibility of prevailing in these cases. Contingency reserves as of June 30, 2015 amounted to approximately $6 million, and its included as part of accounts payable and other accrued liabilities.

## 14. POLLUTION REMEDIATION CONTINGENCIES

Because of the nature of the operations of the different tenants, under certain circumstances PRIDCO is responsible for pollution remediation in all its facilities. 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. At June 30, 2015, PRIDCO's reserve for pollution remediation obligations amounted to approximately $5 million, and was reported as environmental liabilities, $2.4 million presented as current liability, and $2.6 million presented as noncurrent liability.

PRIDCO has been a party to several claims and lawsuits related to environmental pollution remediation obligations in which the Federal Environmental Protection Agency (EPA) and the Puerto Rico Environmental Quality Board (EQB) have been involved for many years. Such liabilities are pursuant to the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA, or commonly known as Superfund), a United States federal law designed to cleanup sites contaminated with hazardous substances. This law authorizes EPA to identify parties responsible for contamination of sites and compel the parties to remediate environmental pollution.

Financial responsibility cleanup costs have been and/or are being undertaken by the industrial potentially responsible parties (PRP's) at two CERCLA sites (Vega Alta, Guayama, Cidra, Cabo Rojo, Maunabo and San Germán) where the federal government named PRIDCO a PRP solely for being part owner of both sites. There are other sites where PRIDCO has called former tenants in order to make them accountable for cleanup costs and some others are currently under remedial monitoring actions either by EPA or PRIDCO itself.

Experience has shown that uncertainties associated with environmental remediation contingencies are pervasive and often result in wide ranges of outcomes. Estimates developed in the early stages of remediation can vary significantly. A finite estimate of costs does not normally become fixed and determinable at a specific time. Rather, the costs associated with environmental remediation become estimable over a series of events and activities that help to frame and define a liability.

Estimates of the amount and timing of future costs of environmental remediation requirements are by their nature imprecise because of the continuing evolution of environmental laws and regulatory requirements, the availability and application of technology, the identification of presently unknown remediation sites and the allocation of costs among the potentially responsible parties. Based upon information presently available, such future costs are not expected to have a material effect on PRIDCO's financial position. However, such costs could be material to results of operations in a particular future year.

## 15. RISK MANAGEMENT

The Treasury Department of PRIDCO is responsible of assuring that PRIDCO's property is properly insured. Annually, the Treasury Department in conjunction with other departments of PRIDCO compiles the information of all property owned and its respective market value. After evaluating this information, it is submitted to the Area of Public Insurance at the Department of the Treasury of the Commonwealth, which is responsible for purchasing all property and casualty insurance policies of all governmental instrumentalities. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

## 16. SUBSEQUENT EVENTS

PRIDCO evaluated subsequent events through March 31, 2016, the date on which the financial statements were available to be issued.

Voluntary Pre-Retirement Program

On December 8, 2015, Act No. 211 was approved to create a Voluntary Pre-retirement Program. This Act, among other provisions, establishes that employees who started contributing to the ERS before April 1, 1990 with at least 20 years of service may be eligible to participate in the program. Those who participate in the program would be paid 50% of their average salary (except police officers, which would be paid 60%). These payments will be made until the employee becomes eligible to receive payments from the ERS. Other benefits would include the payment of the participant's health care plan during the first two years of the program.

Management of PRIDCO accepted this project and is evaluating the effect on its financial statements. There were no other material subsequent events that would require further disclosure.

* * * * *

# OTHER SUPPLEMENTARY INFORMATION

***Puerto Rico Industrial Development Company***
***(A Component Unit of the Commonwealth of Puerto Rico)***
*Schedule of Changes in Cash and Sinking Fund per Trust Indenture (In thousands)*
*For the Year Ended June 30, 2015*

| | | | U.S. Bank Trust Indenture Sinking Fund | |
|---|---|---|---|---|
| | **Total** | **General Fund** | **Principal and Interest** | **Reserve Account** |
| Balance at June 30, 2014 | $ 52,582 | $ 20,864 | $ 9,718 | $ 22,000 |
| Cash provided by operating activities | 15,910 | (398) | 16,303 | 5 |
| Collections from capital contributions | 19,752 | 19,752 | - | - |
| Payments for capital assets | (22,785) | (22,785) | - | - |
| Payment of bonds | (10,020) | - | (10,020) | - |
| Proceeds from notes and loan payables | 14,862 | 14,862 | - | - |
| Payments of notes and loan payables | (15,284) | (15,284) | - | - |
| Payment of notes payable to GDB | (1,000) | (1,000) | - | - |
| Payment of interest | (19,701) | (10,036) | (9,665) | - |
| Payment of obligations under capital lease | (280) | (280) | - | - |
| Collections from notes receivable | 29 | 29 | - | - |
| Investment in certificates of deposit | (125) | (125) | - | - |
| Interest collected on investments, loans and other nonoperating revenue | 559 | 559 | - | - |
| Net payments from Commonwealth of Puerto Rico | 7,296 | 7,296 | - | - |
| Balance at June 30, 2015 | $ 41,795 | $ 13,454 | $ 6,336 | $ 22,005 |
| Balance at June 30, 2015 represented by: | | | | |
| Cash and cash equivalents available for operations | $ 13,454 | $ 13,454 | $ - | $ - |
| Cash and cash equivalents held by the Trustee | 6,336 | - | 6,336 | - |
| Investment in U.S. Treasury bond stips, held by the Trustee, at market value | 22,005 | - | - | 22,005 |
| | $ 41,795 | $ 13,454 | $ 6,336 | $ 22,005 |

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